



**ASIC**

Australian Securities & Investments Commission

REGULATORY GUIDE 79

# **Managing conflicts of interest: A guide for research report providers**

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# What this guide is about

**1** This guide about managing conflicts of interest is for licensees who are research report providers. It is directed towards traditional providers of research on investment products—known variously as research analysts, securities analysts or research houses—and the research reports they traditionally provide.

Note: The important expressions ‘research report’, ‘research report provider’ and ‘research staff’ are defined in paragraphs [1.1]–[1.5] of this guide.

**2** The timely and accurate flow of information about issuers and securities is vital to the fair, efficient and transparent operation of financial markets. Research report providers are fundamental in the transmission of this information, and the integrity of their research impacts directly on the integrity of our financial markets.

**3** The conflicts management obligation requires a licensee to have adequate arrangements to manage conflicts of interest: s912A(1)(aa) of the *Corporations Act 2001*. This obligation and Policy Statement 181 *Licensing: Managing conflicts of interest* [PS 181] apply to all licensees, including research report providers and the integrity of their research. What an individual licensee needs to do to comply with the obligation varies according to the nature, scale and complexity of its financial services business.

Note: The conflicts management obligation has effect from 1 January 2005.

**4** This guide supplements [PS 181], and should be read together with that policy statement. [PS 181] focuses on broad principles and guidance for licensees generally in managing conflicts of interest, and sets out expectations that licensees should meet in order to comply with the conflicts management obligation: see [PS 181.16].

**5** Building on [PS 181], this guide describes various issues that research report providers should take into account in the design, implementation and maintenance of their conflicts management arrangements. It has three sections:

(a) **Section 1** is an introduction containing some important definitions (including the definition of ‘research report’ and ‘research report provider’), an overview of licensee obligations relating to conflicts of interest, and some background information on other Australian and international standards and principles that have influenced us in the preparation of this guide;

- (b) **Section 2** provides guidance on the issues that research report providers need to address in *controlling* and *avoiding* conflicts of interest; and
- (c) **Section 3** provides guidance on the issues that research report providers need to address in *disclosing* conflicts of interest.

Note: While this guide only applies to research report providers, it may assist others (particularly those licensees that provide general advice which is similar to the concept of 'research report' in this guide) to determine what they need to do to comply with the conflicts management obligation.

**6** This guide is not a summary of all legal obligations relating to conflicts of interest. Research report providers should consider other legislation, regulations and common law that apply to conflicts of interest situations, both within and wholly outside the licensee's financial services business.

Note: This guide does not apply to conflicts of interest that occur *wholly* outside a research report provider's financial services business, as these are beyond the scope of s912A(1)(aa).

## Why have we produced this guide?

**7** Australian and overseas experience has shown that there is considerable potential for conflicts of interest in the production of research reports. We are publishing this guide to supplement [PS 181] for research analysts because of the level of concern here and overseas to ensure that the integrity of the research report process is not compromised by conflicts of interest. This can be seen in:

- (a) the introduction of the conflicts management obligation as part of the *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004 (CLERP 9 Act)*;
- (b) 'Research analyst independence', ASIC surveillance report, 22 August 2003;
- (c) the Statement of Principles for Addressing Sell-side Securities Analyst Conflicts of Interest published by the Technical Committee of the International Organization of Securities Commissions on 25 September 2003; and
- (d) 'Report on analyst conflicts of interest, A report of the Technical Committee of the International Organization of Securities Commissions', September 2003; and
- (e) a number of initiatives by international regulators and industry representatives.

Note: See paragraph [1.12] for examples of these international regulatory initiatives.

## Why follow this guide?

8 Together with [PS 181], we will take this guide into account in administering the law, including whether to take action against any particular research report provider. In our view, licensees whose conflicts management arrangements are not consistent with the guidance and expectations in this guide are less likely to be complying with their obligations (in particular, the conflicts management obligation: see [PS 181.16]) and will be exposed to a greater risk of regulatory action.

9 In this guide, we describe various issues that we believe research report providers should consider in the design, implementation and maintenance of their conflicts management arrangements. What an individual licensee needs to do to comply with the conflicts management obligation may vary according to the nature, scale and complexity of the business the licensee carries on (and we will take this into account in administering the law). We do not think that we can, or should, provide exhaustive guidance on what research report providers need to do to comply with the law.

**Important note:** This guide is based on the law as at 3 November 2004. Examples are purely for illustration; they are not exhaustive and are not intended to impose or imply particular rules or requirements. This guide does not constitute legal advice. We encourage you to seek your own professional advice to find out how the Corporations Act applies to you. It is your responsibility to determine your obligations under the Corporations Act and regulations.

# Section 1: Background

## 'Research report' and related important definitions

### Research report

1.1 For the purposes of this guide, a research report is general advice that:

- (a) is in writing;
- (b) includes an express or implicit opinion or recommendation about a named or readily identifiable investment product; and
- (c) is intended to be, or could reasonably be regarded as being intended to be, broadly distributed (whether directly or indirectly) to clients (whether wholesale or retail) in Australia.

Note 1: Investment products include securities, warrants traded on a financial market, managed investment products, superannuation products and investment life insurance products. Reports about whether to buy, sell or hold these products prepared by research analysts, securities analysts or research houses are typical examples of 'research reports'.

Note 2: The expression 'broadly distributed' includes, but is not limited to, publication.

1.2 It does *not* include any of the following:

- (a) general advice that is provided only to an individual or small number of related clients (e.g. a family);
- (b) general advice that is provided only to related bodies corporate of the licensee;
- (c) general advice that is only about products issued by the licensee or its related bodies corporate;
- (d) a communication or piece of information that does not constitute general advice;
- (e) advice that does not contain any express or implied opinion or recommendation to buy, sell or hold a named or readily identifiable investment product;
- (f) advice that is merely a re-statement, summary or extract of another research report that has already been broadly distributed (whether in Australia or elsewhere and whether by the licensee or another person);

- (g) personal advice; or
- (h) advice that is not provided in Australia.

### **Research report provider**

**1.3** For the purposes of this guide, and subject to paragraph [1.4], a research report provider is a licensee that provides research reports to other persons (clients). This includes the situation where the licensee causes or authorises another person (such as an authorised representative of the licensee) to provide research reports to other persons (clients). A person that does not hold an Australian financial services (AFS) licence is not a research report provider for the purposes of this guide.

**1.4** If a research report prepared by one licensee (A) is provided to other persons (clients) by another licensee (B) then, for the purposes of this guide, A is the research report provider, and not B (regardless of whether B puts its own name on the research report), but only where:

- (a) A's licence covers the provision of the financial service;
- (b) A causes or authorises B to provide the advice contained in the research report to other persons; and
- (c) no material changes to the advice contained in the research report are made by B.

Where any of these conditions is not met, B will be the research report provider.

In any event, it is important to note that both A and B must consider the obligation to comply with the conflicts management obligation and should, in this regard, be guided by [PS 181].

### **Research staff**

**1.5** For the purposes of this guide, the research staff of a research report provider are all those natural persons (whether employees of the research report provider or not) that are involved in the preparation of research reports provided by the research report provider (including the managers of those natural persons). This guide has been written primarily to deal with the situation where the research staff are employees of the research report provider. However, where this is not the case, research report providers will still need to take reasonable steps to ensure that the integrity of the research they distribute is not undermined by conflicts of interest.

## Licensee obligations

**1.6** Research report providers are obliged (among other things) to:

- (a) do all things necessary to ensure that their financial services are provided efficiently, honestly and fairly (s912A(1)(a)); and
- (b) have in place adequate arrangements for managing conflicts of interest that may arise wholly, or partially, in their financial services business (s912A(1)(aa)).

**1.7** The conflicts management obligation and the obligation to operate efficiently, honesty and fairly are interconnected: see [PS 181.18]. Having adequate conflicts management and risk management arrangements will help licensees ensure they operate efficiently, honestly and fairly. Without such arrangements, it would be difficult for a licensee to ensure that it operates efficiently, honestly and fairly.

**1.8** A licensee must comply on an ongoing basis with the licensee obligations. This means that a licensee must determine on an ongoing basis what mechanisms need to be in place to ensure their conflicts management arrangements are adequate.

## Inputs to this guide: related standards and guidance

### Australian guidance

**1.9** We acknowledge the work done by the Securities Institute of Australia (SIA) and the Securities and Derivatives Industry Association (SDIA) in developing ‘Best practice guidelines for research integrity’, November 2001 (SIA/SDIA Guidelines).

We believe our guidance and expectations are generally consistent with these guidelines. We recognise that on some topics, this guide is more detailed or extensive than the guidelines.

### International guidance

**1.10** We have considered equivalent overseas requirements for analyst independence, the integrity of research reports and conflicts management. We recognise that some research report providers will also be subject to foreign rules or standards for managing conflicts of interest. Regardless of this, each research report provider must ensure compliance with the Australian conflicts management obligation. However, by complying with comparable foreign rules or standards, we anticipate that

some research report providers will already be acting consistently with most of this guide.

**1.11** The International Organization of Securities Commissions published a ‘Statement of Principles for Addressing Sell-side Securities Analyst Conflicts of Interest’ on 25 September 2003. We have taken these principles into account in developing this guide. We believe that this guide and the IOSCO principles are consistent.

Note: The IOSCO principles are available at [www.iosco.org](http://www.iosco.org).

**1.12** We have also taken into account:

- (a) the UK Financial Services Authority’s work on conflicts of interest and investment research (CP 171, CP 205 and PS 04/06), which has resulted in changes to the ‘Conduct of business handbook’;
- (b) the European Union amendments to the Investment Services Directive and Market Abuse Directive that subject research services to the provisions about conflicts of interest and include a conflicts disclosure obligation respectively;
- (c) the US Securities and Exchange Commission’s Regulation Analyst Certification (Regulation AC) that requires a statement by the research analyst(s) certifying that the views expressed in the research report accurately reflect their personal views and that other possible influences on the integrity of the research have been managed; and
- (d) the new conflicts management rules introduced by the National Association of Securities Dealers (NASD) and the New York Stock Exchange (NYSE), Rule 2711, and Rules 351 and 472, respectively.

## Section 2: Controlling and avoiding conflicts of interest

**2.1** To comply with the conflicts management obligation, a research report provider needs to have adequate arrangements to manage conflicts of interest. What is adequate depends on the facts and circumstances. Some conflicts of interest should be avoided entirely. Other conflicts, however, can be addressed by adequate controls and appropriate disclosure.

The three key mechanisms we expect research report providers generally to use to manage conflicts of interest are *controlling*, *disclosing* and *avoiding* conflicts of interest: see [PS 181.20]. This section provides guidance on the issues that need to be considered in *controlling* and *avoiding* conflicts of interest, while Section 2 discusses issues that need to be considered in *disclosing* conflicts of interest.

### General guidance and overview

**2.2** Research report providers should take reasonable steps to ensure that conflicts of interest:

- (a) do not compromise the integrity of the advice they give in their research reports;
- (b) do not result in the licensee breaching its duties including (but not limited to) the duty to act efficiently, honestly and fairly; and
- (c) are adequately disclosed.

**2.3** To control conflicts of interest, research report providers should have mechanisms to:

- (a) identify conflicts of interest;
- (b) assess and evaluate those conflicts; and
- (c) decide upon and implement an appropriate response to those conflicts: see [PS 181.29].

**2.4** A culture of integrity that includes an ethical approach to conflicts of interest should be encouraged. However, this is no substitute for implementing, maintaining and monitoring robust policies and procedures.

Note: See paragraph 5.47 of ASIC's surveillance report 'Research analyst independence' for a discussion on an 'unacceptable level of reliance on staff integrity in some entities'.

2.5 The rest of this section provides guidance on issues that research report providers should address when developing and implementing their arrangements for controlling and avoiding conflicts of interest. The issues are summarised in Table 1.

**Table 1: Issues to be considered in controlling and avoiding conflicts of interest**

Issue	Summary
Documentation	Conflicts management arrangements should be documented: see paragraph [2.6].
Monitoring compliance	There should be a person or separate unit responsible for monitoring compliance with the research report provider's conflicts management arrangements: see paragraphs [2.7]–[2.8].
Communication	Research report providers should have a detailed policy on communications within and outside the licensee, including ensuring that research reports are not communicated outside the research report provider before they are broadly distributed: see paragraphs [2.9]–[2.10].
Information barriers	Any information barriers should be robust. Generally, research staff should be physically separate from, and not supervised by, any staff who are performing an investment banking, corporate advisory or dealing function: see paragraphs [2.11]–[2.12].
Approval before distribution	To maintain the quality and integrity of reports, research reports should be reviewed and approved by an experienced supervisor (or by a group of peers) before they are distributed to clients: see paragraph [2.13].
Provision of non-research services	Research report providers should have a policy on how and when non-research services are provided to an issuer for whom the research report provider also produces research: see paragraphs [2.14]–[2.16].
Benefits and remuneration	Decisions about the remuneration of research staff should be made by staff not directly connected with another business unit: see paragraph [2.17].
Trading restrictions	Research report providers should have a policy on trading restrictions: see paragraphs [2.18]–[2.25].
Reports based on 'reasonable grounds'	Research reports should be based on 'reasonable grounds', with each research report reflecting the views of the research staff who wrote or approved it: see paragraphs [2.26]–[2.27].
Reports for 'proper purpose'	Offers or threats of favourable or unfavourable research must not be used to solicit benefits or other business, and research must not be used to <i>unfairly or artificially</i> increase trading volumes: see paragraphs [2.28]–[2.29].

## Documentation

**2.6** Research report providers should maintain specific policies and procedures for managing conflicts of interest, and make these available to all staff. To be adequate, these policies and procedures need to be documented: see [PS 181.43]–[PS 181.44].

## Monitoring compliance

**2.7** Research report providers also need to ensure their conflicts management policies and procedures are implemented, maintained and actually complied with in practice. The appropriate monitoring and supervision practices for a research report provider will depend on the nature, scale and complexity of its business: see [PS 181.35]–[PS 181.37].

Note: We expect that conflicts management policies will include specific reference to supervision, monitoring, review, audit and disciplinary matters.

**2.8** Generally, research report providers should maintain an organisational unit separate to the business units (e.g. part of the compliance area) that is responsible for ensuring that conflicts management arrangements are implemented, monitored, reviewed and updated. It is important that the unit responsible for monitoring the research report provider's compliance with its conflicts management obligations is separate from the business units where the potential conflicts are likely to arise. In smaller firms, it may be an individual person rather than an organisational unit who has this responsibility.

Note: We expect that all units of the research report provider will contribute to its management of conflicts of interest, not just the compliance unit.

## Communication

**2.9** A communications policy should outline appropriate and inappropriate communications practices within the organisation and with external parties. Particular attention needs to be paid to communications between research staff and other staff of the research report provider, and between research staff and external organisations (particularly product issuers). The communications policy should be made clear to all staff (both research staff and others). This includes, but is not limited to, information barriers: see paragraphs [2.11]–[2.12].

**2.10** Research report providers should ensure that research reports or information about their contents are not communicated outside the research report provider before the report is provided to clients in the

normal course of business. This does not mean that a research report provider cannot check the factual accuracy of parts of a research report with a product issuer before it is provided to clients. However, we expect that this checking would be done in a carefully controlled way (e.g. without communicating the recommendations or opinions also contained in the report).

## Information barriers

**2.11** Robust information barriers may help a research report provider to manage their conflicts of interest. To be effective, robust information barriers must actually prevent information passing between research staff (and their managers) and other staff. Whether the non-research services have, or are likely to have, an impact on the preparation of research will depend on all of the facts and circumstances.

Note: See paragraphs 5.39–5.42 of ASIC’s surveillance report ‘Research analyst independence’ at for a discussion on the use of information barriers in practice.

**2.12** Generally, we expect research report providers to ensure that research staff are structurally and physically separated from (and are not supervised by) any staff who are performing an investment banking, corporate advisory or dealing function.

What will be appropriate structures and supervision practices for a research report provider will depend on the nature, scale and complexity of its business: see [PS 181.35]–[PS 181.37]. Smaller firms may have less capacity to fully separate research and other staff, and may need to consider other measures to ensure their research reports are provided efficiently, honestly and fairly and that the integrity of the advice they contain is not compromised (e.g. internal, independent and senior approval of research reports: see paragraph [2.13]).

## Approval before distribution

**2.13** To maintain the quality and integrity of reports, research reports should be reviewed and approved by an experienced supervisor or by a group of peers (e.g. review committee) before they are distributed to clients. Reports should not be reviewed or approved by staff from another business area (e.g. investment banking, corporate advisory or dealing function), other than a restricted review for factual accuracy purposes. A written record should be kept of the review and approval of each research report.

## Provision of non-research services

**2.14** If research report providers also provide non-research services to a product issuer, there is a potential conflict of interest. Conflicts management arrangements need to take this into account to ensure the integrity of research reports is not compromised.

Note: Examples of non-research services include:

- (a) underwriting a public offering;
- (b) advice about the prospects for a potential public offering (including likely reception in the financial market);
- (c) help in marketing and promoting a public offering (including participation in 'roadshows' and 'conference calls'); and
- (d) advice on structuring and developing new financial products.

**2.15** Research report providers will need to consider, among other measures, whether they should:

- (a) ensure that research on a product issuer is not published while non-research services are being provided to the product issuer, and for a short period afterwards (i.e. a 'quiet period'); and/or
- (b) fully disclose in relevant research reports the nature of any non-research services provided to a product issuer: see also paragraph [3.10].

**2.16** What is an appropriate solution will depend on the circumstances and the nature of the non-research services being provided. Senior management will need to consider how they manage the conflicts of interest inherent in providing non-research services to entities that they publish research about.

Note: What is an appropriate solution will also depend on the extent to which robust information barriers ensure that research staff are not aware of any non-research services being provided to an issuer. See paragraphs [2.11]–[2.12] for a discussion of information barriers.

## Benefits and remuneration

**2.17** Decisions about the remuneration of research staff should not be made by staff that are directly connected with another business unit (e.g. investment banking, corporate advisory or dealing). Remuneration decisions should not be contingent on:

- (a) research staff introducing new clients or retaining existing clients for the investment banking, corporate advisory or dealing units;

- (b) any specific investment banking, corporate advisory or dealing transaction; or
- (c) the level of any asset management fee.

## Trading restrictions

**2.18** If research report providers or their research staff trade in the financial products that they publish research about, there is a potential conflict of interest. Conflicts management arrangements need to take this into account to ensure the integrity of research reports is not compromised. The following sections deal with some of the things a research report provider may need to consider including:

- (a) its policy on the distribution of research reports on financial products that the research report provider or its research staff have an interest in (see paragraphs [2.19]–[2.21]);
- (b) ensuring that it (the research report provider) does not *unfairly* trade ahead of the distribution of a research report (e.g. through appropriate compliance arrangements and information barriers) (see paragraphs [2.22]–[2.25]); and
- (c) having formal review and approval processes for trading by its research staff (see paragraph [2.24]).

What is an appropriate solution will depend on the circumstances.

### Having an interest in the researched product

**2.19** Research report providers need to consider whether there are any types of conduct that are so inconsistent with proper management of conflicts of interest that they should be avoided completely: see [PS 181.42]. If research reports are provided about products that the research report provider or its research staff hold a material interest in, there is a potential conflict of interest. Research report providers should ensure that this conflict does not result:

- (a) in a failure to comply with their duties as licensees (including the duty to act efficiently, honestly and fairly); or
- (b) in the integrity of the advice contained in their research reports being compromised.

**2.20** Research report providers may wish to consider adopting one or more of the following approaches:

- (a) ensuring that they do not publish research on financial products that they have a material interest in;
- (b) prohibiting their research staff from holding or trading in financial products that they prepare research on;
- (c) adopting robust information barriers (see paragraphs [2.11]–[2.12]) that ensure that research staff are not aware of the trading conducted by the research report provider; and
- (d) ensuring that any holding or trading of financial products by their research staff is properly approved.

**2.21** What is an appropriate solution will depend on the circumstances. The senior management of each research report provider will need to consider how the research report provider manages the conflicts of interest inherent in trading in financial products it publishes research about. Whatever arrangements are put in place, care should be taken by the research report provider to ensure that its trading intention or trading strategy, or that of its research staff, does not affect the contents of its research reports.

Note: For example, a research report provider may prohibit research staff from trading in securities (or derivatives of that security) that they cover, or any securities in that industry sector (e.g. following the relevant sector indices). Trading restrictions should take into account both direct and indirect interests (e.g. a person may have an indirect interest due to derivatives they hold, or the assets of a discretionary account that they manage).

### **Trading ahead of distribution**

**2.22** Care needs to be taken where the research report provider or its research staff trade in a financial product before (or shortly after) the research report provider broadly distributes a research report about that product (e.g. proprietary trading by or on behalf the research report provider and personal trading by research staff). A research report provider may wish to consider the following approaches:

- (a) imposing a ‘quiet period’ on itself and/or its research staff; or
- (b) adopting robust information barriers that ensure that trading staff are not aware of pending research.

**2.23** If adopting a quiet period, the research report provider will need to assess what is a reasonable period before and/or after the distribution of research for trading to be restricted. Quiet periods may also need to cover:

- (a) discretionary trading on accounts managed by the research report providers (as well as dealings on the research report provider's own account); and
- (b) dealings in derivatives of the financial products that are the subject of research reports.

**2.24** Research report providers should take reasonable steps to ensure that their research staff do not circumvent any trading restrictions by encouraging or arranging for others (e.g. the staff member's family or other associated persons) to deal during the quiet periods. Generally, the trading activities of research staff should be monitored and recorded.

**2.25** Non-public information about the timing of and recommendations contained in future research reports may amount to inside information: s1042A. This is especially so where the report is based on information which is itself not generally available. To the extent that the research report itself is or involves 'inside information', trading before or shortly after its publication is likely to amount to insider trading: s1043A(1).

Note 1: Information barrier defences may apply: s1043F–1043G.

Note 2: It is important that product issuers and research report providers take reasonable steps to avoid selective disclosure. See 'Heard it on the grapevine...', Draft ASIC guidance and discussion paper—Disclosure of information to investors and compliance with continuous disclosure and insider trading provisions, November 1999.

## Reports based on 'reasonable grounds'

**2.26** Research report providers should ensure that research reports are based on objective, verifiable facts and analysis, and not on the special interests of the research report provider's research staff, the product issuer or others. Research reports that are not based on reasonable grounds may be misleading or deceptive within the meaning of the Corporations Act: s1041H. Cases decided under the analogous Trade Practices Act provisions have held that a statement of opinion by a person in their professional capacity involves an implied assertion that the opinion has a reasonable basis, is the result of the exercise of due care and skill, and is able to be relied upon.

Note: See s52 of the Trade Practices Act; *MGIGA (1992) Ltd v Kenny & Good Pty Ltd* (1996) 70 FCR 236; *RAIA Insurance Brokers Ltd v FAI General Insurance Co Ltd* (1993) 41 FCR 164; and *Chiarabaglio v Westpac Banking Corporation* (1989) ATPR 40–971.

**2.27** To reduce the risk that research reports are not based on reasonable grounds, research report providers should ensure that each report reflects

the views of the person who takes responsibility for it (e.g. its author or the person who approves its distribution).

## **Reports for ‘proper purpose’**

**2.28** Research report providers should ensure that favourable research is not offered, or changes to research threatened, as an inducement to secure the business of a corporate client or receive other benefits.

**2.29** Care needs to be taken to ensure research reports are not used to artificially increase trading volume and revenue. While high quality research may well attract dealing business to research report providers, their conflicts management arrangements need to identify and respond to the risk that attempts to attract dealing business do not unduly distort the content of any research reports.

Note: If research report providers were able to use research reports as a way of artificially increasing trading volume, there would be a risk that, for example, they might be tempted to make a disproportionate number of ‘buy’ and ‘sell’ (as opposed to ‘hold’) recommendations to increase trading volume.

## Section 3: Disclosing conflicts of interest

**3.1** Research reports are, by their nature, likely to be relied on by retail and wholesale clients as a source of useful information for making decisions about investing in financial products. Users of research reports should be given sufficient information about conflicts of interest relating to the report so that they are able to form a realistic view about the report and whether to rely on it. Specific, prominent and meaningful disclosures about conflicts of interest are needed either in or with each research report: see [PS 181.52].

Note: For a discussion on the need for disclosure to focus on material conflicts, see paragraph [3.13].

**3.2** We recognise there are some situations where disclosing a particular conflict will be inappropriate (e.g. where the relevant matter is highly confidential). In these situations, research report providers will need to assess whether the conflict can be adequately managed through other mechanisms. If it cannot be adequately managed, research report providers may need to avoid the conflict altogether: see [PS 181.60].

**3.3** Conflicts of interest disclosures are important, regardless of whether the client is wholesale or retail. We expect that research report providers' conflicts management arrangements will include procedures to ensure all clients receive conflicts of interest disclosure (not just retail clients): see [PS 181.58]–[PS 181.59]. What is appropriate disclosure to a wholesale client will depend on all the facts and circumstances. We acknowledge that in some cases, the disclosure a research report provider needs to give to a wholesale client to comply with the law may be less detailed than for a retail client: see [PS 181.58].

**3.4** Research report providers should provide conflicts of interest disclosure to all clients, including generally disclosing:

- (a) any material interests they have in financial products that are the subject of the report (see paragraphs [3.7]–[3.8]);
- (b) any benefits they are likely to receive from the report (see paragraph [3.9]);
- (c) their relationship (if any) to the product issuer, including any other services they provide to the product issuer (see paragraph [3.10]);
- (d) any help they were given by the product issuer (see paragraph [3.11]);

- (e) the date the research report was written and who took responsibility for it (see paragraph [3.12]); and
- (f) the reasons behind the opinions and recommendations in the research report (see paragraph [3.13]).

**3.5** We generally expect research report providers to provide some disclosure about each of these matters (where applicable) to all clients. We would expect research report providers to take into account the factors in [PS 181.58] in assessing the disclosure that should be provided to any given client.

**3.6** Robust information barriers (see paragraphs [2.11]–[2.12]) may mean the staff preparing and authorising a research report are unaware of some of matters in paragraph [3.4]. To be effective, such barriers must actually prevent information going to research staff. For example, research staff may be unaware of some confidential non-research services being provided to a product issuer by another department. In this case, we would not expect the research report to include disclosures relating to that service. Whether any particular matter does not need to be disclosed in a research report will, of course, depend on the facts and circumstances: see [PS 181.62].

## Interests

**3.7** Research report providers should disclose in or with each research report whether they (or any associated persons) have, or are likely in the future to have, a material interest in financial products that are the subject of the report. Disclosure will generally need to cover both the existence and extent of the interest.

Note: For example, the disclosures should cover:

- (a) beneficial interests in and derivatives relating to the financial product;
- (b) likely allocations as part of a public offering; and
- (c) significant interests that the research report provider (or its staff) may have in the product issuer.

**3.8** It is important that conflicts of interest disclosures are specific and clear. It would be inadequate simply to make a generic statement that the research report provider may from time to time have interests in those financial products that are the subject of research: see [PS 181.53]. It would also be inappropriate for these disclosures to be hidden in small print or otherwise obscured.

## Benefits

**3.9** Research report providers should disclose whether they (or any associated persons) are likely to receive any benefits from the report. Disclosure will generally need to cover both the existence and extent of the benefits: see [PS 181.54].

Note: For example, the disclosures should generally cover:

- (a) if the research staff member principally responsible for preparing the report received, or expects to receive, any benefit or inducement; and
- (b) if the research report provider (or its research staff) received compensation from the subject of the report recently, or if the research report provider (or its research staff) expect to receive compensation in the near future.

## Associations/relationships

**3.10** If any of the following apply, they should be disclosed in or with the research report:

- (a) that the research report provider (or an associated person) provides underwriting, managerial, consultancy or market-making services to the product issuer;
- (b) that the product issuer is otherwise a corporate client of the research report provider; or
- (c) that the product issuer is related to or otherwise associated with the research report provider.

Note 1: For example, the disclosures should cover the following relationships (if present) between the research report provider (or its associates) and a product issuer (or its associates):

- (a) underwriting or sub-underwriting;
- (b) making a market in the relevant financial product;
- (c) acting as broker or sponsor in a securities issue;
- (d) holding a position (including as a director) with the issuer;
- (e) providing expert opinions; and
- (f) investment banking, corporate advisory and dealing services.

Note 2: It will generally be appropriate for the disclosures to cover the last two years (analogous to s711(2), which deals with disclosing interests in prospectuses); however, this will depend on all the facts and circumstance relevant to the individual research report provider.

## Assistance provided by product issuer

**3.11** The research report (or accompanying disclosures) should disclose whether the research staff who prepared the research report were helped in any way by the product issuer. Disclosure will generally need to state the type of assistance given.

Note: For example, the disclosures should refer to any assistance provided via site visits or other means.

## Who wrote the report and when

**3.12** The research report (or accompanying disclosures) should state:

- (a) the date the research report was written or finalised; and
- (b) who takes responsibility for the report (e.g. who authored or approved the report).

We believe that clients will reasonably require disclosure about each of these matters in forming a view about the research report and whether to rely on it.

## The reasons for opinions/recommendations

**3.13** As a matter of good practice, the research report (or accompanying disclosures) should state the reasons for the opinions and recommendations. This will help clients form a view about the research report and whether to rely on it.

## Additional disclosure issues

### Focus on material conflicts

**3.14** Adequate disclosure means providing enough detail to allow clients to make an informed decision about how the conflict may affect the service being provided to them. We expect disclosure by research report providers to focus on material conflicts: see [PS 181.50]. Overly detailed or irrelevant disclosure is likely to confuse clients and reduce the effectiveness of the disclosure: see [PS 181.61].

**3.15** Other matters that a reasonable person might take into account in assessing the impact of conflicts of interest on a research report and whether to rely on it should also be disclosed. This information could be provided in a number of ways, including in or with research reports, in a separate document and on the research report provider's website. We

suggest research report providers consider making available to their clients (whether or not in research reports):

- (a) the status of current research reports;

Note: For example, research report providers should make available information about when the research recommendations in each research report were made and last reviewed.

- (b) which financial products they provide research on from time to time;

Note: If the research report provider begins or ceases to cover a financial product, they should make this known publicly and, where practicable, provide reasons.

- (c) the proportion of each type of recommendation they make that has been given to product issuers who are corporate clients (compared to other product issuers); and

Note: For example, the research report provider could state what proportion of product issuers who are corporate clients have received a 'buy' recommendation over a 12-month period compared to the proportion of product issuers who are not corporate clients.

- (d) information about the relative performance of their research recommendations in the market.

Note: For example, the research report provider could state what proportion of shares for which they gave a 'buy' recommendation actually increased in value relative to the market index over a 12-month period. Research report providers will need to consider how best to present the information, what to base the comparison on, how to present changes in recommendations, and when this information is updated and made available.

### **Access to conflicts disclosures**

**3.16** Sometimes the advice contained in a research report (or a summary or extract of the advice) is broadly distributed to a wide range of end-users (e.g. through the media or a public announcement). Research report providers should take reasonable steps to ensure that end-users have access to the disclosures discussed in this section. The most appropriate way to make this information available will depend on all of the facts and circumstances.

Note 1: For example, research report providers should take reasonable steps to ensure that:

- (a) research reports are disseminated together with conflicts of interest disclosure (or made available by reference); and
- (b) where the advice contained in a research report (or a summary or extract of the advice) has been (or is likely to be) broadly distributed to a wide range of end-users (e.g. through the media or a public announcement), the relevant conflicts of interest disclosures are made available by reference (e.g. on a website).

Note 2: This paragraph does not apply where the advice contained in a research report (or a summary or extract of the advice) is reported in the media where the research report provider has taken reasonable steps to prevent that advice being so reported.

### **Clear, unambiguous and transparent recommendations**

**3.17** To improve the effectiveness of conflicts of interest disclosures and appropriate use of research reports, research report providers should take reasonable steps to ensure that their recommendations are clear, unambiguous and transparent.

Note: This is particularly so for the main recommendation or opinion given in the report (if any). For example, research report providers should ensure that research reports explain terminology, rating systems and valuation methods used in the report.

# Key terms

In this guide, unless a contrary intention appears, terms have the following meanings.

**AFS licence** An Australian financial services licence under s913B that authorises a person who carries on a financial services business to provide financial services.

Note: This is a definition contained in s761A.

**ASIC** The Australian Securities and Investments Commission.

**ASIC Act** The *Australian Securities and Investments Commission Act 2001*.

**associated person** An associate (within the meaning of Division 2 of Part 1.2 of the Corporations Act) of the research report provider, including its research staff.

**CLERP 9 Act** The *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004*.

**conflicts management obligation** Section 912A(1)(aa) (which takes effect on 1 January 2005).

**conflicts of interest** As defined in [PS 181.15]:

‘...conflicts of interest are circumstances where some or all of the interests of people (clients) to whom a licensee (or its representative) provides financial services are inconsistent with, or diverge from, some or all of the interests of the licensee or its representatives. This includes actual, apparent and potential conflicts of interest.’

**Corporations Act** The *Corporations Act 2001*, including regulations made for the purposes of that Act.

**financial product** A facility through which, or through the acquisition of which, a person does one or more of the following:

- (a) makes a financial investment (see s763B);
- (b) manages financial risk (see s763C); and/or
- (c) makes non-cash payments (see s763D).

Note: This is a definition in s763A.

**financial product advice** A recommendation, a statement of opinion or an interpretation of information, or a report of any of those things, that:

- (a) is intended to influence a person(s) in making a decision about a particular financial product or class of financial products, or an interest in a particular financial product or class of financial products; or
- (b) could reasonably be regarded as being intended to have such an influence;

but does not include anything in an exempt document.

Note: This is a definition in s766B.

**general advice** Financial product advice that is not personal advice.

Note: This is a definition in s766B.

**licensee or financial services licensee** A person that holds an Australian financial services (AFS) licence.

Note: This is a definition in s761A.

**personal advice** Has the meaning set out in s766B(3).

**PS 181 (for example)** An ASIC policy statement (in this example numbered 181).

**representative** A representative of a financial services licensee means:

- (a) an authorised representative of the licensee;
- (b) an employee or director of the licensee;
- (c) an employee or director of a related body corporate of the licensee;  
or
- (d) any other person acting on behalf of the licensee.

Note: This is a definition in s910A.

**research report** As defined in paragraphs [1.1]–[1.2] of this guide.

**research report provider** As defined in paragraphs [1.3]–[1.4] of this guide.

**research staff** As defined in paragraph [1.5] of this guide.

**retail client** Has the meaning set out in s761G.

**s912A** (for example) A section of the Corporations Act (in this example numbered 912A).

**Trade Practices Act** The *Trade Practices Act 1974*.

# Related information

## Headnotes

Conflicts of interest, internal controls, information barriers, conflicts management, disclosure, avoiding, research report, research analyst, research report provider, securities analyst

## Policy statements and practice notes

Policy Statement 164 *Licensing: Organisational capacities* [PS 164]

Policy Statement 175 *Licensing: Financial product adviser—Conduct and disclosure* [PS 175]

Policy Statement 181 *Licensing: Managing conflicts of interest* [PS 181]

## Legislation

*Corporations Act 2001*, s912A(1)(aa), 912A(1)(a), 1041H and 1042A

*Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004*

*Trade Practices Act 1974*, s52

## Policy proposal papers

*Licensing: Managing conflicts of interest* (October 2003)

## Discussion papers and reports

‘Best practice guidelines for research integrity’, the Securities Institute of Australia (SIA) and the Securities and Derivatives Industry Association (SDIA), November 2001 (SIA/SDIA Guidelines)

Commentary on the Draft Provisions (CLERP (Audit Reform and Corporate Disclosure) Bill)

‘Corporate disclosure: strengthening the financial reporting framework’, Corporate Law Economic Reform Program, Proposals for Reform: Paper No 9, Commonwealth Treasury, 2002

Draft Guidance Note ‘Independence of research, disclosure of conflicts of interest and dealing before research recommendations’, Australian Stock Exchange Ltd (ASX), February 2003 (ASX draft Guidance Note)

‘Heard it on the grapevine...’ Draft ASIC guidance and discussion paper—Disclosure of information to investors and compliance with continuous disclosure and insider trading provisions, November 1999

‘Insider trading discussion paper’, Companies and Securities Advisory Committee, June 2001

‘Investment research: conflicts and other issues’, Financial Services Authority, July 2002 (DP 15)

‘Research analyst independence’, ASIC surveillance report, 22 August 2003

‘Statement of principles for addressing sell-side securities analyst conflicts of interest principles’, International Organization of Securities Commission’s Securities Analyst Task Force, 25 September 2003

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