REPORT 595

Response to submissions on CP 300 Approval and oversight of compliance schemes for financial advisers

September 2018

About this report

This report highlights the key issues that arose out of the submissions received on Consultation Paper 300 *Approval and oversight of compliance schemes for financial advisers* (CP 300) and details our responses to those issues.

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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.

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- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
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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.

This report does not contain ASIC policy. Please see Regulatory Guide 269 *Approval and oversight of compliance schemes for financial advisers* (RG 269).

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A Overview/Consultation process

1 For a number of years, ASIC and others have voiced concerns that the professional, ethical and educational standards of financial advisers are too low and need to be lifted.

2 In response to these concerns, the Australian Government introduced reforms to raise the professional, ethical and educational standards of financial advisers. The adviser professionalism reforms, introduced by the *Corporations Amendment (Professional Standards of Financial Advisers) Act 2017* (professional standards legislation), commenced on 15 March 2017, but many of the obligations will be phased in over time.

3 From 1 January 2020, an individual who is authorised to give personal advice to retail clients on relevant financial products (financial adviser) must:

(a) comply with a code of ethics (code); and

(b) be covered by a scheme under which their compliance with the code will be monitored and enforced (compliance scheme).

4 Compliance schemes must be approved by ASIC.

5 In Consultation Paper 300 *Approval and oversight of compliance schemes for financial advisers* (CP 300), we consulted on our proposed process and criteria for determining whether to grant approval to a compliance scheme and our proposed oversight of compliance schemes on an ongoing basis.

6 This report highlights the key issues that arose out of the submissions received on CP 300 and our responses to those issues.

7 This report is not meant to be a comprehensive summary of all responses received. It is also not meant to be a detailed report on every question from CP 300. We have limited this report to the key issues.

Feedback received

8 We received two confidential and nine non-confidential responses to CP 300. Responses came primarily from professional associations in the financial advice and related industries. We are grateful to all respondents for taking the time to send us their comments.

9 For a list of the non-confidential respondents to CP 300, see the appendix. Copies of these submissions are currently on the ASIC website at www.asic.gov.au/cp under CP 300.

10 All submissions recognised the importance of supporting high professional standards among financial advisers, and acknowledged the professional standards legislation as contributing to higher standards. Some submissions supported minimal requirements for approving compliance schemes, so that most existing professional associations could become monitoring bodies of approved compliance schemes with very minor changes to their rules and processes. However, most submissions supported enhanced requirements broadly in line with those we proposed in CP 300.

11 The main issues raised in submissions related to:

(a) the composition of a governing body, and the qualifications of its chair and members;

(b) the timeframes in which a monitoring body and governing body are to make a determination;

(c) what role proactive monitoring should play in the activities of compliance schemes; and

(d) what reporting requirements—both to the public and to ASIC—should apply to compliance schemes.

ASIC's response

12 We have issued Regulatory Guide 269 *Approval and oversight of compliance schemes for financial advisers* (RG 269). RG 269 has been informed by the feedback received on CP 300. While the thrust of our guidance is in keeping with our proposals in CP 300, we have made several changes with a view to clarifying our intentions, minimising the compliance burden where appropriate and allowing more efficient operation of compliance schemes.

13 Among other changes, we have provided greater detail on the composition and role of a governing body—to ensure it can be established with appropriate representation and conduct its operations effectively. We have provided for a brief transitional period in the first three months of a compliance scheme's operation to allow it to prepare its annual work plan and proactive monitoring activities. We have extended the indicative timeframe for making determinations from 45 days to 60 days. We have also clarified our requirements on compliance scheme approval processes and on appeals of governing body decisions.

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B Composition and role of governing bodies

Key points

This section outlines the feedback we received about our proposals that:

- a governing body comprise only non-executive members, include an independent chair, and have a balance of industry and consumer representatives;
- certain criteria be applied to determine the chair's independence, including non-membership of professional associations;
- at a minimum, one member of the governing body has met, at some point in the five years before being appointed to the governing body, the training and competence standards that would have allowed them to give personal advice to retail clients on 'Tier 1' or relevant financial products; and
- a governing body be responsible for making final determinations about whether a financial adviser has failed to comply with the code.

This section includes our responses to the feedback we received.

Independence and balance of governing body

14 In CP 300, we proposed that a monitoring body for a compliance scheme should have an independent governing body that makes determinations about code non-compliance and sanctions, sets the strategic direction of the monitoring body and oversees its operations.

15 To ensure a compliance scheme can meet these requirements, we proposed that a governing body should comprise only non-executive members, should include an independent chair, and should have a balance of industry and consumer representatives.

Stakeholder feedback

16 Most submissions supported the requirement that the governing body comprise only non-executive members. Only one submission, from a professional association, objected to this proposal, on the basis that it meant that it could not operate a compliance scheme using the board of its association as the governing body. The submission suggested that this and other requirements for the governing body were inconsistent with a professional association operating a compliance scheme.

17 Similarly, most submissions supported the requirement that the chair be independent (though there were differing views on the criteria for independence, discussed in paragraphs 20–24). One submission proposed

that the harshest critics of a financial adviser would be the adviser's peers, suggesting that a governing body comprising peers (presumably including the chair) would be more important than ensuring independence.

18 There was more divergence on the question of there being a balance of industry and consumer representatives on the governing body. In particular, several submissions from industry representative bodies questioned the benefit of equal consumer representation, or of any consumer representation at all. However, most submissions recognised the importance of consumer representation and the appropriateness of balanced representation (though some suggested these considerations, while important, were not as important as the knowledge, skills and experience of governing body members).

19 Some submissions noted that, if there is a large number of approved compliance schemes, it may become difficult to find a sufficient number of suitably qualified and experienced consumer representatives.

ASIC's response

We expect that a governing body will meet the requirements for independence and balance set out in CP 300.

We consider it essential that consumer interests be represented directly in the decision making of a compliance scheme. It is common to many schemes investigating conduct that may harm consumers that consumer representation be at least equal to industry representation—see, for example, the requirements for external dispute resolution in s1051 of the *Corporations Act 2001* (Corporations Act).

Our guidance in RG 269 maintains the requirement for an equal balance of consumer representatives and members with relevant background and experience in the financial advice industry. We have also provided some additional guidance on who might constitute a governing body member with consumer representative experience.

We have also provided additional clarity on the independence of the members bringing an industry perspective to the governing body. There is an inherent conflict of interest that members would face if they were making determinations in relation to themselves or their businesses, or were deciding on a program of proactive monitoring that could include them. To avoid this conflict, RG 269 clarifies that these members should not themselves be covered by that particular compliance scheme.

While the professional standards legislation expressly acknowledges that a professional association could operate a compliance scheme, we consider that independent scheme administration is key to ensuring effective compliance with the code and to managing conflicts of interest that a monitoring body that is also a professional association may have.

It is also not the case that the existing disciplinary processes of those professional associations can always be approved without modification to meet the requirements of the professional standards legislation. In most cases, a professional association proposing to operate a compliance scheme will have to establish new processes or enhance existing ones in order to be approved.

Criteria for independence of chair

20 In CP 300, we noted the importance of independence for the monitoring body of a compliance scheme, ensuring that conflicts of interest are avoided or managed appropriately. We gave as an example that a monitoring body's interest in attracting and retaining financial advisers could discourage robust enforcement of compliance with the code.

21 An important element of a monitoring body's independence is the independence of the chair of the governing body. In CP 300, we proposed that, to be classified as independent, the chair must not be a member of any financial advice industry association, or currently be a financial adviser.

Stakeholder feedback

22 Most submissions recognised the importance of an independent chair. A minority of submissions proposed instead that the chair, with the rest of the governing body, be drawn from the financial advice industry (in keeping with the suggestion that an adviser's peers will be the adviser's harshest critics).

23 Some submissions identified practical difficulties that might arise. For example, applying the criteria strictly would mean that a life member of a professional association, who had ceased playing any active role with the association, would nevertheless be disqualified from the role of chair. There was a concern that the independence criteria may mean the chair has insufficient knowledge and experience to provide leadership for the compliance scheme, both in terms of decision making and setting the compliance scheme's strategic direction.

24 Solutions proposed for these practical difficulties included allowing a life member who had suspended their membership to be chair and allowing the chair to be a member of a professional association other than the association sponsoring the compliance scheme.

ASIC's response

The rationale for requiring an independent chair is to avoid any real or perceived conflicts of interest in decision making and administration of the compliance scheme. We consider that

permitting the exceptions proposed in submissions would allow real or perceived conflicts of interest in the chair to persist. We have therefore retained the requirements for an independent chair that we outlined in CP 300 in our guidance in RG 269.

We have also provided greater clarity on the requirement that the chair be completely independent. The chair must not:

- be a member of any financial advice industry association;
- currently be a financial adviser (i.e. an individual who is authorised to give personal advice to retail clients on relevant financial products);
- be an Australian financial services (AFS) licensee whose advisers are covered by a compliance scheme; or
- be a director or responsible officer of an AFS licensee whose advisers are covered by a compliance scheme.

This is consistent with the notion that the chair be disinterested in the decision making and administration of the compliance scheme.

Experience in providing personal advice

25 Section 921K of the Corporations Act requires, among other things, that a monitoring body has sufficient expertise to appropriately monitor and enforce compliance with the code. In CP 300, we proposed that, at a minimum, we would expect that one member of the governing body has met, at some point in the five years before being appointed to the governing body, the training and competence standards that would have allowed them to give personal advice to retail clients on 'Tier 1' or relevant financial products.

Stakeholder feedback

26 All submissions that addressed this point acknowledged the importance of expertise in financial advice. Several submissions from professional associations proposed that, more than simply having met the training requirements for providing financial advice, the qualifying member of the governing body should have experience in providing financial advice. One submission proposed that the qualifying member of the governing body should also be a member in good standing of a reputable professional association.

ASIC's response

We consider it appropriate that at least one member of the governing body should have relevant background and experience in the financial advice industry, and we have included this requirement in our guidance in RG 269.

Governing body role in decision making

27 In CP 300, we proposed that the governing body should be responsible for making final determinations about whether a financial adviser has failed to comply with the code. This proposal sought to ensure that a different entity is responsible for investigating a matter (the monitoring body) and making a final determination (the governing body), avoiding any perceived lack of impartiality.

Stakeholder feedback

28 While accepting the division between the monitoring body's investigative role and the role of the final decision maker, several submissions noted the benefits of a 'panel approach'. Submissions discussed variations of this approach, but, essentially, it would involve a smaller panel, which may or may not be composed of members of the governing body, making final determinations.

29 Most submissions that raised the panel approach suggested the panel could be made up of appropriately qualified members of the compliance scheme, selected on a case-by-case basis depending on their expertise and lack of conflicts of interest.

30 The rationale for the panel approach is to ensure there is a pool of appropriately qualified adjudicators, relieving the governing body of the burden of making every final determination. It could be open to appropriately qualified members of the governing body to participate in the panel.

ASIC's response

We originally proposed that all determinations be made by the governing body to ensure that there was separation between those investigating complaints and those making decisions. We also considered it was appropriate given the proposed requirements for independence and expertise of members of the governing body.

However, we understand that the panel approach is attractive for reasons of practicality and efficiency. Our guidance in RG 269 states that determinations can be made by a panel—whether a sub-group of the governing body or a completely separate panel—so long as the panel reflects the same balance as the governing body itself. Most importantly, the panel should have an independent chair, equal consumer and industry representatives, and meet the expertise requirements of the initial governing body.

If a compliance scheme proposes that panels be established to make determinations about failures to comply with the code, the governing body should retain the capacity to make determinations itself (at its discretion), rather than referring all matters to a panel.

C Monitoring, decision making and reporting

Key points

This section outlines the feedback we received about our proposals that:

- as a guide, the decision-making processes of a monitoring body and a governing body should generally be completed within certain specified timeframes;
- a governing body should undertake both reactive and proactive monitoring of compliance with the code, and that proactive monitoring should take the form of at least one compliance statement process and one thematic 'own-motion' inquiry each year; and
- a compliance scheme should be required to report regularly—to ASIC and to the public—on its activities and its proposed work plans.

We also sought feedback on the transition to the new regime (e.g. whether we should delay the requirement that the monitoring body conduct proactive monitoring activities).

This section includes our responses to the feedback we received.

Decision-making timeframes

31 Section 921L of the Corporations Act requires that determinations about whether a financial adviser has failed to comply with the code be made within a reasonable period of becoming aware of the possible failure.

32 In CP 300, we proposed the following guidance on what would, in normal circumstances, constitute a reasonable period:

(a) monitoring body staff to complete an initial assessment of a report of failure to comply with the code within *28 days*;

(b) if the initial assessment recommends further investigation, that investigation to take place within *90 days* of the initial assessment; and

(c) if the matter is then referred to the governing body for final determination, that determination to be made within *45 days* of the referral.

33 These timeframes are expressly indicative only. They reflect the timeframe of 160 days in which determinations must be made if a financial adviser notifies the monitoring body that they intend to be covered by a different compliance scheme.

Stakeholder feedback

34 Most submissions expressed some concern with at least some of the timeframes, suggesting that they would be tight and might lead to rushed decision making, compromising procedural fairness to affected financial advisers.

35 Several submissions nevertheless expressed support for the timeframes, noting that they are indicative and are not intended to preclude longer timeframes for more complex matters or impose strict requirements when there are unavoidable delays.

36 Generally, there was more support for the 28-day timeframe for initial assessments, less support for the 90-day timeframe for investigations, and the least support for the 45-day timeframe for final determinations. For final determinations, submissions noted that the monthly governing body meetings envisaged by CP 300 may not be practicable. Further, a governing body may refer matters back to the monitoring body for additional investigation or reconsideration, and this will inevitably lead to a longer time before final determinations are made.

37 One submission noted it was important that all the timeframes be paused should a matter go before the courts.

ASIC's response

We recognise that monitoring bodies and governing bodies will be faced with a variety of matters, some of which will be complex and require extensive investigations, and that for these matters the suggested timeframes may prove insufficient.

Nevertheless, we consider it important that matters be dealt with in a timely manner. Most matters should be capable of conclusion within the specified timeframes, without rushing proceedings or undermining procedural fairness.

Our guidance in RG 269 includes an expectation that final determinations be made within 60 days of a referral to the governing body, rather than 45 days, recognising the logistical challenges that may be associated with regular governing body meetings at particular times of the year.

We have not amended the other decision-making timeframes. However, we have provided more context in RG 269 to explain that these timeframes are guides. The timeframes are relevant to an assessment of whether determinations are made within a reasonable period, but they are not intended to be met at the expense of a thorough investigation or procedural fairness.

Proactive monitoring

38 In CP 300, we proposed that monitoring bodies carry out both proactive and reactive monitoring. Proactive monitoring would be determined each year and should consist of at least one compliance statement process and one thematic 'own-motion' inquiry each year.

39 Proactive monitoring is considered an essential element of a monitoring body's activity, as it will encourage higher standards of ethical behaviour. Financial advisers will know that any misconduct is capable of being detected even without a complaint being made, and they will benefit from the good and bad behaviours highlighted by monitoring body reviews.

40 The thematic own-motion inquiry is expected to result in a report on a particular topic, with analysis and recommendations for financial advisers and AFS licensees to improve standards of conduct. The annual compliance statement might consist of a questionnaire to financial advisers, seeking information about non-compliance, emerging risks and examples of good practice.

Stakeholder feedback

41 Submissions varied in their support for proactive monitoring, the form it should take, and the frequency at which proactive monitoring activities should be undertaken.

42 Most submissions believed that some form of proactive monitoring is appropriate. Several submissions saw it as a secondary form of monitoring, which can complement reactive monitoring, but it should not be the monitoring body's primary focus and it should not divert resources away from reactive monitoring.

43 A minority of submissions contended that proactive monitoring was not appropriate at all, suggesting that it would be duplicative of ASIC's responsibilities. Conversely, some submissions strongly supported proactive monitoring, considering it the best way to prevent consumer detriment (or detect it early), and to share examples of good and poor practice with the industry.

44 In terms of the form of proactive monitoring, several submissions either questioned the value of thematic inquiries or sought further guidance on what would constitute a thematic inquiry. Some submissions, especially from accounting industry associations, suggested that random audits would be a more effective form of proactive monitoring than thematic inquiries and compliance statements. Some submissions questioned the usefulness of the compliance statement process, noting that publication of non-compliance on

the financial advisers register would be a significant disincentive to advisers to self-report non-compliance in a compliance statement.

45 Submissions were mostly supportive of a monitoring body undertaking some regular proactive monitoring activity. One submission suggested that a single thematic inquiry and compliance statement process each year ought to be sufficient (in CP 300, we had suggested this be the minimum). Another suggested that the frequency of proactive monitoring could be reduced—for example, by requiring the thematic inquiry and the compliance statement process to be conducted in alternate years.

ASIC's response

Proactive monitoring is an essential element of a compliance scheme. While investigating complaints is equally important, proactive monitoring means a financial adviser cannot avoid scrutiny just because their conduct is not reported to a compliance scheme. Proactive monitoring does not duplicate ASIC's responsibilities, because we undertake proactive monitoring of compliance with the financial services laws, whereas monitoring bodies will be responsible for proactive monitoring of compliance with the code.

Thematic inquiries are an important component of proactive monitoring, and our guidance in RG 269 reflects this. A thematic own-motion inquiry is well suited to providing the industry with guidance and examples of good and poor practice, which is a key objective of proactive monitoring.

We have accepted submissions that compliance statements are a valuable but less incisive form of proactive monitoring. Accordingly, a compliance scheme may choose to make a compliance statement process part of its proactive monitoring activities (either annually or less regularly), but we will not expect every scheme to undertake one.

We will expect each compliance scheme to pursue best practice in proactive monitoring, which will require them to consider additional activity beyond the minimum annual thematic own-motion inquiry where it is necessary or appropriate. This may include a compliance statement process, additional thematic inquiries, random audits, or other proactive monitoring suited to the characteristics and practices of a scheme's membership.

Transitional arrangements

46 AFS licensees must ensure their financial advisers are covered by a compliance scheme by 1 January 2020. In CP 300, we proposed that we would announce initial approval of compliance schemes by early October 2019. We also proposed that compliance schemes undertake certain

activities—including reactive and proactive monitoring, publication of an annual work plan, and data analysis and reporting—from the commencement of the scheme.

Stakeholder feedback

47 Most submissions noted some practical difficulties associated with meeting these requirements immediately the compliance scheme commences. Some suggested that proactive monitoring would be better undertaken after an initial annual work plan had been completed, and relevant issues had been identified over the course of a year's reactive monitoring. Proactive monitoring may also require new systems and expertise for associations accustomed only to undertaking reactive monitoring.

48 Submissions offered a number of suggestions for easing transition by delaying proactive monitoring requirements. Some suggested deferring the requirement for one year, some suggested two years, and others suggested a staged approach (e.g. a pilot inquiry in the first year to be followed by a full thematic inquiry).

49 Additionally, some submissions suggested that the requirement to publish an annual work plan could be delayed to the second year of the compliance scheme's operation, so that there will be information from the first year of monitoring to inform the scheme's monitoring plans.

50 A few submissions noted that it would also be appropriate to delay the requirement for data analysis and reporting, although most submissions agreed that data collection should start immediately upon commencement of code monitoring. Some said that given the size of the task of setting up a compliance scheme, it would be appropriate to delay the requirement for data analysis and reporting for one year until set-up activities have come to an end. Delaying reporting would also give compliance schemes time to develop a common reporting standard and implement technology-based systems.

51 One submission suggested a two-year transitional period to give monitoring bodies time to implement policies and procedures to efficiently collect, analyse and report to ASIC. On the other hand, another submission expressed the view that the requirement for data collection, analysis and reporting should not be delayed, although the reliability of any data needs to be tempered given that there would be limited historical data owing to this being a new regime.

ASIC's response

It is important that each compliance scheme be prepared to accept financial advisers' applications to be covered and

investigate reports of failures to comply with the code as soon as the new arrangements commence.

We acknowledge that a compliance scheme in its first year of operation may not have information related to its members' compliance histories to inform its annual work plan or undertake proactive monitoring. However, we expect that a compliance scheme's monitoring and governance bodies will be familiar with practices and risks in the industry, and we do not consider that the development of a work plan, including a thematic own-motion inquiry, is too onerous a requirement for a scheme's first year.

That said, we also acknowledge that there is limited time between when a compliance scheme is approved and when it would ordinarily be expected to produce an annual work plan and determine its work program for the year. Our guidance in RG 269 therefore notes that, in the first year of monitoring, it will be sufficient for:

- a partial-year work plan to be submitted to ASIC by 31 March 2020;
- proactive monitoring to commence from 1 April 2020;
- data analysis to commence from 1 April 2020 (after data collection begins on 1 January 2020); and
- the first six-monthly report to ASIC only to cover the monitoring body's resources and expertise and any proposed changes to the compliance scheme (i.e. reporting on matters that would be covered in the annual report is not required until the second six-monthly report).

This does not preclude a compliance scheme from completing an annual work plan, conducting proactive monitoring and undertaking data analysis immediately upon commencement if it is able to do so.

Reporting and publication requirements

52 In CP 300, we proposed that a monitoring body report regularly—to ASIC and to the public—on its activities and on the data it collects. We proposed public annual reports covering the outcomes of proactive monitoring, insights about failures to comply with the code and investigations the monitoring body had undertaken, any serious contraventions or systemic issues identified, any emerging trends, and good practice examples. Additionally, a monitoring body would report quarterly to ASIC on the same matters, and be required to meet with ASIC quarterly to discuss the reports. The public report would not be required to publish full details of every matter.

53 Further, a monitoring body would be required to publish its annual work plan, setting out what it will be focusing on in the year ahead, based on identified risks.

Stakeholder feedback

54 There was broad support for the regular reporting arrangements outlined in CP 300. Some submissions noted a concern that the reporting may become burdensome and may prove less necessary over time. Submissions differed on how the reporting frequency might be better managed. Some suggested beginning with quarterly reporting to ASIC, but reducing the frequency in later years if compliance schemes were proving effective. Others suggested having only two reports in the first year, but increasing the frequency as compliance schemes became established. Some considered that less frequent reporting (six-monthly or annual) would be sufficient, and noted concerns that more frequent reporting and meetings could lead to ASIC micro-managing compliance schemes.

55 Most submissions were supportive of publishing an annual report, while emphasising that this report should be at a summary level and not a detailed report of every matter the monitoring body had considered. One submission proposed that annual reports not be published. That submission and one other suggested it would be better for ASIC to publish consolidated reports. Other submissions suggested that ASIC produce a standard reporting template.

56 Many submissions noted concerns about the proposal to publish an annual work plan. These concerns were founded on the risk that it would lead to 'compliance scheme shopping' by financial advisers seeking to choose a compliance scheme that would not focus on their areas of poor compliance. There were also concerns that plans could include confidential material, or that they may lock a compliance scheme into a particular compliance approach for a year without the flexibility to change tack in response to new information. One submission suggested that the task of compiling and publishing an annual work plan would divert resources away from standard-setting and enforcement activity.

ASIC's response

Our intention in requiring regular reporting by compliance schemes is not to impose a regulatory burden or to micro-manage schemes, but to ensure that we are aware of any emerging issues and to give us confidence that approved schemes are operating as intended.

To minimise the reporting burden, compliance schemes must report six-monthly to ASIC (instead of quarterly). However, we will still meet with monitoring bodies quarterly. These meetings

should not require excessive preparation by a monitoring body, but they should give us an understanding of how the compliance scheme is operating. These requirements are set out in our guidance in RG 269.

It may be possible that formal reporting and meeting requirements can be scaled back over time, as compliance schemes become established, but we expect always to have ongoing regular contact with monitoring bodies.

To ensure compliance schemes are publicly accountable, and to provide covered financial advisers with information about the compliance schemes available to them, we expect that annual reports will be published. However, not every detail of a monitoring body's activities and decisions needs to be published.

Annual work plans are a valuable mechanism for ensuring the compliance scheme's operations and areas of interest are considered specifically each year. We accept that publishing annual work plans could lead to compliance scheme shopping or other unintended outcomes. We expect that annual work plans will be produced and provided to us, but only a high-level overview of the scheme's compliance focus should be published each year.

D Other issues

Key points

This section outlines the feedback we received about our proposals that:

- ASIC follow a timeline for approval of compliance schemes, with initial approvals to be announced in early October 2019;
- a monitoring body be resourced sufficiently;
- a governing body be able to impose a range of sanctions when it determines a financial adviser has not complied with the code;
- a compliance scheme has a documented process for dealing with appeals of governing body decisions; and
- AFS licensees and authorised representatives be required to comply with monitoring body requests for information for the purposes of proactive monitoring.

This section includes our responses to the feedback we received.

Approval process and timeline

57 AFS licensees must ensure that all new financial advisers who operate under their licence are covered by a compliance scheme by 1 January 2020.

58 To meet these commencement dates, in CP 300 we published an indicative timeline for the approval of compliance schemes. It proposed:

(a) expressions of interest from entities wishing to become monitoring bodies in September 2018 (following publication of our regulatory guide);

(b) draft applications in November–December 2018;

(c) feedback to applicants in January–March 2019;

(d) final applications in June 2019; and

(e) approvals announced in early October 2019.

59 Applications that do not meet these dates would still be considered, but priority would be given to applications that do keep to the timeline, and approvals of applications that do not keep to the timeline may not be announced at the same time as those that do.

Stakeholder feedback

60 While most submissions acknowledged the importance of establishing compliance schemes by the legislated commencement date, many noted

concerns for the tightness of the timeline. None suggested that meeting the timelines would be impossible, but there were concerns that the timeline may be inflexible and demanding on resources (both for prospective applicants and for ASIC).

61 There was a particular concern that announcing approvals in early October 2019 would leave little time before new financial advisers must be covered by a compliance scheme (15 November 2019). Some submissions also noted practical difficulties with the timeline—for example, that prospective compliance schemes may wish to see the final code before submitting their final applications, and that they may not be in a position to name the prospective members of their governing bodies until late in the process (or indeed after they have been approved).

62 Aside from concerns about the timeline, there was broad support for the process itself. However, there was some concern that the process involved discrete steps (expression of interest, draft application, final application), and that a more iterative process with strong engagement between applicants and ASIC would be appropriate. Some submissions sought further guidance on the expressions of interest process. One submission considered that a substantial level of detail should accompany the expression of interest, to avoid frivolous applications, while another suggested that the expression of interest may be a redundant step.

ASIC's response

The timeline published in CP 300 reflects the need for compliance schemes to be approved in time for financial advisers to be covered, factoring in an appropriate amount of time for interested parties to make submissions and for ASIC to undertake our approval processes.

RG 269 sets out the timeline for the announcement of approvals. We have not changed the proposed timeline. However, depending on the number of proposed compliance schemes that apply, the quality of their applications, and our available resources, we will endeavour to have approvals in place as soon as is practicable.

Our engagement with all applicants will involve an iterative process, rather than a single instance of feedback on a draft application.

We are not asking for a great deal of information in the expression of interest. We seek expressions of interest only to ascertain the number of potential applicants for initial approval, which will allow us to devote sufficient resources to the approval processes.

Resourcing of monitoring bodies

63 Section 921K of the Corporations Act requires a monitoring body to provide evidence that it has sufficient resources and expertise to appropriately monitor and enforce compliance with the code. We may only approve a compliance scheme if we are satisfied that it has sufficient resources and expertise.

64 In CP 300, we proposed that a monitoring body would provide a statement to ASIC outlining the basis on which it considered its resources to be sufficient. We did not propose to set a specific benchmark for resourcing, but sought stakeholder views on whether a benchmark could be appropriate.

Stakeholder feedback

65 Most submissions supported flexibility in how a monitoring body would meet the resourcing requirements. Several submissions noted that different membership profiles would require different types of expertise, which may imply different resourcing requirements.

66 One submission noted the practical difficulty associated with a monitoring body settling its resourcing requirements before knowing how many financial advisers will be covered by its compliance scheme. This submission did consider specific benchmarks to be appropriate, but suggested resourcing should be based on the resources of the sponsoring entity of the compliance scheme (e.g. a professional association), not on those of the monitoring body itself.

67 Another submission noted the practical difficulty of raising initial funding, as fees may not cover all start-up costs, suggesting the need for a plan to meet financing requirements over time. Alternatives to resourcing benchmarks were proposed, including applying a solvency or positive net assets test.

ASIC's response

We have not set a specific benchmark for resourcing.

Our guidance in RG 269 recognises that resourcing decisions will depend, in part, on how many financial advisers are covered by a compliance scheme. It is important for an applicant for compliance scheme approval to demonstrate its plans for matching its resourcing requirements to the number of financial advisers covered.

Sanctions for non-compliance with the code

68 In CP 300, we proposed that a governing body have access to sanctions ranging from a warning or reprimand to revocation of the financial adviser's coverage by the compliance scheme in extreme circumstances. Compliance schemes should include sufficient sanctions to be imposed on financial advisers determined not to have complied with the code—to provide a deterrence against non-compliance and to foster a willingness to comply in future.

Stakeholder feedback

69 Several submissions noted that CP 300 did not mention any financial penalties in the indicative list of sanctions. These submissions considered that financial penalties could be useful. They could be graduated according to the seriousness of the non-compliance, and they could help recover the costs associated with investigating the matter and enforcing it against the financial adviser. One submission queried whether compliance schemes could expect to have the power to order financial sanctions.

ASIC's response

RG 269 includes a non-exhaustive list of sanctions that a governing body may impose on covered financial advisers against whom an adverse determination has been made.

We recognise the benefits of financial penalties, especially to assist in recovering the costs of enforcing the matter. If a monitoring body considers that costs orders and/or other financial penalties would benefit its compliance scheme, and it is confident is has the legal power to do so, it is free to allow its governing body to impose financial sanctions.

Appeals of governing body decisions

70 Section 921K of the Corporations Act requires an application for compliance scheme approval to detail arrangements for resolving disputes between the monitoring body and covered financial advisers. We anticipate that the most common form of such disputes will be appeals by covered financial advisers of adverse determinations made by a governing body and the sanctions imposed.

71 In CP 300, we proposed that a monitoring body have a documented process for dealing with appeals and other disputes, and that the process would allow the governing body another opportunity to consider the matters raised by the financial adviser. We recommended that monitoring bodies consider preparing a guide for covered advisers on the appeals process.

Stakeholder feedback

72 Several submissions considered that it would be appropriate for a body other than the governing body (which made the original decision) to consider appeals. Some suggested that an existing independent agency (e.g. ASIC or the Financial Adviser Standards and Ethics Authority) could be an appropriate independent appeals body. One submission suggested that, if a panel or sub-group of the governing body had made the original decision, then the full governing body could consider the appeal.

73 That said, several submissions considered that internal review (i.e. reconsideration by the governing body) was an appropriate appeals mechanism, at least in the first instance. One submission considered that an external appeals body would be costly and unnecessary.

ASIC's response

The professional standards legislation does not prescribe the mechanism for an appeals process; it only provides that there should be arrangements for resolving disputes.

An appeals process is appropriate to ensure decision making is robust and fair. The extent of the appeals process should reflect the seriousness of the consequences for the affected financial adviser, and should not unduly delay finalisation of a matter.

RG 269 sets out our expectation that there be a documented appeals process, but we have not prescribed its form. It is open to a compliance scheme to adopt an approach that meets these objectives. Such an approach may involve reconsideration of the matter by the governing body, consideration by the full governing body (if the original matter had been considered by a sub-group of the governing body or a panel), or any other arrangement that may be suitable. Where possible, a monitoring body should appoint people who were not involved in the original decision to consider any appeal.

ASIC's role is to administer the financial services laws, not to arbitrate disputes between financial advisers and their compliance schemes. It would not be appropriate for ASIC to hear appeals of governing body determinations.

Provision of information for proactive monitoring

74 Section 921L(3) of the Corporations Act provides that a monitoring body may request information from AFS licensees, authorised representatives or relevant providers when investigating a failure or possible failure to comply with the code. Section 921M(2) makes it an offence for a person to fail to comply with such a request.

75 In CP 300, we proposed that we amend these provisions (using our declaration power in s926A(2)(c)) to require compliance with requests made before the monitoring body has identified a failure or possible failure to comply with the code. This amendment would allow a monitoring body to use the power in s921L(3) in its proactive monitoring activities, not just in investigating suspected failures to comply.

Stakeholder feedback

76 Submissions indicated broad support for this proposal, indicating the amendments were necessary for monitoring bodies to carry out proactive monitoring efficiently. Stakeholders also welcomed the prospect that people complying with monitoring body requests in relation to proactive monitoring would be doing so in compliance with the law, addressing concerns about their obligations under privacy law.

77 Some submissions noted the consequence of the amendments that failure to comply with a monitoring body request may constitute an offence (consistent with the existing obligation concerning reactive monitoring). One submission sought clarity about whose responsibility it would be to prosecute such an offence, while another called on ASIC to be prepared to prosecute offences as necessary.

ASIC's response

We will make the amendments to s921L(3) and 921M(2) of the Corporations Act. We will ensure these amendments are in place by the time code monitoring commences.

We confirm that ASIC is responsible for enforcing these provisions of the Corporations Act (including these provisions as they will be amended), and will do so in accordance with our policies, priorities and resources.

Appendix: List of non-confidential respondents

- Association of Financial Advisers
- Association of Securities and Derivatives Advisers of Australia
- Australian Small Business and Family Enterprise Ombudsman
- CPA Australia
- Financial Planning Association of Australia
- Financial Services Council
- GRC Institute
- SMSF Association
- Stockbrokers and Financial Advisers Association