



Action and no-action on superannuation advice

Mark Bland CLARENDON LAWYERS

On 7 November 2008, Tony D'Aloisio threw a lifeline to superannuation trustees trying to answer switching queries from members amid these choppy market conditions. The lifeline took the form of a letter from the chairman of the Australian Securities and Investments Commission (ASIC) offering to provide no-action relief to trustees on application (chairman's letter). Service providers put their hands up for relief too, and so two weeks later ASIC threw another lifeline by way of email to enquiring service providers (or via their lawyers). Accountants and financial advisers may legitimately wonder whether one might be thrown at them, too.

The relief appears to be targeted at protecting trustees and their service providers from unintentionally giving "implied advice". While industry associations are polarised on whether or not this is an admission that the current definition of financial product advice prohibits so-called "limited advice", it is generally welcomed as an extraordinary measure in extraordinary times. However, David Atkin, CEO of Cbus, reportedly said Cbus doesn't need the relief. If Jacques Derrida, father of deconstruction, were alive he might encourage us to first scrutinise the assumptions underlying the language in chairman's letter. Derrida was big on irony. And the irony of this no-action is the action in its underlying assumptions.

The action in the chairman's offer of no-action is to reinforce ASIC's interpretation of the financial product advice laws, an interpretation that has been previously reinforced by ASIC policy announcements and ASIC surveillance and enforcement actions. This interpretation has been generally accepted by industry, as is evidenced by numerous submissions made to parliamentary enquiries, working groups and regulators alike. However, taken with an additional dose of risk management it has paralysed industry. One industry body took the no-action letter as confirmation that the law "does not support the provision of information and limited advice without regulatory intervention".

This article first addresses the no-action letter and its evolution, scope and effect. It then sets out a legal basis for casting doubt in the minds of industry and, it is hoped, the federal government's Financial Services

Working Group about the validity of the concept of "implied advice". It goes on to touch upon the foundations of an alternative interpretation of financial product advice that would facilitate more accessible and affordable advice and enable trustees to provide genuine consumer education where conflicts are absent or effectively managed.

Trustees and service providers may still be considering whether they need the relief. Perhaps by the end of this article, they will find that they need it less than they presently think.

No action

Outline of relief

In the letter to industry associations dated 7 November 2008, the chairman stated that:

ASIC is prepared to provide relief [to provide limited guidance to members' switching queries] on application by superannuation trustees on the terms outlined below.

The letter goes on to note ASIC's awareness that funds have been receiving member requests to either change investment options out of "growth", switch funds or switch to a non-superannuation investment. It also states ASIC's desire to ensure that members have "full access to information about the effects" of such actions, "particularly at this time of market volatility".

The letter then sets out a list of the kinds of statements in respect of which trustees will be granted relief from strict compliance with the licensing and disclosure provisions in Ch 7 of the Corporations Act 2001 (Cth) (the Act). Naturally, the kinds of statements are designed to deal with questions from members arising from the recent market volatility.

The relief is to be provided by way of a no-action position and is subject to a number of conditions, relating to both conduct and disclosure.

The conduct conditions are that no "express recommendation or statement of opinion" is made to switch funds or change investment options or contribution levels. The trustee must also keep a record of particulars of statements made to members and maintain adequate dispute resolution mechanisms.

The disclosure conditions require statements that the trustee is not licensed to provide the advice (if applicable), that personal circumstances have not been taken into account, and that the trustee may have an interest in the member maintaining their current investment options or retaining their investment in the fund.

Later advice from ASIC is that any no-action position towards a trustee applicant will be extended to "persons acting on the trustee's behalf" where the trustee identifies those persons and has obtained confirmation in writing from those persons that they will comply with the conditions of the no-action position.

The application fee is waived and there is no need to make out the case, as an applicant is usually required to do under Regulatory Guide 108: *No-action letters* (RG 108).

What is a no-action letter?

The regulatory purpose of a no-action letter is business facilitation. No-action letters are often sought for past and continuing breaches; however, RG 108 does contemplate the use of no-action letters for future conduct. No-action letters give ASIC the flexibility to provide relief for future conduct in circumstances where it is unable to modify the law or grant an exemption.

In this case, no-action letters are being granted by way of a sort of "invitation to treat" with pre-approved terms and conditions. This is unusual and ASIC's efforts of business facilitation should be acknowledged.

However, trustees that successfully apply and rely on this no-action letter should be aware of the limitations of no-action letters. A no-action letter is no safe-harbour. RG 108 clearly states that a no-action letter:

- is only a statement of current regulatory intent. It is not a guarantee that ASIC will not take regulatory action in the future (see RG 108.2 and RG 108.13-16);
- is not a substitute for applicants carefully considering their actions and the consequences of their actions; and
- is not a de-facto ruling or precedent.

Rigorous monitoring and supervision procedures are required to comply with the financial product advice laws, for non-licensed entities as much as licensed ones. While a trustee is encouraged to take full advantage of the no-action letter, a prudent approach would be to rely on this no-action as a second line of defence and not as a wholesale replacement of existing procedures. In any case, exactly how much relief has been granted depends on the interpretation of the financial product advice laws you adopt.

Service providers

It will be interesting to see how ASIC applies the service provider extension. Service providers can come in all shapes and sizes. Some service providers have their own AFS licence; however, others may be authorised representatives of the trustee, authorised representatives of another licensee or entirely unlicensed.

ASIC has indicated that it will extend relief to service providers "acting on the trustee's behalf". This appears to be a clear reference to s 911B(1) of the Act, which contemplates representatives, authorised representatives and a licensee acting on behalf of another licensee. However, where these relationships do not exist (ie in an unlicensed environment), the "acting on the trustee's behalf" requirement could also be satisfied by common law principles of agency.

Before applying for relief for its service providers, it would be prudent for trustees to consider the extent of their liability for representations made by their service providers.

The first question to consider is the existence and scope of any agent/principal relationship. Whether a relationship of agency exists depends on the circumstances and true nature of the relationship, not on the terminology used by the parties.¹ While the traditional view of agency involves the agent having the capacity to create legal relations between the principal and a third party, the terms of agency may be limited so far as merely to make representations on behalf of the principal.

Under the common law principles of agency, a principal is liable for the conduct of its agent (including any misleading or deceptive conduct), not only where the agent's conduct is within authority but also where the agent acts outside its authority and this fact is not apparent to a third party.² By way of illustration, if a service provider was authorised to give general financial product advice only, but gave implied personal advice to a member, it is unlikely that the member would be aware that the service provider is acting outside its authority because the member is unlikely to be able to distinguish between general and personal advice. Accordingly, the trustee is likely to be liable for any implied personal advice that the service provider gives to a fund member.

Division 6 of Pt 7.6 of the Act enhances the liability of a principal for its agent where the principal is a licensee and the agent a representative (including authorised representative), particular in relation to conduct outside the agent-representative's authority.

If the service provider has its own licence and provides advice on behalf of the trustee licensee, although the Act provides that the advice is provided under the service provider's licence,³ the common law principles of agency will apply in respect of liability.



Scope of the relief

Relief is granted for statements of the following kind:

- “the differences between a guaranteed bank deposit and a long-term investment in a portfolio of marked-linked investments”;
- “the implications of transferring changing investment options, transferring to another fund or withdrawing their super (including, for the latter two, loss of insurance and crystallisation of investment losses and, for withdrawals, taxation consequences”);
- “that superannuation is a long-term investment”; and
- “reasonable statements concerning the relative return and volatility characteristics of different kinds of investments”.

However, this is limited by the prohibition on “express recommendations” mentioned above. More precisely, this condition is that the trustee (or service provider):

... not make any express recommendation or statement of opinion that the superannuation fund member:

- acquire or dispose of a financial product of class of financial products; or
- change their investment options within, or contribution level in relation to, any financial product or class of financial product.

The requirement that the trustee disclose that it may have an interest in the member not changing investment options or funds potentially puts certain trustees in the same position as they are for the Consumer Advisory Warning in the fee template, declaring something that does not exist. However, the extreme nature of the volatility may have led some trustees to reflect on how disinterested they (or their agents) really are.

Intended effect of the relief

The prohibition of express recommendations suggests that the relief appears to be targeted at so-called “implied advice”. In other words, ASIC is saying that it will take no action where a trustee gives factual information to a member which, because of the surrounding circumstances in which the information is given, constitutes a recommendation and is therefore financial product advice.

Actual effect of the relief: implied advice

The actual effect of the relief depends on the concept of “implied advice” and, more broadly, the definition of financial product advice⁴(Definition).

The predecessor and obvious parent to the concept of “implied advice” is the concept of “implied recommendation” in the pre-FSR Corporations Act and Corporations Law (pre-FSR Act).

The pre-FSR Act required certain disclosures and a reasonable basis when a securities adviser provided a “securities recommendation”.⁵ “Securities recommendation” was defined to mean:

... a recommendation with respect to securities or a class of securities, whether made expressly or by implication.⁶

In considering what “recommendation” means in this definition, Justice Lehane observed:

Whether what is said in a particular case amounts to a recommendation involves a consideration of the precise words used and of their context.⁷

This was subsequently applied in a number of AAT decisions relating to ASIC administrative actions.⁸

The importation of the concept of an implied recommendation into the FSR regime was made in ASIC’s Regulatory Guide 36: *Licensing: financial product advice and dealing*:

Where factual information is presented in a manner that may reasonably be regarded as suggesting or implying a recommendation ... the communication may constitute financial product advice (e.g. where the features of two products are compared in a manner that suggests that one compares more favourably than the other).⁹

This may be the most troublesome statement of the FSR era. It is the genesis of the concept of “implied advice”, but it is questionable on two grounds.

First, the Act does not contain any definition of “recommendation”. And nowhere has the concept of a recommendation being either express or implied been brought from the pre-FSR Act into the Act. Furthermore, “securities recommendation” was used in the pre-FSR Act in the context of being made by a “securities adviser”. “Recommendation” is used in a more neutral context in the Act, being made by “a person”. It can be reasonably concluded from this that Lehane J’s comments and subsequent judgments that emphasise the importance of the context of a communication have limited application to the interpretation of the Definition.

Second, ASIC’s statement in RG 36.22 appears to confuse different aspects of the Definition to create a concept not in the Definition itself.

Commentary reinforces the confusion, illustrating RG 36.22 with this example:

This may occur, for example, if factual information is provided selectively with the intention of influencing a financial product decision.¹⁰

The commentator goes on to say that such conduct would also likely be misleading or deceptive, a statement with which I entirely agree. However, it is not clear that it is financial product advice.

The Definition requires, among other things, both:

- a recommendation or statement of opinion; and

- an intention to influence a person in making a decision, etc, including where such an intention could “reasonably be regarded”.

The phrase “reasonably be regarded” imports a concept of implied (or more correctly, inferred) advice, but it relates to the “intention to influence” element. It does not relate to the existence of a recommendation or statement of opinion. Considering the express inclusion of the concept of a reasonable inference in one place, it is very difficult to read into another place in the same section.

The Definition would incorporate implied advice if the words “opinion or recommendation” were replaced with “a representation”. However, it does not state that and to read it as such gives no weight to the words “opinion or recommendation”.

On this interpretation, a communication is unlikely to be financial product advice unless the communication is an express opinion or recommendation. If factual information is given with the intention to influence a person to make a decision about a financial product, etc, it may be misleading or deceptive, but it is unlikely to be financial product advice.

This interpretation gives the words in the Definition their literal meanings and is consistent with their ordinary usage. It is not contradicted by anything in the relevant explanatory memoranda or statements.

Based on this interpretation, the no-action may have no legal effect. Because it excludes any express recommendation, it therefore potentially excludes any financial product advice. Ironically, it will still achieve its regulatory purpose of business facilitation and getting more information to members in response to their switching queries, because trustees generally are concerned about implied advice.

And trustees may well be right to be concerned about implied advice because, although a no-action letter is not a statement of the law, it is consistent with ASIC policy and has been reinforced by ASIC surveillance and enforcement actions. An example of enforcement action on implied advice is the AMP Financial Planning Enforceable Undertaking (AMPFP EU).¹¹

It is noted that while the no-action letter focuses on providing certainty in relation to the difference between factual information and financial product advice, the AMPFP EU was concerned with a different type of implied advice. It was concerned with an express recommendation (to join AMP super fund) containing an implied recommendation about something else (to leave a client’s existing super fund). The alternative interpretation proposed above can apply equally to the AMPFP EU circumstances.

Interpreting “financial product advice”

The accepted interpretation of the Definition appears to provide little room for advice that is not financial product advice.

Most of the current debate about accessible and affordable intra-fund advice is confined to a linear perspective. It is about the boundaries between factual information, general advice and personal advice. This perspective ignores the difference between financial product advice and non-financial product advice. In other words, there is advice that can be given in relation to superannuation that is not financial product advice.

Close scrutiny of the Definition reveals four other aspects of the definition that are critical to its scope. These four aspects are the meanings of “intention to influence”, “in relation to [a particular financial product]”, “class of financial product” and the concept of implied advice (as it relates to an inferred intention to influence).

There is some informative case law, both in a financial services context and in other contexts. However, many of the recent consent orders and Federal Court declarations touching on the Definition have been obtained by ASIC largely unopposed. This raises a concern that ASIC’s interpretation of the Definition is gaining legitimacy by way of judicial application in the absence of the rigour that comes from a strong contradictor.

Intention to influence

The most forgotten element of the Definition is the “intention to influence” element. This element is crucial because it imports a conflict of interest scenario into the Definition. Where there is no conflict of interests or conflicts are effectively managed, there is unlikely to be any actual or reasonably inferred intention to influence. An interpretation that gives appropriate weight to this element could open the door to genuine educational communications by freeing them from the burdens of AFS licensing and disclosure obligations.

Class of financial product

While it is generally accepted that “superannuation” is a class of financial product for the purpose of the Definition, there are numerous arguments against that view. The most compelling argument lies in the text of the so-called asset allocation exemption,¹² the language in which is entirely inconsistent with “superannuation” being a class of financial product.

Notwithstanding this, there are a number of judgments that treat “securities”, “derivatives” and, by extension, “superannuation” as either financial products themselves or as a class of financial products, apparently adopting



ASIC submissions without closely scrutinising the relevant provisions of the Act. These cases generally relate to wealth creation seminars on, for example, exchange traded options (ETOs), without referring to specific products.¹³

While there are numerous aspects of the Act that support a narrower definition of class for the purpose of the Definition, regulations that could be made in this respect have not been made.

"In relation to"

The meaning of "in relation to" has been discussed at great length in Australian and English case law.¹⁴ There is a general consensus on how this "protean concept"¹⁵ should be interpreted. However, there is disagreement in its application in specific legislative contexts.

Goldberg J applied the case law recently in *ASIC v Citrofresh International Ltd*,¹⁶ which related to a statement made by Citrofresh International Ltd, a public company listed on the ASX, suggesting that Citrofresh (the company's disinfectant product) may cure HIV and other viruses.

His Honour stated that while the phrase gathers its meaning from the context in which it appears, it does not extend to "any relationship however tenuous". It must be based on some more substantial ground. Quoting Taylor J in *Tooheys*,¹⁷ Goldberg J said that the "vital question is whether [it] "relates" and not whether it may be "related" by an examination of extraneous circumstances".

While his Honour's interpretation was found on appeal to be too narrow,¹⁸ the Full Federal Court's reasoning was heavily influenced by the particular wording in s 1041H and the broad compass of the misleading and deceptive conduct prohibition. There is potential for the application of these principles to create a significant narrowing of the scope of the Definition.

Where an intention to influence can be reasonably regarded

An intention to influence generally arises in a conflict situation. Furthermore, it is reasonable to regard (or infer) such an intention where conflicts of interest exist. However, there may be considerable scope for trustees, fee for service planners and accountants to manage the reasonableness of any such inference by managing its conflicts and using effective disclosures.

Conclusion

The positive practical effect of ASIC's no-action position is to be welcomed and ASIC congratulated for its efforts to facilitate business and to improve consumer education. However, the no-action letter also contains

the action of reinforcing ASIC's interpretation of the definition of financial product advice which has been generally accepted by industry and gathers legitimacy with each undefended prosecution borne out of the commercial impracticalities of litigating against ASIC.

This article only touches on some of the key legal arguments that support an interpretation that recognises the role of advice that is not financial product advice, creates more certainty about what communications are caught by the Definition and gives appropriate weight to the concept of conflicts of interest which is imported by the "intention to influence" element. It is also an interpretation that requires no law reform to facilitate more affordable and accessible advice and genuine consumer education from financial services providers where conflicts are absent or effectively managed.



Mark Bland,
Senior Associate,
Clarendon Lawyers,
Mark.Bland@clarendonlawyers.com.au,
www.clarendonlawyers.com.au

Footnotes

1. *Re Nevill; Ex parte White* (1871) LR 6 Ch App 397.
2. This may be subject to judicial notice of established practice in a particular context or industry, as was considered for settlement practices of stockbrokers in regards to share transfers in *Tobin v Broadbent* (1947) 75 CLR 378; [1948] 1 ALR 25; (1947) 21 ALJR 478; BC4700530.
3. Section 911B(3).
4. Section 766B(1).
5. Sections 849 and 851.
6. Section 9.
7. *Hadid v Lenfest Communications Inc* [1999] FCA 1798; BC9908522 at [1049].
8. *Jungstedt v ASIC* (2003) 73 ALD 105; [2003] AATA 159; BC200308952 (14 February 2003) and *Felden and ASIC* (2003) 73 ALD 149; 45 ACSR 111; [2003] AATA 301 (1 April 2003).
9. RG 36.22.
10. LexisNexis Financial Services at [7.0200].
11. In the AMPFP EU, it is clear that ASIC considered that when many AMPFP advisers expressly recommended an AMP superannuation fund, they impliedly recommended to their client that they should either cease contributing to their existing fund and/or roll their superannuation out of their existing superannuation fund into the AMP fund. Based on this view, ASIC concluded that the AMPFP advisers were providing financial product advice not only on the AMP fund, but also on the client's existing, non-AMP fund (see paras 2.5.3 and 3.2-3.5 of the EU).

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12. Regulation 7.1.33A of the Corporations Regulations 2001 (Cth) is entitled "Allocation of funds available for investment". This is not a note of the kind excluded from the Act by operation of s 13(3) of the Acts Interpretation Act 1901 (Cth).
13. *ASIC v Giann & Giann Pty Ltd* (2005) 141 FCR 278; 23 ACLC 276; [2005] FCA 81; BC200500281 See also *ASIC v Oxford Investments (Tas) Pty Ltd* (2008) 169 FCR 522; [2008] FCA 980; BC200805045 (30 June 2008). In *ASIC v Online Investors Advantage Inc* (2005) 23 ACLC 1929; 194 FLR 449; [2005] QSC 324; BC200509400 (26 October 2005), ASIC submitted that "the effect of reg 7.1.33A is to prevent the problem of general and educational comments in for example textbooks from the operation of the provisions".
14. In addition to cases cited below, see also *Rein v Lane* (1867) LR2QB 144; *Smith v Cator* (1819) 106 ER 549; *Tooheys Ltd v Commissioner of Stamp Duties (NSW)* (1961) 105 CLR 602; [1962] ALR 195; (1961) 35 ALJR 109; BC6100860 and *ASIC v Oxford Investments (Tas) Pty Ltd* (2008) 169 FCR 522; [2008] FCA 980; BC200805045.
15. *Regina v Lewis* [1989] NTSC 33 (30 June 1989) per Kearney J at [6].
16. (2007) 164 FCR 333; 245 ALR 47; [2007] FCA 1873; BC200710475.
17. Above, note 14.
18. *ASIC v Narain* (2008) 169 FCR 211; 247 ALR 659; [2008] FCAFC 120; BC200805198.