

CHAPTER 2

REVIEW OF REGULATION 7.1.29

History

2.1 Regulation 7.1.29 was one of many regulations made to support the reforms introduced into the *Corporations Act 2001* (the Act) by the *Financial Services Reform Act 2001* (the FSR Act) from 11 March 2002.¹

2.2 The original regulation was intended to provide a licensing exemption for certain activities carried out by ‘recognised accountants’ in the course their work. Without such an exemption, accountants would have to be licensed to engage in these activities as they constituted the provision of a ‘financial service’ under the Act.²

2.3 During the Committee’s inquiry last year into the regulations and ASIC policy statements made under the FSR Act, regulation 7.1.29 attracted extensive criticism from the accounting profession.³

2.4 The main objections were that:

- the regulation defied interpretation; and
- the intended licensing exemption was too narrowly framed.

2.5 In relation to the second point, accountants argued that the exemption should cover ‘traditional accounting activities’. This, they said, was consistent with the findings of the Financial System Inquiry’s Final Report and similar to the ‘incidental advice exemption’ that had worked well under the previous regime.

2.6 They argued that an exemption falling short of the ‘incidental advice exemption’ would merely increase costs and do little for consumer protection. They were concerned that small accounting practices which they said looked after the

1 Regulation 7.1.29 was contained in Corporations Amendment Regulations 2001 (No. 4), Statutory Rules 2001 No. 319. References to ‘qualified accountant’ were replaced by ‘recognised accountant’ in Corporations Amendment Regulations 2002 (No. 3), Statutory Rules 2002 No. 41 to provide ASIC with the flexibility to make determinations regarding a person’s status as a ‘recognised accountant’ for the purposes of the regulation.

2 See subsection 766A(1) which sets out when a person provides a financial service. Section 911A says that a person who carries on a financial services business must hold an Australian financial services licence. See also section 911D. These provisions were introduced into the Act by the FSR Act.

3 *Report on the regulations and ASIC policy statements made under the Financial Services Reform Act 2001*, tabled on 23 October 2002. See Chapter 5, pp. 29-37.

majority of self-managed superannuation funds (SMSFs) would no longer be able to deliver cost-effective services or any services at all to these funds.

2.7 Although paragraph 766B(5)(c) of the Act provides a licensing exemption in certain instances to tax agents registered under the *Income Tax Assessment Act 1936* (ITAA), accountants said this was not wide enough to cover the type of taxation advice they commonly gave to clients. They said the regulation should incorporate an exemption for this type of advice as well.

2.8 The Committee's conclusions were that the regulation was unworkable. It also thought that the intended licensing exemption was too narrow and recommended that:

- The Act or regulation 7.1.29 should be amended to provide a licensing exemption for accountants similar in terms to that provided to lawyers in paragraphs 766B(5)(a) and (b) of the Act. This was a fairly broad exemption more akin to the 'incidental advice exemption' previously in place.
- The exemption should not apply where payment for the activity was in the form of commission or a similar benefit made by a third party not connected with the client.⁴

2.9 The Report by the Labor Members urged the Government to re-draft the regulation as soon as possible to ensure certainty about what activities would be regulated. The Labor Members thought the licensing exemption should not apply where advice given by accountants was financial product advice.⁵

Overview of the provisions

2.10 Regulation 7.1.29 has been made under paragraph 766A(2)(b) of the Act which provides that the regulations may set out the circumstances in which persons are taken to provide, or are taken not to provide, a financial service.

2.11 The regulation sets out 'the circumstances in which a person is taken not to provide a financial service and therefore does not need to be licensed' when performing those services.⁶ The Explanatory Statement summarises these circumstances as relating to:

- administrative tasks such as the registration of companies;
- advice on shelf companies and trusts;
- audit advice;
- business advice;

4 *Report on the regulations and ASIC policy statements made under the Financial Services Reform Act 2001*, tabled on 23 October 2002. See Chapter 5, p. 36.

5 *Report on the regulations and ASIC policy statements made under the Financial Services Reform Act 2001*, tabled on 23 October 2002, p. 82.

6 Explanatory Statement, Corporations Amendment Regulations 2003 (No. 3), p. 1.

- risk management advice;
- superannuation advice; and
- taxation advice.⁷

2.12 Unlike its predecessor, which applied to a ‘recognised accountant’, the current regulation refers to ‘a person who provides an eligible service’ and is therefore capable of applying to persons other than accountants.

The provisions in detail

2.13 Under subregulation 7.1.29(1), a person who provides an ‘eligible service’, which is one and the same as a ‘financial service’, is taken not to provide a financial service if the following three criteria are satisfied:⁸

- the eligible service is provided in the course of conducting an ‘exempt service’; and
- it is reasonably necessary to provide the eligible service to conduct the ‘exempt service’; and
- the eligible service is provided as an integral part of the ‘exempt service’.

2.14 Subregulations 7.1.29(3), (4) and (5) specify the activities that constitute an ‘exempt service’. According to the Explanatory Statement, these activities are those to which the exemption applies.

2.15 The ‘exempt services’ listed in subregulation 7.1.29(3) include:

- Advising on auditing activities.⁹
- Advising on risk assessment for a business.¹⁰
- Advising on the acquisition or disposal, administration, due diligence, establishment, structuring or valuation of an incorporated or unincorporated entity provided it is given to an interested party (or a person who is likely to become an interested party) and is confined to a decision about:
 - the securities of an entity that carries on or may carry on the business of the entity; and
 - the interests in a trust that carries on or may carry on the business of the trust,

7 Explanatory Statement, Corporations Amendment Regulations 2003 (No. 3), p. 1.

8 Subregulation 7.1.29(2) defines ‘eligible service’ as conduct mentioned in paragraphs 766A(1)(a) to (f) of the Act.

9 Paragraph 7.1.29(3)(a).

10 Paragraph 7.1.29(3)(b).

but the advice cannot be about other financial products that the entity or trust may acquire or dispose of and it cannot be advice included in an exempt document or statement.¹¹

- Advising on securities in a company if the company is not carrying on a business and has not carried on a business (except where such securities are or will be the subject of the fundraising provisions of Chapter 6D of the Act)—in other words, advice on a shelf company.¹²
- Advising on interests in a trust if the trust is not carrying on a business and has not carried on a business (and excluding a superannuation fund or managed investment scheme that is registered or required to be registered)—in other words, advice on a shelf trust.¹³
- Advising in relation to the transfer of financial products between related bodies corporate.¹⁴
- Arranging for a person to deal in relation to interests in a self-managed superannuation fund in the circumstances specified in paragraphs (5)(b) and (c) of regulation 7.1.29.¹⁵
- Arranging for a person to deal in a financial product by preparing transfer or registration documents on instruction from that person.¹⁶
- Advising on the provision of financial products as security except when the security is used to acquire other financial products.¹⁷

11 Paragraph 7.1.29(3)(c). The Explanatory Statement for this provision says: ‘This activity concerns advice to an incorporated entity or unincorporated entity on administrative and operational issues. The most common use of this provision is likely to be a person advising the management of a company. The advice must only be in relation to the actual entity carrying on the business or related entities such as subsidiaries’.

12 Paragraph 7.1.29(3)(d)(i)

13 Paragraph 7.1.29(3)(d)(ii).

14 Paragraph 7.1.29(3)(e). The Explanatory Statement for this provision says that licensing is not needed here ‘because there is largely limited or no change in beneficial ownership of the financial products involved, such as insurance’.

15 The Explanatory Statement for this provision says: ‘This allows a person to undertake tasks such as rolling over funds into a SMSF, such as where the decision to roll over the funds has already been made. However, this arranging exemption will only apply to a SMSF given the need to assist member-trustees operate their own funds. Arranging can only be provided to persons mentioned in paragraph (5)(b) and must not be inconsistent with the limitation in paragraph (5)(c)’.

16 Paragraph 7.1.29(3)(g). The Explanatory Statement says for this provision that: ‘The provision of ‘arranging’ activities needs to be distinguished from the ‘financial product advice’ that recommends the registration or transfer of a financial product. That advice must fall within an exemption (either under this regulation or elsewhere under the Act) or require licensing’.

17 Paragraph 7.1.29(3)(h).

2.16 Under subregulation 7.1.29(4), a person provides an exempt service if the person advises on taxation issues involving financial products and:

- the adviser will not receive a benefit (for example, commission) other than from the client as a result of the client's acquisition of a financial product recommended by the adviser and either—
 - the advice is not a recommendation or opinion about a financial product¹⁸ given to a retail client; or
 - if the advice is such a recommendation or opinion given to a retail client, the retail client must be advised in writing that the adviser is not licensed to provide such advice, that taxation is only one matter relevant to a decision on a financial product and the client should consider obtaining advice from an Australian financial services licensee.

2.17 The Explanatory Statement says in relation to subregulation 7.1.29(4) that:

This activity provides an exemption from FSR licensing when providing taxation advice...

...this exemption cannot be used...to market or sell financial products without a licence on the basis that a person is promoting taxation advantages and providing taxation advice. Therefore, a person cannot use this exemption if they receive a benefit from a third party, such as a commission, following a client acquiring a financial product as the result of the advice.

Taxation advice should not be the only consideration in making an investment decision. Therefore, if taxation advice includes financial product advice provided to a retail client, a written disclosure statement must be provided.¹⁹

2.18 Subregulation 7.1.29(5) provides that an exempt service is advice given regarding the establishment, operation, structuring or valuation of a superannuation fund in the following circumstances:

- advice included in an exempt document or statement is not exempted; and
- the person advised is or is likely to hold an office in or control the management of the fund; and

18 The term used in the legislation is 'financial product advice' which is defined in subsection 766B as being a recommendation or a statement of opinion that is intended to influence or could reasonably be regarded as intended to influence a person in making a decision about a financial product.

19 Explanatory Statement, Corporations Amendment Regulations 2003 (No. 3), p. 4.

- except for advice given for the sole purpose and to the extent reasonably necessary to ensure the advised's compliance with superannuation legislation (but not concerning the fund's investment strategy),²⁰ the advice²¹—
 - must not concern the acquisition or disposal of specific financial products by the fund;
 - must not include a recommendation that a person acquire or dispose of a superannuation product;
 - must not include a recommendation about a person's investment strategy in a fund or level of contributions; and
- if the advice is financial product advice given to a retail client, the client must be advised in writing that the adviser is not licensed to provide the advice and the client should consider taking advice from an Australian financial services licensee.

2.19 To summarise, the exemption in subregulation 7.1.29(5) applies to advice given to actual or proposed office bearers or managers of a superannuation fund or proposed fund. This advice can be about the structure a new fund should take or what is required to ensure compliance with relevant legislation, for example. The advice cannot consist of recommendations about the suitability of a superannuation fund as an investment (or preferred investment) vehicle or what investment strategy the fund should adopt. The exemption clearly does not apply to any advice given to a retail client about joining a superannuation fund or about the client's existing membership in a fund.

2.20 The Explanatory Statement for subregulation 7.1.29(5) says the following are circumstances in which consumers cannot be advised on investment decisions unless the adviser is licensed:

- a person becoming a member of a fund;
- an existing member of a fund joining another subplan of that fund;
- a superannuation product changing from the growth to the pension phase;
- transferring benefits between investment options;
- making additional and voluntary contributions to a superannuation fund; and
- deciding what financial products should be held by a superannuation fund.²²

20 This is the *Superannuation Industry (Supervision) Act 1993* (except for paragraph 52(2)(f)), the *Superannuation Industry (Supervision) Regulations 1994* (except for regulation 4.09) or the *Superannuation Guarantee (Administration) Act 1992*.

21 These exceptions relate to the trustee's covenants to formulate and give effect to a fund's investment strategy taking into account specified circumstances.

22 Explanatory Statement, *Corporations Amendment Regulations 2003* (No. 3), p. 5.