

PARLIAMENT OF THE COMMONWEALTH OF AUSTRALIA

Review of the Australian Securities and Investments Commission Annual Report 2015

Standing Committee on Economics

© Commonwealth of Australia

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Chair's foreword

The committee held its first public hearing with ASIC on 14 October 2016 to examine its role in corporate, market, financial services and consumer credit regulation, recent surveillance and enforcement activities, and priorities for the coming year. Of particular interest to the committee were ASIC's investigations into the life insurance and financial advice sectors.

ASIC outlined to the committee its primary role under the *Australian Securities and Investments Commission Act 2001* (ASIC Act), the *Corporations Act 2001* (Corporations Act) and a range of other legislation. This role includes promoting confidence by investors and consumers in the financial system, maintaining and improving the performance of the financial system, and facilitating efficient registration for financial services providers.

The committee was concerned by evidence of practices of denying claims in the life insurance sector, and sought an update from ASIC on its investigations following the release of its report *Life insurance claims: An industry review* (October 2016). The committee heard that, in many cases, claims were denied on technical or contractual grounds that did not meet a policyholder's reasonable expectations about their coverage when they took out a life insurance policy. The committee notes that, as a result of the review, ASIC has proposed a number of key areas for action to improve claims handling outcomes for consumers. The committee expects that insurers will work diligently with ASIC and the government to implement these recommendations without delay.

The committee also sought evidence on ASIC's investigations into the financial advice sector, following a number of high profile cases where consumers were adversely affected by unscrupulous financial advisers. Many of these advisers

were employed by the major banks, either directly, or through subsidiaries. The committee heard that these investigations are complex and ongoing, and looks forward to further reports from ASIC on its surveillance and enforcement activities across the sector.

On behalf of the committee I would like to thank the Chairman of ASIC, Mr Greg Medcraft, and his colleagues for appearing at the public hearing on 14 October 2016. ASIC has an important role to play as Australia's corporate watchdog, protecting consumers, investors and creditors. The committee will continue to provide oversight of ASIC into the future.

David Coleman MP

Chair

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Membership of the Committee

Chair

Mr David Coleman MP

Deputy Chair

Hon Matt Thistlethwaite

Members

Mr Adam Bandt MP

Ms Julia Banks MP

Mr Scott Buchholz MP

Mr Pat Conroy MP (to 7 November 2016)

Mr Trevor Evans MP

Mr Kevin Hogan MP

Mr Craig Kelly MP

Mr Matt Keogh MP

Ms Madeleine King MP (from 7 November 2016)

Committee Secretariat

Mr Stephen Boyd, Committee Secretary

Dr John White, Inquiry Secretary

Ms Jazmine Rakic, Office Manager

Terms of Reference

The House of Representatives Standing Committee on Economics is empowered to inquire into, and report on, the annual reports of government departments and authorities tabled in the House that stand referred to the committee for any inquiry the committee may wish to make. The reports stand referred in accordance with the schedule tabled by the Speaker to record the areas of responsibility of the committee.

Abbreviations

ACCC	Australian Competition and Consumer Commission
AFS	Australian Financial Services
ANZ	Australia and New Zealand Banking Group
APRA	Australian Prudential Regulation Authority
ASIC	Australian Securities and Investments Commission
BBSW	Bank Bill Swap Rate
CBA	Commonwealth Bank of Australia
DPP	Commonwealth Director of Public Prosecutions
FCA	Financial Conduct Authority (United Kingdom)
LIBOR	London Interbank Offered Rate

1. Introduction

Background

- 1.1 The House of Representatives Standing Committee on Economics (the committee) is empowered to inquire into, and report on, the annual reports of government departments and authorities tabled in the House, that stand referred to the committee in accordance with the Speaker's schedule.
- 1.2 The 2015 Australian Securities and Investments Commission (ASIC) Annual Report (annual report) stands referred to the committee in accordance with this schedule. The committee resolved at its meeting on 15 September 2016 that it would conduct an inquiry into the annual report.
- 1.3 ASIC is an independent Commonwealth statutory authority whose role is to administer the *Australian Securities and Investments Commission Act 2001* (ASIC Act), the *Corporations Act 2001* (Corporations Act) and a range of additional legislation.¹
- 1.4 ASIC was established in 1991 as the Australian Securities Commission, replacing the National Companies and Securities Commission and the Corporate Affairs offices of the states and territories. It was renamed ASIC in 1998 when it was given responsibility for consumer protections in superannuation, insurance and deposit taking. ASIC's responsibilities were expanded in 2010 to regulate trustee companies, consumer credit and

¹ Australian Securities and Investments Commission (ASIC), *Laws we administer*, <<http://asic.gov.au/about-asic/what-we-do/laws-we-administer/>> viewed 11 October 2016.

finance broking and for supervising trading on Australian licensed equity, derivatives and futures markets.²

1.5 ASIC currently comes under the portfolio responsibilities of The Treasury. ASIC's stated aims include promoting investor and financial consumer trust and confidence, ensuring fair, orderly and transparent markets and providing efficient and accessible registration for businesses and companies.³

1.6 Under the ASIC Act, ASIC is responsible for:

- maintaining, facilitating and improving the performance of the financial system and entities in it (including the licensing of financial services providers);
- promoting confident and informed participation by investors and consumers in the financial system (broadly through the delivery of financial literacy education);
- receiving, processing and storing, efficiently and quickly, the information given to ASIC under the law (that is, the operation of the government's registry business);
- ensuring that information is available as soon as practicable for access by the public;
- administering the law effectively and with minimal procedural requirements; and
- enforcing and giving effect to the law.

1.7 ASIC's service charter further describes its role in relation to corporate, market and financial system regulation as encompassing, among other activities:

- registering companies and managed investment schemes;
- registering auditors and liquidators;

² ASIC, *How we operate*, <<http://asic.gov.au/about-asic/what-we-do/how-we-operate/history/>> viewed 11 October 2016.

³ ASIC, *What we do*, <<http://asic.gov.au/about-asic/what-we-do/our-role/#priorities>> viewed 11 October 2016.

- registering business names;
- licensing financial services and consumer credit businesses;
- examining new market licence proposals; and
- maintaining publicly accessible registers of companies, and registered and licensed entities, as well as disqualified directors and people who are banned from the financial services industry.

1.8 ASIC may also:

- grant relief for companies or individuals from some sections of the *Corporations Act 2001* (Corporations Act) and *National Consumer Credit Protection Act 2009* (National Credit Act); and
- pursue companies or individuals who may have breached the laws ASIC administers.⁴

Scope and conduct of the review

1.9 ASIC appeared before the committee at the first public hearing to review its 2015 annual report in Canberra on 14 October 2016.

1.10 The proceedings of the hearing were webcast over the internet, through the Parliament's website, allowing interested parties to view or listen to the proceedings as they occurred. The transcript of the hearing is available on the committee's website.⁵

1.11 This report focusses on the issues raised in the annual report and, in particular, on matters raised at the public hearing in Canberra on 14 October 2016.

1.12 At the public hearing, the committee examined the current policy settings in corporate, market and financial system regulation, focussing on ASIC's surveillance and enforcement activities.

⁴ ASIC, *Service Charter*, <<http://asic.gov.au/about-asic/what-we-do/how-we-operate/asic-service-charter-results/asic-service-charter/>> viewed 11 October 2016.

⁵ House of Representatives Standing Committee on Economics, *Past Public Hearings and Transcripts*, <http://www.aph.gov.au/Parliamentary_Business/Committees/House/Economics/ASICAnnualReport/Public_Hearings> viewed 24 October 2016.

2. Current issues in financial systems regulation

Overview

- 2.1 ASIC appeared before the committee at a public hearing on 14 October 2016 as part of the review of ASIC's 2015 Annual Report. Key issues examined at the hearing included surveillance and enforcement, in particular investigations being undertaken by ASIC into the life insurance industry, the financial advice sector and the alleged manipulation of the bank bill swap rate (BBSW).
- 2.2 The committee also took evidence regarding the financial services regulation framework, and corporate governance at ASIC, including funding and staffing changes.

Surveillance and enforcement

- 2.3 During the hearing, the Chairman of ASIC, Mr Greg Medcraft outlined to the committee how ASIC views its role in financial regulation:

Our vision is to allow markets to fund the economy and in turn economic growth and in doing so contribute to the financial wellbeing of all Australians, which we do, as we have just mentioned, by promoting investor and

consumer trust and confidence, ensuring that markets are fair and efficient and by providing efficient registration services.¹

- 2.4 To achieve this vision, Mr Medcraft said that ASIC undertakes a range of activities focussing on surveillance and enforcement to ‘promote investor and consumer trust’, and stressed that ‘at the end of the day we are a law enforcement agency’.²
- 2.5 The committee questioned ASIC on the scope of its surveillance and enforcement activities, in particular in financial markets and areas that are dominated by small business entities and individual professionals. ASIC Commissioner Mr Greg Tanzer said that while much of ASIC’s surveillance and enforcement activities are ‘primarily targeted at public companies and large proprietary companies’, there is a body of work in compliance in small business, mainly focussed on maintaining small business reporting obligations.³
- 2.6 Mr Tanzer added that a particular target area is in respect of phoenix company activity,⁴ because ‘small business people tend to be the victims of phoenix company activity; and, in some cases, they may be the perpetrators of that activity’.⁵
- 2.7 When asked whether ASIC had taken any action against small business directors, ASIC responded:

¹ Mr Greg Medcraft, ASIC Chairman, *Transcript*, 14 October 2016, p. 1.

² Mr Greg Medcraft, ASIC Chairman, *Transcript*, 14 October 2016, p. 1.

³ Mr Greg Tanzer, ASIC Commissioner, *Transcript*, 14 October 2016, p. 14.

⁴ Illegal phoenix activity involves the intentional transfer of assets from an indebted company to a new company to avoid paying creditors, tax or employee entitlements. See: ASIC, *Small business-illegal phoenix activity*, February 2015, <<http://asic.gov.au/for-business/your-business/small-business/compliance-for-small-business/small-business-illegal-phoenix-activity/>> viewed 19 October 2016.

⁵ Mr Greg Tanzer, ASIC Commissioner, *Transcript*, 14 October 2016, p. 14.

From January to June 2015, ASIC's small business compliance and deterrence area had 155 pending criminal actions against directors and 12 pending criminal actions related to efficient registration and licensing.⁶

- 2.8 In answers to questions taken on notice by the committee, ASIC noted a mistake in Table 4 of *ASIC Report 444: ASIC enforcement outcomes* which relates to its small business compliance and deterrence area. ASIC committed to updating the table.⁷
- 2.9 Mr Medcraft added that ASIC is working with small businesses through its Innovation Hub to assist people who are starting up a business to navigate relevant regulations.⁸
- 2.10 The committee was interested in whether reductions in staffing at the Commonwealth Director of Public Prosecutions (DPP) had adversely affected ASIC's surveillance and enforcement activities. Commissioner Tanzer informed the committee that 'we try to keep the flow going'.⁹ ASIC Senior Executive Leader Mr Chris Savundra said that while the number of DPP staff had been reduced, it had moved to a 'national practice model'. Mr Savundra commented that 'we are not facing any throughput issues of a significant nature which we would raise' and remarked that 'we think the national model is working well'.¹⁰ Mr Savundra added:

The ability to resource matters across states and also develop expertise in those corporate matters has been a good thing. So we are now seeing Queensland matters being resourced by Melbourne staff and so on and so forth. So at the moment we are content with the service that is being provided by the Commonwealth DPP.¹¹

⁶ ASIC, *Response to Questions on Notice*, 2 November 2016, p. 9.

⁷ ASIC, *Response to Questions on Notice*, 2 November 2016, p. 9. See also: ASIC, *Report 444 ASIC enforcement outcomes: January to June 2015*, 5 August 2015, p. 26.

⁸ Mr Greg Tanzer, ASIC Commissioner, *Transcript*, 14 October 2016, p. 14.

⁹ Mr Greg Tanzer, ASIC Commissioner, *Transcript*, 14 October 2016, p. 18.

¹⁰ Mr Chris Savundra, ASIC Senior Executive Leader, *Transcript*, 14 October 2016, p. 18.

¹¹ Mr Chris Savundra, ASIC Senior Executive Leader, *Transcript*, 14 October 2016, p. 18.

- 2.11 The committee questioned ASIC on its complaints handling processes, in particular the volume of complaints relating to various corporate, market and financial products. Mr Warren Day, ASIC Senior Executive Leader, provided an outline of ASIC's complaints handling mechanism, the starting point of which was an allegation of misconduct:

In terms of what you might call a complaint, we call them reports of alleged misconduct. We get from the general public, and that might include lawyers, accountants, financial planners as well as mums and dads—for want of a better expression—and we get between 9½ thousand and 10 thousand of those types of communications a year. On top of that, we will receive thousands of reports from liquidators, breach reports, breach reports from auditors—all of those types of things. The 9½ thousand to 10 thousand matters will cover everything that ASIC is responsible for. Some of it will even include stuff that ASIC is not responsible for; stuff that may be better dealt with by ATO—something that is actually not covered by anyone's legislation; a whole range of those types of things. We do our best to try to triage those and help people get information very early in terms of what they might do to resolve some of those disputes themselves.¹²

- 2.12 Mr Day added that around 45 to 55 per cent of complaints were submitted electronically through ASIC's website, in comparison to complaints lodged using paper, and that this proportion varied throughout the year. Mr Day said it was ASIC's preference for complaints to be lodged electronically to expedite responses, and that the website provided information 'that will help people resolve a lot of their common disputes'.¹³

- 2.13 In terms of the volume of ASIC complaints relating to various corporate, market and financial products, Mr Day stated that around 35 to 40 per cent are related to financial services, a similar number relate to corporate governance and insolvency type matters, and less than 10 per cent are complaints from the public around markets. Mr Day added that many of the

¹² Mr Warren Day, ASIC Senior Executive Leader, *Transcript*, 14 October 2016, p. 18.

¹³ Mr Warren Day, ASIC Senior Executive Leader, *Transcript*, 14 October 2016, p. 20.

complaints about markets relate to matters ASIC is already aware of through their market surveillance activities.¹⁴

2.14 Mr Day reported that the volume of complaints relating to financial services varied depending ‘on what actually is mentioned in inquiries, hearings or in the media and those sorts of things’, but in general terms the breakdown of complaints tends to be evenly spread ‘across financial planning and financial advice but also other dealings with their banks in terms of their loans and those types of things – and credit’.¹⁵

2.15 When asked how many complaints ASIC receives relating to credit cards, ASIC responded:

In the three financial years from 2013–14 to 2015–16, ASIC received 225 reports of alleged misconduct raising concerns about credit cards. This represents 6 per cent of the 3,645 reports of alleged misconduct we received about credit matters generally, and 0.8 per cent of the 29,957 reports of alleged misconduct we received in total during the same period.¹⁶

2.16 The committee was particularly interested in three major investigations being undertaken by ASIC into the life insurance industry, the financial advice sector, and the alleged manipulation of the BBSW, which will be examined separately in the following sections.

Life insurance claims industry review

2.17 In October 2016, ASIC released its report *Life insurance claims: An industry review* (industry review). The purpose of the industry review was to find out if there were ‘systemic issues across the industry, as well as more specific issues relating to particular products or insurers’.¹⁷

¹⁴ Mr Warren Day, ASIC Senior Executive Leader, *Transcript*, 14 October 2016, p. 20.

¹⁵ Mr Warren Day, ASIC Senior Executive Leader, *Transcript*, 14 October 2016, p. 20.

¹⁶ ASIC, *Response to Questions on Notice*, 2 November 2016, p. 11.

¹⁷ ASIC, *Life insurance claims: An industry review*, Report 498, October 2016, p. 4.

- 2.18 In addition to the industry review, ASIC is conducting a separate investigation of the life insurance business of CommInsure.¹⁸
- 2.19 The committee questioned the Chairman about the findings of the industry review and whether ASIC found instances of conflict of interest in the life insurance industry, where remuneration was linked to the denial of claims. Mr Peter Kell, Deputy Chairman of ASIC, responded that, out of the 15 insurers investigated, 'there were two that had potentially conflicted remuneration structures'.¹⁹ Mr Michael Saadat, Senior Executive Leader of ASIC, added that:

With the two insurers that we identified with that issue, what was happening was that their staff were remunerated using a balance scorecard. In that balance scorecard one component of their incentive structure was related to the number of claims that were denied. So it made up a portion of their balance scorecard. From memory, I think it was 15 per cent. That was one of the factors that was taken into consideration as part of the scorecard for the incentives that those staff could earn.²⁰

- 2.20 In relation to the potentially conflicted remuneration structures, Mr Kell said that ASIC will be 'following up to look at that', and has recommended law reform around 'removing the exemption for claims handling under the Corporations Act'. Mr Kell remarked that:

This would help give us better ability to target issues such as conflicts of interest arising in incentives for claims handling staff and management, including whether they are in conflict with insurers' obligation to assess each claim on its merits. We think that law reform would help us.²¹

- 2.21 The committee was interested in hearing when ASIC would report publically on the companies being investigated in the industry review, in

¹⁸ ASIC, Update on ASIC's investigation into CommInsure, *Media Release 16-348*, 12 October 2016, <<http://asic.gov.au/about-asic/media-centre/find-a-media-release/2016-releases/16-348mr-update-on-asic-investigation-into-comminsure/>> viewed 20 October 2016.

¹⁹ Mr Peter Kell, ASIC Deputy Chairman, *Transcript*, 14 October 2016, p. 2.

²⁰ Mr Michael Saadat, ASIC Senior Executive Leader, *Transcript*, 14 October 2016, p. 2.

²¹ Mr Peter Kell, ASIC Deputy Chairman, *Transcript*, 14 October 2016, p. 2.

particular on the rates of claims rejected by particular insurers. Mr Saadat said that ‘we cannot name those insurers. The information was provided to us confidentially, and so we are not able to name them’. Mr Saadat explained it is ASIC’s view that:

The legislative provisions that we operate under—the confidentiality arrangements under the ASIC Act—prevent us from releasing confidential information, and the information was provided by those insurers under ASIC’s compulsory notice powers, and it is commercial-in-confidence.²²

2.22 When asked why ASIC was unable to name the insurers now, but intends to publish the information in the future, Mr Kell responded:

There are two points there. The first is that, at the moment, as well as having been collected under notice, we found that insurers for, say, claims denial rates, claims withdrawal rates, the number and nature of disputes—that information is not being categorised or collected consistently across insurers. This was, in effect, the first time this information had been gathered. Therefore, we need to ensure that there is a consistent way of measuring and presenting that information. If we were to release it at the moment, it would be comparing apples with oranges, and we do not think that would help. So it is a high priority to ensure that there is consistent categorisation around those key elements.

On the second point, we are working with APRA on how we would ensure that it could be published. APRA will, in effect, manage the collection and publication of some of that data. They do not have the same types of restrictions that ASIC has on confidentiality. So it will be a joint exercise by the two regulators to put in place a public reporting regime around claims outcomes.²³

2.23 The committee also sought to clarify with ASIC what limits there are in terms of what it will or will not publically disclose. Mr Tanzer said that Section 127 of the ASIC Act ‘imposes requirements and then provides for certain releases in the terms of 127’, and that ‘other laws also provide for particular types of releases’. Mr Tanzer stated that:

²² Mr Michael Saadat, ASIC Senior Executive Leader, *Transcript*, 14 October 2016, p. 2.

²³ Mr Peter Kell, ASIC Deputy Chairman, *Transcript*, 14 October 2016, p. 2.

The commission does not have a blanket discretion to release information that is covered by section 127. It has to be released either under one of the permitted uses under 127 or under some other law that would prevent that or subject to a procedure such as a subpoena.²⁴

- 2.24 The committee was interested in why ASIC used its compulsory powers to investigate various life insurance companies, and whether this has hampered the public's right to know. Mr Kell responded:

It would have been very difficult, given the relatively short time frame and the range of information we are collecting, to have approached it on some sort of purely voluntary basis. That is one of the reasons we were using those powers. We were also obviously collecting some information that was quite sensitive commercially, so that is where those powers come into play.²⁵

- 2.25 Mr Saadat added:

To clarify, although we did use our compulsory powers to get the information, had we obtained the information without using our powers, had we asked the insurers to provide it voluntarily, in all likelihood they would have required us to keep that information commercially confidential. They can do that if they are providing the information voluntarily. They can consent to us publicly revealing their information, but they have not done so.²⁶

- 2.26 Mr Saadat also remarked that, since the release of the report on 12 October 2016, 'the insurers we have spoken to so far have expressed significant concerns about having their identity revealed publicly'.²⁷

- 2.27 The committee asked if ASIC has sought more powers to enable it to disclose information that was collected using compulsory orders. ASIC responded that, since 2013, while it has 'not made any submissions specifically on amending section 127 of the ASIC Act to allow public disclosure of information that was collected using ASIC's compulsory information gathering powers' it has 'made submissions advocating the benefits of

²⁴ Mr Greg Tanzer, ASIC Commissioner, *Transcript*, 14 October 2016, p. 16.

²⁵ Mr Peter Kell, ASIC Deputy Chairman, *Transcript*, 14 October 2016, p. 11.

²⁶ Mr Michael Saadat, ASIC Senior Executive Leader, *Transcript*, 14 October 2016, p. 11.

²⁷ Mr Michael Saadat, ASIC Senior Executive Leader, *Transcript*, 14 October 2016, p. 11.

compelling industry to publicly release more data to inform consumers and assist their decision making'.²⁸

2.28 The committee was concerned why ASIC did not agree on a methodology with insurers to get consistent results during the industry review. Mr Kell said that it was due to the need for producing the report quickly to enable ASIC to implement greater transparency in the industry:

If we wanted to report by about the middle of next year we could have embarked upon such a process. We wanted to come out with the report in a time frame that would allow us—as we said, one of the key objectives of this report was to identify where there were possible risk areas, where there were possible problem areas for follow-up work, to allow us to, as well as identifying and systemic problems, identify where we were going to have to undertake further actions. Obviously the No. 1 further action is to implement a new transparency regime. The complexity in coming up with a whole categorisation framework in reality would have meant we would not be having this conversation until well into 2017.²⁹

2.29 ASIC's industry review found that there were a number of shortcomings in some insurers' investment in claims systems and processes, including:

- manual processes that are antiquated and do not readily allow reporting;
- systems that are too highly dependent on key staff;
- paper-based files;
- policy administration systems that do not support customer service; and
- poor data quality.³⁰

2.30 In reference to these findings, the committee asked ASIC whether work was progressing to ensure that all claim files held by insurers were digitised. Mr Kell responded that both ASIC and APRA were working with insurers

²⁸ ASIC, *Response to Questions on Notice*, 2 November 2016, p. 7.

²⁹ Mr Peter Kell, ASIC Deputy Chairman, *Transcript*, 14 October 2016, p. 12.

³⁰ ASIC, *Life insurance claims: An industry review*, Report 498, October 2016, p. 91.

to ascertain 'how they are going to ensure those systems meet customer needs going forward'. Mr Kell said:

I would say on this issue that the law reform that we have proposed around removing the exemption for claims handling under the Corporations Act will potentially give ASIC greater ability to put in place guidelines around claims handling that may go to things like time frames for claims handling. Those sorts of issues will ultimately only be effectively addressed by insurers if they have modern technology and better systems in place.³¹

- 2.31 Mr Kell added that while ASIC had not given insurers particular time frames to improve their systems, ASIC would be working with insurers to respond to the findings of the industry review:

I hope it does not come as a surprise, but there is very strong interest on the part of basically all of the insurers that we have dealt with in now sitting down and understanding what the report and the findings mean for them. That in itself is a good indication.³²

- 2.32 The committee asked the representatives of ASIC when the investigation into CommInsure would be finalised and if it had been delayed. Mr Kell answered that a reporting date had not been set because the investigation was still underway:

...we are still conducting interviews and we are still seeking expert advice on some aspects of the matter, for example, from medical experts. But we understand that there is a high degree of community interest, and it is a very high priority issue for ASIC. So, even if it is not completed, we will seek to provide another update prior to the end of the year.³³

- 2.33 When asked if ASIC was satisfied with the Commonwealth Bank of Australia's (CBA) response to the CommInsure investigation, the Chairman said:

³¹ Mr Peter Kell, ASIC Deputy Chairman, *Transcript*, 14 October 2016, p. 8.

³² Mr Peter Kell, ASIC Deputy Chairman, *Transcript*, 14 October 2016, p. 8.

³³ Mr Peter Kell, ASIC Deputy Chairman, *Transcript*, 14 October 2016, p. 6.

I believe they have taken action that is looking to deal with the issue. So, yes, the actions they have taken to date I believe are headed in the right direction. However, we are examining CommInsure at the moment. We so far have requested 68,000 sets of documents. So, yes, the actions they have taken to date I think are the right ones, but, in terms of more detailed view on CommInsure, we may take action as well.³⁴

- 2.34 The committee was interested in whether ASIC had instituted measures to ensure that senior executives of companies were held accountable when ASIC investigations held adverse findings against those companies. In particular, the Chairman was asked what oversight ASIC has had of senior executives, and whether there was a proactive leadership framework in place to deal with issues such as the allegations against CommInsure.
- 2.35 The Chairman agreed that there were problems in internal systems of control and managing risks at CommInsure, where 'it has been demonstrated that there was a major problem that was occurring within the company which had not elevated to senior management'.³⁵
- 2.36 The Chairman added that ASIC was meeting with the boards, management and risk committees of the major banks as part of a broader engagement process 'to make sure that, where we identify issues on the front line, basically it was clear that it flowed right from the top—there was nowhere to basically hide'.³⁶
- 2.37 When asked how it could be that the Chief Executive Officer of the Commonwealth Bank was not aware of systemic problems at CommInsure prior to media reports, Mr Medcraft said that 'at the end of the day CBA has to establish their own system of internal control'.³⁷
- 2.38 The committee questioned ASIC's on its recommendations arising from the life insurance claims industry review to Government about strengthening

³⁴ Mr Greg Medcraft, ASIC Chairman, *Transcript*, 14 October 2016, p. 9.

³⁵ Mr Greg Medcraft, ASIC Chairman, *Transcript*, 14 October 2016, p. 9.

³⁶ Mr Greg Medcraft, ASIC Chairman, *Transcript*, 14 October 2016, p. 9.

³⁷ Mr Greg Medcraft, ASIC Chairman, *Transcript*, 14 October 2016, p. 9.

the regulatory and dispute resolution frameworks, follow-up surveillance and industry standard practices.³⁸ Mr Kell outlined the recommendations as follows:

Some recommendations will go to government. There is some law reform that we are recommending, and we have had discussions with government about these issues already. I think you may have seen in the minister's response that the government is open to considering the issues we have proposed. Some of the recommendations go to the way that dispute resolution schemes operate. We are making part of our submission to the current Ramsay review on the way that dispute schemes operate—what their coverage is, how they deal with different types of complaints—and we are recommending that that coverage be expanded in relation to life insurance. Some of the recommendations go to industry itself about strengthening their own code that they have just come out with. And, of course, some of the follow-up actions are for ASIC and APRA to undertake.³⁹

Financial advice sector investigations

2.39 ASIC's 2014-15 Annual Report states that ASIC conducted 166 surveillances to monitor whether financial advisers and Australian Financial Services (AFS) licensees are complying with their obligations and to take action where ASIC detected breaches of the law.⁴⁰ In 2014–15, ASIC completed 114 civil and criminal court proceedings and administrative actions, and 88 investigations to promote investor and financial consumer trust and confidence in the financial system, resulting in six criminal convictions and three imprisonments.⁴¹ ASIC also recovered \$30 million in compensation for investors and financial consumers suffering losses due to alleged failures in financial advice and services.⁴²

2.40 The committee asked the Chairman why investigations into alleged failures in financial advice at the National Australia Bank were taking so long to

³⁸ ASIC, *Life insurance claims: An industry review*, Report 498, October 2016, p. 11.

³⁹ Mr Peter Kell, ASIC Deputy Chairman, *Transcript*, 14 October 2016, p. 8.

⁴⁰ ASIC, *Annual Report 2014-15*, p. 37.

⁴¹ ASIC, *Annual Report 2014-15*, p. 43.

⁴² ASIC, *Annual Report 2014-15*, p. 37.

complete. Ms Louise Macaulay, ASIC Senior Executive Leader, responded that the investigations were complex:

Our work in relation to the large financial institutions has been going on for some time. It has got a number of different aspects to it. Fee for no service is one. Looking at compliance is another. We have been working with the National Australia Bank and with the other banks to put in place a remediation scheme that looks across the advisers that are identified as high risk and puts a process for assessing the clients of those advisers and whether or not they have been subject to poor advice.⁴³

2.41 Mr Kell stressed that ‘this is a very broad piece of work’, and that further updates would be released in the coming months:

We have already undertaken some bannings and we have further investigations underway in relation to some NAB advisers. We will be releasing a report within the next few weeks that provides an update on the issue of where the large financial planning firms were charging customers for advice but not providing the advice. We will also be releasing the report before the end of the year on how those entities dealt with poor advisers in the past, how they have remediated clients for that poor advice and what has happened to those advisers.⁴⁴

2.42 The committee asked if ASIC was concerned about the increasing number of financial advice breaches at ANZ.⁴⁵ Mr Kell said that part of the increase in breach reporting is a result of the wealth management project ASIC is undertaking. Mr Kell said:

We have very significant concerns about the way the financial advice industry has operated in the past. That is why we have undertaken this project. We are in the process of dealing with the four majors, plus AMP and Macquarie, requiring them to go back and look at all of their financial advisers because of the extent of the systemic problems that we have identified in the industry.

⁴³ Ms Louise Macaulay, ASIC Senior Executive Leader, *Transcript*, 14 October 2016, p. 9.

⁴⁴ Mr Peter Kell, ASIC Deputy Chairman, *Transcript*, 14 October 2016, p. 9.

⁴⁵ See: House of Representatives Standing Committee on Economics, Review of the Four Major Banks, *Transcript*, Canberra, 5 October 2016, p. 16.

That is why we are now requiring them to breach report them to us in a way they did not in the past.⁴⁶

- 2.43 The committee was interested in hearing how ASIC's financial advisors register was progressing and whether a consumer would find information regarding the poor behaviour of particular financial advisors on the register. Mr Kell responded that the register was going well:

It has actually ended up having greater interest than I think we had anticipated. As at the end of last month there were 24,908 financial advisers listed on the register, and there have been over 1.2 million searches of the register completed as at the end of last month. So, it is certainly demonstrating that there is an appetite for that information about advisers.⁴⁷

- 2.44 In relation to finding information regarding banned financial advisors, Mr Tanzer added that:

In the early stages of the institution of the register there were concerns that some people might have been on the register who should not have been on the register, or, conversely, people who were not on the register who should have been. All of that goes to when the register actually started. It was designed deliberately to be a record from a particular point in time—the middle of last year, about March 2015. So, people who were in the industry at that stage are on the register. People who were not in the industry at that stage are not on that register. But if they have been banned they can be searched through the banned register anyway.⁴⁸

- 2.45 The committee asked ASIC whether there was a backlog of applications for registering for an Australian financial services licence. Mr Tanzer said that there had been a three year transition period for accountants to apply for a licence and that the exemption was removed from 1 July 2016. Mr Tanzer said that ASIC has received about 1,000 applications, with about half of the applications received in the month before the exemption was removed.

⁴⁶ Mr Peter Kell, ASIC Deputy Chairman, *Transcript*, 14 October 2016, p. 13.

⁴⁷ Mr Peter Kell, ASIC Deputy Chairman, *Transcript*, 14 October 2016, p. 15.

⁴⁸ Mr Greg Tanzer, ASIC Commissioner, *Transcript*, 14 October 2016, p. 15.

Mr Tanzer added that he expects 'that we will get through most of the backlog probably by the end of this year'.⁴⁹

- 2.46 On 27 October, ASIC released an update on its work to address systemic failures in the provision of financial advice, focusing on the conduct of the largest financial advice institutions, including the relevant arms of the four major banks. The failures set out in the report relate to instances where customers were charged a fee for ongoing financial advice, but had not been provided with the service. The report notes that, to date, around \$23.7 million of fee refunds and compensation has been paid to over 27,000 customers. It estimates that total compensation could be in excess of \$178 million, plus interest, to over 175,000 customers.⁵⁰

Bank bill swap rate investigations

- 2.47 The committee asked ASIC for an update on its investigations in relation to the alleged manipulation of the BBSW by some Australian banks. Ms Cathie Armour, ASIC Commissioner, advised that ASIC has brought proceedings against the National Australia Bank, ANZ and Westpac, on the basis that:

...those organisations had a practice of trading in bills of exchange and similar instruments for the purposes of unconscionably affecting the bank bill swap rate. We have also alleged that the practices manipulated the price of certain financial instruments. We have alleged that the institutions did not conduct themselves in accordance with their licence obligation to act efficiently, honestly and fairly, and we alleged that there were misrepresentations made to the administrator of the bank bill swap rate.⁵¹

- 2.48 When asked how the alleged activities were uncovered by ASIC, Ms Armour said:

ASIC has been reviewing the way that certain financial benchmarks have been compiled, if you like, in the Australian markets, following on from issues that

⁴⁹ Mr Greg Tanzer, ASIC Commissioner, *Transcript*, 14 October 2016, p. 15.

⁵⁰ ASIC, *Financial advice: Fees for no service*, Report 499, October 2016, p. 7.

⁵¹ Ms Cathie Armour, ASIC Commissioner, *Transcript*, 14 October 2016, p. 23.

arose overseas in relation to LIBOR [London Interbank Offered Rate], which is an interest rate benchmark, and in relation to foreign exchange benchmarks. We have been testing practices in Australia in relation to setting our equivalent interest rate benchmark, which is BBSW, and in the foreign exchange spot market. So it was proactive surveillance by ASIC.⁵²

2.49 Ms Armour added:

Since the period of time that we have reviewed, there has been significant change in the way the BBSW interest rate is constructed, and the Council of Financial Regulators, the government and the administrator are working through future changes, as well, with a view to us being very confident that we have a very robust regulatory regime in relation to benchmarks.⁵³

2.50 The committee also sought information regarding potential penalties against the banks under investigation. Ms Armour responded:

It varies in each case, but we have alleged a number of contraventions and the penalties then depend on the number of specific instances of contravention. The penalties depend on whether those contraventions fall under the unconscionable conduct head or the market manipulation head. So it is a case of waiting to see what the court will find.⁵⁴

2.51 The committee notes that in hearings later that day, APRA stated it had been provided such information.⁵⁵

Regulatory framework

2.52 The committee asked about ASIC's role in regulating and promoting competition in the banking sector alongside the Australian Competition and Consumer Commission (ACCC). In particular, the committee asked if ASIC had opposed any bank mergers. The Chairman responded that, at present, ASIC has 'basically no involvement in competition power', but added that

⁵² Ms Cathie Armour, ASIC Commissioner, *Transcript*, 14 October 2016, p. 23.

⁵³ Ms Cathie Armour, ASIC Commissioner, *Transcript*, 14 October 2016, p. 23.

⁵⁴ Ms Cathie Armour, ASIC Commissioner, *Transcript*, 14 October 2016, p. 23.

⁵⁵ House of Representatives Standing Committee on Economics, Review of the Australian Prudential Regulation Authority Annual Report 2015, *Transcript*, 14 October 2016, p. 14.

the Financial Services Inquiry did recommend that ‘competition power be extended to ASIC, particularly where it had an impact on consumers’.⁵⁶

- 2.53 The committee questioned the Chairman on whether there was a poor compliance culture in the banking sector, and if the banks would be more compliant if ASIC had additional powers. The Chairman said that, in the past, ‘clearly there has been a poor compliance culture’, however the banks ‘are making significant efforts to improve their compliance culture’ and ‘to basically make sure that they do the right thing by their customers’.⁵⁷
- 2.54 On the question of giving ASIC additional powers, the Chairman highlighted four measures arising out of the Financial System Inquiry:⁵⁸
- a ‘product intervention power which the government has said it will allow ASIC to have, which is consistent with what the UK FCA [Financial Conduct Authority] has’;
 - a ‘product governance obligation on the banks to consider the best interests of the consumer’;
 - to expand the enforcement penalties available to ASIC; and
 - ‘giving ASIC a competition power’.⁵⁹
- 2.55 The committee was also interested in hearing whether there was overlap in regulatory functions between ASIC and the Australian Prudential Regulation Authority (APRA). Mr Saadat said that while there is some overlap, there is a distinction between the focus of the two regulators:

The focus of ASIC in regulating the activities of lenders and intermediaries such as mortgage brokers is a different focus to that of APRA. We are concerned to make sure that consumers are being put into loans that they can afford and that lenders are engaging in responsible lending practices to make sure that that happens. APRA's focus is slightly different. It focuses on the institution and making sure that the institution is prudentially sound and is

⁵⁶ Mr Greg Medcraft, ASIC Chairman, *Transcript*, 14 October 2016, p. 21.

⁵⁷ Mr Greg Medcraft, ASIC Chairman, *Transcript*, 14 October 2016, p. 5.

⁵⁸ The Treasury, *Financial Systems Inquiry (FSI) Final Report*, November 2014, p. vii.

⁵⁹ Mr Greg Medcraft, ASIC Chairman, *Transcript*, 14 October 2016, p. 5.

not taking on risk that will put the institution at risk, whereas we are concerned about the consumer and making sure that the consumer is not being put into loans that they cannot afford. So it is a different focus. I guess there is overlap in terms of the idea that if you have a well-managed bank and a prudentially-run bank you would expect that they would only be lending to consumers who can repay those loans, but that is not always the case. Sometimes those interests do not always coincide perfectly. That is why we have a consumer protection regime that focuses on the consumer and the borrower.⁶⁰

- 2.56 The committee was also interested in hearing ASIC's perspective on whether the introduction of tracker mortgages (a type of housing loan that is linked to the movements of the Reserve Bank cash rate) would benefit competition in Australia's banking sector. The Chairman was positive about the potential benefits of tracker mortgages for Australian consumers in terms of transparency, timing and comparability. He added that the current absence of tracker mortgages in the Australian market was evidence of a lack of competition:

We are in a market which is, frankly, an oligopoly. I was talking to somebody earlier. Competition has declined even since the global financial crisis. We have a more concentrated banking sector. I get that. One of the reasons I do not think we have them today is that, frankly, we do have a lack of competition. Where you do have competitive markets, whether it be in Europe, Ireland or the UK, clearly you have tracker mortgages.⁶¹

Corporate governance, funding and staffing

- 2.57 The committee was interested in hearing how changes to ASIC funding had affected its operation following the 2014 Budget, which reduced ASIC's funding by \$120 million over five years.⁶²
- 2.58 The Chairman responded that, following the funding cuts, about 12 per cent, or approximately 200 jobs, were lost across the board at ASIC. Mr Medcraft

⁶⁰ Mr Michael Saadat, ASIC Senior Executive Leader, *Transcript*, 14 October 2016, p. 19.

⁶¹ Mr Greg Medcraft, ASIC Chairman, *Transcript*, 14 October 2016, p. 5.

⁶² The Treasury, *Budget measures: budget paper no. 2: 2014–15*, 2014, p. 214.

noted that ASIC was yet to receive the additional budgetary allocations announced in 2016, which has meant the commission has been unable to begin recruiting the additional 200 staff this funding will allow. The Chairman added that since 70 per cent of ASIC's activities relate to surveillance and enforcement, the funding cuts meant that 'we cut back surveillance, which then results in lower levels of enforcement'.⁶³

2.59 In April 2016, the ASIC Capability Review was released and, in response, the Government announced a \$127.2 million reform package to strengthen ASIC. The purpose of the reform measures were to:

...equip ASIC with stronger powers and funding to enhance surveillance capabilities better enabling our corporate watchdog to combat misconduct in Australia's financial services industry and bolster consumer confidence in the sector. .⁶⁴

2.60 As a consequence of the Government's decision to return funding to ASIC, the Chairman said that while the funding was not yet available, it will 'allow us to recruit approximately 200 people. The details we have set out in our corporate plan; we have set out the position over the next four years in terms of resources'. The Chairman added:

We are ready to go as soon as the budget additional moneys are passed. We have been advertising but we cannot actually take people on board, so we are gearing up so that over the next few months we would start that recruitment. We would be appointing people and putting people in place as soon as we can.⁶⁵

2.61 The committee also asked whether there was a 'bullying culture' at ASIC, following media reports outlining allegations made by an ASIC staff

⁶³ Mr Greg Medcraft, ASIC Chairman, *Transcript*, 14 October 2016, p. 16.

⁶⁴ The Hon. Scott Morrison MP, Treasurer, Turnbull Government bolsters ASIC to protect Australian consumers, *Media release*, 20 April 2016.

⁶⁵ Mr Greg Medcraft, ASIC Chairman, *Transcript*, 14 October 2016, p. 17.

member.⁶⁶ Mr Price declined to speak directly to the allegations, citing ongoing legal proceedings, but said that ASIC was making improvements in employee engagement. Mr Price remarked that while there was previously a high response rate around bullying, staff surveys now show ‘that they are less concerned about bullying. That has been a consistent trend over the last four or five years’.⁶⁷

Conclusion

- 2.62 ASIC has an important role to play in corporate, market, financial services and consumer credit regulation, and helps to ensure that markets are efficient and fair for both consumers and investors.
- 2.63 The committee will continue to monitor ASIC’s performance, particularly in relation to the Government’s financial system reforms, and will maintain scrutiny of ASIC in relation to its surveillance and enforcement activities, including ASIC’s investigations into the life insurance and financial advice industries.

Mr David Coleman MP

Chair

9 November 2016

⁶⁶ See: M Han, ‘ASIC senior executive raises “disharmony, bullying and lack of respect” issues’, *Australian Financial Review*, 21 September 2016, <<http://www.afr.com/news/asic-senior-executive-raises-disharmony-bullying-and-lack-of-respect-issues-20160920-grkrip>> viewed 24 October 2016.

⁶⁷ Mr John Price, ASIC Commissioner, *Transcript*, 14 October 2016, p. 19.

A. Public hearing details and documents

Public hearing

Friday 14 October 2016, Canberra

Australian Securities and Investment Commission

Mr Greg Medcraft, Chairman

Mr Peter Kell, Deputy Chairman

Ms Cathie Armour, Commissioner

Mr John Price, Commissioner

Mr Greg Tanzer, Commissioner

Mr Warren Day, Senior Executive Leader

Mr Greg Kirk, Senior Executive Leader

Ms Louise Macaulay, Senior Executive Leader

Mr Michael Saadat, Senior Executive Leader

Mr Chris Savundra, Senior Executive Leader

Documents

Document 1 Australian Securities and Investment Commission
(Responses to Questions on Notice)