**FSC Response to the Treasury Consultation: Industry codes in the financial sector**

Thank you for the opportunity to provide a submission on this topic.

**About the FSC**

The Financial Services Council (FSC) has over 100 members representing Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advisory networks and licensed trustee companies.

The industry is responsible for investing more than $2.7 trillion on behalf of 13 million Australians. The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Securities Exchange and is the fourth largest pool of managed funds in the world.

The FSC promotes best practice for the financial services industry by setting mandatory Standards for its members and providing Guidance Notes to assist in operational efficiency.

**Positioning of the Consultation**

FSC notes the positioning of the 28 June 2017 Position and Consultation Paper 4 *Industry Codes in the Financial Sector* (**Paper**). A central premise is that … *the existing regime, if bolstered by mandated participation and compulsory ASIC approval, is the preferred option*. This is a co-regulatory model and the Taskforce adopts in the Paper *a preliminary position consistent with the co-regulatory model.*

It proposes that:

- Position 1: The content of and governance arrangements for relevant codes (those that cover activities specified by ASIC as requiring code coverage) should be subject to approval by ASIC.
- Position 2: Entities engaging in activities covered by an approved code should be required to subscribe to that code (by a condition on their AFSL or some similar mechanism).
- Position 3: Approved codes should be binding on and enforceable against subscribers by contractual arrangements with a code monitoring body.
- Position 4: An individual customer should be able to seek appropriate redress through the subscriber's internal and external dispute resolution arrangements for non-compliance with an applicable approved code.
- Position 5: The code monitoring body, comprising a mix of industry, consumer and expert members, should monitor the adequacy of the code and industry compliance with it over time, and periodically report to ASIC on these matters..


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**FSC Response**

If the proposed regime were to be introduced, codes would effectively become quasi-regulations with the following potential consequences to the detriment of consumers:

- *Scaling back aspirational standards to the base level* – Codes are likely to set only base level standards which could undermine many existing aspirational best or good practice standards in Codes that benefit consumers.
- *Less agility* – Codes could become less agile in response to innovation, changing consumer needs and external influences.
- *Disincentives* – It could become a disincentive for industry to develop new codes and/or standards.
- *Less approachable* – Codes are currently written in consumer facing language but may become less approachable if effectively written as regulations.
- *Additional costs* – Additional costs to establish bodies to develop Codes

These points are explored in more detail below.

*Scaling back aspirational standards to the base level*

At paragraph 19, the Paper states (our emphasis) that *Each code would set out base level (rather than 'best practice') service standards* … This is to be contrasted with paragraph 5, which discusses the aims of the Life Insurance Code of Practice (**LICoP**) being developed to set standards of best practice for life insurers.[1]

If the regime were adopted, Codes would have to lower standards from "best practice" to "base level" to the significant detriment to consumers. If consumers need "base level" protections, surely this is the role of legislation and regulation. However, the Paper states at paragraph 19 that a Code *should not repeat or paraphrase existing legal obligations*. Accordingly, we are not entirely clear as level of obligation the Paper contemplates.

We believe that "voluntary" Codes have a key role in aiming to set aspirational "best practice" or good practice standards above the base level of regulation. This consultation confuses the two.

Codes currently allow industry to set aspirational best or good practice standards through self-regulation, which benefits consumers by going beyond legislated or regulated "base level" standards. Indeed, the Paper makes the point that Codes currently can be effective. At paragraph 8, the Paper states *Codes are able to provide efficient and effective dispute resolution, as well as having potential to improve industry practices*.

*Less agility*

A key advantage of voluntary Codes is that they can be agile – that is, developed and updated quickly in response to innovation, changing consumer needs and external influences. For example, the LICoP was developed in a little over 12 months. This raises the question about how agile Codes would be under a co-regulatory model.

For example, the foundation medical definitions in LICoP will need to be reviewed and updated regularly to reflect changes in Australian medical practice. If the proposed regime were to be introduced, it is questionable whether these medical definitions would be sustainable.

[1] The LICoP is an example of a Code which we refer to in this submission as a "voluntary" Code.

*Disincentives*

The proposed regime could have the unintended consequence of providing a strong disincentive for industry producing a Code. This would be unfortunate, because Codes provide a useful way to set agile and aspirational standards beyond legislated or regulated minimum standards that benefit consumers.

*Less approachable*

If, as proposed, Codes become enforceable it is likely that the drafting of Codes is likely to be framed more with a legal interpretation in mind, rather than as now where Codes can be written in plain language that is easy for consumers to understand. This raises the question about how approachable consumers would find any Codes produced under the proposed regime.

*Additional Costs*

The Paper states that Codes would be *formulated by an incorporated code body, the board of which includes an appropriate mix of industry representatives, consumer representatives and independent experts.*

We are not aware of any existing Codes that were formulated by bodies that meet these requirements, especially noting the requirements for the composition of boards. This raises important questions:

- What would be the status of existing Codes that were formulated by bodies that do not meet these requirements? Would these need to be re-formulated and, if so, at what cost?
- What additional costs would be required to set up and run such incorporated bodies for the purpose of developing and managing Codes? To understand this, a full Cost Benefit Analysis would be required which we have not yet seen.

**Existing powers**

The Paper highlights two issues that:

- The benefits of industry Codes are not available to significant numbers of consumers because not all players in relevant industry sub-sectors are code subscribers.
- Codes are not currently required to be approved by ASIC and therefore are not subject to a requirement to contain a minimum set of consumer protections or minimum standards on enforceability.

However, Government already has the means to address both these issues, and has already done so with the adviser standards legislation. This year, Government introduced legislation – part of the *Corporations Amendment (Professional Standards of Financial Advisers) Act 2017* **(Adviser Standards Legislation)** – which requires all financial advisers to be bound by a Code of Ethics – a Code monitored and enforced under Schemes approved by ASIC.

Generally, we express our concern with the position taken in the Paper that ASIC be given the power to specify activities as requiring code coverage with the content of and governance arrangements for the relevant code to be subject to ASIC approval.

In our view, if the Government feels that a code is required in a particular area, it should introduce specific legislation to address any particular issue as it did with the Adviser Standards Legislation. Certainly, in our view, industry should be free to develop and implement codes of practice and conduct – breach of which has implications for recalcitrant subscribers. The LICoP

is an example of this approach. Indeed, under the LICoP, consumers effectively achieve the benefits outlined in positions 3 and 4 of the Paper. That is, there is an independent body to review activities of insurers – the Life Code Compliance Committee (**LCCC**) – and consumers may take action under internal and external dispute resolution procedures. A non-compliant insurer may be subject to sanctions and, in extreme cases, faces expulsion from the FSC for failure to comply with an LCCC determination.

It does not seem to us to be an efficient process to have ASIC having such a wide-ranging power. For the reasons we have mentioned, we believe voluntary Codes are preferable and are likely to achieve similar outcomes to those which the Paper advocates. We are concerned that the establishment of a body to formulate Codes would add a layer of complexity and cost to areas which are more appropriately dealt with by industry.

Accordingly, our view is that Government already has the ability to implement mandatory codes where required and to confer this power on ASIC is not appropriate and, with all due respect to ASIC, is unlikely to be as effective or efficient as industry adopting voluntary Codes as required.

**Conclusion**

For the reasons set out above, we do not believe that the case has been made for these changes, especially given that the powers to address the issues raised already exist, and that the Paper gives no consideration to the option of "no change".

We strongly believe that:

- Industry should be free to choose to apply to have a Code approved by ASIC.
- Where the Government takes a view that there should be mandatory compliance with a particular code by all participants of the relevant sector, the government can, and should, legislate for this. The Adviser Standards Legislation is an example of this approach.

Overall, it appears that the proposed "co-regulation" model is materially closer to legislation and regulation than to self-regulation. Imposing a quasi-regulatory framework on industry self-regulation would impact industry's ability to develop and raise standards in a way which is flexible and can respond to changing industry and customer needs.