

# FEATURE ARTICLE

*For Immediate Release*

## ‘ The Perils of Not Giving Advice ’

As a consequence of the Financial Services Reform Act (FSRA) in early 2004, the strata and insurance industries in Australia have undergone radical changes as to how they provide financial (insurance) services to their clients.

New concepts and obligations were introduced which nowadays govern how Body Corporate Managers provide insurance services under their Management Agreements. Those reforms include the differentiation between ‘retail’ and ‘wholesale’ clients and products, and how Body Corporate Managers communicate with their respective Body Corporate.

### How can I provide a financial service?

To be able to provide a financial service and arrange insurance under the Corporations Act a Body Corporate Manager must choose to be appointed as either (1) a ‘Distributor’ or (2) an ‘Authorised Representative’ of an Australian Financial Services (AFS) licensee.

The financial product information that can be imparted by ‘Distributors’ and Authorised Representatives’ does vary.

**(1) ‘Distributor’** - Body Corporate Managers appointed as ‘Distributors’ may only ‘arrange’ financial products – they are **not** allowed to provide any advice (general or personal) at all in relation to the insurance product or services. Distributors may, however, provide factual information (which is regarded as being accurate and objective) about the insurer and the insurance product.

**(2) ‘Authorised Representative’** – Body Corporate Managers appointed as ‘Authorised Representatives’ may provide factual information **and** advice, in addition to arranging the strata insurances. Advice authorities are dependent upon the level of training undertaken and the authorisations issued by the licensee.

### What are the differences between the two ‘models’?

Aside from providing financial product advice, both the Distributor and Authorised Representative models are the same as to how they impact a Body Corporate Manager. Disclosure requirements differ depending on the model selected however the Body Corporate Manager must still issue a Product Disclosure Statement (PDS) and continue to provide a Financial Services Guide (FSG) which outlines remuneration received, etcetera.

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## How does this impact my obligations and responsibilities?

The two main considerations for a Body Corporate Manager, when determining the appropriate model are:

- (1) the model which most appropriately fulfils his or her fiduciary obligations to the Body Corporate; and
- (2) the level of financial product advice it is they require to service their clients.

A fiduciary relationship exists between the Body Corporate Manager and the Body Corporate through the application of the Management Agreement, and through the relationship developed.

The relationship is also based on trust, honesty and confidence, which arises when one person is bound to act in good faith and in the interests of another person. The relationship that is developed between the two parties can be seen as a relationship of reliance. At the centre of any fiduciary relationship, a duty exists that relates to making available to the Body Corporate all information relevant to the beneficiary.

As the strata industry becomes more complex and more competitive, Body Corporate Managers will be expected to provide an improved level of service to their clients, which **will** include some form of advice required at some point by the Body Corporate. To successfully discharge this duty, a Body Corporate Manager would need to become an Authorised Representative with the appropriate advice authorisations issued.

## How appropriate is Factual Information?

Consideration should also be given to how the factual information best supports the services provided by a Body Corporate Manager.

Factual information should not contain an opinion or recommendation of any kind (actual or implied) and must contain only objectively ascertainable information. For example, a statement about the specific limits provided within the policy cover is considered to be factual information because this can be supported by the policy wording.

Let's say, for example, three lot owners are renovating their lots for \$150,000 each. The Body Corporate is aware of the renovations and would like to know whether the lot owners should increase the sum insured by \$450,000.

How would a reasonable Body Corporate Manager answer this question when factual information is defined as being accurate and objective information that does not contain an opinion or a recommendation?

The real danger in answering questions such as these is the ease in which they lend themselves to be answered with general advice. Remember, when a person provides financial product advice, they are making a recommendation or a 'statement of opinion' that is intended to influence the person making the decision about the financial product. Advice can be defined also as being given when the recommendation or opinion provided could reasonably be regarded as having that intention.

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It is also questionable as to whether a Body Corporate would be able to make an adequate assessment of their insurance needs and understand their obligations under the relevant strata legislation with factual information alone, despite those situations in which the presiding Body Corporate Manager is confident of his or her ability to provide factual information alone.

### **Is Training necessary for Distributors and Authorised Representatives?**

Both models require Body Corporate Managers to undergo thorough training. It is a misconception within the industry that training is not required when appointed as a Distributor. Under both models, Licensees must ensure the Body Corporate Manager is adequately trained and competent to provide a financial service.

### **What is the best solution?**

Although the 'Distributor' model offers the simplest and most cost-effective solution for Licensees to the authorisation process, situations will arise where providing factual information alone would not be possible, suitable or advisable.

All being said, Body Corporate Managers do have an overriding fiduciary obligation to their Bodies Corporate that should require them to provide some form of financial product advice.

The main issues involved in providing advice and the reluctance of some Body Corporate Managers to provide this advice, whether general or personal, can easily be attributed to misconceptions about the legislation and misinformation that is provided by various AFS Licensees.

Unfortunately, several licensees within the insurance industry have been advising the strata industry that it would be beneficial to reduce the level of strata services currently enjoyed by the market, such as providing factual information only and not providing general advice

In an industry where some sectors are questioning the payment of commissions to Body Corporate Managers, it would seem inadvisable and ill-conceived to reduce any of the services and standards currently enjoyed within the strata market.

Considering no further effort is really required in obtaining general advice authorisations, a prudent Body Corporate Manager should seriously consider becoming or remaining as an Authorised Representative.

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## **ASIC releases proposed reforms – November 2006**

In light of the issues raised above, ASIC has released notification of proposed reforms which will allow insurance agents such as Body Corporate Managers to provide advice (both general and personal) without triggering FSR compliance requirements.

The proposed reforms will allow Body Corporate Managers (most likely through the Authorised Representative model), to provide simple advice and guidance to help a customer decide whether a product suits their needs. The 'product sales recommendations' provided will not involve giving either a Statement of Advice (SOA) if the information is personal, or the General Advice Warning if the information is general.

Those reforms will greatly benefit the strata industry and allow more freedom in the provision of financial product advice being given to the Bodies Corporate.

CHU will closely monitor those reforms and provide more information when it becomes available.

For information concerning this article, or to enquire about CHU's training program, please phone Brad Sutton or Sylvia Wasef on 1300 361 263 or email [compliance@chu.com.au](mailto:compliance@chu.com.au)

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### **For more information contact:**

Shalom Paul, Marketing & Public Relations Manager

CHU Underwriting Agencies Pty Ltd

**Telephone: 02 8923 5340**

**Email: [shalomp@chu.com.au](mailto:shalomp@chu.com.au)**

Facsimile: 02 89235363

Address: Level 6, 1 Northcliff Street, Milsons Point NSW 2061 Australia

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