

# Council of Financial Supervisors

*The Chairman of the Council of Financial Supervisors, Reserve Bank Governor Bernie Fraser, recently released the Council's 1994 Annual Report. The following passages draw on Chapter 1 of the Report, copies of which are available from the Reserve Bank.*

## The Council and its Aims

The Council of Financial Supervisors is a co-ordinating body which brings together the heads of Australia's main financial supervisory authorities. Its members are the Reserve Bank of Australia (RBA), which chairs the Council; the Insurance and Superannuation Commission (ISC); the Australian Securities Commission (ASC); and the Australian Financial Institutions Commission (AFIC). The Council was formed in 1992, following a recommendation by the 1991 Parliamentary Inquiry into Banking and Deregulation (the 'Martin Committee').

Council aims to enhance the quality of financial supervision and regulation in Australia by:

- facilitating exchanges of information bearing on the efficiency and health of the financial system;
- assisting each supervisor to be aware of, and to understand, developments in parts of the financial system outside his

particular area of responsibility;

- identifying important issues and trends in the development of the financial system as a whole; and
- avoiding unintended gaps, duplication or inconsistencies in regulation.

Council reports, and makes recommendations, to the Federal Treasurer (through the Parliamentary Secretary to the Treasurer) and other Ministers, as appropriate.

The Council encourages the harmonisation of regulatory requirements where the interests of agencies overlap. It does not, however, promote the application of identical standards to all financial institutions or products. Approaches to the protection of depositors and investors vary from one part of the financial system to another depending on a range of factors, including: the nature of the products in question and the degree of risk attaching to them; the numbers and characteristics of the institutions and investors involved; and the statutory responsibilities and community expectations of supervisors.

The Council is not itself a statutory body, nor is it a prudential supervisor or regulator in its own right. Its creation has not altered the individual statutory responsibilities and powers of its members, or replaced other channels of communication between them.

Through its Annual Reports, the first of which was released in 1993, the Council aims

to provide the public with an overview of regulatory and other trends in the financial system, together with commentary on particular issues affecting its members. Annual Reports of the individual members of Council contain further details about their responsibilities and activities.

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## Council Activities in 1994

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In 1993 Council agreed on guidelines for the effective supervision of financial conglomerates, where two or more agencies have supervisory responsibilities. These guidelines recognise the critical importance of information-sharing among supervisors responsible for different parts of conglomerates. During 1994 Council members agreed to pursue legislative changes necessary to facilitate such information sharing, as well as establishing operating guidelines for the exchange of data.

During 1995 Council will be further considering aspects of conglomerates, including the supervisory treatment of holding companies.

The States have been reviewing supervisory arrangements for State-regulated financial institutions, such as friendly societies. In January 1994, Council wrote to the Federal Treasurer lending its support to a proposal that friendly societies be supervised under a uniform national framework, with AFIC as the co-ordinating and standard-setting body. Council argued that this would build on arrangements already in place for building societies and credit unions and help to minimise supervisory costs and overlaps. That proposal is now being implemented and is expected to be in place in 1995. In similar vein, Council is taking an interest in discussions on the regulatory framework for trustee companies.

During the year, Council discussed many other issues affecting two or more members. Notable among these was the regulation of derivatives, an issue which is receiving much

attention internationally. The Report provides some background on derivatives markets and their regulation. Council is helping its members to keep abreast of the various reviews in this area, as well as providing a forum to help avoid inconsistencies and overlap in regulations which might be proposed.

The Council also reviewed the financial institutions which operate outside the regulatory framework of its members. While sizeable in aggregate terms – representing around \$44 billion in assets or 5 per cent of the financial system – these diverse institutions are mainly government-owned and/or government-guaranteed entities. Their activities are considered unlikely to pose significant risks to financial system stability.

In addition to Council's own work, staff of Council members have contributed to task forces reviewing regulations in various areas, including derivatives, publicly-offered common funds and friendly societies, and the exemptions from accounting standards given to banks and life insurance companies.

More details on these and other matters are provided in the Report and its appendices.

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## The Framework of Supervision/Regulation

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The Council has an important role in ensuring that Australia's regulatory framework allows for a competitive and efficient financial system while promoting its stability and reliability. Council aims also to ensure that regulation in Australia is in line with community and government goals, and is consistent with overseas supervisory trends.

Council members appreciate that Australia's supervisory arrangements will need to evolve with changes in the structure of the financial system. The establishment of the Council was itself a recognition of the changes that were occurring and the need for adaptation. For the time being at least, members are not persuaded that 'megasupervisors' or 'lead regulators' need to be established; in their

view, the Council and the way it is developing in relation to financial conglomerates, will enable it to handle satisfactorily any policy issues which arise in this area.

Suggestions are sometimes made that prudential supervision should be organised on a functional, rather than the present institutional, basis. These seem misguided so far as the conduct of prudential supervision is concerned; to be effective, that can only be conducted on an institutional basis. On the other hand, regulation related to the disclosure of terms and conditions of financial services (sometimes called 'consumer protection' or 'investor education') is more amenable to a product or functional basis. It is already done

partly in this way: the ASC, for example, regulates primarily on a functional basis and the ISC is a functional regulator in respect of superannuation products. The recent development of broadly similar codes of practice for banks, credit unions and building societies is another example of functional standards being developed. Many consumer protection standards do, however, retain an institutional focus. As some financial services offered by different groups of institutions tend to converge, there could well be scope – in the interests of a 'level playing field' for similar products – to bring consumer protection standards more into line. Council will be investigating such possibilities during 1995.