



# RESEARCH NOTE NO. 1:

## ENFORCEMENT EFFECTIVENESS OFF THE AGENDA: A RECIPE FOR DISASTER

By

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## The political arguments

Federal Opposition Leader Bill Shorten is spruiking the Labor government's intention to hold a Royal Commission into misconduct in the banking sector if elected on July 2.

Prime Minister Malcom Turnbull and Treasurer Scott Morrison whilst acknowledging the problem (the need for increased transparency in the banking sector) have put their faith in the current regulatory arsenal. Morrison said:

We have a tough cop on the beat in that area — it is called ASIC. We have a strong regulator — it is called APRA. We have the Reserve Bank which provides a broader framework in which the banks operate in. Our banking system is well regulated.<sup>1</sup>

## Powers of a Royal Commission

Commonwealth Royal Commissions are 'temporary ad hoc bodies'<sup>2</sup> that comprise of Commissioners appointed under the *Royal Commissions Act 1902 (Cth)* to conduct "public inquiries" in respect of a governments "Terms of Reference" approved by the Governor-General. The powers of the Royal Commission are set out in Part 2 of the legislation. These include coercive powers such as the power to summon witnesses and take evidence, issue search warrants, obtain evidence and tap phones in addition to impose penalties for failing to comply under Part 3 and a number of protections specifically aimed at protecting witnesses and inquiry members.

## Powers of ASIC

ASIC is independent of the Government. ASIC is appointed under the *Australian Securities and Investments Commission Act 2001* (ASIC Act) to administer the ASIC Act in harmony with the *Corporations Act 2001* (Corporations Act).<sup>3</sup> ASIC's main role is the regulation of financial and

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<sup>1</sup> Anna Henderson and Dan Conifer, 'What is a royal commission and why does Labor want one into the banking industry?', *ABC News* (online), 11 April 2016 <<http://www.abc.net.au/news/2016-04-08/what-is-a-royal-commission-and-why-does-labor-want-one/7312216>>.

<sup>2</sup> Scott Prasser, 'Royal commissions: how do they work', *The Conversation* (online), 13 November 2012 <<https://theconversation.com/royal-commissions-how-do-they-work-10668>>.

<sup>3</sup> A comprehensive guide to the laws administered by ASIC is available here: Australian Securities and Investment Commission, *Laws we administer* (2016) <<http://asic.gov.au/about-asic/what-we-do/laws-we-administer/>>.



corporate markets and services through regulatory and enforcement powers, such as in this instance the power to initiate an investigation under the ASIC Act, conduct hearings and compel the production of evidence and issue search warrants.

### **Arguments for a Royal Commission**

Shorten argues that ‘many Australians have suffered through the decisions of banks and financial institutions .... [and] .... literally tens of thousands of victims, if not more’.<sup>4</sup> Similarly, Shadow Treasurer Chris Bowen argues that:

‘A royal commission has the power to hold public and private hearings, to use search warrants, to compel the production of documents and to call witnesses from a wider pool than an individual investigation of the kind ASIC normally runs [and it is better] equipped to identify and prevent illegal and unethical behaviour, ... [because] ASIC cannot examine their own capacity in the way a royal commission can’.<sup>5</sup>

### **Arguments against a Royal Commission**

Treasurer Scott Morrison argues that ‘ASIC has the powers of a royal commission and, in fact, it has greater powers than a royal commission’.<sup>6</sup> In formulating such an argument, Morrison issued a one page fact sheet outlining the respective roles of ASIC and Royal Commissions under the *Royal Commissions Act 1902* (Cth) and *Australian Securities Investment Commission Act 2001* (Cth) (‘ASIC Act’).<sup>7</sup>

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<sup>4</sup> Michelle Grattan, ‘Labor pledges royal commission into bank behaviour’, *The Conversation* (online), 8 April 2016 <<https://theconversation.com/labor-pledges-royal-commission-into-bank-behaviour-57490>>.

<sup>5</sup> Mark Dreyfus QC MP, *Malcolm And Slomo Wrong On Royal Commission* (2016) <[http://markdreyfus.nationbuilder.com/malcolm\\_and\\_slomo\\_wrong\\_on\\_royal\\_commission](http://markdreyfus.nationbuilder.com/malcolm_and_slomo_wrong_on_royal_commission)>.

<sup>6</sup> The Hon Scott Morrison MP, ‘Bill Shorten playing politics on Royal Commission’ (Doorstop Interview Melbourne, 8 April 2016) <<http://sjm.ministers.treasury.gov.au/transcript/045-2016/>>.

<sup>7</sup> The Hon Scott Morrison MP, ‘Fact Sheet – ASIC and Royal Commission’ (Media Release, 12 April 2016) <<http://sjm.ministers.treasury.gov.au/media-release/038-2016/>>.

## Fact Sheet – ASIC and Royal Commission

	Royal Commission	ASIC
<b>When can coercive investigatory powers be utilised?</b>	As part of a Royal Commission to the extent the information sought is directly relevant to the investigation as outlined in the Terms of Reference	As part of an investigation. ASIC must have a reason to suspect a contravention has occurred. However, <b>ASIC can be directed by the Minister to commence an investigation in the public interest</b>
<b>Coercive powers</b>	Power to summon a person to give evidence on oath and/or produce documents, <b>subject to exceptions</b> where a person has been charged with an offence (s6A(3)) or proceedings in response to a penalty have commenced (s6A(4))  Power to apply for search warrants (s4)	Coercive powers to require appearance of a witness for examination on oath (s19) inspect documents without warrant (s29), require production of documents (ss30-34) <b>including</b> where evidence may be self-incriminating (s 68)  Power to apply for search warrants (s35)
<b>Offence for resisting requests</b>	Criminal offences for failing to give evidence, providing false or misleading evidence, destroying documents etc (ss 3,6,6H, 6O)	Criminal offences for failing to produce (or concealing) documents, to attend examination or answer questions, and for giving false information, or obstructing investigation etc (ss63-67)
<b>Admissibility</b>	Statements made by a witness and documents produced by a person under compulsion are not admissible against them in any civil or criminal proceedings (s6DD)	Statements made of documents produced by a witness are not admissible against them in any civil penalty or criminal proceedings, where person claims before making the statement that it might be self-incriminating (s68)
<b>Prosecution powers</b>	A Royal Commission has <b>no power to prosecute misconduct</b> but may refer matters to other investigatory bodies (s6P)	ASIC has the power to initiate civil and criminal proceedings, and pursue prison terms, court orders and fines

### Historically Labor has overlooked such investigations: why the change of heart?

At least from a political standpoint, it could be argued that the most recent move from Shorten is nothing more than ‘political opportunism’.<sup>8</sup> Taking a look back to 2009, six leading economists highlighted the ‘fundamental flaws in Australia’s ageing regulatory architecture ... exacerbated by the relentless changes in financial markets since the essential elements of our

<sup>8</sup> Christopher Joye, ‘Bill Shorten has unconvincing case for a royal commission’, *Financial Review* (online), 10 April 2016 < <http://www.afr.com/business/banking-and-finance/bill-shorten-has-unconvincing-case-for-a-royal-commission-20160410-go2t9p>>.



regulatory infrastructure were put in place decades ago'.<sup>9</sup> The economists emphatically recommended an inquiry into Australia's financial system that was dismissed by the then Treasurer Wayne Swan.<sup>10</sup> Similarly in 2010, the Gillard government dismissed such an inquiry.

In October 2010, Shadow Treasurer Joe Hockey in an address to the AIG Annual National Forum Canberra backed 'a new financial system inquiry', a "Son of Wallis" (emphasis of the original).<sup>11</sup> Hockey first tabled the idea in 2009.<sup>12</sup>

### **The Murray Review**

In 2013, Joe Hockey commissioned the financial system inquiry, a third wave of inquiry that led to what is coined the Murray review releasing its report entitled '*Financial System Inquiry*' ('FSI') making 44 recommendations on 7 December 2014.

On 20 October 2015, the government released its response to the inquiry accepting 'the vast majority of the review's recommendations'.<sup>13</sup> The Murray review being the most significant inquiry since the Campbell Report in 1981 and Wallis Report in 1997.<sup>14</sup> The Murray review

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<sup>9</sup> Joshua Gans, Nicholas Gruen, Christopher Joye, Stephen King, John Quiggin and Sam Wylie, 'Rules underpin prosperity', *The Age* (online), 08 July 2009 <<http://www.theage.com.au/federal-politics/rules-underpin-prosperity-20090707-dbsl.html?skin=text-only>>.

<sup>10</sup> Peter Martin, *Son of Wallis, daughter of Campbell* (2009) <<http://www.petermartin.com.au/2009/07/son-of-wallis-daughter-of-campbell.html>>.

<sup>11</sup> The Hon Joe Hockey MP, 'It's Time To Talk Banking' (Speech delivered at the AIG Annual National Forum Canberra, 25 October 2010) <[http://www.aigroup.com.au/portal/binary/com.epicentric.contentmanagement.servlet.ContentDeliveryServlet/LIVE\\_CONTENT/National%2520Forum/2010/Hockey\\_address\\_forum2010.pdf](http://www.aigroup.com.au/portal/binary/com.epicentric.contentmanagement.servlet.ContentDeliveryServlet/LIVE_CONTENT/National%2520Forum/2010/Hockey_address_forum2010.pdf)>

<sup>12</sup> *Ibid*, 4.

<sup>13</sup> Gareth Hutchens, 'Turnbull government backs Murray Review, setting up major overhaul of Australia's financial system', *The Sydney Morning Herald* (online), 20 October 2016 <<http://www.smh.com.au/business/banking-and-finance/turnbull-government-backs-murray-review-setting-up-major-overhaul-of-australias-financial-system-20151019-gkd6yu.html>>.

<sup>14</sup> All three reports available here: <http://fsi.gov.au/publications/>



concluded that ‘the system is not sufficient to deliver fair treatment to consumers’<sup>15</sup> consequently arguing for increased funding and resources to combat anti-competitive practices and increase market surveillance.<sup>16</sup>

### **A review into ASIC’s capabilities**

In response to the FSI, the Turnbull government announced a review examining the corporate watchdog ASIC’s capabilities on 24 July 2015. On 4 December 2015, the Capability Review released its findings to the Minister making a total of 34 recommendations in its report entitled ‘*Fit for the Future: A Capability Review of ASIC*’ released to the public on 20 April 2016.<sup>17</sup> The Panel raised six priority areas:

1. External governance and performance reporting;
2. Internal governance;
3. Commission, workforce planning and culture;
4. Strategic communication and stakeholder management;
5. Organisation structure and regulatory toolkit; and
6. Data management.

Of the 34 recommendations, five are specifically addressed by the ‘*Government Response to ASIC Capability Review Report Recommendations*’.<sup>18</sup> The remaining recommendations and objectives are addressed in ‘*ASIC’s Implementation Plan*’.<sup>19</sup>

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<sup>15</sup> The Australian Financial Review, ‘Morrison to act on Murray recommendations on ASIC powers over banks’, *Financial Review* (online), 20 April 2016 <  
<http://www.afr.com/opinion/editorials/morrison-to-act-on-murray-recommendations-on-asic-powers-over-banks-20160420-goaydf>>.

<sup>17</sup> Australian Government, *Fit for the future: A capability review of the Australian Securities and Investments Commission A Report to Government*, The Treasury, December 2015 <  
<http://www.treasury.gov.au/PublicationsAndMedia/Publications/2016/ASIC-capability-review>>.

<sup>18</sup> Recommendations 1, 6, 7, 11, 24. Australian Government, *Government Response To Asic Capability Review Report Recommendations*, The Treasury, April 2016 <  
<http://www.treasury.gov.au/~media/Treasury/Publications%20and%20Media/Publications/2016/Fit%20for%20the%20future/Downloads/PDF/ASIC-Capability-Review-Govt-Response.ashx>>.

<sup>19</sup> Australian Securities and Investment Commission, *ASIC capability review* (2016) <  
<http://www.asic.gov.au/capability-review>>.



## The announcement

The release of the findings of the Capability Review ('the Panel') coincided with the Turnbull governments announcement that it would increase ASIC's funding to monitor the financial market, the announcement of an ASIC commissioner with prosecution skills and extensive strengthening of ASIC's expert surveillance arsenal in line with the power enjoyed by the Australian Prudential Regulation Authority ('APRA').<sup>20</sup> ASIC Chairman Greg Medcraft in a Media Release said:

This will enable further surveillance and enforcement in areas such as financial planning, responsible lending, life insurance, and misconduct and breach reporting. It will also allow us to build our technological capacity to identify and assess risks and misconduct ... [w]e will work with the Government and Treasury to make sure the regulatory framework allows ASIC to most effectively address market misconduct and contains the appropriate incentives for firms to put their customers first.<sup>21</sup>

Notably, the government has implemented changes that go a long way toward achieving the overarching objectives of the panel's findings to: 'ensure ASIC is best placed to deal with a rapidly changing external environment and promote enhanced industry, consumer, investor and community confidence in ASIC'.<sup>22</sup>

## Recommendation 27: A cause for concern?

It reads:

ASIC to enhance enforcement effectiveness through developing a more targeted risk based approach to litigation for cases that are strategically important, and prosecutes through more focussed pleadings and strategic appointment of senior counsel.

ASIC's response:

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<sup>20</sup> Above n 15.

<sup>21</sup> Australian Securities and Investment Commission, 'ASIC welcomes significant reforms' (Media Release, 16-119MR, 20 April 2016) < <http://www.asic.gov.au/about-asic/media-centre/find-a-media-release/2016-releases/16-119mr-asic-welcomes-significant-reforms/>>.

<sup>22</sup> Australian Government, *Background to Fit for the Future: A capability review of the Australian Securities and Investments Commission* (2016) < <http://www.treasury.gov.au/PublicationsAndMedia/Publications/2016/ASIC-capability-review/Fit-for-the-Future>>.



ASIC strongly supports the objectives set out in the recommendation, and, while we are always striving to improve our enforcement effectiveness, they do reflect ASIC's current practice.<sup>23</sup>

Arguments advancing the Labor government's announcement that it will assemble a Royal Commission in addition to the Liberal governments recent cash boost are essentially ill equipped in context of this. ASIC have no intention to beef up "enforcement effectiveness" despite a poor track record in terms of enforcement. In this respect, a Royal Commission is unable to police its own findings and effectively will rely upon ASIC to get the job done, whilst ASIC will not increase surveillance enforcement.

### **Concluding remarks**

Although the intention of the Labor government is a good one, recent history would suggest that the outcomes and recommendations of Royal Commissions are seldom acted upon by ASIC. Without wide reaching powers to initiate criminal and civil proceedings, the Royal Commission becomes a costly exercise that ultimately a body with a lack of funding is unlikely to pursue. The recent announcements, at least in the shorter term provide an opportunity for ASIC to prove itself as the regulator and increase the prosecution of financial institutions behaving badly. Sadly, if the lack of interest in enhancing enforcement effectiveness is a reality, no amount of funding will solve the problem. Perhaps, the Labor government's proposal for a Royal Commission will ultimately prevail. Even if a Royal Commission does possess broader powers and reach than ASIC'S powers, a lack of ability to prosecute matters is severely limiting regardless of which way you look at it - the ability to conduct a broader inquiry than APRA and ASIC<sup>24</sup> achieves little without a power to prosecute and thereby compromising the best efforts of both political parties, amounting to a recipe for disaster.

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<sup>23</sup> Above 19.

<sup>24</sup> Anna Olijnyk and Vicky Comino, 'Fact Check: does ASIC already have the powers of a royal commission and more?', The Conversation (online), 18 April 2016 <<https://theconversation.com/factcheck-does-asic-already-have-the-powers-of-a-royal-commission-and-more-57666>>.



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