



ASIC

Australian Securities & Investments Commission

REPORT 123

A Report on Costs of Financial Services 2007

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(A.B.N. 63 005 428 268)

610 Glenferrie Road
Hawthorn
Victoria 3122
Phone: 613 9819 5244
Fax: 613 9819 6270

**A REPORT ON
COSTS OF FINANCIAL
SERVICES 2007**



Project 2995

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Prepared for:

Liz Roberts

Manager, Policy & Research, Regulatory Policy Branch
Australian Securities and Investments Commission
GPO Box 9827
Sydney, NSW 2001

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1. EXECUTIVE SUMMARY

1.1 Background

This reports presents the findings from interviews conducted by Chant Link & Associates with 64 financial services organisations in November and December 2007.

The key objectives of the research were to assist ASIC to:

-] Develop its understanding of industry perceptions of and attitudes about the overall size and direction of compliance costs
-] Develop an ability to deal with information about costs and thereby inform and guide ASIC's approach to its regulatory decision-making.

This report presents the detailed findings from the research as well as conclusions and recommendations. A summary of the key findings follow:

1.2 Key Findings

1.2.1 Attitudes To Compliance

Positive to regulation: Respondents were positive to the principle of regulatory control, seeing many benefits to their own organisation and to the market in general.

Perceived benefits of regulation: The main benefits were said to be:

-] **Organisation reputation:** Complying with regulatory requirements, and being seen to comply, was an important element in maintaining a good corporate reputation;
-] **Industry standards:** The introduction of more rigorous regulatory requirements was seen to have improved industry standards overall;
-] **Market stability:** Strong regulation led to market stability and thus to market confidence;
-] **Improvement of business processes:** FSR had prompted many to improve their business processes, which were now seen to be more efficient;

-] **Providing staff development:** Staff received on going training;
-] **Improving organisational culture:** Some felt their organisations had developed a more professional and procedural driven culture as a result of regulatory requirements;
-] **Level playing field:** Because all market participants were subject to the same standards, individual organisations could not gain a competitive advantage by avoiding certain activities.

Some criticisms: There were however, some criticisms of regulatory control from three main perspectives:

-] Poor implementation of some legislation;
-] Some regulation was seen to be unnecessary;
-] The volume of regulatory requirements was difficult to manage.

1.2.2 Collecting Compliance Cost Information

Costs not known: Most respondents readily admitted to not knowing the costs of their organisations' compliance activities. The main reasons for this were:

-] The costs were integrated into the business rather than being discrete costs. The philosophy of many organisations was that compliance activities should be embedded into the everyday activities of all staff, rather than being seen as something extra that they had to do. This was the main reason why organisations were unable to accurately track their compliance costs.
-] Compliance costs varied from year to year, depending on the changes to legislation;
-] There was little perceived value in knowing the compliance costs;
-] Monitoring compliance costs would in itself incur further cost.

Some major costs identified: Most respondents could identify only a few discrete and visible compliance costs. These included:

-] Compliance staff costs (but not the compliance activities of staff not in the Compliance Department);
-] Staff training (this included the cost of training, but not of staff time to attend training, nor other associated costs);

-] External consultancy services (although costs relating specifically to compliance could not always be separated from costs for other services);
-] Implementation of major projects to meet the requirements of new legislation.

1.2.3 Compliance Costs

Compliance costs generally accepted: At one level the majority of respondents were not greatly concerned by compliance costs, because they were viewed as an integral part of doing business, and thus could not be avoided.

Compliance costs seen to be high: Notwithstanding this acceptance, and a lack of awareness of specific costs, most respondents thought compliance costs were high. This perception was based on:

-] **Visible costs:** The costs which were most visible to respondents tended to be high costs (eg, staff costs, training, IT);
-] **High profile costs:** Cost related to the implementation of specific compliance projects were often top of mind, and high cost;
-] **Specific individual costs:** Some specific costs (eg, customer communications) were regarded as too high;
-] **Low / no return on some costs:** Some compliance costs were seen to have no benefit to the organisation or to the market, and these costs in particular added to the perceived burden of compliance costs;
-] **Pervasiveness of compliance activities:** As compliance was integrated into all aspects of business operations, respondents assumed the costs had to be high;
-] **Information provided to regulators:** Respondents were aware of the amount of information they needed to provide to various regulators, both in terms of ongoing reporting, and in response to regulator requests, and understood the amount of activity (and staff time) necessary to meet these requirements.

Some provided cost estimates: Despite these difficulties, some respondents provided estimates of the total cost of compliance to their organisation. Figures cited by respondents were in nearly all cases broad estimates, based on aggregating estimates of the major cost components. This meant that **identified costs under-estimated total costs**, as not all compliance costs were included in these estimates.

Major cost components identified were:

-] **Staff costs** (compliance staff; senior management and Board, legal staff, customer facing staff, other staff);
-] **Training** (training programs, staff time in attending training, development, management and monitoring of training programs);
-] **Documentation** (researching, writing, printing and dissemination of documents, including SOAs and PDSs);
-] **IT** (new hardware and software, upgrades, integration into existing systems);
-] **Outsourcing** (legal, audit, compliance consulting);
-] **Procedures** (development and implementation throughout the organisation);
-] **Monitoring and recording** (dedicated compliance staff and input from many customer facing staff);
-] **Opportunity cost** (staff time, impeding business expansion, limiting new product development, delays in implementation of new products);

Compliance costs increasing: The majority of respondents said that compliance costs were increasing year to year, with many quoting increased costs of between 15-20% per year, although there was considerable variation around this estimate.

1.2.4 Reporting to the Board

Board reporting focused on risk management, not costs: Few respondents reported to their Board on compliance costs. Compliance related reporting to the Board tended to relate to the extent which the organisation had / had not met its regulatory obligations in the previous period. Boards were primarily concerned about whether the organisation had committed any breaches, and if so, what those breaches were, what the impact had been on the organisation, and what actions were being taken to prevent such breaches in the future.

1.2.5 Perceptions of ASIC

ASIC believed to have been effective: The majority of respondents believed that ASIC had been effective in regulating the markets.

Impact of ASIC on costs: Most respondents found it very difficult to separate out compliance costs which were due to ASIC, compliance costs which were due to other regulators, and costs which were associated with the cost of doing business.

Little impact for some: Some respondents, primarily from global organisations, commented that they would incur a large proportion of their compliance costs regardless of ASIC activities.

Substantial cost reduction for most: The majority said their compliance costs would be reduced significantly in the absence of ASIC, primarily related to:

-] Less senior management and Board member time devoted to compliance;
-] Reduced training requirements;
-] Reductions in monitoring and reporting activities;
-] Significant savings in document preparation and publication costs.

Dealing with ASIC: Many were somewhat frustrated in dealing with ASIC because:

-] They believed that ASIC did not provide sufficient guidance in interpreting legislation;
-] They felt that ASIC was too far removed from the market, and did not always understand the implications of its requests on businesses;
-] They wanted ASIC to take a more relationship based approach to dealing with individual organisations and with specific industry sectors;
-] ASIC appeared to assume malicious wrongdoing where breaches occurred.

1.2.6 Suggested Actions for ASIC

The main suggestions made by respondents which they felt would help to reduce their compliance costs were:

-] **Reduce documentation requirements (PDS, SOA, FSG):** This was the single main cause of dissatisfaction with the cost of financial markets regulation. Respondents believed that the amount of information they had to provide meant:
 - Costs were far higher than necessary (preparation time, printing and dissemination costs);
 - Customers were poorly served (many organisations had withdrawn from providing advice to consumers because it was too costly to do so; customers did not want large amounts of information).
-] **Provide market guidance:** Many felt ASIC provided insufficient guidance in terms of what organisations were required to do to comply with legislation;
-] **Consult with industry:** Many felt that ASIC should take a more consultative approach with industry;
-] **Initiate greater interaction with the market:** There was a belief that ASIC lacked understanding of the impact that compliance requirements had on individual organisations because it did not have sufficient market interaction;
-] **Account management:** Many expressed a desire for ASIC to take an account management approach, which it was felt would help develop a more co-operative mode of working;
-] **Principles based approach:** Some argued for a principles based approach to regulation, which they felt allowed organisations the flexibility to differentiate themselves in the market, while still meeting their regulatory obligations;
-] **Greater flexibility in interpretation:** Some felt that ASIC focused too much on the letter of the law rather than the spirit of the law, and thus organisations sometimes incurred unnecessary costs;
-] **Address duplication across regulators:** While this related to a number of regulators, duplication between requirements of ASIC and APRA was raised as the most common problem;

-] **Address lack of co-ordination between ASIC departments:** Some said that they could be asked for the same or similar information by several different ASIC departments, which indicated that the internal ASIC departments didn't share information.
-] **Greater consideration of information requests:** Respondents noted that it could be difficult for them to meet ASIC requests for information because:
 - **Ad hoc requests:** Some ad hoc requests were for information the organisation had not expected to provide, and the information was not in a readily retrievable format;
 - **Old information:** Old information could be difficult to retrieve quickly.

2. CONCLUSIONS & RECOMMENDATIONS

2.1 Conclusions

1. **Wide variation in defining compliance costs:** While most identified cost of compliance staff and cost of external consultants as compliance costs, there was little consistency across the total sample with respect to what other cost categories should be included in calculations of compliance costs.

2. **Almost no knowledge of total compliance costs:** None of the respondent organisations had a full picture of how much compliance activities were costing them overall, nor of the specific costs associated with ASIC related compliance. Further, most believed it was not possible to generate accurate compliance costs. There were multiple reasons for this:
 - **Compliance activities were integrated into organisational activities and systems:** This made it very difficult to disaggregate costs:
 - Across business units;
 - Across Australian regulators;
 - Across international regulators.

 - **Little perceived value in knowing costs:** Respondents saw little value in keeping a detailed account of what compliance cost their organisation since many organisations argued that they were not in a position to impact compliance costs

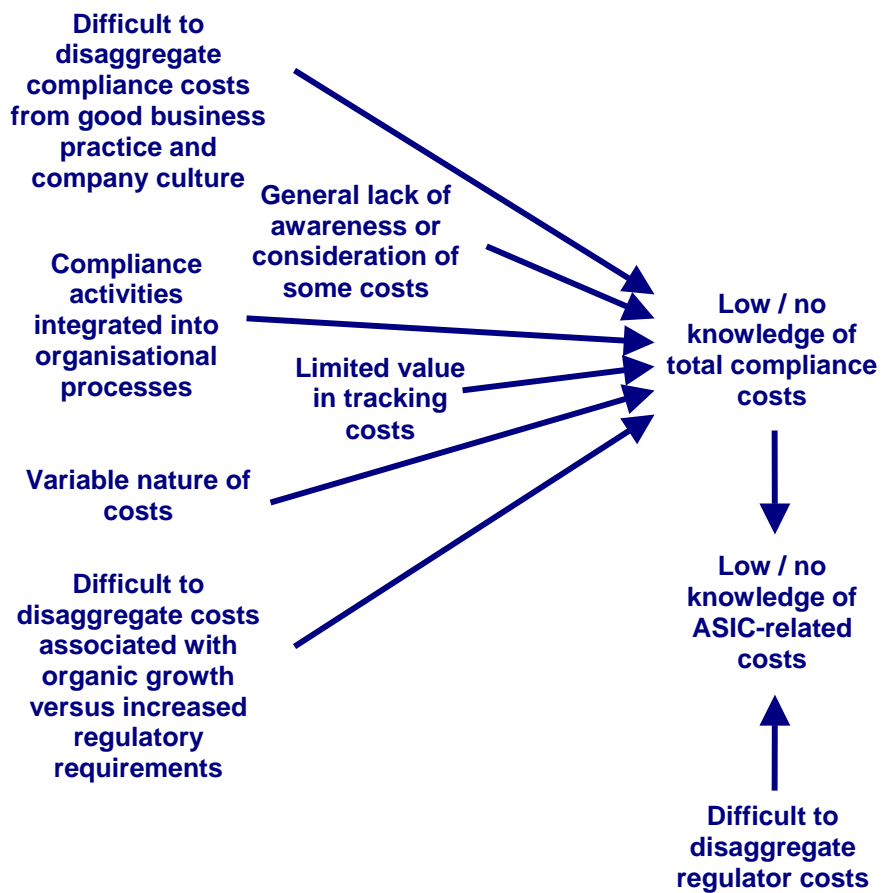
 - **Difficult to disaggregate compliance cost increases from organic business growth;**

 - **Difficult to disaggregate compliance costs from good business practice and company culture:** Many organisations said that their reputation was paramount and that adhering to 'best practice' was part of the company culture and would occur even without ASIC regulation;

- **General lack of awareness or consideration of some costs:** Some simply had not thought in detail about cost categories and only after prompting did they recognise some cost areas
- **Variable nature of costs:** Costs tended to change over time with implementation and ongoing costs changing making estimation of annualised costs difficult.

This is summarised in the following exhibit.

Exhibit 1: Factors Contributing to Low Compliance Cost Awareness



3. **Need for caution in accepting cost estimates:** Because of the lack of agreement in what constituted compliance costs, and given the great difficulty in disaggregating costs, even the estimates of those respondents who could supply compliance cost estimates should be treated with great caution.

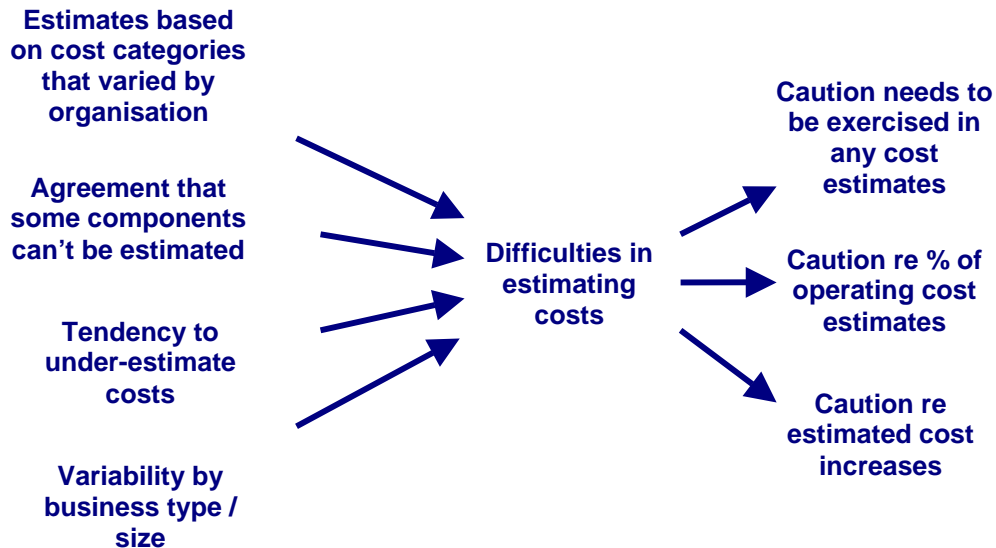
4. **Belief that compliance costs are high:** Notwithstanding their lack of knowledge of compliance costs, most respondents believed that compliance costs were high. Respondents believed compliance costs were high because:
 - **Visibility:** Some costs were high and very visible. Even where the exact costs were not known, respondents were aware that some cost components were high. This included:
 - **Staff remuneration:** Respondents had high visibility of the number of compliance staff and salaries paid. While time incurred by other staff on compliance activities was less clear, it was apparent that a considerable proportion of staff spent at least some time on compliance activities.
 - **Training costs:** Respondents typically had a good idea of actual training program costs (but other training associated costs were not known).
 - **Outsourced services:** These costs were discrete and relatively easily identifiable
 - **Major new legislation** (such as AML currently, and FSR in the past) necessitated the development of major new systems at high costs. These activities were very high profile within the organisation, and served as a reminder of high compliance costs;
 - Any **change to the organisation's systems or processes** was expensive to implement.

5. **Inability to estimate compliance costs:** As might be expected, few respondents were able to provide estimates of their total compliance costs in absolute terms or as a percentage of total operating costs. However, a small proportion of respondents provided rough estimates, which ranged between less than 1% to 10% of total operating costs.

6. **Compliance costs were under-estimated:** Although they believed that compliance costs were high, respondents comments indicated they had almost certainly under-estimated the true cost of compliance. Not all compliance costs were given consideration and this was due to:
- ❑ Some respondents believed some compliance costs were too difficult to identify and estimate;
 - ❑ Some respondents had not considered the compliance cost implications of some business activities.
7. **Compliance costs were believed to be increasing:** The majority of respondents believed that compliance costs were increasing year to year, with the most common estimate being an increase of around 10-20% per annum. Perceptions of increased costs were due to many reasons including:
- ❑ Increased costs associated with staffing;
 - ❑ Increased regulatory change, across multiple regulators (in particular, AML is currently having a major impact on perceptions of compliance costs);
 - ❑ Organic business growth;
 - ❑ Increased importance placed on risk management;

The difficulties in estimating costs are summarised in the following Exhibit:

Exhibit 2: Difficulties in Estimating Compliance Costs



8. **Concept of market regulation was well accepted:** Respondents overall were very positive towards the concept of regulation, and accepted that compliance costs were an inevitable part of doing business in the financial services sector.

9. **Some criticisms of implementation:** Despite the overall positive response to regulation, there were some criticisms in relation to:
 - Poor implementation of legislation, and lack of clear guidance re implications for compliance activity (this particularly applied to FSRA);
 - A belief that some regulation was counter productive, in that:
 - It created large costs for limited market participant benefits;
 - It did not provide consumer protection, and in fact could make it more difficult for customers to understand products and obtain advice;
 - It deterred some organisations from introducing new products or services.

10. **Caution in rapid action:** The complexity and ambiguity associated with some legislation led to many organisations taking a “wait and see” approach to compliance because of risk associated with:

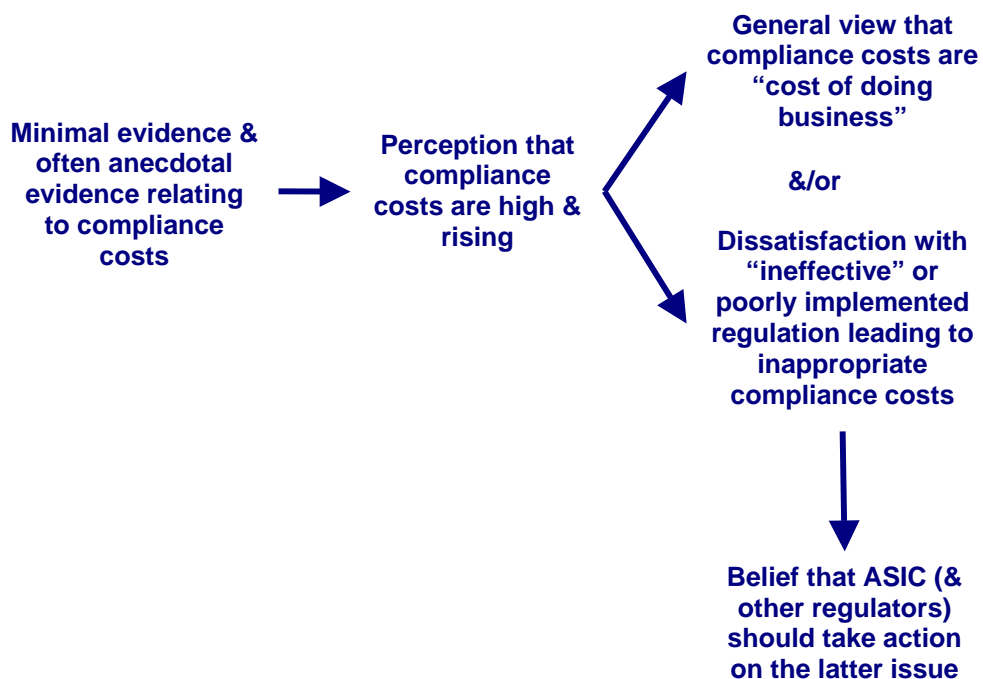
- Difficulties in interpreting legislation;
- Adopting an unnecessarily rigorous approach and therefore incurring unnecessary costs;
- Failure to adopt a sufficiently rigorous approach and thus risking non compliance.

11. **Limited collection and monitoring of costs:** Organisations in the sample tended to collect data on costs in a limited and ad hoc way. Whilst some organisations collected and reported data in areas such as consultant costs or IT costs, none were able to provide a summary of specific costs related to compliance.

2.2 Recommendations

The Exhibit below summarises the rationale leading to the following recommendations. In effect, while organisations lack information on their compliance costs, there is a view these costs were substantial and increasing. While there is a general view that this is fundamentally a cost of doing business (and indeed delivers a range of benefits), there is a strong view that ASIC (and other regulators) need to address some of the more inappropriate compliance costs.

Exhibit 3: Summary of Compliance Cost Perceptions



The above view held by the market place suggests three potential courses of action for ASIC:

1. **Educate the market on costs:** One option (that we do not recommend) would be to educate the market with respect to compliance costs. This approach would necessitate both encouraging the market to assign value to ascertaining their compliance costs and then providing organisations with a model of assessing those costs.

However this approach has a number of downsides including:

- It is likely to be very difficult for most organisations to access the information that would be required to generate a compliance cost estimate;
- Almost certainly any accurate estimate of compliance costs would generate a figure that is somewhat higher than what organisations currently believe might be the case;
- Even if organisations were able to assess their compliance costs, most organisations would find it difficult to generate value from knowing these costs.

2. **Do nothing:** Of course one option for ASIC would be to take no action at all regarding the market's knowledge of compliance costs or outcomes associated with perceptions of compliance costs. However we suggest that such an approach is likely to result in a negative reaction from stakeholders.

In effect many stakeholders are dissatisfied not so much with overall compliance costs, but with compliance costs they believe are unnecessary and little or no action from ASIC in this area.

Thus we suggest it is not an option for ASIC to take no action on this matter, and this leads to the third alternative.

3. **Develop strategies to illustrate to stakeholders that ASIC is attempting to reduce compliance costs:** This approach would aim to demonstrate to the market that ASIC is aware that a need exists to reduce the cost of compliance, especially with respect to areas where organisations are incurring costs as a result of perceived inefficiencies associated with the implementation of aspects of various regulation. Some of the areas that ASIC could address here include:

- **More effective communication:** Demonstrating to the market that ASIC has implemented approaches that would result in ASIC communicating more effectively with its stakeholders. This approach could address a range of areas including, for example, Account Management approaches, and provision of advice or opinion regarding ASIC's likely interpretation of various compliance related issues.
- **More consultation with industry (and perhaps other regulators):** There is a view that ASIC needs to consult more with stakeholders (especially industry bodies) and perhaps other regulators prior to the development and/or implementation of various regulations. Many stakeholders hold the view that some regulation could be implemented more efficiently if the views of stakeholders were sought.
- **Address current approaches that have not proved to be effective:** A substantial number of stakeholders believe some aspects of FSR are not proving effective with respect to their original objectives. A key example here is PDSs (where many argue that consumers rarely read these documents, and thus large costs occur without delivering the expected benefits).
- **Better staff contact:** There is also a view that a need exists for ASIC to provide better access to expert staff and for ASIC to manage its (high) staff turnover better. Some stakeholders argue that having to develop new relationships with new ASIC staff relatively frequently adds considerably to compliance costs.

3. INTRODUCTION

The Australian Securities and Investments Commission (ASIC) is an independent Commonwealth government body, employing approximately 1,500 full-time staff around Australia. ASIC enforces company and financial services laws to protect consumers, investors and creditors. ASIC regulates and informs the public about Australian companies, financial markets, financial services organisations and professionals who deal and advise in investments, superannuation, insurance, deposit taking and credit.

ASIC has been aware for some time that a general perception exists in the business community that costs associated with complying with ASIC's current and future regulations are unreasonably high. This awareness coupled with the recent Better Regulation initiatives has led to ASIC committing to developing and applying a methodology to more systematically analyse the impact of ASIC's regulation and proposed regulation.

ASIC comments at its web-site *"ASIC is keen to better understand the impact of its actions on the entities it regulates, and the costs incurred by business in complying with the laws it administers and the policies and guidance it issues. ASIC has examined various models of business and regulatory impact analysis, both in Australia and overseas."*

This commitment to the development and application of a methodology resulted in ASIC deciding to commission research to examine the cost impact of financial services regulation in Australia.

Accordingly, ASIC commissioned Chant Link & Associates to conduct research amongst a variety of organisations operating in the financial services marketplace. The research outcomes are the subject of this report.

4. RESEARCH OBJECTIVES

4.1 Overall Objectives

ASIC specified three overall objectives as follows:

1. Develop its understanding of:
 - Industry perceptions of and attitudes about the overall size and direction of the costs of the regime ASIC administers (e.g. perceptions about where compliance costs are increasing or decreasing);
 - What information is collected and monitored by financial service providers about the costs and impacts of ASIC's regulatory decision-making;
 - The business areas most heavily affected by compliance obligations and the cost impact of ASIC's regulatory decision-making (including overall business impact).

2. Develop an ability to deal with information about costs and thereby inform and guide ASIC's approach to its regulatory decision-making, including:
 - Conducting business impact assessments and cost-benefit analyses;
 - Drafting new policy and guidance;
 - Reviewing existing policy and guidance.

3. Deepen ASIC's understanding of organisations' perceptions of compliance costs and perceived regulatory burdens and create a factual background for further ASIC-industry dialogue on the impact of regulation on financial services businesses.

5. RESEARCH APPROACH

This research consisted of detailed face to face interviews with senior compliance personnel from a variety of organisations operating in the financial services marketplace.

Participating Organisations: The organisations included in this research were organisations that are (ultimately) members of FICA (the actual members of FICA are industry bodies, and it is their members who are the ultimate target).

FICA supplied lists of organisations and individuals who were considered appropriate to include in this research. These lists were supplemented by suggestions from:

-] **ABACUS:** Credit Unions;
-] **SDIA:** Stockbrokers and investment banks;
-] **NIBA:** Insurance brokers.

All potential respondents were first contacted by Chant Link & Associates consultants by email. This email explained the objective of the research, and attached a letter from Malcolm Rodgers, requesting assistance (this letter is included in the Appendices to this report). This initial contact was then followed up by email and/or phone. The participation rate amongst potential respondent organisations was very high, with only 10 individuals contacted refusing to participate (in most cases, these people said they were too busy at the current time to participate).

In total, 64 organisations and 90 individuals participated in this research.

The following exhibit summarises the number of organisations interviewed by industry sector and state.

Exhibit 4: Summary of Organisation Types Interviews

Industry Type	State				Total
	Vic	NSW	Qld	SA/WA/ACT	
Banking	5	10	1	1	17
Building Societies, Credit Unions		4	1	2	7
General Insurance	2	4	1		7
Insurance Brokers/ Agents organisations / International Brokers	5	5	1		11
Investment Management, Fund Managers / Wholesale		1			1
Superannuation Life Insurance Managed Investments	3	6			9
Stockbroking		1			1
Financial planning	1	2	3	2	8
Others	1	2			3
Total	17	35	7	5	64

Interviews: The majority of interviews were conducted face to face, and typically took around one hour. Interviews with participants located in Brisbane, Adelaide, Perth and regional areas were conducted using a combination of face to face and telephone interviews.

The discussion guide used is included in the Appendices to this report.

Multiple people participated in a number of the interviews. The table below shows the total number of participants by industry sector and state.

Exhibit 5: Summary of Total Number of Participants

Industry Type	State				Total
	Vic	NSW	Qld	SA/WA/ACT	
Banking	7	12	2	1	25
Building Societies, Credit Unions		5	1	2	5
General Insurance	2	5	2		9
Insurance Brokers/ Agents organisations / International Brokers	7	8	1		16
Investment Management, Fund Managers / Wholesale		1			1
Superannuation Life Insurance Managed Investments	8	11			19
Stockbroking		1			1
Financial planning	1	2	6	2	11
Others	1	2			3
Total	26	47	12	5	90

6. MAIN FINDINGS

6.1 Compliance Structures Within Organisations

There was considerable variation between organisations in the way their compliance operations were structured. The differences were largely due to organisational size, although type of business operations also affected this to some extent.

Compliance and Risk Management were typically split into two individual functions in all but the smaller organisations. Smaller organisations generally did not have staff dedicated to compliance but rather had staff who managed compliance along with a range of other responsibilities.

6.2 Attitudes to Compliance

6.2.1 What is Compliance?

Respondents' definitions of compliance were somewhat similar, although few had definitions that they appeared to have given a lot of thought to. The following are typical examples of definitions of compliance given by respondents.

"Compliance is mainly concerned with complying with regulatory authorities ... but it extends well beyond the compliance department. It involves advisory functions ... that is day to day advice concerning transactions, policies. It also involves training, position monitoring, investigations, monitoring and surveillance, control room activities and anti-money laundering issues."

"I'd define it as how a business complies with legislation issues in a way that helps the business achieve its business objectives and to add value."

"It's compliance with Government mandated issues as well as compliance with investment mandates for discrete trusts and PDSs."

"It's our involvement with any operation risk or compliance activity ... our role is to ensure we meet the businesses' promises to our customers."

Differentiation between Risk Management & Compliance: Many differentiated between risk management and compliance.

"They are really both parts of a single process. But Risk Management is evaluating the risks of business and evaluating how the risks look after the controls have been put in place. The need to answer the question is this OK? Compliance on the other hand looks at the controls and asks are they adequate to reduce the risk and do they work effectively? ... So in Compliance we ask are people following the rule book whereas in Risk Management we ask do people understand risk. Risk Management is more conceptual."

6.2.2 Overall Views Of Regulatory Controls

Positive to regulation: Overall, respondents were positive towards the principle of regulatory controls, seeing many benefits both to their own organisation and to the market in general accruing from regulation (this is discussed further in 6.2.3).

“I think that Government has to have a hand over most things – human nature is fragile and as such, you need to protect systems against weakest links. And especially in banking, the regulation needs to be harder and tighter to make people honest. I’m for regulation. Regulation gives surety to staff and stakeholders. ... If you apply the right method around regulation, you can improve your business.”

“Compliance overall has been a good thing for the industry (insurance). There used to be 1200 general brokers and that has reduced to 800 to 900. It meant that a lot of people without procedures either sold out or merged with other companies.”

Impact on reputation: Many made the point that ensuring compliance was a critical factor for their organisation, as it directly impacted on their reputation, and thus their market positioning. Indeed, some emphasised that because they were operating an intangible business, their reputation was a paramount consideration, as that in effect, was what they were offering the market. Compliance was thus seen as a fundamental cost of doing business.

“Compliance is all about protecting the reputation of the Bank.”

Compliance is critical: A number also made the point that compliance was critical in order for the organisation to maintain its license, and without its license, it did not have a business.

“We could easily lose our licence and would have to stop trading over night. This is too high a risk to take not to vigorously implement the legislation.”

“Basically if we don’t comply, we don’t have a business. Compliance is all about our licensing obligations and covers a reasonably wide area.”

Indeed, for this reason, in most organisations many compliance activities were totally integrated into the normal day to day activities of the organisation.

“We try to have compliance activities embedded in the company which is both (corporate UK requirement) and part of our strategic integrity of a customer focus.”

“Most staff now don’t even realise that they are doing compliance activities – like opening an account. It’s just part of business practice for them.”

“It is part of our culture. There are hard deadlines and consequences. ... If on an audit a staff member missed compliance on a sale then they may miss their incentive. If they were really bad then they may be dismissed.”

As will be discussed in detail later (see Section 6.3.1), this approach to compliance had a major impact on the ability of organisations to cost out the various elements of compliance, and to thus determine what compliance activities actually cost them.

Some criticism of regulatory control: Nevertheless, despite the positive response to the principles of regulatory control, there were criticisms of regulatory control by a substantial proportion of the sample for the following reasons:

-] **Poor implementation:** Many argued that while the principles of legislation were appropriate, in some cases the implementation was too effort intensive and often ineffective. In arguing this, many referred to various elements of FSR to illustrate their case.

“It gets down to the complexity of the obligations. It is the devil in the detail, that causes the problem. Generally you can’t find too many people that would argue or disagree with the conceptual approach of a piece of legislation, because there are sound reasons for doing it, it is the way that it gets implementation that is the cause of the major issue, and FSR is the perfect example of that.”

“Members have a lot of issues with compliance. Whether it is IT backup or more specific issues. In all most of it is common sense; but some of it is over the top. For example some of the requirements directed to the life insurance and planning area are not suitable for general insurance and car insurance.”

Some argued that because there was uncertainty about the interpretation of some legislation, there was a lack of fairness in the market, because organisations interpreted requirements in different ways, giving some a perceived unfair advantage. For example, one respondent from a general insurance organisation explained that problems could arise when they had to make decisions about what disclosure practices to follow. If a competitor made a different decision in this regard, they could have a competitive advantage, if they took a less conservative approach in their interpretation. They could, for example, take the view that a broker selling their product was not giving financial advice, and thus avoid disclosure and advice issues.

-] **Some regulations are unnecessary:** Some respondents felt that some regulations were unnecessary, and did not add to market standards or controls.

“I am not critical of the time we must spend on compliance. However, for general insurance, the changes due to FSRA have placed a big burden on us. It is inappropriate for us to face the same disclosure requirements as investment products. ... For example, disclosure of commission remuneration. If you take a conservative approach, you may be disadvantaged in the marketplace. Once we have made our assumptions about what the regulations require, we apply those standards of disclosure, for example, to all our products. Then we find we are in a business relationship with other parties who claim that competitors see the regulations differently and we are in a quandary. ... ASIC is not doing a poor job, it is the legislation that is poor.”

“My argument is this – if you are operating in a market for wholesale participants – then you don’t need to be regulated because you are already regulating the end user and that means duplication. ... but ASIC says we are a separate legal entity and therefore we need to be regulated.”

In relation to this point, many discussed the level of detail required in documentation, which they saw as unnecessary, and indeed confusing for many customers. This is discussed further in Section 6.2.4.

-] **The volume of requirements is difficult to keep up with:** While there were respondents from various sized organisations who raised this issue, it tended to be more of a concern amongst smaller organisations where there were relatively few resources to deal with regulatory requirements.

“Compliance is a good way of maintaining the quality in work that we do. ... but keeping up with them is just really overwhelming. ... since 2003 (FSRA), there is a constant change – just trying to keep up with what is latest in compliance is overwhelming. ... You never finish with reviewing one, when there was another change you need to know, interpret, let staff know, change and implement. ... So frustrating!”

6.2.3 Perceived Benefits of Regulation

As noted above, respondents were positive to the concept of regulation, seeing a number of benefits to both their organisation and to the market place in general.

Several respondents pointed out that the perceived benefit of regulation depended on the perspective of the individual. Thus:

“Accounting view regulatory compliance as a largely unnecessary cost; the Financial Planning division found it supported useful business practices.”

Benefits of regulation were said to be:

-] **Organisation reputation:** Complying with regulatory requirements, and being able to demonstrate to clients / potential clients that they were complying was an important element to maintaining a good corporate reputation.

“Compliance is for our benefit. It is the future. It adds to the image of the industry.”

“We tell our clients that our people are all accredited, professional, totally product trained and that we back them up with continual training and up-grading of their skills and knowledge.”

“We would adopt best practice anyway and this matches reasonably closely with ASIC needs. Overall, the cost of compliance is at is should be—after all it is other people’s money we are dealing with.”

“We do it (manage risk and compliance closely) because we are risk averse and our reputation is everything.”

-] **Industry standards:** Many felt that the introduction of more rigorous regulatory requirements had improved standards within their industry overall, thus giving the market greater confidence.

“Compliance is important. Industry wide it is necessary (to weed out cowboys), however in practice we are keen to deliver on the needs of our clients. It is part of doing business and we have to carry the costs. It has brought everyone into line.”

“The impact on clients due to the increased transparency has been positive as they are now more trusting.”

“You derive value from this – no question. Consumers are more nervous about what is going on out there and they need to know that there is someone out there taking care of them.”

-] **Market stability:** Strong regulation was seen to lead to a more stable market, again leading to market confidence.

“So protecting the consumer is about having a stable market and this obviously assists everyone. Take the example of India – there is no certainty in that market and because of that there is no investment. ... It is to our favour that ASIC regulate the market. It means the market is stable and so is the competitive environment. That is a good thing.”

-] **Improvement of business processes:** Many commented that with the introduction of FSR, they had improved their business processes and now were more efficient and had better systems in place. Some also mentioned other regulatory requirements such as Anti Money Laundry (AML) in this regard. Compliance was seen as a way of keeping policies and procedures up to date. For example, breaches had to be reported in a certain number of days and that was regarded as a good management tool.

“In certain areas the formalisation has been good for practice procedures across the industry. It has helped to get staff to toe the line. ... For the insurance industry it may have improved many of their skills and training.”

“The Australian company had a major rethink about compliance before the FSRA regulations. We needed to make a change and this was identified over 10 years ago. The introduction of the FSRA made it plain.”

“It’s taught our business how to prepare a comprehensive business plan. We did have a business plan previously, but it was not as comprehensive as what is required now. ... some of what we have now probably over-kill, but I think going through the formal process has been good for the organisation.”

“There is no doubt that as a result of the FSR we had to make a lot of changes and that meant significant costs. So, yes the costs of complying were without doubt over and above the costs of us previously doing business. But one aspect of the FSR that I think has actually improved our business practice is this area of formal agreements. Prior to that, we didn’t have any documentation anywhere that said who the authorised reps were or our agreement with them. It was all on a handshake.”

-] **Providing staff development:** Ensuring that the organisation followed regulatory requirements means that staff were protected and received on going training.

“Where compliance is exceptionally good is where it forces us to be more stringent on training. It needs to be formalised and forces up to keep up the training.”

“The legislation means we have a focus on having all staff up-to-date with the latest legislation requirements and changes.”

-] **Improving organisational culture:** Allied to the above two points, some respondents felt that their organisation had developed a more professional and procedural driven culture as a result of regulatory requirements.

For example, one insurance broker said they had decided to implement all the ASIC requirements into their New Zealand business practices because they saw the Australian regime as raising the standard of good business practice. (In addition, they believed that the NZ legislators would significantly increase the compliance regime in 2008 and as NZ had been looking closely at the Australian legislative regime, they anticipated at least some of the Australian requirements would be enforced in New Zealand.)

“We have a greater transparency about what we do and that is also a good thing. ... This greater transparency about what we do has also had a good impact on the culture. There is less finger pointing when things go wrong and more of a willingness to just get on and fix things up. So that has been great for our organisation.”

“There have been some benefits as a result of FSR, but it is a constantly moving feast and that has been difficult. ... I think it is important to say that some of the changes brought about by FSR have meant greater efficiency and transparency in what we do. So, there is an argument that the costs associated with these changes were really costs to doing better business. On the other hand, there are a lot of additional requirements as a result of FSR that I don't believe necessarily add value to the business and I would consider them to be a cost of compliance.”

“Compliance makes good business sense and fits with our culture.”

-] **Level playing field:** Many respondents felt that because all market participants were subject to the same standards, individual organisations could not gain a competitive advantage by avoiding certain activities (although as noted in the previous section, some said that this did not always in fact happen).

“It has set standards and this means quality of service. There are also prudential benefits which mean quality of capital and this does protect the ethical members of the industry. Of course regulation is important and it should mostly be there but where it becomes difficult is in the interpretation. Regulation is necessary and it does drive ‘good’ behaviour in corporations, but what we need is clarity. I go to the Board and say that I believe the regulation means this and at best all I can say is that is what ‘I think’. I can never say with absolutely certainty.”

“There is a perception that the costs of compliance have increased. This is not necessarily a bad thing. What the government and ASIC have not done is sold the community benefits (of the regulations) properly to consumers.”

6.2.4 Perceived Disadvantages Of Regulation

Respondents did not see any negatives associated with the underlying principles of regulation, but there were some criticisms of the implementation of regulation, particularly in relation to FSRA. Comments that follow refer to FSRA.

-] **FSR overly prescriptive:** Respondents from some industry sectors (credit unions, banks) argued that FSR had originally been written to protect consumers against the ‘fringe’ sector (e.g. mortgage brokers), and that the more “reputable” sectors were overly burdened by the FSR.

“I’ve always maintained that within this country, the financial services industry and particularly the authorised deposit taking institutions are exceptionally heavily regulated, whereas other sections of the financial services industry are not. ... you’ve got fringe lenders ... (mortgage brokers) ... and a lot of the FSR stuff was originally designed to try and counter the perception that there were a lot of cowboys out there. And in my personal view FSR has failed absolutely miserably, all it has done is create this massive amount of work, with almost no benefit, and the cowboys are still out there.”

“The business is better for (the regulatory regime) but I think some things are too prescriptive, and this adds enormously to costs. ... We would halve the (compliance) team, or more, if ASIC was not there, and still display good business practice and low/acceptable risk.”

-] **Excessive documentation:** Many respondents argued that documentation which complied with FSR requirements (PDS, SOAs) were far too long and detailed. This was said to have two major negative outcomes:

- **Increased costs:** In addition to these negative outcomes for the customer, many also said that the excessive documentation requirements had resulted in very large increases in compliance costs.

“SOAs are the main issue for not providing advice to client on small end of town. ... I know they’re trying to protect consumers but compliance adds additional layers of work beyond the level that we see as required. Regulation hasn’t stopped the rogues but it has put extra weight of compliance on us – it has sent our compliance costs through the roof and disadvantaged our smaller clients.”

- **Ineffective consumer protection:** Many argued that these documents worked against the intent of FSR for two primary reasons:

- Customers did not read these documents because they were not interested and regarded them as too long and complicated.

“The PDSs need to be better quality and shorter; they are not read and are an absolute waste of time. The short form PDS can’t comply to the law and no one uses them.”

“We can find ourselves issuing a 25 page statement of advice, for something that is going to cost \$480, and the client looks at it and just shakes his head, and says ‘what on earth are you doing giving me this; I’m not remotely interested!’”

- Many organisations no longer gave advice to retail customers because it was too expensive for them to do so. This meant that customers were simply given factual information, and told to make their own decision, whereas many customers wanted to obtain advice. Many argued that as a consequence, customers frequently choose inappropriate products for their situation.

“The attitude of the client is you are my broker, just tell me what I need to do.”

“If the policy is worth \$500 then the broker may get \$50. ... Brokers need to make money out of the deal. ... It has pushed the consumer to a non advice area such as the internet, whereas in the past the broker gave (the consumer) advice. This has led to under insurance being a big issue. This was evidenced during the Canberra bushfire report where many properties were underinsured. Customers had been pushed to use the Internet (for insurance). ... It has also meant the general advice is mostly given which is not tailor made for the individual.”

“We have had to undergo extensive training with our people regarding the fact that they can no longer answer customers questions – we cannot give advice. ... This impact of this on the Financial Planners has been huge because people basically go to them to get advice and they can no longer give it. The consequence of this will be far fewer Financial Planners.”

“The legislation went overboard on retail insurance for home and motor. It required a FSG (Financial Services Guide) and needs analysis and that pushed a lot of brokers out of this area. ... The average consumer now deals with a direct marketer and the loser was the consumer. Now the consumer has to do the homework themselves. While the requirement has relaxed we have not gone back to it (retail home and motor insurance).”

“We have a disclaimer that states that we have given the customer what they asked for, and that no advice has been given. This saves us lots of time and money. ... and trees! And we get them (the client) to sign an acknowledgement of this. ... The public now have to buy their retail insurance products through banks who don’t give advice either.”

“FSR is moving us toward a ‘no advice’ model because the cost of compliance in giving advice is huge. What that means is that when we speak to the customer we literally don’t give any advice – much like just stating the facts. This is a major issue and really changes the nature of our business.”

“Clients don’t read the product disclosure statements from the insurance companies. So now we are more and more giving general advice rather than statements of advice. It is easier to do. ... For individuals a full statement of advice costs \$500 on a policy of \$500 so it is not worth it.”

“The legislation pushes us to more simplified, commoditised products which aren’t in the consumer’s interests in the end. Where’s the opportunity to add value!”

-] **Staffing issues:** Some said that the advent of FSR had resulted in increased difficulty in attracting high quality staff, because staff were deterred by the high levels of paperwork and perceived low productivity.
-] **Legislation too complex:** Many respondents said that because the legislation was complex, and because ASIC did not provide sufficient guidance, they had to spend a large amount of time and money in gaining legal advice about the implications for their business.

“Some areas are overly regulated and too complex. The FSRA is very complicated and often we have to seek external advice.”

“The Corporations Act is broken. I’ve been in this game for 15 years and I’m not confident interpreting the Act.”

-] **Duplication across regulators:** Many commented that there was duplication across regulators, resulting in excessive workload. For example, different regulators often asked organisations to collect and report on very similar information, but in somewhat different ways, so that the organisations had to separately compile information for each regulator.

“We have to gain authorities in different ways for APRA, ASIC and Austrac. They are all asking a lot of the same questions.”

Summary: Attitudes To Compliance

Positive to regulation: Respondents were positive to the principle of regulatory control, seeing many benefits to their own organisation and to the market in general.

Perceived benefits of regulation: The main benefits were said to be:

-] **Organisation reputation:** Complying with regulatory requirements, and being seen to comply, was an important element in maintaining a good corporate reputation;
-] **Industry standards:** the introduction of more rigorous regulatory requirements was seen to have improved industry standards overall;
-] **Market stability:** Strong regulation led to market stability and thus to market confidence;
-] **Improvement of business processes:** FSR had prompted many to improve their business processes, which were now seen to be more efficient;
-] **Providing staff development:** Staff received on going training;
-] **Improving organisational culture:** Some felt their organisations had developed a more professional and procedural driven culture as a result of regulatory requirements;
-] **Level playing field:** Because all market participants were subject to the same standards, individual organisations could not gain a competitive advantage by avoiding certain activities.

Some criticisms: There were however, some criticisms of regulatory control from three main perspectives:

-] Poor implementation of some legislation;
-] Some regulation was seen to be unnecessary;
-] The volume of regulatory requirements was difficult to manage.

6.3 Collecting Compliance Cost Information:

6.3.1 Attitudes Toward Collecting Compliance Cost Information:

Compliance costs unknown: Most respondents readily admitted to not knowing the total costs of their organisations' compliance activities, arguing that it was too difficult to establish what the costs were. There were a number of reasons for this, as follows.

] **Costs integrated into business:** Many organisations had a philosophical view that compliance should be embedded into the everyday activities of all staff, rather than being seen as something "extra" that they had to do. This was seen to be the best way to instil a culture of compliance and to ensure that the organisation met its regulatory obligations. Respondents said that it would be very difficult to reliably collect cost information because compliance permeated all aspects of their business.

This was the main reason why organisations were unable to accurately track their compliance costs.

"Compliance is distributed across the total business. ... even if we were able to identify the components within the compliance department, we would still struggle to identify the components of compliance in other parts of the organisation where they have been embedded."

"How could you measure the compliance costs associated with the Board? The Board is the responsible entity, and while you could estimate the time spent by the compliance committee, you really can't quantify it."

"If you need telemarketing staff to mention a change in the Product when speaking with customers, you need to know how long it will take to communicate the change, and then have a means for recording the total number of calls. If the change is going to be communicated via the mail, you need the cost of communicating the change multiplied by the number of customers that will be contacted."

] **The variable nature of compliance costs:** Some respondents pointed out that compliance costs varied with the environment; e.g. AML was the cause of major current compliance costs, but previously, compliance costs had primarily been associated with FSR.

] **Little interest in determining compliance costs:** In addition to the difficulty of establishing costs, the majority of respondents were of the view that there was little value in collecting detailed compliance cost information. This was for several reasons:

- **No utility:** Many argued that they had no choice but to comply with regulatory requirements, and as such, knowing the specific costs involved had no value to them, as they could do nothing to change the costs.

“There’s no value in estimating compliance costs. ... I’m not sure what we would do with the information. Although some people do talk about needing to estimate the cost benefits of new regulatory issues ... but I can’t see us ever trying to seriously estimate these costs.”

- **Additional cost:** Many pointed out that in order to track compliance costs they would have to set up new monitoring systems, which would incur further expense for no return.

“Monitoring costs would be futile. We have to comply to be in business so to go to the bother of capturing all that information would simply be an exercise for interest sake – it wouldn’t alter the fact that we have to do it and the process of recording it would be substantial.”

“It would be a huge project to address (estimating compliance costs) ... you’d need all the direct costs, but the whole business is involved ... and I’m not sure what we’d do with the information anyway.”

Some exceptions: There were a few exceptions to this, but only a few.

For example, one respondent said he was currently working on trying to establish compliance costs because:

“I think it is important from the point of looking for better efficiency in what we do. We need to understand what doesn’t add value to our business and then assess from a direct cost and opportunity cost point of view. Perhaps we could be eliminating some steps in some processes which may mean that we need fewer staff.”

However, in this case the focus was on direct costs of compliance as these were easily identified and measured with respect to Product Disclosure Statements. The specific costs that he intended to identify with respect to Product Disclosure Statements related to:

-] **Documentation:** Costs and time to modify existing Statements or develop new statements, and cost of distribution (mail);
-] **Training:** Training of employees and authorised representatives regarding changes to Product Disclosure Statements;
-] **Monitoring:** Ensuring compliance to regulatory requirements with respect to changes to Product Disclosure Statements. This included ensuring sales representatives and telephone conversations noted the appropriate changes to the Product Disclosure Statement when speaking with customers.

A respondent from another organisation said that they were part way through this process. This organisation had a strong focus on costs, with costs attributed as far as possible to cost centres within the organisation.

“We have Compliance Cost Centres and Risk Management Cost Centres and we know exactly what the clear identifiable costs are with these centres. So, remuneration of our people and their associated costs, study costs and the cost of external consultants. ... We are starting to track the work of governance because this plays a part in compliance, risk management and legal. ... In 12 months we will be able to say what it costs to undertake specific projects – but at the moments we can only tabulate costs associated with specific cost centres. So down the track we would be able to tell you how much it cost us to modify a Product Disclosure Statement for example.”

The CFO from another organisation said he had “toyed” with trying to allocate compliance costs to a specific cost centre, but “it all got too hard” to apportion compliance and non-compliance cost components, and he couldn’t see the real benefit in the end for all this effort.

A respondent in another organisation said he had once suggested a project to the Board to define, track and monitor costs of compliance. However the Board rejected this idea because it decided that there were other more beneficial projects that the organisation could apply its resources to, to bring in more revenue rather than track specific costs.

6.3.2 Monitoring Of Compliance Costs

As is evident from the above discussion, few organisations had a clear understanding of what their total compliance costs were. Most organisations collected only very limited compliance cost information.

With the exception of Compliance Department, it was very rare for other areas or business units within organisations to have a budget for compliance. Compliance activities were in most cases subsumed under normal business operations costs. In many cases, this was a deliberate philosophy, because management wanted compliance activities to be fully integrated into their day to day operations.

“So much of compliance stuff is integrated into what we do. ... if staff don’t differentiate between business and compliance then that is the best situation for us.”

“We don’t necessarily look at activities as a cost because that is simply what we do to be in business. ... At a global level they would be watching to see that our departmental costs (ie compliance) don’t become excessive – but they can’t be isolated easily because of the way we do business. ... You have to remember that compliance is the single most important requirement for our business. It we don’t have the business practices that we do, then we don’t have a business.”

“We tend to embed this activity (and related costs) in the business processes to ensure we get it right. That is, it must be owned by the businesses and find its way into all the processes. It is better to do it there. A side effect is that the cost of it (compliance) is hard to isolate.”

“We collect cost information but it is hard to show any value and we can’t influence this anyway.”

Respondents had a much clearer understanding of costs which could be classified as discrete items than of other costs.

Specific discrete costs which some respondents could identify included:

] **Compliance staff costs:** Because most organisations had staff dedicated to dealing with compliance, the remuneration costs associated with those staff was often allocated to a specific cost centre, and respondents therefore had a very good view of what these specific costs were. However, a number of respondents pointed out that the only components of these costs identified and tracked were salary and associated costs such as superannuation, Workcover and so on. Associated costs such as office space and equipment were generally included in organisational overheads, rather than attributed specifically to compliance.

Many respondents commented that because there is a shortage of compliance staff, salaries had been rapidly increasing and the total salary cost for compliance staff had therefore risen substantially in recent years.

Further, many pointed out that the only staff costs attributed to compliance were those associated specifically with compliance staff. Staff costs associated with other staff, such as internal legal services, and general staff work involved in undertaking compliance activities were typically not measured.

“Most of what I do is clearly directed at a quite unique element of a particular piece of legislation ... whereas a lot of the day to day activities of the staff following a policy or procedure are there specifically to ensure that we meet our obligations under some form of legislation, code of conduct or whatever. So you’ll find that a lot of staff won’t appreciate that they are undertaking an activity that’s strictly there as a compliance control or obligation.”

Thus in terms of monitoring costs, for non compliance staff it was often hard to determine:

- Which activities were compliance related (because they might also be standard business practice anyway);
- How much time was spent on compliance versus other activities;
- Which code or piece of legislation the activities were related to.

] **Staff training:** Many organisations tracked costs associated with compliance training because it represented a discrete cost which could be directly attributable to compliance.

“The cost of training new authorised reps and establishing and monitoring their agreements. This is a new requirement and whilst I think it has been a good improvement to our business practice, it has been very costly in terms of time.”

However, it should be noted that not all organisations monitored training costs as it related to compliance, because compliance training could be integrated into other staff training. Further, where training costs were monitored, this typically included only the cost of delivering the training; it did not take into account the time of the staff members being trained.

] **External consultants:** The majority of organisations were aware of the specific costs they had incurred in using external consultants because they often represented a discrete cost which could be directly attributable to compliance. The consultants most frequently identified were:

- Legal advice in relation to new legislation;
- Ongoing legal advice;

- Audit;
- Compliance consultant, typically used by smaller organisations.

However, costs specifically relating to compliance were not identified by all respondents. For example, legal costs were not always specifically divided into compliance issues and other legal matters; accountancy services were not always divided into compliance issues and others.

Specific project costs: In addition to the above, many respondents said they could identify the costs associated with specific projects, which were often tracked quite carefully because:

-] They represented large one off costs;
-] Because of the costs involved, they typically represented an additional budget expense item that had to be approved by the Board;
-] Many of the associated costs could be clearly allocated to the project, with specialist teams typically set up to manage the project. For example, one banking respondent said that a specific project team set up each time new legislation was released. The team was required to review the new legislation and with the assistance and professional advice of external experts, decide what part of the legislation was appropriate to this business, and how it would be integrated into its daily business practices.
-] Reporting to the Board on the project progress to time and budget was usually required.

“This kind of expenditure is managed as part of an identified management of change project, it is budgeted, measured and monitored. This is not only because of the large expenditure involved, but also, crucially, because the projects must deliver reliable compliance on time.”

These specific projects were developed in order to implement processes associated with new compliance requirements. It is noteworthy that once the implementation phases of a project had been completed, in nearly all cases the ongoing management of such systems and processes were subsumed into the ongoing organisational operating costs, and were not tracked as a compliance costs on an ongoing basis.

Respondents discussed a number of different projects in relation to this point, and were aware that not all project costs they discussed were specific to ASIC. Nevertheless, a number of specific legislative changes were identified as indicative of the types of compliance costs incurred.

Anti Money Laundering: Many respondents discussed the cost of Anti Money Laundering legislation as this was a top of mind cost, because organisations were currently working through the requirements of this legislation (managed by Australian Transaction Reports and Analysis Centre [Austrac]). This represented a large cost because it involved:

-] Dedicated staff to manage and work on the project;
-] Legal consulting fees obtaining opinions on how the legislation applied to the organisation, and assisting the organisation to determine what it needed to do to comply with the legislation;
-] IT costs for new systems.

“We are running the Anti-Money Laundering project at present (from the Compliance Department). There are major costs in system changes (hardware, software and people costs), people to run the project, and development of training material.”

Financial Services Reform (FSR): Specific project work most relevant to ASIC was of course FSR. This had constituted a major cost for most respondent organisations, with many saying that this had been the single biggest cost to compliance for their business:

“There’s probably two reasons for that. Given that we are in the business of insurance and retail, there is no greater obligation on businesses than when you are talking disclosure. ... I also think the costs to implement the changes for FSR were significantly greater because of the huge number of changes that were made along the way – and continue to be made. This is very costly. I can give you an example. We might have something before Treasury on which we are waiting for a response. We start to look at resources in terms of how we are going to implement the change once it has been approved by Treasury and then another change is made – which makes the work that has been done in terms of resource useless.”

It should be noted that many respondents said implementation costs of FSR had declined in recent years (although, as noted below, ongoing costs were often thought to be increasing).

Summary: Collecting Compliance Cost Information

Costs not known: Most respondents readily admitted to not knowing the costs of their organisations' compliance activities. The main reasons for this were:

-] The costs were integrated into the business rather than being discrete costs. The philosophy of many organisations was that compliance activities should be embedded into the everyday activities of all staff, rather than being seen as something extra that they had to do. This was the main reason why organisations were unable to accurately track their compliance costs.
-] Compliance costs varied from year to year, depending on the changes to legislation;
-] There was little perceived value in knowing compliance costs;
-] Monitoring compliance costs would in itself incur further cost.

Some major costs identified: Most respondents could identify discrete and visible compliance costs. These included:

-] Compliance staff costs (but not the compliance activities of staff not in the Compliance Department, nor other associated costs);
-] Staff training (this included the cost of training, but not of staff time to attend training);
-] External consultancy services (although costs relating specifically to compliance could not always be separated from costs for other services);
-] Implementation of major projects to meet the requirements of new legislation.

6.4 Compliance Costs

6.4.1 Attitudes to Compliance Costs

Costs generally accepted: At one level, the majority of respondents were not greatly concerned by compliance costs because they were viewed primarily as an integral part of doing business, and could not be avoided.

Respondents tended to regard compliance costs as acceptable for a variety of reasons, as follows:

-] **Benefits of regulation:** All respondents saw benefits of regulation both to their own organisation and the market overall, and accepted that as participants in the market, they would inevitably incur compliance costs.

“Compliance is very good for your business. If you apply the right mindset, then it can be really beneficial.”

-] **Reputation:** As noted previously, organisations in the financial services sector are primarily operating intangible businesses where their reputation is paramount. Any compliance cost incurred in maintaining this reputation were therefore viewed as an essential business cost.

“Our (the Compliance Department’s) whole purpose is to mitigate risks – and we will pay whatever it takes to do this.”

-] **Best practice:** Activities required to ensure compliance were often seen as activities that the organisation would undertake in any case as they presented best practice. Thus, these costs were not directly attributed to compliance.

“It would be very difficult for me to say what the costs were because so much of what we do was set up a long time ago and is part of our best business practice. There are a few things that have happened as a result of regulation – but nothing unreasonable or out of the ordinary.”

Some of the global organisations commented that their Head Office had implemented procedures that met or exceeded what was necessary to meet Australian regulatory requirements, and thus relatively little cost had been incurred in meeting new legislative requirements within Australia.

“Our global parent often sends out, via the international compliance group, modules on various issues. We were already prepared for AML because it had already been done globally.”

Costs seen to be high: Notwithstanding a general acceptance of compliance costs, and a lack of awareness of what the specific costs were, most respondents thought compliance costs were high. This was based on:

-] **Visible costs:** The costs which were most visible to respondents tended to be high costs. Thus, when they thought about compliance costs, the costs they first considered were those which were known to be high. These costs, which are discussed in detail in section 6.4.4, included staff costs, training, and IT.
-] **High profile costs:** Costs related to the implementation of specific projects were often high profile, and tended to be top of mind. Thus, many respondents discussed costs associated with the Anti Money Laundering Act (AML) because although this was not regulated by ASIC, they were currently going through the process of dealing with this. In relation to ASIC, respondents discussed the cost of implementation of the Financial Services Reform Act (FSRA) (see Section 6.4.2 for further discussion).
-] **Specific individual costs regarded as too high:** Further, many respondents were able to identify specific costs relating to compliance which they regarded as too high and were able to identify specific issues which resulted in compliance costs being higher than they felt were necessary.
-] **Low / no return on costs:** Some costs associated with compliance were seen to have no benefit to the organisation and / or consumers and these costs in particular added to the perceived burden of compliance costs.

“I resent the increased compliance costs. If I felt it had increased consumer protection or improved our processes I would be more accepting, but PDSs are now unreadable.”

-] **Pervasiveness of compliance activities:** As noted previously, many respondents said that compliance was integrated into all aspects of their business operations. Given this, they assumed that cost had to be high.

“We are so highly regulated that compliance has to be part of everything ... that means you can’t tease it out. So it’s impossible to come up with a divisible cost. Over 50% of total business costs are probably associated with compliance. ... most of what finance and administration does has to be associated with compliance. ... compliance costs are also a major part of OH&S and employment and other things. If you took apart all of the costs of our business, there is little doubt that compliance would account for around 50%.”

“We don’t have a real figure (for compliance costs), but it would be in the millions ... everyone in the business is doing some sort of compliance checking.”

] Information provided to regulators: Respondents were aware of the amount of information they needed to provide to various regulators, both in terms of ongoing reporting, and in response to regulator requests, and understood the amount of activity (and staff time) necessary to meet these requirements.

Greater impact on smaller organisations: In general, smaller companies tended to be less positive about the cost of regulation than larger companies because it tended to have a proportionally greater impact on smaller companies.

“Generally the costs (of compliance) are similar to the costs of a large organisation which is four times the size, so it hurts the mid to small sized companies.”

“This ongoing and ever-changing compliance regime just distracts us (i.e. senior management) from having our hands on the levers of our business. We are forced to spend more and more time on process than on outcomes.”

For this reason, many small organisations tended to rely quite heavily on their industry bodies such as Abacus (Association of Building Societies and Credit Unions) and NIBA (National Insurance Brokers Association), and on affiliated groups such as cluster groups, to assist them in interpreting new legislation and managing their compliance.

“I can’t see how you could go through compliance without a cluster group. You can bounce ideas off them and they are a great help.”

One small insurance broker, previously established in New Zealand, said it cost around \$155,000 in compliance costs to establish their business in Australia. These costs were broken up as follows:

-] \$70,000 for its licence costs;
-] \$22,000 for an internal auditor;
-] \$18,000 to certify that their New Zealand complied with Australian accounting standards;
-] \$30,000 in legal costs to obtain their Australian licences and all the bookwork that went with their applications;
-] \$2,000 in printing costs;
-] \$5,000 to employ a compliance company to maintain its compliance documentation;
-] \$8,000 in compliance related training.

6.4.2 Specific Project Costs

As noted above, respondents often had a fairly good idea of costs associated with specific projects because they represented large one off costs which were tracked and monitored while in progress.

One major bank for example, estimated that in the past three or four years, FSR, Basel 2, Sarbanes-Oxley Act and AML would have cost \$400 million or \$100 million per annum. A major issue and driver of cost was that the business could not always calculate or foresee what might become a blocking point in installing new compliance processes to meet new regulations. Where this occurred, they then needed to duplicate capacity in their systems and this was expensive and time consuming.

“Such system blockages caused by new regulation can cause you to rewrite the system specifications mid-project, with high resulting costs and sometimes, with downtime.”

Financial Services Reform (FSR): This had represented a major cost for organisations because the changes required in the way most organisations operated were extensive. In addition, there had been a great deal of uncertainty when FSR was first implemented about how it should be interpreted and implemented, and thus uncertainty had resulted in significant costs in staff time and consultancy services.

“For us this meant a lot of work which included training most of our staff on processes that hadn’t existed previously. We also had to build new capabilities and new compliance routines.”

“Even now there is uncertainty about what some aspects of the regulation mean for our business.”

“FSR has been the biggest cost and ASIC have even re-released various regulatory guides where the meaning had been obscure.”

“I think FSR is just a fixed cost of business. The implementation project was huge but even now there is work to be done with it.”

Respondents said the complexity of the Act was a major contributor to the extra costs, because:

-] Guidance notes were open to interpretation;
-] The FSRA (and ASIC) did not always provide “*practical and meaningful guidelines*”;
-] There was uncertainty about the FSRA requirements, and fear of negative ASIC sanctions if mistakes were made.

As noted previously, although respondents typically said these costs were tracked, most could give only estimates of implementation costs. Nevertheless, the following provides examples of cited costs for FSR implementation.

Estimated costs to implement FSR were as follows:

-] One general insurance company estimated a cost of \$5m to implement FSR.
-] One respondent from another general insurance company initially estimated that it had cost them in the vicinity of \$2m to implement FSR (including the cost of bringing compliance up to date). When questioned on this given that implementation has been occurring for the period 2001 – 2007 (inclusive) the respondent revised the estimate to \$10m.

“At the time the FSR changes were being made we estimated that it cost between \$17 and \$20 million per annum. These were project costs and included changes to documentation as well as training of FSR. It didn’t include IT and admin costs in the business units. ... We started making the changes with FSR in October 2001 and the changes continued until mid 2004. There wasn’t much work in the first phase but most of the work happened in 2003 because we had to re-train the authorised reps and this meant changing policy documents as well.”

Key components of the FSRA that accounted for the majority of the expense for this organisation were:

- The need to reappoint every authorised agent (as a component of the establishment of formal agreements);
 - Training of every authorised agent;
 - Creation of training courses;
 - Ongoing obligation in terms of personal advice, which was regarded as being very time consuming and therefore costly;
 - Ensuring that every product disclosure statement was registered with ASIC;
 - Reconciliation demands, where the organisation had to fulfil registration obligations within five days, which necessitated the use of express post envelopes, which was very costly on a large scale.
-] One bank estimated that costs to its IT systems as a result of FSRA had been in the vicinity of several hundred thousand dollars. Coupled with staffing costs (e.g. Secretariat staff and corporate steering committee) external consultants and legal advice, and documentation updates, the overall implementation cost was estimated to be millions.
-] A small insurance broker said they had spent \$10,000 at implementation on consultancy;
-] A stockbroker said implementation of FSR cost them \$7m;
-] A respondent from a credit union said implementation of FSR cost them \$60,000;
-] One respondent could not estimate costs of FSR implementation, but said:
“When FSR was introduced we spent days, weeks and months sitting with lawyers here and trying to understand what we needed to do. I hate to think the amount of money that we would have spent at that time. So there was the cost of lawyers, my time and also extensive discussion with ASIC. ... ASIC didn’t really know either so it was a big learning curve for everyone.”

6.4.3 Overall Ongoing Compliance Costs

Respondents had great difficulty in identifying the overall cost of compliance, and particularly costs as they related to ASIC. This was for a number of reasons:

-] **Definition of what was included under the compliance umbrella.** Respondents varied quite widely in what specific activities they included under compliance. Some took a quite narrow perspective, and considered only direct and visible costs such as staff and training. Others took a much broader view, and attributed a wider range of costs to compliance.
-] **Integrated into business activities:** As noted previously, many organisations had integrated compliance into all their operations, and they could not therefore disaggregate compliance costs from operational costs.
-] **Cost related to various regulators:** The majority of respondents who could give an indication of compliance costs could not separate these costs by regulator, although a few provided estimates.

Some provided estimates: Despite these difficulties, some respondents provided estimates of the total cost of compliance to their organisation. It should be noted that the figures cited by respondents were in nearly all cases broad estimates, based on aggregating estimates of the major costs components. This meant that **identified costs under-estimated total costs**, as not all compliance costs were included in these estimates.

Variable estimates of compliance costs: Estimates of compliance costs provided by individual respondents were as follows. It will be seen that there was very wide variation in estimates due to the above factors, and to the varying sizes of the organisations taking part in the research.

Banking: The majority of banking respondents were able to give broad estimates of overall compliance costs, although some did this in terms of a percentage of operating costs, and some in dollar terms. Estimates were:

-] One respondent estimated that across the total bank compliance costs would be around 10% of operating costs. However, the respondent noted that costs varied widely depending on which business unit was being considered. Retail banking, as the most regulated business, had the highest costs, and it was estimated that these could be as high as 30% of operating costs.
-] One respondent from a global bank estimated compliance costs at less than 1% of operating costs.

“The total cost of all legal and compliance functions for the Group is about 1.3% of the Banks operating expenses. Compliance accounts for about half of that so we would be costing about 0.65%.” (worldwide, not just Australia).

-] One respondent estimated compliance cost at about \$10m, 60% of which was attributed to compliance related to ASIC requirements. (The other 40% was said to be primarily related to loan contracts and collections, required by the ACCC consumer credit related code of Banking Practice, Austrac, and Privacy Legislation/Privacy Commissioner information.) Much of the ASIC associated costs were related to retail banking, particularly the disclosure documents for consumers. Licensing matters were also a major cost driver.
-] One respondent estimated compliance costs in 2007 to be around \$10m, which represented approximately 1.5% of turnover. This was said to be a significant increase from a few years previously, with the increase due in part to acquisitions and in part to an increase in compliance requirements.

-] Several guessed compliance costs at between 5-10% of operating costs

Some estimated costs based on assessing the cost of compliance staff only:

-] One estimated \$700,000 in staff costs (this included only direct compliance and legal staff).
-] One estimated \$5m in staffing costs for the compliance department.
-] One estimated \$15m in staff costs for direct compliance staff. In addition, unspecified costs were incurred for external lawyers and consultants, and for compliance activities carried out by other staff as part of their day to day role.

Some simply said to was too difficult to estimate costs.

“It’s hard, if not impossible to quantify, since a lot of compliance work is tied up with daily business.”

Financial planning: These organisations were quite variable in how much information they held about compliance costs. As can be seen below, a few had detailed calculations (although they did not cover all costs), while others could provide only a broad estimate, or no estimate at all.

] Ongoing costs for a large financial planner were estimated at \$7.4m per annum. Within that figure, the annual cost of the Compliance Department (staffing cost) was \$2.4m. Around 80% of this was said to be directly related to compliance costs across all Australian authorities. This organisation had standard cost allocations for senior management on (all) compliance issues which were:

- COO – 3 days a month;
- MD – 2 days a month;
- CEO – 2 days a month.

They noted that any additional compliance activities that came up during the month were not additionally costed.

“We had an ASIC audit this year, but this did not change our compliance cost allocations.”

In addition, this organisation allocated portions of time of its key staff (including Training & Development Managers and Internal Auditors) to compliance issues. In addition, it made an allocation of specific costs to compliance, such as an apportionment of processing costs and part of the cost of communications to the network.

In addition, other costs were said to be:

- Professional Development and Training: 1,400 advisors x \$200 per course x five courses a year. Allocating 50% of that cost to compliance requirements equated to \$700,000 million per annum.
- Compliance Audits: 1,400 X two hours each x three a year X \$200 an hour (for auditor and advisor to be involved) = \$1.7 million (not including travel time and disruption to business flow);
- Board, Senior Management & State Managers Time: 460 days at around \$5,000 a day equated to \$2.3 million;

Other ongoing costs which were not separately allocated to compliance, but which were deemed to be significant were:

- IT: Cost unknown but thought to be very large;
- Production, printing & distribution of client materials: This included forms, booklets, SOAs, PDSs etc., and the cost of destroying old stock and printing new stock when changes were issued;

- Communication costs of advising the advisor network and all staff of compliance updates. In reality, the time it took staff and advisors to read and absorb the compliance communication, and take action on it if necessary should be included in cost calculations (but was not);
 - Opportunity Cost: This was a subject that was discussed at Board level, but there had been agreement that it could not be calculated.
-] A small financial planner calculated their compliance costs to be in excess of \$830,000, as follows (based on all compliance, not just ASIC related compliance):
- Compliance Consultant (based on most recent requirements): \$120,000+ per annum;
 - Additional legal work required for one-off new legislative releases: \$100,000;
 - Time to create and produce each new PDS was estimated at \$25,000 each by four per year (\$100,000) plus legal costs to review the documents before release. Every three years they had a “major rewrite” of the PDS, so staff and legal costs on these occasions would increase (although this was not wholly compliance related);
 - Planners time to produce SOAs: The respondents estimated that each planner could produce five SOAs a week by five planners by six hours per SOA. This equated to around \$500,000 per annum (based on 150 hours a week by \$68.50 an hour by 48 weeks);
 - External audit: Around \$10,000 per annum;
 - Printed material: Writing, design, printing, distribution were included here, but cost were unknown;
 - Executive time was large, but could not be reliably calculated;
 - Directors Fees, for time involved in the Compliance Committee;
 - IT changes: These were numerous, as required by a range of regulators (these were primarily attributed to APRA and ATO rather than ASIC);
 - Opportunity cost: While this was thought to be significant, they did not know how to calculate it.
-] A small organisation identified compliance related costs of around \$70,000 per annum (this equated to approximately 5% of its operating cost). This was based on the following calculations:

- Remuneration \$20,000 (compliance manager only; other staff would spend an additional total of 7-10 hours per week, but were not costed for);
 - Training cost of \$20,000 (this did not include staff time while being trained, totalling 270 hours);
 - Preparing FSGs and SOAs (additional information that would not be included if not required by ASIC) was costed at \$8,000 per annum;
 - External audit \$6,500 per annum;
 - Legal advice varied considerably from year to year, depending on specific issues (estimated at anywhere between \$1,000-\$10,000 per annum);
 - Software \$8,000-\$12,000 per annum.
-] A respondent from a large financial planning organisation estimated compliance costs of \$100,000-\$150,000 per year, but admitted he was very uncertain of the costs because there was no specific tracking of any compliance costs.
-] A medium size financial planning organisation estimated 1-1.5% of operating costs.
-] A small financial planning organisation estimated costs were approximately \$250,000 per year, which as said to equate to around 10% of the overall operating costs.

Superannuation, Life insurance and Managed Investments

-] One respondent thought that compliance cost his organisation about \$10 million per annum which equated to around 2% of operating costs. He further estimated that around \$400,000 of this \$10m could be attributed to specific compliance costs which were over and above what they would do as their normal business practice.
-] Another respondent said the cost of implementing FSR to date would exceed \$4 million. The biggest ticket item in this was external legal costs to interpret the legislation. This respondent said that the organisation had initiated a project around six months before the legislation was released so it had time to consider and plan what actions it was going to take, and that this cost it a considerable amount of money. He then noted that many smaller organisations did nothing until much closer to the implementation deadline, and by that time a number of changes to the legislation had been made to simplify or clarify it, as requested by the big organisations that were already considering these issues.

As a result, he concluded that had they waited to start implementation until much later, they would not have not incurred such heavy up-front costs.

Indeed, several respondents from large organisations made this point.

“In hindsight, we should have waited a while after the FSR was introduced. But we got right onto it and tried to work out what we had to do and quite frankly it was a big learning curve for everybody. ... We were penalised for being an early adopter in terms of the time and money it cost us.”

General Insurance

-] One organisation estimated compliance costs of around 5% of operating costs, which equated to around \$100,000 per year.
-] A large insurer estimated that the direct costs of the compliance department were \$3 to \$4 million per annum. This was attributed primarily to retail type products and excluded the costs of large projects.
-] A large insurer estimated that annual compliance costs were less than 1% of operating costs.
-] Another large insurer estimated total compliance costs of up to 10% of total expenses.

“My guess is that the direct costs for the Compliance Team are about 1.5% of the total expense cost but this could increase to anything up to 10% if you included all components of the business that fall under the compliance umbrella. We don’t have all those costs itemised and accounted for at this stage and for that reason it is just a guess. The 1.5% is factual – those are the Cost Centres that are attributed to compliance but the difference on top of that is pure guesswork.”

Insurance Brokers

-] Two small brokers estimated that the compliance costs they could readily identify cost them around 5% of their operating costs, while other compliance costs (which were more hidden) were thought to probably account for around another 5% of operating costs.
-] One respondent noted that a survey of National Insurance Brokers on the cost of compliance indicated the following range of costs:
 - 21% paid \$11,000 to \$15,000;

- 40% paid \$16,000 to \$30,000;
- 20% paid \$31,000 to \$45,000;
- 2% paid \$46,000 to \$70,000;
- 14% paid \$71,000 to \$100,000;
- 3% paid more than \$100,000.

However, it is not known what cost elements were included in these estimates.

Credit Unions

-] One credit union respondent estimated a cost of \$320,00 for meeting compliance requirements of both ASIC and APRA (with an estimated breakdown of 55% of costs due to meeting APRA requirements, and 45% due to meeting ASIC requirements). This equated to around 10% of total operating cost, but included only staffing, audit and external consultancy services.
-] One respondent estimated compliance costs related to ASIC of \$25,000 per annum.
-] One larger credit union estimated total compliance costs of around \$9m per annum.
-] One larger credit union respondent estimated that implementation of FSR had cost them \$1.5m. Further, the respondent estimated ongoing costs of around \$200,000 per annum in ongoing costs to comply with ASIC guidelines. This was said to represent less than 2% of the company's total operating costs.

6.4.4 Major Cost Components

As noted above, respondents were more likely to be aware of stand alone costs. However, it must be remembered that it was often very difficult for respondents to separate costs of individual activities because they were not viewed as discrete elements. Respondents gave many examples of where costs merged together, making it extremely difficult to allocate costs to specific cost categories.

Examples of this included:

-] Staff costs often merged into other areas. Thus, while staff in some organisations spent considerable time on monitoring activities, this was typically viewed as a staffing cost, and was not attributed specifically to a monitoring cost.

-] A number of respondents said their compliance staff used their database system to track staff training and to monitor other activities such as breach reporting and this therefore impacted on IT costs.

It should also be noted that in discussions, respondents were first asked to identify major cost categories unprompted, and were then prompted with a detailed list of potential costs (this list was developed from information provided by FICA, and is included in the Appendices to this report).

Compliance costs under-estimated: When shown this list, all respondents said that all or most categories did in fact apply to their organisation, but they did not directly attribute many of these costs to compliance when they were considering overall compliance costs. Thus, we conclude that when estimating compliance costs, organisations under-estimated the true cost to their organisation.

Notwithstanding the above points, when asked to identify major cost components relating to compliance, the following were identified, in approximate order of cost impacts.

-] **Staff costs:** When thinking about staffing costs, most respondents considered only remuneration costs, as there were relatively readily definable. A number pointed out that their estimates of costs did not include the true cost of staffing, as it did not include factors such as office space, office furniture, and IT equipment and support. Respondents typically divided staff costs into a minimum of compliance staff and other, and in some cases, divided staff into a number of different categories, as follows:

- **Compliance and risk management staff:** The cost of these staff was identified by virtually all respondents as a specific compliance cost, and many had a good idea of what these costs were. Many commented that these costs were very high and increasing, as compliance and risk management staff were in short supply and salaries were therefore increasing.

“In the last five years a whole layer of management has been introduced in risk and compliance.”

- **Senior management and board:** While the majority of respondents acknowledged this as a cost, most were unable to specify what these costs were, or how much time these people spent on compliance issues. Nevertheless, many felt that a large amount of time and therefore cost was involved.

“The Board and senior management time spend a huge amount of time on compliance issues because of the risk to the business of not complying.”

- **Legal staff:** The larger organisations all had legal staff who spent a proportion of their time on compliance. However, in most cases, respondents were unable to specify or how much time legal staff spent on compliance issues. Smaller organisations were more likely to outsource this function and therefore had a better idea of costs.
 - **Customer-facing staff:** The amount of time spent by customer facing staff on compliance issues was said to be considerable, but because compliance activities were integrated in the job function, no respondents were able to provide more than a rough estimate of how much time was involved or what the cost was. Organisations with large proportions of customer-facing staff regarded this as a high cost because these staff undertook compliance activities in many of their dealings with customers, and also had to undergo training each year.
 - **Other staff:** All or most staff in the respondent organisations typically had some involvement in compliance activities, but respondents were unable to estimate how much time was involved or what the cost was. Some made rough estimates of cost based on head count by approximate number of hours involved compliance activities.
-] **Training:** Training was identified as a major cost, particularly for organisations with a large proportion of customer facing staff, such as banks, insurance brokers and financial planners. One bank respondent said that their training had a budget of between \$4 million and \$5 million per annum, and estimated that around 80% of this was related to FSRA compliance issues.

A credit union put their training cost at around \$1m per annum.

Factors contributing to training costs included:

- Senior management had to keep up to date with FSRA requirements, what this meant for their procedures, and what implications it had for training;
- External consultants had to be hired to consult on legislative requirements and to conduct external audits.
- Resources had to be allocated to conduct and attend training.

A number of respondents said they believed each organisation should be able to undertake in house staff training, rather than all staff being required to undergo PS 146 as provided by external registered training organisations, because external courses were seen to be much more expensive internal training programs.

Virtually all respondents identified two sub components to training costs.

- **The training programs themselves.** Where the training was outsourced, the cost was clearly delineated. Where training was managed in house, the training costs themselves were sometimes known, but more often were not.
- **Staff time:** While very few calculated the cost of staff time in undertaking training, it was known by many to be a large cost, because they knew the number of staff and the numbers of hours per staff involved in the training. This included both initial training of new staff, and ongoing training of all staff.

For example, insurance brokers said that all their brokers had to undertake a minimum of 20 hours training per annum in order to maintain their licence. One broker estimated a cost of \$1,500 per broker per year for training related to PS 146, and with 75 brokers, this totalled \$112,500 per annum.

One small financial planner estimated their training costs at \$30,000 per annum, although they also indicated that most of this training would be done regardless of regulatory requirements, as part of a good business practice

Other cost elements of training which were considered by a smaller number of respondents were:

- **Management of training programs:** Some included aspects here such as keeping up with legislative changes so the organisation was aware of training requirements, identification of specific training needs within the organisation, and development of training programs and/or identification of appropriate external trainers. Some noted that time devoted to understanding the legislation and its impact on various areas, including training requirements was complicated by the varying requirements of different regulators (such as APRA, ABA, Austrac and ASIC).

“We have a part time employee for 2 days a week to check and arrange our training and that costs us \$70,000 per year.”

- **Monitoring:** Some included here the development and maintenance of recording systems identifying the specific training undertaken by each staff member.

One respondent noted that it was a licensing requirement by ASIC for training to be provided or at least signed off by an accredited trainer. Thus, even if the organisation provided in house training, it had to pay for an accrediter to signoff on the training. This was said to cost over \$400 per staff member.

-] **Documentation:** This included the costs associated with Statements of Advice (SOA) and Product Disclosure Statements (PDS). Cost included researching and writing documents, printing, and dissemination.

“The PDS adds 10-15 minutes to the time required to open each account. Any changes to the process require all the documentation to be updated, which is very time consuming and expensive.”

Version control was also said to be difficult by organisations with dispersed networks. Organisations with retail businesses regarded these costs as very large. Several organisations included the cost of subscriptions used to keep the compliance officers up to date in this category.

As discussed previously, costs associated with document preparation drew a great deal of criticism and were regarded as unreasonably large.

“Printing costs are massive ... it’s not cheap to print ... and nobody reads them, but we’ve got an obligation to print them.”

Credit unions varied in their estimates of costs, based on their size. Thus, a small credit union estimated \$430,000 per annum, a medium size credit union estimated \$100,000 per annum, and a large credit union estimated \$200,000 per annum.

An issue associated with document production was the requirement to retain many documents for 7 years, which was regarded as unreasonable, and expensive. AML was now going to require some additional documents to be kept for 5 years. This requirement resulted in a significant storage costs for organisations such as banks and credit union.

-] **IT:** Estimates of IT costs related to compliance varied widely. This depended to a large extent on whether the organisation required new systems or upgrades (hardware and/or software) in order to manage its compliance, or whether it could use its existing systems to do this. Many of the larger organisations said that every time a new major piece of legislation such as AML and FSR was introduced, it necessitated the development of expensive new systems. Further, there was typically additional cost involved because the new systems had to be integrated into their existing IT architecture.

“I can’t think an example of any piece of legislation or code of conduct ... that doesn’t have a systems implication.”

“When a change to legislation is made there is usually a reporting or documentation implication which means a further change to the automated process for implementing the new requirements.”

“Although we don’t record costs associated with compliance and costs associated with improving our business practices separately, the IT costs for accommodating and implementing all compliance requirements (including ASIC) are huge! ... I’d guess that about 60% - 70% of all our IT costs are compliance-related.”

However, many noted that while IT cost were driven by compliance requirements, the organisation also derived significant benefits in its day to day operations from the IT changes.

“We’re in the process of developing a new electronic platform and this is primarily because ASIC only allows three days to report a breach or a complaint. ... there are benefits to us as well because it means it will minimise our paperwork and improve our turnaround time.”

One respondent from a medium sized credit union said the organisation had spent \$350,000 over three years on IT hardware and software, in order to comply with corporations law. However, in further discussion the respondents indicated that not all of this amount would be attributed to ASIC, and further, a large part of this cost was simply part of the cost of running a business.

A respondent from another credit union indicated that the business had invested in extensive hardware and software systems, in order to meet its compliance obligations. However, the respondent suggested that even if there was no compliance, the business would still have proceeded with implementing the majority of its systems. The respondent estimated that of total costs (\$70-\$80,000pa), costs related to compliance would account for between 10-15%.

“If we didn’t have ASIC regulations, we would still do a lot of this as part of our normal business practice.”

] **Outsourcing:** The extent to which organisations outsourced various compliance related activities varied widely. Many small organisations outsourced most activities as they did not have the resources internally to manage them. Where activities were outsourced, organisations were likely to have a good idea of the costs involved, and these costs were thus very visible to the organisation. Outsourced activities including the following:

- **Training:** This has been discussed above.
- **Legal:** For many, this was of particular concern as their legal costs in obtaining interpretations of the legislative requirements were very high and unnecessarily large.

“We need an interpretation because it (the legislation) is not drafted clearly, and is not prescriptive. There are lots of fine grey areas that need to be interpreted.”

One credit union estimated that at least 10% of all its legal costs were compliance related.

- **Audit:** Respondents saw this as an important activity, and thus in general, the costs associated with this were accepted as part of good business practice. Typical examples of costs mentioned included:

- One small financial planner said the organisation was audited twice a year by an external compliance group to confirm that the business was on the ‘right track’ with compliance. This cost approximately \$4,000 per annum. In addition, the business was subject to a corporate compliance auditor which cost approximately \$2,500 per annum.
- Another small financial planner said their auditor was also the company’s accountant as well, and therefore, the respondent was not sure what this audit cost. The estimate was around \$3,000 - \$5,000 per year.
- A large financial planning organisation said they regularly undertook field audits of their advisors. Each audit took around two hours each.

“With 1400 advisors, these field audits cost us a lot of money and take up a lot of our time.”

- A credit union said they had an internal audit each year by one of the major accounting firms, and this cost company approximately \$10,000 per annum.

- One respondent pointed out that audits were often carried out for regulatory reasons that were beyond ASIC's scope (e.g. AML, privacy legislation), and that this also contributed to overall costs.
- A respondent from an insurance company noted that because ASIC had not issued a benchmark for audits, there was wide variation in how they were conducted, and they cost anything from \$5000 to \$20,000.
- **Compliance consultants:** Smaller organisations which did not have an internal compliance team typically used compliance consultants to assist them in ensuring they met all their regulatory obligations.

"These days you cannot run a business without a compliance consultant and that is to make sure you are not breaking the law."

For example, a respondent from a small financial planner said that they had external consultants review compliance issues and audit the company's licence once a year. The consultant would set up an electronic diary which would remind staff of activities they were required to do. The consultant would also review the company's files to ensure that ASIC guidelines were met properly and further they would answer any questions/issues that the respondents may have. In addition to the respondents' time in preparation, this cost the organisation around \$8,500 per year. In addition, this organisation had an annual audit by a separate consultant as a check (separate from their formal audit). In addition to the respondents' time, this cost an additional \$8,000-\$10,000 per year.

-] **Monitoring and recording:** Again, the majority of respondents did not raise this unprompted as a compliance cost. However, some said it was one of the largest areas of cost, as it required dedicated compliance staff and input from many customer-facing staff.

"Staff at the branches have to collate the information and then it needs to be reviewed. Compliance at branch level would be 15% of staff time, where most staff are paid \$70,000 to \$100,000, and the random audits require more of their time. ... The compliance officer allocates about 10% of his time to this and he is paid \$225,000."

“Staff fill in weekly time and activity sheets in the Employee Risk System Reporting and that takes a lot of time and training and follow-up to ensure the correct and complete information is given. ... Information staff document includes complaints, breaches, time sheets, submission of ASIC forms, any ASIC late fees paid, record of training undertaken.”

-] **Policy and procedures:** The majority of respondents did not raise this unprompted as a compliance cost, although upon prompting there was general acknowledgment that it was indeed a cost.

“Once the change is understood in terms of its requirements and what that means for the business, it then has to be communicated throughout the organisation taking into account the processes previously adopted. This has huge implications for not only our employees but also authorised representatives.”

-] **Opportunity cost:** Some respondents raised this unprompted as a major cost for their organisation. Some did not spontaneously mention it, but most agreed when prompted that it was a significant cost, albeit one that they found very difficult to quantify. Major opportunity costs identified were as follows:

- **Staff time:** In most cases, the most significant opportunity cost was seen to be the time staff spent on compliance issues, which meant they weren't addressing other areas of the business.

“If we were not regulated, then we would be more industry focussed rather than compliance focussed. At the moment we are trying to balance shareholder interest and regulatory requirements. ... For example, if someone says at a Board meeting, let's do this – the reality is that our interests are not perfectly aligned with shareholders. It might be a good idea but because of our split focus in terms of compliance, innovation may be stifled.”

“An incredible amount of time has been spent by our Compliance Department over the course of many years ensuring that we complied with the FSR. ... If we hadn't been implementing the FSR, we would have been doing other things like perhaps looking at the way we present information or product disclosure statements and saying - could we do that another way? ... While you are spending so much time on complying, you aren't looking at better ways to do business.”

Several banking respondents noted that the business people in the bank talked about opportunity cost of compliance activities and obligations, but that the compliance department did not really consider this because they were more focused on the direct costs of compliance.

Many could not identify any specific opportunity cost beyond staff time, while some thought cost extended beyond this. A few mentioned quite specific instances of opportunity cost, as follows:

- **Impeding business expansion:** One respondent from a financial planner said that the size of compliance costs affected the company's desire to grow the business.

"I don't want to set up another office because it would be too hard to see if they are going the right thing."

- **Limiting new product development:** An example given was the difficulty of establishing a Christmas Club Savings account, which was a relatively straightforward bank account designed to encourage customers to save for Christmas, but which had had to be treated as a separate financial product for FSRA reasons (thus requiring training, amendments to the FSG and a PDS).

Another credit union respondent said that some new services or products had not been progressed past the pre feasibility stage as a result of potential compliance overheads. This was attributed to a lack of clarity in the legislation, which meant they were not sure how new products would be treated, and they judged it as too expensive to obtain legal advice to determine this.

One respondent from a credit union said:

"FSR has had a real impact on our culture ... it stifles innovation because of the complexity of understanding how compliance applies to innovative services or products."

A respondent from a superannuation organisation said the business calculated a return on investment on individual products taking into account major costs caused by regulatory requirements, and as a result, it had ceased product lines in the past, because they would have no longer been profitable. It had also made significant business decisions such as to provide no advice in general insurance, rather than carry the costs of implementing the compliance legislation.

A bank respondent said of the cost of compliance:

“It makes the business more conservative as we have to think (deeply) before developing products. We need to understand the risks. ... It has stopped us entering the reverse mortgage business as there was too much angst (associated with setting it up).”

- **Delays in implementation:** A bank respondent said that compliance requirements resulted in delays to branches being opened, because all staff needed to be trained in order to meet licensing obligations.

“There have been a number of proposed products in the past, which had not been progressed past pre feasibility, because of compliance issues. A lot of this is to do with a lack of clarity surrounding the Act.”

“An opportunity cost is the significant delays in launching new products because the PDS has to be drafted, we have to get legal advice and have it all checked off before release. ... bigger organisations had a competitive edge in this area because of their economies of scale.”

- **Lack of adequate systems:** Some viewed opportunity costs in terms of the costs of not installing adequate compliance and risk management systems for new products, so costs were then incurred for remedial actions against breaches.

“These are often new product related. A manual process is often the way they kick off. This usually results in breaches and associated costs. Product Managers often don’t see that spending up front will save costs, or they are under time and Capex cost pressures during the launch phase, so they feel they have to have manual systems at first. ... Sometimes these new product related temporary (often manual) compliance systems costs are enormous.”

- **No significant opportunity costs:** A minority of respondents did not believe that regulatory requirements had resulted in opportunity cost.

“All new business opportunities are looked at by us for risk assessment. This includes regulatory risks. There are no examples in the last few years where a new initiative has been torpedoed on regulatory issues.”

-]
- **Permissions and authorisations:** Several respondents noted that a lot of documentation and therefore compliance staff time was involved in removing individuals as Responsible Officers.

-] **Breach reporting and surveillance:** In this respondents included the cost in staff time in accommodating ASIC surveillance visits and regularly providing information to ASIC and other regulators.

A bank noted that breach rectification cost could be very significant, and gave the example of writing to one million customers about a breach at a cost of around \$1m.

-] **Insurance:** A small number of organisations said that the complexity of FSRA had resulted in an increase in professional indemnity insurance. This was particularly raised by insurance broking and financial planning respondents.

-] **Licensing fees:** A small number of respondents mentioned payment of licences (Australian Financial Services Licences and APRA) as a compliance cost. A few respondents included the cost of training and /or audits within the cost of licensing.

Licensing and training were said to be particularly expensive for the life insurance business. The organisation paid a fee to a Licence Provider, who was supposed to ensure that the life insurance business remained licensed and complied with the regulations. However, this was very expensive, and appeared to provide little value (e.g. the respondents also had to contribute significant time to managing this side of the business).

6.4.5 Overall Size and Direction of Costs

The majority of respondents said that compliance costs were increasing year to year, with many quoting increased costs of between 15-20% per year, although there was considerable variation around this estimate.

“Our compliance costs have probably doubled in the last two or three years ... and this is primarily due to staff increases and having to support a range of regulatory projects. In recent years this has included FSR, Super Safety, AML ... which will cost many millions, and a raft of smaller projects.”

“I’m not sure. ... perhaps compliance costs have increased by 10% to 15% per annum ... it tends to go in waves. Compounded it’s probably 150% over seven years. The major contributors to these increases are PDS preparation, AML ... which is very big, getting FSR and the Managed Investments Act.”

“Compliance costs are going up all the time ... if you look at direct costs via our budgets it has gone up 30% to 40% over the last three to four. But I suspect we are now at a high water mark. After AML it might level off a bit, and maybe some regulations will be removed with the new Government.”

“Our costs increase by about 20% per annum ... but a lot of it is due to general growth in this company ... but we are not really sure as we simply don't track it ... and why would we? What benefits would accrue?”

“About 15% per annum is a reasonable estimate ... but it could be more. In fact when you spread it across all the regulators – both Australia and overseas – it's probably more like 30%.”

“Our legal team has doubled in size, entirely due to ASIC related issues, in the last three or four years.”

“Five years ago we had one lawyer and an assistant, now we have six, all directly related to the complexity of the financial services regime.”

Some respondents forecast that ongoing compliance costs will continue to increase but that one-off regulatory changes will reduce because they could not foresee any additional major legislation changes that would introduce a range of new costs, with the possible exception of new environmental compliance issues.

Amongst those who thought costs were increasing, there was fairly widespread agreement that compliance costs were becoming greater due to the following issues:

] Increased costs associated with staffing: Individual organisations need larger numbers of compliance staff to manage their compliance obligations. Some for example, said their compliance staff had increased from 25% to 50% (or more) in the last few years, and attributed this directly to new regulatory environments, (e.g. currently Austrac). This meant there was significant competition for compliance staff in the marketplace, which is placing upward pressure on salary packages. Some also noted that compliance staff are paid more than previously because the complexity of compliance has risen and therefore more senior people are devoted to the role than previously.

“On average about 15% per annum. ... a lot of it is to do with trying to obtain specialised compliance officers. ... we are finding we have to pay more and more, remuneration levels are really increasing. The increased costs are going up exponentially. ... and this reflects the increase in overall head counts in our compliance area.”

“The cost of compliance itself is not going up but the cost of salaries is. There are not enough qualified people in the industry so finding suitable staff is a problem.”

“I can't hire people in compliance now who don't have a law degree.”

-] **Increased regulatory change:** As noted above, more and larger regulatory change resulted in increased costs. Although FSR was a large part of this, not all this change was related to ASIC; for example, many raised Austrac and the Privacy Legislation in this context. Other changes mentioned included 2005 changes to the General Insurance Code of Practice and the Simple Super reforms.

“AML ... it’s a huge cost ... it’s all compliance ... and it doesn’t really help our customers, it’s only a Government requirement. ... \$50 million to \$70 million is quoted by the main banks for implementation of AML, and for us it’s likely to be about \$5 million.”

“Overall the costs have increased by 10% each year as there is more and more regulation. Every time ASIC makes a change it costs money and time to evaluate the significance of it.”

“APRA regulation everybody had to re-license. We had to apply for our license but we had to give proof that we were complying. This meant a lot of work and in some cases we had to develop the processes to demonstrate that we were complying with the regulations.”

“There is an increasing cost related to compliance as it all gets bigger and the officers responsible have to spend more time on it. The fixed costs are much the same but it takes more staff time. We may need to involve the outside consultant more often.”

A few respondents also noted that while some changes had been made to FSR to try to reduce the costs of compliance, these changes had increased costs in the short term as organisations had to change their systems and processes again in response to these changes.

“While I understand the sentiment of trying to ease the regulatory burden, tinkering at the edges is only creating more of a headache. ..you’ve got to determine what the new legislative requirements are, design the changes, implement them, reprint the documents.”

-] **Increased training requirements:** Some noted that a greater proportion and number of staff now have to undergo training than previously, and the training now takes longer to deliver because there is a greater volume of it.

“Training sessions are now three hours long when a few years ago they were 90 minutes. The difference is the extra training required under FSRA.”

] **Increased disclosure requirements:**

“Providing customers with service now requires more disclosure. They must be given a PDS, so now they must get three documents for a simple product that may have involved one document a few years ago.”

] **Regulatory problems in the market:** Allied to the above point, some noted that regulatory requirements tended to increase after a serious problem within the industry. Some said, for example, that the Westpoint collapse had resulted in a significant increase in costs.

Organisational growth attributed to increased costs: Some respondents attributed increased compliance costs to organic growth of the organisation overall rather than an increase in compliance costs per se.

Some felt compliance costs were levelling / declining: In contrast to the above majority view, a small number said that compliance costs were levelling or decreasing because implementation of FSR had been completed. (Note that while all agreed implementation costs had decreased, the majority felt that ongoing costs were increasing year on year.)

“Costs had increased year on year since 2000. There was a substantial increase in costs to implement the Privacy Legislation and GST, it then plateaued in 2002 and rose again in 2003. Cost have remained fairly constant since 2003, although they are significantly higher than pre 2000.”

“The costs of complying are going down. Initially after FSR 2002, we had huge costs just trying to work out what we had to do and what we didn't have to do – but the software has been developed now and it is all up and running.”

Summary: Compliance Costs

Compliance costs generally accepted: At one level the majority of respondents were not greatly concerned by compliance costs, because they were viewed as an integral part of doing business, and thus could not be avoided.

Compliance costs seen to be high: Notwithstanding this acceptance, and a lack of awareness of specific costs, most respondents thought compliance costs were high. This perception was based on:

-] **Visible costs:** The costs which were most visible to respondents tended to be high costs (eg, staff costs, training, IT);
-] **High profile costs:** Cost related to the implementation of specific compliance projects were often top of mind, and high cost;
-] **Specific individual costs:** Some specific costs (eg, customer communications) were regarded as too high;
-] **Low / no return on some costs:** Some compliance costs were seen to have no benefit to the organisation or to the market, and these costs in particular added to the perceived burden of compliance costs;
-] **Pervasiveness of compliance activities:** As compliance was integrated into all aspects of business operations, respondents assumed the costs had to be high;
-] **Information provided to regulators:** Respondents were aware of the amount of information they needed to provide to various regulators, both in terms of ongoing reporting, and in response to regulator requests, and understood the amount of activity (and staff time) necessary to meet these requirements.

Some provided cost estimates: Despite these difficulties, some respondents provided estimates of the total cost of compliance to their organisation. Figures cited by respondents were in nearly all cases broad estimates, based on aggregating estimates of the major cost components. This meant that **identified costs underestimated total costs**, as not all compliance costs were included in these estimates.

Summary: Compliance Costs (cont.)

Major cost components identified were:

-] **Staff costs** (compliance staff; senior management and Board, legal staff, customer facing staff, other staff);
-] **Training** (training programs, staff time in attending training, development, management and monitoring of training programs);
-] **Documentation** (researching, writing, printing and dissemination of documents, including SOAs and PDSs);
-] **IT** (new hardware and software, upgrades, integration into existing systems);
-] **Outsourcing** (legal, audit, compliance consulting);
-] **Procedures** (development and implementation throughout the organisation);
-] **Monitoring and recording** (dedicated compliance staff and input from many customer facing staff);
-] **Opportunity cost** (staff time, impeding business expansion, limiting new product development, delays in implementation of new products);

Compliance costs increasing: The majority of respondents said that compliance costs were increasing year to year, with many quoting increased costs of between 15-20% per year, although there was considerable variation around this estimate.

6.5 Reporting to the Board

In organisations which took part in this research, adherence to compliance requirements was closely tracked. However, this tracking focused on whether regulatory obligations were met, rather than on the costs of compliance.

“Each business unit has key metrics they have to attain. This information is sent to the Compliance Review Council which meet every month. The Managing Director and his direct reports receive a report every second month. The Compliance Review Council report to the Board every quarter on the key compliance risk (by exception) as well passing on the minutes of the compliance review meetings.”

Risk management: In most organisations, the Board focus was on risk management, in terms of identifying and addressing any risks. Thus, compliance related reporting to the Board tended to relate to the extent which the organisation had / had not met its regulatory obligations in the previous period. Boards were concerned about whether the organisation had committed any breaches, and if so, what those breaches were, what the impact had been on the organisation, and what actions were being taken to prevent such breaches in the future.

Few respondents reported to their Board on compliance costs. Where this was done, the reporting tended to relate to readily identifiable direct costs, which was most likely related to the costs of specific projects, such as the implementation of a new IT system, or a project addressing some specific new legislation such as AML.

“One-off costs associated with major regulatory changes (eg Basel 2 or AML) is collected by the accountants, and reported up to the Board from a governance process via Project Managers.”

In most cases, the Board had a risk management or a compliance sub committee which was responsible for addressing compliance issues. Examples included the following:

-] An insurance broker said their compliance committee, consisting of the company Chairman, a director, the financial controller and another senior employee, met four times a year just prior a Board meeting. The compliance committee then reported to the Board. This reporting was mostly by exception, if there was a problem or if there was an activity of interest.

-] Another insurance broker said their Board had an Audit and Risk Management sub committee whose charter was to ensure that an effective internal control framework existed within the business. This included such issues as business process, safeguarding of assets, maintenance of proper accounting records, the reliability of financial information, benchmarking of key performance indicators, and compliance issues. The Board delegated its responsibility to this sub-committee for establishing and maintaining a framework of internal control and ethical standards.
-] An international insurance broker had a system where the Executive Management Group reported on a monthly basis to the Board about compliance activities, including a training report, breaches and complaints. This report was based on compliance reports prepared weekly by the Compliance Management Group, who were responsible for managing monitoring, risk management, breaches, complaints, legislative updates and training requirements.
-] A respondent from a large financial planning organisation said that a compliance report was presented to quarterly Board meetings and bimonthly executive meetings. In addition, the Board had a Compliance Review Sub- Committee which met regularly on a monthly basis, and more often when required.

“The threat of a loss of its Practice Licence is a very powerful argument with the Board. We don’t want to be out of business.”

-] A respondent from a small financial planning organisation said that senior management formed the company’s Board of Advice (five people; three of whom were also members of Board of Directors). The Board would spend approximately one hour a month discussing compliance issues, including reviewing any documents that were changing; and discussing any new requirements / legislation.

-] In banking organisations there were multiple boards for each major business. Compliance issues were reported at regular intervals, but the length of the interval varied depending on the business; for example, the Retail Banking board typically received compliance reports more frequently than say, the Asset Finance Board.

“We have regulatory issues that we need to report on at a Board level – but that is not on costs. The Board are concerned with regulatory breaches and where there has been a cost for that – but not in terms of the overall cost to comply.”

One banking respondent noted that their Board has an Audit & Risk Sub-Committee of five Members that met eight times a year. The Compliance department regularly reported back to the Board on the progress – both activity and budget – of any one-off projects for the implementation of any new or changed legislation.

-] A respondent from a superannuation fund said that ASIC had “a huge influence” in the industry.

“Our Board often asks what ASIC’s view would be and they will divert resources accordingly.”

In this organisation, a Board sub-committee had been set up to manage the issue of Privacy across the business. This was because the Board considered non-compliance of Privacy Legislation such a risk to the business that it warranted setting up a micro-Board to deal with this issue, rather than leaving this to line managers to deal with. In addition, Licence Compliance Committees met quarterly and on an ad hoc basis as required.

-] A respondent from a stockbroker organisation said that the Risk committee met weekly looking at new products and transaction. Compliance committee meets monthly looking at new policies, training, and monitors activities. Operation risk and audit committee meets quarterly and sets and reviews schedule for compliance activity. Risk committee and operational risk and audit committee report to monthly board meeting

However, some respondents indicated that a major Board issue is the need for Board members to be familiar with *legislation* (related to legislation managed by ASIC and other regulators). In the past, senior management had been held responsible and accountable, whereas this had now shifted to Directors, who were held responsible for compliance and any issues in breach of compliance.

Summary: Reporting to the Board

Board reporting focused on risk management, not costs: Few respondents reported to their Board on compliance costs. Compliance related reporting to the Board tended to relate to the extent which the organisation had / had not met its regulatory obligations in the previous period. Boards were primarily concerned about whether the organisation had committed any breaches, and if so, what those breaches were, what the impact had been on the organisation, and what actions were being taken to prevent such breaches in the future.

6.6 Perceptions of ASIC

6.6.1 Impact Of ASIC On The Market

ASIC believed to have been effective: The majority of respondents believed that ASIC had been effective in regulating the markets.

Minority believed ASIC was ineffective: A small number of respondents felt that ASIC had not been effective in its regulation of the markets. Westpoint was the case most often mentioned by these respondents, as they believed that ASIC should have intervened much earlier than it did.

“Compliance doesn’t work. We still have (companies like) Westpoint cropping up. ASIC needs the biggest kick in the backside that they allowed it to occur. There is a litany of serious warnings to Westpoint.The purpose of compliance is to protect the consumer and it failed in Westpoint’s case. There were enough warning bells for ASIC to step in.”

“It (Westpoint) had been having issues as a group for a long time. ASIC already had thousands of pages of information on them – but they just wouldn’t enforce the legislation with them ... If ASIC spent more time in the field and amongst industry, they would have know about this (i.e. the practices of Westpoint) long ago.”

A few attributed problems to the legislation itself rather than to the way ASIC enforced that legislation.

“Don’t introduce dumb legislation in the first place. Think long and hard as to whether legislation is the correct solution to the problem. It seems to me that they say ‘here’s a problem, so we’ll introduce some legislation and fix that’, and all that does is forces the good guys into more costs, and the guys that want to keep doing the same thing, will keep on doing the same thing to a large extent.”

“I think that everybody seems to have lost why we introduced it [the FSR]. To my mind, a lot of the reason for introducing FSR was to capture the consumer issues involved with fringe lending by unlicensed organisations ... which are still out there, frankly.”

A few respondents from large organisations felt that ASIC focused too much on the major players, and that “ASIC-style compliance” was probably more appropriate to the small, specialist or boutique organisation which didn’t already have sophisticated internal systems and procedures in place.

“We are in this business for the long term. We have a range of regulators that we need to meet the requirements of – ASIC, APRA, ABA, BFSO – and if we do the wrong thing we get caught. They (the regulators) should focus on (the smaller companies) where the biggest risk of non-compliance is. This is the best way to protect the small, unsophisticated consumer.”

6.6.2 Impact of ASIC on Costs

Respondents were asked to estimate what proportion of their compliance costs could directly be attributed to complying with ASIC requirements, and what proportion they would incur in any case, based on their business practices.

As noted previously, most respondents found it very difficult to separate out compliance costs which were due to ASIC, compliance costs which were due to other regulators, and costs which were associated with the cost of doing business.

“You can only do this once you have clearly identified all the costs and analysed the business from the point of view of inefficiencies and where there is no value. Then you need to consider why that part of the process was happening. Was it part of a regulatory requirement or an old business practice?”

“In terms of compliance, a well run business would do many, if not all of the things that come under compliance. So, distinguishing between ‘pure compliance costs’ and what is just good business practice is well nigh impossible.”

Little impact for some: However, some respondents commented that they would incur a large proportion of their compliance costs regardless of ASIC activities. These were primarily respondents from global organisations, where compliance activities were often developed to be consistent with requirements of major overseas regulators.

“I have quite a large department and it is well structured and running very efficiently. In fact a lot of what we do in terms of compliance is automated. In terms of the regulation, it is all very stable and the requirements are clearly defined. We need to comply with regulation but we’ve always been a bank that has taken great pride in our business practice – so I would say that there is nothing that we currently do because of regulation that we wouldn’t have done anyway.”

“If ASIC was not there then it would not look any different. In some areas ASIC was late to set up measures as we are part of an international bank and we had moved already.”

“For us it (FSR) has not meant a significant difference. We may document processes more completely now that there is a formal structure.there may be a saving of head count and they would not issue Statements of advice in the current format. ...but there would not be a lot of change because our global parent provides most of the compliance direction.”

“ASIC & APRA might add 25% to our cost of doing business but in most cases we would still be doing whatever it is even if we removed one of them (ie ASIC or APRA).”

“We guess that APRA and ASIC have added about 25% to our total operating costs but if you removed one of them, that probably wouldn’t reduce very much. I think it is fair to say that a lot of the costs are just part of doing business.”

Substantial cost reduction for most: The majority of respondents said their compliance costs would be reduced significantly in the absence of ASIC. This was primarily related to:

-] Less senior management and Board member time devoted to compliance;
-] Reduced training requirements;
-] Reductions in monitoring and reporting activities;
-] Significant savings in document preparation and publication costs.

“There would still be a need for a Compliance Department because of the various other legislative requirements. But without ASIC compliance would revert to a policies and procedures function and would not be nearly as high profile, with involvement of the Board, as it is at present. ... significant business costs would be saved, both on direct costs and in Board and senior management time, and we could spend a lot more time on the business rather than in the business.”

“I would estimate that 80% of our \$5m compliance department costs could be attributed to ASIC matters.”

“About 40% of our compliance activity is FSR related (training, time in processing customers, disclosure costs).”

“Prior to being regulated by ASIC, we employed 0.5 people in compliance (now 1.6 staff in compliance). The business has grown, but regulatory costs had increased at a far greater rate than the rate of business growth.”

“We would save staffing costs and opportunity costs associated with reporting so it may be up to \$30-40,000 in total.”

“If we did away with ASIC (regulations on compliance) I am not going to say it would change a lot. But it would change the documentation and a lot of time and cost would disappear as well.”

“We would retain most of the current policies and systems in place, but we would re-write a lot of the client documents over time and remove the unnecessary wording, and only provide clients with what they wanted. ... we would also save considerable costs in not having to pay for the Compliance Consultant, and in IT and printing costs, and management would be able to spend more time on the core business rather than on compliance issues.”

“Most of the costs with FSR are straight out compliance costs. The changes were excessive and we wouldn’t have introduced them without regulation saying we had to.”

“Basically, I wouldn’t have to spend as much time on report generation – that is where the bulk of the cost saving would come from.”

6.6.3 Dealing with ASIC

ASIC one of many regulators: For some respondents, ASIC was just one of many regulators that they dealt with. Australian regulators that respondents deal with included:

-] ASIC;
-] APRA;
-] Austrac;
-] ATO;
-] ACC;
-] Workcover;
-] Office of Fair Trading in each state.

Respondents from global organisations said they and their organisation dealt with many regulators world wide. One respondent from a global investment bank said that their Head Office had recently tallied all the regulators they dealt with world wide, and had counted 452. These respondents with widespread regulator experience tended to be quite positive about their dealings with ASIC.

Some frustrations: Many respondents were somewhat frustrated in dealing with ASIC because:

-] They believed that ASIC did not provide sufficient guidance in interpreting legislation;
-] They felt that ASIC was too far removed from the market, and did not always understand the implications of its requests on businesses;
-] They wanted ASIC to take a more relationship based approach to dealing with individual organisations;
-] Some argued that where breaches occurred, ASIC appeared to assume malicious wrongdoing, whereas they believed that reputable organisations were making every effort to comply with the Act (e.g. if a mistake was made, it was an innocent one).

“We raised concerns at an ASIC forum about the costs of compliance and ASIC’s response was that it is OK because the markets are performing well and that business can afford the costs of compliance. My response was to ask what happens when the markets drop. Will my compliance costs drop? Of course they won’t and they may even increase due to greater risk and complaints.”

6.6.4 Dealing With ASIC Relative to Other Australian Regulators

Views about the ease of dealing with ASIC relative to other Australian regulators were quite variable, with some seeing ASIC as big very easy to deal with, and some being quite critical.

A substantial minority of respondents contrasted ASIC unfavourably with APRA, saying that APRA took a different view of its role, seeing itself as a body to assist organisations in their compliance activities, whereas ASIC took a much stronger regulatory approach.

“APRA has very competent liaison people dedicated to giving advice and hearing a differing view from accepted practice, whereas ASIC sees itself as a policeman.”

“I’m not convinced that ASIC understand the practicality of being regulated. APRA is much more flexible and tolerant in this respect.”

“APRA are prepared to sit around a table and discuss things. They don’t flex muscle which has happened with ASIC in the past. I think they are working on the trust side of things more.”

“ASIC collects a large amount of information compared to APRA and they have a different regulatory style. APRA works on a relationship basis with us on a one to one basis. They have one person who deals with us and we have one person here dealing with them. ASIC is multiple contacts at their end and could be dealing with many people here. Also rightly or wrongly, ASIC focuses on specific customer matters (problems) rather than the process.”

“ASIC is impersonal, bureaucratic and inflexible. ...they are very difficult to deal with. APRA on the other hand drives the relationship, and they are much easier to deal with, more flexible and tolerant.”

“It would be helpful to have people (in ASIC) dedicated the General Insurance side of the act, so as to be able to provide specialised information to our industry. In dealing with APRA, staff were well versed in the requirements and were proactive in providing lectures for Auditors each year prior to the end of the financial year.”

However, there were some exceptions to this point of view, with some very positive about the way ASIC managed regulation.

6.6.5 Australian Regulators Relative to Overseas Regulators

Respondents who had experience in dealing with overseas regulators compared the Australian situation (across all regulators) with their international experience.

Some found Australian regulators easier to deal with: A few regarded Australian regulators in general as easier and more efficient to deal with than regulators in other countries.

“Australian industry is more heavily regulated and I think that is the case for a number of reasons. Firstly the HIH collapse showed flaws and certainly caused heavier regulation. There is also a strong consumer interest in having insurance and investment safely managed.”

“It is less onerous than the UK and USA. We decided not to expand into those countries because of the draconian financial services legislation.”

“There are a number of regulators in Australia – but in comparison with overseas, they are really easy to deal with. ASIC are great to deal with. We haven’t had any problems.”

Some felt there was considerable variation from country to country.

High cost relative to the UK: The cost of dealing with regulators were said by a few to be higher in Australia than in UK because:

“In the UK there are no state regulations (there are no states) where in Australia there are State and Federal legislation. (Thus the costs in Australia the costs were higher).”

“In the UK it is more established and more stable (with changes etc).”

“The FSA has ten principals of best practice and is not as prescriptive as ASIC. It is a great way to regulate – more efficient. Also, being a single regulator makes for lower costs. We have to separate ASIC and APRA compliance teams, and this can be confusing as well as being costly, as they overlap.”

One respondent disagreed with this regarding compliance costs in Australia and the UK as similar.

“ASIC is more like the FSA in London. There is similar, but different wording and the FSA is a more mature market. ... but overall, there is little difference in costs.”

Low cost relative to the USA: The US regulatory system was said by most of those who commented to be very difficult to deal with as it involved extremely high levels of prescription and very high costs of compliance.

“The USA was a couple of years behind and they had a different attitude to regulatory. The SEC or Department of Justice are very predatory. If a company is in non compliance in the USA they try to close you down. In Australia they try to get you back on track.”

There was one dissenting point of view:

“The SEC is more technical and it understands the market better. It engages more with industry and operates a relationship manager approach.”

Asian experience variable by country: The cost of dealing with Asian regulators was seen to vary substantially from country to country.

“In Asia, doing business throughout the region is difficult because of the large number of countries involved, each with a different regulatory approach. Also, some Asian countries lack clarity and consistency, but this is not a problem in Australia.”

“Singapore looked at Australia (the Australian Financial Services regulatory environment) before it created its own – a much simpler version. There, the onus is on the Financial Planner to disclose information to their client, and they can do that in five pages, not the 30+ that we have to do.”

“In Japan the regulator is very draconian. They could land at your door and stay for two months.”

Summary: Perceptions of ASIC

ASIC believed to have been effective: The majority of respondents believed that ASIC had been effective in regulating the markets.

Impact of ASIC on costs: Most respondents found it very difficult to separate out compliance costs which were due to ASIC, compliance costs which were due to other regulators, and costs which were associated with the cost of doing business.

Little impact for some: Some respondents, primarily from global organisations, commented that they would incur a large proportion of their compliance costs regardless of ASIC activities.

Substantial cost reduction for most: The majority said their compliance costs would be reduced significantly in the absence of ASIC, primarily related to:

-] Less senior management and Board member time devoted to compliance;
-] Reduced training requirements;
-] Reductions in monitoring and reporting activities;
-] Significant savings in document preparation and publication costs.

Dealing with ASIC: Many were somewhat frustrated in dealing with ASIC because:

-] They believed that ASIC did not provide sufficient guidance in interpreting legislation;
-] They felt that ASIC was too far removed from the market, and did not always understand the implications of its requests on businesses;
-] They wanted ASIC to take a more relationship based approach to dealing with individual organisations, and with specific industry sectors;
-] ASIC appeared to assume malicious wrongdoing where breaches occurred.

6.7 Suggested Actions for ASIC

As noted in Section 6.4.1, many respondents were critical of the cost of some aspects of compliance associated with ASIC. Many suggestions were made about how such costs could be reduced. While some of these suggestions did not appear to go directly to costs, as they all had at least some impact on staff time, they all did have at least some impact on cost.

Issues raised by many respondents: The main issues raised by respondents were as follows.

Documentation requirements: As has been discussed elsewhere in this report, this was a major issue for many respondents, and the single main cause of dissatisfaction with the cost of financial markets regulation.

Specific issues related to:

-] **Length of PDS, SOA and FSG:** The amount of detail that had to be provided in PDS, SOA and FSG made these documents very long and time consuming to produce. As noted previously, this meant that many organisations had moved from providing any advice to retail customers because of the cost of doing so.

"We should just be able to ask the customer what they want, and then provide that. We shouldn't have to provide all the fees and charges and how the account works if they don't need that information. We should just provide the basics of what the customer wants. It's better that the customer gets the information they want, rather than being given everything and then it is all thrown in the bin."

"The amount of information we are required to give a customer opening a new bank account is too much; I don't believe any customers really read it. It would be better if we could just draw the customer's attention to the availability of this information on our website, rather than being forced to give the information to the customer and telling them they had to read it and keep it."

-] **PDS:** In particular, a number said that there should be no regulatory requirement to provide PDS at all, or alternatively, that they should be able to provide a short form PDS.

"Fix PDS. Get rid of this requirement. ... We should just give a copy of the contract to the customer and let them get advice."

“Reduce the amount of disclosure required. For example, the policy booklet for travel insurance. is 15 pages long and has a comprehensive list of exclusions that consumers understand. Why then, do we need a PDS as well, showing taxes and charges on premiums.”

“There could be a short-form PDS and the detail could be incorporated by reference to another source such as a website. It should be clear, concise, and easy to understand by the average client – not the huge amount that is required at the moment.”

“The PDS should only be about two pages, not the currently required 40 pages. They (ASIC) won’t tell you what to cut out and they won’t give advice. We know what we would like to cut out, but we don’t want to get it wrong. They (ASIC) just say – “You work it out” but then they (ASIC) will criticise us if we get it wrong.”

Some argued that not only would it be cheaper and more efficient to provide PDS information on their website, it would also be more accurate because it would be up to date.

“We redo PDSs once a year, and in this we have to include our latest return. These are out-of-date by the next month and are incorrect for the rest of the year. It would be much better to refer clients to the website where the rates can be continually updated.”

“The principles of disclosure are necessary, but how you set the length of the document and the extent of disclosure is a bone of contention and we think ASIC wants way too much in there. Our products are not investments, just simple insurance cover. If you can use the internet to sell insurance, the costs can be so much reduced. You can do this under the regulations, but it depends how you do it.”

-] **SOA:** Many respondents felt that the length of time it took to SOAs was too long, and too costly, and that it did not deliver a benefit to customers.

“In the Statement of Advice you have to get to page 79 before the client gets to the real issue. It is way off track as (an) advice (Instrument). ... We need advice in two to three pages, that is all that is needed.”

One respondent from a financial planning organisation said that it took on average six hours to complete a SOA, whereas she thought that around one hour would be more reasonable.

“The advisor has to make very specific requests of the client, and assess the client’s current knowledge. Sometimes the clients don’t want to be provided with advice – they know what they want, and they don’t want or need an SOA, but the Advisor still has to complete it and this all takes time.”

A number argued that the Statement of Advice provided far more detail than the majority of clients wanted, and some gave examples from their own personal experience.

“I am a lawyer and have a Diploma in Financial Planning, as well as being Managing Director of a Funds Management and Financial Planning organisation. I recently wanted to change the ownership of my personal life cover to my self-managed superannuation fund and even I still had to receive a completed SOA for this. I didn’t need any advice, I didn’t ask for any advice, and I certainly didn’t need an SOA to know what I wanted to do. It was just a total waste of time and of course I never looked at it.”

Some argued that there should be various categories for SOAs such as for those who:

- Request advice;
- Don’t know what they want; or
- Don’t have knowledge in the area.

Many also argued that they should be able to provide electronic Statements of Advice rather than hard copy.

“Companies are now allowed to provide their Annual Report information in soft copy on the web, and we should be able to do this with much of the information that we now have to give in hard copy.”

] **Other issues:** In addition, a few respondents said that specific information requirements were unnecessary and could be confusing to customers. Examples given included:

- Comparison rates, where some respondents said many customers people did not understand what comparison rates were.
- The prescribed format that ASIC required for organisations to list its fees confused clients of not for profit organisations, but ASIC did not make allowances for this.

Lack of market guidance: Many respondents felt that ASIC provided insufficient guidance in terms of what was required of organisations in order to comply with legislation. This had a direct impact on costs, as individual organisations then had to obtain legal advice about what their obligations were, and what they had to do in order to meet them. Many saw this as very inefficient, not only for their own organisation, but for the market overall, as each organisation had to obtain its own advice.

“There is a need to get back to reality, and not be too theoretical about the approach. Legislation needs to be practical, and not subject to ambiguity and massive costs trying to interpret what it means. You think ‘OK, if we want some clarification on something, we’ll go and ask ASIC’, but it doesn’t work like that! Oh no, you’ve got to go and get your own legal advice, we’re not going to tell you what this stuff means, we’re just going to put it out ... and everybody does exactly the same thing, so the solicitors are doing well out of it.”

“ASIC attended a lot of industry forums about FSR and there was a lot of ‘we don’t know’. We don’t actually see ASIC from one year to the next. There is no ongoing process of interaction. We do have this with APRA – we have monthly meetings and they are helpful. I think it helps them to understand the insurance business. And if we have a problem then we can have a conversation with them. What we need from ASIC is a clear understanding of what the law looks like and what they are trying to achieve. They have a tough job and the political environment in which they work must make it difficult. I’m not saying we need to have meetings with ASIC every month – but rather if they were able to give us a better understanding of what the regulation was trying to achieve – then that would help.”

“We’d like more feedback from ASIC on what is required. The only breaches that are promoted in the media are extreme examples. ... we’d like to hear about fringe examples where companies didn’t quite get something right. ... we could use that too help us make sure we get it right.”

“ASIC just says that they will leave it up to us – but they will also hit us over the head if we don’t get it right. We would rather that they gave some guidance – some specifics to include. We took the approach that we will include everything because we were given no direction, and we didn’t want to see our Financial Planners on the front page of the Courier Mail. So we provide a 120 page Statement of Advice. But one of our competitors now has its disclosure down to 15 pages and it gives a reference for its clients to seek out the other 75 pages.”

“We approach ASIC and ask them if our proposed approach or new product is OK and they say we can’t advise you on the record. Off the record, we think its OK, or it may be OK but we don’t like it, are not helpful responses, because they reinforce the uncertainty and promote a non level playing field.”

A number of smaller businesses thought a lack of clarity in regulations applied only to them, but in fact it applied to businesses of all sizes. Often it was not very clear what ASIC expected and how to apply ASIC guidelines.

“When ASIC makes rules and regulations they should be black & white with no grey areas which cause confusion – guidelines should be clear cut and simple. ... This is what we expect of you. Sometimes ASIC themselves don’t know how to interpret their own guidelines.”

Some respondents felt that ASIC needed to have greater consistency in its guidance, and this was mentioned particularly in relation to conflict of interest regulations. Several cited the guidelines given by ASIC in the CitiGroup case, saying they were contrary to its earlier guidelines.

Several respondents suggested that it would be useful for ASIC to provide guidelines which were more closely tailored to the size and type of the business, as they suggested that these factors often determined how compliance is managed.

Insufficient consultation with industry: Many felt that ASIC should have a more consultative approach rather than its *“big stick approach of throwing the baddies in jail.”* Some felt there was an atmosphere where organisations were scared of ASIC, rather than an environment where people and organisations were happy to work with ASIC.

“We are reluctant to go to ASIC if we don’t quite understand because we are afraid we will get hit or a big fine for asking. We want to get it right, but its all in the interpretation. They (ASIC) should have a more conciliatory approach to those who are trying to get it right.”

“There are so many grey areas. You have to ask yourself is it a breach or not. ASIC is not helpful to say whether it is a significant breach or not. I can’t seek advice from ASIC as they will treat it as a breach. So I have to seek legal advice and that costs me \$3000 to \$5000.”

“The majority of the financial services industry are not shysters, whereas ASIC, when approached, takes a non-committal hard line that adds costs and makes the products harder to sell against less restricted competitors who appear able to continue in business without ASIC taking action against them.”

Greater interaction with market: A considerable number of respondents felt that ASIC did not have a sufficient degree of contact with the market, and therefore did not have an adequate understanding of the impact that compliance requirements had on individual organisations. This was frequently contrasted with the approach used by APRA, and to some extent by Austrac, which were seen to have more interaction with market.

“ASIC brings in technical pieces without fully understanding the market. It is outside the issues and market and it needs to have more discussion with industry.”

“You get ASIC people coming and presenting at an industry luncheon, but the official will only come for his presentation, will not take any questions, and will leave immediately afterwards.”

“ASIC senior staff make themselves scarce at industry functions. They disappear straight after speeches and won’t answer any questions. ... They can’t elaborate on anything unless it is all signed off by their legal people. That’s why they don’t take questions after their carefully scripted speeches.”

Some suggested that it would be valuable for ASIC to collect and disseminate feedback on best industry practice on compliance matters.

“ASIC do issue consultation papers inviting comment but the process doesn’t really work. In the past we have spent considerable time formulating a response to these papers only to find down the track that the legislative change wouldn’t apply to us anyway. So, we have spent a considerable amount of time for nothing – it is all costly. It is a tricky situation because ASIC are unwilling to be put on record on these things – so they are not likely to say up front if it isn’t going to impact us. ... I think ASIC need more understanding of the industry.”

Account management: Many expressed a desire for ASIC to take more of an account management approach. Respondents acknowledged that ASIC had many organisations to deal with, and it could not do this for all organisations. However, the larger organisations thought it would be feasible for ASIC to take an account management approach with say, the 100 largest organisations it regulates.

Further, some of the smaller organisations suggested that ASIC could assign staff to particular industry segments, so that these individuals developed a very good understanding of the particular industry sector (for example, insurance broking, credit unions, financial planning, etc).

It was thought that this would help to develop a more co-operative mode of working, rather than the confrontational approach that some respondents felt ASIC took at present.

“This would not necessarily reduce compliance costs. We won’t spend less because of the risk to us, but we will target our resources more effectively and we would be happier about it all.”

“ASIC need a better understanding of the general insurance industry.”

“ASIC need to be more focused on building trust and that means being prepared to discuss things.”

“I’d like to be able to meet with ASIC on a regular basis, say quarterly, to build a relationship, to explain our business and processes, to float some ideas and get feedback from ASIC prior to implementation; and to have a regular point of contact within ASIC who knows our business and key personnel.”

“A Liaison Officer could learn about a particular business and the market place it operated in, and would give guidance and help it review new legislation or changes before it was required to make the changes. The Financial Services Act was around 1500 pages long and the ASIC Regulations Guide was a further 200 pages long. ... and no one could completely know all that and be able to implement it without any omissions or misinterpretations. If there was an ASIC Liaison Officer allocated to each organisation, he could become familiar with the standard dealings of these organisations, assist and guide them in the correct procedures. He could also find out about any incorrect practices and help the organisation to alter them without the fear of ASIC coming in to close them down because of this.”

“ASIC will never meet us for a cup of coffee, and when they meet, they always have at least two people present. They consciously don’t want to develop a relationship.”

Some felt that the approach of ASIC staff was more confrontational than collegiate.

“We would like ASIC to have a look over our programs, tell us where we could improve, and give us a tick for being a compliant organisation.”

A few respondents said they thought such an approach would also help ASIC to really get to know which companies they needed to focus on, and which ones not to, and therefore they could make better use of their resourced in *“weeding out the bad operators in the industry.”*

A few respondents said that it appeared that recently, ASIC was trying to have a more consultative approach; that is, they were more open to talking to organisations, giving advice and sharing what other organisations were doing on compliance.

Principles based approach: Some respondents argued for a principles based approach to regulation, which they felt allowed organisations the flexibility to differentiate themselves in the market, while still meeting their regulatory obligations.

“I prefer the ASX Corporate Governance Guidelines where organisations can apply to the ASX not to comply on a certain issue if they can show good cause why not, or can demonstrate appropriate alternatives. ... I would like more robust industry debate on what the legislation should contain. I'd like to see a quasi-independent body set up, made up of regulatory, government and industry representatives, to look at any legislation before it gets to the political table so the legislation can be debated beforehand. ... some high-ranking academics have suggested this ... Professor Ian Harper and Professor Wallace from Melbourne University, but it has not been tried. A high-level review body would collectively iron out many of the key issues within the legislation and make it far easier and less costly for all organisations to implement. ASIC does consult with individual industry bodies, but I think they get lost in the detail of the responses. ... all legislation should go through an 'original purpose' test to see whether it is meeting its original purpose, or whether it's become lost in the detail. ... Much of Australian regulation is like cracking a walnut with a sledge hammer.”

Greater flexibility in interpretation: Some respondents felt that ASIC focused too much on the letter of the law rather than the spirit of the law, and thus organisations sometimes incurred unnecessary costs.

For example, one respondent from an insurance broker explained that she was the Responsible Officer and the Financial Controller of the organisation but not a practicing broker. However ASIC required that all Responsible Officers had to undertake the same training as a practicing broker which cost \$3,000 for three assessment areas and \$4,000 for another seven assessment areas, and she didn't see the value of her business having to pay these costs for her.

“Brokers are staff and deal directly with clients and their portfolio reviews. I do not. I am a Director of this organisation and have a senior role. I also have a financial interest in the company, so there is good reason why I would be a Responsible Officer. But I think there should be different (ASIC) guidelines for a Responsible Officer who is a practicing broker and a Responsible Officer who has a management role.”

“ASIC is too pedantic in disclosure requirements, which causes costs to be too high with no commensurate consumer protection delivered by this cost impost.”

Address duplication across regulators: A number of respondents discussed duplication between requirements of ASIC and APRA. Some acknowledged that ASIC and APRA had tried to resolve this issue, and that while some progress had been made, there was still considerable duplication. Duplication of effort by organisations thus had an impact on their overall costs. Some noted that duplication also increased costs for the regulators.

“ASIC and APRA don’t talk about regulatory matters of mutual interest and so it causes extra work and delays for us. For example, the issue of custody and unit pricing took 3 months just to get ASIC and APRA together. It would be better if they were a single regulator.”

“Resolve this dual oversighting of superannuation – either get ASIC to do it all or APRA. ...there are disagreements exist between the two in terms of priorities.”

“There’s a lot of overlap between information required by APRA and ASIC. ... often the same information is required in a slightly different format which doubles the cost of providing it. For example, we have to report some of the same breaches to both authorities, but different tests have to be applied for each.”

While discussion of duplication usually focused on ASIC and APRA, respondents also mentioned:

-] Duplication between ASIC and ATO, saying it would be preferable for them to share their databases, which would reduce duplication caused by the two organisations asking for the same or similar information.
-] Lack of harmonisation between ASIC and ASX, so that there was a lack of consistency in the corporate and market rules.

“You can be in compliance with one and be in breach with the other.”

Lack of co-ordination between ASIC departments: Some respondents said that they could be asked for the same or similar information by several different ASIC departments, which indicated that the internal ASIC departments didn’t share information.

“In the last two months up to six ASIC people have contacted as many as six of our staff and it is just not efficient.”

One respondent noted that some requirements under the Corporation Act for Market licensees meant there was a need to report to multiple area within ASIC. For example, information relating to changes to Officeholders and changes to Shareholder Structure had to be submitted to two different areas within ASIC.

Requests for information: Respondents noted two problems in relation to requests for information:

-] **Ad hoc requests:** A few respondents noted that when they received requests for information they had not expected to provide, it created a great deal of work because the information was not in a readily retrievable format.

“You never know what they are going to ask for!”

“ASIC can overwhelm a small business with its requirements to provide documentation. I don’t think ASIC even looked at a lot of it ... that’s a huge cost for a small organisation, which does not benefit anyone [if ASIC are not using it].”

“I’ll give you an example of just one ad-hoc request from ASIC which cost us a lot in time and money. Our advisors are required to record certain actions within the company records, although ASIC normally does not ask for this information. ... on one occasion they did ask for it and they wanted the information within two weeks. We had to retrieve all the company records from the Advisors going back over some period of time. ... it was about 250 files of about 100 pages each. Once the specific information was found, then it had to be copied and sent to ASIC. That took a lot of resources and staff had to drop other things they were doing just to comply with this one ASIC request. If ASIC specified what information it requires, we could organise our information collection in a way that was easy for it to be retrieved.”

-] **Old information:** A few respondents noted that if the matter was an old one, it was extremely difficult to track down all records. For example, a respondent from a financial planning organisation said that in old matters, it was possible that the relevant adviser had moved to another organisation. As the records remained the property of the adviser, it could be extremely difficult to track the records down (although the adviser was obliged to submit the records if requested, the adviser had to be first located).

ASIC staff inexperience: Allied with the above point was the view that some ASIC staff, particularly the more junior staff we very inexperienced, with no previous industry experience, and thus did not understand their implications of request they made. Respondents acknowledged that it was very difficult for ASIC to resolve this issue.

“They (i.e. ASIC staff) are lawyers rather than industry practitioners. They don’t know what it’s like to work in our industry and to have to comply with what they are asking.”

“There are some very good people in the most senior positions, but there is a lack of depth in the organisation. Some of the junior people are over zealous and lack commerciality.”

High turnover of ASIC staff. A few respondents said that because there is high turnover of ASIC staff, the organisation’s own staff had to explain the organisation and business operations to new ASIC staff enforcement officers. Respondents did not see how this could be resolved, but indicated that it represented a cost to them in staff time.

ASIC websites: While the main ASIC website was seen to contain a large amount of very useful information, some felt it was difficult to navigate. In addition, a couple suggested promoting FIDO and the information on it more heavily in the media and to the general public.

Issues raised by a small number of respondents: In addition to the above broad issues, respondents made many suggestions which related to very specific issues or beliefs relevant to their own business or industry sector. Each of these issues was identified by only one or a very small number of respondents.

Personal General Advice Model: One respondent felt this was insufficiently defined.

“This is the structure that ASIC has put around advice requirements and it needs to be amended. What is personal and what is general advice?”

Training: Respondents individually raise several issues in relation to training:

] **Training standards:** One respondent believed that Financial Advisors should have more stringent testing to lift the standard, and advocated increasing the level and quality of training for financial advisors.

“The PS 146 of the Codification of Quality Standards gives the standard in order to give advice. It is such a low bar to get over and the customers do not know the level of the advisors training.”

] **External trainers:** Several respondents said they would prefer to not to have to use external trainers for training, especially for PS146. This was because the cost of trainers was continuing to rise, and they would have preferred the option of writing and delivering their own PS146 accreditation

Frequency of changes: One respondent wanted changes to be released less frequently, so that organisations could make the changes once and not have to keep redoing them. This respondents said that Regulation Guides 104, 105 and 146 were “constantly being rewritten.”

Mediation: One respondent said that ASIC should show a greater willingness to use mediation before using the courts to resolve matters.

Banking: Several banking respondents individually raised some specific issues as follows:

-] **Review the advice model:** Several argued that the legislation determining the advice tellers can give is too onerous and needed revision.
-] **Harmonise the legislation and codes of conduct:** One argued there needed to be a streamlining and harmonisation of the various codes and legislation.

Credit Unions: Several Credit Union respondents said that ASIC did not allow for the unique structure of credit unions in its requirements, and that this created reporting difficulties for them, where they were unable to meet some of ASIC’s information requests. A specific example given was the Top 20 shareholders list. Credit unions typically had many shareholders with equal shareholdings and were therefore unable to provide reports on the top 20 shareholders.

These respondents suggested that ASIC may need to consider introducing a new section in the corporations law that would acknowledge mutuals and credit unions with their unique shareholding structure.

Reporting: Some specific issues in relation to reporting were raised by respondents. These were:

-] **Online:** Several respondents said that ASIC should accept online reporting.
-] **Multiple reports:** One respondent suggested that the same report should be able to be directed to different agencies (particularly online). He said this was already in place between ASIC and APRA, and it was very easy to use (just tick a box to indicate which agencies the report needed to go to).
-] **Timeframes:** One respondent suggested that reporting timeframes should be standardised;

] **Breach reporting:** One respondent suggested that reporting obligations regarding significant breaches should be reduced, and there should be greater clarity around what was meant by “significant” breaches.

Simpler product classifications: A few respondents said that currently their implementation overhead was too high for new products, and this was at least in part due to complex product classifications and documentation requirements.

Consistency across regulators: One respondent noted that when new legislation was introduced, it was important for the regulators to ensure that industry could comply. This respondent gave the example of AML, where there were requirements for checking personal information, but privacy legislation prevented the organisation from verifying personal ID (e.g. checking with the RTA re drivers licences).

ASIC Guide for the Audit process: One respondent said this had not been updated, and completion of the FS 70 & FS 71 documents was therefore confusing.

Review FSR: One respondent indicated that ASIC had provided some relief on basic deposit products and felt that ASIC should do the same for general insurance products because:

-] Most insurance products were simple;
-] The general public understood most insurance products as they were not new or complex products.

Positive Responses to ASIC

No improvements necessary: Despite an invitation in the interview to suggest actions that ASIC could undertake to reduce compliance costs, a few respondents could not identify anything that ASIC could do to reduce business costs and reiterated that ASIC’s requirements were not onerous.

ASIC already taking steps: A few respondents mentioned that ASIC was already putting procedures in place to improve efficiencies. For example, one mentioned that she could now appoint an authorised representative via ASIC website portal and this would take a lot less time compared to a manual application.

Others mentioned an apparent improvement in liaison between ASIC and APRA.

“There has been a change over the last four to five months where there has been a consolidation of terms between APRA and ASIC. This has been a really good thing.”

Research viewed positively: Some respondents also commented positively on the fact that ASIC was undertaking research in the marketplace, as they felt this demonstrated that ASIC was serious about identifying ways in which it could assist industry in managing and reducing compliance costs.

Summary: Suggested actions for ASIC

The main suggestions made by respondents which they felt would help to reduce their compliance costs were:

-] **Reduce documentation requirements (PDS, SOA, FSG):** This was the single main cause of dissatisfaction with the cost of financial markets regulation. Respondents believed that the amount of information they had to provide meant:
 - Costs were far higher than necessary (preparation time, printing and dissemination costs);
 - Customers were poorly served (many organisations had withdrawn from providing advice to consumers because it was too costly to do so; customers did not want large amounts of information).
-] **Provide market guidance:** Many felt ASIC provided insufficient guidance in terms of what organisations were required to do to comply with legislation;
-] **Consult with industry:** Many felt that ASIC should take a more consultative approach with industry;
-] **Initiate greater interaction with the market:** There was a belief that ASIC lacked understanding of the impact that compliance requirements had on individual organisations because it did not have sufficient market interaction;
-] **Account management:** Many expressed a desire for ASIC to take an account management approach, which it was felt would help develop a more co-operative mode of working;
-] **Principles based approach:** Some argued for a principles based approach to regulation, which they felt allowed organisations the flexibility to differentiate themselves in the market, while still meeting their regulatory obligations;

Summary: Suggested actions for ASIC (cont.)

-] **Greater flexibility in interpretation:** Some felt that ASIC focused too much on the letter of the law rather than the spirit of the law, and thus organisations sometimes incurred unnecessary costs;
-] **Address duplication across regulators;** While this related to a number of regulators, duplication between requirements of ASIC and APRA was raised as the most common problem;
-] **Address lack of co-ordination between ASIC departments:** Some said that they could be asked for the same or similar information by several different ASIC departments, which indicated that the internal ASIC departments didn't share information.
-] **Greater consideration of information requests:** Respondents noted that it could be difficult for them to meet ASIC requests for information because:
 - **Ad hoc requests:** Some ad hoc requests were for information the organisation had not expected to provide, and the information was not in a readily retrievable format;
 - **Old information:** Old information could be difficult to retrieve quickly.

7. APPENDICES

7.1 Appendix A: Discussion Guide

Background information

Prior to interview, obtain some background information about organisation from website, annual report etc, to provide context for interview. Look for information re:

-] Nature, size and geographic spread of the respondent's organisation, including type of clientele and main products or services.
-] Number of employees
-] Annual income and operating costs of organisation

Face-to-Face Interview Discussion Guide

*This is a discussion **guide** (a list of issues that will be raised in interviews). It is not a questionnaire. The interviewer will encourage the respondent to explore issues surrounding each of these topics and to raise issues about ASIC that they feel are relevant, in addition to this checklist.*

1. Introduction

Explain the nature and process involved in this research:

-] We are doing this work on behalf of ASIC.

The objectives of this research are to develop ASIC's understanding of:

-] Industry perceptions about the overall costs of the regime that ASIC administers;
-] The overall size and direction of these costs (i.e. how they have changed over time);
-] The business areas most heavily affected by regulatory compliance obligations; and
-] How regulated businesses keep track of costs.

ASIC will use the findings to deepen its understanding of the cost impact of its regulatory decision-making on business and to create a factual background for further ASIC-industry dialogue on cost and business impact issues.

The approach is an open-ended discussion that will take about an hour. The respondent's views will be confidential and amalgamated with views of others in the report to ASIC.

2. This Organisation, This Person: Obtain some background contextual information about the respondent:

-] The role of the respondent in the organisation.
-] Identify how this organisation is structured to manage compliance – specific departments, staffing, resource allocation, perceived importance to the business, etc.

3. Overview of Compliance Activities

(Note: The aim of this section is to understand overall how the respondent defines, understands and categorises compliance.)

-] Explore respondent perceptions of what compliance entails, unprompted, including:
 - Respondent definition of compliance and scope (what does it include / exclude);
 - Components of compliance.
-] Prompt with list of possible compliance categories (Card attached). Explore how well this list fits with respondent perceptions of cost categories including identifying any gaps. *(Note those that apply to this organisation on the card, and take comments as you go through the categories.)* For each category (not already discussed), at an overview level explore:
 - Whether this category applies to this organisation;
 - The relative importance to the organisation.

(Interviewer Note: Many of these cost categories have been provided by FICA, based on an assessment of the Business Cost calculator methodology. Aim to establish if these categories are consistent with the way interviewees think about costs, and collect and monitor cost information.)

4. Information Collected And Monitored By Businesses In Relation To Compliance Costs

(Note: In this section we are particularly interested in whether businesses identify and report on ongoing/ recurring costs. This should be the main emphasis of the conversation.)

-] Do you identify and report on compliance and regulatory costs within your business? What information is kept?
-] If so, who is asking for this information? For example, does a report go to the Board every month? What information does the Board have in front of them?
-] How is this information used? Does it influence any of your business decisions? In what ways?
-] How do you monitor and collect this information? For example, do you have specific computer software to monitor and track compliance costs?
-] Do you have any data related to implementation and ongoing costs of the regulatory changes introduced in the last 5 years? Do you have any information that might be useful to share with us?

5. Perceptions About Overall Size And Direction Of Costs

Costs are defined as the costs incurred by your organisation to comply with financial regulation administered by ASIC; i.e. capital costs, staffing, policies and procedures, publications, legal, advisory, audit, insurance, etc. *(Interviewer note: It may be difficult for the interviewee to separate out ASIC costs from costs of compliance with other regulatory bodies such as APRA and ASX, both from an internal systems point of view, and because of overlapping compliance requirements. As far as possible, aim to disentangle these costs.)*

At a general level, explore perceptions about overall direction and size of costs: Throughout the discussion, note how confident the interviewee is of estimates provided.

-] What would you estimate are the total identifiable current costs of compliance for your business as a percentage of total costs (e.g. less than 2%, from 2 to 5%, 5 to 10%, etc.)?

-] Have these costs changed over the past 5 years? To what extent have they changed (percentage of increase/decrease/ in absolute/relative terms)?
-] What are the big picture items that have been introduced in the last 5 or 6 years that have driven up compliance costs in your business? In rank order, which ones are the most costly for your business? Why is this the case?¹
-] What are the most costly regulatory obligations for your business?
-] To what extent do you think your ongoing compliance costs represent costs over and above the costs of good business practice to promote your firm's reputation and ensure quality?
-] What value do you derive from being a regulated entity? What benefits of regulation are there to the market overall?
-] What types of expenses would be reduced in the absence of ASIC regulations?
-] What would be the extent of the reduction in costs in the absence of ASIC regulations (no difference, 0 – 10% less, 10 –25% less, 25 – 50% less, etc.)?
-] How do you see the evolution of compliance costs in the future?
-] How do the costs of the regulations that ASIC administers compare with other regulatory requirements you must meet (eg, APRA, ASX, ATO)?

Supplementary questions for global organisations

-] How do the costs of financial regulation in Australia compare with the costs you incur in other places?
-] Are there any particular areas where costs in Australia seem high compared to costs elsewhere?

¹ Respondents might raise items that are not within ASIC's remit – an example is the Anti-money laundering legislation or capital requirements. We are happy to hear about these items.

6. Business Areas Most Heavily Affected And The Associated Costs - Compliance In Detail

Refer back to Card (attached). Encourage respondent to discuss each of the cost categories that apply to their organisation (but use respondent classification if they think of costs in a different way).

(Note: In thinking about the cost categories, we are particularly interested in ongoing/ recurring costs. This should be the main emphasis of the conversation.)

-] What are the main cost categories? Please be as **concrete** as possible.
-] What is the exact nature of these costs? What aspects of the legislative and regulatory process have had the most adverse impact on these costs?
-] Are you able to separate specific one-off costs associated with planning for and implementing regulatory changes from ongoing/recurring annual compliance costs?
-] How do you calculate / evaluate what the costs are?
-] What proportion of these costs is incurred specifically to comply with regulatory requirements (i.e. costs that would not be incurred in the absence of the regulatory requirements)?
-] How do you separate costs associated with compliance from costs associated with good business practice?

7. Business Impact

For cost categories identified by the respondent:

-] How do these cost categories affect your business overall?
-] For example, have there been any negative impacts on products, services, or customers?
-] Is there anything you are not doing because of your compliance obligations? Did compliance obligations lead you to stop/ relocate/ outsource some activities?
-] How do compliance costs affect the nature and degree of competition in your industry?

-] Do you think innovation (e.g. development of new financial products) is being restricted in any way? If so, how? What exactly is stopping you?
-] What would change in the absence of ASIC regulation?

8. Summary and Final Suggestions: Identify and explore any suggestions as to how the burden of compliance costs should best be reduced (if they believe it should be).

-] What 3 – 5 things do you think ASIC should do to reduce your business costs?

9. Costs Not Incurred (If time available): For each individual cost identified as not applicable to this organisation, explore why this cost does not apply; i.e., determine whether this is a cost incurred but not one that is attributed to compliance costs, or whether it not incurred at all.

POTENTIAL TYPES OF COMPLIANCE COSTS

CATEGORY	SUB CATEGORY	APPLICABLE (YES / NO)
GOVERNANCE - Time spent by management & staff on compliance issues:		
Board		
Senior management		
Specific departments:	Compliance	
	Internal audit	
	Risk management	
	Legal	
	Other areas which may not be directly related; eg, IT, Finance & Accounting, HR, etc.	
DIRECT OPERATING COSTS		
Capital expenditure	IT software & hardware	
	Reporting systems	
	Compliance workflow	
	Generation of reporting / exception reporting	
	Electronic storage & retrieval	
	Other	
Staff & staff remuneration	Remuneration	
	Additional staff	
Administration & Enforcement		
Permissions & authorisations		
Education & Training		
Policies & procedures		

CATEGORY	SUB CATEGORY	APPLICABLE (YES / NO)
Publications & documentation		
Monitoring & record keeping		
Notification & Reporting		
Systems		
Other direct operating costs		
INDIRECT COSTS		
External Resources	Legal	
	Accounting	
	Insurance	
	Audit	
	Other consultancy services	
Customer related	Customer communications re products / processes	
	Other	
Opportunity cost	Management & staff time on compliance activities	
	Staff training time	
	Delay in development / introduction of new products	
	Uncertainty leading to inability to develop / introduce new products	
	Discontinuation of products / restriction of supply / limitation of product features, etc.	
	Need to explain regulatory requirements to clients – time; potential loss of client	

7.2 Appendix B: Letter To Respondents From ASIC



ASIC

Australian Securities & Investments Commission

MALCOLM RODGERS

Executive Director
Strategy

No. 1 Martin Place, Sydney
GPO Box 4866 Sydney NSW 1042
DX 653 Sydney

Telephone (02) 9911 2000
Facsimile: (02) 9911 2316

To Whom It May Concern

ASIC study on the costs of compliance

As part of its Better Regulation initiatives, and with the support of the Finance Council of Australia (FICA), the Australian Securities and Investments Commission (ASIC) is conducting a preliminary study on the cost impact of the regulatory framework we administer. We would be grateful for your participation in this study.

We have commissioned Chant Link & Associates to conduct the research. Chant Link & Associates has conducted a large amount of research in the finance industry over many years and is very familiar with the area.

We have asked Chant Link & Associates to conduct a survey and report to us on:

- industry perceptions about the overall costs of the regime ASIC administers;
- the overall size and direction of these costs (i.e. how they have changed over time);
- the business areas most heavily affected by regulatory compliance obligations; and
- how regulated businesses keep track of costs.

We will use the findings to deepen our understanding of the cost impact of our regulatory decisionmaking on business and to create a factual background for further ASIC-industry dialogue on cost and business impact issues.

To protect the confidentiality of respondents, FICA has agreed to provide the names of relevant businesses and contact persons directly to Chant Link & Associates. Chant Link & Associates will not disclose this information to ASIC.

We envisage reporting publicly on the results of this research but any information relating to you or your business will remain strictly confidential.

Your contribution to this study would be greatly appreciated.

Malcolm Rodgers
Executive Director, Strategy