



ASIC

Australian Securities & Investments Commission

ASIC: The strong, fair and progressive regulator

An Address by Jeffrey Lucy AM

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Australian Securities and Investments Commission

ASIC Summer School 2006

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Check against delivery

Good Afternoon. I would like to extend a warm welcome to you all today to ASIC's 11th Summer School.

This year, as a result of the work of the project team led by Mark Adams, ASIC's Director of Regulatory Policy, we are proud to be hosting our largest Summer School ever. You are each one of 210 participants. 36 of you join us from overseas and represent 15 countries – New Zealand, Republic of Ireland, Republic of Vanuatu, Fiji Islands, Singapore, Hong Kong, Korea, Malaysia, Papua New Guinea, Indonesia, Thailand, Sri Lanka, Cyprus, Pakistan and Saudi Arabia. We are absolutely delighted that this Summer School has such a broad international focus and participation. I also welcome 28 colleagues within ASIC representing each of our directorates – Compliance, Consumer Protection, Enforcement, Operations and Regulation – from states and territories throughout Australia.

During the course of this week, you will each witness a wonderful program that highlights the broad framework in which many of us must operate. This framework recognises the separate roles of regulators, industry, consumers and other stakeholders like the media and is designed to maintain and enhance market confidence.

Our theme this year, therefore, is *'Maintaining Consumer Confidence: Regulation and its limits'*. Why is this the theme we have chosen at this point in time? The answer, in my view, is clear. Regulation is a tool that has been used in most major jurisdictions in recent years against the backdrop of unprecedented economic growth worldwide. Historically, economic cycles suggest that a downturn will eventually follow. It is time, therefore, to consider the effectiveness and efficiency of regulation in this context.

We all witnessed a spate of corporate collapses earlier this century, both in Australia and abroad, with the demise of companies including WorldCom, Enron, Parmalat, HIH and One.Tel, to name but a few. In response to these perceived market failures, we saw a raft of new and more demanding

standards introduced. These attempt to establish good corporate governance practices related to financial reporting, audit, disclosure and corporate conduct generally. The United States, for example, introduced *Sarbanes-Oxley*. The Australian Federal Government continued its corporate law economic reform program with its CLERP 9 initiative, which calls for the provision of adequate, timely and reliable information about corporate performance.

Additionally, in Australia, we have witnessed an overhaul of our financial services regulatory framework in the last few years. The *Financial Services Reform Act*, or FSR as it has become fondly known, has created:

- a single licensing regime for all financial services providers;
- a consistent and comparable financial product disclosure regime across all financial products; and
- a single set of conduct requirements for providers of investment advice.

Estimates suggest that legislation in Australia grows at over 10% per annum¹. This does not even include the numerous individual exemptions and modifications that ASIC processes each year!

At the same time, markets worldwide, and particularly in Australia, are enjoying an unprecedented period of economic growth and broad public participation. Our equity markets have had one of their longest bull runs ever. Each day, we read in the press about how the stock market has hit 'yet another' record high. The growth of participation from the retail sector has been tremendous. Recent studies by the Australian Stock Exchange², for example, suggest that Australia is witnessing the highest penetration of share ownership ever experienced in Australia. They indicate that the trend of share ownership in Australia has increased steadily since the late 1980s and that, in 2004, 55% of the Australian population, or about eight million people, owned shares *directly* in listed companies, property trusts, managed

¹ Pearce, C., 'A Simpler Regulatory System', Address to G100 Dinner Meeting, 1 February 2006.

² See Australian Stock Exchange, Australia's Share Owners: An ASX study of share investors in 2004, February 2005 and Australian Stock Exchange, International Share Ownership (Comparison of Share Owners): Key Highlights, September 2005.

funds, derivatives or interest rate securities, or *indirectly* via managed funds or self-managed superannuation funds. The Australian Stock Exchange believes that this is among the highest reported level of share ownership in the world. Additionally, Australian interest rates remain at moderate levels and unemployment is historically low. Clearly, the market is offering opportunities to *all* investors, not simply big business and the wealthy.

These economic conditions are clearly spurred by an underlying level of market confidence. It is a timely reminder that economies typically work in cycles and historically, with each growth period, a downturn has followed. We are clearly at a point in the economic cycle, therefore, at which many begin to question, among other things, the efficacy and efficiency of regulation³ (that is, how well it all works).

History has shown that decisions (both wise and foolish) made in the good times can have repercussions in the bad. We must be open to the fact that many in the market – corporate directors and consumers alike – may feel overconfident making financial decisions because of the rosy economic landscape we are living in. However, overconfidence, apathy or complacency in decision-making can potentially return to haunt these punters when the economy moves in the opposite direction. To some extent, investors must take responsibility for their own decisions. My concerns are exacerbated given that many of the decision makers have not seen or lived through an economic downturn at all. I might add that this observation is also true of staff within ASIC. We are already seeing examples of people being blinded to the fact that risk has gone up, as distinct from having gone down, because we have been riding an upward cycle for so long.

It is time, therefore, to ask ourselves some hard questions.

□ Why regulate?

³ Pearce, C., 'A Simpler Regulatory System', Address to G100 Dinner Meeting, 1 February 2006.

- What are the ingredients of an 'appropriate' regulatory balance and what role can the regulator, industry, consumers and the media play in bringing this about?
- Are there other options?
- And, most importantly, does regulation really drive consumer confidence? In the context of disclosure rules and enforcement of laws, what impact does it ultimately have on consumer confidence? Is it the best way of maintaining consumer confidence, or is it little more than an unnecessary cost of doing legitimate business?

I have no intention of answering these questions now; they raise some complex issues and this week's program will, no doubt, allow you to more fully delve into them.

Instead, I would like to turn now to the role of the regulator in this debate, from my own perspective, as Chairman of ASIC. As many of you would be aware, amongst our broad range of responsibilities, ASIC must regulate and enforce company and financial services laws in order to protect consumers, investors and creditors.

Our role as the regulator is an important one in ensuring confident markets are maintained. We must pause here, however, to recognise that our task is not maintaining confidence alone; rather, it extends to ensuring that participants in those markets – the investors and consumers – are informed and in a position to make appropriate financial decisions.

ASIC essentially undertakes this particular role by carrying out the tasks required of it under the *ASIC Act*. We undertake to promote informed participation of investors and consumers in the market by educating them. We protect investors and consumers from improper and illegal practices by enforcing laws. And we balance these undertakings by facilitating business to improve performance of the market as a whole.

These actions help to ensure that our markets are clean and fair, so that all participants are confident to get involved. The key element of achieving this is finding the *right* balance between the series of apparent competing interests of investors, consumers, industry and ourselves. It might appear, taking a short-term view of the world, that such interests are impossible to mesh with each other. Industry might argue, for example, that consumers 'get their way' in being provided with disclosure documents like Financial Services Guides, Product Disclosure Statements and Statements of Advice. Consumers, on the other hand, might suggest that the length of some of these documents indicates that they are not for their protection at all, but rather simply to mitigate potential liability of their creator.

Whatever your view, I am of the firm belief that these interests are not competing, but indeed, complement one another. After all, industry would not exist without customers and, in order to avoid reputational damage and keep such customers, industry players must act in a way that retains consumers' confidence in them.

Of course, the reality is that we must accept that it is impossible to regulate to zero risk. The question, therefore, must be: how far can regulation actually be utilised, given its limits?

The answer, I think, is that our actions as a regulator alone will never achieve informed and confident markets. We face challenges such as the relatively low level of financial literacy in Australia⁴. Industry and consumers alike must, therefore, *also* take responsibility for making it work. This is exemplified by the fact that high levels of confidence do not necessarily correlate with quality financial product advice; nor does strong market confidence remedy disengaged or overly confident consumers who make poor financial decisions. Consumers must be open to learning about how to make good financial decisions. Industry can assist, and must.

⁴ ANZ Survey of Adult Financial Literacy in Australia, November 2005.

But, more importantly, maintaining and enhancing market confidence requires us all to look to maintaining an effective regulatory system able to adapt to change in a timely manner and meet the needs of all stakeholders. Engaging stakeholders through dialogue and building partnerships is key to achieving this.

There is no doubt that our **strong, fair** and **progressive** regulatory approach to date has been a key driver of market confidence in the Australian economy in recent years. Above all else, we have kept our feet on the ground in the present, looking towards the future with eyes that have witnessed the past.

The debates on the role of regulation in maintaining and enhancing consumer confidence are being echoed worldwide. You will shortly hear about the regulatory approach taken in the United States by their Securities and Exchange Commission, which I will not pre-empt at the moment. Tomorrow morning, you will hear about the Financial Service Authority's experience in promoting risk-based regulation in the United Kingdom.

For the time being, I will draw on the numerous initiatives that the Australian Federal Government and its agencies, including ASIC, have taken to address the challenge of getting the regulatory balance right.

In large part, we have challenged our cultural mindset; we are now thinking outside the regulatory box that many of us are accustomed to thinking in. We have been working hard at reducing regulatory burden and improving regulatory efficiency, wherever and whenever prudent.

More broadly, against the backdrop of principles-based regulation and active engagement with stakeholders, we are guided by principles of good regulation such as proportionality, accountability, transparency and consistency⁵.

⁵ Such principles, with the addition of targeting, are in fact the five principles of good regulation adopted in the United Kingdom.

From a proportionality viewpoint, ASIC intervenes only where necessary and fundamentally chooses delivery options that aim to achieve desired results and minimise costs and burdens.

We have simplified and streamlined many of our compliance and lodgment requirements. We implemented CLERP 7, which simplified company lodgment, reporting and compliance procedures. More recently, we have simplified the process Australian financial services providers must go through to obtain an Australian financial services licence, reducing the paperwork involved by at least 50%!

Similarly, we have assisted the Parliamentary Secretary to the Treasurer ('PST') in delivering a range of 'FSR Refinement' initiatives aimed at fine-tuning the day-to-day challenges that implementing FSR posed to industry and consumers. You will consider, for example, the limits of disclosure that these refinements addressed in some of this Thursday's sessions.

Additionally, we are improving the quality and 'useability' of our regulation communications. We are looking, in particular, at the nature, clarity and effectiveness of our policy documents.

We aim for openness and transparency in much that we do, particularly given that we are held accountable for all of our decisions and actions. The Minister responsible for ASIC is the Treasurer, the Hon Peter Costello MP and, in matters determined by him, the PST, the Hon Chris Pearce MP, who you will hear from this coming Friday. We must also answer to the Parliamentary Joint Committee on Corporations and Financial Services and appear before Committees such as the Senate Economics Committee as part of the Estimates process. Additionally, our decisions are subject to, among other things, a robust administrative law regime and, as a regulator, we ensure that the regulated themselves understand how they are being regulated.

To minimise the risk of regulatory inconsistency and duplication, we have established a joint ASIC/APRA working group. It will review areas of

perceived regulatory overlap or duplication between the two agencies and evaluate how each one might be resolved in a manner recognising the interests of all of our stakeholders. In our view, this is consistent with an appropriately balanced regulatory approach.

The Australian Federal Government, too, is committed to achieving such an approach. It has established an annual red tape reduction agenda through an annual review process of the cumulative stock of regulation. It also established the Regulation Taskforce last October, chaired by Gary Banks, Chairman of the Productivity Commission (and who will address you on Wednesday afternoon), which was given the task of, among others, identifying unnecessarily burdensome or complex regulation and providing practical options for alleviating the 'red tape' burden on business. We are yet to see the findings of this Taskforce. However, we nonetheless recognise the benefits of reducing any unnecessary and unproductive regulatory burden on business. We embrace the need for effective, reliant and efficient regulation.

I am providing many value-based propositions today. However, the full debate is still to be had. As the Australian corporate sector moves from looking at the cost of transitioning to any new regime, to considering the costs of complying with those regimes on an ongoing basis, the next step for ASIC is to come forward with a considered action plan setting out what we have done to date and what we are going to do moving forward. In doing so, we can establish further substantive means of achieving better, more efficient regulation in Australia.

During this process, we will need to maintain focus, determine appropriate means of undertaking cost-benefit analysis, analyse risk and, perhaps the most difficult of all, deal with embedding cultural change in the market generally, including industry, consumers, the media and ourselves, as the regulator. This has been recognised by the Hon Chris Pearce, MP, who recently addressed a G100 Dinner Meeting advocating 'A Simpler Regulatory System', where he stated that it is 'only with the support of the business

sector that we can begin to critically assess where we are, and what we want our regulatory framework to be⁶. I agree with that observation.

However, with respect, I might go further to suggest that the support required is not simply bi-faceted (us and industry), but rather, multi-faceted, the culmination of views of the Federal Government, other regulatory agencies, industry representatives, consumer advocates, the media and the broader community as a whole. I acknowledge the PST's comments that consultation presents limitations of its own, particularly where diverse views are revealed. However, I am of the firm opinion that ASIC, and the Australian Federal Government more broadly, are in a position to consider the various opinions of stakeholders and the costs and benefits of regulation. From such analysis, we can decide on the appropriate regulatory balance in particular class and individual cases.

I hope that I have given you a flavour of some of my own perspectives on these important issues. I would encourage you all to take advantage of the opportunities during the course of this week that will allow for discussion of the roles of the various stakeholders in regulation and consider their frames of reference, to formulate your own view.

We are fortunate to have many esteemed speakers this week that will fuel this discussion, including fellow international and domestic regulators, prominent business colleagues, industry, consumer and media representatives and the PST. We thank them for joining our forum and leading debate in this area.

You, too, will make an important contribution this week. You, the participants, are from a range of backgrounds, from fellow regulators and government agencies, to industry and consumer advocates. Importantly, many of you come to our Summer School providing an international perspective, which is invaluable. I encourage you all to take advantage of the ample opportunity that you have to develop effective working

⁶ Pearce, C., 'A Simpler Regulatory System', Address to G100 Dinner Meeting, 1 February 2006.

relationships with your fellow attendees – both during the days and at the evening social functions. This will allow us, in a robust manner, to confront, head on, the challenges in finding an appropriate regulatory balance in the interests of all stakeholders. Of course, it should also make for some very lively debate during the course of this week and, I expect and hope, that by the end of the week, we will have built the foundations of a much broader based community debate about the role of regulation in maintaining and enhancing consumer confidence.

I encourage you to participate in this debate and very much look forward to your participation.

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