3

ASIC’s achievements by sector

Purpose and structure

This section of the report discusses activities and outcomes achieved for each industry funding sector this financial year, to help stakeholders better understand the regulatory effort we expended in their subsector.

Industry funding

ASIC industry funding means that those who create the need for regulation bear the costs of that regulation. Under the model, entities pay a share of the costs to regulate their subsector through industry levies, which are based on a range of business activity metrics. The model provides a reasonable indication to industry year on year about the levies to be paid. Any changes to the model over time will have an impact on the costs of regulation recovered from each sector.

We published our indicative industry levies for 2018–19 as part of our Cost Recovery Implementation Statement (CRIS) in June 2019. The CRIS explains how the costs of ASIC's regulatory activities will be recovered from each sector. The CRIS is available on our website.

Publication of this information helps industry better plan for the actual levy for 2018–19, which is billed in January 2020 after ASIC's regulatory costs are published and business activity metrics for each subsector are provided by regulated entities.

Under industry funding, there are seven sectors (deposit-taking and credit; insurance; financial advice; investment management, superannuation and related services; market infrastructure and intermediaries; corporate; and large financial institutions) and 52 subsectors.

For ASIC achievements by regulatory tool, see Chapter 2.

3.1 Deposit-taking and credit

The deposit-taking and credit sector comprises **credit licensees** (credit providers and credit intermediaries), **deposit product providers**, **payment product providers**, and **margin lenders**.

ASIC's work in this sector during 2018–19 focused on responsible lending and ensuring that consumers are sold products that are appropriate for their needs.

Credit providers

Credit card project

In July 2018, we released Report 580 *Credit card lending in Australia*, which reported that more than one in six consumers were struggling with credit card debt.

Our review analysed over 21 million credit card accounts from 12 credit providers between 2012 and 2017.

We found that:

- in June 2017, there were almost 550,000 people in arrears, an additional 930,000 people with persistent debt, and a further 435,000 people repeatedly repaying only small amounts
- consumers could have saved $621 million during the 12 months to June 2017 if they had carried their balance on a card with a lower interest rate
- over 30% of consumers who transferred their balance to a new credit card increased their debt by 10% or more during the promotional period and 63% of consumers did not cancel a card after a balance transfer
- four credit providers continued to apply old repayment allocation rules for some or all credit card contracts entered before July 2012. We estimate that almost 525,000 consumers were charged more interest as a result.

During our review, the Government passed legislative reforms which included:

- tightening the responsible lending requirements for credit cards, by introducing a requirement that a credit card contract be assessed as unsuitable if the consumer was unable to repay the credit limit within a period prescribed by ASIC. In September 2018, following our review, we prescribed a three-year period
- strengthening the existing prohibition on unsolicited credit limit increase offers
- changes to interest calculations, particularly when applying interest charges retrospectively
- the right to request credit limit reduction and card cancellation online.

In addition to implementing the responsible lending reforms, we required industry to improve issues with conduct and outcomes that we identified in our review. In December 2018, we reported on changes being made by providers to help consumers with credit card debt. This included requiring providers to:

- trial proactive steps to help consumers with potentially problematic credit card debt or who are failing to repay balance transfers
- restrict the amount by which consumers may exceed their credit limit to 10% of the limit
- allocate repayments for all credit cards in the more favourable way required for cards entered into after July 2012.

We will monitor compliance with the new requirements and commence a follow-up review in 2020–21.

Unfair contract terms protections for small business borrowers

In September 2018, we announced that, following ASIC's review, Prospa Advance Pty Ltd (Prospa) changed loan terms in its standard form small business loan contract to address terms being unfair to small business borrowers.

The changes included addressing problematic terms of the kind outlined in ASIC Report 565 *Unfair contract terms and small business loans*, and changes to other terms that could have operated unfairly for borrowers and guarantors. For example, Prospa amended its early repayment clause so that:

- borrowers may repay their loan early without requiring Prospa's consent
- if borrowers repay their loan early, Prospa will provide a discount on the remaining interest payable (previously, Prospa had an absolute discretion to provide a discount if borrowers repaid early).

Prospa agreed that all customers who entered into or renewed contracts from 12 November 2016 would have the benefit of these changes.

Reverse mortgage providers

In August 2018, we published Report 586 *Review of reverse mortgage lending in Australia*, as part of ASIC's work for older Australians. Our report identifies that although there is an important role for such products, there is a risk that some borrowers may not recognise the longer-term impact on their future financial needs.

Importantly, we also found that the enhanced consumer protections introduced for reverse mortgages in 2012 have reduced risks to consumers. These protections include a 'no negative equity guarantee' that protects borrowers from owing more than the market value of their property, a presumption of unsuitability for high loan-to-value ratios, and additional obligations to inquire about the needs and objectives of potential borrowers.

We analysed data on 17,000 reverse mortgages, 111 loan files, lender policies and procedures, and complaints. We also commissioned in-depth consumer research interviews with 30 randomly selected borrowers and consulted over 30 industry and consumer stakeholders.

Our review found that lenders needed to make more detailed inquiries about consumers' requirements and objectives, including how a loan would affect their future financial needs, tenancy protection and pension income. We identified potentially unfair contract terms, such as unilateral variation clauses and non-monetary default clauses, which entitled a lender to take action disproportionate to the related breach. Lenders have now acted to remove these types of clauses from their loan contracts.

We also formed a working group involving lenders and industry participants to improve lending practices, and we are trialling a comprehension testing regime to monitor consumer outcomes in this industry.

Small and medium amount credit providers

We continued to act against non-compliance with responsible lending obligations under consumer credit laws. This year, we focused on offers of high-cost credit and the consumer leasing industry. We also examined emerging products that give consumers additional payment options but are not regulated credit and may potentially cause consumer harm.

Local Appliance Rentals Pty Ltd

In November 2018, after ASIC identified concerns about compliance with responsible lending obligations and supervision of franchisees, Local Appliance Rentals paid infringement notices totalling $157,500. We also obtained a court enforceable undertaking from Local Appliance Rentals to remediate consumers for past practices, appoint an independent compliance consultant, and pay a community benefit payment of $100,000.

Local Appliance Retails leased household goods, including to low-income consumers, recipients of payments from Centrelink, and people in regional and remote Australia. The remediation included refunds of excess payments and excessive late fees.

Buy now pay later arrangements

This year, we continued to examine emerging products that give consumers additional payment options but can potentially cause consumer harm.

In November 2018, we released Report 600 *Review of buy now pay later arrangements*, ASIC's first review of this rapidly growing industry.

Buy now pay later arrangements allow consumers to buy and receive goods and services immediately but pay for their purchase over time.

Buy now pay later

MERCHANTS

In just two years...

50x more merchants with Zip Pay

45x more merchants with Afterpay

CONSUMERS

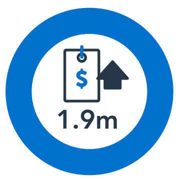
400,000 FY16

2 million FY18

REVENUE OF PROVIDERS

$32 million Q2 2016

$78 million Q2 2018



TRANSACTIONS

June 2016 80,000

June 2018 1.9 million

We identified signs that some consumers, including many young people, are already struggling with too much debt from these arrangements. We also found that some buy now pay later arrangements resulted in the price of goods being inflated and some had influenced consumers to spend more overall.

Only one of the six providers in our review examined the income and existing debts held by consumers before providing its services. After feedback from ASIC, all six providers changed some of their practices to help consumers stay in control and make informed decisions about their purchases and payments.

The buy now pay later industry will be an area of ongoing focus for ASIC, while we monitor whether additional protections are required.

Previously, ASIC's jurisdiction to regulate conduct and address risks to consumers who use these kinds of products was limited. This was one of the reasons we supported the extension of ASIC's proposed product intervention power to all credit facilities regulated under the ASIC Act. These new powers came into effect in April 2019.

Credit intermediaries

Ban on flex commissions in car finance market

Our ban on flex commissions in the car finance market came into force on 1 November 2018. Flex commissions were paid by lenders to car finance brokers, allowing the car dealer to set the interest rate on the car loan. Dealers would earn a larger commission on loans with higher interest rates, leading to vulnerable consumers paying excessive interest rates on their loans. We are monitoring lenders' compliance with the ban, which we expect will result in consumers being charged lower interest rates and will end exploitative pricing practices.

Deposit product providers

Review of deposit accounts with third-party access

In August 2018, we announced that following a review by ASIC, five banks would improve compliance measures and controls for deposit accounts that can be operated by a third party, such as a financial adviser. Our report, Report 584 *Improved protections for deposit accounts with third-party access*, identified that banks needed to do more to manage the risks to customers arising from third parties having access to money in the accounts.

The banks involved agreed to improve their practices, including by:

- ensuring that account application forms and communications are clearer
- improving the monitoring of advisers' use of the accounts and their transaction requests
- analysing any fraud that occurs on the accounts and remediating customers who have lost funds due to unauthorised transactions.

Approval of Banking Code

In June 2019, ASIC approved the first stage of changes to the Australian Banking Association's (ABA's) new Banking Code of Practice. The changes include:

- new provisions to ensure that a bank will not charge fees for services to deceased customers, where services are no longer being provided to that customer's estate
- changes to the commitments around the provision of valuations to small business customers
- changes to reflect ASIC's implementation of law reforms to credit card responsible lending.

The new Code commenced on 1 July 2019.

All ABA member banks will be required to subscribe to the Code as a condition of their ABA membership. The protections in the Code will form part of the banks' contractual relationships with their banking customers.

ASIC will decide on further changes to the Code in 2019 after consultation with key stakeholders. These further changes are designed to address recommendations of the Royal Commission and relate to the accessibility of banking products and services for vulnerable consumers, the charging of default interest on agricultural loans in the event of natural disasters, and various small business protections.

Payment product providers

Review of the ePayments Code

In March 2019, we published Consultation Paper 310 *Review of the ePayments Code: Scope of the review*, seeking feedback on the topics we propose to include in our review of the ePayments Code. We are undertaking the review to ensure that the Code continues to be effective and relevant to consumers and Code subscribers. In light of significant continuing developments in financial technology and innovation, a key focus of consultation has been consideration of options to future-proof the Code.

3.2 Insurance

The insurance sector comprises life and general insurance and includes **insurance product providers** (including friendly societies), **insurance product distributors**, and **risk management product providers**.

This year, ASIC continued to focus on the sale of inappropriate products and the way products are sold. We undertook targeted reviews, building on previous work to raise industry standards, and introduced new levels of transparency to enable consumers to make more informed decisions.

Insurance product providers

Life insurance claims data

In a world-first initiative in March 2019, APRA and ASIC published life insurance data and an online tool that allows consumers to compare life insurers' performance in handling claims and disputes. The latest data was released in June 2019, covering the 12 months to December 2018.

The launch of the online life insurance tool with Sean Hughes and Geoff Summerhayes from APRA.

Consumers may now review an individual life insurer's claims and disputes outcomes and compare them against other insurers and the industry average. The full set of published data may be accessed on APRA's website and the life insurance claims comparison tool is available on ASIC's MoneySmart website. As a result, consumers may compare each insurer's:

- claims-acceptance rates
- average claim time
- number of claims-related disputes
- policy cancellation rates.

This level of transparency and accountability plays a critical role in increasing demand-side pressure and improving trust in financial services.

Insurance product distributors

Consumer credit insurance

This year, our work to address the inappropriate sale of consumer credit insurance (CCI) focused on ensuring that consumers who have been harmed are remediated, CCI products offer consumers better value, and sales practices comply with our requirements.

In 2018–19, ASIC identified a range of consumer harms, including:

- an average claims ratio of 19 cents in the dollar for CCI sold with personal loans and home loans, and 11 cents in the dollar for CCI sold with credit cards
- consumers being sold CCI despite being ineligible to claim against one or more types of cover
- the use of pressure selling techniques or other unfair sales practices
- consumers receiving inappropriate personal advice under a general advice model for the purchase of unsuitable policies
- consumers being charged incorrect premiums for their CCI policy.

We have addressed the problems we identified by:

- commencing enforcement investigations into the sales practices of several firms
- requiring lenders and insurers to undertake large-scale remediation programs for consumers who have suffered harm. ASIC estimates that lenders and insurers will collectively pay in excess of $100 million to over 300,000 consumers
- consulting on banning the unsolicited outbound telephone sales of CCI, due to the consumer harms we have seen as a result of this practice
- requiring lenders and insurers to comply with new and strengthened minimum standards when offering CCI products
- expecting all lenders to incorporate a four-day deferred sales model for all CCI products sold across all channels (not just lenders that subscribe to the Banking Code of Practice).

We published a report on the findings of our work on 11 July 2019.

Sale of direct life insurance

In August 2018, ASIC published Report 587 *The sale of direct life insurance* and Report 588 *Consumers' experiences with the sale of direct life insurance*, after reviewing various products, including term life, accidental death, trauma, total and permanent disability, and income protection insurance. Direct life insurance sales are often made by telemarketing, online or face to face, including through bank branches. The review explored whether and how the design and sale of these products contribute to poor consumer outcomes.

Our review found:

- high cancellation rates and poor claims outcomes: a sign that people are being sold products they do not want or cannot afford, or that are not right for them
- three in five of all policies sold were cancelled within three years
- of the claims we looked at:
  - 58% of claims were accepted
  - 15% of claims were rejected
  - 27% of claims were withdrawn
- some products offered little value to customers – for example, accidental death insurance had a claims ratio of 16.1%, meaning that for every dollar paid in premiums only 16 cents was paid in claims.

Our report made clear our expectations, namely that:

- the outbound selling of life and funeral insurance will be restricted
- firms stop selling products that do not meet the needs of consumers
- firms respond and raise standards through their code of practice.

We will intervene and take enforcement action if industry does not stop selling poor value products.

Sale of add-on products through car yards

This year, we finalised further refund programs from Aioi Nissay Dowa Insurance Company Australia (ADICA), Eric Insurance, Virginia Surety Company, Sovereign Insurance Australia, LFI Group and NM Insurance for insurance products sold by motor vehicle dealers, including guaranteed asset protection (GAP) insurance, consumer credit insurance, extended warranty, and tyre and rim insurance. This brings the total customer refunds to over $130 million.

These insurance providers refunded sales of insurance offering low or no value to consumers – for example, because they were ineligible to claim at the time the policy was sold to them, or because unnecessary life insurance was sold to young people with no dependants.

Our engagement with industry contributed to significant changes in the add-on market, including:

- a reduction in commissions paid to dealers, from a maximum of 75% of the premium to around 20%
- an increase in claims paid compared to premiums paid – for example, the average loss ratio for both GAP and CCI across the three main insurers has doubled since 2016–17
- improvements to product design
- the introduction of knock out questions by car dealers to check that the customer is eligible under the policy before it can be sold to them
- some insurers ceasing to sell some add-on products, and four insurance providers exiting the market completely.

Insurance claim investigations

In 2018, at a workshop hosted by ASIC, regulators and industry stakeholders analysed and discussed proposed mandatory minimum standards for claim investigations for inclusion in the General Insurance Code of Practice, with the aim of addressing consumer harms from investigation practices.

This year, ASIC gathered data on the number of comprehensive motor vehicle claims investigated over a one-year period, and the outcome of the claims. We found that:

- over 71% of claims investigated are found to be valid and are paid out
- only 4% of investigated claims are declined due to fraud, revealing a very high 'false positive' rate for suspected fraudulent claims
- 15% of investigated claims are withdrawn.

We proposed a set of mandatory minimum standards to address identified consumer harms related to the investigation process. The minimum standards seek to ensure that insurers maintain active, timely and visible oversight of claim investigations, claims are assessed in a reasonable time, and consumers have the support they need.

In July 2019, we published Report 621 *Roadblocks and roundabouts: A review of car insurance claim investigations*, a report on the findings of our work on insurance claim investigations.

3.3 Financial advice

The financial advice sector includes **AFS licensees and their representatives** who provide **personal advice or general advice to retail and/or wholesale clients**.

In 2018–19, ASIC's work in this sector focused on remediating consumers who were charged fees for no service, licensee oversight, understanding consumer awareness around general financial advice, and banning advisers engaging in misconduct.

Financial advisers

Charging clients without providing advice

In 2018–19, we continued to supervise the remediation of customers of ANZ, AMP, CBA, Macquarie Bank, NAB and Westpac who were charged annual fees for services, including an annual advice review, which were not provided (fees for no service).

This work resulted in significant compensation being paid, or to be paid, to affected customers. As at 30 June 2019, the banks have collectively provisioned around $1.7 billion for fees-for-no-service remediation.

In August 2018, we released Information Sheet 232 *Fees for no service: Remediation* to assist licensees in remediating clients. Our media release of 11 March 2019, 19-051MR *ASIC provides update on further reviews into fees-for-no-service failures*, publicly disclosed the status of the banks' further reviews in relation to fees for no service and further set out ASIC's expectations of remediation programs.

Mind the Gap (Report 614)

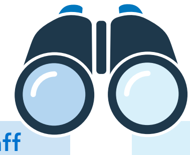
In March 2019, ASIC published Report 614 *Financial advice: Mind the gap*, which analysed consumer awareness and understanding of the differences between personal or general financial advice.

ASIC's research revealed that many consumers confuse general and personal advice, exposing them to greater risk of making poor financial decisions. For example, despite receiving a general advice warning, many Australians receiving general advice may incorrectly think that:

- their personal circumstances have been taken into account, and/or
- the adviser has an obligation to act in their best interests when providing the advice.

Factors that can influence how consumers perceive advice

Consumers are more likely to perceive advice that …



is from **customer service staff**	is from **more qualified staff**
is from **mass media** (e.g. TV, radio)	is from a **face-to-face appointment**
is a **sales** or **marketing recommendation**	requires the **consumer to provide personal information**
has **no fees**	has **upfront fees**
is about **'less personal'** topics (e.g. term deposits)	is about **'more personal'** topics (e.g. superannuation)
… as **general advice**	… as **personal advice**

ASIC is commissioning further research that will seek to identify a more appropriate label for general advice, or different labels for general advice provided in different circumstances, and will consumer test different versions of the general advice warning.

Solar Financial Advisory Pty Ltd AFS licence cancellation

In November 2018, ASIC cancelled the AFS licence of Sydney-based Solar Financial Advisory Pty Ltd (Solar), following a surveillance relating to concerns about licensee oversight. ASIC found that Solar had failed to:

- manage conflicts of interest. A Solar representative had recommended that clients establish SMSFs to invest in a private development company owned and administered by the representative and the representative's associated companies. It was found that Solar had failed to:
  - undertake adequate background checks on its representatives to identify and test potential conflicts of interest
  - update and test personnel information on an ongoing basis
  - train its representatives on conflicts of interest
  - have adequate arrangements to manage conflicts of interest
- ensure that its representatives complied with financial services laws, by failing to provide appropriate oversight
- properly monitor and supervise its representatives
- maintain adequate human and financial resources
- adequately manage its internal dispute resolution process, by failing to acknowledge and/or record complaints and properly communicate with complainants.

The cancellation of Solar's AFS licence forms part of ASIC's ongoing efforts to improve standards across the financial services industry.

Adviser bannings

ASIC takes administrative action, such as banning individual advisers, to protect investors and consumers and to deter misconduct.

This year, the Financial Advisers team banned 11 advisers from providing financial services.

Bans imposed in 2018–19 include:

- **Peter Anthony Chigwidden:** Mr Chigwidden was banned from providing financial services for five years. ASIC found that he had consistently failed to address the stated needs and objectives of his clients and as a result did not provide advice that was in their best interests. When advising clients on product switching, he failed to adequately consider the cost impact or other consequences of that advice, leaving clients poorly informed. Crucially, the switching advice failed to show that the recommended products better met the clients' needs than their existing products.
- **Subeer Luthra:** ASIC permanently banned Mr Luthra from providing financial services and engaging in credit activities as a result of his dishonest conduct. ASIC was notified of Mr Luthra's misconduct by Westpac. Mr Luthra advised his clients to switch their superannuation to a product issued by BT (part of the Westpac Group), and to obtain comprehensive personal insurance, without taking their needs and objectives into consideration. He also recommended BT insurance and superannuation products to all his clients without adequately investigating their existing financial products. The advice resulted in Mr Luthra's clients paying excessive premiums that eroded their superannuation contributions at a point in their lives when they did not have time to rebuild their assets for retirement. ASIC found that Mr Luthra is not of good fame or character to provide financial services because his conduct was dishonest and deliberate, and motivated by personal enrichment. ASIC also determined that Mr Luthra is not a fit and proper person to engage in credit activities.

3.4 Investment management, superannuation and related services

The investment management, superannuation and related services sector includes **superannuation trustees**, **responsible entities**, **wholesale trustees**, **operators of notified foreign passport funds**, **custodians**, **investor directed portfolio service (IDPS) operators**, **managed discretionary account (MDA) providers**, **traditional trustee company service providers**, and **crowd-sourced funding intermediaries**.

In 2018–19, ASIC focused on the responsibilities of superannuation trustees to consumers in relation to insurance offered through superannuation and dispute resolution. These are both areas in which significant legislative change occurred during the year.

Our regulatory work and the Royal Commission highlighted the importance of trustees properly overseeing advice fee deductions from superannuation accounts. To help consumers understand product fees and costs, we consulted on changes to the fee and cost disclosure requirements applying to superannuation and managed investment products in Consultation Paper 308 *Review of RG 97 Disclosing fees and costs in PDSs and periodic statements*. This followed the release of Report 581 *Review of ASIC Regulatory Guide 97: Disclosing fees and costs in PDSs and periodic statements*, an external review of these requirements involving extensive industry engagement.

Our work in the managed funds sector ranged from investigating illegal conduct and pursuing compensation for investors, to identifying compliance failures and monitoring the rectification process or taking action to address non-compliance. We also worked with industry to facilitate good business practices, issued revised guidance, released the findings of sector surveys to improve understanding of these sectors, and undertook thematic reviews about MDAs and IDPSs.

Superannuation trustees

ASIC is primarily responsible for ensuring that superannuation trustees meet certain obligations in their dealings with consumers, including disclosure and advice to members, and ensuring that members have access to complaints processes.

Insurance in superannuation

Millions of Australians hold insurance through superannuation, yet this insurance is not always delivered in a way that meets consumer expectations. In September 2018, we released Report 591 *Insurance in superannuation*, our review of the insurance arrangements of 47 superannuation trustees. The report identified improvements needed across the industry in relation to:

- claims processes and complaints handling
- disclosure
- defaulting of consumers into smoker premium rates in the absence of information that the consumer is a smoker.

We have been monitoring, through public information and onsite visits to trustees, the industry's progress in implementing the Insurance in Superannuation Voluntary Code of Practice. This Code aims to improve product design, consumer understanding, and complaints and claims processes for consumers. At the end of 2018–19, 62 trustees have publicly indicated that they are adopting the Code.

This year, we also focused on ensuring that automatic smoker defaults do not apply to any public offer superannuation funds. ASIC considers that the practice of automatically defaulting members as 'smokers' when setting premiums is unacceptable, because high premiums can significantly erode members' retirement benefits. Our work resulted in trustees who we identified as automatically defaulting new members as smokers ceasing this practice.

Dispute resolution arrangements for superannuation

We identified through our insurance work long timeframes for the resolution by some trustees of complaints concerning insurance claims. This can impact consumers when at their most vulnerable. We consider that superannuation trustees' approach to internal dispute resolution (IDR) provides a meaningful measure of the way trustees treat their members and whether they act in their members' best interests.

We investigated trustees with insurance complaint response timeframes beyond 90 days, to identify the drivers of complaints and what improvements were being made to IDR practices. We gave feedback to individual trustees and published our findings in industry publications. In May 2019, we released Consultation Paper 311 *Internal dispute resolution: Update to RG 165*, on IDR requirements. It proposes a shorter timeframe for dispute resolution (45 days) and improved practices to deal with complaints.

We continued to engage with trustees about their failure to provide adequate written reasons in response to complaints about death benefit payments. This led to improvements in trustee processes, including updated template letters and additional employee training. As well as promoting trustee accountability and consumer confidence, proper written reasons can help a consumer decide whether to escalate their complaint to external dispute resolution.

We also took steps to ensure that trustees acted to help consumers access the appropriate external dispute resolution body.

From 1 November 2018, the Australian Financial Complaints Authority (AFCA) became the dispute resolution body responsible for resolving superannuation complaints. Before this, superannuation complaints were considered by the Superannuation Complaints Tribunal. We followed up with individual trustees who were slow to join AFCA to ensure that they did so ahead of 1 November 2018.

We also contacted 46 trustees, with a collective membership of over 6.6 million Australians, that had inadequate disclosure on their websites about AFCA's role in complaints management. These trustees subsequently updated their consumer-facing disclosure, so members had easy access to information about their right to contact AFCA. In the first six months of AFCA's operation, superannuation complaints accounted for 9% of all complaints received by AFCA.

Responsible entities

ASIC is responsible for ensuring that responsible entities meet their obligations to members. We undertake proactive supervision and surveillances of responsible entities that have been identified through our threat, harm and behaviour framework as being most likely to cause harm or potential harm to consumers, investors, and fair and efficient markets.

Endeavour and Linchpin

ASIC obtained orders that Endeavour Securities (Australia) Limited (Endeavour) and Linchpin Capital Group Limited (Linchpin) be placed into liquidation and that receivers be appointed over the assets of a registered scheme operated by Endeavour and an unregistered scheme operated by Linchpin into which the registered scheme was invested.

Endeavour and Linchpin are related entities. Linchpin on-lent the funds to directors, related entities and authorised representatives who recommended that clients invest in these schemes, generally on an unsecured basis. The court found that Endeavour:

- did not act in the best interests of the members of the registered scheme
- failed to provide financial services efficiently, honestly and fairly
- failed to exercise due care and skill as a responsible entity
- engaged in related party transactions without member approval.

In total, the registered scheme received $17.3 million from 131 investors. There were 41 investors in the unregistered scheme, which had assets of $21.2 million.

Australian Mutual Holdings Limited

Following an ASIC investigation, on 17 April 2019, ASIC's Financial Services and Credit Panel banned Jeffrey Worboys and Matthew Barnett from providing financial services for six years. Mr Worboys and Mr Barnett were joint executive officers and directors of Australian Mutual Holdings Limited (AMHL).

ASIC found that Mr Worboys and Mr Barnett did not exercise the degree of care and diligence required and failed to act in the best interests of the members of the Courtenay House Capital Investment Fund, which was operated by AMHL. This included a failure to ensure that the persons responsible for trading funds had the requisite qualifications and experience to manage a foreign exchange and derivatives fund.

Infringement notices related to exchange-traded bonds

Australian Corporate Bond Company Pty Ltd (ACBC) paid $25,200 in penalties after ASIC issued two infringement notices for alleged misleading statements made in the promotion of exchange-traded bonds on the ACBC website between May and December 2017.

We were concerned about ACBC's misrepresentation about term deposits and exchange-traded bonds carrying a similar risk while producing a higher return. For example, investments in a term deposit of up of $250,000 are protected by the Australian Government guarantee for authorised deposit-taking institutions, while investments in exchange-traded bonds are not.

Interim and final stop orders for schemes involving defective disclosure

This year, we also issued interim and final stop orders in respect of Product Disclosure Statements relating to offers of interests in property development schemes, a mortgage scheme and an initial coin offering (ICO) where we found disclosure to be defective. We also reviewed disclosure by exchange-traded funds to identify defective disclosure.

Cancelled licences

We cancelled the AFS licence of CWS Mortgages Ltd for failing to comply with professional indemnity insurance requirements and of Vesta Living Communities Ltd for failing to fulfil its organisational competence and financial resource requirements.

Guidance

This year, to improve our understanding of the market, we commenced a pilot program to collect recurrent data for all registered managed investment schemes and reviewed our regulatory settings against IOSCO recommendations about liquidity in collective investment vehicles.

We released reports in relation to crowd-sourced funding intermediaries (Report 616) and marketplace lending providers (Report 617). These reports provide a deeper understanding of new and existing business models, as well as insights into our monitoring of activity levels and assessment of risks in these sectors.

We also revised Information Sheet 157 *Foreign financial services providers – practical guidance*. This information sheet provides guidance for foreign financial services providers seeking to provide services in Australia.

In addition, we reissued class order relief for business matching services and out-of-use notices for warrants.

Wholesale trustees

We continue to monitor and conduct risk-based surveillance of compliance by wholesale trustees with their licence conditions and any conduct that may result in harms to investors. Our subsequent actions have included addressing misleading and deceptive statements about an ICO offering, requiring amendments to promotional materials in relation to statements about past performance, requiring additional measures to manage processes for certifying wholesale clients, and causing the voluntary cancellation of an AFS licence.

We also reissued Regulatory Guide 192 *Licensing: Wholesale equity schemes* due to the sunsetting of the existing relief. The revised guidance relates to amendments to the existing relief to take into account a strengthening of financial and custody requirements in 2013.

Managed discretionary account providers and platforms

We began a review of the market practices of MDAs and platforms to identify issues affecting consumer outcomes in this growing sector of the market – for example, transparency and conflicts of interest.

3.5 Market infrastructure

The market infrastructure sector includes **Australian market licensees**, various types of **market operators**, **benchmark administrators**, **clearing and settlement (CS) facility operators**, **Australian derivative trade repository operators**, **exempt market operators**, and **credit rating agencies**.

ASIC's work in this sector during 2018–19 continued to focus on improving the effectiveness of Australia's capital markets. This included technology governance and operational risk management for market operators, supporting legitimate crypto-asset businesses to operate lawfully in Australia through direct feedback to firms, ongoing oversight of and policy development for clearing and settlement facility operators, implementation of the tiered market licensing regime, publication of the Yieldbroker (OTC trading platform) report, and implementation of an oversight model for benchmark administrators.

Large securities exchange operators

Market integrity rules for technology and operational resilience

In September 2018, following an extensive review with the assistance of KPMG and the Reserve Bank of Australia (RBA), ASIC published Report 592 *Review of ASX Group's technology governance and operational risk management standards*.

In June 2019, we released Consultation Paper 314 seeking feedback on proposed market integrity rules for securities and futures market operators, and market participants, to promote the resilience of their critical systems. Failures of critical systems can severely impact market integrity, and it is important that we update the rules to align with changes in the technology and processes that underpin financial markets, particularly as the multimarket environment for Australian listed securities creates interdependencies between participants and operators, and the outsourcing and offshoring of critical systems is becoming more prevalent.

The proposed rules apply to both the securities and futures markets and address:

- maintaining critical systems
- change management in relation to critical systems
- outsourcing
- risk management, and data and cyber security
- incident management and business continuity planning
- governance and resourcing
- fair access to markets and trading controls.

Supporting legitimate crypto-asset business in operating lawfully

To support legitimate crypto-asset business in operating lawfully in Australia, we updated Information Sheet 225 *Initial coin offerings and crypto-assets*. Crypto-assets such as cryptocurrency, or tokens, are created and dispersed using distributed ledger technology, sold through initial coin offerings (e.g. to raise capital to fund projects), and traded on crypto-asset trading platforms.

The technology surrounding crypto-assets can be complex and can fall under the jurisdiction of several regulatory agencies. Information Sheet 225 reinforces the obligation on crypto-asset businesses to avoid misleading and deceptive conduct whether or not the crypto-asset is or involves a financial product. Information Sheet 225 also provides high-level regulatory signposts as a starting point to help crypto-asset participants comply with the obligations administered by ASIC.

ASIC has taken action to stop several proposed initial coin offerings or token-generation events (together, ICOs) targeting retail investors. We have stopped the issue of a Product Disclosure Statement for a crypto-asset managed investment scheme, and on five other occasions since April 2018 have acted to prevent ICOs raising capital without the appropriate investor protections. These ICOs have been put on hold and some are considering how to restructure to comply with relevant legal requirements.

Clearing and settlement facility operators

Chicago Mercantile Exchange

On 26 February 2019, the overseas CS facility licence of the Chicago Mercantile Exchange (CME) was varied to authorise it to provide central counterparty services to the licensed exchange-traded derivatives market to be operated by FEX Global Ltd. CME's authorisation facilitates greater competition in the Australian financial system by permitting a US-based central counterparty (CCP) to provide CCP services to a licensed domestic market. CME is licensed as an overseas CS facility because of the regulatory equivalence of the US and Australian CS facility regimes.

Established specialised market operators

Yieldbroker assessment

In November 2018, we reported on our assessment of the Yieldbroker market. We recommended improvements to the market's arrangements for conflicts and governance, supervision and enforcement, and systems and controls. Yieldbroker addressed each of our recommendations, resulting in a significant strengthening of governance and compliance arrangements, including an upgrade of its conflicts arrangements. Among other improvements, it developed a remuneration policy, a compliance manual, and enhanced monitoring systems.

Exempt market operators

Implementation of the Market Licence Regime

In May 2018, we introduced a two-tiered market licence regime that allowed us to tailor our licences to assist the operation of specialised and emerging financial markets. We implemented this regime across the year, and most of the exempt professional market platforms in the commodities, FX and fixed income sectors applied for licences. As of 30 June 2019, the Minister's delegate had granted the first licences for these platforms, with most of the outstanding applications being in the latest stages of processing.

3.6 Market intermediaries

The market intermediaries sector includes **market participants**, **securities dealers**, **corporate advisers**, **over-the-counter (OTC) traders**, **retail OTC derivatives issuers**, and **wholesale electricity dealers**.

ASIC's work in this sector during 2018–19 included enhancing our supervision model for the most complex and high-risk market intermediaries, which involves broader engagement across each entity and the development of tailored supervision plans.

We embedded our oversight of market intermediaries' fixed income, currency and commodities businesses, including through a thematic review of foreign exchange practices, onsite reviews, and detailed surveillance of large transactions. We also addressed harms to retail consumers in the retail OTC derivatives market through a range of licensing action, referrals to our Enforcement teams, and disrupting unlicensed conduct.

Enhanced market intermediary supervision

We have enhanced our supervisory approach for the largest and most complex market intermediaries in order to facilitate early detection of actual and potential harms and to foster constructive and timely behavioural change. We are doing this by, among other things, developing a deeper understanding of governance arrangements and internal controls that can help prevent poor conduct.

We are increasing our engagement through onsite reviews and meetings in order to identify areas of potential harm, to provide faster feedback on how to address the potential harms, and to act where appropriate. Our onsite reviews have covered themes such as culture and conduct, risk programs and training, corporate governance, compliance arrangements, pre- and post-trade controls, client money, and client disclosure arrangements.

For more information on corporate governance and Close and Continuous Monitoring, see Section 1.10

Oversight of fixed income, currency and commodity market intermediaries

This year, we continued to enhance our oversight of fixed income, currency and commodity markets. We conducted several onsite and targeted surveillance reviews where we assessed wholesale foreign exchange market participants against their obligations under the Corporations Act, the FX Global Code and Report 525 *Promoting better behaviour: Spot FX*. We also focused on the use of 'last look' practices in Australia and the use of mark-ups in foreign exchange businesses.

We reviewed the fixed income businesses of several firms and began reviews of the management of conflicts of interest by commodity businesses and intermediaries. We also completed targeted reviews of significant fixed income transactions to identify breaches of the law or compliance failures by market intermediaries.

Allocations in equity raising transactions

In December 2018, ASIC published Report 605 *Allocations in equity raising transactions*, summarising our review of transactions and practices by large and mid-sized AFS licensees. The report underscores the potential impact of conflicts of interest in allocation decisions and highlights areas of improvement for licensees and issuers when raising equity on our listed markets.

We recommended that licensees:

- engage with issuers at various stages during a transaction
- ensure that messages to investors are not misleading and deceptive
- review the adequacy of allocation policies and procedures
- avoid allocations to connected persons
- proactively identify and manage potential conflicts of interest.

The issuer's objectives should be the primary driver of allocation recommendations. Licensees should ensure that their controls, including policies and procedures, training and monitoring, are appropriate and that they are providing financial services efficiently, honestly and fairly.

Issuers should also be engaged with their capital raising transactions, with a particular focus on raising funds on the best terms possible.

ASIC continues to periodically review transactions and we have found that our ongoing presence is changing behaviour in this sector.

High-frequency trading

ASIC's latest review of high-frequency trading revealed that high-frequency traders are responsible for a quarter of equity market and Australian–US dollar cross rate transactions.

In November 2018, we published Report 597 *High-frequency trading in Australian equities and the Australian–US dollar cross rate*, which analyses high-frequency traders and their impact on measures of market quality. We found that high-frequency traders maintain a significant presence, they do not appear to degrade investor execution outcomes, and the costs imposed on investors for trading with high-frequency traders are small and continue to decline. We also found that intraday trading has decreased and that holding times are increasing.

Retail OTC derivatives market

Retail OTC derivatives issuers in Australia offer various products, including margin foreign exchange, binary options and contracts for difference. We continue to respond to a high incidence of misconduct in the retail OTC derivatives sector, involving large client losses.

This year, we continued to closely monitor this market and progressed a number of enforcement and administrative actions where we found breaches of the law. In April 2019, we conducted an extensive information-gathering exercise of the licensed entities active in retail OTC derivatives, covering 18 areas. Information obtained will be used to help us address key themes and concerns in the sector.

We publicly warned Australian issuers that they may be dealing with offshore investors illegally and to cease any non-compliant activities, particularly given that many jurisdictions – such as China, Europe, Japan and North America – have restricted or prohibited the provision of certain OTC derivatives to retail investors. We also worked to ensure that retail OTC derivatives providers are complying with foreign laws. We have liaised with various foreign regulatory agencies on this issue.

Progress on benchmark reform

Financial markets around the world, including Australia, use LIBOR (London Interbank Offered Rate) as a benchmark rate underpinning trillions of dollars of financial contracts. Preparation for the upcoming end of LIBOR is a key challenge for the global finance industry. In 2019, ASIC began a project with the support of APRA and the RBA to ensure that the end of LIBOR is understood and well managed. We have written to systemically important firms in the industry about their preparedness, asking them to identify their exposures to LIBOR and how they will transition to alternative rates.

Strengthening local financial benchmarks and fall-back provisions is another key issue in benchmark reform. While ASIC is confident that the BBSW will remain a significant benchmark, we are overseeing ongoing reforms to the BBSW calculation methodology to minimise potential future disruption.

ASIC licensed the administrator of the BBSW (ASX) to ensure reliability, market integrity and investor confidence. The European Commission determined that the Australian regime for benchmark administrators is equivalent to that of the European Union. This decision allows Australian licensed benchmark administrators to comply with EU regulations without the need to be dually licensed.

ASIC monitors the trades and orders that contribute to the BBSW rate set for misconduct and activity that may undermine the integrity of the process. Surveillance and reporting tools were enhanced during the period, which has improved efficiency.

3.7 Corporate

The corporate subsectors include **corporations** (listed corporations, **unlisted public companies**, **large proprietary companies**, and small proprietary companies[1]), **auditors of disclosing entities**, **registered company auditors**, and **registered liquidators**.

The Royal Commission and inquiries such as the APRA inquiry into CBA have highlighted that poor governance practices can lead to significant consumer and investor losses, as well as loss of confidence in our markets.

ASIC's work in this sector during 2018–19 focused on improving corporate governance practices and enhancing fairness and disclosure for retail investors in corporate finance transactions.

Corporations

Climate risk disclosure

In September 2018, ASIC published Report 593 *Climate risk disclosure by Australia's listed companies*, in response to the increasing foreseeability of climate change-related risks and the growing focus on the issue by investors. The report follows a surveillance project examining the climate risk disclosure practices of a sample of companies in the S&P ASX 300 and contains recommendations about consideration and disclosure of climate risk.

Our report recommends that directors and advisers adopt a probative and proactive approach to climate risk, comply with the law where it requires disclosure of material risk, and consider reporting under the framework developed by the Taskforce on Climate-Related Financial Disclosures. We anticipate continued work in this area as disclosure practices develop over time.

1 Small proprietary companies will be charged through an increase to the annual review fee for proprietary companies in the Corporations (Review Fees) Regulations 2003.

ASIC intervention in de-listing application

ASIC intervened in a de-listing application by Flinders Mines Limited (Flinders). Flinders is a public mining company listed on ASX. In December 2018, Flinders applied for de-listing, together with a share buy-back and rights issue. The proposed transactions would have had the effect of increasing its major shareholder's relevant interest in Flinders from 56% to a maximum of 65% and the resolutions could be passed by the shareholder.

ASIC received numerous reports of misconduct regarding Flinders and considered the concerns raised by minority shareholders. Following a Takeovers Panel declaration of unacceptable circumstances in proceedings in which ASIC was an active participant, Flinders withdrew its de-listing application and abandoned its other proposed corporate actions.

ASIC also worked with ASX in relation to its release of amended Guidance Note 33: *Removal of entities from the ASX official list*. The revised Guidance Note indicates that ASX will now usually require a listed entity to obtain the approval of its security holders before its removal from the official list by way of a special resolution (rather than an ordinary resolution).

Withdrawal rights for retail shareholders

In June 2019, we intervened in a rights 'low document' entitlement offer by St Barbara Mines Limited (St Barbara), which resulted in the company allowing retail shareholders to withdraw their acceptances. A low document offer is a security offer generally undertaken by listed entities where the securities can be offered for sale or issue without a public document.

During the retail offer period, St Barbara announced a production downgrade that negatively impacted its share price. ASIC intervened as we believed that retail shareholders were not being given the chance to reconsider their investment decision, even though the new trading price was now below the entitlement offer price. After our intervention, St Barbara announced that retail investors would be given an opportunity to withdraw their acceptances.

Small business outcomes

ASIC focuses on helping small businesses understand and comply with their legal obligations under the Corporations Act and conducts surveillance, enforcement and policy work. Where necessary, we take administrative, civil or criminal action against companies, directors and other officeholders who fail in their duties. By doing so, ASIC helps to ensure that all market participants can benefit from a level playing field.

This year, ASIC recorded 514 small business-related outcomes (see Table 3.7.1).

As at 1 July 2019, ASIC had 161 small business-related criminal matters underway that had not achieved a final result (see Table 3.7.2). They were not included in Table 3.7.1 because either:

- the court or tribunal has determined liability but not decided the penalty or final order
- a plea was entered but the court or tribunal has not yet made a decision on conviction or sentence
- the court has not yet decided if a breach of law or an offence was committed.

For more on ASIC's Office of Small Business, see Section 5.3

Table 3.7.1 Small business enforcement outcomes by misconduct and remedy type

Misconduct type	Criminal	Administrative	Total (misconduct)
Action against persons or companies	364	132	496
Efficient registration and licensing	18	0	18
Total (remedy)	**382**	**132**	**514**

Table 3.7.2 Small business criminal cases underway as at 1 July 2019

Misconduct type	Criminal
Action against persons or companies	154
Misconduct related to registration and licensing	7
Total	**161**

Auditors of disclosing entities

Financial reporting surveillance

In 2018–19, ASIC proactively reviewed 300 financial reports of listed and other significant entities, with the aim of improving the quality of financial reports and providing useful information for investors and other stakeholders.

We continue to publicly highlight financial reporting focus areas for directors, preparers and auditors in our surveillance of financial reports. Our releases allow stakeholders to address key reporting matters before issuing their financial reports and ensure that the market is properly informed on a consistent and comparable basis. Areas of focus include impairment of non-financial assets, recognition of revenue, and the adoption of new accounting standards on revenue and financial instruments.

Premier Investments writes down brand name assets

ASIC raised concerns about the value of the casual wear brand name assets in the financial report of Premier Investments Limited (Premier) for the year ended July 2017. We questioned the reasonableness and supportability of the royalty rate assumptions and sales growth forecasts used in testing the assets for impairment.

As a result of ASIC's work, Premier wrote down the value of the relevant assets by $30 million in its financial report for the following year ended July 2018.

Audit inspection program

Auditors play a vital role in underpinning investor trust and confidence in the quality of financial reports. To improve and maintain audit quality, we reviewed approximately 65 financial reports of listed entities during the year. In January 2019, we released Report 607 *Audit inspection program report for 2017–18*, reporting the results of our audit firm risk-based inspections for the 18 months to 30 June 2018.

This year, we emphasised the importance of good leadership in audit firms, including their staff members embracing the need to improve audit quality and being accountable for their work in conducting quality audits.

ASIC's reviews also ensured that audit firms continue to focus on the sufficiency and appropriateness of the audit evidence they obtain, their professional scepticism, and their appropriate use of the work of experts and other auditors. We also continued to encourage auditors to focus on the impairment of non-financial assets, revenue recognition, and the impact of the new accounting standards.

Registered liquidators

Liquidator of suspected phoenix company

Through the Assetless Administration Fund (AA Fund), ASIC combats the harms associated with illegal phoenix activity, such as losses for employees, businesses and consumers. The AA Fund supports registered liquidators in investigating and examining matters involving pre-insolvency advisers and illegal phoenixing. This may include funding a liquidator to conduct public examinations, where there is a reasonable basis to suspect that this may reveal evidence to support recovery action by the liquidator or possible prosecution by ASIC.

This year, a registered liquidator used their own firm's resources and undertook sufficient investigations to find that a liquidated company's director had likely engaged in misconduct. To complete the investigation and conduct public examinations, the liquidator applied for funding from the AA Fund. The funding allowed the liquidator to gather enough evidence to launch recovery actions against the director and their spouse. ASIC is also funding the liquidator's recovery action through the AA Fund. This case highlights the utility of the AA Fund when liquidators are appointed to companies otherwise devoid of assets – enabling liquidators to investigate, seek recovery for creditors, and combat illegal phoenix activity.

Former liquidator imprisoned

In February 2018, ASIC commenced an investigation into the conduct of a registered liquidator alleged to have stolen $800,000 from the bank account of an external administration that he jointly controlled.

Following our investigation, the liquidator was charged and on 3 May 2019 he pleaded guilty to three charges of fraud. He was sentenced to seven years imprisonment and will be eligible for parole after serving 22 months in custody.

ASIC also referred the alleged misconduct to the Liquidators Disciplinary Committee, which cancelled the liquidator's registration. Other liquidators will be prohibited from allowing him to work on their behalf for eight years.

Liquidators forced to repay remuneration

In June 2019, the Federal Court fixed remuneration sought by liquidators John Sheahan and Ian Lock for the voluntary administration and liquidation of the Cedenco Group. Remuneration was fixed at $3.9 million compared to the $5.8 million sought, a reduction of 33%. The liquidators were ordered to repay the difference plus interest at the court's interest rates and were ordered to pay ASIC's costs.

Earlier in February 2019, the court found that the remuneration reports provided to creditors fell 'well short' of the requirements, including in some cases not providing any remuneration reports. The court found that creditors had suffered substantial injustice as they were not able to properly consider the reasonableness of the remuneration.

The court found that external administrators should:

- ensure that remuneration reports comply with the Act
- ensure that time sheet narrations accurately record tasks undertaken
- review work in progress
- write off time where relevant
- appropriately tailor templates or precedent documents.

3.8 Large financial institutions

Entities subject to Close and Continuous Monitoring

We have enhanced key aspects of our supervisory approach, as part of our response to widespread conduct failures in the Australian financial services industry.

Our approach now includes the CCM program, which introduces a new supervisory model for Australia's largest financial services institutions (AMP, ANZ, CBA, NAB and Westpac) and features a periodic onsite ASIC presence in these institutions to review specific practices. We are also in the process of a targeted review of corporate governance practices of these institutions and a selection of other ASX 100 listed entities.

For more information on the CCM program and our review of corporate governance practices, see Section 1.10