



**ASIC**

Australian Securities & Investments Commission

# **ASIC Class Order [CO 05/1195]**

***Proposed class order relief to  
simplify oral general advice  
warnings***

**Regulation impact statement (RIS)**

**November, 2005**

## What this regulation impact statement is about

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ASIC proposes to issue class order relief to minimise unnecessary repetition of the general advice warning by holders of Australian financial services (AFS) licences (licensees) and their authorised representatives when they provide oral general advice. In this paper licensees and their authorised representatives who provide general advice will together be described as general advice providers.

This Regulation Impact Statement (RIS) will explore the costs and benefits of the different options available to ASIC.

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# Issue/problem

## Background

### The Law

1. When a licensee or their authorised representative provides general advice to a retail client they must give that client a general advice warning (GAW) under s949A(2) of the *Corporations Act 2001* (Corporations Act). That warning must convey the following messages:
  - (a) the advice has been prepared without taking account of the client's objectives, financial situation or needs; and
  - (b) because of that, the client should, before acting on the advice, consider the appropriateness of the advice, having regard to the client's objectives, financial situation and needs; and
  - (c) if the advice relates to the acquisition, or possible acquisition, of a particular financial product – the client should obtain a Product Disclosure Statement (PDS) relating to the product and consider the PDS before making any decision about whether to acquire the product.
2. In addition, the GAW must be given to the client at the same time and by the same means as the advice is provided.

### Purpose of the GAW

3. The GAW is primarily required for consumer protection. It is designed to alert the retail client to the fact that the advice is general in nature and does not take into account their personal circumstances. If the warning is not given, there is a risk that the retail client will treat the advice as personal advice (i.e. as though it were necessarily appropriate for them) and act on it without first considering whether it is, in fact, appropriate for them.
4. The explanatory statement to the Good Advice Regulations (*Corporations Amendment Regulations 1998* (SR 1998 No 161)), which introduced the GAW requirement, stated that:

The purpose of the proposed regulation is to prescribe certain licence conditions which give effect to the recommendations made by the ASC<sup>1</sup> in its 1995 report:

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<sup>1</sup> The Australian Securities Commission, which was the precursor to ASIC.

'Good Advice, Licensing Review of Investment Advisory Services'. This report examined regulatory issues relating to investment general advice providers in response to criticisms regarding the standard of investment advice available and in response to developments in the financial services sector and the investment advisory industry. The regulations propose that licensees who give investment advice be required to provide retail investors with information to facilitate informed decision making. This in turn will enhance investor protection and promote market efficiency.

## What is the issue/problem being addressed?

5. More recently, concerns have arisen that the full repetition of the GAW may not be appropriate in all circumstances. It has been suggested that retail clients do not understand or do not listen to the GAW when it is given orally.

6. The consequences of a retail client not understanding or not listening to the GAW are significant if the client makes an inappropriate decision to acquire, sell or hold a financial product based on the mistaken belief that the advice that they received was necessarily appropriate for them. For example, the retail client may:

- be underinsured and suffer significant financial loss if the insured event occurs;
- not have access to their money when it is needed because their investment cannot be realised in the desired time frame; or
- incur significant losses through a high risk investment in circumstances where, given their needs, objectives and financial situation, they should not have made a high risk investment.

7. It is important that retail clients understand that it is their responsibility to assess, or obtain personal advice on, whether general advice is appropriate for them, because the general advice provider has not undertaken this assessment. The GAW requirement is intended to ensure that retail clients have that basic understanding and, therefore, make more informed financial decisions.

8. It has also been suggested that giving an oral GAW in certain circumstances may cause some clients to become frustrated and end their inquiry prematurely. This would lead to delays for those clients in gathering the product information that they require. It could also reduce financial product sales.

9. The provision of an oral GAW also increases the time required to deal with oral enquiries and so increases costs for general advice providers.

10. The Federal Government released its proposals paper *Refinements to Financial Services Regulation (May 2005)* on 2 May 2005. *Refinement Proposal 5.1* (the Refinement) states that ASIC will:

...provide further guidance to develop simple General Advice Warnings conveying the substance of the legislative requirements, instead of relying on the precise wording of the Corporations Act. ASIC will also use its powers to provide relief, where appropriate.

11. The following discussion accompanied the proposal:

The General Advice Warning (GAW) requirement in section 949A of the Corporations Act is designed to alert consumers that advice is general in nature and does not take into account their personal circumstances.

The legislation does not prescribe the actual wording of the GAW, however, most licensees and their authorised representatives have chosen to adopt the wording in the legislation. It is not always practical to use this exact wording and it might also not be particularly meaningful for consumers. For example, where there are regular communications between the general advice provider and its client, full repetition of the GAW wording, as set out in the legislation, for each communication is unnecessary.

It is the substance of the GAW that is important. The form of the GAW should be modified to suit the circumstances. To encourage this, ASIC will assist licensees to refine GAWs to be more easily understood by consumers. ASIC will also use its powers to provide relief from the GAW requirements, where appropriate.

12. The issue is whether ASIC should grant class order relief to allow general advice providers to provide a simpler warning than the GAW when providing oral general advice.

Note: ASIC has already issued guidance explaining that it is not necessary to repeat the exact words in s949A(2) when giving a GAW; it is only necessary to convey the substance of the GAW: see QFS 157 *Do I need to follow the exact wording in the Corporations Act when I give a general advice warning?*

## Objectives

13. The purpose of the GAW is to ensure that consumers who are given general advice understand that it is not personal advice. This

means that they understand that the advice that has been provided is not necessarily suitable for them.

14. ASIC's objective in providing class order relief is to improve the likelihood that retail clients will understand this message when they receive oral general advice. In doing this, ASIC also aims to make it easier for general advice providers to communicate this information to retail clients in a way that best meets their client's needs.

## Options

### Option 1 – Maintain the *status quo*

15. If this option were adopted, general advice providers would be required to comply with the obligation to provide a GAW as set out in s949A(2) of the Corporations Act.

16. As there would be no relief applying generally, individual applications for relief would be considered by ASIC on a case-by-case basis.

### Option 2 – Grant class order relief to allow general advice providers to give a simplified warning instead of the GAW when oral general advice is provided

17. If this option were adopted, ASIC would grant class order relief to general advice providers to allow them to provide a simplified warning instead of the GAW when they provide oral general advice to a retail client.

18. Unlike the GAW, the simplified warning would not require any reference to be made to the Product Disclosure Statement when the advice relates to the acquisition or possible acquisition of a particular financial product. In addition, the simplified warning would not include separate references to the client's: (i) objectives; (ii) financial situation; and (iii) needs. Instead, the simplified warning would combine those matters in a warning to the effect of "The advice is general and may not be right for you".

19. Under the class order, general advice providers would be able to choose whether to rely on the relief and give a simplified warning instead of the GAW when they give oral general advice. If they did not wish to rely on the relief they could instead comply with the

obligation under s949A(2) of the Corporations Act and provide a GAW.

20. This means that the relief would be available but not mandatory.

21. ASIC would not prescribe the words to be used to convey the simplified warning. This means that a general advice provider would be able to choose their own words to convey the simplified warning. Under s949A(2) of the Corporations Act a general advice provider can also choose their own words to convey the GAW.

22. This means that whether complying with the relief or the law, general advice providers would be able to tailor the language that is used to convey the warning to best suit their retail clients.

### **Option 3 – Grant class order relief to general advice providers to give a simplified warning when oral advice is provided, the GAW has previously been given orally and the adviser satisfies a belief test**

23. This option was proposed in ASIC's consultation paper, *Repetition of the general advice warning* (31 August 2005). If this option were adopted, ASIC would grant class order relief to allow a simplified warning to be provided instead of the GAW if a number of conditions were satisfied, that is:

- (a) an oral GAW has previously been given by the general advice provider or a member of the same licensee group;
- (b) the general advice provider tells the retail client that the advice is general and the client should consider whether the advice is appropriate for them (the words used to convey this message would not be prescribed); and
- (c) the general advice provider believes, and a reasonable person in the general advice provider's position would have no reason not to believe, that the retail client understood the reminder.

### **Option 4 – Grant complete unconditional relief**

24. Unconditional relief from the obligation to provide a GAW is not considered to be a feasible option and so is not analysed in this RIS. Unconditional relief is not a feasible option because of the significant consumer detriment that would result from consumers not being warned about the inherent limitations of general advice, when it is provided.

# Impact analysis

## Affected parties

25. The parties that would be affected by ASIC's proposals are:

- (a) licensees who are authorised to provide general advice;

Note: As at 22 November 2005, there were close to 4000 licensees authorised to provide general advice. This includes persons who are authorised to give both personal and general advice as well as persons who are authorised to give only general advice. It also includes persons who are authorised to give advice to wholesale clients only.

- (b) persons who are appointed as authorised representatives to provide general advice;

Note: We do not know how many people fall into this category, although there are a total of 50,616 authorised representatives, across all fields of financial services, registered with ASIC as at 14 October 2005.

- (c) consumers who are given oral general advice; and

Note: Oral general advice may be given whenever a consumer makes a telephone or face to face inquiry about a financial product (including inquiries about bank accounts, credit cards, insurance or investment products). Given that the majority of Australians hold financial products of one kind or another, it seems likely that very many Australian consumers would be affected by ASIC's proposals. However, it is not possible to ascertain how many people receive oral general advice about financial products each year.

- (d) ASIC.

## Costs and benefits of each option

### Option 1 – Maintain the *status quo*

#### Costs

26. If this option were adopted, industry would incur the same costs they currently incur and maintain the same compliance and monitoring systems. The costs for general advice providers include:

- setting up and maintaining compliance systems to ensure that the GAW is given when oral general advice is provided;
- initial and follow-up training of staff who give oral general advice about the obligation to provide a GAW;
- additional time taken to deal with oral inquiries where general advice is given (or for all oral inquiries if a blanket GAW is



given for all calls received prior to the caller speaking to a call centre operator);

- loss of business when clients who become frustrated with sitting through the GAW end their inquiry prematurely.

Note: We do not have information that would enable us to quantify these costs for any individual general advice provider or across the financial services industry. In particular, we do not have information about the number of times oral general advice is given to retail clients in any period in Australia.

27. For consumers, the cost of this option includes having to sit through the entire GAW when making an oral inquiry about a financial product. A consumer could also incur significant costs if the length and complexity of the GAW results in them not listening to, or not understanding, the warning. This could lead to the consumer accepting general advice on the assumption that the advice is appropriate for them, when this is not necessarily the case because the general advice provider has not considered whether the advice is appropriate for that particular client.

Note: We do not have information to enable us to quantify these costs. In particular, we do not have information about the number of times oral general advice is given to retail clients in any period in Australia. In addition, we cannot assess the impact individually or generally of a consumer mistakenly treating general advice as though it were personal advice.

28. ASIC would not be affected by this proposal as there would be no additional regulatory burden in administering this obligation.

## **Benefits**

29. Benefits for general advice providers in maintaining the status quo would include not needing to make any changes to their compliance systems or provide any additional staff training. In addition, the GAW is a simple obligation to satisfy and does not require complex systems to administer.

30. Retail clients would benefit from continuing to receive the detailed GAW.

31. ASIC would not be affected by the proposal as the regulatory task would be unchanged.

## **Option 2 – Grant class order relief to allow general advice providers to give a simplified warning instead of the GAW when oral general advice is provided**

### **Costs**

32. If this option were adopted, general advice providers who chose to rely on the relief would have the costs associated with changing the oral warning that they provide when they give oral general advice. This would require training of relevant staff about the changes to the warning and updating compliance practices and procedures to reflect this change. Where the GAW is given in a recorded message before the consumer speaks to a call centre operator, that recorded message would need to be revised.

Note: We do not have information to quantify these one-off transition costs. These costs will vary for different general advice providers, depending on their business model.

33. However, it should be noted that compliance with the relief would not be mandatory; general advice providers could continue to give the full GAW. This means general advice providers could individually assess whether the long-term savings would be sufficient to justify the transition costs.

34. If this option were adopted, consumers would receive a less detailed warning than the GAW when they receive oral general advice. However, this would only be a cost for consumers if the simplified warning is not an adequate substitute for the GAW in the context of oral general advice. This is unlikely to be the case as the simplified warning highlights the central message of the GAW.

35. ASIC would not be affected by this proposal as there would be no additional regulatory burden in administering this obligation.

### **Benefits**

36. Consumers would receive a warning that communicates the central theme of the GAW in a more succinct way should the general advice provider choose to simplify their GAW. This is likely to benefit consumers as a simpler, more concise message is more likely to be listened to and understood than a longer more complicated message.

Note: We are unable to quantify the benefits to consumers of receiving a warning that is easier to understand when provided orally.

37. General advice providers would benefit by having the option to provide a more succinct warning that would reduce the time taken to

deal with inquiries, and this time saving would translate into a cost saving.

Note: Speaking clearly, it could take as long as 30 seconds to give the GAW whereas the simplified warning could take as little as 5 seconds to give. We do not have information about the number of times the oral general advice warning is given to retail clients in any period in Australia. Therefore, we cannot quantify the potential total saving.

38. This option may also result in fewer calls terminated by clients who feel frustrated by having to sit through the GAW.

Note: We are unable to estimate the extent of this change.

39. ASIC would not be affected by the proposal as the regulatory task would be equivalent to administering the GAW.

### **Option 3 – Grant class order relief to general advice providers to give a simplified warning when oral general advice is provided, the GAW has previously been given orally and the adviser satisfies a belief test**

#### **Costs**

40. If this option were adopted, there would be significant compliance costs for general advice providers including the cost of each of the following:

- setting up systems to record whether an oral GAW has been provided to a particular client (as this would be a precondition to providing the simpler warning);
- accessing those systems each time a call is received, to ascertain whether the simpler warning can be given instead of the GAW;
- training general advice providers to use these systems to record the giving of an oral GAW and to check that information for each call;
- training general advice providers in the belief test;
- recording the factors that led to the belief being formed; and
- reviewing and monitoring compliance with the conditions of the relief.

41. According to the submissions received on the consultation paper, these costs would make the relief largely unviable in the context of

general advice provided via call centres. Therefore, it is likely that the relief would not be used in this situation and these general advice providers would instead continue to comply with the GAW.

Note: We have not been provided with information to quantify these costs. However, based on the submissions, it is expected that these costs would not be insignificant and, for call centres, would be greater than the benefits of being able to provide a simplified warning instead of the GAW.

42. The cost for retail clients is likely to be that they will not gain the benefits of the simplified warning because the relief is unlikely to be used by many general advice providers. If the relief were used, it is likely that the additional costs would, eventually, be transferred to retail clients. In addition, because this option requires an oral GAW to be given before the simplified warning can be used, first time callers would not benefit from the relief.

Note: We have not been provided with information to quantify these costs.

43. There would be increased costs for ASIC in administering this proposal because of the difficulties inherent in administering a belief test.

Note: We have not quantified these costs.

## **Benefits**

44. The simplified warning would be bolstered by the initial provision of the more detailed GAW and the requirement for the general advice provider to form a view that the retail client understood the simplified warning. The initial provision of a more extensive warning (i.e. the GAW) would benefit consumers if it improves consumer's comprehension of the simplified warning by providing a base for their understanding of the simplified warning. However, it is unlikely that the initial provision of the GAW would significantly improve understanding of the simplified warning as the simplified warning highlights the central message of the GAW.

45. General advice providers would benefit from being able to provide a simplified warning on subsequent occasions (i.e. after the full oral GAW has been provided). This would result in an approximately 25 second/call time saving and would lead to fewer calls being terminated because the client feels frustrated about having to sit through the full GAW again. However, as noted at paragraphs [40]-[41], these benefits are unlikely to be realised due to the compliance costs associated with complying with this proposal for many general advice providers.

46. Benefits for ASIC would primarily flow from the increase in consumer protection associated with requiring general advice

providers to form a positive belief that the retail client understood the simplified warning.

## Consultation

47. On 31 August 2005 ASIC issued a consultation paper, *Repetition of the general advice warning*, seeking comments on proposed relief to give effect to the Refinement. Option 3 of this RIS embodies the relief proposed in the consultation paper.

48. ASIC received a total of 8 submissions from industry associations as well as general insurance and superannuation product issuers.

49. The strong central theme of those submissions was that the cost of implementing the consultation paper proposal (i.e. Option 3) would be so great that it would be simpler and cheaper to comply with the GAW.

50. Submissions focussed on the costs of complying with the belief test and the difficulties faced by call centres in administering a disclosure obligation that changed, depending on whether or not the client had previously received an oral GAW. In addition, some submissions highlighted the costs associated with long oral statements that are required to be made to clients.

51. ASIC responded to these concerns by developing Option 2 which does not have a two stage disclosure obligation, does not have a belief test and significantly shortens (by approximately 25 seconds) the oral GAW that is required to be given to retail clients.

## Conclusion and recommended option

52. ASIC considers that Option 2 (grant class order relief to general advice providers to give a simplified warning instead of the GAW when oral general advice is provided) would be the preferable alternative. This option would:

- (a) provide consumers with a warning they are more likely to listen to and understand, when given orally;
- (b) provide lower costs to industry; and
- (c) provide the relief contemplated by the *Refinements to Financial Services Regulation*.

53. Option 2 would not disadvantage consumers, as they would still receive the core message of the GAW in the simplified warning, which would alert them to the inherent limitations of general advice.
54. Option 2 would reduce the costs of oral general advice providers by reducing the time taken to provide the requisite warning from approximately 30 seconds to approximately 5 seconds.
55. ASIC would not be affected if Option 2 were adopted as the cost of administering the simplified warning would be equivalent to the cost of administering the GAW.
56. Option 1 (maintain the status quo) is not the preferred option because consumers and industry could both benefit from the relief proposal (without additional cost to ASIC).
57. Option 3 (grant class order relief to general advice providers to give a simplified warning when oral general advice is provided and the GAW has previously been given orally and the adviser satisfies a belief test) is not the preferred option because the additional conditions (when compared to Option 2) would significantly increase the cost of implementing the relief to such a degree that the relief would be unviable for a significant proportion of general advice providers. As a result, it would seem inappropriate to proceed with this proposal.
58. Option 4 (grant complete unconditional relief) has been rejected as it is not considered to be a feasible option. This is because it is important for consumers to be warned about the inherent limitations of general advice in order to reduce instances of consumers acting on general advice because they mistakenly believed that the adviser had formed the view that it was appropriate for them.

Note: See further, paragraphs [3], [4], [6] and [7].

## Implementation and review

59. ASIC will implement the recommendations in this RIS by issuing a class order in conjunction with an information release. It is proposed that the class order relief would be available to general advice providers from early December 2005. No transition period would be required because it would not be mandatory to use the relief. This means that general advice providers could transition to the relief at any time (or not at all).
60. The information release will be posted on ASIC's website. We expect that industry and the public are aware that new announcements

are made on ASIC's website. Currently ASIC has no plans to specifically monitor the implementation of the change.