



ASIC

Australian Securities & Investments Commission

Getting the right balance: ASIC's regulatory reform and deregulatory experience

*A speech by John Price, Commissioner,
Australian Securities and Investments Commission*

Progressing Regulatory Reform Conference

19 November 2014

CHECK AGAINST DELIVERY

Introduction

Thank you for inviting me to speak today, on what we at ASIC see as an important topic and a fundamental part of what we do.

Today I will draw on our experience at ASIC to speak about:

- how we balance our objectives of facilitating business and enforcing the law
- the hallmarks of good regulatory reform and how to develop a culture to support that, and
- finding ways to cut red tape.

How ASIC balances its statutory objectives of facilitating business and enforcing the law

Today I was asked to speak about how ASIC balances its *competing* statutory objectives of facilitating business and enforcing the law. But the truth is, we don't see these as competing objectives.

On enforcement, we believe a well-functioning regulatory framework will include appropriate enforcement as a necessary prerequisite to the efficient operation of business.

Markets cannot perform their fundamental purpose if investors and issuers do not have trust and confidence in them.

Regulation provides the framework for a resilient and dynamic financial system. It creates a system which all parties can feel confident participating in. Without this confidence, the financial system cannot fund the economy and allow for economic growth.

Enforcement considerations aside, ASIC also has a statutory obligation to facilitate and improve the performance of the financial system

We are obliged to do this in a way that reduces costs and supports commercial certainty and economic growth.

This in itself supports the businesses that are operating the system, but we are also required to facilitate and improve the performance of businesses in the same way.

This mandate – to both enforce the law and facilitate business – is reflected in our strategic priorities. These priorities are to promote investor and financial consumer trust and confidence, to ensure fair, orderly and

transparent markets, and to provide efficient and accessible registration of the people we regulate.

Enforcement, although a big part of our work, is just one tool in our toolkit. We have a multifaceted regulatory approach that includes assisting entities to comply where we can.

We do this in three key ways:

- through our relief and guidance
- through our work to improve financial literacy, and
- through our surveillance and enforcement.

Relief and guidance

We are empowered to give waivers (relief) from many parts of the laws we administer, to facilitate business where we can and where it is appropriate. When we do this, our guiding principle is that there should only be a small regulatory detriment in granting relief – and any detriment should be outweighed by the compliance cost savings to businesses or individuals. Looking to facilitate business in this seemingly small way can make a big difference. We estimate it results in compliance costs savings of tens of millions of dollars each year.

We also support business by providing detailed guidance on what they need to do to meet their obligations. We have a special focus on small businesses, who make up the vast majority of all businesses in Australia. For example, we have recently produced guidance material in a dedicated hub section on our website to help small businesses who might not have dedicated compliance staff.

Financial literacy

ASIC is responsible for financial literacy and the National Financial Literacy Strategy. We believe that consumers who are empowered with financial knowledge have the confidence to participate fully in the financial system. Money smart financial consumers can make better financial decisions, meaning the market for financial goods and services operates more efficiently and hopefully with less need for regulation.

Surveillance and enforcement

Our surveillance and enforcement work is critical in providing the foundation for a well-functioning financial system.

We take a risk-based approach to surveillance and enforcement, so that our actions are proportionate and appropriate.

We focus our resources on where we see the highest risk of harm to investors and financial consumers or markets, and where our action can have the greatest impact.

This means that our surveillance and enforcement actions are often directed at what regulatory writer Malcolm Sparrow calls the ‘sabotage of harms’. That is, not just punishing misconduct or identifying risk, but intervening where we can to eliminate problems.¹ This might be a problematic operator, practice or product.

Using this risk-based approach, only those participants or industries that present the most risk are typically targeted by us. This means less regulatory compliance burden on others.

We use around 70% of our regulatory resources on surveillance and enforcement. This is because, when investors or issuers are making decisions, it is not the strength of the underlying laws that matter the most, it is the confidence that these laws will be enforced.

Without clear punishment for breaking the law, without a regulator keeping an eye on potential trouble spots, bad behaviour is more likely to occur. Businesses doing the right thing will find it harder to compete with those that are not. And whether wrongdoing happens or not, investors and financial consumers cannot have trust and confidence in a system where enforcement is absent.

Fast and decisive action when the law is broken means bad apples are removed and all Australians can have confidence in the system.

Strong enforcement also levels the playing field, making competition between firms more effective, because it means that any competitive edge to be gained from operating outside the law is not worthwhile.

Appropriate penalties and the real risk of getting caught if you do the wrong thing create a powerful disincentive to engage in law-breaking behaviour.

That is why ASIC has released a paper to encourage discussion about what the penalties for corporate wrongdoing should be.² As our Chairman often says, penalties should create enough fear so that people won’t be greedy and break the law.

Our view is that penalties for doing the wrong thing should underpin a reliable financial system that works for the businesses that operate as part of it and for the investors and financial consumers who participate in it.

¹ MK Sparrow, *The character of harms: Operational challenges in control*, Cambridge University Press, Cambridge, England, 2008.

² Report 387 *Penalties for corporate wrongdoing* (REP 387).

The hallmarks of good regulatory reform and how to develop that culture

I will now move on to regulatory reform.

Financial regulation is not often compared to art museums, but when I read an article written by David Walsh – Walsh is the founder of Tasmania’s Museum of Old and New Art (MONA) – I was reminded of ASIC’s deregulatory and regulatory reform experience.

Walsh, when describing the process of developing MONA, said there is an easy way, and a hard way, to get something done:

The hard way is [to] have a vision and relentlessly pursue it ... The easy way is to start small and iterate. Imagination will only get you so far, perspiration helps, desperation is an essential tool, but iteration is the answer, at least for me.³

It’s a familiar sentiment and it is a great way to describe much of ASIC’s experience, both in regulatory reform and as we look for ways to cut red tape. While I don’t think we are lacking vision, a lot of our policy development is very much a process of iteration.

We see the most effective regulatory reform as reform that is designed to address a specific problem and to do that with the least intervention possible.

Ultimately, the best regulation is the kind that regulated entities want to comply with, because they know that it makes their own business better or that it makes the system as a whole better.

Critical to achieving this is defining the problem in the right way. At ASIC we have a number of fairly rigorous policy-making processes in place, particularly through our regulatory policy group – a key policy decision-making body – that encourage us to examine what the problem we are trying to solve is and what the options are for solving it.

Of course, broader Government regulatory impact assessment processes also encourage these same disciplines, and ASIC has historically been at the forefront of best practice regulation.

A rigorous approach to analysing the need for regulation, including building a strong evidence base, is also an important part of good regulatory reform.

At ASIC, we are increasingly using behavioural insights to inform our work and are using behavioural techniques, including in pilot trials to test whether

³ D Walsh, ‘Australian multi-millionaire gambler David Walsh spending his winnings to bring art to the people’, *Daily Telegraph*, 12 October 2014, www.dailytelegraph.com.au/news/australian-multimillionaire-gambler-david-walsh-spending-his-winnings-to-bring-art-to-the-people/story-fni0cx2y-1227085027762?nk=6f1d07b4e694c178a57f3acb82b60bed.

regulatory intervention is needed or to identify the best way to achieve our regulatory goals.

Transparency aids in building a strong evidence and support base for regulatory reform. Being transparent about what we are doing and how we are intending to do it not only reduces the risk of surprises, but it also means we are informed by the people who will have to work with the rules we make.

A major component of this is our strong focus on consultation. I cannot emphasise enough how critical consultation is to both understanding regulatory issues and to developing a solution. The policy documents ASIC produces and the legislative instruments we make are subject to wide, formal consultation. We also consult less formally both on individual issues and through our external advisory panel, our consumer advisory panel and our director advisory panel where appropriate.

But even in the best-case scenario of defining the problem and designing a solution in consultation with industry and consumer representatives, regulators and policy makers sometimes don't get it perfect the first time. Circumstances change and the archenemy of policy makers – unintended consequences – arise. So it is very important to continue to reflect on and review regulations.

Evaluation is essential, and mandatory processes like the sunseting of legislative instruments do mean that we review rules and relief to determine whether it remains fit for purpose, proportionate and appropriate.

I believe that ASIC's role in providing waivers from the law in appropriate circumstances is critical in creating good regulatory reform. We can use the law flexibly to accommodate businesses and transactions that weren't contemplated at the time of drafting the regulations, or where the law applies in a way that was not intended. This can encourage or remove barriers to innovation and ensure that the law has a proportionate impact on those entities it affects.

A good example of this is our work on employee share schemes. When we first provided this relief it was focused on less complex schemes – where employees were offered shares or options over shares in their listed company employers. But the world became more complex.

We reviewed our relief and guidance in light of market developments and changes to the tax environment.

We concluded that to meet our goal of facilitating employee incentive schemes where they are intended to enable employees to participate in the financial success of the company, we needed to make changes. You might

have noticed that we now call them ‘employee incentive schemes’, because they extend beyond just shares.

Following consultation, we expanded the types of products that can be offered, the categories of people who can participate and the structures that can be used when offering employee incentive schemes.

Of course, we are conscious that reducing the burden of regulation for businesses can come with a cost, and we are mindful that reducing red tape should not mean unduly shifting risk onto consumers and investors. As part of this expanded relief, we are ensuring that employees who are invited to participate in these schemes still receive adequate information to enable them to understand the terms and conditions of any offer.

Another big part of getting regulatory reform right is taking a proportionate, risk-based approach to policy and regulation that targets the behaviour that we want to prevent, but goes no further.

One way to create an environment where regulation is targeted and appropriate might be through a user-pays funding model for ASIC. This is intended to provide the economic incentives for business to achieve the Government’s policy outcomes in the most efficient way possible. If an industry sector knows they will need to pay to fix a regulatory issue it provides a great incentive for them to do it themselves rather than rely on Government to do so.

Looking for opportunities to cut red tape

And now to red tape.

As I’m sure you all know, the current Government has a target of \$1 billion in red-tape reduction each year. So, we have redoubled our efforts to remove red tape.

We have already made significant progress in contributing to the Government’s target. ASIC has reported more than \$60 million in compliance cost savings in the year to September 2014 alone.

ASIC has had a long-term commitment to cutting red tape. As I mentioned earlier, achieving regulatory outcomes while minimising compliance costs is part of our legislative mandate and is a fundamental part of our day-to-day work.

Having said that, cutting red tape and deregulating can be a challenge for regulators.

Without clear guidance from policy makers, there may be little incentive for regulators to reduce compliance costs where there is a possible detriment to the public. The question of what areas to focus on in cutting red tape becomes very important.

So, in making our own choices about what things to focus on we have sought input from across our organisation and across our regulated population.

We have found that there seems to be no single area of law or regulation that businesses are pointing to and telling us it is strangling them with red tape. It is more the cumulative impact of many regulations.

As a result, we are taking a multi-pronged approach to reducing unnecessary red tape. There are numerous ways where our work and the regulation we work with can either increase or decrease compliance costs for regulated entities.

It is often the people who are working day to day with businesses or with our forms that can see unnecessary processes or procedures. So, internally, we have taken a crowdsourcing approach. We encourage all members of our staff to identify opportunities to cut red tape and to send them in to our deregulation team.

We are also looking right across our work areas for opportunities to remove or reduce unnecessary red tape. We are doing this through:

- Our international work, where compliance cost savings can be achieved by overseas recognition of Australian laws and through our contribution to the development of international regulatory standards. For example, the work we are doing on OTC derivatives.
- We are upgrading ASIC systems, including our website, which has been overhauled to increase accessibility and save time and effort for businesses and individuals searching for information.
- We also provide relief (waivers) – which, as I mentioned earlier, enables the law to accommodate innovation or unanticipated outcomes.
- Through ongoing guidance we provide, which helps reduce the cost of complying with regulation – such as recent guidance we have released following a court decision on responsible lending.⁴
- And, finally, through recommending potential law reforms to the Government when we identify changes that might reduce business costs while maintaining an appropriate level of regulation for investors and financial consumers.

⁴ Regulatory Guide 209 *Credit licensing: Responsible lending conduct* (RG 209).

Another important example of the work we are doing to reduce compliance costs is re-evaluating the data and information we collect.

Last year we went through a process of looking at all the data we collect from business in forms lodged with us and how that data was used. We found that most of the information we collect is used in our regulatory functions. But we did identify:

- some information that we collect, but no longer need
- some forms that are redundant or obsolete, and
- some places where we can collect information in a smarter way.

Through this we identified a list of approximately 10% of our forms to remove or streamline. We took this list to consultation. As a result of consultation, we learned that some of the information we do not use is used by others and may have a benefit. We are reconsidering whether these forms can be removed.

But we have already started on removing some of the other forms, representing over \$300,000 in savings for industry, and we will likely request that the Government remove some that are fixed in legislation.

Beyond this, we are currently working through the 30 or so submissions we received in response to our public request for deregulatory ideas, and we are always open to hearing where and how we can make it easier for business to meet our regulatory outcomes. We are listening to the businesses we regulate to identify where there are opportunities to do this.

We are also committed to more transparency. One example of this is the recent publication of our Strategic Outlook. The precursor to a more comprehensive Strategic and Risk Outlook, this document provides clear guidance on what is driving our work.

We are also strongly supportive of objective measures of our performance against our mandate. This will partly come, along with more transparency, from the Government's new regulator performance framework. This framework is designed to give Governments and the public more clarity and insight to how regulators like ASIC interact with the regulated population. Over time, it is hoped this will minimise the impact that administering the law has on the regulated population.

We will start reporting from the end of financial year 2015–16 on how we are performing against the framework's key performance indicators (KPIs), which are:

- not unnecessarily impeding the efficient operation of regulated entities
- clear, targeted and effective communication
- proportionate actions

- streamlined and coordinated compliance and monitoring
- openness and transparency, and
- contributions to the continuous improvement of regulatory frameworks.

While it will be a different way of reporting, these KPIs largely reflect our own standards and approaches to dealing with our regulated population.

Conclusion

I'd like to finish by emphasising that, overall, we should not forget that regulation generally exists for good reason.

Regulation is necessary to support the operation of our financial system. Good regulation, good administration of regulation and strong enforcement results in a system people and businesses can feel confident about participating in. That in turn means the system can work to do its job of funding the economy to support and drive growth.

But, of course, there are always ways we can do this better and more efficiently.

It starts with asking the right question and having the processes in place to analyse and assess the right policy approach. This includes consultation from very early in the policy development process. It ends with an ongoing review process. That means having the courage to say that we no longer need this regulation if it does not address the problem, if the problem is no longer there or if it is a disproportionate solution.

But, of course, it never really ends. By taking an iterative approach to policy development, we can have a regulatory framework that builds on the past and accommodates the future to meet the needs of all of its participants.

It means we can apply what we have learned as business and markets change and as new techniques, such as behavioural economics, gain currency.

Finally, the way we go about administering regulation does matter. Cutting red tape is not just about removing regulatory obligations. We have been looking at every interaction we have, all of the aspects of compliance, to make sure that what we are asking or imposing serves the purpose it was intended to and does so in the most efficient way.