The integration of financial regulatory authorities – the Australian experience

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1. What does our financial landscape look like?

Thank you very much for inviting me to speak today. In this session, I will provide you with an Australian perspective on the integration of financial system regulators.

Australia has a population of only 20.6 million people (less than 0.5% of world population, particularly as it compares to a population of over 186 million in Brazil). Yet our economy is ranked 15th in the world in size and we have over 1,900 entities listed on the Australian Stock Exchange (ASX). The total market capitalisation of listed entities on ASX is approximately US$900 billion[1] and it is ranked 8th in size on the Morgan Stanley Capital International Index of stock exchanges[2].

Not only do we have a larger than expected share market (ie twice as large as the size of our economy might suggest), but a high proportion of Australians invest in it. Roughly 55% of the Australian adult population own shares either directly or indirectly through collective investment and pension savings vehicles.

Australia also has a very large managed funds industry, amounting to approximately US$625 billion, which is the fourth largest in the world, after the United States, Luxembourg and France and ahead of Japan, Hong Kong and Singapore. This means that, on average, each Australian has approximately US$34,000 invested in managed funds – the highest average figure in the world.

This sets the context for an explanation of how Australia decided to structure its financial regulatory authorities.

2. Why good regulation is important

While the introduction of compulsory pension savings in 1992[3] has played an important role in the growth of investor participation in our markets, the importance of good regulation cannot be underestimated.[4] In our well-regulated environment:

- companies can get on with doing business confident that the same rules apply to everybody. They can seek capital in Australian markets at rates that are broadly competitive with leading world markets and without paying a significant market risk premium;
- financial services businesses can operate profitably and efficiently, while treating customers honestly and fairly. Being in a well-regulated market also helps them do business across borders;

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1 An exchange rate of US$1.00 to A$1.33 has been used throughout this paper.
2 As at 30 June 2006.
3 Under this system, all employers must contribute 9% of the gross salaries and wages of employees to a pension fund that cannot be accessed until retirement. Generally, the employee is able to choose which pension fund they want their contributions paid to.
4 This year, ASIC launched a special program called *Better Regulation* which, as the name suggests, is a series of initiatives aimed at improving the way we regulate. The brochure is on our website at: www.asic.gov.au.

- financial markets are well respected and attractive internationally, and are clean, fair and reliable;
- all participants can understand their obligations;
- investors and consumers can participate confidently in the financial system, using reliable and trustworthy information to make decisions, with access to suitable remedies if things go wrong; and
- the community is confident that markets, corporations and the businesses involved in them operate efficiently and honestly and contribute to improving Australia's economic performance. Firm action is taken against fraud, dishonesty and misconduct. The regulatory system is respected.

3. Origins of modern financial regulation in Australia

Our current system of financial regulation traces its origins back to 1996 when the Australian Government established the Financial System Inquiry.[5]

The Inquiry followed a period of financial deregulation in Australia that started in the early 1980s. The Inquiry was tasked with:

- providing a stocktake of the results arising from that financial deregulation;
- analysing the forces driving further change to the financial landscape with particular emphasis on technological change;
- recommending the best overall framework for the efficient delivery of regulation; and
- recommending ways to improve the then current regulatory arrangements.

A respected Australian businessman, Stan Wallis, chaired the Inquiry, which became known as the 'Wallis Inquiry' or just 'Wallis'. It is important to note that the Wallis Inquiry was not prompted by any particular failure or financial crisis – indeed it came at a time of steady growth and relative calm in the Australian financial markets. So, Wallis was able to consider what should be the shape of Australia's financial system regulation, without any pressure to redress a systemic or other regulatory or financial failure.

4. Options for financial regulation in Australia

Wallis put forward three main regulatory options; a *mega regulator*, a *lead regulator* and a '*twin peaks*'[6] regulatory model.

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5 The Financial System Inquiry website is at: http://fsi.treasury.gov.au/content/default.asp

6 The'twin peaks' idea and nomenclature are attributable to Michael Taylor, a former officer of the Bank of England, and a director of a course in financial services regulation at London Guildhall University in the mid 1990s. In 1995, Taylor wrote an article entitled*: 'Twin Peaks': a regulatory structure for the new century*, which was published by the Centre for the Study of Financial Innovation in London. There is no obvious link to the 1989 American TV series of the same name created by David Lynch.

Under the mega regulator model, it was envisaged that a single regulator would undertake market regulation, consumer protection and prudential regulation.

The model received some support with proponents arguing that it would create regulatory consistency, allow more in-depth supervision of diverse financial groups and diminish the scope for 'regulatory arbitrage' (ie playing off one regulator against another or exploiting gaps or 'jagged edges' of jurisdiction between the two).

Opponents were concerned that a mega regulator would have too much power and risked adopting a 'one size fits all' approach to regulation.

Under the *lead* regulator model, a single regulatory agency would take responsibility for assessing the risk profile and capital adequacy of the entire operation of a diversified group. The theory was that the lead regulator would gather and disseminate information about the financial group from and to other regulatory agencies and co-ordinate the handling of any issues or problems arising in the financial group.

The main argument in favour of the lead regulator model was that it would ensure a coordinated approach to financial groups, while retaining the specialist expertise of existing regulatory agencies.

The arguments against the model included that it could lead to fragmentation of regulatory arrangements, competition between regulators and confusion for the regulated population as a result of different objectives, styles, staff and IT systems between regulators, with flow-on effects on the wider population.

The idea behind the 'twin peaks' model was that there would be only two financial regulators, together with the central bank, the Reserve Bank of Australia (**RBA**), and the competition regulator, the Australian Competition and Consumer Commission (**ACCC**) – one responsible for prudential regulation and the other responsible for the integrity of financial markets, largely through regulation of the participants' conduct and the quality of their disclosure about the financial products traded on those markets.

The 'twin peaks' model had the advantage of creating two highly specialised agencies with clearly defined and understandable regulatory roles – in essence it created a division along functional lines.

Some arguments against the 'twin peaks' model included the potential for regulatory overlap and duplication, conflict between different regulatory perspectives and objectives and important regulatory issues to 'fall between the cracks'.

5. The birth of 'twin peaks'

Wallis considered that the optimal regulatory structure would have a single regulator capable of dealing with each of four identified facets of market failure which were:

- market misconduct;
- information asymmetry;

- anti-competitive behaviour; and
- systemic instability.[7]

However, Wallis did not ultimately favour the single agency or 'mega-regulator' model because it was thought that:

- the existing agencies, with changes to their powers and functions, will perform best with their own distinct cultures;
- at that stage in the history of our financial system and regulatory arrangements, fusion of those agencies' functions and approaches would be premature;
- a single regulator with all of these functions might become excessively powerful; and
- those functions might be too extensive to be combined in one agency with full efficiencies.

As a result, the Committee decided that the best structure for Australia at that time would involve two regulators: one responsible for prudential regulation of *any* entity that needed to be prudentially regulated; and one responsible for market and disclosure regulation of *any* financial products being offered to Australian consumers. In line with the Committee's recommendations, the Government adopted the 'twin peaks' model of financial regulation and created the Australian Securities and Investments Commission (**ASIC**) and the Australian Prudential Regulation Authority (**APRA**).

ASIC was given the power to regulate market integrity and consumer protection with the objectives of promoting market fairness and consumer confidence, while APRA was given the power to regulate asymmetric information problems by setting and enforcing standards of prudential behaviour on all institutions making promises in the areas of deposit taking, insurance and superannuation.

The Government retained the already-established Reserve Bank of Australia (**RBA**) and the Australian Competition and Consumer Commission (**ACCC**), albeit with slightly altered powers. The RBA oversees systemic stability, predominantly through its influence over monetary policy, and the ACCC regulates anti-competitive behaviour.

6. Why not combine the central bank and the prudential regulator?

The Wallis Inquiry concluded that APRA, as the prudential regulator, should be separate from the central bank, the RBA, for the following main reasons:

- The combination of deposit taking, insurance and superannuation regulation is unlikely to be carried out efficiently and flexibly by a central bank whose primary operational relationships are with banks alone and whose operational skills and culture have long been focused on banking;

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[7] The Wallis Committee considered these four factors to be the root cause of market failure.

- Separation will clarify that, while the central bank may still provide support to maintain financial stability, there is no implied or automatic guarantee of any financial institution or its promises in the event of insolvency; and
- Separation enables both the RBA and APRA to focus clearly on their primary objectives and will clarify the lines of accountability for the regulatory task.

Current thinking is therefore that the systemic stability of the financial system should remain the responsibility of the central bank.

7. About the Australian Prudential Regulation Authority

Under the 'twin peaks' model, APRA is the national regulator of prudential institutions – deposit takers, insurance companies and superannuation funds. APRA supervises financial institutions with, collectively, over US$1.65 trillion in assets.

APRA is primarily a supervisory agency and its principal aim is to ensure that financial promises made by regulated entities are met within stable, efficient and competitive financial markets. APRA does this by seeking to ensure that the quality of a financial institution's systems for identifying, measuring and managing the various risks in its business (including, for example, adequacy of capital) are sound and act to reduce the risk of failure. When failure does occur, APRA works to maintain public confidence in the financial system by helping the entity make an orderly exit from the market.

APRA's powers

APRA, which was originally established in 1988, has three main types of powers in regulating financial institutions:

- authorisation or licensing powers;
- supervision and monitoring powers; and
- powers to act in circumstances of financial difficulties to protect depositors, policy holders and superannuation fund members, including powers relating to taking control of entities and/or winding up insolvent entities.

APRA's approach to regulation

A defining moment in APRA's history was the US$3.75 billion corporate collapse of Australian insurance group, HIH, in March 2001. Following the collapse, the Government set up a Royal Commission to investigate what happened. Among a number of findings, the head of the Royal Commission, Justice Owen, recommended that APRA develop a more sceptical questioning and, where necessary, aggressive approach to prudential regulation.

Following HIH's collapse, APRA introduced a Probability and Impact Rating System, known as PAIRS, to classify regulated financial institutions in two areas:

- the probability that the institution might be unable to honour its financial promises to beneficiaries – depositors, policyholders and superannuation fund members; and
- the impact on the Australian financial system should the institution fail.

By June 2005, around 1,550 entities, accounting for over 99% of APRA-regulated assets, had been PAIRS rated and almost half of those entities had been rated more than once.

APRA now has an active program of direct contacts with supervised entities through on-site visits, consultations and tripartite meetings involving the supervised entity and its external auditor.

The Royal Commission also provided lessons about the relationship between APRA and ASIC. Justice Owen found that there were difficulties in that relationship, which arose principally because APRA and ASIC had overlapping and unclearly delineated roles in relation to financial services providers; one of the downsides of the ‘twin peaks’ model. Exacerbated by differences in regulatory philosophy, the differences of approach extended to information exchange between the regulators to such an extent that, throughout 2000, ASIC was less well informed about HIH than it should have been. These issues have largely been remedied following the enhancement of inter-agency communication arrangements, an issue I will expand on shortly.

Challenges facing APRA

Like all regulators, APRA has the challenge of keeping up with a rapidly evolving and increasingly complex financial services sector. In addition, corporate collapses often involve an element of fraud and this can be very difficult for a regulator to detect prior to the inevitable occurring, regardless of the regulatory model adopted.

Perhaps APRA’s biggest challenge, however, is public perception. Unlike ASIC, APRA largely acts as a ‘behind the scenes’ regulator and, as Dr Jeffrey Carmichael, the then Chairman of APRA observed:

> The difficulty for a prudential regulator is that it is much easier for the community to identify when you are doing a poor job than it is for them to identify when you are doing a good job. Unlike a conduct regulator, which can at least count ‘heads on pikes’, there is no ready metric for APRA’s performance.[8]

8. About the Australian Securities and Investments Commission

ASIC is Australia’s corporate, market and financial services regulator. It regulates 1.5 million corporations, 4,415 financial services businesses and 15 financial markets.

ASIC seeks to ensure that Australia’s capital and financial services markets are fair and transparent, supported by confident and informed investors and consumers.

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[8] Jeffrey Carmichael, *APRA speaks on Palmer*, APRA Media Release, 22 November 2002.

ASIC's powers

ASIC has broad-ranging powers, which include being able to:

- investigate situations where a breach of its legislation might have occurred;
- prosecute in a criminal court;
- bring a civil action;
- apply for a civil penalty order;[9]
- accept and enforce an undertaking to comply with the law;
- apply to the Takeovers Panel;[10] and
- disqualify people from managing corporations or dealing in financial services.

A regulator with many hats

As the *corporate regulator*, ASIC is responsible for ensuring that company directors and officers carry out their duties honestly, diligently and in the best interests of their companies. ASIC regulates company fundraising, takeovers and schemes of arrangement (facilitating reconstructions between companies and their members or creditors), audit and financial reporting, market disclosure, managed investment schemes, shareholder rights, company administration and windings up. It also registers all companies and ensures that information about them is available efficiently and quickly.

As the *markets* regulator, ASIC assesses, and reports on, how well authorised financial markets, including the ASX, are complying with their legal obligations to operate fair, orderly and transparent markets, and advises the Minister about authorising new markets and any changes to the rules of those markets.

As the *financial services regulator*, ASIC licenses and monitors financial services businesses to ensure that they operate efficiently, honestly and fairly. These businesses typically deal in superannuation,[11] managed funds, shares and company securities, derivatives, and insurance and give advice about those products.

ASIC has general powers to protect consumers against misleading or deceptive and unconscionable conduct affecting all financial products and services, including credit and, along with other regulators, administers aspects of legislation relating to insurance, superannuation and retirement savings accounts.

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9 A pecuniary penalty prosecuted by ASIC in a civil court that is matched to the seriousness of the breach up to a maximum of A$200,000 (US$150,000) for an individual and A$1 million (US$750,000) for a body corporate.

10 A specialist body designed to adjudicate disputes relating to takeovers and other changes of control of companies in an informal, timely and cost-effective manner.

11 Retirement savings or pensions.

A risk-based approach to regulation

ASIC's approach to regulation is largely risk-based. This means that ASIC focuses on areas that it assesses as being of the *greatest risk*, such as misconduct and non-compliance that affect consumers' decisions, threaten the reputation of our markets or undermine Australia's international reputation as a safe, well-regulated place to do business. It then decides what available regulatory tools best deal with those risks.

ASIC also aims to identify areas where *new risks* might emerge, or where existing risks could have a larger impact. To help ASIC with this task, it regularly consults with industry and consumers.

To strengthen our consultative activities, ASIC announced the establishment of a Business Consultative Panel in July this year.[12] The participants of the Panel are senior business leaders and reflect a wide cross-section of the Australian business community.

The Panel provides a forum for more effective and open dialogue between ASIC and the business community on current and emerging market issues and risks.

ASIC also has a Consumer Advisory Panel, which was established in 1998.[13] This Panel's role is to advise ASIC on current consumer protection issues and give feedback on ASIC policies and activities. The Panel advises ASIC on key consumer research and education projects.

ASIC's enforcement record

To maintain public confidence in companies, financial markets and financial services businesses, ASIC aims to act *effectively and quickly* against fraud, dishonesty and misconduct. Although a 'heads-on-pikes' measure is not entirely reflective of our ability to achieve this objective, it does provide at least one metric. In the 2005-06 financial year, ASIC had 27 criminals convicted, completed 102 civil proceedings and commenced 195 criminal, civil or administrative proceedings against 391 people or companies.

Some 43 directors were banned from managing corporations for a total of 195 years. ASIC also acted against 102 illegal fund raising schemes involving some 5,000 investors and in excess of US$590 million.

Challenges for ASIC

ASIC faces numerous challenges including:

- keeping up with a rapidly evolving and complex financial system;
- balancing business facilitation with consumer protection;

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12 Influential business leaders join ASIC's new Business Consultative Panel, ASIC Media Release, 7 July 2006.

13 For more information on the Consumer Advisory Panel see www.fido.asic.gov.au.

- keeping unscrupulous operators offering 'pie in the sky' investment schemes out of the market; and
- managing investor and community expectations – ASIC is not a 'zero failure' regulator.

9. Comparisons with Brazil's financial regulatory system

ASIC's regulatory objectives are very similar to those of the Comissão de Valores Mobiliários (**CVM**), as are our specified legislative duties and the powers afforded to each, particularly the ability to undertake administrative actions to protect investors from offenders.

There are two areas I would like to touch on briefly where differences between our systems might result in different regulatory approaches.

Disclosure

ASIC and the CVM both have a role to play in the registration of public securities offerings and publicly held companies and neither guarantees the accuracy of the information in the documents lodged, although both have established rules relating to the standards of disclosure and the presentation method.

While periodic financial reporting continues to play an important role in informing investors, both their and our expectations of companies providing updates or changes to material information have changed. Investors expect, and the law requires, any material information required to make an informed decision as to the price or value of securities is released immediately (subject to certain carve-outs). In this way, the concept of 'continuous disclosure' has become paramount in Australia.

ASIC has been active in this area in recent years taking companies to task for such things as selective briefings or delays in releasing price-sensitive information – good or bad. ASIC has also built its capacity in the area of real-time monitoring of market activity where price and volume data might indicate informational asymmetry (ie that the market does not have equal access to relevant information). Obviously, the first priority is to ensure that such information imbalances are rectified immediately in order to maintain the 'fairness' of our market. To that end, ASIC has the power to halt trading in such circumstances, but its regulatory interventions (including imposing fines or seeking significant penalties from the courts) have had an impact on how company directors approach their ongoing obligations to communicate with the marketplace.

The separation of the prudential and market conduct and disclosure regulator creates procedural issues that necessitate clear and constant communication to balance their differing regulatory objectives. However, the overlap of their remit can also raise dilemmas for the regulated population on matters of disclosure.

Take for instance a large, diversified financial service provider that is prudentially regulated by APRA. It will also likely be a publicly listed company and regulated by ASIC both as a disclosing entity and a licensed provider of financial services.

I have already noted that much of the work of APRA is conducted 'behind the scenes'. Let us assume that APRA is in serious discussions with an entity about ameliorating excessive levels of risk that potentially threaten its viability. It is understandable that APRA would want these communications to remain confidential. It is also conceivable that the directors of the company in question, having due regard to ASIC's focus on continuous disclosure obligations, might think that the discussions with the prudential regulator are required to be disclosed to the market.

Certainly there is a point where an intervention by the prudential regulator becomes information that must be shared with the market. But even a market conduct and disclosure regulator can acknowledge that release of such information prematurely can have significant implications not only for the particular entity, but also the confidence of the market generally. The point at which disclosure is necessary is not easily identifiable and will depend on the facts of the individual case. What is important here is that the 'twin peaks' model does not simply afford prudential activities a cloak of secrecy without due consideration to the role that disclosure plays in proper market functioning and investor confidence.

Supervision of market participants

My understanding of the Brazilian regulatory model is that the CVM takes some comfort from the self-regulatory practices of the marketplace and intervenes only where it forms the view that those practices are not effective.

One of the many significant recent legislative amendments that was introduced in Australia with the *Financial Services Reform Act 2001* was the removal of the official regulatory standing of self-regulatory organisations (**SROs**). SROs, whether they are exchanges, industry associations or some other form of 'peer' group, have traditionally set standards of behaviour or codes of conduct for market participants.

While there is still a role to be played by such peer groups in maintaining standards and indeed raising them, the Australian financial services licensing regime now puts the onus firmly on the individual licensee and creates a direct and ongoing link between them and ASIC as the regulator.

An Australian financial services licensee must (among other things):

- do all things necessary to ensure that the financial services covered by the licence are provided efficiently, honestly and fairly;
- ensure that its representatives are adequately trained, and are competent, to provide those financial services; and
- have available adequate resources (including financial, technological and human resources).

Interestingly, the 'twin peaks' regulatory model means that – although ASIC administers the Australian financial services licensing regime – requirements such as the latter (ie having available adequate resources) do **not** apply to entities that are also regulated by

APRA. These entities must instead comply with APRA's prudential requirements, which reduces the potential for regulatory overlap and duplication between regulators as potentially envisaged in Wallis.

10. Supervised, but self-regulated, stock exchanges (including derivatives)

The ASX, as a listed company, does not supervise itself – it is supervised by ASIC, which is the designated listing authority for oversight of ASX's own listing. Physical and procedural structures (such as 'Chinese walls' and codes of conduct) separate commercial activities from supervisory activities and quarantine supervision decision-making.

Reflecting a recognition of the need to continually improve governance and accountability, a new supervisory structure for ASX was introduced on 1 July 2006:

- The operational supervisory functions of ASX have been placed in a separate subsidiary that will oversee supervisory and enforcement operations relating to the market rules. A Chief Supervision Officer will make all supervisory decisions and report to a separate subsidiary board and not to the CEO of ASX.
- The new subsidiary company has three directors drawn from the ASX board (including the Chairman) and two external directors.

Merger of ASX and SFE

In July 2006, Sydney Futures Exchange Limited (**SFE**) and ASX merged. This resulted in the combination of Australia's primary equity and derivatives exchanges, creating a leading integrated financial markets exchange in the Asia-Pacific region.

This development is part of a very fast-moving global landscape that is challenging all financial and securities regulators, particularly in terms of the effect on supervisory structures that will, no doubt, continue to evolve.

11. Other important components of the Australian approach

Coordination between the separate financial regulators is paramount and there are several structures established specifically to facilitate an appropriate level of communication and collaboration between them.

Council of Financial Regulators

The Council of Financial Regulators is the co-ordinating body for Australia's main financial regulatory agencies: the Reserve Bank of Australia (which chairs the Council), APRA, ASIC and The Treasury.

The Council operates as an informal body in which members are able to share information and views, discuss regulatory reforms or issues where responsibilities overlap and, if the need arises, co-ordinate responses to potential threats to financial stability. The Council also has a role in advising the Government on the adequacy of

Australia's financial system architecture in light of ongoing developments. These arrangements provide a flexible, low-cost approach to co-ordination among the main financial regulatory agencies. The Council is non-statutory and has no regulatory functions separate from those of its members.

Financial Sector Advisory Council

The Government established the Financial Sector Advisory Council (**FSAC**), comprising respected experts from the private financial sector, as part of it response to Wallis. FSAC acts purely as an advisory council with no official monitoring role; it is not a statutory body.

FSAC is intended to provide advice to the Treasurer on:

- progress on implementation of new regulatory arrangements, and their effects on the financial sector and the economy;
- new and potential developments in the financial system and their policy implications;
- the cost effectiveness and relevance of the regulatory framework for the financial system;
- the compliance costs occasioned by financial regulation; and
- the international competitiveness of Australia's financial sector and how Australia could become a preferred location for financial activities in the region.

In August 2004, FSAC released a report on the outcomes of Wallis[14]. It found that Australia's financial system and its regulation are sound and compare favourably with the rest of the world. FSAC sees globalisation, convergence and technological change to be three important forces that will continue to drive the evolution of the financial system. It identifies the importance for policy development and regulatory structures to keep pace with these forces.

Regulatory Advisory Committee

The Regulatory Advisory Committee was established in 1999 to assist Axiss Australia[15] to promote the development of Australia as a centre for global financial services. Reporting to the Treasurer, it is composed of members representing ASIC, APRA, the Australian Bureau of Statistics, the ACCC, the Australian Taxation Office, the Reserve Bank of Australia, The Treasury and Axiss.

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14 Review of the Outcomes of the Financial System Inquiry 1997 – www.treasury.gov.au.

15 Axiss is a division of Australia's national inward investment agency, Invest Australia, and assists financial services companies who are considering establishing in Australia. Axiss also acts as a one-stop reference point for information on Australia's financial services industry, researching and compiling data and publishing benchmark studies on key business location determinants such as workforce, infrastructure and regulation – www.axiss.gov.au.

12. Recent developments

12.1 Deposit protection proposal

On the recommendation of the Council of Financial Regulators, the Australian Federal Treasurer, Mr Peter Costello, recently announced[16] a proposal that deposits and general insurance products owned by Australian consumers would be protected by the Government up to a ceiling of A$50,000 (US$37,500). The proposal brings Australia into line with most other countries that provide a financial safety net on the failure of financial institutions. The protection would not extend to equity-linked and other financial products, but only deposits with a financial institution and general insurance products. This is also likely to involve a levy on institutions to create the necessary liquidity to fund the protection.

12.2 Rethinking regulation

In January this year, the Federal Government released a report called *Rethinking Regulation*.[17] The aim of the Report was to revisit and consider the effectiveness of Australia's regulatory structures and, in particular, any unnecessary burden imposed on the regulated population.

The Report did not recommend any changes to the 'twin peaks' model of financial regulation saying that:

> Australia's financial and corporate sectors, and the associated regulatory structures, are highly regarded internationally. Moreover, the broad policy framework has widespread support within business and the wider community in Australia.[18]

While wholesale change was not recommended, the Report did raise issues of regulatory overlap between APRA and ASIC. One example is the obligation to notify the regulator of breaches of the law. In broad terms, APRA requires **all** breaches of prudential requirements to be reported. ASIC, on the other hand, imposes a materiality test to limit reporting to breaches that may represent a significant risk. Additional costs are imposed on regulated entities through the need to maintain separate compliance and reporting procedures applicable to each agency.

The Taskforce suggested that a materiality threshold should be introduced into the APRA requirements, and that reporting processes and timeframes should be aligned.[19]

ASIC and APRA have created a joint working group to identify and resolve issues of regulatory overlap, streamline processes and share information more effectively.

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16 24 August 2006.
17 The Report is available at: www.regulationtaskforce.gov.au.
18 *Rethinking Regulation*, Report of the Taskforce on Reducing Regulatory Burdens on Business, January 2006, p88.
19 *Ibid* p94.

13. Benefits and challenges surrounding the 'Twin Peaks' model

One of the major strengths of the Australian model is that APRA and ASIC can independently pursue their prudential and corporate regulation/consumer protection/market integrity objectives, while taking appropriate account of the other's differing perspectives.

That said, to function properly, the 'twin peaks' model requires a high degree of commitment from both agencies at Commission/Board and operational level to achieve continuing 'real time' information sharing about emerging risks and mutual concerns.

This is more of a challenge than ever given the impact of globalisation. Indeed, IOSCO says that, as a result of the increasing internationalisation of financial activities, the information required for market supervision can be beyond the reach of national regulatory authorities in particular jurisdictions. Thus, international cooperation between regulators internationally is necessary for the effective regulation of domestic markets.

Much of Australia's market conduct and disclosure regulation is affected by international issues, ranging from the activities of global financial institutions in our markets, enforcement matters involving offshore transactions, complex cross-border ownership structures and policy issues involving international regulatory standards.

14. Conclusion

For now, the 'twin peaks' model provides an excellent framework for regulating the financial system in Australia. But, as the Regulation Taskforce recently noted:

> Just as individuals and businesses need to compete successfully to achieve their goals, nations must do the same. In recent years, following wide-ranging reforms, Australia has shown how successful it can be in the international arena. However, even successful nations cannot rest on their laurels.[20]

The Australian Government and its agencies, including ASIC, are all committed to continually perfecting our model of financial regulation. This is an ongoing task and our success going forward – domestically and in the international arena – will be measured by the strength and integrity of our financial markets and by the level of confidence businesses, investors and consumers show when investing in Australia.

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[20] *Ibid* Foreword.

