ASIC review should make it smarter

Refocusing ASIC on stakeholders and regulation, writes **Pamela Hanrahan**, could enhance market efficiency.

The Australian Securities and Investments Commission's announcement last week of the results of its strategic review was well timed.

ASIC chairman Tony D'Aloisio decided to conduct the review some months ago, before the extent of the current market correction and its impact became apparent. That ASIC can now release and act on its findings means both D'Aloisio and Superannuation Minister Nick Sherry can be seen to be "doing something", without being forced into hasty policy or legislative change.

The review's big-picture items are the decisions to reorganise ASIC along "stakeholder" lines, and to devote a greater share of its resources to market regulation. Their significance lies in what they say about the direction financial regulation has taken in Australia since Stan Wallis's Financial System Inquiry released its final report a decade ago.

A key finding of the Wallis report was that the old regulatory system was piecemeal and varied, determined along path-dependent, institutional lines rather than functional ones.

This piecemeal approach was seen "as being inefficient, as giving rise to opportunities for regulatory arbitrage, and in some cases leading to regulatory overlap and confusion".

Regulation was reorganised along functional lines, aggregating all market-integrity and consumer-protection regulation in ASIC and bringing disparate financial service providers, financial markets and financial products together under a single regulatory umbrella.

Among this model's limitations are the dangerous signal it sends to retail investors that because different markets or products are similarly regulated, they carry with them similar risk. More directly, this "one-size" approach makes it difficult for ASIC staff to understand and respond to the particular issues arising in specific parts of the sector.

The decision to abolish ASIC's four existing directorates (regulation, compliance, enforcement and consumer protection) and to replace them with "17 outwardly-focused stakeholder teams covering different parts of the financial economy" (such as investment managers, investment banks, superannuation funds and financial advisers) must be understood in this context.

The challenge, of course, is to ensure that the change does not result in recurrence of the very problems (inefficiency, inconsistency or gaps) targeted by the Wallis report, particularly for regulated entities, or new products and services covered by more than one of these new teams.

The decision to refocus resources on market regulation is also important. The challenge for regulators everywhere is to maintain balance between the three main goals of financial regulation: investor protection, efficiency, and stability.

The short-term pressure on regulators to concentrate their resources on the first of these goals is often intense, particularly when retail participation is high and occurring across the risk spectrum.

In these circumstances, the line between investor protection (which assumes that risk has been properly disclosed and knowingly incurred) and consumer protection (which does not) can become blurred.

But protecting individual investors is not enough on its own to achieve the other goals. Devoting sufficient resources to activities that support greater market efficiency by forcing transparency is also crucial.

The decision to spill existing executive director and director positions, reducing their number from 54 to 41, and opening them up to both internal and external candidates, provides a good opportunity for renewal at the upper levels of an organisation that is now nearly 20 years old.

Hopefully the flattened management structure also signals a greater level of direct responsibility for regulatory decision-making by the membership of the commission itself, which has sometimes appeared unsure of its proper role.

It is harder to be enthusiastic about the proposal for the Expert Advisory Panel, which may at best confirm problems with market access or information at the commission level that should not exist, and at worst a pre-emptive strike against calls for an external review panel with power to address regulatory myopia or curb its excess.

But the review's focus on building ASIC's intellectual capital is welcome. In complex regulatory systems like that administered by ASIC, intellectual ability and agility is at least as important as market savvy.

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