

Regulating culture

The carrot or the stick?

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Outline

- What is culture?
- What are the drivers of culture?
- How is the focus on culture influencing what regulators do?
- How is the focus on culture influencing the financial services regulatory regime?



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What is culture

Culture is a set of shared values and assumptions within an organisation. It reflects the underlying 'mindset of an organisation', the 'unwritten rules' for how things really work.



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What is culture

- Section 12.3(6), the Criminal Code, (Schedule to the *Criminal Code Act 1995*)

“corporate culture” means an attitude, policy, rule, course of conduct or practice existing within the body corporate generally or in the part of the body corporate in which the relevant activities takes place



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Key drivers of culture



TONE FROM THE TOP

Senior executives and the board should lead by example and demonstrate conduct that supports the firm's values.



ACCOUNTABILITY

Staff should be held to account for their conduct in relation to firm values.



EFFECTIVE COMMUNICATION AND CHALLENGE

Firms should promote a culture of open communication and challenge.



RECRUITMENT, TRAINING AND REWARDS

Staff selection, training and rewards all need to be aligned to, and support, the values of the firm.



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Regulators

- Focus on culture influences
 - Surveillance/supervision
 - Education and guidance
 - Policy/regulation making
 - APRA *Prudential Standard CPS 510 Governance*
 - APRA *Prudential Standard CPS 220 Risk Management*



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Regulators: Surveillance and Supervision

- Two models
 - Specific team, bespoke approach
 - Australian Prudential Regulation Authority
 - De Nederlandsche Bank
 - Integrating culture into existing surveillance work
 - Australian Securities and Investments Commission
 - Direct life insurance surveillance
 - Advice compliance project (REP 515 *Financial advice: Review of how large institutions oversee their advisers*)



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Regulation

- Prohibition on conflicted remuneration
- Professional standards for financial advisers
- Product design and distribution obligations



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Regulation: Conflicted remuneration

For advice to retail clients, the *Corporations Act 2001* prohibits

- AFS licensees and their representatives from accepting conflicted remuneration (s963E, 963G and 963H)
- Product issuers and sellers from giving conflicted remuneration to AFS licensees and their representatives (s963K)
- Employers of an AFS licensee or representative from giving their AFS licensee or representative employees conflicted remuneration for work they carry out as an employee (s963J)



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Regulation: Conflicted remuneration

Conflicted remuneration means any benefit, whether monetary or non-monetary, given to a financial services licensee, or a representative of a financial services licensee, who provides financial product advice to persons as retail clients that, because of the nature of the benefit or the circumstances in which it is given:

(a) could reasonably be expected to influence the choice of financial product recommended by the licensee or representative to retail clients; or

(b) could reasonably be expected to influence the financial product advice given to retail clients by the licensee or representative. (s963A)



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Regulation: Advisers' professional standards

- Compulsory education requirements
- Exam
- Supervision requirements for new advisers
- Code of ethics
- Ongoing professional development

(Corporations Amendment (Professional standards of Financial Advisers) Act 2017)



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Regulation: Product design and distribution

- Issuers must
 - identify appropriate target and non-target markets for their products
 - select distribution channels that are likely to result in products being marketed to the identified target market
 - review arrangements with reasonable frequency to ensure arrangements continue to be appropriate
- Distributors must
 - put in place reasonable controls to ensure products are distributed in accordance with the issuer's expectations
 - comply with reasonable requests for information from the issuer related to the product review
- Obligations will apply to financial products made available to retail clients, except ordinary shares

Design and Distribution Obligations and Product Intervention Power: Proposals Paper (Cth Treasury, Dec 2016)



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Concluding remarks



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**Macquarie's Bad Apples
Still Working in
Financial Planning**

The Age, 21 April 2015

PARTY'S OVER FOR ROGUE TRADERS

SMH, 9 January 2016

**French Bank Says Rogue
Trader Lost \$7 Billion**

New York Times, 25 January 2008

**BANKS TO IDENTIFY
BAD APPLES**

Money Management, 31 January 2017

**A Rogue Trader, a Swiss Bank
and Another Financial Scandal**

ABC, 4 October 2011

**Rogue NAB Traders Face Their
Judgement Day**

The Age, 1 July 2006



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A Few Bad Apples? It's a
Dodgy Adviser Orchard

SMH, 18 March 2017

**More Questions over NAB Culture
after Huge Clydesdale Fine**

SMH, 15 April 2015

BANKING - THE CULTURE WARS

The Conversation, 6 April 2016

BANKS URGED TO MAKE A SHARP BREAK

WITH THE PAST TO IMPROVE CULTURE

ABC, 18 April 2017

**CBA needs a Cultural
Change**

AFR Weekend, 5 August 2017



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