

ASIC rapped over financial scrutiny

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By John Garnaut

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THE corporate regulator was so overwhelmed by the burden of supervising the new financial services regulatory regime that it issued licences without properly scrutinising applicants or recording reasons for decisions, the Auditor-General has found.

The Financial Services Reform Act was intended to impose stringent, consistent and consumer-friendly standards on every kind of financial service. Instead, it is being held up by business as Exhibit A in the case for cutting red tape.

A damning report by Auditor-General Ian McPhee found only a fraction of the expected number of financial services are licensed - raising the possibility that many financial planners, dealers and insurance brokers have chosen to evade the complex regulatory system altogether.

Pamela Hanrahan, associate professor of law at Melbourne University, said the flawed design of the regime forced the Australian Securities and Investments Commission to make administrative decisions that should have been made by industry bodies.

"ASIC by nature will err on the side of caution. This has resulted in an overly complex and insufficiently focused regulatory regime that business is entitled to complain about. The intention was right, the drafting was adequate but the problem was design."

ASIC had expected to issue between 6000 and 8000 licences by March 10, 2004. But by June 2005, more than a year after the transition to the new regime, only 4135 licences had been issued.

And ASIC still struggled to cope with the lower number.

It dealt with a late influx of applications "by reallocating resources from other activities, such as the surveillance of licences, and by curtailing analysts' scrutiny of applications," the Australian National Audit Office report said.

ASIC also cut corners by failing to write down why it accepted or rejected applicants - in breach of principles of administrative law.

ASIC defended its strategy and procedures and blamed the poor quality of applications.

"We would not agree with the conclusion that this was due to any inefficiency in the licensing process," ASIC said in a statement to the Auditor-General. "Rather this was driven by workload and by the generally poor quality of the majority of the licence applications."

ASIC was also responsible for educating the public and guiding businesses through the licensing regime.

The Auditor-General noted ASIC's early estimates of the number of licences required were even further off the mark. Only 251 superannuation funds had been licensed by May 2004, compared with an expected 1576. Only 16 out of 100,000 expected small general insurers, brokers and agents received licences. And only 799 financial planners were licensed - less than a third of the 2500 expected.

The Auditor-General also criticised the limited surveillance activity that ASIC did perform on financial service providers.

Half of all surveillances were recorded as requiring no further action, when action was in fact required.

The report did not look in detail at the quality of product disclosure statements (previously called prospectuses).

But it noted that almost a third of statements examined by ASIC required "significant changes" - raising serious questions about the quality of information available to consumers under the new regime.