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Mr Mark Fitt
Committee Secretary
Senate Economics Legislation Committee
PO Box 6100
Parliament House
CANBERRA ACT 2600
By email: economics.sen@aph.gov.au

Dear Mr Fitt

Inquiry into consumer protection in the banking, insurance and financial services sector

The Australian Bankers' Association (**ABA**) welcomes the opportunity to provide a submission to the Senate Standing Committee on Economics inquiry into consumer protection in the banking, insurance and financial services sector.

With the active participation of its 25 members, the ABA provides analysis, advice and advocacy for the banking industry and contributes to the development of public policy on banking and other financial services. The ABA works with government, regulators and other stakeholders to improve public awareness and understanding of the industry's contribution to the economy and to ensure Australia's banking customers continue to benefit from a stable, competitive and accessible banking industry.

The banking industry has heard the concerns of Australians and is committed to taking action so customers receive a better experience. This led to the announcement of the industry's Banking Reform Program[1] and subsequent launch of the Better Banking campaign[2], which is a program of initiatives that demonstrates the industry's commitment to continue to raise the standards, service and trust of the industry.

The ABA believes trust and confidence in the banking and financial services industry requires a foundation of:

- Strong legal and regulatory obligations which protect consumer interests, promote fair and efficient markets, and support competition, innovation and productivity in the banking and financial services industry
- Continuous improvement in banking standards through self-regulation. This strengthens industry commitments to customers by building on legal and regulatory obligations and evolving to reflect the needs of consumers and the industry, in particular accountability, transparency and ethical behaviour, and
- Institutional leadership to ensure customer value, creation of financial opportunities, reduction of financial risks, economic growth, commercial sustainability and financial wellbeing, and ultimately good customer outcomes.

A number of aspects of the Committee's Terms of Reference for this inquiry are addressed through the initiatives of the industry's Banking Reform Program. Additionally, recent changes to the law, or law reform underway, also address aspects of the Terms of Reference. This submission steps through these issues and ABA would be willing to provide further updates on these initiatives to the Committee should it be required.

[1] http://www.bankers.asn.au/media/media-releases/media-release-2016/banks-act-to-strengthen-community-trust and http://www.bankers.asn.au/media/media-releases/media-release-2016/we-hear-you-banks-announce-more-changes-to-make-banking-better
[2] http://www.betterbanking.net.au/

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1. Banking Reform Program

Banks recognise they haven't always lived up to the community's standards and need to do better.

The banking industry recognises that customers expect banks to keep working hard to make sure they have the right culture, the right practices and the right behaviours in place. The industry's Better Banking program is a multi-million-dollar investment by the industry, aiming to strengthen cultural and ethical standards and improve the delivery of products and services.

On 21 April 2016, the Australian banking industry announced a comprehensive package of initiatives to protect consumer interests, increase transparency and accountability, and build trust and confidence in banks.[3]

The Banking Reform Program was developed following close consultation with key stakeholders and regulators. It targets areas of concern to the community about governance, conduct and culture in banks. The six initiatives cover the areas of remuneration, complaints handling and dispute resolution, whistleblowing, reference checking and stopping misconduct moving round the industry, banking standards and regulation of banks.

The banks and the ABA continue to work closely with key stakeholders and regulators on implementation. Progress with the implementation of the reform program is being overseen by an independent governance expert[4], Mr Ian McPhee. Quarterly progress reports have been published by Mr McPhee since the announcement outlining implementation results, challenges and identifying areas requiring additional attention.[5] Overall progress of each of these initiatives is outlined below.

1.1 Banking Reform Program

1. Reviewing product sales commission

- *Conduct an independent review of commissions and payments in retail banking with a view to the banks removing or changing payments where they could lead to poor customer outcomes, and*
- *Each bank develops and publishes overarching principles on remuneration and incentives to support good customer outcomes and sound banking practices.*

Implementation update

Banks work hard to promote the right behaviours of their employees, and in recent years many banks have made changes to remuneration practices to place more of an emphasis on good behaviour rather than sales targets.

An independent review is being conducted into how banks pay and reward their staff, led by former Australian Public Service Commissioner, Mr Stephen Sedgwick AO ('Sedgwick Review'). The aim of the review is to identify whether commissions, bonuses or other incentives in retail banking might motivate bank staff to focus on their financial interest rather than their customers'. Banks have committed to change or remove payments that could lead to poor customer outcomes.

The independent review is also examining the overall remuneration framework across banks. The reviewer has been asked to make any observations about remuneration and incentive structures. Banks have committed to make sure they have in place principles on remuneration and incentives that aligns with good customer outcomes and sound banking practices.

Mr Sedgwick published the Issues Paper in January, and received submission responses in February.[6] Banks and the ABA have provided significant information and data in support of the independent review. Banks look forward to receiving the Final Report, which is due to be published in early April.

[3] http://www.bankers.asn.au/media/media-releases/media-release-2016/banks-act-to-strengthen-community-trust
[4] http://www.betterbanking.net.au/accountability/
[5] http://www.betterbanking.net.au/faster-industry-repair/ian-mcphee/
[6] http://retailbankingremreview.com.au/2017/01/17/issues-paper/

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2. *Making it easier for customers when things go wrong*

- *Each bank appoints a dedicated customer advocate to ensure their retail and small business customers have a voice and customer complaints are appropriately escalated and responded to within specified timeframes*
- *Support the Government's review to broaden external dispute resolution (EDR) by promoting easier access and increasing eligibility thresholds for retail and small business customers*
- *Support expanding of customer remediation programs from personal advice to all types of financial advice and products, and*
- *Establish an industry-wide, mandatory last resort compensation scheme covering financial advice.*

Implementation update

Guiding principles on the customer advocate have been published by the ABA. The major banks and a number of other banks have, or have recently announced, their customer advocates. Banks are expected to have customer advocates in place by the end of March.

Banks are backing a 'one-stop-shop' external dispute resolution system to make sure disputes are resolved faster, easier and cheaper for customers. Professor Ian Ramsay is currently conducting a review of the system for the Federal Government ('Ramsay Review').

The industry believes the external dispute resolution (**EDR**) system should be simple and easy for consumers to access, navigate and understand. A revised EDR framework should have a singular or simple path for resolution of disputes. Alternative processes or legal requirements may apply given the type of customer or nature of dispute, however, these processes should operate in an integrated way, which provides a consistent consumer experience. Banks and the ABA have been actively contributing to and supporting the Ramsay Review. The Ramsay Review is expected to report to the Government by end March.

Banks are also supporting the establishment of a prospective last resort compensation scheme.[7] The major banks and the ABA provided funding and supported the paper prepared by Oliver Wyman as part of the project led by the Financial Ombudsman Service (**FOS**).

As part of our support for a prospective last resort compensation scheme, the banking industry believes that the scheme must be industry-wide and mandatory for all "financial advisers". We also believe that is must be a scheme of last resort to cover consumers who have not been paid a determination made by an ASIC-approved EDR scheme due to insolvency of a financial adviser, and that all other redress avenues have been exhausted.

We also support improved regulatory standards and oversight, including higher professional standards for financial advisers, appropriate professional indemnity (PI) insurance and adequate compensation arrangements (including capital requirements) to prevent the vast majority of unpaid disputes from arising in the first place, and appropriate enforcement powers for the Australian Securities and Investments Commission (**ASIC**) to ensure licensees meet, and continue to meet, their licence obligations.[8] The Ramsay Review is expected to report to the Government on the last resort compensation scheme by end June.

The ABA made a submission to ASIC encouraging the expansion of regulatory guidance on client remediation programs to be applicable for all types of financial advice and financial products. Banks are currently assessing their policies and implementing changes to reflect Regulatory Guide *256: Client review and remediation programs conducted by advice licensees* [RG 256].

3. *Reaffirming our support for employees who 'blow the whistle' on inappropriate conduct*

- *Ensure the highest standards of whistleblower protections by ensuring there is a robust and trusted framework for escalating concerns.*

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[7] http://www.bankers.asn.au/media/media-releases/media-release-2016/aba-supports-improved-external-dispute-resolution-and-new-compensation-scheme
[8] https://futureofadvice.treasury.gov.au/content/consultation/compensation_arrangements_report/downloads/Final_Report_CACFS.pdf

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Implementation update

The industry understands it is important that banks provide proper support for whistleblowers, promote a 'speak up' culture and help prevent and detect misconduct. Employees should feel confident to report inappropriate behaviour without fear of adverse consequences. This has led the ABA to develop guiding principles on whistleblower protections for banks to ensure their whistleblower policies meet the highest standard. These principles were developed in consultation with the public and stakeholders as well as based on commissioned independent research on best practice international standards.

A whistleblower policy is of the highest standard if it meets various criteria, including:

- Board and executive management team endorsement
- Application of protections applying to a broad range of people connected to the bank – not only employees but also consultants, suppliers and former employees, and
- Zero tolerance of retaliation against whistleblowers.

Banks are updating their whistleblower policies, with the major banks expected to have policies consistent with the principles by the end of March, and non-major banks by the end of June.

4. Removing individuals from the industry for poor conduct

- *Implement an industry register or mechanism to identify individuals who have breached the law, codes of conduct, standards or policies, so that employers can make their own informed recruitment decisions.*

Implementation update

Banks employ around a quarter of the financial advisers in Australia, but are determined to set the highest professional standards for ethical conduct among advisers.

The ABA has established a new, industry-wide hiring protocol, which builds on banks' existing reference checking practices, to ensure they know a lot more about a financial adviser's conduct history before employing them. The protocol, which came into effect on 1 March 2017 for subscribing licensees, sets minimum standards for banks to check the adviser's previous conduct history, quality of advice, risk management and compliance record.[9]

Design principles for a new Conduct Background Check Protocol for bank employees have also been developed, with this new protocol expected to be published in April. The major banks are looking to implement this protocol by the end of June, and the non-major banks by the end of September.

These protocols build on existing recruitment practices and address misconduct moving around the industry. The industry continues to work on the introduction of a register to also support robust conduct checking across the financial services industry. There are a number of legal issues and mixed stakeholder views to be resolved.

5. Strengthening our commitment to customers in the Code of Banking Practice

- *Conduct an independent review of the Code of Banking Practice with a view to improving banking standards, disclosure and principles of conduct.*

Implementation update

The independent review of the Code of Banking Practice was brought forward from its schedule so the industry could examine how it can strengthen commitments to customers. The review was led by Mr Phil Khoury, with banks and the ABA, along with other stakeholders, providing significant contributions to the review.

The Final Report was published in February. The industry is considering the 99 recommendations in the Final Report and is working with stakeholders on the complex, diverse and technical issues raised in the review, some of which are also the subject of other reviews, consultations and inquiries.

[9] http://www.bankers.asn.au/financial-advice

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The ABA expects the industry response will be published by the end of March, indicating industry views on the recommendations, next steps and timeframes for the development of a new and enhanced Code of Banking Practice.[10]

The new Code will be written in plain English, have a detailed commitment to fair and ethical behaviour, better support customers in financial difficulty and a separate section on specific issues relating to small businesses. The industry is looking at how we can strengthen the governance of the Code.

6. Supporting ASIC as a strong regulator

- *Support the Government's announcement to implement an industry funding model for ASIC, and*
- *Work with ASIC to enhance the current breach reporting framework.*

Implementation update

Banks and the ABA have been actively supporting the introduction of the ASIC industry funding model.

The ABA has made submissions to the Treasury's interim and final proposal paper on the industry funding model, and most recently commented on the exposure draft legislation, affirming the industry's support for an ASIC industry funding model. The ABA will work with the Government and ASIC to implement the model to enhance ASIC's ability to investigate matters brought to its attention and to ensure ASIC remains a strong and properly funded regulator.

The ASIC Enforcement Review is looking at matters including breach reporting. The industry has developed principles on breach reporting and awaits the consultation on breach reporting as part of the review.

The ABA believes that the breach reporting framework is critical to effective and efficient regulation of the financial services industry. The industry supports reviewing the effectiveness of the existing breach reporting regime to understand whether there is systemic under-reporting or whether issues primarily relate to challenges with meeting the technical compliance requirements. Importantly, the industry believes that any regime review should maintain focus on reporting material (systemic) breaches, rather than all breaches. As a general principle, any reform should consider how the change will improve consumer protection and/or law enforcement outcomes.

1.2 The new initiatives

In addition to the Banking Reform Program, the industry announced further initiatives in early 2017 through the Better Banking campaign.[11]

1.2.1 Financial hardship and debt management

Banks have renewed their longstanding commitment to support customers in financial difficulty, by making financial hardship support programs more accessible and working with financial counsellors to support the setup of a new debt repayment service to help people manage multiple debts.

The industry has an ongoing focus on helping customers in financial hardship. Banks understand financial difficulty can happen to anyone and work to identify solutions appropriate to each customer's circumstances. Financial difficulty is often associated with a change in the customer's personal situation, such as unemployment, illness or relationship breakdown. Additionally, in some circumstances, banks can put in place special arrangements to help customers and their communities affected by a natural disaster, such as a flood or bushfire.

Banks are committed to improving their practices and working collaboratively with stakeholders to ensure customers' evolving needs are met. The industry updated its guideline on dealing with customers in financial hardship in 2015 to reflect feedback from the financial counselling sector and customers. Customers can now get more information about the type of support that is available to assist them, including when a debt reduction and debt waiver may be appropriate.

[10] http://www.bankers.asn.au/media/media-releases/media-release-2017/code-of-banking-practice-review-final-report-published
[11] http://www.bankers.asn.au/media/media-releases/media-release-2016/we-hear-you-banks-announce-more-changes-to-make-banking-better

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To increase the chances that banks can help, the ABA encourages customers to contact their bank as early as possible if they are in financial difficulty.

Banks are also working with financial counsellors on the establishment of a new debt repayment service, to assist customers with debts from multiple creditors, not just banks but other lenders and utilities.

This new service is about making life easier and less stressful for people struggling to meet multiple debts, and who have fallen behind with their repayments and bills. It will help people put in place an affordable plan to manage and pay off their debts. The intention is for the service to be free of set up or monthly fees for consumers.

1.2.2 Small businesses and farmers

The industry is a strong supporter small businesses. The industry recognises that most businesses in Australia are small businesses, and they provide over 40 per cent of all jobs. Australia's banks have a long history of supporting a competitive and profitable small business sector.

The ABA estimates that there are just over 1 million loans by banks to small businesses. Over the 12 month period to September 2016, new lending commitments remained high at $88.6 billion. Total loan outstandings by banks to small businesses are at a record level of $270 billion, growing by $8.5 billion or 3.3 per cent over the past year. Banks acknowledge that businesses go through ups and downs and that sometimes financial stresses can arise. When they do, banks seek to work with the customer to resolve issues and to restore the business to financial health. Maintaining viable and healthy businesses is good for the businesses, for the banks, and for the economy.

The industry is working with small businesses on initiatives to:

- Improve how we work with small business customers by making the loan application process and approval criteria clearer, making it easier to apply for a loan.
- Introduce new industry guidelines on the appointment of receivers and the use of valuations.
- Support changes to the external dispute resolution (**EDR**) system so more small businesses have access to get their problem resolved.
- Review and develop financial literacy resources for small businesses and farmers, including the 'Financing Your Small Business' website in partnership with CPA Australia, Council of Small Business Australia and NSW Chamber of Small Business.

The industry also has a long history of working with the agriculture sector.

Over the 12 month period to September 2016, new lending commitments remained high at $88.6 billion. Total rural loan outstandings by banks to primary producers and farmers is $70 billion, increasing by 3 per cent over the past year. Over the past four years, rural loan outstandings with banks have increased by $7.2 billion or 12 per cent. Banks now account for over 96 per cent of rural loan outstandings.

The industry also recognises the particular hardship which can be faced by farmers through the various business and seasonal cycles. Banks work with agribusiness customers who may be experiencing difficulties, including through putting in place special loan arrangements. These are assessed on a case-by-case basis and are a matter for individual banks.

In addition to the initiatives for small businesses, the industry is advocating for a nationally consistent and mandatory approach to farm debt mediation that helps farmers in financial difficulty, which is modelled on the existing NSW and Victorian schemes.

1.2.3 Switching

On 9 March, the ABA hosted a roundtable with around 45 participants, including consumer groups, payments experts, regulators, government representatives, card schemes, and banks. The key points identified as causing difficulties with switching include:

- Difficulty of closing accounts
- Difficulty of cancelling and transferring recurring payments using a debit or credit card

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- The limitations of the existing switching facility developed by the Australian Payments Clearing Association, and
- The need for simpler explanatory material and better customer education.

The ABA and the banks are now working with stakeholders to explore these issues and identify workable solutions. The industry will need to collaborate with the card schemes and others in the payments industry.

1.3 Raising awareness of better products, services and culture

The Better Banking campaign also raises awareness of industry action underway in other areas important to customers.

Banks have a range of low cost and fee-free products and services to suit low income earners and retirees. More information about free basic bank accounts can be found at the Affordable Banking website.

Banks also provide protection for customers who are the innocent victims of fraud.

Banks will also be working on new resources about banking to help improve transparency. The ABA has recently published some new consumer education materials, including a list of the most common types of bank fees and how to avoid them and a step-by-step guide on how to make a complaint with a bank.

Banks are also making a $1 billion investment in a new payments system to allow payments and transfers to happen in 'real time', overcoming the current delays when money is transferred from one bank account to another.

Banks also support measures to make financial advice a trusted profession. The industry supported the legislation to introduce the new professional standards framework. Additionally, the banks are helping fast-track professionalisation by funding the initial set up of the new standards setting body.

2. Other reforms benefitting customers

Additionally, the industry has been working to implement recent changes to the law, or law reform underway, which also address aspects of the Terms of Reference.

2.1 Retail customers

The ABA supports reforms to the existing regulatory framework to improve outcomes for consumers. We support consumer protection recommendations made in the Final report of the Financial System Inquiry (**FSI**) and the Government's response including:

- Strengthen product issuer and distributor accountability through a new product design and distribution obligation for financial products (**FSI**; recommendation 21)
- Introduce a new product intervention power for ASIC when there is a risk of significant consumer detriment (**FSI**; recommendation 22)
- Facilitate innovative disclosure by removing impediments to communications with customers (**FSI**; Recommendation 23), and
- Clarifying the definition of basic deposit products (additional Government recommendation).

The ABA strongly supports the implementation of these recommendations, and notes that necessary Treasury resources will be required.

2.1.1 Product design and distribution obligation

The ABA supports a principles-based approach to ensuring a range of factors are considered with the design and distribution of financial products. The approach should promote consumer protection by encouraging more consumer focussed product design, better management of conflicts of interest, and enhanced communication and transparency between product issuers and distributors.

The new obligation should be a clear duty in its own right and be based on a clear and defined policy intent. It is important that the requirements are flexible and scalable depending on the nature of the financial

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product, its complexity and investment risk. This approach will ensure further consumer protections are introduced, without adding unnecessary complexity, and costs for consumers that are not balanced with corresponding improvements to customer outcomes.

The new obligations will not require an individual suitability test. Individual suitability issues are addressed by requirements of the Corporations Act, including the Future of Financial Advice (**FOFA**) obligations when personal advice is provided, and there are other sources of obligations relating to superannuation, margin loans and certain complex products. These existing obligations should be taken into account to avoid duplication or conflict with any new principles-based approach.

The design of the new obligations should take into account overseas experiences with a similar duty[12] to avoid unintended consequences such as the creation of unnecessary costs so that some products have become uneconomical. The new obligations should not apply to credit products, including consumer credit, as these products are covered by a separate comprehensive consumer protection regime.

2.1.2 Product intervention power

The ABA, in principle, supports a targeted product intervention power where there is a risk of significant detriment or harm to consumers, particularly where products have been mis-sold in a reckless, fraudulent or negligent manner. Any new power should be based on a clear and defined policy intent, and needs to manage unintended consequences and adverse implications for consumers invested in the relevant product.

The ABA believes that the power should apply where there is "significant consumer detriment" and be used only as a last resort; the regulator should provide clear explanation on how and when the power will be used; be transparent in the use of the power; be accountable in the use of the power and ensure appropriate safeguards; and the exercise of the power should be subject to administrative and judicial review.

Separately, the ABA supports ASIC conducting a review of current market practices and the establishment of a commonly understood language, notably for structured products, in consultation with industry and stakeholders. Changes to improve use of language should also involve consumer testing and research to ensure that language adopted by the industry is readily understood and based on principles to assist in improving consumer understanding.

The ABA also supports ASIC adopting more formalised market-wide surveillance programs. For example, ASIC conducts reviews into certain market and industry practices. The results of these reviews should be the subject of consultation with industry and stakeholders to identify any systemic issues. Where the reviews do not uncover systemic issues, these matters should continue to be addressed via targeted consultation and/or direct action between the regulator and the financial institution or regulated entity.

2.1.3 Regulated disclosure requirements

The ABA supports streamlining and modernising the disclosure requirements in the law to ensure clear and effective product disclosure and communication with customers. Effective disclosure is dependent on customers being able to understand and apply disclosures to their financial needs and situations. Interactive disclosures, such as assessment tools and calculators, and better use of online communications, offer significant opportunities to raise levels of awareness and assist informed decision making by customers.

However, the legislative disclosure requirements must be balanced with the costs and benefits of industry providing these disclosures and the effectiveness for customers. Disclosure principles should seek to promote efficiencies in delivery and effectiveness of disclosures and communications by focusing on removing regulatory impediments to interactive disclosures, rather than imposing obligations on product issuers and intermediaries, and promoting greater use of interactive elements and channels preferred by customers, for example, electronic, online or digital technologies. Legislative changes should be made so customers can opt-in to receive disclosures and communications in writing, but the default is via electronic, online or digital channels.

Adopting a layered approach to disclosures in the legislative requirements will also ensure regulated disclosures and communications are more effective, and can focus on the information of most relevance for

[12] See International Organization of Securities Commissions' final report, *Suitability Requirements with Respect to the Distribution of Complex Financial Products* and the Australian Financial Markets Association (**AFMA**) guide, *Principles relating to product approval – retail structured financial products,* both outline a number of relevant principles in this regard.

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customers, such as fees and charges, risks and product features. A layered approach to disclosure accommodates varied customer interests and needs, as well as different levels of understanding. We believe that a layered approach can provide consistent and simple disclosure for basic retail banking products where customers are seeking minimal, but sufficient, information and advice as well as in a wealth management context, where customers may receive multiple regulated disclosures.

Improvements should be made to disclosures on fees and charges, risks and product features. The industry has taken some efforts to streamline and simple disclosures, however, there are significant and prescriptive legislative requirements. We consider that simplified disclosures should be pursued, while maintaining consistency and comparability objectives. Based on our consumer research, customers consistently complain about lack of transparency about fees and charges. Some of this is caused by the legislative requirements imposed on regulated disclosures.

Therefore, the ABA also supports the Government conducting a review of current regulated disclosures. A review should include consumer testing and research to ensure disclosure is meeting its purpose in terms of content, presentation and format, and in particular, whether improvements can be made to Financial Services Guides (**FSGs**) and Product Disclosure Statements (**PDSs**) which enhance customer engagement with these regulated documents. Certain insights from behavioural economics may also be a useful contributor to research into ways to improve regulated disclosures.

2.1.4 Definition of basic deposit product

As at 1 January 2015, Authorised Deposit Taking Institutions (**ADIs**) have implemented the requirements of Prudential Standard APS 210 Liquidity. Among the requirements, ADIs must maintain an adequate level of unencumbered assets that can be converted into cash to meet its liquidity needs for a 30 calendar day time period.[13]

Currently, the definition of a basic deposit product under section 761A of the Corporations Act does not specify the period of notice that an ADI may impose on a depositor for an early withdrawal from a term deposit of up to two years. For term deposits of between two and five years, a depositor may make an early withdrawal without prior notice to the ADI.

ASIC has provided class order relief[14] on this matter to address the implications relating to financial services laws. A no action position has been adopted in respect to the implications relating to the offer of term deposits with a 31 day notification period relating to the FOFA laws.

We support the Government's commitment to amend the law. ASIC has extended its relief to provide additional time for law reform and Treasury consultation on this matter has been delayed.

The ABA supports consultation being prioritised and the law amended to introduce a principles-based approach consistent with CO 14/1262 and apply to term deposits under 5 years with a 31 day notification period.

2.2 Small business and agribusiness customers

The ABA and the banks have actively engaged with the inquiry by the Small Business Ombudsman into the adequacy of the law and industry practices on impairment of customer loans ('Carnell Inquiry').

The industry has indicated support for many of these reforms and will continue to work with the Government in achieving better outcomes for small business customers. The existing review of the Code of Banking Practice is also considering a number of issues captured in the recommendations. However, there are some recommendations that require further and closer examination to ensure credit remains readily available to small business and competition in small business lending is not adversely impacted.

The ABA is also working with small business organisations to make sure they have the information they need to manage and grow their businesses, including revamping the existing *Financing Your Small Business* website[15].

[13] Attachment A, APS 210, http://www.apra.gov.au/adi/Documents/Prudential-Standard-APS-210-Liquidity-(January-2014).pdf
[14] http://asic.gov.au/about-asic/media-centre/find-a-media-release/2014-releases/14-347mr-asic-provides-relief-for-31-day-notice-term-deposits/
[1515] http://www.financingyoursmallbusiness.com.au/

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2.3 Financial advice

When consumers seek financial advice, they rightly expect it to be in their best interests. They also expect their financial adviser to be skilled and competent, and be required to meet high standards of ethical behaviour and professional conduct.

The ABA strongly supports improving the quality of financial advice, building confidence and trust in the financial services industry, and creating financial advice as a trusted profession.

2.3.1 Professionalisation of financial advice

The industry welcomes new legislation to raise the competency and ethical standards of financial advisers, including the introduction of a new code of ethics, higher minimum entry qualifications and ongoing professional development requirements.

Raising education, ethical and professional standards is important in creating a trusted profession. The new legal obligations will have a significant impact on financial advice. We believe it is important for the transition to be staged as contained in the legislation to allow new education and professional development programs to be developed and for new induction and other programs to be adjusted to accommodate the new standards.

Banks are helping to fast track the introduction of the new professional standards framework for financial advisers by providing initial funding to set up the new standards body that will establish and monitor the new professional standards.

The ABA's Reference Checking & Information Sharing Protocol for financial advisers is also an important contribution to the new framework. This protocol, currently adopted by the financial advice banks and AMP, is a series of standardised questions on a financial adviser's conduct history and has been created to improve reference checking during the recruitment of financial advisers. It is intended to promote better information sharing about financial advisers focusing on compliance, risk management and advice quality.

The ABA believes that *Regulatory Guide 146: Licensing: Training of financial product advisers* [RG 146] will need to be amended by ASIC as a consequence of the new legislation. The training requirements now covered by the new legislation should be removed from RG 146. Additionally, RG 146 should be amended to address industry concerns with aspects of the guidance for financial product advice on Tier 2 products and general advice on Tier 1 products. In the longer term, these training requirements should also be transferred to the new standards body so there is single administration of education, competency and training requirements.

2.3.2 Unpaid compensation

The ABA believes that managing the risk to consumers of unpaid compensation requires a multifaceted response. The ABA supports a number of risk management measures and reforms intended to improve the regulatory framework. Some of the complementary measures will also be advocated by the ABA through the review of the financial system external dispute resolution framework and the ASIC enforcement review.

Professional indemnity insurance

Industry should work with professional indemnity (**PI**) insurers to examine improving the cost, availability and coverage of PI insurance, including mandatory run-off cover for licensees, and responses to insolvency, fraud and other misconduct. Industry should introduce additional financial planner education in relation to the duty of disclosure, notification and settlement requirements, and the effect of replacing policies.

Regulation and regulatory activities

ASIC should require an annual assurance statement from all AFS licensees that they meet their licence obligations, including compliance with ASIC's *Regulatory Guide 126: Compensation and insurance arrangements for AFS licensees* [RG126]. ASIC should review the compensation requirements under RG126 to ensure they remain fit-for-purpose.

ASIC should also review the financial requirements for financial advice licensees under *Regulatory Guide 166: Licensing: Financial requirements* [RG 166], to consider whether capital requirements for AFSLs with a financial advice authorisation remain sufficient. Sufficient resources to compensate clients and meet any insurance deductible payments should form part of the resources required for an orderly wind-down of a financial advisory business.

AFS licensing criteria

The past conduct of a person as a manager of a financial services business, including whether that business had unpaid EDR determinations, should be part of ASIC's AFS licensing and credit licensing assessment.

Appropriate enforcement powers for ASIC

Establishing the LRCS should be accompanied by additional provisions to:

- Publish the details of licensees that do not comply
- Give appropriate powers for ASIC to take enforcement action against persons responsible for the licensee's failure to comply (this may extend beyond the adviser to directors / managers in certain circumstances)
- Stop non-complying licensees from operating, and
- Prevent those persons from establishing a new financial services or credit assistance business.

Appropriate enforcement powers for ASIC should specifically address the risk of licensees winding up their businesses with the intention of avoiding paying an EDR determination.

2.3.3 Banning individuals

The ABA supports introducing a new power to ban individuals from management (**FSI**; recommendation 24). The extension of the current enforcement requirements and actions that apply to financial advisers and to those managing a financial service business, provide an additional mechanism to enhance consumer confidence and trust in the financial advice industry, and the financial services industry more broadly. The new power should specifically contemplate managers of financial service business that have an unpaid External Dispute Resolution (EDR) determination.

2.4 Remuneration

The Sedgwick Review of bank remuneration will provide important insights to banks. The findings will provide an important basis for the industry to identify responses and actions needed to remove or change product sales commissions and product based payments that could lead to poor customer outcomes and seek any regulatory approvals necessary for the banking industry to take action. The findings will also help banks to review current and develop new overarching principles on how they pay and incentivise all employees.

The ABA notes that there is regulation already in place in relation to director and executive remuneration. We believe these provisions are adequate to ensure accountability and transparency.

Banks are subject to existing disclosure obligations in relation to remuneration and incentives.[16] Regulatory obligations require the disclosure of information about the design of remuneration and incentives structures, how they are overseen, and how they are adjusted to reflect risk, and longer term performance. Banks also disclose the detail of executive remuneration, including the amounts paid to certain executives, in reports to shareholders and the market.

Information about the way staff are paid is also included in the Financial Services Guide and Credit Guide, which banks must provide to customers in most circumstances.

The Productivity Commission's inquiry into Executive Remuneration, completed in 2009, canvassed these issues. Importantly, the Productivity Commission recognised that liberalisation of the Australian economy and global competition, increased company size, and the shift to incentive pay structures, have been major drivers of executive remuneration - companies compete to hire the best person for the job, and try to structure pay to maximise the executive's contribution to company performance[17]. It also made no recommendation to introduce caps or binding shareholder votes.

[16] Prudential Standard APS 330 Public Disclosure.
[17] http://www.pc.gov.au/inquiries/completed/executive-remuneration/report/executive-remuneration-report.pdf

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The Productivity Commission's final report recommended strengthening the corporate governance framework, including removing conflicts of interest with independent remuneration committees and use of remuneration consultants, and promoting board accountability and shareholder engagement.

The third version of the ASX Corporate Governance Principles, to which ABA members are bound, includes amendments to Principle 8, primarily to improve transparency about remuneration decisions.[18]

2.5 Competition and innovation

The ABA has consistently encouraged competition in the banking industry to ensure that banks compete to provide customers with the best products and services while delivering strong returns for shareholders and boosting innovation and productivity in the Australian economy.

The FSI also made an important recommendation to strengthen the focus on competition in the financial system (**FSI**; Recommendation 30). The Government agreed to implement periodic reviews of competition in the financial sector, and to this end the Government committed to tasking the Productivity Commission with reviewing the state of competition in the financial system by end 2017.

The ABA believes there is a need for a thorough, robust and credible assessment of the state of competition in the financial system to ensure policy prescriptions regarding competition have a sound factual underpinning. On this basis, the ABA encourages the Government to commission the Productivity Commission review as soon as possible for reporting and public release by the end of 2017.

On innovation, the industry has consistently advocated for measures that expand consumer choice. The ABA agrees with the Productivity Commission in their draft Data Availability and Use report that expanding access to data, could enhance consumer outcomes by facilitating better-informed customer decision making and more targeted and tailored product and service offerings. It could also allow customers greater autonomy with their products and services and would promote innovation and efficiencies in the financial system.

Banks support sharing data subject to adequate safeguards around privacy, security and protecting incentives to invest in data. As a principle, we believe that the development of detailed standards for the banking sector should be industry led. Governments should avoid unnecessary regulation and place greater compliance burdens on an already highly-regulated industry when industry-led reform is achievable and in fact desirable to ensure customers' needs are well served.

3. Conclusion

The industry is currently progressing with a significant reform program making changes to ensure better products, better service and better culture in banking.

If you have any queries regarding the issues raised in our submission or otherwise, please contact me or Christine Cupitt, Policy Director, on

Yours sincerely

Diane Tate
Executive Director – Retail Policy

[18] http://www.asx.com.au/documents/asx-compliance/cgc-principles-and-recommendations-3rd-edn.pdf