Australian Government
Australian Accounting Standards Board

Cover Memo

Project:	**Other Business – Public**	**Meeting:**	February 2019 (M169)
Topic:	**Final Report – Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry**	**Agenda Item:**	13.3.9
Contact(s):	Shachini Dassanayake sdassanayake@aasb.gov.au 03 9617 7633 James Barden jbarden@aasb.gov.au 03 9617 7643	**Project Priority:** **Decision-Making:** **Project Status:**	n/a n/a n/a

OTHER BUSINESS – OTHER

Paper No.	Title	Staff comment	Board action
13.3.9	Final Report – Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry *(extracts only)*	The final royal commission report on banking has important and equally relevant advice for financial reporting framework reform which is consistent with the objectives of the AASB's Conceptual Framework and Financial Reporting Framework projects. The report states that "it is time to start reducing the number and area of operation of special rules, exceptions and carve outs. Reducing their number and their area of operation is itself a large step toward simplification. Not only that, it leaves less room for 'gaming' the system" (section 1.5.3, page 16) Other important sections relevant to the above projects are highlighted in page 19 and 42.	Included for noting only. No action required.

1. Introduction

1 This report

The central task of the Commission has been to inquire into, and report on, whether any conduct of **financial services entities** might have amounted to misconduct and whether any conduct, practices, behaviour or business activities by those entities fell below community standards and expectations. The conduct identified and described in the Commission's *Interim Report* and the further conduct identified and described in this Report includes conduct by many entities that has taken place over many years causing substantial loss to many customers but yielding substantial profit to the entities concerned. Very often, the conduct has broken the law. And if it has not broken the law, the conduct has fallen short of the kind of behaviour the community not only expects of financial services entities but is also entitled to expect of them.

This *Final Report* seeks to take what has been learned in respect of each part of the financial services industry that has been examined and identify:

- issues;
- causes; and
- responses and recommendations.

1.1 Four observations

Those analyses, taken together, will reveal the importance of four observations about what has been shown by the Commission's work: the connection between conduct and reward; the asymmetry of power and information between financial services entities and their customers; the effect of conflicts between duty and interest; and holding entities to account.

Each of those observations should be explained.

First, in almost every case, the conduct in issue was driven not only by the relevant entity's pursuit of profit but also by individuals' pursuit of gain,

whether in the form of remuneration for the individual or profit for the individual's business. Providing a service to customers was relegated to second place. Sales became all important. Those who dealt with customers became sellers. And the confusion of roles extended well beyond front line service staff. Advisers became sellers and sellers became advisers.

The conduct identified and condemned in this *Final Report* and in the *Interim Report* can and should be examined by reference to how the person doing the relevant acts, or failing to do what should have been done, was rewarded for the conduct.

Rewarding misconduct is wrong. Yet incentive, bonus and commission schemes throughout the financial services industry have measured sales and profit, but not compliance with the law and proper standards. Incentives have been offered, and rewards have been paid, regardless of whether the sale was made, or profit derived, in accordance with law. Rewards have been paid regardless of whether the person rewarded *should* have done what they did.

Second, entities and individuals acted in the ways they did because they could. Entities set the terms on which they would deal, consumers often had little detailed knowledge or understanding of the transaction and consumers had next to no power to negotiate the terms. At most, a consumer could choose from an array of products offered by an entity, or by that entity and others, and the consumer was often not able to make a well-informed choice between them. There was a marked imbalance of power and knowledge between those providing the product or service and those acquiring it.

Third, consumers often dealt with a financial services entity through an intermediary. The client might assume that the person standing between the client and the entity that would provide a financial service or product acted for the client and in the client's interests. But, in many cases, the intermediary is paid by, and may act in the interests of, the provider of the service or product. Or, if the intermediary does not act for the provider, the intermediary may act only in the interests of the intermediary.

The interests of client, intermediary and provider of a product or service are not only different, they are opposed. An intermediary who seeks to 'stand in

more than one canoe' cannot.[1] Duty (to client) and (self) interest pull in opposite directions.

Chapter 7 of the *Corporations Act 2001* (Cth) (the Corporations Act), and the *National Consumer Credit Protection Act 2009* (Cth) (the NCCP Act) (but not the *Superannuation Industry (Supervision) Act 1993* (Cth) – the SIS Act), speak of 'managing' conflicts of interest.[2] But experience shows that conflicts between duty and interest can seldom be managed; self-interest will almost always trump duty. The evidence given to the Commission showed how those who were acting for a client too often resolved conflicts between duty to the client, and the interests of the entity, adviser or intermediary, in favour of the interests of the entity, adviser or intermediary and against the interests of the client. Those persons and entities obliged to pursue the best interests of clients or members too often sought to strike some compromise between the interests of clients or members and their own interests or the interests of a related third party (such as the person's employer, or the entity's owner). A 'good enough' outcome was pursued instead of the *best* interests of the relevant clients or members. (Notions of best interests and conflicts between duty and interest are further examined below in connection with **mortgage brokers**, financial advice and superannuation.)

Fourth, too often, financial services entities that broke the law were not properly held to account. Misconduct will be deterred only if entities believe that misconduct will be detected, denounced and justly punished. Misconduct, especially misconduct that yields profit, is not deterred by requiring those who are found to have done wrong to do no more than pay compensation. And wrongdoing is not denounced by issuing a media release.

The Australian community expects, and is entitled to expect, that if an entity breaks the law and causes damage to customers, it will compensate those affected customers. But the community also expects that financial services entities that break the law will be held to account. The community

---

1 *Re Minister for Immigration and Multicultural and Indigenous Affairs; Ex parte Ame* (2005) 222 CLR 439, 448.

2 The SIS Act requires trustees to give priority to the duties to and interests of the beneficiaries over the duties to, or the interests of, others. See s 52(2)(d).

recognises, and the community expects its regulators to recognise, that these are two different steps: having a wrongdoer compensate those harmed is one thing; holding wrongdoers to account is another.

Some may see what has emerged from the work of the Commission only through the lens of public accountability for what has happened. And public accountability is critically important. But it cannot be the only focus. It is necessary to look to the future as well as to the past.

The responses and recommendations made in this Report will attract varied responses. Those who oppose change will appeal to real or supposed difficulty in altering present arrangements. Reference will be made to change bringing 'unintended consequences'. That argument is easily made because it has no content; the 'consequences' feared are not identified.

But choices must now be made. The arrangements of the past have allowed conduct of the kinds and extent described here and in the *Interim Report* of the Commission. The damage done by that conduct to individuals and to the overall health and reputation of the financial services industry has been large. Saying sorry and promising not to do it again has not prevented recurrence. The time has come to decide what is to be done in response to what has happened. The financial services industry is too important to the economy of the nation to allow what has happened in the past to continue or to happen again.

1.2 Primary responsibility

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 that is said in this Report should be understood as diminishing that responsibility. Everything that is said in this Report is to be understood in the light of that one undeniable fact: it is those who engaged in misconduct who are responsible for what they did and for the consequences that followed.

Because it is the entities, their boards and senior executives who bear primary responsibility for what has happened, close attention must be given to their culture, their governance and their remuneration practices.

1.3 Key questions

In its written submission in response to the *Interim Report*, Treasury identified the key questions emerging from the *Interim Report* as:[3]

- To what extent can the law be simplified so that its intent is met, rather than merely its terms being complied with, and how can this be done?
- Should the approach to addressing conflicts of interest change from managing conflicts to removing them, either by banning all or some forms of **conflicted remuneration** and sales or profit-based remuneration and/or changing industry structures?
- What can be done to improve compliance with the law (and industry codes), and the effectiveness of the regulators, to deter misconduct and ensure that grave misconduct meets with proportionate consequences?

Treasury submitted that a fourth key question should be added:[4]

- What more can be done to achieve effective leadership, good governance and appropriate culture within financial services firms so that firms 'obey the law, do not mislead or deceive, are fair, provide fit for purpose service with care and skill, and act in the best interests of their clients'?

Treasury submitted that answers to these four questions 'would form the pillars of any comprehensive policy response to what the Commission has publicly exposed'.[5]

I agree. These are the pillars of the policy responses to be made. And, as is explained in the body of the Report, some particular changes to the law are necessary to improve protections for consumers against misconduct, to provide adequate redress and to address asymmetries of power and information between entities and consumers.

---

3 Treasury, Interim Report Submission, 1 [2].

4 Treasury, Interim Report Submission, 1 [3]. See also, FSRC, *Interim Report*, vol 1, 290.

5 Treasury, Interim Report Submission, 1 [4].

1.4 Extending the Commission

Why deal with these issues now? Why make my *Final Report* now? Why not extend the work of the Commission? Many suggested that I seek an extension of the time by which my *Final Report* was due to allow for further public hearings.

I did not seek any extension of time for this *Final Report* for the reasons I gave in the Introduction to the *Interim Report*. As I said there:[6]

> The Letters Patent require me to inquire into, and report on, whether any conduct by financial services entities, including banks and their associated entities, might have amounted to misconduct and whether any conduct, practices, behaviour or business activities by those entities fall below community standards and expectations. I must execute those tasks conscious of the fact that the banking system is a central artery in the body of the economy. Defects and obstructions in the artery can have very large effects. Likewise, prolonged injections of doubt and uncertainty can affect performance.

I concluded then, and remain of the view, that these reasons oblige me to execute my tasks promptly and do so in ways that would achieve two related purposes: to identify properly the underlying causes of conduct of the kinds referred to in the Terms of Reference; and to prompt proper consideration of how best to avoid recurrence of similar conduct.

One reason often given for proposing to extend the work of the Commission was to give more persons who had been affected by relevant misconduct the chance to give evidence of those events. Throughout the work of the Commission I have paid close regard, and given great significance, to the Commission conducting a public inquiry so that there might be public exposure of misconduct and the vindication those affected by misconduct derive from its being exposed. All of the many public submissions made to the Commission were read and considered, and many were considered repeatedly.

6 FSRC, *Interim Report*, vol 1, 1.

Not every complaint that was made could be publicly examined. There were too many to do that. Hence, choices had to be made and, inevitably, the choices that were made will have disappointed those not chosen.

But the cases that were the subject of case studies were chosen as being reasonably illustrative of kinds of conduct and general issues that could be seen as emerging from the very active public engagement with the Commission's work and from the Commission's own investigations. The case studies provided a sufficiently broad and firm platform for drawing the conclusions that are expressed in this Report. Multiplying examples would not have altered the breadth or depth of that platform to any useful extent. And, as I point out more than once in this Report, every financial services entity, whether examined in a case study or not, must look at its own conduct and the way in which it governs itself.

The decision not to seek an extension was taken recognising that the Commission could provide no remedy to those who complained that they had been affected by misconduct. The most that could be done was to provide them with a public platform to voice their complaint. I recognise the importance of a Royal Commission in giving public voice to the issues and concerns that prompted its establishment. But the decision not to seek extension was also taken recognising the central importance that the health of the financial system has for the nation's economy and thus for every member of this society. For me, these wider considerations were determinative.

It is time to grapple with the key questions identified. And it is necessary, therefore, to state plainly the principles and general rules that underpin the answers that are to be given.

1.5 Underlying principles and general rules

In my *Interim Report* I asked many questions. As I said at that time, I sought to provoke informed and useful debate about the issues that have emerged in the course of the Commission's inquiries.

Many of those questions were explored in the course of the final round of the Commission's public hearings and in the many submissions made to the Commission. Submissions were received from financial services entities; the Australian Prudential Regulation Authority (APRA); the

Australian Securities and Investments Commission (ASIC); Treasury; those who have been affected by the conduct that has been the subject of the Commission's inquiries; other interested parties given leave to appear at some of the Commission's hearings (including the Finance Sector Union and consumer bodies such as CHOICE and the Consumer Action Law Centre); industry associations (including the Australian Banking Association (ABA) bodies representing financial advisers, mortgage brokers and others); academics; and members of the public more generally.

The focus of this Report must be on issues, causes and responses. I will deal separately with the various sectors of the financial services industry. More particularly I will deal separately with:

- banking;
- financial advice;
- superannuation; and
- insurance.

Some more general issues extend across all sectors of the financial services industry. They are issues about

- culture, governance and remuneration; and
- regulators.

The responses to the issues that are identified in each of those separate areas are informed by some underlying principles. It is useful, therefore, to begin by stating those principles.

1.5.1 Underlying principles

At their most basic, the underlying principles reflect the six norms of conduct I identified in the *Interim Report*:

- obey the law;
- do not mislead or deceive;
- act fairly;

- 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 norms of conduct are fundamental precepts. Each is well-established, widely accepted, and easily understood.

Of course, when these norms are stated in the terms I have, it will be said that borderline cases can be identified. And applying the norms to some of those borderline cases may not be easy. But real or imagined cases testing the boundaries of a rule do not show that the rule has no content. Debate about whether the wire runs one side or the other of one or more fence posts must not obscure the size of the field the fence encloses.

The six norms of conduct I have identified are all reflected in existing law. But the reflection is piecemeal.

The general obligations of **Australian financial services licence** (AFSL) holders, stated in section 912A of the Corporations Act, and the general obligations of **Australian Credit Licence** (ACL) holders, stated in section 47 of the NCCP Act, stand out.

First, both provisions impose an overarching obligation to 'do all things necessary to ensure' that the financial services or credit activities authorised by the licence are provided 'efficiently, honestly and fairly'.[7] Understood properly, this requirement would embrace all six norms.

Second, both provisions oblige licence holders to comply with, in the case of AFSL holders, the financial services laws and, in the case of ACL holders, the credit legislation.[8] That is, licence holders must obey the law.

Third, both provisions oblige licence holders to maintain their own competence to provide the licenced services and to ensure that their representatives are both adequately trained and competent to provide

---

7 Corporations Act s 912A(1)(a); NCCP Act s 47(1)(a).

8 Corporations Act s 912A(1)(c); NCCP Act s 47(1)(d).

those services.[9] That is, they are required to have the *capacity* to deliver services with reasonable care and skill.

As the law now stands, breach of these general obligations carries no penalty. They are licence conditions enforceable only indirectly, by threatening withdrawal of the licence.

That said, the requirement that an AFSL holder acts honestly is expressed further in section 1041G of the Corporations Act, which makes it an offence to engage in dishonest conduct in relation to a **financial product** or financial service. But the offence relates only to conduct in relation to a financial product or financial service, and Divisions 3 and 4 of Part 7.1 of the Corporations Act are given over to defining what is, and is not, a financial product, and when a person provides a financial service.

The more particular norms I state about not misleading or deceiving and acting fairly are reflected in the provisions of the *Australian Securities and Investment Commission Act 2001* (Cth) (the ASIC Act) about misleading or deceptive conduct,[10] false or misleading representations,[11] unconscionable conduct[12] and unfair contract terms.[13] And the requirement to provide services that are fit for purpose and deliver services with reasonable care and skill are also reflected in the ASIC Act.[14] But some of those provisions apply generally and some apply only to dealings with consumers. And the unconscionable conduct and consumer protection provisions use definitions of 'financial product' and 'financial service' that differ from those provided by Chapter 7 of the Corporations Act.[15]

The sixth norm – when acting for another, act in the best interests of that other – is reflected in the financial advice sector by the best interests duty imposed by section 961B of the Corporations Act, together with the

---

9 Corporations Act s 912A(1)(e) and (f); NCCP Act s 47(1)(e) and (f).

10 ASIC Act s 12DA.

11 ASIC Act s 12DB.

12 ASIC Act ss 12CA–12CC.

13 ASIC Act ss 12BF–12BM.

14 ASIC Act ss 12EA–12ED.

15 ASIC Act ss 12BAA,12BAB.

associated obligation provided by section 961J to give priority to the client's interests over other interests.

The norms are dealt with differently in respect of superannuation and insurance. In superannuation, they find their most prominent reflection in the SIS Act, in the best interests covenant and associated covenants by **registrable superannuation entity** (RSE) licensees and directors of trustees.[16] And those covenants also provide direct reflection of the norm that a person or entity acting for another, must act in the best interests of that other.

In insurance, all of the norms may be seen as embodied in the duty of utmost good faith imposed on each party to an insurance contract by section 13 of the *Insurance Contracts Act 1984* (Cth) (the Insurance Contracts Act).

As I say, the six norms of conduct I have set out are reflected in existing law, but the reflection is piecemeal.

1.5.2 General rules

The six norms of conduct I have identified support, and in some cases entail, some general rules:

- the law must be applied and its application enforced;
- industry codes should be approved under statute and breach of key promises made to customers in the codes should be a breach of the statute;
- no financial product should be 'hawked' to retail clients;
- intermediaries should act only on behalf of, and in the interests of, the party who pays the intermediary;
- exceptions to the ban on conflicted remuneration should be eliminated;

16 SIS Act ss 52, 52A.

- culture and governance practices (including remuneration arrangements) both in the industry generally and in individual entities, must focus on non-financial risk, as well as financial risk.

Why these general rules?

Apply and enforce the law

The first general rule, that the law must be applied and its application enforced, requires no development or explanation. It is a defining feature of a society governed by the rule of law.

The conduct identified and criticised in the Commission's *Interim Report* and in this Report has been of a nature and extent that shows that the law has not been obeyed, and has not been enforced effectively. It also points to deficiencies of culture, governance and risk management within entities. Too often, entities have paid too little attention to issues of regulatory, compliance and conduct risks. And the risks of regulatory or other non-compliance and of misconduct are the risks of departure from the first general rule of 'obey the law'. What consequences follow, and whether this amounts to effective enforcement of the law, bears directly upon the nature and extent of the regulatory, compliance and conduct risks that entities must manage.

Industry codes

Industry codes are expressed as promises made by industry participants. If industry codes are to be more than public relations puffs, the promises made must be made seriously. If they are made seriously (and those bound by the codes say that they are), the promises that are set out in the code, and are intended to govern the particular relations between the provider and the acquirer of a financial product or financial service, must be kept. This must entail that the promises can be enforced by those to whom the promises are made: the customer who acquires the product or service, and the guarantors of loans to individuals and small businesses.

Hawking

'Hawking' company securities, by making unsolicited approaches to potential buyers, has long been unlawful.[17] The practice has long been unlawful because it too readily allows the fraudulent or unscrupulous to prey upon the unsuspecting.[18] There is no real check on what is said to the target and often the target is not able to check the truth of what is said. The asymmetry of power and information between the provider of the product and service and the acquirer is very large. Even if the 'hawker' is not fraudulent or unscrupulous (and, too often, cases examined in evidence showed that the hawker was at least unscrupulous) the acquirer is nevertheless 'unsuspecting'. The potential acquirer who has not sought out the product or service comes to the encounter unprepared to look critically at whatever is said. The potential acquirer often does not know what questions to ask.

Hawking financial products and managed investment products is now generally prohibited.[19] But there are some exceptions. Other than the provisions relating to offers *not* made to retail clients and offers made under an eligible employee share scheme,[20] however, there is no immediately apparent basis for thinking that the exceptions are areas where the fraudulent or unscrupulous may not yet prey upon the unsuspecting. And the evidence given to the Commission points firmly against maintaining exceptions to the general prohibition, at least in respect of superannuation and insurance products, other than the two exceptions mentioned: offers *not* made to retail clients and offers made under an eligible employee share scheme.

For the avoidance of doubt, it should also be made plain that a solicited meeting, or telephone call, to discuss one type of financial product must not

---

17 The 1926 Report of the UK Company Law Amendment Committee chaired by Mr Wilfrid Greene KC (Cmnd 2657) recommended that the offering from house to house of shares, stock, bonds, debentures or debenture stock or similar securities either for subscription or sale should be made an offence. Hawking company securities has long been an offence under Australian company law. See now Corporations Act s 736.

18 United Kingdom, Report of the UK Company Law Amendment Committee (Cmnd 2657), 48 [92].

19 Corporations Act ss 992A and 992AA.

20 Corporations Act ss 992A(3A) and (3B).

be used for the unsolicited offering of some other type of product. (In that regard, common forms of banking products, like transaction accounts and credit card accounts should be treated as together forming the one kind of product. But each superannuation product and each insurance product is, and should be treated as, a distinct product type.)

Intermediaries

In the *Interim Report*, I pointed out how difficult it may be to decide for whom intermediaries act and to whom a particular intermediary may owe duties and responsibilities.[21] As I indicated then, the difficulties may be acute in the case of mortgage brokers. But the difficulties are not confined to home lending. Point-of-sale negotiation of credit arrangements (by car dealers, white goods retailers and the like) presents similar difficulties.

The point is much more important than a dry point of legal analysis. For whom the intermediary acts determines what duties the intermediary owes and to whom they owe them.

The general rule that should apply throughout the financial services industry is that an intermediary who is paid to act as intermediary:

- acts for the person who *pays* the intermediary;
- owes the person who pays a duty to act *only in the interests* of that person; and
- ordinarily owes the person who pays a duty to act in the *best* interests of that person.

The particular working out of these principles, especially with respect to mortgage brokers and the home lending market, is dealt with in the chapter about banking.

Conflicted remuneration

The definition of 'conflicted remuneration' in the Corporations Act shows why the practice should be prohibited.

---

21 FSRC, *Interim Report*, vol 1, 56–9.

Section 963A of the Corporations Act defines 'conflicted remuneration' as any benefit (whether monetary or non-monetary) given to a **financial services licensee** or a representative of the licensee, who provides financial product advice to persons as retail clients, that, because of the nature of the benefit or the circumstances in which it is given, could have either or both of two effects:

- it could reasonably be expected to influence the choice of financial product recommended by the licensee or representative to retail clients; or
- it could reasonably be expected to influence the financial product advice given to retail clients by the licensee or representative.

That is, as I said in the *Interim Report*, 'the very hinge about which the conflicted remuneration provisions turn is that the payment is one that "could reasonably be expected to influence the choice of financial product recommended to retail clients"'.[22]

For **grandfathered commissions**, the time when the initial advice was given and the initial conflict arose has passed. The influence of the commission has already done its work once. But the problem remains. The influence continues. Advisers have an incentive to keep their clients in products with grandfathered commissions rather than advise them to move to better products. There can be, and is, no justification for maintaining the grandfathering provisions.

Culture and governance

After the Global Financial Crisis (GFC), financial services entities and regulators, in Australia and elsewhere, gave close attention to financial risk. Until recently, however, too little attention has been given in Australia to regulatory, compliance and conduct risks. Too little attention has been given to the evident connections between compensation, incentive and remuneration practices and regulatory, compliance and conduct risks. The very large reputational consequences that are now seen in the Australian financial services industry, especially in the banking industry, stand as the clearest demonstration of the pressing urgency for dealing with these

22 FSRC, *Interim Report*, vol 1, 92.

issues. As the Group of Thirty (G30) said in November 2018, 'getting culture and conduct right is not a supervisory requirement. It is necessary for banks' and banking's economic and social sustainability'.[23]

1.5.3 Making change carefully and simply

Treasury,[24] and many of the entities that made submissions,[25] urged the need for caution before recommending change. This is undeniably right.

As I said in the *Interim Report*, adding a new layer of regulation will not assist. It will add to what is already a complex regulatory regime. No doubt the financial services industry is itself complicated. That may be said to explain why the regulatory regime is as complicated as it is. But closer attention will show that much of the complication comes from piling exception upon exception, from carving out special rules for special interests. And, in almost every case, these special rules qualify the application of a more general principle to entities or transactions that are not different in any material way from those to which the general rule is applied.

History shows, as Treasury submitted, that legislative simplification can be a long and difficult task. Programs to simplify the law relating to income taxation and to reform corporate law have extended over many years – well beyond the life of a single Parliament. And I do not doubt that simplifying the law that relates to the financial services industry would be a large task. But there are two parts of that task that can inform, and I consider should inform, what is done in response to this Report.

First, it is time to start reducing the number and the area of operation of special rules, exceptions and carve outs. Reducing their number and their area of operation is itself a large step towards simplificiation. Not only that,

23 G30, *Banking Conduct and Culture: A Permanent Mindset Change*, November 2018, Foreword, v.

24 Treasury, Interim Report Submission, 1 [4]–[5].

25 See, eg, AMP, Interim Report Submission, 7 [34]; ANZ, Interim Report Submission, 2 [11]; CBA, Interim Report Submission, 41 [223]; Westpac, Interim Report Submission, 2 [6]; NAB, Interim Report Submission, 17 [50]; Mortgage Choice, Interim Report Submission, 3 [3].

it leaves less room for 'gaming' the system by forcing events or transactions into exceptional boxes not intended to contain them.[26]

Second, it is time to draw explicit connections in the legislation between the particular rules that are made and the fundamental norms to which those rules give effect. Drawing that connection will have three consequences. It will explain to the regulated community (and the regulator) *why* the rule is there and, at the same time, reinforce the importance of the relevant fundamental norm of conduct. Not only that, drawing this explicit connection will put beyond doubt the purpose that the relevant rule is intended to achieve. And, the further consequence will be to highlight the fact that exceptions and carve outs like grandfathered commissions constitute a departure from applying the relevant fundamental norm. Emphasising the fact of departure may assist in reducing both the number and the extent of these qualifications.

In their submissions, some entities used the undoubted need for care in recommending change as a basis for saying that there should be *no* change. The 'Caution' sign was read as if it said 'Do Not Enter'.

An assertion was necessarily implicit in the submissions that sought to maintain some aspect of the present regime unchanged: that doing nothing about those matters would carry less cost than making *any* change to the rules under consideration. But rarely, if ever, was the submission developed beyond the point of bare assertion. Rarely, if ever, was there explicit examination of, or comparison between, the costs of doing nothing and the costs and consequences of changing the rules. The rules that govern grandfathered commissions provide a useful example.

Two grounds have often been given for maintaining the present rules about grandfathered commissions without modification: orderly transition and constitutional infirmity.

If the provisions were made to allow orderly transition within the industry, that time has now passed. How much longer is the transition to take? For all the suggestions that it will 'wither on the vine', the charging and receipt of

[26] For example, the preservation of grandfathered commissions during a successor fund transfer by potentially treating the succeeding RSE licensee as a 'platform operator': see the NULIS Nominees (Australia) Ltd case study discussed in vol 2 of this Report.

grandfathered commissions remained alive and well until some of the larger participants in the industry (especially the banks) sensed the wind of change may be blowing and found it best to bend now by phasing it out rather than have the wind grow to such intensity that it snap off this branch of their activities.

Whenever change is mooted, someone will suggest that changing the permitted forms of remuneration would lead to constitutional difficulties because it would amount to an acquisition of property otherwise than on just terms. As I said in the *Interim Report*, two points must be made.[27] First, where would be the acquisition? Who would acquire anything? What proprietary benefit or interest would accrue to any person?[28] Second, if the point is good, it was good at the time when most forms of conflicted remuneration were prohibited. Yet no-one sought then to challenge the validity of the relevant provisions and the **Future of Financial Advice** (FoFA) ban on conflicted remuneration has now operated for more than five years without challenge.

It is time to ignore the ghostly apparition of constitutional challenge conjured forth by those who, for their own financial advantage, oppose change that will free advice about, or recommendation of, financial products from the influence of the adviser's personal financial advantage.

A third point is sometimes made in attempting to justify preserving grandfathered commissions. It is said that prohibiting this form of remuneration once and for all will carry with it unintended consequences and the advice industry will be disrupted.

Generalised fears of this kind should not be heeded.

'Disruption' and similar terms can be used, and in some submissions to the Commission were used, as little more than pejorative synonyms for 'change'. As the Treasury submissions show, however, it is always necessary to identify the nature and the extent of the consequences that will or may follow from the change under consideration before speaking of the change as 'disruptive'. Without identifying those consequences, 'disruption' has no useful content.

---

27 FSRC, *Interim Report*, vol 1, 95.

28 Cf *JT International SA v The Commonwealth* (2012) 250 CLR 1.

If an exception to the rules prohibiting grandfathered commissions is to be preserved, the exception must be closely and cogently justified. Saying only that there may be 'disruption' or 'unintended consequences' is nothing but a naked appeal to fear of the future. And it seeks to graft some exception onto the body of law intended to give effect to a coherent set of policy objectives without any attempt to identify the competing policy objectives.

Creating exceptions that depart from underlying principles has consequences. Those consequences are amply demonstrated by the grandfathering arrangements made in respect of FoFA. 'Temporary' or 'transitional' carve outs departing from principle too often become (and in this case did become) entrenched. Carve outs and exceptions are too often exploited (and in this case have been exploited) for purposes having nothing to do with the stated purpose of their creation. Creating carve outs and exceptions impedes, and may even prevent (and in this case did prevent) achieving fully the intended policy objectives that inform the body of the law. Instead, the law is (and here it was) made more complex; it is (and here it was) made harder not only for regulators to administer but also for the regulated community, and the public more generally, to understand.

2 Recommendations

In the succeeding chapters of this Report, I make a number of recommendations. It is desirable to set them out here and to do that:

- first, by reference to subject matter, recording the recommendations in the order in which they are considered in the body of the Report; and
- second, restating the recommendations but reordering them by reference to the key questions identified above, and then by reference to the more particular changes that must be made to protect consumers against misconduct, to provide adequate redress and to address asymmetries of power and information.

2.1 Reading the recommendations

All of the recommendations set out below are to be read and understood in the light of what is said in the body of the Report. In particular, each recommendation is to be read in light of the reasons given for making it and what is said about other steps regulators, entities and the industry more generally can, and should, take in response to the conduct and events referred to in the *Interim Report* and this Report.

3 Recommendations by subject matter

3.1 Banking

Consumer lending: Direct lending

Recommendation 1.1 – The NCCP Act

The NCCP Act should not be amended to alter the obligation to assess unsuitability.

Consumer lending: Intermediated home lending

Recommendation 1.2 – Best interests duty

The law should be amended to provide that, when acting in connection with home lending, mortgage brokers must act in the best interests of the intending borrower. The obligation should be a civil penalty provision.

Recommendation 1.3 – Mortgage broker remuneration

The borrower, not the lender, should pay the mortgage broker a fee for acting in connection with home lending.

Changes in brokers' remuneration should be made over a period of two or three years, by first prohibiting lenders from paying trail commission to mortgage brokers in respect of new loans, then prohibiting lenders from paying other commissions to mortgage brokers.

Recommendation 1.4 – Establishment of working group

A Treasury-led working group should be established to monitor and, if necessary, adjust the remuneration model referred to in Recommendation 1.3, and any fee that lenders should be required to charge to achieve a level playing field, in response to market changes.

Recommendation 1.5 – Mortgage brokers as financial advisers

After a sufficient period of transition, mortgage brokers should be subject to and regulated by the law that applies to entities providing financial product advice to retail clients.

Recommendation 1.6 – Misconduct by mortgage brokers

ACL holders should:

- be bound by information-sharing and reporting obligations in respect of mortgage brokers similar to those referred to in Recommendations 2.7 and 2.8 for financial advisers; and
- take the same steps in response to detecting misconduct of a mortgage broker as those referred to in Recommendation 2.9 for financial advisers.

Consumer lending: Intermediated lending for vehicles and other consumer goods

Recommendation 1.7 – Removal of point-of-sale exemption

The exemption of retail dealers from the operation of the NCCP Act should be abolished.

Access to banking services

Recommendation 1.8 – Amending the Banking Code

The ABA should amend the Banking Code to provide that:

- banks will work with customers:
  - who live in remote areas; or
  - who are not adept in using English,

  to identify a suitable way for those customers to access and undertake their banking;
- if a customer is having difficulty proving his or her identity, and tells the bank that he or she identifies as an Aboriginal or Torres Strait Islander person, the bank will follow AUSTRAC's guidance about the identification and verification of persons of Aboriginal or Torres Strait Islander heritage;
- without prior express agreement with the customer, banks will not allow informal overdrafts on basic accounts; and
- banks will not charge dishonour fees on basic accounts.

Lending to small and medium enterprises

Recommendation 1.9 – No extension of the NCCP Act

The NCCP Act should not be amended to extend its operation to lending to small businesses.

Recommendation 1.10 – Definition of 'small business'

The ABA should amend the definition of 'small business' in the Banking Code so that the Code applies to any business or group employing fewer than 100 full-time equivalent employees, where the loan applied for is less than $5 million.

Recommendation 1.11 – Farm debt mediation

A national scheme of farm debt mediation should be enacted.

Recommendation 1.12 – Valuations of land

APRA should amend Prudential Standard APS 220 to:

- require that internal appraisals of the value of land taken or to be taken as security should be independent of loan origination, loan processing and loan decision processes; and
- provide for valuation of agricultural land in a manner that will recognise, to the extent possible:
  - the likelihood of external events affecting its realisable value; and
  - the time that may be taken to realise the land at a reasonable price affecting its realisable value.

Recommendation 1.13 – Charging default interest

The ABA should amend the Banking Code to provide that, while a declaration remains in force, banks will not charge default interest on loans secured by agricultural land in an area declared to be affected by drought or other natural disaster.

Recommendation 1.14 – Distressed agricultural loans

When dealing with distressed agricultural loans, banks should:

- ensure that those loans are managed by experienced agricultural bankers;
- offer farm debt mediation as soon as a loan is classified as distressed;
- manage every distressed loan on the footing that working out will be the best outcome for bank and borrower, and enforcement the worst;
- recognise that appointment of receivers or any other form of external administrator is a remedy of last resort; and
- cease charging default interest when there is no realistic prospect of recovering the amount charged.

Enforceability of industry codes

Recommendation 1.15 – Enforceable code provisions

The law should be amended to provide:

- that ASIC's power to approve codes of conduct extends to codes relating to all APRA-regulated institutions and ACL holders;
- that industry codes of conduct approved by ASIC may include 'enforceable code provisions', which are provisions in respect of which a contravention will constitute a breach of the law;
- that ASIC may take into consideration whether particular provisions of an industry code of conduct have been designated as 'enforceable code provisions' in determining whether to approve a code;
- for remedies, modelled on those now set out in Part VI of the Competition and Consumer Act, for breach of an 'enforceable code provision'; and
- for the establishment and imposition of mandatory financial services industry codes.

Recommendation 1.16 – 2019 Banking Code

In respect of the Banking Code that ASIC approved in 2018, the ABA and ASIC should take all necessary steps to have the provisions that govern the terms of the contract made or to be made between the bank and the customer or guarantor designated as 'enforceable code provisions'.

Processing and administrative errors

Recommendation 1.17 – BEAR product responsibility

After appropriate consultation, APRA should determine for the purposes of section 37BA(2)(b) of the Banking Act, a responsibility, within each ADI subject to the BEAR, for all steps in the design, delivery and maintenance of all products offered to customers by the ADI and any necessary remediation of customers in respect of any of those products.

3.2 Financial advice

Ongoing fee arrangements

Recommendation 2.1 – Annual renewal and payment

The law should be amended to provide that ongoing fee arrangements (whenever made):

- must be renewed annually by the client;
- must record in writing each year the services that the client will be entitled to receive and the total of the fees that are to be charged; and
- may neither permit nor require payment of fees from any account held for or on behalf of the client except on the client's express written authority to the entity that conducts that account given at, or immediately after, the latest renewal of the ongoing fee arrangement.

Lack of independence

Recommendation 2.2 – Disclosure of lack of independence

The law should be amended to require that a financial adviser who would contravene section 923A of the Corporations Act by assuming or using any of the restricted words or expressions identified in section 923A(5) (including 'independent', 'impartial' and 'unbiased') must, before providing personal advice to a retail client, give to the client a written statement (in or to the effect of a form to be prescribed) explaining simply and concisely why the adviser is not independent, impartial and unbiased.

Quality of advice

Recommendation 2.3 – Review of measures to improve the quality of advice

In three years' time, there should be a review by Government in consultation with ASIC of the effectiveness of measures that have been implemented by the Government, regulators and financial services entities to improve the quality of financial advice. The review should preferably be completed by 30 June 2022, but no later than 31 December 2022.

Among other things, that review should consider whether it is necessary to retain the 'safe harbour' provision in section 961B(2) of the Corporations Act. Unless there is a clear justification for retaining that provision, it should be repealed.

Conflicted remuneration

Recommendation 2.4 – Grandfathered commissions

Grandfathering provisions for conflicted remuneration should be repealed as soon as is reasonably practicable.

Recommendation 2.5 – Life risk insurance commissions

When ASIC conducts its review of conflicted remuneration relating to life risk insurance products and the operation of the ASIC Corporations (Life Insurance Commissions) Instrument 2017/510, ASIC should consider further reducing the cap on commissions in respect of life risk insurance products. Unless there is a clear justification for retaining those commissions, the cap should ultimately be reduced to zero.

Recommendation 2.6 – General insurance and consumer credit insurance commissions

The review referred to in Recommendation 2.3 should also consider whether each remaining exemption to the ban on conflicted remuneration remains justified, including:

- the exemptions for general insurance products and consumer credit insurance products; and
- the exemptions for non-monetary benefits set out in section 963C of the Corporations Act.

Professional discipline of financial advisers

Recommendation 2.7 – Reference checking and information sharing

All AFSL holders should be required, as a condition of their licence, to give effect to reference checking and information-sharing protocols for financial advisers, to the same effect as now provided by the ABA in its 'Financial Advice – Recruitment and Termination Reference Checking and Information Sharing Protocol'.

Recommendation 2.8 – Reporting compliance concerns

All AFSL holders should be required, as a condition of their licence, to report 'serious compliance concerns' about individual financial advisers to ASIC on a quarterly basis.

Recommendation 2.9 – Misconduct by financial advisers

All AFSL holders should be required, as a condition of their licence, to take the following steps when they detect that a financial adviser has engaged in misconduct in respect of financial advice given to a retail client (whether by giving inappropriate advice or otherwise):

- make whatever inquiries are reasonably necessary to determine the nature and full extent of the adviser's misconduct; and
- where there is sufficient information to suggest that an adviser has engaged in misconduct, tell affected clients and remediate those clients promptly.

Recommendation 2.10 – A new disciplinary system

The law should be amended to establish a new disciplinary system for financial advisers that:

- requires all financial advisers who provide personal financial advice to retail clients to be registered;
- provides for a single, central, disciplinary body;
- requires AFSL holders to report 'serious compliance concerns' to the disciplinary body; and
- allows clients and other stakeholders to report information about the conduct of financial advisers to the disciplinary body.

3.3 Superannuation

Trustees' obligations

Recommendation 3.1 – No other role or office

The trustee of an RSE should be prohibited from assuming any obligations other than those arising from or in the course of its performance of the duties of a trustee of a superannuation fund.

Recommendation 3.2 – No deducting advice fees from MySuper accounts

Deduction of any advice fee (other than for intra-fund advice) from a MySuper account should be prohibited.

Recommendation 3.3 – Limitations on deducting advice fees from choice accounts

Deduction of any advice fee (other than for intra-fund advice) from superannuation accounts other than MySuper accounts should be prohibited unless the requirements about annual renewal, prior written identification of service and provision of the client's express written authority set out in Recommendation 2.1 in connection with ongoing fee arrangements are met.

'Selling' superannuation

Recommendation 3.4 – No hawking

Hawking of superannuation products should be prohibited. That is, the unsolicited offer or sale of superannuation should be prohibited except to those who are not retail clients and except for offers made under an eligible employee share scheme.

The law should be amended to make clear that contact with a person during which one kind of product is offered is unsolicited unless the person attended the meeting, made or received the telephone call, or initiated the contact for the express purpose of inquiring about, discussing or entering into negotiations in relation to the offer of that kind of product.

Nominating default funds

Recommendation 3.5 – One default account

A person should have only one default account. To that end, machinery should be developed for 'stapling' a person to a single default account.

Recommendation 3.6 – No treating of employers

Section 68A of the SIS Act should be amended to prohibit trustees of a regulated superannuation fund, and associates of a trustee, doing any of the acts specified in section 68A(1)(a), (b) or (c) where the act may reasonably be understood by the recipient to have a substantial purpose of having the recipient nominate the fund as a default fund or having one or more employees of the recipient apply or agree to become members of the fund.

The provision should be a civil penalty provision enforceable by ASIC.

Regulation

Recommendation 3.7 – Civil penalties for breach of covenants and like obligations

Breach of the trustee's covenants set out in section 52 or obligations set out in section 29VN, or the director's covenants set out in section 52A or obligations set out in section 29VO of the SIS Act should be enforceable by action for civil penalty.

Recommendation 3.8 – Adjustment of APRA and ASIC's roles

The roles of APRA and ASIC with respect to superannuation should be adjusted, as referred to in Recommendation 6.3.

Recommendation 3.9 – Accountability regime

Over time, provisions modelled on the BEAR should be extended to all RSE licensees, as referred to in Recommendation 6.8.

3.4 Insurance

Manner of sale and types of products sold: Hawking

Recommendation 4.1 – No hawking of insurance

Consistently with Recommendation 3.4, which prohibits the hawking of superannuation products, hawking of insurance products should be prohibited.

Recommendation 4.2 – Removing the exemptions for funeral expenses policies

The law should be amended to:

- remove the exclusion of funeral expenses policies from the definition of 'financial product'; and
- put beyond doubt that the consumer protection provisions of the ASIC Act apply to funeral expenses policies.

Specific steps in respect of particular products: Add-on insurance

Recommendation 4.3 – Deferred sales model for add-on insurance

A Treasury-led working group should develop an industry-wide deferred sales model for the sale of any add-on insurance products (except policies of comprehensive motor insurance). The model should be implemented as soon as is reasonably practicable.

Recommendation 4.4 – Cap on commissions

ASIC should impose a cap on the amount of commission that may be paid to vehicle dealers in relation to the sale of add-on insurance products.

Pre-contractual disclosure and representations

Recommendation 4.5 – Duty to take reasonable care not to make a misrepresentation to an insurer

Part IV of the Insurance Contracts Act should be amended, for consumer insurance contracts, to replace the duty of disclosure with a duty to take reasonable care not to make a misrepresentation to an insurer (and to make any necessary consequential amendments to the remedial provisions contained in Division 3).

Recommendation 4.6 – Avoidance of life insurance contracts

Section 29(3) of the Insurance Contracts Act should be amended so that an insurer may only avoid a contract of life insurance on the basis of non-disclosure or misrepresentation if it can show that it would not have entered into a contract on any terms.

Unfair contract terms

Recommendation 4.7 – Application of unfair contract terms provisions to insurance contracts

The unfair contract terms provisions now set out in the ASIC Act should apply to insurance contracts regulated by the Insurance Contracts Act. The provisions should be amended to provide a definition of the 'main subject matter' of an insurance contract as the terms of the contract that describe what is being insured.

The duty of utmost good faith contained in section 13 of the Insurance Contracts Act should operate independently of the unfair contract terms provisions.

Claims handling

Recommendation 4.8 – Removal of claims handling exemption

The handling and settlement of insurance claims, or potential insurance claims, should no longer be excluded from the definition of 'financial service'.

Status of industry codes

Recommendation 4.9 – Enforceable code provisions

As referred to in Recommendation 1.15, the law should be amended to provide for enforceable provisions of industry codes and for the establishment and imposition of mandatory industry codes.

In respect of the Life Insurance Code of Practice, the Insurance in Superannuation Voluntary Code and the General Insurance Code of Practice, the Financial Services Council, the Insurance Council of Australia and ASIC should take all necessary steps, by 30 June 2021, to have the provisions of those codes that govern the terms of the contract made or to be made between the insurer and the policyholder designated as 'enforceable code provisions'.

Recommendation 4.10 – Extension of the sanctions power

The Financial Services Council and the Insurance Council of Australia should amend section 13.10 of the Life Insurance Code of Practice and section 13.11 of the General Insurance Code of Practice to empower (as the case requires) the Life Code Compliance Committee or the Code Governance Committee to impose sanctions on a subscriber that has breached the applicable Code.

External dispute resolution

Recommendation 4.11 – Co-operation with AFCA

Section 912A of the Corporations Act should be amended to require that AFSL holders take reasonable steps to co-operate with AFCA in its resolution of particular disputes, including, in particular, by making available to AFCA all relevant documents and records relating to issues in dispute.

Recommendation 4.12 – Accountability regime

Over time, provisions modelled on the BEAR should be extended to all APRA-regulated insurers, as referred to in Recommendation 6.8.

Group life policies

Recommendation 4.13 – Universal terms review

Treasury, in consultation with industry, should determine the practicability, and likely pricing effects, of legislating universal key definitions, terms and exclusions for default MySuper group life policies.

Recommendation 4.14 – Additional scrutiny for related party engagements

APRA should amend Prudential Standard SPS 250 to require RSE licensees that engage a related party to provide group life insurance, or who enter into a contract, arrangement or understanding with a life insurer by which the insurer is given a priority or privilege in connection with the provision of life insurance, to obtain and provide to APRA within a fixed time, independent certification that the arrangements and policies entered into are in the best interests of members and otherwise satisfy legal and regulatory requirements.

Recommendation 4.15 – Status attribution to be fair and reasonable

APRA should amend Prudential Standard SPS 250 to require RSE licensees to be satisfied that the rules by which a particular status is attributed to a member in connection with insurance are fair and reasonable.

3.5 Culture, governance and remuneration

Remuneration

Recommendation 5.1 – Supervision of remuneration – principles, standards and guidance

In conducting prudential supervision of remuneration systems, and revising its prudential standards and guidance about remuneration, APRA should give effect to the principles, standards and guidance set out in the Financial Stability Board's publications concerning sound compensation principles and practices.

Recommendations 5.2 and 5.3 explain and amplify aspects of this Recommendation.

Recommendation 5.2 – Supervision of remuneration – aims

In conducting prudential supervision of the design and implementation of remuneration systems, and revising its prudential standards and guidance about remuneration, APRA should have, as one of its aims, the sound management by APRA-regulated institutions of not only financial risk but also misconduct, compliance and other non-financial risks.

Recommendation 5.3 – Revised prudential standards and guidance

In revising its prudential standards and guidance about the design and implementation of remuneration systems, APRA should:

- require APRA-regulated institutions to design their remuneration systems to encourage sound management of non-financial risks, and to reduce the risk of misconduct;
- require the board of an APRA-regulated institution (whether through its remuneration committee or otherwise) to make regular assessments of the effectiveness of the remuneration system in encouraging sound management of non-financial risks, and reducing the risk of misconduct;
- set limits on the use of financial metrics in connection with long-term variable remuneration;

- require APRA-regulated institutions to provide for the entity, in appropriate circumstances, to claw back remuneration that has vested; and
- encourage APRA-regulated institutions to improve the quality of information being provided to boards and their committees about risk management performance and remuneration decisions.

Recommendation 5.4 – Remuneration of front line staff

All financial services entities should review at least once each year the design and implementation of their remuneration systems for front line staff to ensure that the design and implementation of those systems focus on not only what staff do, but also how they do it.

Recommendation 5.5 – The Sedgwick Review

Banks should implement fully the recommendations of the Sedgwick Review.

Culture and governance

Recommendation 5.6 – Changing culture and governance

All financial services entities should, as often as reasonably possible, take proper steps to:

- assess the entity's culture and its governance;
- identify any problems with that culture and governance;
- deal with those problems; and
- determine whether the changes it has made have been effective.

Recommendation 5.7 – Supervision of culture and governance

In conducting its prudential supervision of APRA-regulated institutions and in revising its prudential standards and guidance, APRA should:

- build a supervisory program focused on building culture that will mitigate the risk of misconduct;
- use a risk-based approach to its reviews;
- assess the cultural drivers of misconduct in entities; and
- encourage entities to give proper attention to sound management of conduct risk and improving entity governance.

3.6 Regulators

Twin peaks

Recommendation 6.1 – Retain twin peaks

The 'twin peaks' model of financial regulation should be retained.

ASIC's enforcement practices

Recommendation 6.2 – ASIC's approach to enforcement

ASIC should adopt an approach to enforcement that:

- takes, as its starting point, the question of whether a court should determine the consequences of a contravention;
- recognises that infringement notices should principally be used in respect of administrative failings by entities, will rarely be appropriate for provisions that require an evaluative judgment and, beyond purely administrative failings, will rarely be an appropriate enforcement tool where the infringing party is a large corporation;

- recognises the relevance and importance of general and specific deterrence in deciding whether to accept an enforceable undertaking, and the utility in obtaining admissions in enforceable undertakings; and
- separates, as much as possible, enforcement staff from non-enforcement related contact with regulated entities.

Superannuation: Conduct regulation

Recommendation 6.3 – General principles for co-regulation

The roles of APRA and ASIC in relation to superannuation should be adjusted to accord with the general principles that:

- APRA, as the prudential regulator for superannuation, is responsible for establishing and enforcing Prudential Standards and practices designed to ensure that, under all reasonable circumstances, financial promises made by superannuation entities APRA supervises are met within a stable, efficient and competitive financial system; and
- as the conduct and disclosure regulator, ASIC's role in superannuation primarily concerns the relationship between RSE licensees and individual consumers.

Effect should be given to these principles by taking the steps described in Recommendations 6.4 and 6.5.

Recommendation 6.4 – ASIC as conduct regulator

Without limiting any powers APRA currently has under the SIS Act, ASIC should be given the power to enforce all provisions in the SIS Act that are, or will become, civil penalty provisions or otherwise give rise to a cause of action against an RSE licensee or director for conduct that may harm a consumer. There should be co-regulation by APRA and ASIC of these provisions.

Recommendation 6.5 – APRA to retain functions

APRA should retain its current functions, including responsibility for the licensing and supervision of RSE licensees and the powers and functions that come with it, including any power to issue directions that APRA presently has or is to be given.

The BEAR: Co-regulation

Recommendation 6.6 – Joint administration of the BEAR

ASIC and APRA should jointly administer the BEAR. ASIC should be charged with overseeing those parts of Divisions 1, 2 and 3 of Part IIAA of the Banking Act that concern consumer protection and market conduct matters. APRA should be charged with overseeing the prudential aspects of Part IIAA.

Recommendation 6.7 – Statutory amendments

The obligations in sections 37C and 37CA of the Banking Act should be amended to make clear that an ADI and accountable person must deal with APRA and ASIC (as the case may be) in an open, constructive and co-operative way. Practical amendments should be made to provisions such as section 37K and section 37G(1) so as to facilitate joint administration.

Recommendation 6.8 – Extending the BEAR

Over time, provisions modelled on the BEAR should be extended to all APRA-regulated financial services institutions. APRA and ASIC should jointly administer those new provisions.

Co-ordination and information sharing

Recommendation 6.9 – Statutory obligation to co-operate

The law should be amended to oblige each of APRA and ASIC to:

- co-operate with the other;
- share information to the maximum extent practicable; and
- notify the other whenever it forms the belief that a breach in respect of which the other has enforcement responsibility may have occurred.

Recommendation 6.10 – Co-operation memorandum

ASIC and APRA should prepare and maintain a joint memorandum setting out how they intend to comply with their statutory obligation to co-operate.

The memorandum should be reviewed biennially and each of ASIC and APRA should report each year on the operation of and steps taken under it in its annual report.

Governance

Recommendation 6.11 – Formalising meeting procedure

The ASIC Act should be amended to include provisions substantially similar to those set out in sections 27–32 of the APRA Act – dealing with the times and places of Commissioner meetings, the quorum required, who is to preside, how voting is to occur and the passing of resolutions without meetings.

Recommendation 6.12 – Application of the BEAR to regulators

In a manner agreed with the external oversight body (the establishment of which is the subject of Recommendation 6.14 below) each of APRA and ASIC should internally formulate and apply to its own management accountability principles of the kind established by the BEAR.

Recommendation 6.13 – Regular capability reviews

APRA and ASIC should each be subject to at least quadrennial capability reviews. A capability review should be undertaken for APRA as soon as is reasonably practicable.

Oversight

Recommendation 6.14 – A new oversight authority

A new oversight authority for APRA and ASIC, independent of Government, should be established by legislation to assess the effectiveness of each regulator in discharging its functions and meeting its statutory objects.

The authority should be comprised of three part-time members and staffed by a permanent secretariat.

It should be required to report to the Minister in respect of each regulator at least biennially.

3.7 Other important steps

External dispute resolution

Recommendation 7.1 – Compensation scheme of last resort

The three principal recommendations to establish a compensation scheme of last resort made by the panel appointed by government to review external dispute and complaints arrangements made in its supplementary final report should be carried into effect.

ASIC Enforcement Review Taskforce Government Response

Recommendation 7.2 – Implementation of recommendations

The recommendations of the ASIC Enforcement Review Taskforce made in December 2017 that relate to self-reporting of contraventions by financial services and credit licensees should be carried into effect.

Simplification so that the law's intent is met

Recommendation 7.3 – Exceptions and qualifications

As far as possible, exceptions and qualifications to generally applicable norms of conduct in legislation governing financial services entities should be eliminated.

Recommendation 7.4 – Fundamental norms

As far as possible, legislation governing financial services entities should identify expressly what fundamental norms of behaviour are being pursued when particular and detailed rules are made about a particular subject matter.