PROFESSIONALISM AND PROFESSIONAL EDUCATION OF INVESTMENT ADVISERS: PART I

by

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1. INTRODUCTION

Since the recent release of the Green Paper by the National Companies and Securities Commission (NCSC) on the licensing provisions of the Securities Industry Act and Codes (NCSC 1985), spirited debates have developed within the securities industry. This series of two papers is concerned with the debate relating to the qualifications of licensees under the Act and Codes. The debate has mainly centered upon superficial reasoning without any consideration for the more fundamental issues of professionalism, leaving unanswered the question of whether an investment adviser is a professional or a "dignified salesman".

These two papers examine, through an in-depth analytical approach, the nature, role and community expectation of a profession, as well as the educational standards of a professional. The first paper presents a series of fundamental arguments which lead to an assessment of whether investment advisers are "professionals". The discussion focuses strongly upon the belief that the community's expectation of investment advisers should override the self centered views of various interest groups within the securities industry, as well as those of government and regulatory agencies. The second paper outlines an appropriate educational system and curriculum consistent with the findings of the first paper.

2. WHO ARE THE INVESTMENT ADVISERS?

In Australia, the terms "investment adviser" and "investment dealer" are at present strictly defined by the Securities Industry Act and Codes. In this paper, the strict legal definition is not applicable, and the terms "investment advisers" and "investment practioners" are used interchangeably and in a general sense. "Investment advisers" or "practitioners"refers to persons who, for compensation, give investment advice to clients and/or deal in securities transactions on behalf of clients.

Under the existing Securities Industry Act and Codes, the NCSC is empowered, through each State's Corporate Affairs Commission, to issue and revoke investment advisers' and investment dealers' licences. These two types of licences must be held by advisers and dealers respectively and may have various restrictions placed upon them. An example of such restrictions is to practice only in the field of fixed interest securities.

Even though the different types and restrictions of licences are for the public protection, the public often not only is unable to distinguish among the diverse array of licences, but also is unaware that there are differences. To add to the confusion, titles such as securities dealers, securities brokers and investment advisers are used interchangeably by many practitioners to convey the same meaning. Thus in an attempt to avoid such confusion and reduce monitoring costs, the NCSC in the green paper justifiably recommends that the present licence categories of dealers and advisers be merged into one class of licences. All licensed practitioners may then be known as "Securities Industry Licensees".

As the number of practitioners in the securities industry grow over the recent years, a number of associations have been formed. Practitioners of the securities industry may belong to one or more of such bodies as The Securities Institute of Australia, Australian Investment Planners Association, and more recently the International Association for Financial Planning (Australia). These associations attempt to set a minimum standard for admission to membership, promulgate their codes of ethics among their

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members, and generally represent the members' views to the public and governmental agencies.

3. WHAT DO INVESTMENT PRACTITIONERS DO?

In the present finance industry, the types of tasks undertaken by investment practitioners are extremely varied, and dependent upon a number of significant factors.

Firstly, the physical size and location of a securities firm have an important bearing on the kind and range of products and services offered. For example, a small firm with a single principal in a suburb is more likely to have many individual clients with smaller amounts of investable funds, while a larger city based firm may be expected to have corporate clients with larger funds for investment. Each of these investment practices needs to tailor their expertise and knowledge to suit their clients. This situation is not unlike that of the legal or accounting professions.

Secondly, to cope with competitive trends in the industry, investment advisory firms are increasing the range of products and services offered to clients. Some firms involved in underwriting of large issues of securities are launching retail business of unit trusts; whereas some investment counselling firms specialising in the retail sales of unit trusts are moving towards underwriting of film investment and other securities which may involve substantial sums.

The highly deregulatory business environment created in the last few years has also engendered an ever increasing number of new products and services in the market place. Some of these products may require very up to date knowledge or skilled analysis in order to render optimum service to the client. The international investment trusts, unit trusts in high technology and investments in Management and Investment Companies (MIC's) are some examples of the relatively recent products which have enjoyed popular support.

Some of this support may be due to a third factor, namely the increasing maturity of the public in financial matters. The Australian public is becoming more knowledgeable in financial matters. They are progressively demanding a high level of competence in their investment advisers no less than that expected of other professional advisers such as accountants and lawyers. This has required investment advisers to possess a broader and more fundamental knowledge of economic and financial matters, as well as the flexibility and innovative skills to encompass a more sophisticated and wider range of investment advisory and dealing services.

Furthermore, it can be seen that the different services of investment advice are closely intertwined. For example, listed and unlisted unit trust in equity investment requires both knowledge of the unit trust industry and the equity market. Therefore, the investment adviser must have a basic understanding of the industry, as well as the critical faculty and learning skills to cope with these new demands.

A fourth factor to impinge upon the nature of the work of the investment adviser is technology. Recent developments in such areas as computer hardware and systems, software, database management, and communication technology have combined to create a newer and more efficient approach of providing the products and services. For an investment adviser to cope with such changes, he or she must be flexible and innovative to understand and apply such techniques in the most appropriate manner.

Investment advisers must therefore possess a comprehensive base of knowledge and an understanding of basic principles, such as economic analysis, corporate accounting, financial mathematics, investment analysis, international finance, business law, taxation, risk management, computer utilisation and many other areas. The practitioners would need to have the analytical capacity in order to apply such principles to a wide variety of specific situations. Furthermore, as knowledge in these different fields are constantly changing in a dynamic environment, the advisers have to keep abreast with the latest development, in order to render their services in the best interest of the clients.

4. WHAT IS THE ROLE OF INVESTMENT PRACTITIONERS IN THE COMMUNITY?

As discussed in the previous section, the Australian public is increasingly knowledgeable about financial matters. They are more aware of their personal financial positions such as superannuation planning and retirement planning.

In the case of individual clients, more of their funds are being invested in a wide range of investment products such as unit trusts and insurance bonds than ever before. As the sale of such investment products are normally handled by investment advisers, this phenomenon reflects to a large extent the influence advisers have over the investment behaviour of their clients. Such investment often represents a significant proportion of the personal savings or superannuation lump sum of the clients. Many of these clients rely totally upon their advisers for making investment decisions by virtue of the expertise professed by these advisers. The practitioners therefore need to have undoubted integrity and high moral values. Failure to provide sound and up to date advice may not only result in foregoing the opportunity to create a higher level of wealth, but may cause a complete loss of saving of the clients. At the other end of the financial spectrum, investment practitioners often deal in funds or advise on investing funds of not inconsiderable amounts. Their clientele may include corporations and institutions.

Sound investment decisions will not only ensure the economic welfare of individuals and clients, but will also ensure that, in the wider perspective, scarce resources in the economy are collectively channelled to optimal use. In the long run, such optimal resource management will lead to a steady growth of our economy. Thus investment advisers have a valuable role to play in the society in that the competent discharge of their duty is essential to the economy as a whole.

Serious legal charges of negligence and gross misconduct have been made against some investment advisers in the past. In some of these cases, these litigations have resulted in the award of sizeable damages. It is therefore apparent that the community has a high expectation for investment practitioners to provide and maintain a high standard of service and ideology. Because of this expectation, the investment practitioners enjoy a high level of reward, esteem and social status comparable to that enjoyed by other status professionals such as solicitors, barristers and medical practitioners.

Thus, it can be seen that as well as knowledge and skills, an investment practitioner must possess an ethical and legal perspective to his or her work, and right attitude to discharge his or her duty. Practitioners ought also to have a sense of responsibilities and obligations towards the society in which they serve. It is therefore incumbent upon the adviser to keep himself or herself up to date with all current developments and maintain his or her mastery of the field of practice.

5. IS AN INVESTMENT PRACTITIONER A PROFESSIONAL?

The term "professional" has dual meaning. Firstly, it has been used in a colloquial sense to mean someone who performs a given task proficiently, or who receives emoluments for the task performed. Thus a carpenter, who is a professional according to that usage, can imply either that he or she is proficient in carpentry, or that he or she is paid for the carpentry work performed. Secondly, the term "professional" is generally associated with members of such groups as lawyers, dentists and medical practitioners. The green paper assumes implicitly that the investment practitioner is a professional in the second sense (NCSC 1985:84).

However, no basis for such an assumption was given in the green paper. The question of whether the investment practitioner is a professional in the latter sense is addressed in this section.

Various writers (Schein 1972, Friedson 1970) have emphasised different aspects of professionalism. However, nearly all would agree that there are certain characteristics which distinguish a "profession" from "non-professional" groups. We shall identify three main characteristics.

Firstly, a professional possesses a specialised body of knowledge and skills, as well as a set of principles or theories with which to apply in solving a specific client's problem (Schein 1972: 8-9). Our previous discussion has shown that, as with other established professions, an investment adviser ought to possess a core of specialised knowledge and skills relating to the carrying out of economic and investment analysis. Such knowledge and skills have to be acquired over a significant period. There are also general investment principles and theories, which have to be selectively applied and tailored to the situations of individual clients.

Secondly, a professional uses his or her knowledge and skills to serve members of the community. As Friedson (1970:151) puts it, professionalism may be defined as "commitment of professional ideas and career ... expressed in attitudes, ideas and beliefs". Clearly this is true of investment advisers, as they strive to protect and enhance the economic well being of their clients. We have also argued earlier that the practitioners ought to be responsive to the community's need and expectation.

Thirdly, a profession has undergone a well defined professionalisation process. Several writers have discussed such transition of a vocation towards a full fledged profession. For example, Wilensky (1964) suggested that there is an overall pattern of progression towards professionalism:

1. Commencement of full time vocation.
2. Establishment of training school which forges a link with the University either at the outset or at some later stage.

3. Formation of a professional association with a published code of ethics.
4. Protection of territorial integrity by licensing and certification.

Investment practitioners have a full time vocation; they have also formed professional associations. These associations have their code of ethics for their members. As it is a legal requirement to be licensed in order to practice, territorial protection was achieved by default. Although The Securities Institute of Australia, which is a professional institution, does have training activities, no formal link has been established with any University in conducting its courses. However, a university degree recognised by the Institute is a requirement for admission to the Institute's diploma programme. Thus, it can be argued that investment practitioners have undergone a well defined professionalisation process.

However, it is also possible for a profession to become deprofessionalised, as Jarvis (1983:26) argues that: "If training for any occupations were to change and become more practically orientated and less knowledge based, it might be argued that in occupational terms the process of professionalisation had been reversed and occupational deprofessionalism had occurred. Such deprofessionalisation might have occurred within branches of other status professions, such as general practice in medicine ..." Although this has not occurred to investment practitioners, such a possibility should not be overlooked.

6. CONCLUSION

Our foregoing discussion has led to the conclusion that investment practitioners have all the hallmarks of a well defined profession, including a clearly defined body of knowledge, a service to the community and the process of professionalisation. In order to preserve and enhance its capacity to serve the public, training for investment practitioners should not be based predominantly on a practical orientation at the expense of building up a core of fundamental knowledge. This is to ensure innovation and flexibility for change in a dynamic world. However it is the sense of ethical values and dedication to community service that should ultimately determine the degree of professionalism, rather than sheer self interest. There is an increasing community expectation that practitioners should act in a highly professional and ethical manner, as increasing reliance is placed upon investment practitioners and the important influence practitioners may exert on the economic well being of their clients.

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