

Steve Mark AM



24 October 2018

Submission to the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, Interim Report

Dear Commissioner,

Thank you for accepting and considering this short submission to your inquiry.

This brief submission is based on my experience in the regulation of the legal profession and the work I have done with several other occupational associations in their path to professionalization through the Professional Standards framework.

I have closely followed the work of the Commission, including many of the transcripts and submissions publicly available, and have more recently had the opportunity of reading volume 1 of the Commissions Interim Report. I am extremely impressed with the depth to which the Commission has explored the causes of complaints made and concerns raised about practices in the Banking Superannuation and Financial Services industries, and would now like to make a small submission outlining a possible solution to some of the matters raised. In doing so, I will attempt to address paragraph (h) of the Commissions Terms of Reference – “whether any further changes to the legal framework; practices within financial services entities; and or the financial regulators are necessary to minimise the likelihood of misconduct by financial services entities in the future.” However, this brief submission should be seen as a response to the Commissions Interim Report.

At the outset I would like to ask the Commission to consider the work I did as NSW Legal Services Commissioner at the Office of the Legal Services Commissioner (OLSC) in creating “ethical infrastructure” within law firms (in particular incorporated legal practices (ILP), as a means of encouraging ethical culture within such practices¹. The system devised by my office resulted in the reduction of complaints against participating firms by two thirds². Our approach in regulating the profession was to form a partnership with the professional associations (the Law Society and Bar Association of NSW) to deliver improved service and ethical conduct by the profession to the consumer, and to ensure consumer protection. The focus of this form of regulation was directed squarely on maintaining a culture of consumer protection.

¹ S Mark and T Gordon, ‘Innovations in Regulation: Responding to a Changing Legal Service Market’ (2009) 22 *Georgetown Journal of Legal Ethics* 501.

² C Parker, T Gordon, S Mark, ‘Regulating Law Firm Ethics Management: An Empirical Assessment of the Regulation of Incorporated Legal Practices in NSW’ (2010) 37 *Journal of Law and Society Studies* 466.

I have observed that many commentators, on what has been revealed to date by the Commission, have focused on the need to address and improve the culture of the banking and financial services industries. I have also noted that suggestions have been made that one way of improving an ethical culture within those industries could be achieved by placing “compliance officers” within the organisations providing financial services to ensure ethical service delivery. Unfortunately, I do not share the optimism of those who hold that belief.

I teach ethics in the law faculty at the University of NSW. As such, I am familiar with concepts of behavioural ethics. One of the issues addressed by commentators in this field is the impact of organisational culture on the ethical behaviour of individual employees. Concepts of “emersion” leading to “ethical blindness” are often referred to when discussing how otherwise normal ethical people can act unethically within an organisational culture which promotes (for example) profit over customer protection. My learnings in the field of legal ethics, and a study the scandals of HIH, AWB, James Hardy, Enron etc. have resulted in me being somewhat sceptical of the efficacy of compliance officers, and indeed, with whistle blowing generally in Australia.

Concerns have been raised before the Commission and in the media about the efficacy of ASIC and APRA in attempting to improve the culture of regulated organisations through a “top down” compliance based approach. Perhaps this is based on what appears to be their approach of being directed primarily at protecting the market, not consumers of financial services. ASIC in evidence to the Commission stated that their role was to oversee compliance by advisors with the law, not to supervise or monitor their work.

Perhaps a better approach would be to require those that provide financial services within banks, financial Services firms, Insurance Companies etc., should be required to meet high ethical standards, set by a Professional Association of which they are required to be members, and be held against those standards externally from their employer organisation, by that Professional Association, in a similar way that Lawyers and Certified Public Accountants are so regulated.

The Commissions Interim Report makes reference to proposed changes to educational requirements of financial service providers, improved supervision of those providers and the work by FASEA in developing a Code of Ethics for the industry. The Report also suggests that such Code might be dealt with by Part IV B of the Competition and Consumer Act as an “Applicable Industry Code” and thereby potentially enforceable. While this could be a useful step in improving ethical behaviour within the industry due to its deterrent and potential reputational impact, my concern is that any enforcement would be directed at the organisation rather than the individual the subject of a complaint.

Further, the Report notes that when the proposed amended regulatory provision come into effect, all financial advisers must become members of a “code monitoring body” (eg: AFA or FPA). While this requirement goes some way towards achieving oversight of individual behaviour within financial service organisations, I would suggest that it could go further. It is my submission that the relevant code monitoring body (Professional Association) should have the power not only to exclude a member in breach of the code from membership in the body, but where appropriate, to remove their ability to practice entirely. This would require the code monitoring body, or Professional Association as it would become known, to have the power and authority to do so, either by statute or recognition through a Professional Standards Scheme, in a similar way to how lawyers are regulated.

Cultural change for financial service providing organisations will, I believe be slow. The wave of public reaction to the findings to date of the Commission will fuel this change. However, it is my submission that an additional, and potentially more successful and expeditious method in achieving cultural change and client protection within the financial services industry could be achieved by requiring the professionalization of financial services providers.

Sincerely,

Steve Mark AM

