ASIC Chief Tell Banking Summit - Trust Must Be Rebuilt

Summary:
ASIC boss James Shipton is talking tough with calls to rebuild trust in the finance sector and for bankers to be fair in their dealings with clients. It shouldn't be so hard. All that is required is for ethical behaviour to become the norm. Bankers need to realise they don't deserve a disproportionate share of their client's and the nation's wealth. The fleecing must stop.

This is Shipton's speech to the AFR Banking and Wealth Summit. There are some choice points made. How serious is ASIC? Their time to prove themselves is pretty close to up.

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The fairness imperative

A speech by James Shipton, ASIC Chair, Conduct regulator's address, the AFR Banking and Wealth Summit, (Sydney, Australia) 27 March 2019.

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1. Introduction

Let me start by endorsing Wayne Byres' remarks, especially the fundamental importance of a sound financial system and the banking system's financial, operational, organisational and cultural resilience. Wayne is right: small individual problems need to be looked at together, and we need to objectively look for blind spots, and executives of boards need to do the heavy lifting.

I also want to endorse ASIC Deputy Chair Karen Chester's comments from yesterday about the need for fairness towards superannuation members.

Last year at the AFR I gave ASIC's perspective on the challenges, and opportunities, the banking and wealth industry faces in rebuilding trust. In doing so I covered:

- the importance of trustworthiness as a means of rebuilding trust
- the economic and societal role of finance, particularly the purpose of the banking and wealth sectors
- professionalism in finance, and its crucial role in developing trust, and
- how identifying the characteristics of a good financial services industry would help finance be more trusted by the community.

I ended by saying there was a window of opportunity for the financial industry to:

- take proactive steps to improve professionalism
- always recognise that we are dealing with other people's money, and
- most importantly, make a difference for Australians. Crucially, I said the financial industry has both a legal and societal role – namely to support the fair and proper functioning of the financial system.

All these points still stand as strongly as they did 12 months ago. Moreover, it is safe to say that the Royal Commission clearly reinforced these themes.

Unfortunately, industry has not made as much progress as we would have liked.

The Royal Commission has finished. However, the important thing is that ASIC and APRA are now left on the field and we have every intention of maintaining the momentum and pace of change.

We now all need to implement the lessons of the Royal Commission – particularly its spirit (that is, not just its words).

However, remember - meaningful change is the ultimate responsibility of financial institutions. As the Royal Commission made very clear:

'There can be no doubt that the primary responsibility for misconduct in the financial services industry lies with the entities concerned and those who managed and controlled those entities: their boards and senior management.'

'Nothing…should be understood as diminishing that responsibility.'

Drawing on these sentiments, today I would like to cover:

- The 'fairness imperative' for the financial services industry; and
- What ASIC is doing to promote that imperative, particularly:

ASIC's strategic change program moving forward; and
Our new regulatory approaches – including our enforcement and supervisory initiatives.

What is the end goal to all of this? It is:

- Building real trust and confidence in a financial system so that is fair, strong and efficient; and that
- Fairness is embedded into every aspect of a financial services firm's business.

2. The fairness imperative

Fairness is already a core part of our work: ASIC's vision is for a fair, strong and efficient financial system for all Australians.

Fairness is also already embedded in the law – in section 912A - the obligation to act 'efficiently, honestly and fairly'.

Fairness is also a central tenant for the Australian Financial Complaints Authority (AFCA):

- Already - in its first 4 months of operations AFCA received about 24,000 complaints - which is a 42% increase in volume compared with the predecessor schemes.
- AFCA is incredibly important for setting standards in the industry, achieving fair outcomes for consumers and helping guide positive behavioural change by financial institutions.
- ASIC is committed to working with AFCA and collaborating on projects and data to improve industry behaviour.

The Royal Commission has also helpfully highlighted the fairness imperative.

So, what is meant by fairness?

Some people might say fairness is intangible. Nevertheless, through the lens of the Royal Commission it was very clear to the community, and even industry itself, that certain types of conduct was very clearly unfair.

The fact is 'fairness' is a concept we can all readily understand. Moreover, humans can clearly recognise unfair outcomes.

Fairness means doing what's right; it's the quality of being reasonable and just.

Commissioner Hayne acknowledged that fairness 'may lie at, or at least close to, the heart of community standards and expectations about dealings with consumers'.

From a legal perspective, existing case law suggests fairness is the ethical performance of functions in accordance with **professional** standards. This would include observance of common law, fiduciary and statutory duties.

Hence my earlier emphasis on professionalism as a base standard for the financial industry.

Fairness also connotes a requirement of competence in providing advice.

Again, this aligns closely with concepts of professionalism.

The core statutory obligation on licensees to act 'efficiently, honestly and fairly' (which I mentioned

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earlier) implies an element - not just of even handedness in dealing with consumers - but also the concept of sound ethical values and judgment in matters relevant to a consumer's affairs.

In this, again, I hear echoes of professionalism.

Commissioner Hayne went on to state in both the Royal Commission's Interim and Final Reports that 'there is a need to adhere to six basic norms of behaviour' – they are:

- obey the law
- do not mislead or deceive
- **be fair**
- provide services that are fit for purpose
- deliver services with reasonable care and skill, and
- when acting for another, act in the best interests of that other.

These six principles are not new, in fact they very much align with existing law – especially s912A – as well as with our own regulatory work.

Today I want to emphasise one particular aspect – **fairness** – as this concept runs through each of the other principles.

The need to embrace the fairness imperative

To start with, as we have seen, 'fairness' is already a statutory obligation. That is to do all things necessary to ensure financial services are provided efficiently, honestly and fairly (s912A).

Importantly, we now have a penalty for breach of that primary obligation that banks and other licensees owe to all their customers.

This is an important foundation to our new enforcement posture of asking ourselves 'Why not litigate?'.

Financial institutions must embrace and embed in everything they do the fairness imperative for there to be meaningful cultural change in the industry.

Financial institutions must respond responsibly to the challenge and not, as we have seen in some segments, with resistance and reluctance to the job we as a conduct regulator are expected to do.

Separately, directors and officers (including of super trustees) are also on notice as to their directors' duties and responsibilities in relation to non-financial risks, including conduct risk and operational risks such as cyber resilience, privacy and data management.

Again, we are not creating new obligations here – it is already the law that directors and officers are ultimately accountable for their company's management of non-financial risks.

My suggestion to the officers and directors in finance – finance's leaders – is that you need to 'lean into the future' as regards senior management and director responsibility and accountability.

You can start work immediately by leveraging off existing guidance coming from the APRA's CBA inquiry, the Royal Commission and our own supervisory and corporate governance work.

Given that there will be an extension of the Banking Executive Accountability Regime (BEAR) obligations to firms regulated by ASIC, with an additional focus on conduct, this leaning into the future is a very real and practical *imperative.*

Addressing push back

In only 50 days since the handing down of the Royal Commission's Final Report, we are already reading criticisms of our approach to litigation.

ASIC's mandate is crystal clear: **If the law is broken we need to enforce it.**

In response to the emerging criticism, I will start with an assurance that we will *always* act responsibly, within appropriate boundaries and procedures.

We are doing the job the community expects us to do.

Push back from this clear mandate concerns me though – it says:

- Despite the Royal Commission there is resistance to a meaningful mindset change.
- There is a fundamental misunderstanding of our broader fairness mandate and our statutory mandate to enforce the law.
- It suggests we would use our powers inappropriately, irresponsibly and without foundation to, it has been suggested, unfairly target particular names.
- Most importantly, it suggests there are still things to hide.
- These sentiments ultimately and unfortunately perpetuate an unhelpful culture of resistance and reluctance.
- Accordingly, they run counter to our role of enforcing the law, protecting consumers and catalysing positive behavioural change.

The simple solution is: **don't break the law.**

Build systems and processes within the law and within community expectations of fairness.

Act *fairly and professionally.* If you are confident about your governance, management and operational systems, as well as the way you go about your business, there is nothing to worry about.

3. ASIC's strategic change program moving forward

When my appointment at ASIC was announced a little over a year ago I said publicly that I wanted to position ASIC as a: strong, proactive, efficient, innovative and strategic regulator that will utilise its many regulatory tools, including gatekeeping, supervising and enforcement.

The only thing that has changed in the 18 months since I said these words is the redoubling of my core belief in that statement.

Since then there has been a **significant expansion in ASIC's priorities and work:**

- We are significantly increasing and accelerating court-based enforcement outcomes driven by our new enforcement strategy ('Why not litigate' – something I will come back to in a minute) and we are looking to use the full extent of our new penalties and powers;
- We are embedding and expanding new supervisory approaches and promoting best practice and innovation in regulation; and
- We are also implementing the Government's package of reforms and our new obligations and responsibilities in response to the Royal Commission. Importantly, this includes an expanded role for ASIC to become the primary conduct regulator in superannuation.
- We therefore welcome the Government's announcement of significant additional funding to give effect to each of these goals.

4. New regulatory approaches

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Enforcement

Last year ASIC adopted a 'Why not litigate?' enforcement stance and publicly committed to that posture going forward.

Let me be clear - this is a very different concept to a 'litigate first' or a 'litigate everything' strategy.

In fact, 'Why not litigate?' is our own strategic construct that we first postulated in October 2018.

The aim of this stance is to deter future misconduct and address the community expectation that wrongdoing be punished and denounced through the courts. This means that once:

- ASIC is satisfied that breaches of the law are more likely than not and
- it is evident from the facts of the case that the pursuit of the matter would be in the public interest,
- then we will actively ask ourselves: why not litigate this matter?

ASIC initiated an Internal Enforcement Review, led by Deputy Chair, Daniel Crennan QC, and assisted by Michael Wyles QC, Professor Ian Ramsay of The University of Melbourne and Deputy Commissioner Leanne Close of the Australian Federal Police. The Review, completed in December 2018, includes a number of significant recommendations, foremost being the establishment of an Office of Enforcement within ASIC.

The guiding principles and operational guidelines for our enforcement work, coordinated by the Office of Enforcement, will have as their starting point a focus on *deterrence, public denunciation and punishment* of wrongdoing by way of litigation.

Deputy Chair Crennan will no doubt talk more about this next in the roundtable discussion.

Again, let me be clear – our approach to the use of enforcement is that if we find evidence that the law has been broken we will investigate it.

A breach of the law is the starting point. It is wrong, and unhelpful, to suggest that we would instead start with a name and work backwards with an enforcement action in mind.

New powers and penalties

ASIC's adoption of the *'Why not litigate?'* enforcement stance is strengthened with the expansion of penalties and powers recently available to ASIC.

Many new civil penalties now apply to misconduct that before had no penalty at all. Penalties have also been strengthened by:

- increasing maximum prison penalties for the most serious offences to 15 years; and
- increasing the maximum civil penalties to $1.05M for individuals and over $500M for companies.

In ASIC's view a primary purpose of penalties in relation to the misconduct we regulate is of **deterrence,** at the individual and broader level – deterrence against breaking the law.

These new powers and penalties will be of greater deterrence value and will make a meaningful difference.

As mentioned, we are also accelerating our court-based enforcement outcomes driven by our '*Why not litigate stance?*'.

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From February 2018 to March 2019:

- there has been a 15% increase in the number of ASIC enforcement investigations
- a 65% increase in enforcement investigations involving the big six (or their officers or subsidiary companies), and
- a 129% increase in wealth management investigations.

Supervision

Moving forward, ASIC will continue to enhance the way we regulate, particularly with the adoption of a more intensive supervisory approach.

Our new supervisory approach helps detect cultural failings that lead to conduct problems and breaches of the law. Supervision adds a focus beyond current known breaches to look at factors that create significant risk of future breaches. An important element of our new supervision approach is the use of data and market analysis to detect misconduct early.

Since supervision has a strong focus on governance and culture, it allows ASIC to thoroughly understand the business models and risk management of firms and adjust our regulatory approach to the complexity, innovations and continuous change in entities and markets.

ASIC's pilot supervision program, the 'close and continuous monitoring' (CCM) program, commenced in October 2018.

- To date, ASIC has conducted over 170 onsite interviews with banking staff at all levels. There has been continuing engagement with CEOs and CROs, including providing direct feedback.
- ASIC staff have been onsite in these institutions for more than a total of 70 days since the CCM Program was launched in October.

Initial findings are proving of significant regulatory value and will be fully and frankly disclosed to CEOs and boards to improve their processes, systems and culture.

Already we are providing important feedback to the CEOs and other business leaders on concerns we are finding in their management, reporting and control systems - so this work is off to an early but extremely strong start.

ASIC is also reviewing the corporate governance practices of the CCM institutions, as well as reviewing these practices across a broader range of financial services organisations and other ASX 100 entities.

Key areas for this work are governance processes and practices on the oversight of non-financial risk, and practices regarding variable remuneration granted to key management personnel.

New frontiers

Finally, we continue to work on developing the regulatory frontier – that is regulation's 'next generation' of tools and approaches through leading developments in behavioural economics, data analytics and regulatory technology.

5. Conclusion

In conclusion, our focus is on making Australia's financial system a ***fair,*** *strong and efficient one for all Australians.*

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My message to you is that *meaningful change within the industry is needed to meet this goal.*

I do not want to have to relay this same message again in a year's time.

- *Now* is the time for meaningful change.
- *Now* is the time to build a trusted and professional financial services sector.
- *And now* is the time to put fairness first.

Thank you.

Websites For More Information: The fairness imperative - James Shipton - ASIC
https://asic.gov.au/about-asic/news-centre/speeches/the-fairness-imperative/

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