Putting the customer first: Creating a win–win

A speech by Greg Medcraft, Chairman,
Australian Securities and Investments Commission

CFA Australia Investment Conference (Sydney, Australia)
13 October 2015

Introduction

Ladies and gentleman, it's a pleasure today to be speaking at the CFA Australia Investment Conference.

Today my topic is: 'Putting the customer first: Creating a win–win'.

Putting customers first builds customer trust and confidence. This is a win for the customer and a win for firms.

So today, I would like to talk about two things:

- First, what ASIC is doing to assist investor trust and confidence:
  - in general, and
  - specifically in relation to financial advice.
- Second, how industry can build trust and confidence, with a focus on creating a customer first culture.

My key message for today is that putting the customer first is a win for the customer, a win for the firm, and good for relations with the regulator.

What ASIC is doing to assist investor trust and confidence generally

So first I will turn to what ASIC is doing generally to assist investor trust and confidence.

ASIC's fundamental objective is to allow markets to fund the real economy and, in turn, economic growth. This contributes to improved standards of living for all Australians.

Markets cannot perform their fundamental purpose – funding the real economy and, in turn, economic growth – if investors and issuers do not have trust and confidence in them.

Making sure investors and issuers have trust and confidence in our markets is at the heart of everything we do. It is reflected in our twin regulatory strategic priorities of:

- investor trust and confidence, and
- fair, orderly, transparent and efficient markets.

Behaviour drivers in the financial system

Australia is a free market-based economy. The Australian financial system is predominantly privately owned and operates according to free market principles.

There are three cornerstones of the free market-based financial system. These are:

- investor responsibility
- gatekeeper responsibility, and
- the rule of law.

The ability of the free market-based system to function effectively and efficiently and to meet investor and financial consumer demands is greatly influenced by the real behaviour of its participants. There are a number of behavioural drivers that influence conduct in the financial system. They can either threaten or promote or threaten our strategic priorities.

For investors and financial consumers, their behaviour is driven by financial literacy – including their knowledge, skills, attitudes – and behavioural biases.

For gatekeepers – those who have a legal responsibility in the legal system, including product manufacturers, responsible entities, lenders, advisers, directors and auditors to name a few – their behaviour is driven by three things:

- Culture – the internal controls (i.e. policies, rules, courses of conduct, practices or attitudes) within a firm which shape its behaviour or mindset. A poor firm culture may encourage or tolerate an employee's breach of the law or encourage them not to act in the customer's best interests.
- Incentives including remuneration structures – these have a strong influence on the way that firms and their employees behave; for example, whether you compensate a whistleblower when they report issues to senior management.
- Deterrence – the likelihood and impact of getting caught. We are focused on detecting, understanding and responding to misconduct.

At ASIC we focus a lot of attention on deterrence. We use our 'detect, understand and respond' approach where there is wrongdoing or risk of wrongdoing in the market.

We gather intelligence from a range of sources, including surveillance, breach reports from gatekeepers, reports from the public, and reports from whistleblowers. Increasingly, we are using data analytics and connecting the dots in how we capture, share and use data to increase the likelihood of getting caught.

In terms of how we respond, we take enforcement action to provide credible deterrence, including criminal, civil and administrative actions. For gatekeepers, we take action to punish or remediate their behaviour. And we take action that will protect or compensate investors and financial consumers.

So each of these drivers I have talked about – culture, incentives and deterrence – affects the behaviour of gatekeepers, and can have potential impacts on investor and financial consumer trust and confidence.

ASIC's role in creating the right nudge

Making sure investors and issuers can have trust and confidence means that we use the right nudge to:

- provide education and tools to assist investors and financial consumers to take responsibility for their financial decisions
- ensure gatekeepers fulfil their legal responsibilities through our guidance, surveillance and enforcement, and
- see that the rule of law is enforced, and operates in a way that deters bad conduct – through providing policy advice to Government.

What ASIC is doing to build trust and confidence in financial advice

I would now like to talk about what ASIC is doing to build trust and confidence in the financial advice sector.

Trust and confidence in the financial advice sector is a major concern. Recent events in this area have impacted significantly on investor and financial consumer trust and confidence. According to Roy Morgan's national survey of Australians, only 24% of Australians say they trust financial advisers. ANZ's most recent Financial Literacy Survey also points to an erosion of trust in financial professionals since 2011.

Lifting trust and confidence in financial advice is critical, and needs to be based on the three cornerstones of the financial system.

Investors

For investors and financial consumers, we assist them with trusted financial education.

This education is delivered through multiple channels, and is targeted at a wide cross-section of communities – from primary, secondary and trade schools to multi-lingual people, indigenous people and military personnel – not to mention those who are simply approaching or going through a life financial event such as buying a home, divorce, or retirement.

For example, ASIC's MoneySmart website – moneysmart.gov.au – has over 500 webpages of consumer information, and has been visited over five million times in the last year. This is more than a 14% increase on the year before.

With our MoneySmart Teaching program, our target is embedding financial literacy from K–12. So far, 35% of the nation's 10,000 schools have engaged in the program. And to date, 14,000 teachers have undertaken professional development in financial literacy.

Gatekeeper responsibility

We shape the behaviour of our gatekeepers to lift trust and confidence in the financial advice sector through our guidance, surveillance and enforcement.

Guidance

We are proving guidance on remediation to firms.

- Over the last few years, ASIC has negotiated a number of major review and remediation programs by financial advice firms. These programs have been large-scale exercises to review personal financial advice provided to retail clients and to compensate those clients where losses have been suffered as a result of non-compliant advice, fraud or other breaches of the law.
- We recently announced that we will develop a regulatory guide on review and remediation programs conducted by advice firms, where clients may have suffered loss. We want to ensure that if a financial advice firm needs to provide remediation, they do so in a way that is fair, honest and efficient. Consumers will have greater trust if they can be confident that any remediation program is consistent and transparent.

Looking to the future, we are providing guidance to industry on robo-advice. In the last three years, robo-advice has been growing in popularity in the United States and United Kingdom. In Australia, some existing advice firms and new start-ups are looking to develop new robo-advice models.

We are engaging with industry on these new developments and how they fit within the regulatory framework. We see the potential of robo-advice to offer a convenient low-cost trusted advice offering to consumers. We have a common interest in seeing these opportunities harvested, while at the same time mitigating the risks to consumer trust and confidence.

Surveillance

In response to problems in the financial advice sector, we have set up a specialist wealth management team to focus on the large advice entities – namely, the four major banks, Macquarie and AMP. We have a significant number of individual surveillances underway in relation to those entities.

Two particular aspects of this are:

- advice compliance – we are looking to ensure that historic issues with advice are addressed and that, moving forward, appropriate systems are in place to ensure quality advice, and

- bad apples – we are looking closely at how the largest banks deal with 'bad apple' advisers. Adviser firms need to take greater responsibility for removing bad apples on an ongoing basis.

Enforcement

Our wealth management project includes a number of investigation activities related to financial advice failings and licensee breaches. In 2014–15:

- ASIC permanently banned 14 individuals from providing financial advice.
- A further 23 individuals were banned or agreed to stay out of the industry for a period of time.
- ASIC cancelled, suspended or placed conditions on 17 AFS licensees, with one additional AFS licensee agreeing to implement a regime of supervision, review and audit.

Rule of law

We provide advice to Government on the operation of the rule of law. In the financial advice sector:

- We have provided advice to Government on lifting professional standards.
  - There is agreement in the industry that the competency and professional standards need improving. A number of inquiries – including the Ripoll Inquiry, the Senate inquiry into the performance of ASIC and the Financial System Inquiry – reached the same conclusion.
  - We have worked with Treasury to improve adviser professionalism and ethical standards, including training.
  - The PJC inquiry into proposals to lift the professional, ethical and education standards in the financial services industry reported in December 2014. It put forward a comprehensive set of proposals for a new framework which ASIC broadly welcomes and which Government is currently considering.
- ASIC launched the financial advisers register on 31 March 2015.
  - This register provides key information on all individuals who provide personal retail advice on investment products and life insurance.
  - There are now over 22,000 advisers listed on the register, and to date there have been over 290,000 searches of the register.
  - This register allows consumers to find out information about their adviser before they choose an adviser or receive advice. It will give employers greater ability to assess new financial advisers. It will also improve ASIC's ability to identify and track the movements and history of financial advisers.
  - The data is available on data.gov.au and we expect it will assist development of web-based investor driven tools for the sector.

How industry can build trust and confidence

I would now like to touch on what industry can do to build investor trust and confidence.

Both regulators and industry have a role to play in building trust and confidence. At the centre of what industry can do is creating a ‘customer first’ culture. We care about culture because there is often a strong connection between poor culture and poor conduct. We consider it to be a key risk area with respect to our role as a conduct regulator, as it often is a red flag to broader regulatory problems.

I see that trust and confidence are not just important to regulators. It is also critical to the firms we regulate that their customers have trust and confidence in them. A firm with a poor culture that does not put the customer first will see the impacts on long-term sustainability. There are a number of ways that having a good culture can benefit the firm itself in building a sustainable business model. For example:

- maintaining customer loyalty and brand reputation
- avoiding the financial impact of fines or remediation, and
- employee retention.

Customer loyalty and brand reputation

Having a brand that has customer trust and confidence can bring with it a competitive advantage. If you don’t want to be disrupted, you need to have a brand that has trust and confidence.

In a competitive industry, customer satisfaction is a primary driver of customer loyalty and retention. If a client or customer loses trust and confidence in the products or services that a firm provides, the firm will soon see that the customer either exits, stops buying from the firm, or moves to a competitor. Obviously this will affect market share.

In the digital world, you have to think about the power of the crowd. A customer that has lost trust and confidence may also voice their concerns publically, to a friend or neighbour, or more broadly through social media. This, in turn, can have flow on effects to the retention and acquisition of customers. So, poor culture can damage brand and reputation, and the value of the firm itself.

Financial impact of fines and remediation

Even more tangible may be the fines, remediation and compensation paid out as a result of misconduct stemming from poor culture. In fact, a recent report by KPMG suggested that, since 2011, the largest banks in Britain have paid almost 60% of their profits in fines and repayments to customers. Put more simply, a bad culture impacts on the bottom line.

Employee retention

But also think about whether you personally would want to work for a firm that has a bad culture. Individuals increasingly want to work for an employer that can deliver both a profit as well as an impact. By creating a customer first culture, a firm makes itself a desirable place to work, an 'employer of choice'. And this, in turn, enables the firm to attract and employ the best staff, which of course is good for the bottom line.

Conclusion

In closing, I want to leave you with one message.

A customer first culture that gives customers trust and confidence is good for the customer. It's good for the bottom line of a firm, and building a sustainable business model. And it is good for your relationship with the regulator.

Having the right culture is essential for a long-term sustainable business.

I am very happy to take questions.

