



# UNSW Business School

## School of Taxation and Business Law

# Empowering Financial Services Regulators

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Warmest 你好 and hello from the University of New South Wales in Sydney and the Dean and Faculty of UNSW Business School, particularly to our alumni here today

Thank you to CFRED and the AIIFL and to my visit host, Professor CK Low from CUHK Business School



# A scary topic?



- For a range of economic and social reasons, the participation of ‘retail’ customers in the market for quite complex financial services and financial products has increased significantly this century
- A contributing factor in Australia has been our compulsory retirement savings (superannuation) system, but it is not the only one
- Some of these retail customers have lower levels of financial literacy and sophistication, and products offered to them have become increasingly complex

# The context

- Financial services regulators have been given the task of regulating providers of products and services to these customers
- Today I want to look at the **powers** given to financial services regulators in this area, through the lens of recent developments in Australia
- It is less about the content of the substantive law (that is, what the legislation administered by the regulator actually requires of or prohibits for providers) although this is related
- Nor am I looking at resourcing – that is, levels of funding and expertise within regulators – or the accountability or oversight of regulators

## OECD *Policy Framework for Effective and Efficient Financial Regulation* (2010)

- *Confidence in the financial system:* Public confidence in the financial system is maintained so that the key functions of the financial system can operate, such as financial intermediation
- *Systemic stability:* The financial system as a whole is resilient against external shocks and is not susceptible to a systemic breakdown, for instance where the failure of one or more financial institution causes the collapse of other, otherwise safe, financial institutions
- *Safety and soundness of financial institutions:* Financial institutions involved in the intermediation process and in the management, pooling and transfer of risks are managed prudently, with the scope for failure of poorly managed and weak institutions
- *Market integrity and transparency:* The financial system operates in a fair and transparent manner, with the absence of fraud and market abuse, and fair, accurate and timely disclosures
- *Market conduct and consumer protection:* The providers of financial products and services in the financial system interact with their customers in a fair, transparent, and professional manner, and the interests of consumers are adequately safeguarded and their needs addressed
- *Efficiency:* The financial system generates efficient outcomes, with capital allocated efficiently to the most productive uses, the pricing of financial services reflecting costs, and the expected return on financial services, products and instruments appropriately reflecting risks

# The questions...

Are regulators failing in the market conduct and consumer protection space?

If so, is it because they have inadequate or inappropriate powers?

# In the UK

The Financial Conduct Authority recently released two papers, including [Approach to Consumers](#). Andrew Bailey, Chief Executive, said:

'Consumer protection is absolutely central to the FCA's purpose and Mission. Nearly everyone at some stage in their life will come into contact with a financial organisation and people need to know that they are being treated fairly and that the right protections are in place. Different groups of consumers have different financial needs, which will naturally change over their lifetime.

As we have demonstrated in the past we will act to address harm or potential harm using the range of powers and tools at our disposal to protect consumers. To ensure we provide the necessary protections and deliver good outcomes for consumers we need to regularly review our approach, so we can reflect the diverse population of the UK and consumers' changing needs in a rapidly-evolving and increasingly complex environment.'

# In the USA

The Obama-era [Consumer Financial Protection Bureau](#) has survived the change of administration

‘We hold companies accountable for illegal practices:

- \$12.4 billion in relief to consumers from our enforcement actions
- 31 million+ consumers will receive relief because of our actions’



Consumer Financial  
Protection Bureau

# In Australia

- There is currently a Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry. It was established in December 2017 and is due to report in February 2019
- Its terms of reference include, at paragraph (g), ‘the effectiveness and ability of regulators of financial services entities to identify and address misconduct by those entities’
- This is the most recent of 70+ government or other inquiries into these and related issues in Australia over the last decade, some of which are ongoing
- These include several recent inquiries addressing the powers of the Australian Securities and Investment Commission (ASIC)

# ASIC Enforcement Review

- The [ASIC Enforcement Review Taskforce](#) was established in October 2016
- It followed the [Financial System Inquiry](#) which reported in December 2014, and the [ASIC Capability Review](#) in 2015
- The Taskforce reported to government in December 2017 and the government responded in April 2018
- Legislation was introduced this month



... to detect, deter and address ...

# Taskforce terms of reference

Dealt with penalties and breach reporting, and also:

- The adequacy of enforcement related financial services and credit licensing powers
- The adequacy of ASIC's power to ban offenders from occupying company offices following the commission of, or involvement in, serious contraventions where appropriate
- The adequacy of ASIC's information gathering powers and whether there is a need to amend legislation to enable ASIC to utilise the fruits of telephone interception warrants or to grant the equivalent of Federal *Crimes Act* search warrant powers under ASIC's enabling legislation for market misconduct or other serious offences
- The adequacy of ASIC's powers in respect of licensing of financial services and credit providers, including the threshold for granting or refusing to grant a license, the circumstances in which ASIC may vary, suspend, or cancel licenses; and its coercive powers (including whether there is a need for ASIC to have a power to direct licensees to take, or refrain from taking, particular action)

# Regulator powers

Four groups:

- Power to obtain information about the conduct and affairs of a financial services business
- Power to take protective action to exclude products or service providers, such as occupational licensing, bannings and product intervention
- Power to change business practices or extract sanctions without being required to commence legal proceedings
- Power to commence legal proceedings (criminal and civil)

# Power to obtain information

- Compulsory information-gathering powers: for example the right to demand businesses provide information, either with or without suspicion that offending has occurred (can raise privilege questions)
- Gatekeeper and whistle-blower reporting
- Surveillance powers, warrants and the like
- Breach reporting regimes
- Product claim justification notices

# Power to take protective action

- This is action that the regulator can take administratively. Usually subject to judicial review (as is any exercise of administrative power)
- Licensing: conditions and revocations
- Individual bannings: occupational, managing corporations, responsible manager regimes (BEAR in Australia)
- Product intervention powers – the right to have products withdrawn or redesigned
- Product stop orders – for product disclosure
- Public warning notices

# Enforcement without court proceedings

- On-the-spot fines or infringement notices
- Agreed settlements, including court enforceable undertakings and deferred prosecution agreements
- Often these involve remediation or supervised compliance programs
- A key issue is admissions of liability



# Court enforcement proceedings

- Criminal prosecutions
- Civil penalties
- Civil actions, including injunction
- Regulators in Australia are very attracted to civil penalty proceedings, particularly following *ASIC v Whitebox*
- Compliance systems are important here too

*Does raising maximum penalties change behaviour? By regulated entities and by regulators?*

# ALRC and the aims of penalties

- retribution ('just deserts' for having committed the contravention);
- social condemnation (expressed through the stigma of a criminal record or severe penalty such as imprisonment);
- specific deterrence (deterrence of the person sanctioned from repeating the contravention);
- general deterrence (deterrence of others from engaging in the prohibited behaviour);
- protection of third parties or the public at large; and
- payment of reparation or compensation.

# 'Gutless leadership'

*'This is about accountability,' she said. 'You should resign, you should give back the money you took while this scam was going on and you should be criminally investigated by both the Department of Justice and the Securities and Exchange Commission.'*

*'The only way that Wall Street will change is if executives face jail time when they preside over massive frauds,' she added. 'Until then it will be business as usual, and at giant banks like Wells Fargo, that seems to mean cheating as many customers, investors and employees as they possibly can.'*

US Senator [Elizabeth Warren](#), to Wells Fargo Chairman and CEO John Strumpf, September 2016



