Consumer protection in financial services

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In pursuit of world class consumer policy

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Check against delivery

Good Afternoon. I would like to thank Consumer Affairs Victoria for inviting me to address you today as we together pursue world-class consumer policy.

I understand that you have spent the last couple of days discussing and debating a range of consumer policy issues – from the direction in which such policy is traveling at State, Federal and global levels to the role of consumer agencies and consumers themselves.

Today, I would like to confront these issues in the context of ASIC's regulation of financial products and services. In particular, I will focus on:

- ASIC's role as a consumer protection regulator;
- some of our recent consumer protection activities, which span the responsibilities of both industry and consumers; and
- how ASIC intends to clear some of the challenging hurdles that lie ahead.

ASIC: Consumer protection in financial services

As most of you will be aware, ASIC is the national regulator and enforcer of company and financial services laws in Australia. We have a statutory mandate to promote the confident and informed participation of investors and consumers in the financial system[1]. ASIC has a dedicated Consumer Protection directorate that focuses on consumer priorities and liaises directly with many of you here today. The staff in that directorate play a central role in influencing ASIC's consumer strategies.

One important difference between the regulatory responsibilities of ASIC and the ACCC (as we have just heard from Graeme Samuel) is that ASIC also has a direct licensing role. We currently licence most providers of financial services and products including financial advisers, superannuation trustees, general and life insurance companies, banks and other

[1] *Australian Securities and Investments Commission Act 2001 (Cth)*, s1(2)(b).

intermediaries such as insurance and stockbrokers. The main omission from our licensing regime is credit providers and credit intermediaries.

In very simple terms, ASIC grants licences to financial services providers where they prove that they have the organisational competency to comply with a range of obligations under the *Corporations Act*. Licensees are also required to put in place compliance arrangements, make certain disclosures and join an ASIC approved dispute resolution scheme.

Our responsibilities under the *ASIC Act* focus on the same types of conduct that the ACCC has responsibility for under the *Trade Practices Act*. We too work to prevent and take action in relation to unconscionable, misleading or deceptive conduct connected to financial services and products. It is important to note that our jurisdiction under the *ASIC Act* is broader than under the *Corporations Act*. It does extend to credit, which I know plays a prominent role in the casework of many people here today.

Balancing business facilitation and consumer protection is a complex business. At a very simplistic level, it involves ASIC considering each of the following questions:

- ‘when is business behaviour unacceptable?’; and
- ‘when are consumer behaviours or expectations unreasonable?’.

Further investigation of these two questions will form the basis of my presentation today. Because there is no one answer – or silver bullet – ASIC routinely calls on a suite of responses which include enforcement, promoting better industry standards and providing consumer education and warnings. We also work extensively in the alternative dispute resolution sector to ensure that consumers have access to remedies.

Before I move on, I would like to mention ASIC’s Consumer Advisory Panel (‘CAP’), which we consider to be a great success. Fiona Guthrie has most recently chaired CAP and I would like to take this opportunity to publicly acknowledge and thank Fiona for the fantastic job that she has done over the last two years in this role. I wish her well in her new endeavour as

Senior Adviser to Queensland's Attorney-General and Minister for Justice, Linda Lavarch MP.

CAP meets quarterly. It provides ASIC with robust views about emerging or ongoing consumer issues that Panel members think we might – or should – respond to. In the last 12 months, these have ranged from the conduct of debt agreement administrators to the emergence of shared equity products, the operation of share buyback schemes and concerns about the quality of advice.

ASIC provides CAP with an annual research budget, which it has applied in the past to projects including a review of the mortgage broker industry, research into book-up practices in indigenous communities and more recently, the experience of consumers who establish and operate self-managed superannuation funds. This research, together with the input from CAP members more generally, play an extremely important role in informing ASIC's work.

Tackling unacceptable industry conduct

But retuning to the broader consumer protection challenge, the first point I would like to make is at the pointy end: ASIC is prepared to take strategic action against unacceptable industry conduct.

A primary obligation of all licensed financial services providers is that they operate honestly, efficiently and fairly. Our annual reports set out the range of enforcement actions that ASIC takes across our entire corporate jurisdiction (and which collectively influence the proper functioning of financial markets). However, I want to focus today on some specific actions – enforcement and beyond – that more directly relate to our consumer protection role in financial services.

Commonwealth Bank of Australia – Indigenous lending

In January this year, ASIC announced a negotiated settlement with the Commonwealth Bank about misconduct by brokers organising loans with indigenous consumers. This was achieved in conjunction with the South Australian Office of Consumer and Business Affairs. The conduct involved three brokers. Our view was that, as the lender, the Commonwealth Bank should have been aware of discrepancies and inaccuracies in loan applications, and more systemically, that its eligibility criteria facilitated loans being approved that dramatically overcommitted borrowers.

The incoming CEO of the Commonwealth Bank, on being made aware of the issue by ASIC, immediately required a thorough, unbiased investigation. This led to the Commonwealth Bank and ourselves reaching a settlement, thereby avoiding totally unnecessary litigation costs, with their inherent delays.

As part of the settlement, the Commonwealth Bank agreed to:

1. introduce new eligibility criteria for remote communities that take into account the higher cost of living and variability in borrowers' incomes in these areas;
2. write off or restructure up to approximately 75% of the loans introduced by the three brokers; and
3. fund a financial counseling position that will work with Indigenous communities for at least the next three years.

In this case, ASIC wanted to effect systemic change within the institution. We also wanted to acknowledge that Indigenous Australians are among the least empowered of all consumers and that, as a regulator, we are compelled to act on this sort of conduct. This was not an issue that could have been addressed through consumer education alone.

Superannuation advertising

At the other end of the spectrum, since the introduction of Superannuation Choice of Fund in July 2005, ASIC has been proactively monitoring superannuation advertising through print, radio and television. The importance of superannuation has been one of ASIC's strategic consumer priorities.

This has been complemented by a specific focus on superannuation fees. In February this year, we enforced changes to advertising claims made by two superannuation funds, Virgin Super and maxSuper. This was in response to ASIC's concerns that the funds were promoting single low fees, which did not take into account *all* of the costs that consumers might incur.

We are confident this focus is warranted when you consider that a 1% difference in fees each year could mean up to a 20% difference in a consumer's retirement benefit over 30 years. Putting this into context, on an opening balance of $50,000 and a salary of $55,575, the difference between fees of 1% and 2% each year could be $61,000 – a clear indication that we should continue to watch this area closely.

To help consumers compare the cost of funds, we have undertaken two important initiatives. We have created a superannuation calculator that lets consumers compare the costs of funds based upon their particular circumstances, as well as shows them the impact of fees over time on their super balances. We have also provided comparative information on the fees charged by over 800 super funds and will soon have fee information on all funds. You can find both these tools on our FIDO website.

Equity release report

To continue the pre-emptive theme, in November last year, ASIC released a report about 'equity release products'. These are products that allow consumers to access the equity in their homes while still living there. The most well recognised of these is the reverse mortgage, which has also seen the most significant growth in the last two years (in the 12 months to March 2005, the number of reverse mortgage providers leapt from three to more than 15).

Generally, ASIC's jurisdiction over these products is limited to our *ASIC Act* powers over misleading, deceptive and unconscionable conduct connected to credit and does not extend to our *Corporations Act* licensing powers.

ASIC is actively monitoring this sector and working with industry to promote best practice, particularly given the fact that these products also do not fit neatly within the provisions of the *Uniform Consumer Credit Code*.

To this end, last month, we released a calculator on our FIDO website which shows the likely cost of reverse mortgages over time. We are currently investigating misleading representations by one product provider and we will also be releasing fact sheets about each of the equity release products on the market, including (in addition to reverse mortgages) home reversion schemes and shared appreciation mortgages, by the end of March.

Improving industry standards

Another important aspect of our relationship with industry is in working to raise industry standards. Recent examples that have impacted the market include guidance about soft-dollar commissions and our collaborative work with the ACCC on debt collection guidelines.

Another example that reflects industry initiative in raising standards is the Financial Planning Association's ('FPA') conflicts of interest principles, which were released earlier this month. Our Deputy Chairman, Jeremy Cooper, and policy team actively engaged with the FPA in the development of these principles, meeting with the FPA and providing comment (as appropriate). We applaud this approach, which exemplifies the benefits of combining different streams of thought leadership to current and important issues.

Many of you would also be aware of ASIC's shadow shopping surveys in relation to financial advice. From July to December last year, ASIC undertook its second survey since the introduction of the *Financial Services Reform Act* – we completed the first in 2003. The current survey tested superannuation advice given to around 300 consumers. I cannot pre-empt our findings in this survey today; they are to be released shortly. I do want to stress, however, that ASIC's commitment to funding these surveys is not only to identify problems in the market for advice – as some industry players might have you believe – but also to give us a platform from which to promote continuous improvement in the advice industry. ASIC's focus on this segment of the market reflects our recognition of how essential advice is for Australian consumers, who now face self-funded retirements and are obliged to make significant and informed financial decisions well beyond the purchase of their family home. The valuable information these surveys provide about consumers' actual experiences in the market and their ability to create a positive momentum for industry improvement is, I think, one of our most important tools.

In finishing on the industry side of the ledger, I also want to reflect on the Regulation Taskforce established by the Federal Government, which was charged with, among other things, identifying unnecessarily burdensome or complex regulation and providing practical options for cutting 'red tape' to reduce the regulatory burden on business. The Prime Minister is yet to make the findings of this Taskforce public. However, we recognise the benefits of this initiative and are, ourselves, committed to reducing any unnecessary and unproductive regulatory burden on business, which can also lead to suboptimal outcomes for consumers, who will ultimately bear the cost.

Inherent risk in investing

Before I move on to the topic of consumer behaviour and expectations, I would like to raise an issue that relates more to our dealings with consumers as investors, but nonetheless affects everyone's confidence in financial markets generally.

All investments carry some degree of risk depending on their nature and type and I would like to preface my comments with two facts: ASIC does not operate solely to protect consumers and ASIC cannot ever regulate to zero risk. Businesses fail, and will continue to fail, and investors in those business will suffer losses. But after 14 years of economic prosperity, I am deeply concerned that many in the community have become blinded to the real risk of economic downturn, which historically has followed such growth.

This is a pertinent message in the wake of the recent collapse of the Westpoint group of companies. I do not want to go into all the details of this collapse or ASIC's ongoing investigations in this matter. There is dedicated information on our website, including specific messages for investors who have lost money. However, I would like to share a recent experience arising out of a meeting I hosted last month in Sydney for about 60 Westpoint investors.

Many of these people lost a substantial part of their life savings, some having fully geared their family homes to invest in Westpoint.

Notwithstanding ASIC's concern about the conduct of advisers in relation to investments in Westpoint – and this is something that we are investigating – it was clear that many investors were unclear about what 'high risk' meant in the context of promoted returns. One investor at the meeting indicated that, in their view, returns of 25% and over were high risk (Westpoint was promoting returns of about 12%). It was also clear that there was a real lack of understanding about what diversification means – in an investing context.

We are actively encouraging consumers who have suffered loss as a result of the Westpoint collapse to lodge complaints. I have written to all licensed advisers that we understand received commission payments from Westpoint, indicating our expectations about the prompt, fair and effective resolution of such complaints using their internal dispute resolution processes. I have also written to all major industry associations, requesting that they provide effective leadership to their members about responding to genuine complaints by consumers affected by the Westpoint collapse quickly and consistently. The text of both of these letters will be available on ASIC's website shortly.

Nonetheless, I would like to mention the significant role that the Financial Industry Complaints Service ('FICS') – a scheme approved by ASIC – will play in assisting Westpoint investors to resolve disputes about the conduct of licensed advisers. ASIC has strongly supported the role of FICS as an appropriate, independent and free service for consumers. In my view, however, the Westpoint collapse presents something of a test for the dispute resolution sector, which is ultimately funded by industry representatives. It is the first large systemic event affecting a single dispute resolution scheme. We will work closely with FICS over the coming months.

Consumer behaviour and expectations

Moving now to the consumer side, we have to also acknowledge that consumers can make poor financial decisions. This is an incontrovertible fact. As I have already discussed, it can be driven by inappropriate or illegal industry conduct or advice. In other cases, it reflects low levels of financial literacy. However, it can also be symptomatic of:

- fear of an impending poorly self-funded retirement;
- having English as a second language; or
- simply put, unreasonable expectations that the government will always ‘bail you out’.

Consumers are not homogenous and they do not always act rationally. In my view, however, they are likely to fall into three broad categories:

- those who are financially responsible because they choose to be, probably labeled the ‘conservative’;
- those who are ‘gamblers’ and pursue inappropriate risk-taking behaviour; and
- those who fall somewhere in between – possibly financially literate, but with a tendency to either act on impulse or accept, without question, advice provided to them.

I know that you are well aware of these complexities and we are currently planning to undertake market research to test my perceptions, as it is important that we have the most reliable understanding of the environment in which we, as regulators, are expected to communicate with and protect consumers. I would, therefore, like to share some examples of how ASIC has recently gone about responding to this communication challenge.

Basic information through the popular media

ASIC is specifically targeting basic information about money management through high circulation daily newspapers like the Herald Sun in Melbourne, the Daily Telegraph in Sydney and the Courier Mail in Brisbane. Our Media Relations Unit has worked hard to establish relationships with journalists to develop newsworthy stories and tips that consumers can engage with. Our driving philosophy with these releases is to keep it simple.

Our traditional messages in a range of ways

Last year, ASIC released the very popular 'Your Money' booklet, which was reproduced in the Herald Sun and Daily Telegraph on release. We are now using the content of this brochure to produce a series of programs for community radio, covering a range of topics including credit, insurance, superannuation and investing. Some consumer representatives here today have been interviewed for the programs and I would like to thank you for your participation. ASIC has already had strong interest from more than 100 regional radio stations across Australia.

Schools competition

Now in its third year and with the support of the Department of Education in the Northern Territory and, more recently, the ACT, ASIC runs an annual high school competition in which students design posters with slogans that convey a money-related consumer protection message. This aims to encourage high school students to think about money matters at an age when they may soon be making their own financial decisions about what to do with their first income from part-time work.

Simple tools

ASIC has also developed a suite of its own online calculators. In addition to the reverse mortgages and superannuation calculators that I mentioned earlier, these include a simple compound interest calculator and a credit card calculator that indicates the effect of paying only the minimum payment on a credit card each month, compared to paying a little extra.

The challenges ahead: Clearing the hurdles

ASIC is justifiably proud of these initiatives – from enforcement to raising industry standards to countering consumer behaviour and expectations.

However, my recent meeting with 60 Westpoint investors reminded me that:

- not all consumers can access a computer and download information from the ASIC or FIDO websites;
- there is no guarantee that our press releases and warnings reach the consumers that need them most (probably because they often get coverage in the business section of the press instead of the early general news section); and
- even when our warnings do reach consumers, do they heed them?

This means that we need to keep working on our communication strategies, and we intend to do so. We need to ask ourselves: what is the most effective way to communicate with consumers?

As I mentioned earlier, a prime example is continuing to get the message out about the relationship between risk and return. We have all been saying for many years: 'if it's too good to be true, then it probably is'. But given that we estimate that at least 6,000 investors have lost around $500 million of their life savings chasing high returns in the last three years or so – not including potential losses in the Westpoint Group collapse – then we clearly have not won the war.

At ASIC, we are currently thinking about possible additional ways in which we can more effectively speak to consumers. One option is establishing a telephone service for consumers to call about money offers – a 'dial before you dig' approach, drawing on our canine consumer icon, FIDO.

While warnings are one approach, we must also remind consumers that investing can, and **should**, be simple. There is credible choice available, there are prudentially regulated entities, there are other sound investments and good advisers are available.

Conclusion

ASIC is committed to maintaining and enhancing market confidence in a strong, fair and progressive way, but we cannot do this alone.

Regulation is a complex balancing act and it is only through collaboration with both industry and consumers that we can make it work for the financial system as a whole.

ASIC values its relationship with the consumer sector, and the important role you play in influencing policy and strategic outcomes. My final message in this context is, therefore, an invitation to consider how we can continue to support each other and develop stronger relationships, communicating with consumers together at a grassroots level to ensure that they are in a position to make informed and confident financial decisions.

Ends