ASIC’s focus on culture, governance and pay

ASIC continues to ramp up its focus on corporate culture.

On 31 August, the Australian Securities and Investments Commission (ASIC) published their corporate plan for the next four years. According to their report, one of their major priorities for the years ahead is to “promote investor and financial consumer trust and confidence.” ASIC plans to accomplish this by promoting positive and transparent gatekeeper conduct and culture.

ASIC’s focus for at least the next 4 years suggests that company boards respond by ensuring corporate culture is a more permanent and regular feature of the oversight process.

“A positive culture and corresponding conduct is central to investor and financial consumer trust and confidence, market integrity and growth.” According to ASIC’s chairman, Greg Medcraft, culture, incentives and deterrence are the main drivers of gatekeeper behaviour. By focussing on these areas, ASIC can work to ensure that investors and financial consumers can trust gatekeepers to make decisions in their best interest.

Within the group of gatekeepers, focus will be placed on responsible entities, lenders, markets and director, auditor and insolvency practitioners.

1. Responsible Entities (e.g. fund managers)

a) ASIC’s goal: Improve culture incentives, including weak compliance systems, in order to prevent investor losses

b) Plan of Action: To promote this desired culture, ASIC will increase surveillance and monitoring on areas where misconduct
and risks to trust and confidence are highly probable for responsible entities, including:

- Reward and incentive structures, including promotions
- Recruitment and training policy
- Whistleblowing policy
- Conflicts of interest
- Nature and level of complaints and complaint handling
- Remediation policy and procedures
- Corporate governance frameworks to support customer-centric culture
- Innovations and new financial products and services

2. Lenders

a) ASIC’s Goal: Promote responsible lending practices and curtail lenders from selling products that result in financial difficulties for borrowers

b) Plan of Action: ASIC will increase surveillance on:

- Interest only loans
- Finance broker compliance
- Pay day lending
- Consumer leases

3. Markets

a) ASIC’s Goal: Reduce conflicts of interests arising from remuneration that can affect market integrity and investor outcomes

b) Plan of Action:

- Identify poor practices and systems in managing conduct risk... by issuers, brokers and investment banks
- Focus on business models, transactions and activities that pose a high conduct risk
- Act to improve standards and behaviour in handling confidential information by issuers, brokers and
investment banks, and handling conflicts of interest by investment bans, with a particular focus on analysts

- Focus on conduct risk in wholesale markets, such as the manipulation of financial market benchmarks and the practices of investment banks

4. Directors, auditors and insolvency practitioners

a) ASIC’s goal: Identify and report inappropriate conduct of principals to reinforce market integrity and investor outcomes

b) Plan of Action:

- See to improve the quality of information provided to investors and the market, including through enhancing audit quality, financial reporting and other disclosures
- Take action against gatekeepers who do not keep markets, investors and creditors properly informed
- Focus on ensuring gatekeeper competence and independence, and aim to prevent improper gain

What are the overall implications for remuneration and governance? First and foremost, remuneration of those in a financial advisory role cannot lead to a conflict of interest. It should promote behaviour that will coincide with the best interests of investors and financial customers. Cultures of openness, honesty and integrity must be upheld in companies, throughout all levels.

The report states: “Remuneration, incentives, performance management and promotions can act as motivators and reinforce behaviour. They should be linked to a firm’s values at all levels, and should act as a mechanism to reward good behaviours and penalise good conduct.”

To an extent the increasing investment of banks and others in robots to provide financial advice may be an effective response to some of the cultural issues identified by ASIC. Coincidentally it should save the banks a lot on commission
costs as a few hundred technologists and their robots replace thousands of advisers. As these develop, it may be interesting in the future to see how a technician’s incentives are related to their algorithm’s ability to generate business.

More broadly, listed company boards may well consider formally including corporate culture as part of their regular oversight process. This may mean revisiting the board remuneration committee’s charter.

To read more on ASIC’s four year plan, click HERE.