

Senate Economics Legislation Committee
ANSWERS TO QUESTIONS ON NOTICE
Treasury Portfolio
Budget Estimates 2014
3 June to 5 June 2014

Department/ Agency: ASIC

Question: BET 8

Topic: Action against Banks

Reference: Hansard pg 13-14, 4 June 2014

Senator: Bishop

Question:

Senator MARK BISHOP: I understand that, but my question wasn't, 'What were the problems and what was the cultural focus of the bank?' My problem is that, when all of the sins have been disclosed, identified, reviewed and assessed by ASIC and correspondence sent to them identifying these 38 miscreants, they only revoke the authorisation of 12. My question is: why were the other 26 still flogging financial products? What is the answer?

Mr Kirk: The bank had not revoked their authorisations.

Senator MARK BISHOP: Thank you, I understand that.

Mr Medcraft: I might take that on notice, because on that one I would like for us to come back you.

Senator MARK BISHOP: Make it pretty quick, if you don't mind—I do not mean that rudely.

Mr Medcraft: I personally would like to get a clear answer.

Senator MARK BISHOP: The next question then, is: you said to a three interesting things this morning, Mr Kirk. You said that the Commonwealth Bank's processes prior to 2006-07 were pretty bad, you did your surveillance, you did your investigation, you had negotiations, you imposed conditions, they accepted them and then it got to the stage that, notwithstanding their undertakings and the trust that ASIC had given to them, new licence conditions had to be imposed. You now tell me that 26 did not have their authorisations revoked because the Commonwealth Bank chose not to. Why did not ASIC sometime in 2010, 2011 or 2012 just go in there, kick the doors down, and tell them at a minimum that those 26 you forgot to revoke, we are now telling you to revoke them? Why didn't you do that?

Mr Kirk: Again, without going back and looking at each of the individual advisers, it may well be that, whilst they were rated as critical, that within the bank system that did not justify revocation; it was something that could be managed by means other than revocation, like very close management or taking the more front-line advice and putting them in another role. We would have to go back and look at each individual one. Similarly, in terms of anything that ASIC could do, in terms of banning individuals, whether for any of them there was enough evidence of wrongdoing to ban them, I cannot tell you.

Mr Medcraft: Again, Senator, we will come back with a fuller response.

CHAIR: I will allow a couple of minutes just to wrap up. We will move to some other senators. If we have got time, will come back.

Mr Medcraft: Will take that on notice.

Senate Economics Legislation Committee
ANSWERS TO QUESTIONS ON NOTICE
Treasury Portfolio
Budget Estimates 2014
3 June to 5 June 2014

Answer:

8. As set out at paragraph 14 of ASIC's Initial Submission to the Inquiry into ASIC's Performance, the purpose of ASIC's 2007 surveillance of Financial Wisdom and CFPL was not to identify and deal with individual problem advisors. Rather, it was to test the licensee's broader compliance systems and processes for monitoring and management of its advisors. The surveillance revealed the inadequacy of those systems and processes and ASIC then sought to take steps to address that inadequacy through first the Continuous Improvement Compliance Plan (CICP) and, later, the enforceable undertaking.

This approach was adopted in light of a number of important facts.

- a) ASIC had at the time long-standing, publicly-expressed concerns with the quality of advice provided by the financial planning industry in Australia, stemming from our surveillance work, as well as our industry 'shadow shops' (including in 2003 and 2006).
- b) The concerns were not that there were some bad apple advisors or a few bad firms in the industry that needed to be removed. The concerns were that there were widespread problems with both the systems and culture across the industry that were resulting in widespread poor quality advice and that without change to those systems and culture the high level of poor quality advice would continue. ASIC chose to prioritise the use of the resources available to it to working to change systems and practices in the industry, with an initial focus on the larger players in the industry that had the greatest number of authorised representatives. The alternative, focussing more on individual planners would have removed some of the products of the system and cultural problems but not the systems and culture that produced them.
- c) It is a primary tenet of the Corporations Act regulatory settings for financial services that licensees are responsible for the conduct of their authorised and employee representatives. It is thus essential that licensees have a system for monitoring the conduct and quality of advice provided by their representative advisors. CFPL and Financial Wisdom had such systems. Their purpose was to identify risks to the licensee which then needed to be managed by the licensee.
- d) When conducting a surveillance focussed on considering the systems and culture of a firm, ASIC often would obtain and consider the firm's register or list of advisors considered to be a risk to the firm. That was done in the CFPL Financial Wisdom surveillance. The purpose of doing so was to test the adequacy of the systems for monitoring and recording problematic advisors and the systems for addressing the risks that those advisors raised, whether through targeted training, greater monitoring and supervision or in more extreme cases breach reporting to ASIC and/or removal of authorisation. As is clear in ASIC's February 2008 letter setting out the findings of the surveillance, ASIC concluded those systems were inadequate and sought a response from the licensee on how those inadequacies would be addressed which subsequently resulted in the CICP program.
- e) As a general matter, and more particularly in the context of the industry wide problems noted above, ASIC's approach in such matters was not one of obtaining the list of advisors that a licensee's monitoring had rated as high risk in order to conduct its own investigation and potentially take action against each of those advisors. Such an approach

Senate Economics Legislation Committee
ANSWERS TO QUESTIONS ON NOTICE
Treasury Portfolio
Budget Estimates 2014
3 June to 5 June 2014

would involve ASIC using all of its resources doing investigations of individual planners in a firm (in the CFPL/Financial Wisdom matter potentially involving 38 investigations). It would likely be inefficient as a very broad range of conduct could lead to an advisor being rated high risk by its licensee, only some of which might warrant investigation or enforcement action. It would be targeting the symptom of the problem i.e. poor advisors when ASIC was trying to target the cause, i.e. bad systems and culture, and it would be inconsistent with the licensee being responsible for the conduct of its advisors and being required to breach report material breaches. It would also provide an incentive to licensees not to monitor or not to record and fully document information about high risk advisors.

Consistent with this, ASIC did not conduct an investigation of each of the 38 advisors in order to determine whether Enforcement action was warranted. Nor did it investigate in sufficient detail to determine why the licensees had removed the authorisation of some and not of others. It should be noted in this context that some of the range of conduct which would result in an advisor being classified as a critical risk in the licensees' then risk rating system would warrant removal of authorisation and breach reporting to ASIC whilst other conduct may, depending on the detailed circumstances, have been appropriately managed by other mechanisms including training, close monitoring and supervision and changes to remediation. A critical rating did not necessarily mean that inappropriate advice had been provided, but might arise from failings in the documentation of advice and compliance steps. This is consistent with the primary purpose of the risk rating system being to identify risks for the licensee.

It is relevant to note in this context that following the 2007 surveillance, one element of the CICP was to improve the licensee's breach reporting material breaches, and that subsequently breach reporting did occur and, ASIC did take enforcement action against eight CFPL advisers.

Finally, the CBA has advised us that of the 38 critical rated advisers at the time of the 2007 ASIC surveillance 29 are no longer with the business and those 3 of them that remain have been subject to repeated reviews to test their subsequent compliance.