Australian Government

Improving Australia's financial system

Government response to the Financial System Inquiry

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IMPROVING AUSTRALIA'S FINANCIAL SYSTEM

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Foreword

We are pleased to release the Government's response to the Financial System Inquiry.

The Coalition made an election promise on 25 October 2010 to conduct a root and branch examination of Australia's financial system. This promise was delivered with the final report of the Financial System Inquiry, led by David Murray AO, and publicly released on 7 December last year.

The Hon Scott Morrison MP

The Hon Kelly O'Dwyer MP

The financial system affects all Australians.

The financial sector is the largest in our economy, having contributed $139 billion over the past year and employing around 400,000 Australians.

The financial system has a vital role in commercial activity across the Australian economy, contributing to productivity and growth. The biggest decisions Australians make in life — buying a home, providing for their retirement, or starting a business — are all supported by our financial system.

As the attached response details, the Government has accepted the overwhelming majority of the Inquiry's recommendations. Our response also includes six additional measures that are consistent with the Inquiry's underlying philosophy.

The Government's response sets out an agenda for improving our financial system that builds on existing Government policy. The Government's financial system program will be implemented in stages over the coming years. The Government's program will position Australia to respond to the challenges and opportunities of the future.

We are confident that as a result of these changes, Australia can continue to benefit from the best financial system in the world.

The Hon Scott Morrison
Treasurer

The Hon Kelly O'Dwyer
Minister for Small Business and Assistant Treasurer

Government response to the Financial System Inquiry

The Government established a Financial System Inquiry ('the Inquiry') in late 2013, delivering on our election commitment to hold a root and branch examination of Australia's financial system.

The Inquiry, chaired by Mr David Murray AO, was asked to make recommendations that would position the financial system to best meet Australia's evolving needs and support economic growth. The Inquiry found that Australia has a well performing financial system. The Government's response will ensure it is the best in the world.

Following extensive domestic and international consultations, the Inquiry delivered its final report to the Government on 28 November 2014. When releasing this report, the then Treasurer announced a period of consultation to help inform the Government's response to the Inquiry's final recommendations. More than 180 written submissions were received, complemented by extensive stakeholder engagement through meetings and roundtables.

The Government's Financial System Program

Our response to the Inquiry builds on existing measures. In doing so, we are setting out an agenda for improving our financial system.

This agenda aims to:

- strengthen the resilience of the financial system;
- improve the efficiency of the superannuation system;
- stimulate innovation in the financial system;
- support consumers of financial products being treated fairly; and
- strengthen regulator capabilities and accountability.

We all have a vital stake in the operation of our financial system.

The financial system touches the life of every individual, family and business. We rely on the financial system for the multiplicity of transactions undertaken in any week. The financial system helps us manage our household budgets, holds our savings, provides the credit we need and, through insurance, helps us manage risks we face. Our largest lifetime undertakings — including purchasing a home, providing for our retirement or starting a business venture — are all supported by the financial system.

A competitive, innovative and efficient financial system supports the operation of the whole economy. In recent years, we have seen how important the resilience of our banks is during global shocks.

The financial system, like so many other parts of our lives, is being transformed by technological change, innovation and globalisation. If Australia fails to adapt to these developments to take the opportunities they present while managing evolving risks we will fall behind the rest of the world.

If consumers are overcharged or treated unfairly, the losses they incur adversely affect the whole community. And as the population ages, the cost of inefficiencies in our superannuation policy framework will escalate.

Our financial system program is made up of five distinct strategic priorities that deal with each of these challenges.

- The resilience measures aim to reduce the impact of potential future financial crises by ensuring we are better able to weather them and lessen their cost to taxpayers and the economy.
- The superannuation and retirement incomes measures aim to improve the efficiency and operation of the superannuation system and in doing so boost retirement incomes.
- The innovation measures will unlock new sources of finance for the wider economy and support competition.
- The consumer outcomes measures are designed to give consumers confidence to participate in the financial system and the confidence that they are being treated fairly.
- The regulatory system measures aim to make regulators more accountable for their performance, more capable and more effective.

These priorities are discussed below. Further detail is provided in the attachments.

Resilience Measures

Australia weathered the last financial crisis well, but this does not guarantee immunity from future shocks. We cannot be complacent.

Our financial system is strong, stable and well regulated, but has a number of systemic features which represent potential vulnerabilities. Our banks source a considerable share of their funding offshore, reflecting Australia's position as a net importer of capital. Banks provide close to 90 per cent of the domestic credit that local firms and households receive. Our major banks have also adopted similar business models, with home mortgages accounting for around 60 to 70 per cent of their domestic lending. This creates some concentration of risk in the system.

For these reasons, Australia's financial sector regulatory framework needs to be stronger than those of comparable economies. The resilience measures will ensure the banking system is more stable by holding more capital, and will address risk weights, leverage, loss absorbency and regulators' crisis management powers. The Inquiry's focus on bank capital builds on the actions already taken to bolster bank liquidity arrangements in recent years. Both the content and timing of regulatory changes will take into account developments in the Australian economy and in international financial regulatory frameworks.

In simple terms, these measures aim to ensure our financial system remains robust in the face of severe external shocks. The system must be able to maintain its core economic functions in crisis circumstances, including the provision of credit to households and firms. By requiring banks to take greater responsibility for their own resilience, the need for taxpayer-funded bailouts is reduced. The measures reduce the advantages the larger banks have over their smaller counterparts, increasing competition and leading to better outcomes for consumers.

Specific measures:

To date: The Australian Prudential Regulation Authority (APRA) released an international capital comparison study on 13 July 2015.

On 20 July 2015 APRA announced an increase to mortgage risk weights for our larger banks which will improve the resilience of the banking system to crises and promote competition. The major banks have subsequently undertaken capital raisings to increase their capital ratios.

By end-2015: Develop legislation to facilitate participation of Australian entities in international derivative markets and better protect client monies.

By mid-2016: Consult on measures to ensure financial regulators have the tools they need to manage any future financial crisis.

By end-2016: APRA to take additional steps to ensure our banks have unquestionably strong capital ratios.

Beyond 2016: APRA to ensure our banks have appropriate total loss-absorbing capacity and leverage ratios in place.

Superannuation Measures

Superannuation is the largest financial asset many Australians have after the family home. Millions of Australians rely on their superannuation to provide income in retirement. The superannuation system has accumulated over $2 trillion in assets, making it the second largest part of the financial system.

It is critical that the superannuation system is competitive, efficient and transparent and has the highest standards of governance. Australians must have confidence to invest in this system and plan for their retirement. By providing retirement incomes for millions of individuals, the superannuation system encourages greater self-reliance.

We will enshrine the objective of the superannuation system in legislation. This will help align policy settings, industry initiative and community expectations.

There is scope to improve the performance of the superannuation system in a number of areas. The system is fragmented, costly, complex and suffers from a lack of member engagement. Increased member engagement could improve member outcomes broadly, including putting downward pressure on fees and improving after-fee returns. In the retirement phase, the development of new income stream products can better protect retirees from longevity and other risks. Governance can be improved and conflicts of interests can be better managed.

We have already introduced legislation to improve governance in superannuation, committed to enhance transparency of information and to improve competition in superannuation, but more needs to be done. We will implement a number of changes which build on existing commitments to boost efficiency and competition.

We will immediately task the Productivity Commission to develop and release criteria to assess the efficiency and competitiveness of the superannuation system. We will also immediately task the Productivity Commission to develop alternative models for a formal competitive process for allocating default fund members to products. Subsequent to the development of criteria and following the full implementation of the MySuper reforms, we will task the Productivity Commission to review the efficiency and competitiveness of the superannuation system. We will also explore additional measures to improve the efficiency and competitiveness of the current system.

We will develop legislation to allow trustees of funds to provide pre-selected retirement income products to help guide members at retirement and improve outcomes for retirees, including through increased private retirement incomes, increased consumer choice and better protection against longevity and other risks. We will also continue our work to remove impediments to product development.

Specific measures:

By end-2015: Develop legislation to improve governance and transparency in superannuation. Progress the Retirement Income Streams Review. Task the Productivity Commission to immediately develop and release criteria to assess the efficiency and competitiveness of the superannuation system and to develop alternative models for a formal competitive process for allocating default fund members to products.

By end-2016: Develop and introduce legislation to enshrine the objective of the superannuation system. Consult on legislation to facilitate trustees of superannuation funds providing pre-selected comprehensive income products for retirement.

Beyond 2016: Implement legislation to introduce director penalties. Consult on legislation to improve member engagement, consistent with the recommendations in the Inquiry. Monitor leverage and risk within the superannuation system.

Innovation Measures

Innovation in the financial sector is always transforming the financial system and this is likely to continue. New payment methods, innovative funding sources, better use of customer information and deeper cross-border linkages promise enormous opportunities, if properly harnessed. Our policy settings must facilitate entry of these disrupters rather than acting as a blockage.

The development of a crowd sourced equity funding market in Australia is an urgent priority for the Government to support the funding needs of early stage innovators. We will consult on draft legislation to implement this framework before the end of 2015.

We are also already working on proposals in the areas of trusted digital identities, the Asia Region Funds Passport and 'simple' corporate bonds.

We will establish a public-private Innovation Collaboration Committee to give innovation champions a direct voice to contribute to the development of policy. We will develop a plan to ensure that our laws and regulations are technology-neutral. When implemented, this will have a major deregulatory impact.

We will increase the efficiency of the payments system and ensure it achieves fairer outcomes for consumers, merchants and system providers by phasing in a legislated ban on excessive card surcharges. The ACCC will be responsible for enforcing these rules.

The Payments System Board will pursue policies to address problems with interchange fees and provide clarity around what constitutes excessive customer surcharges on card payments. The Payments System Board released a consultation paper on these issues in March.

By better using available data firms can identify new opportunities, develop innovative products and lower costs. We will task the Productivity Commission to examine the scope to broaden access to, and use of, data. We support current industry efforts to expand data sharing under the new comprehensive credit reporting regime rather than through legislation.

We will examine how best to foster the growth of impact investment in Australia to support private and for-profit investment funds being directed to projects with a social or environmental purpose.

Specific measures:

To date: Passed legislation to extend the period before unclaimed banking monies in the banking and insurance sector are captured from three to seven years.

By end-2015: Consult on legislation to support crowd-sourced equity funding. Consult on crowd-sourced debt financing. Task the Productivity Commission to review access to and the use of data.

By mid-2016: Develop legislation to ban excessive card surcharges and better protect consumers using electronic payment systems. Develop legislation to reduce disclosure requirements for issuers of 'simple' corporate bonds. Establish the Innovation Collaboration Committee.

By end-2016: Give legal effect to the Asian Region Funds Passport initiative. Consider technology neutrality in financial sector regulation.

Beyond 2016: Facilitate rationalisation of life insurance and managed investment scheme legacy products.

Consumer Outcomes Measures

While consumers are responsible for the consequences of their financial decisions, they should be treated fairly. The financial services and products they purchase should perform in the way they are led to expect.

Recent history provides a number of examples of product and advice failures. While the circumstances of each case differ, problems have arisen when commercial incentives have overridden consumer interests.

We will do more to lift the standards of financial advisers, including by placing this activity on a professional footing for the first time. Following extensive stakeholder consultation, we will introduce legislation to make the issuers and distributors of financial products accountable for their offerings. This will ensure a stronger customer focus in product design and marketing. The new product design and distribution obligation will be principles-based rather than prescriptive and should be viewed as workable by the industry. Extensive consultation will be needed before these changes are implemented.

We will consult with stakeholders on the development of a new ASIC product intervention power that could be used to modify products, or if necessary, remove harmful products from the marketplace.

We will address the misalignment of incentives by reducing and improving the disclosure of conflicted remuneration in life insurance, stockbroking and mortgage broking.

We will also introduce legislation to facilitate innovative disclosure. This will help to unlock the productivity benefits that technology has to offer.

Specific measures:

By end-2015: Develop measures to address the misalignment of incentives in life insurance.

By mid-2016: Develop legislation which provides a professional standards framework for financial advisers. Consult on development of accountabilities for issuers and distributors of financial products and ASIC product intervention powers.

By end-2016: Develop legislation to give ASIC the power to ban individuals from managing financial firms. Consult on strengthening ASIC's enforcement tools in relation to the financial services and credit licensing regimes. ASIC will review remuneration arrangements in the mortgage broking industry.

Beyond 2016: Consult on and develop legislation to enable innovative disclosure for financial products and to improve the regulation of managed investment schemes. ASIC will review stockbroking remuneration arrangements.

Regulatory System Measures

The Inquiry found that while our regulatory architecture does not require major change, regulator accountability and capabilities should be strengthened.

Businesses have told us that they are not given sufficient time to implement regulatory changes, which are often complex. This represents a significant and growing compliance cost for them. In response, we will work with regulators to give businesses appropriate time to implement regulatory changes.

To strengthen the accountability of our regulators, we will review the Statement of Expectations for APRA, ASIC and the Payments System Board and increase requirements for the regulators' annual reports. A greater focus on performance assessment in these documents will ensure regulators are focusing on their capabilities and performance against their mandate.

The Government is already conducting a capability review of ASIC. We will consider any recommendations the review makes to further enhance the capability of ASIC. We will consider the Inquiry's recommendations on adopting a three year funding model for ASIC and APRA and the operational flexibility and staffing arrangements of ASIC and the other financial regulators in light of any findings by the capability review. We will also review ASIC's enforcement regime to ensure it provides a credible deterrent for poor behaviour and breaches of financial services laws. We have also commenced consultation on a model whereby ASIC's regulatory activities would be funded by industry.

We will strengthen the focus on competition in the financial system by explicitly including consideration of competition in ASIC's mandate and tasking the Productivity Commission to examine the state of competition in the financial sector in 2017.

Specific measures:

By end-2015: Complete a capability review of ASIC. Complete consultation on industry funding arrangements for regulatory activities undertaken by ASIC. Appoint new members and revise the Terms of Reference of the Financial Sector Advisory Council.

By mid-2016: Update the Statement of Expectations for APRA, ASIC and the Payments System Board to provide additional guidance about the Government's expectations for their strategic direction and performance and improve regulator accountability. Consider ASIC capability review and, as appropriate, develop legislation to enhance operational capabilities of regulators.

By end-2016: Introduce competition into ASIC's mandate.

Beyond 2016: Commence a review of ASIC's enforcement regime. Task the Productivity Commission to review the state of competition in the financial system

Attachment: Government's response to Financial System Inquiry Recommendations

Resilience	
Recommendation	**Government action**
Inquiry Recommendation 1 — Capital levels Set capital standards such that Australian authorised deposit-taking institution (ADI) capital ratios are unquestionably strong.	The Government agrees that the capital ratios of Australian banks should be unquestionably strong. This will ensure the financial system remains resilient during difficult times and will maintain investor confidence. We support and endorse APRA as Australia's prudential regulator to implement this recommendation and will continue to closely monitor the resilience of our banks. APRA released an international capital comparison study on 13 July 2015, which found that Australia's major banks' capital levels are currently below the top quartile of internationally active banks (the baseline target proposed by the Financial System Inquiry), even after adjusting for APRA's conservative approach to measuring capital.
Inquiry Recommendation 2 — Narrow mortgage risk weight differences Raise the average internal ratings-based (IRB) mortgage risk weight to narrow the difference between average mortgage risk weights for ADIs using IRB risk-weight models and those using standardised risk weights.	The Government agrees that the gap between average mortgage risk weights should be narrowed. This will aid competition in the banking sector. We support and endorse APRA as Australia's prudential regulator and its initial actions announced on 20 July 2015 to raise the average IRB mortgage risk weights to at least 25 per cent from 1 July 2016 to implement this recommendation. The major banks have subsequently undertaken capital raisings to increase their capital levels. We will take an active and ongoing role in monitoring developments as a result of these changes.

Resilience

Recommendation	Government action
Inquiry Recommendation 3 — Loss absorbing and recapitalisation capacity Implement a framework for minimum loss absorbing and recapitalisation capacity in line with emerging international practice, sufficient to facilitate the orderly resolution of Australian ADIs and minimise taxpayer support.	The Government agrees that steps should be taken to reduce any implicit government guarantee and the perception that some banks are too big to fail. Should an ADI fail, greater loss absorbing capital will facilitate orderly resolution. We endorse APRA as Australia's prudential regulator to implement this recommendation in line with emerging international practice.
Inquiry Recommendation 4 — Transparent reporting Develop a reporting template for Australian ADI capital ratios that is transparent against the minimum Basel capital framework.	The Government agrees that transparent reporting of the capital levels of Australian banks against the Basel framework will support Australian banks to access funding in international markets. We endorse APRA as Australia's prudential regulator to implement this recommendation.
Inquiry Recommendation 5 — Crisis management toolkit Complete the existing processes for strengthening crisis management powers that have been on hold pending the outcome of the Inquiry.	The Government agrees that regulatory settings should provide regulators with clear powers in the event a prudentially regulated financial entity or financial market infrastructure fails. This will ensure the smooth functioning of our financial system and promote a resilient financial system. We will consult on measures to clarify and strengthen regulatory powers by mid-2016.
Inquiry Recommendation 6 — Financial Claims Scheme Maintain the ex post funding structure of the Financial Claims Scheme for authorised deposit-taking institutions.	The Government agrees with this recommendation and as announced on 1 September 2015 will not proceed with the bank deposit tax and the associated Financial Stability Fund proposed by the previous Government.
Inquiry Recommendation 7 — Leverage ratio Introduce a leverage ratio that acts as a backstop to ADIs' risk-weighted capital positions.	The Government agrees that there may be situations when a risk weighted approach to capital requirements may lead to insufficient levels of capital and that a backstop would help to reduce systemic risk associated with over leveraged banks. We endorse APRA as Australia's prudential regulator to implement this recommendation in line with emerging international practice.

Resilience	
Recommendation	**Government action**
Inquiry Recommendation 38 — Cyber security Update the 2009 Cyber Security Strategy to reflect changes in the threat environment, improve cohesion in policy implementation, and progress public-private sector and cross-industry collaboration. Establish a formal framework for cyber security information sharing and response to cyber threats.	The Government agrees that an updated Cyber Security Strategy that is able to minimise the risk of a cyber-crisis in Australia is important for the resilience of the financial system. The Government announced a review of the Cyber Security Strategy on 27 November 2014. This recommendation will be progressed through that review.

Superannuation and retirement incomes	
Recommendation	**Government action**
Inquiry Recommendation 8 — Direct borrowing by superannuation funds Remove the exception to the general prohibition on direct borrowing for limited recourse borrowing arrangements by superannuation funds.	The Government does not agree with the Inquiry's recommendation to prohibit limited recourse borrowing arrangements by superannuation funds. While the Government notes that there are anecdotal concerns about limited recourse borrowing arrangements, at this time the Government does not consider the data sufficient to justify significant policy intervention. The Government will however commission the Council of Financial Regulators and the Australian Taxation Office (ATO) to monitor leverage and risk in the superannuation system and report back to Government after three years. This timing allows recent improvements in ATO data collection to wash through the system. The agencies' analysis will be used to inform any consideration of whether changes to the borrowing regulations might be appropriate.
Inquiry Recommendation 9 — Objectives of the superannuation system Seek broad political agreement for, and enshrine in legislation, the objectives of the superannuation system and report publicly on how policy proposals are consistent with achieving these objectives over the long term.	The Government agrees with the Inquiry's recommendation to enshrine the objective of the superannuation system in legislation. The Government will develop legislation to enshrine the objective within the superannuation law, where it will serve as a guide to policy-makers, regulators, industry and the community about superannuation's fundamental purpose. The objective will be a valuable yardstick against which to measure competing superannuation proposals, providing certainty that measures that do not accord with the objective will be held up to scrutiny. And it will provide a framework for important discussions Australia needs to have about fairness, adequacy and dignity in the superannuation system.

Superannuation and retirement incomes	
Recommendation	**Government action**
Inquiry Recommendation 10 — Improving efficiency during accumulation Introduce a formal competitive process to allocate new default fund members to MySuper products, unless a review by 2020 concludes that the Stronger Super reforms have been effective in significantly improving competition and efficiency in the superannuation system.	The Government agrees to task the Productivity Commission to immediately develop and release criteria to assess the efficiency and competitiveness of the superannuation system. The Government agrees to task the Productivity Commission to immediately develop alternative models for a formal competitive process for allocating default fund members to products. Subsequent to the development of criteria and following the full implementation of the MySuper reforms, the Government will task the Productivity Commission to review the efficiency and competitiveness of the superannuation system. The Government will also explore additional measures to improve the efficiency and competitiveness of the current system. While MySuper has been a strong step in the right direction, more needs to be done to reduce fees and improve after-fee returns for fund members.
Inquiry Recommendation 11 — The retirement phase of superannuation Require superannuation trustees to pre-select a comprehensive income product for members' retirement. The product would commence on the member's instruction, or the member may choose to take their benefits in another way. Impediments to product development should be removed.	The Government agrees to support the development of comprehensive income products for retirement and will facilitate trustees pre-selecting these products for members. Trustees' pre-selection of such products will help guide members at retirement. Comprehensive income products for retirement could improve outcomes for retirees, including through increased private retirement incomes, increased choice and better protection against longevity and other risks. The range of products available at retirement is currently narrow and does not always meet individuals' needs and preferences. We will continue work to remove impediments to retirement income product development. Further consultation is required to develop a principles based framework for pre-selection of a comprehensive retirement income product by superannuation trustees. This framework will be developed with regard to the outcomes of the Tax White Paper process and the Retirement Income Streams Review.

Superannuation and retirement incomes

Recommendation	Government action
Inquiry Recommendation 12 — Choice of fund Provide all employees with the ability to choose the fund into which their Superannuation Guarantee contributions are paid.	The Government agrees to extend the choice of fund arrangements to more employees by removing the deemed choice for certain enterprise agreements and workplace determinations.
Inquiry Recommendation 13 — Governance of superannuation funds Mandate a majority of independent directors on the board of corporate trustees of public offer superannuation funds, including an independent chair; align the director penalty regime with managed investment schemes; and strengthen the conflict of interest requirements.	The Government agrees with the need to improve the governance of superannuation funds. On 16 September 2015 we introduced legislation that requires superannuation fund trustee boards to have a minimum of one-third independent directors, including an independent chair. We support introducing penalty provisions and criminal sanctions for directors who fail to execute their duty to act in the best interests of members, or who use their position to further their interests or the interests of others to the detriment of members. We support APRA requiring board members to acknowledge when a director adds an interest to the conflicts register. This will ensure all board members are aware of interests.
Inquiry Recommendation 37 — Superannuation member engagement Publish retirement income projections on member statements from defined contribution superannuation schemes using ASIC regulatory guidance. Facilitate access to consolidated superannuation information from the ATO to use with ASIC's and superannuation funds' retirement income projection calculators.	The Government agrees that where practicable and cost effective, retirement income projections should be published on member statements. ASIC and the ATO will consider options to facilitate access to consolidated superannuation information. APRA and ASIC will present the data they currently collect in a more consumer-friendly manner.

Innovation

Recommendation	Government action
Inquiry Recommendation 14 — Collaboration to enable innovation Establish a permanent public-private sector collaborative committee, the 'Innovation Collaboration', to facilitate financial system innovation and enable timely and coordinated policy and regulatory responses.	The Government agrees to establish an Innovation Collaboration committee. Innovation is critical to unlocking productivity improvements in the financial system. However, emerging firms and start-ups often struggle to find a way of engaging with government. A permanent innovation committee will provide this point of entry. To avoid unnecessary duplication for industry, the Innovation Collaboration committee will be linked with ASIC's Digital Finance Advisory Committee.
Inquiry Recommendation 15 — Digital identity Develop a national strategy for a federated-style model of trusted digital identities.	The Government agrees that a national digital identity strategy will help to streamline individuals' engagement with government and provide efficiency improvements. The Digital Transformation Office will work across government and with the private sector to develop a Trusted Digital Identity Framework to support the Government's Digital Transformation Agenda.
Inquiry Recommendation 16 — Clearer graduated payments regulation Enhance graduation of retail payments regulation by clarifying thresholds for regulation by ASIC and APRA. Strengthen consumer protection by mandating the ePayments Code. Introduce a separate prudential regime with two tiers for purchased payment facilities.	The Government agrees that a graduated regulatory regime will support innovation. APRA, ASIC and the RBA will review the framework for payments system regulation and develop clear guidance. We will clarify powers held by ASIC and the RBA to ensure that regulators have the power to regulate new payment systems in a graduated way, such as digital currencies (e.g. Bitcoin) and other payment systems as they emerge. We will ensure that minimum acceptable practices consistently apply to the payments industry in the interests of consumers. ASIC will mandate baseline consumer protections in the ePayments Code, subject to the code being fit for purpose and technologically neutral. We will continue to monitor developments in the payments system and assess whether further action is required.

Innovation

Recommendation	Government action
Inquiry Recommendation 17 — Interchange fees and customer surcharging Improve interchange fee regulation by clarifying thresholds for when they apply, broadening the range of fees and payments they apply to, and lowering interchange fees. Improve surcharging regulation by expanding its application and ensuring customers using lower-cost payment methods cannot be over-surcharged by allowing more prescriptive limits on surcharging.	The Government agrees to take action to improve interchange fee and surcharging arrangements to achieve a more efficient system and fairer outcomes for consumers, merchants and system providers. We will phase in a legislated ban on surcharges that exceed the reasonable costs faced by merchants in accepting cards. We will also make the ACCC responsible for enforcing the ban on excessive surcharging. We look forward to the Payments System Board completing its work on interchange fees and customer surcharging through its *Review of Card Payments Regulation*. We will continue to monitor developments in the payments system, in particular surcharging arrangements, and assess whether further action is required.
Inquiry Recommendation 18 — Crowdfunding Graduate fundraising regulation to facilitate crowdfunding for both debt and equity and, over time, other forms of financing.	The Government agrees and committed to develop a regulatory framework to facilitate crowd-sourced equity funding through the 2015-16 Budget. The Government consulted widely on options in early 2015. The Minister for Small Business and Assistant Treasurer will consult on draft legislation to implement this framework by the end of 2015. The Government will consult the community on crowd-sourced debt funding in parallel with legislation to implement crowd-sourced equity funding.
Inquiry Recommendation 19 — Data access and use Review the costs and benefits of increasing access to and improving the use of data, taking into account community concerns about appropriate privacy protection.	The Government agrees to improve the use of data. This has the potential to unlock significant efficiency improvements in the financial system. We will task the Productivity Commission with reviewing options to improve accessibility to data, taking into account privacy concerns and other existing Government processes.

Innovation

Recommendation	Government action
Inquiry Recommendation 20 — Comprehensive credit reporting Support industry efforts to expand credit data sharing under the new voluntary comprehensive credit reporting (CCR) regime. If, over time, participation is inadequate, Government should consider legislating mandatory participation.	The Government agrees to support industry efforts to implement the CCR regime, but will not legislate for mandatory participation at this stage. The CCR regime has been in place for a little over a year and authorised deposit-taking institutions are still in the process of working to participate in the regime.
Inquiry Recommendation 32 — Impact investment Explore ways to facilitate development of the impact investment market and encourage innovation in funding social service delivery. Provide guidance to superannuation trustees on the appropriateness of impact investment. Support law reform to classify a private ancillary fund as a 'sophisticated' or 'professional' investor, where the founder of the fund meets those definitions.	The Government agrees that impact investing has the potential to benefit government and taxpayers. We will develop legislative amendments to provide greater certainty for private ancillary funds wishing to invest in social impact bonds. The provision of guidance to superannuation trustees on their fiduciary duties will be a matter for APRA to consider. We will prepare a discussion paper to explore ways to facilitate development of the impact investment market in Australia, and introduce legislative amendments if necessary.
Inquiry Recommendation 33 — Retail corporate bond market Reduce disclosure requirements for large listed corporates issuing 'simple' bonds and encourage industry to develop standard terms for 'simple' bonds.	The Government agrees to develop legislative amendments to modernise and simplify disclosure requirements for large corporates issuing 'simple' corporate bonds to the retail market. We are working with ASIC and market participants to assess the need for further improvements to support the corporate bond market.
Inquiry Recommendation 36 — Corporate administration and bankruptcy Consult on possible amendments to the external administration regime to provide additional flexibility for businesses in financial difficulty.	The Government agrees, and notes the Productivity Commission is undertaking an inquiry into barriers to business set up and closure, which released a draft report in May 2015. We will consider this recommendation as part of our response to the Productivity Commission's final report.

Innovation

Recommendation	Government action
Inquiry Recommendation 39 — Technology neutrality Identify, in consultation with the financial sector, and amend priority areas of legislation and regulation to be technology neutral. Embed consideration of the principle of technology neutrality into development processes for future regulation. Ensure regulation allows individuals to select alternative methods to access services to maintain fair treatment for all consumer segments.	The Government agrees to amend priority areas of legislation and regulation to be technology neutral. Technology-specific regulation can impede innovation and competition by preventing the adoption of the best technology or the most innovative business models. We will embed the technology neutrality principle into future legislation and regulation making. We will consult with the financial sector on priority areas of existing legislation and regulation that present regulatory impediments to innovation, before commencing work on any amendments.
Inquiry Recommendation 41 — Unclaimed banking monies Define bank accounts and life insurance policies as unclaimed banking monies only if they are inactive for seven years.	The Government agreed to implement this recommendation in the 2015–16 Budget. This change, in conjunction with a number of other improvements to the unclaimed banking monies provisions will commence from 31 December 2015. Legislation received Royal assent on 16 September 2015.
Inquiry Recommendation 43 — Legacy products Introduce a mechanism to facilitate the rationalisation of legacy products in the life insurance and managed investments sectors.	The Government agrees to facilitate the rationalisation of legacy products, in light of consumer, constitutional and fiscal issues. It is important that consumers should not be worse off due to any transition to a newer product. Under the existing framework there are possible tax implications of facilitating the transition away from legacy products, which will be explored in the context of the Government's Taxation White Paper process.
Inquiry Recommendation 44 — *Corporations Act 2001* ownership restrictions Remove market ownership restrictions from the *Corporations Act 2001* once the current reforms to cross-border regulation of financial market infrastructure are complete.	The Government will consider market ownership restrictions in the context of its response to the Council of Financial Regulators' *Review of Competition in Clearing Australian Cash Equities*.

Consumer outcomes

Recommendation	Government action
Inquiry Recommendation 21 — Strengthen product issuer and distributor accountability Introduce a targeted and principles-based product design and distribution obligation.	The Government agrees to create a targeted and principles-based financial product design and distribution obligation. Implementation of this recommendation will be subject to detailed consultation with stakeholders to ensure that the scope of the obligation enhances consumer protection without placing an undue burden on industry.
Inquiry Recommendation 22 — Introduce product intervention power Introduce a proactive product intervention power that would enhance the regulatory toolkit available where there is risk of significant consumer detriment.	The Government agrees to provide ASIC with a financial product intervention power to enable it to modify, or if necessary, ban harmful financial products where there is a risk of significant consumer detriment. Implementation of this recommendation will be subject to detailed consultation with stakeholders to ensure that the power strikes the right balance — providing ASIC with a tool to enable it to take action in exceptional instances, but without stifling industry innovation.
Inquiry Recommendation 23 — Facilitate innovative disclosure Remove regulatory impediments to innovative product disclosure and communication with consumers, and improve the way risk and fees are communicated to consumers.	The Government agrees that regulatory impediments to innovative product disclosure should be removed. We note efforts led by ASIC and the industry to promote innovative product disclosure. With the benefit of information received from these processes, we will develop legislation to remove any regulatory impediments identified when those processes are complete in 2017. We support the Inquiry's calls for industry-led initiatives to improve disclosure of risk and fees.

Consumer outcomes

Recommendation	Government action
Inquiry Recommendation 24 — Align the interests of financial firms and consumers Better align the interests of financial firms with those of consumers by raising industry standards, enhancing the power to ban individuals from management and ensuring remuneration structures in life insurance and stockbroking do not affect the quality of financial advice.	The Government agrees more can be done to better align the interests of financial firms and consumers. However, we intend to take a different approach to that recommended by the Inquiry for retail life insurance. We support the retail life insurance industry's proposed reforms as announced by the then Assistant Treasurer on 25 June 2015. The Government will consider the extent to which legislation and/or action by ASIC may be necessary to implement the industry agreement. A Government review in 2018 will consider whether the new industry arrangements for life insurance advice have better aligned the interests of firms and consumers. If the review suggests further reform, consideration would be given to the Inquiry's recommendation for a level commission structure or further extending the existing Future of Financial Advice provisions on conflicted remuneration to life insurance advice. The Government endorses ASIC reviewing the effect of current remuneration structures in stockbroking on the quality of consumer outcomes. The Government will also ask ASIC to examine remuneration structures in the mortgage broking sector. The Government will also develop legislation to allow ASIC to ban individuals from management within financial firms from operating in the industry.

Consumer outcomes	
Recommendation	**Government action**
Inquiry Recommendation 25 — Raise the competency of advisers Raise the competency of financial advice providers and introduce an enhanced register of advisers.	The Government agrees to develop legislative amendments to raise the professional, ethical and educational standards of financial advisers by requiring advisers to hold a degree, pass an exam, undertake continuous professional development, subscribe to a code of ethics and undertake a professional year. The details of the new standards will be set by an independent, industry funded body, which will be recognised in legislation. The Government will consult on appropriate transitional arrangements for existing advisers. The recently established register of financial advisers will be amended to clearly identify whether individuals meet the new standards and whether there are relevant bans, disqualifications or code breaches applicable to that individual. We will also restrict use of the term ‘financial adviser’ and ‘financial planner’ to those listed on the register. A statutory review in 2019 will consider whether this new regulatory framework has raised the professional standards of financial advisers–and whether further changes are required. The Government has already conducted extensive consultation on the PJC’s proposals in the first half of 2015. The Government will continue to consult on remaining elements of the PJC’s proposals. The Government will introduce legislation to raise the professional standards of financial advisers by mid-2016.
Inquiry Recommendation 26 — Improve guidance and disclosure in general insurance Improve guidance (including tools and calculators) and disclosure for general insurance, especially in relation to home insurance.	The Government agrees to support industry-led initiatives, including supporting specific proposals put forward by industry, to increase guidance and disclosure in general insurance, recognising that work is already underway.

Consumer outcomes

Recommendation	Government action
Inquiry Recommendation 34 — Unfair contract term provisions Support Government's process to extend unfair contract term (UCT) protections to small businesses. Encourage industry to develop standards on the use of non-monetary default covenants.	The Government agrees, as set out in our election commitment, to provide small businesses with the same protections against unfair terms as those that currently apply to consumers. Legislation to extend unfair contract term protections to small businesses was introduced to the Parliament on 24 June 2015. We note the Corporations and Financial Services Parliamentary Joint Committee (PJC) inquiry into the impairment of customer loans, and will consider the use of non-monetary default covenants in the context of the findings of the PJC inquiry.
Inquiry Recommendation 35 — Finance companies Clearly differentiate the investment products that finance companies and similar entities offer retail consumers from ADI deposits.	The Government agrees with the need to clearly differentiate financial products. We support APRA improving product differentiation for retail consumers while at the same time noting that the sensitivities of potential adjustments for particular sectors will need to be considered.
Inquiry Recommendation 40 — Provision of financial advice and mortgage broking Rename 'general advice' and require advisers and mortgage brokers to disclose ownership structures.	The Government agrees to rename 'general advice' to improve consumer understanding. We will consult with a wide range of stakeholders and conduct consumer testing before finalising the new term. We will also develop legislative amendments to ensure that financial advisers and mortgage brokers adequately disclose their relationships with associated entities.
Inquiry Recommendation 42 — Managed investment scheme regulation Support Government's review of the Corporations and Markets Advisory Committee's (CAMAC) recommendations on managed investment schemes, giving priority to matters relating to: • consumer detriment, including illiquid schemes and freezing of funds. • regulatory architecture impeding cross-border transactions and mutual recognition arrangements.	The Government agrees to develop legislative amendments to enhance the regulatory framework for managed investment schemes, drawing on the Corporations and Markets Advisory Committee report and a forthcoming Senate Committee Inquiry report.

Regulatory system

Recommendation	Government action
Inquiry Recommendation 27 — Regulator accountability Create a new Financial Regulator Assessment Board (FRAB) to advise Government annually on how financial regulators have implemented their mandates. Provide clearer guidance to regulators in Statements of Expectations and increase the use of performance indicators for regulator performance.	The Government agrees with the Inquiry's objective of strengthening the regulator accountability framework but does not support the creation of a new Financial Regulator Assessment Board. We consider that new requirements in the *Public Governance, Performance and Accountability Act 2013* (PGPA Act) and the Government's Regulator Performance Framework provide avenues to strengthen regulator accountability along with other existing mechanisms such as Parliamentary hearings. We will reconstitute the Financial Sector Advisory Council with refreshed Terms of Reference to include providing advice on the performance of the financial regulators by the end of 2015. We support providing regulators with clearer guidance in Statement of Expectations and consider that the PGPA Act requirements are consistent with the Inquiry's recommendation for increased use of performance indicators for regulator performance. We will update the regulators' Statements of Expectations in the first half of 2016, including providing a Statement of Expectations to the Payments System Board for the first time.
Inquiry Recommendation 28 — Execution of mandate Provide regulators with more stable funding by adopting a three-year funding model based on periodic funding reviews, increase their capacity to pay competitive remuneration, boost flexibility in respect of staffing and funding, and require them to undertake periodic capability reviews.	The Government agrees to periodic consideration of regulators' capabilities. We commenced a capability review of ASIC in July 2015 and will undertake other capability reviews as appropriate. We will consider the Inquiry's recommendations on adopting a three-year funding model for APRA and ASIC and the operational flexibility and staffing arrangements for each of the financial regulators after the ASIC capability review is completed. We will use the Statement of Expectations to require all financial regulators to consider and discuss their capabilities in each annual report.

Consumer outcomes

Recommendation	Government action
Inquiry Recommendation 29 — Strengthening ASIC's funding and powers Introduce an industry funding model for ASIC and provide ASIC with stronger regulatory tools.	The Government agrees to strengthen ASIC's enforcement tools in relation to the financial services and credit licensing regimes by developing legislative amendments to enable ASIC to: • approve changes of licensee control; • consider a broader range of factors in determining whether an applicant satisfies the 'fit and proper' test to be granted a licence; and • impose conditions on firms to address concerns about internal systems relating to serious or systemic conduct (including external reviews). We will review ASIC's enforcement regime, including penalties and the financial services licensing breach notification framework, in 2017. The Government released a consultation paper on an industry funding model for ASIC on 28 August 2015.
Inquiry Recommendation 30 — Strengthening the focus on competition in the financial system Review the state of competition in the sector every three years, improve reporting of how regulators balance competition against their core objectives, identify barriers to cross-border provision of financial services and include consideration of competition in ASIC's mandate.	The Government agrees to implement periodic reviews of competition in the financial sector. We will task the Productivity Commission to review the state of competition in the financial system by the end of 2017, three years after the completion of the Inquiry. Subsequent periodic reviews will be undertaken as appropriate. We support inclusion of competition in ASIC's mandate and we will develop legislation to introduce an explicit reference to consideration of competition in ASIC's mandate in the second half of 2016. We will also be clear in the Statements of Expectations that regulators should explain in each annual report how they have balanced competition with other elements of their mandates. We are addressing barriers to cross border trade in managed investment schemes through establishment of an Asian Region Funds Passport and we will legislate to give effect to the Asian Region Funds Passport in the second half of 2016.

Consumer outcomes

Recommendation	Government action
Inquiry Recommendation 31 — Compliance costs and policy processes Increase the time available for industry to implement complex regulatory change. Conduct post-implementation reviews of major regulatory changes more frequently.	The Government agrees to provide industry appropriate time to implement regulatory change. This will be reflected in Statements of Expectations to the regulators. The Government does not agree to conduct more frequent post implementation reviews (PIRs), as it has already implemented changes to strengthen the review regime in 2014. This included a new requirement to undertake PIRs five years after implementation of all proposals which have a major economic impact. Departments recently concluded a review of the Red Tape Reduction Framework and agreed that, where a proposal has a major economic impact and the final Regulatory Impact Statement diverges significantly from best practice, the Assistant Minister to the Prime Minister could bring forward the PIR to two years after implementation.

Additional Government action

Recommendation	Government action
Ensure participation in international derivatives markets.	The Government will develop legislative amendments to clarify domestic regulation to support globally coordinated policy efforts and facilitate the ongoing participation of Australian entities in international capital markets. We will develop legislative amendments in the second half of 2015.
Enhance retail consumer protections for client monies.	The Government will develop legislative amendments to improve protections for client monies held in relation to derivatives. These improvements are needed to ensure that investors' monies are adequately protected when held by intermediaries.
Clarify the definition of basic deposit products.	The Government will develop legislative amendments to amend the definition of a basic deposit product in the *Corporations Act 2001*. These amendments will provide certainty for businesses and consumers by clarifying how certain term deposit products are treated under the law.