Digital disruption: Harnessing the opportunities, mitigating the risks

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CHECK AGAINST DELIVERY

Introduction

Good afternoon all. It’s a pleasure to be here today. Today I am going to talk about digital disruption – both the opportunities and the risks.

Five years ago, we weren't thinking about digital disruption. But now, technology is traveling at a faster pace than ever. Technological innovation is rewriting every industry, including of course, the financial services industry. Innovation is disrupting and reshaping the world we live in.

Of course, we don't have crystal ball, and we do not know for sure how digital disruption will unfold in the future. But for now, it is fair to say that we cannot be future proof, but that we can be forward looking and proactive in responding to digital disruption. So today, I would like to talk about two things:

• the challenge posed for ASIC by digital disruption to existing business models and channels, and

• how ASIC is responding, in particular through:
  – ASIC’s Innovation Hub
  – our cyber resilience work, and
  – our robo-advice taskforce.
The challenge posed by digital disruption

I believe that the great drawcard of digital disruption is the opportunity it brings. New digital strategies continue to challenge traditional business models, disrupting financial services and markets and changing how they interact with investors and consumers, across a range of platforms and devices.

Digital disruption can improve the consumer experience. Technology can enable a product or service to be cheaper, quicker and/or more convenient. Businesses have seen the potential for new ways of creating and sharing value with technologically savvy investors and consumers. For example, the potential of:

- peer-to-peer lending/marketplace lending
- robo-advice
- crowd-sourced equity funding, and
- payments infrastructures, for example, digital currencies.

In the future, we will likely see further developments in:

- individually tailored insurance, and
- exchanges using the potential of blockchain technology.

And probably in areas we haven’t yet even thought of.

Digital disruption, by its nature, is not change by evolution – it is radical in the way it changes the landscape. But, of course, financial innovation brings both opportunities and risks. What is fundamentally important in all of this is thinking critically about the implications of digital disruption. In particular, how digital disruption may challenge ASIC’s strategic priorities of:

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

Often disruptive businesses have innovative business models that may not fit neatly within existing regulatory frameworks or policy. And, over recent years, there has been significant growth in the number and severity of cyber attacks around the world. These factors mean that while digital disruption brings great opportunity, it also brings risks.

How ASIC is responding?

So how is ASIC responding? In ASIC’s Corporate Plan 2015-2016 to 2018-2019, released in August this year, we set out how we are responding to our key challenges, including digital disruption and cyber resilience.

To respond to digital disruption and cyber resilience, we are continuing to focus on:

- First, promoting cyber resilience and identifying potential cyber attacks in markets through real-time market monitoring.
• Second, ensuring compliance with licensing obligations. To this end, we have focused on risk management by licensees and issued a report on cyber resilience earlier this year, particularly focused on the National Institute of Standards and Technology (NIST) Framework for improving Critical infrastructure cybersecurity (NIST framework) for measuring and communicating the competence and maturity of an entity’s level of cyber resilience.

• Third, as a pro-active and forward-looking regulator, we are taking steps to help industry take advantage of the opportunities on offer; while also ensuring that investor and financial consumer trust and confidence is not compromised. For example, through our Innovation Hub.

• Fourth, monitoring overseas developments on regulating financial technology (fintech) such as approaches evolving in many jurisdictions, including China and Singapore.

I would now like to talk about three specific ways that ASIC is responding through:

• our Innovation Hub;

• our work on cyber resilience; and

• our robo-advice taskforce.

ASIC’s Innovation Hub

We launched our Innovation Hub this year to foster digital innovation and help innovators navigate our regulatory system. This will in turn deliver potential benefits to investors, consumers and markets. It fits with ASIC’s commitment to cutting unnecessary red tape and facilitating business generally.

To date, through our Innovation Hub we have held 54 external meetings with new fintech businesses, industry organisations and other agencies. We have started work on matters relating to 43 entities, including licence applications and requests for guidance.

The Innovation Hub has five key components:

• Engagement: ASIC engages with fintech initiatives, including physical hubs and co-working spaces that have been established for start-up businesses. We are considering seconding staff to fintech hubs.

• Streamlining: We are streamlining ASIC’s approach to facilitating business for new business models. For example, by looking to streamline common application processes, including applying for or varying a licence and in granting waivers from the law.

• Access: We are making ourselves more accessible to new types of businesses. For example, a portal on our website that offers a one-stop shop for innovative businesses to access information and services directly targeted at them.

• Coordination: Within ASIC, we are adopting a coordinated approach led at Commission level, by Commissioner John Price, to applying any reforms that may apply to innovative businesses in the future.

• DFAC: We have established a Digital Finance Advisory Committee, or DFAC for short. This committee advises ASIC on its engagement with innovative businesses.
DFAC members are drawn from a cross-section of the fintech community, as well as academia and consumer backgrounds.

Last week the UK Financial Conduct Authority issued a report on a proposal to establish a ‘regulatory sandbox’ to allow start-ups a ‘safe space’ to test innovative products.

At ASIC, we are considering a similar approach. In many respects through our Innovation Hub strategy, ASIC already has significant flexibility to reduce regulatory burden and provide assistance on a case-by-case basis for innovative start-ups. But going forward, we are continuing to think about how we can make it easier for innovative start-ups to comply with regulatory obligations.

Cyber resilience

Turning to cyber resilience. There has been significant growth in the number, sophistication and severity of global cyber attacks in the last few years. They are viewed as a systemic risk for the financial sector.

ASIC is seeking to assist our regulated population, including boards, in their efforts to improve cyber resilience – that is, the ability to prepare for, respond to and recover from a cyber attack.

In March this year, we published our Report 429 Cyber resilience: Health check (REP 429) to help our regulated population improve cyber resilience by:

- increasing awareness of the risks
- encouraging collaboration between industry and government
- providing health check prompts to help businesses consider their cyber resilience, and
- identifying how cyber risks should be addressed in the regulatory context, including considering board oversight of cyber risks.

We encourage organisations to use the NIST framework – a voluntary, technology-neutral cybersecurity risk management tool for organisations.

Currently, we are missing a consistent language to identify, evaluate and communicate the capability and maturity of an organisation’s cyber resilience. The NIST framework may provide a starting point for this.

We will continue to improve awareness of the importance of cyber resilience and increase the profile of the issues for our regulated population, including:

- monitoring market developments and incorporating cyber resilience in our surveillance programs, where appropriate
- providing a self-assessment tool based on the NIST framework to our regulated population to assess cyber resilience, and
- updating REP 429, if necessary, to take into account any national or international developments on cyber risk management.
**Robo-advice**

In the last three years, robo-advice has been growing in popularity in the United States and the United Kingdom. Australian licensees and some start-ups have observed the growing popularity of robo-advice models offshore. They are now actively looking to develop, or are developing, their own robo-advice models.

ASIC is very supportive of automated provision of advice. We see that it has the potential to offer a convenient, low-cost advice service to consumers. We also see benefits such as improved compliance and record keeping; and the potential to reduce conflicts of interest.

We want to better understand robo-advice business models. We need to understand the risks and issues that underlie robo-advice.

The same laws and obligations for giving advice apply to digital advice – we see the legislation is technology neutral in the obligations it imposes. Robo-advice does, however, raise some interesting regulatory issues and challenges. Particular issues ASIC will focus on include:

- how robo-advice providers comply with the best interests duty
- how robo-advice providers develop and test their algorithms
- the training and competency requirements for those sitting behind robo-advice models, and
- the adequacy of a robo-advice operator's compensation arrangements.

We have set up an internal Robo-advice Taskforce to look at robo-advice issues. We are discussing these issues with robo-advice providers and those looking to join the space. Digital advice is growing rapidly and we will be working with operators to ensure they are getting it right and that investors can have trust and confidence in the advice they receive.

**Conclusion**

I would like to conclude by saying that, as a regulator, it is my job to be sceptical and ensure we harness the benefits while also mitigating the risks. In other words, we need to help innovation, while preserving both market integrity and the trust and confidence of investors.

At ASIC, we continue to collect data and inform ourselves about new developments. In this way, we can better understand the challenges and opportunities that digital disruption presents. But industry and regulators also need to work together to harvest the opportunities from digital disruption and financial innovation.

We all have a common interest in seeing the opportunities of digital disruption harvested. At the same time we need to mitigate the risks, so that we all enjoy the benefits of:

- investor and consumer trust and confidence in our markets, and
- sustainable growth.