

# The right advice

## Issues surrounding the *Financial Services Reform Act ("FSRA") 2001*

The *Financial Services Reform Act* ("FSRA") received Royal Assent on 28 September 2001 and comes into effect on 11 March 2002. The FSRA repeals Chapters 7 and 8 of the *Corporations Act* and inserts new provisions that regulate financial services and markets.

At present, most people engaged in an investment advice business are required to hold a dealer's licence and their business is regulated by the Australian Securities and Investments Commission. However, the current law states that lawyers and accountants do not require a license if the advice they give is merely incidental to the practice of their profession.<sup>1</sup> The FSRA has partially eroded the breadth of this exemption and imposed a new blanket prohibition on dealing in financial products.

Analysis of the implication of these changes for lawyers and accountants requires an understanding of what is meant by the terms financial product and financial product advice. Financial product advice means giving a recommendation or a statement of opinion that:

- (a) is intended to influence a person or persons in making a decision in relation to a particular financial product or class of financial product...; or
- (b) could reasonably be regarded as being intended to have such an influence.<sup>2</sup>

And, generally speaking, a financial product is a facility through which, or through the acquisition of which, a person does one or more of the following:

- (a) makes a financial investment;
- (b) manages financial risk;
- (c) makes non-cash payments<sup>3</sup>.

### Financial product advice

The FSRA contains exemptions for lawyers and tax agents that are very similar to the current exemption for lawyers and accountants. Viz:

The following advice is not giving financial product advice:

- (a) advice given by a lawyer in his or her professional capacity about matters of law, legal interpretation or the application of the law to any facts;
- (b) ... any other advice given by a lawyer in the ordinary course of activities as a lawyer, that is reasonably regarded as a necessary part of those activities;
- (c) .... advice given by a [registered] tax agent ... that is given in the ordinary course of activities as such an agent and that is reasonably regarded as a necessary part of those activities.<sup>4</sup>

Accountants can find an exemption from the new rules in draft regulations issued on 10 October 2001. The regulations provide

that, as long as the accountant does not make a recommendation or provide an opinion<sup>5</sup>, advice given by qualified accountants on the following matters is not financial product advice:

- (a) Preparing or auditing financial statements;
- (b) Insolvency services;
- (c) Financing the acquisition of assets that are not financial products (for example comparing lease finance to hire purchase);
- (d) Processes for the establishing, structuring and operating a superannuation fund;
- (e) Managing debt, including advice regarding factoring, defeasance and sale of debts;
- (f) Managing taxation issues, including advising on the taxation implications of financial products;
- (g) Management of risk associated with conducting a business (eg: hedging strategies);
- (h) Business planning including establishment, structuring and administration;
- (i) Conducting a due diligence on a business;
- (j) Valuing the assets of, or shares in, a business,<sup>6</sup>

The accountant's professional bodies appear to be satisfied that these regulations are sufficient to take accountants outside

the new regulatory regime.<sup>7</sup> However, this conclusion assumes that accountants will be able to limit their advice to a quasi-academic discussion of the pros and cons of a matter and not take the obvious next step of giving their client an opinion or recommendation.

### Dealing in a financial product

While practitioners from the legal and accounting professions may not require a Financial Services License before giving financial product advice, they are still caught by the prohibition against dealing in a financial product. Dealing is very widely defined as:

- (a) applying for or acquiring a financial product;
- (b) issuing a financial product;
- (c) underwriting securities or managed investment interests;
- (d) varying a financial product;
- (e) disposing of a financial product.

Arranging for another person to engage in the above conduct is also dealing in a financial product, unless your actions only amount to providing financial product advice.<sup>8</sup>

If a professional's conduct amounts to arranging the acquisition, issue, disposal or variation of a financial product on behalf of a client, then they will be required to hold an Australian Financial Services Licence<sup>9</sup>. Section 761E of the FSRA specifies conduct that amounts to providing, issuing and acquiring a financial product. 761A defines disposing of a financial product. Varying a financial product is not defined.

### Conclusion

The prohibition on dealing in a financial product means that lawyers and accountants will not be able to arrange, on behalf of a client, any of the following:

- The issue, transfer, purchase or sale of shares or trust units (therefore professionals will require a Financial Services License to arrange the sale of a family business by way of a transfer of shares in a family company or units in a unit trust);
- Acquiring, cancelling or varying an insurance policy (query whether professional advisers can be involved

with transferring business insurance policies from a vendor to the purchaser, or arranging to segment a work place (into high and low risk activities) to reduce overall worker's compensation premiums?;

- Acquiring, cancelling or varying interest rate, foreign exchange and commodity price hedging products. What role can professionals play in regard to managing the various market risks assumed by a gold miner or wheat farmer?;
- Granting a common law mortgage over shares or other financial products (eg: debentures or units in a trust) to secure loans to a business. Common law mortgages have the legal effect of disposing of the legal estate and granting the mortgagor an equitable right of redemption.

Nor can lawyers and accountants give clients advice on issues such as the need to plan for their retirement or take out insurance on a home or other non-business asset.

While accountants can give advice on the following matters, lawyers will often be prohibited from advising in regard to matters such as:

- Managing business risks by, for example, insuring business assets and taking out professional indemnity and directors' and officers' insurance policies.
- Managing market based risks by hedging, or not hedging, against interest rate, foreign exchange and commodity price risks.
- Choosing between different financial products that are available to fund a business' growth.

Conversely, lawyers can give advice in regard to matters such as the following where accountants can not:

- Any financial product advice that includes a recommendation as to the most appropriate course of action.
- Advice to an executor in regard to managing financial products held in a deceased estate.
- Advice in regard to whether to accept shares in lieu of a lump sum payment, or to dispose of shares in a business, as part of a retirement or litigation settlement strategy.

- Advising a client in a family law matter (a non-business transaction) upon the relative commercial issues raised by a settlement proposal that contemplates use of a financial product.
- Advising a client, on the commercial implications of giving a personal guarantee to secure a relative's business debts. ■

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#### Reference Notes

- 1 section 77(5) Corporations Act
- 2 section 766B(1) Financial Sector Reform Act
- 3 section 763A Financial Sector Reform Act
- 4 section 766B(5) Financial Sector Reform Act
- 5 R 7.1.29(2) Draft Corporations Amendment Regulations 2001 (No. ) 1
- 6 Paraphrased from R 7.1.29(1) Draft Corporations Amendment Regulations 2001 (No. ) 1
- 7 See letter to members from CPA Australia at: [http://www.cpaonline.com.au/01\\_information\\_centre/02\\_financial\\_plan/1\\_2\\_1\\_10\\_update\\_200110\\_11.asp](http://www.cpaonline.com.au/01_information_centre/02_financial_plan/1_2_1_10_update_200110_11.asp)
- 8 For the purposes of this paper I assume that the legislation means "financial product advice" in its broadest sense, and not advice that falls outside the exceptions detailed above.
- 9 section 911A(1) FSRA