

# Chapter 1

## Introduction

1.1 On 20 June 2013, the Senate referred the performance of the Australian Securities and Investments Commission (ASIC) to the Economics References Committee for inquiry and report by 31 March 2014. The committee was to give particular reference to:

- (a) ASIC's enabling legislation, and whether there are any barriers preventing ASIC from fulfilling its legislative responsibilities and obligations;
- (b) the accountability framework to which ASIC is subject, and whether this needs to be strengthened;
- (c) the workings of ASIC's collaboration, and working relationships, with other regulators and law enforcement bodies;
- (d) ASIC's complaints management policies and practices;
- (e) the protections afforded by ASIC to corporate and private whistleblowers; and
- (f) any related matters.<sup>1</sup>

1.2 On 5 August 2013, the then Governor-General prorogued the 43rd Parliament and a general election was held on 7 September 2013. The 44th Parliament commenced on 12 November 2013. Two days later, the Senate agreed to the committee's recommendation that this inquiry into ASIC's performance be re-adopted with a reporting date of 30 May 2014. The Senate also agreed to the recommendation that the committee have the power to consider and use the records of the Economics References Committee appointed in the previous parliament that related to this inquiry. At the commencement of the 44th Parliament, the committee had already published over 250 submissions with another 70 or so waiting for the committee's consideration.

1.3 Initially, the committee called for submissions to be lodged by 21 October 2013, but, in light of the election and the start of a new parliament, the committee resolved to continue to receive submissions with a closing date of 10 January 2014.

1.4 On 28 May 2014, the committee tabled an interim report requesting an extension to present the final report by 26 June 2014.

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1 *Journals of the Senate*, 2010–13, no. 150 (20 June 2013), p. 4110.

## **Conduct of the inquiry**

1.5 The committee advertised the inquiry on its website calling for written submissions. The committee also wrote directly to a range of government departments and agencies, organisations, academics and other people known to be interested in the performance of ASIC, drawing their attention to the inquiry and inviting them to make written submissions.

1.6 The committee received 474 submissions and a further 104 supplementary submissions, as well as additional information including answers to a series of questions taken on notice by witnesses. These documents are listed at Appendices 1 and 2. The committee held five public hearings: two in Sydney (19 and 20 February 2014) and three in Canberra (21 February 2014 and 2 and 10 April 2014). A list of the hearings and the names of witnesses who appeared before the committee is at Appendix 3. In addition to its appearances before this committee on 19 February 2014 and 10 April 2014, while this inquiry was underway ASIC gave evidence at three estimates hearings held by the Economics Legislation Committee (20 November 2013, 26 February 2014 and 4 June 2014). Members of this committee questioned ASIC's chairman, commissioners and other officers at those hearings and this evidence has been taken into account for this report.

## **Background to the inquiry**

1.7 Throughout 2012 and 2013, media reports raised serious concerns about the practices of financial advisers in Commonwealth Financial Planning Limited (CFPL), part of the Commonwealth Bank of Australia Group. ASIC was also issuing notifications regarding actions it had taken on this matter. On 4 June 2013, the Economics Legislation Committee questioned ASIC about the CFPL matter and was clearly dissatisfied with ASIC's response. Within weeks, the Senate referred the inquiry on ASIC's performance to this committee.

1.8 The emerging revelations about the misconduct of financial advisers in CFPL and ASIC's failure to provide satisfactory answers in relation to this matter to the Economics Legislation Committee was the main catalyst for the inquiry. But it was not the only driver. A number of previous inquiries and other information in the public domain had exposed serious shortcomings in corporate conduct in Australia and ASIC's response to them. Thus, the committee's terms of reference reflect this broader context and, indeed, the submissions traverse a wide range of concerns about ASIC's performance.

## **Submissions**

1.9 The majority of the submissions came from individuals or groups of concerned investors or consumers who wanted to draw the committee's attention to their specific grievance. Often their case involved allegations of corporate misconduct that had resulted in significant personal financial loss and sometimes financial ruin.

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### ***Individual grievances***

1.10 Unfortunately, the committee was not able to investigate every individual matter that was raised in submissions. Clearly from the contents of some submissions, people had expectations that the committee could in some way assist them to resolve their difficulties. This was not the committee's role. The committee, however, gave great weight to their accounts and experiences; this evidence helped inform the committee's deliberations and assisted the committee in formulating recommendations.

### ***Confidential material***

1.11 The committee prefers to take evidence in public. With this inquiry, however, a number of submitters requested the committee to receive their submission in confidence or to withhold the publication of their names. Even with the protection of parliamentary privilege, some submitters were not willing to place their criticisms of ASIC on the public record because ASIC makes decisions that may affect their business. Also, in some cases, and without the submitters' request, the committee itself resolved to receive submissions in camera or to withhold sections from publication. Such decisions were based on a variety of reasons including:

- the matter was still under investigation or consideration by a court or tribunal;
- concern over publicising a person's private circumstances; and
- reluctance to allow a person to be publicly traduced or embarrassed where their involvement in an alleged offence appeared to be incidental or not relevant to the committee's inquiry.

1.12 The committee also declined to receive several submissions or sections of submissions. The overriding reason in most instances stemmed from the submissions' failure to address the committee's terms of reference. Some submitters were clearly disappointed with the committee's decision either to not receive their submission or to remove names or sections of their submission before publication. Where such information was deemed to be irrelevant to the committee's inquiry, however, it could not be accepted as evidence.

1.13 Where the committee did include evidence received on an in camera basis in this report, it was careful to ensure that such information was used to support information that was already publicly available or where it had sought verification from other sources.

### ***ASIC's submissions***

1.14 ASIC provided the committee with nine submissions in total. Three submissions addressed the CFPL matter (*Submissions 45, 45.3 and 45.6*). ASIC's first supplementary submission (*Submission 45.1*) related to reforms to the credit industry and low doc loans, and was provided in response to the significant number of submissions the committee received on these topics. In October 2013, ASIC provided

its second supplementary submission: a 196 page document that addressed all of the inquiry's terms of reference (*Submission 45.2*). ASIC and the committee have referred to this submission as ASIC's 'main submission'. The remaining submissions from ASIC dealt with particular issues or cases and were provided in response to evidence the committee received, lines of questioning or developments that occurred as the inquiry was underway. For example, in May 2014 ASIC provided *Submission 45.7* on a proposed alternative model for funding ASIC.

## Scope and structure of the report

1.15 During this inquiry the committee has studied some enforcement actions or allegations of misconduct in detail. These cases have assisted the committee to consider the broad questions that the Senate has asked it to focus on (that is, the specific clauses of the inquiry's terms of reference). One example is the CFPL matter, which provided the committee with key insights into ASIC's approach to misconduct and enforcement action but also informed the committee's analysis of Australia's corporate whistleblower protections.

1.16 Many different and varied issues were raised during the course of the inquiry. Nevertheless, some common themes emerged that linked these disparate matters. This report is divided into the following five parts:

- **Part I (Introduction):** This part outlines recent developments and growth in Australia's financial services industry to provide some context about the environment in which ASIC operates (Chapter 2). It then describes ASIC's current role and functions (Chapter 3) and its approach to regulation (Chapter 4).
- **Part II (Case studies):** In this part, the committee examines two case studies where retail investors or financial consumers found themselves in dire financial difficulties because of bad financial advice and unethical and irresponsible practices. The first relates to consumer credit and poor lending practices between 2002 and 2010. The second case study relates to the CFPL matter. The chapters included in this part examine:
  - the lending practices between 2002 and 2010 based on the experiences of over 160 people who made submissions to the inquiry, and ASIC's response to these practices (Chapter 5);
  - the effectiveness of Australia's new credit laws in redressing some of the problems identified during this period (Chapter 6);
  - the two external dispute resolutions schemes approved by ASIC for financial services and credit—the Financial Ombudsman Service and the Credit Ombudsman Service (Chapter 7);
  - what went wrong at CFPL and why, including how an aggressive sales-based culture fostered an environment where advisers were able to circumvent compliance requirements and take advantage of investors (Chapter 8);

- ASIC's investigation of misconduct at CFPL, and its handling of information from CFPL whistleblowers and other sources regarding that misconduct (Chapter 9);
- the adequacy and efficacy of ASIC's enforcement actions relating to the CFPL matter, and the integrity of the arrangements put in place to compensate CFPL clients (Chapters 10, 11 and 12);
- the internal compliance regimes of Australian companies, using the Commonwealth Bank and Macquarie Bank as recent examples where ASIC raised serious concerns about a culture of non-compliance (Chapter 13).
- **Part III (Investigations and enforcement):** This part examines ASIC's investigative and enforcement function. The chapters in this part of the report cover:
  - Australia's corporate whistleblowing framework, and how that framework might be improved (Chapter 14);
  - ASIC's procedures for receiving complaints and reports of corporate wrongdoing including the processes for the preliminary assessment and investigation of such reports (Chapter 15);
  - factors influencing ASIC's responsiveness to complaints and reports of corporate wrongdoing (Chapter 16);
  - ASIC's approach to enforcement and factors that may influence the remedy it decides to pursue (Chapter 17);
  - ASIC's handling of enforcement matters (Chapter 18).
- **Part IV (Communication and engagement):** In this part of the report, the committee analyses ASIC's engagement and communication with professional bodies in the financial services industry and with retail investors and consumers. It also examines community expectations about ASIC's role, financial literacy and the way the regulator communicates with concerned industry bodies and members of the public. The chapters in this part address:
  - ASIC's relationship with key industry stakeholders (Chapter 19);
  - community expectations of the extent to which ASIC can protect investors and consumers from corporate collapses, substandard financial advice and unsafe financial products and, in this context, the current licensing tests and the importance of financial literacy and education (Chapter 20);
  - ASIC's relationship and communication with people seeking assistance from the regulator (Chapter 21); and
  - how ASIC provides services and publishes information (Chapter 22).
- **Part V (Directions for the future):** The final part of the report evaluates options for enhancing ASIC's ability to fulfil its obligations. It examines possible ways to encourage better enforcement outcomes (Chapter 23) and

options to address concerns about the quality of financial advice given to consumers and improve the professional standing of the financial advice industry (Chapter 24). It also scrutinises ASIC's resources, governance structure and capacity to meet the challenges presented by a dynamic industry where new business models and financial products are constantly emerging (Chapters 25 and 26). This final part of the report will also consider areas that may need to be reformed or where significant legislative changes may be required (Chapter 27) and contains the committee's final conclusions and observations about ASIC (Chapter 28).

## **Acknowledgements**

1.17 During the course of the inquiry, the committee has benefitted greatly from the participation of many individuals and organisations located throughout Australia. The committee thanks all those who assisted with the inquiry, especially the witnesses who put in extra time and effort to answer written questions on notice and provide valuable feedback to the committee as it gathered evidence. ASIC in particular was of great assistance in providing the committee with information that it requested.

1.18 But most particularly, the committee acknowledges the many people who wrote to the committee recalling their experiences. They range from whistleblowers, who placed their careers in jeopardy in order to expose corporate wrongdoing, to individuals who, through no fault of their own, found themselves in dire financial circumstances. Without their personal accounts, the committee would not have been able to appreciate fully the need for stronger action to ensure that Australia's financial services regulatory framework is robust and focused on protecting the retail investor and consumer from unscrupulous operators.