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Financial Services Reform Implementation Taskforce
The Treasury
Langton Crescent
PARKES ACT 2600

AND BY EMAIL: enforceablecodes@treasury.gov.au

These submissions are provided by the Finance Brokers Association of Australia Limited (**FBAA**) in response to the document circulated by the Treasury, entitled "Taking action on recommendation 1.15 of the Banking, Superannuation and Financial Services Royal Commission – Consultation Paper" (**Consultation Paper**).

Background of the FBAA

The FBAA is a professional association which represents approximately 8,500 finance brokers around Australia. The FBAA published a code of conduct which has been approved by the Australian Securities and Investments Commission (**ASIC**) as identified in Appendix B of the Consultation Paper.

The FBAA participates in only a small segment of the larger financial services industry. Accordingly, and generally, at this level, the need for government intervention within this segment would duplicate activities already undertaken by the FBAA or, to the extent that any newly implemented regulation or supervision would render any attempts by the FBAA to regulate the conduct of its members as pointless. Given Government's desire for industries to regulate themselves, such a choice would, in our submission, be considered a step in the wrong direction.

Primary Concerns

Despite the above observation, the FBAA is not opposed to Government prescribing what is expected from finance brokers. However, in the FBAA's view, there are a number of critical issues which must be addressed in order for any prescribed codes to be effective.

Current instability and risk of double jeopardy

As the Consultation Paper identified, the Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (**Royal Commission**) has made several recommendations which impact the financial services industry in different ways. Despite not being the initial target of the Royal Commission, the finance broker community has been significantly impacted by the Royal Commission, in particular, by its recommendation 1.3.

The FBAA observes that as the financial services industry is currently shifting to accommodate these recommendations. Accordingly, any attempt to draft an industry code based on the current state of the finance broker industry may become quickly obsolete due to other legislative changes which may be made in response to the Royal Commission recommendations.

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A particular risk identified is that the Final Report of the Royal Commission provided that the law should be amended so that finance brokers who fail to act in the best interests of the intended borrower will breach a civil penalty provision.[1] The Government agreed with this recommendation.[2] Any industry code would likely include a similar obligation. The FBAA is concerned that if this provision is included in an industry code in addition to being included in other legislation (for example, the *National Consumer Credit Protection Act 2009* (Cth)) imposing civil penalty liability, then a finance broker may become subject to two proscriptive provisions giving rise to two different penalty processes and regimes in respect of the same alleged conduct.

Accordingly, the FBAA considers that any development of industry codes can only be undertaken after the legislative changes to be introduced by Government have been examined and passed. If this process is followed, then industry codes can be developed to either identify and remedy gaps in legislation or to increase a targeted obligation imposed on the relevant individuals so as to drive consumer benefits through co-regulation.

Effectiveness of codes versus constitutionality

In an industry such as finance broking, where many individuals are involved, the FBAA raises whether mandatory codes implemented under a head of federal power are constitutional. We have not considered this aspect in any detail in the time available for response but raise it for Treasury consideration.

Questions on recommendation 1.15

Recommendation 1.15 of the Final Report of the Royal Commission provides:

The law should be amended to provide:

- that ASIC's power to approve codes of conduct extends to codes relating to all APRA-regulated institutions and ACL holders;
- that industry codes of conduct approved by ASIC may include 'enforceable code provisions', which are provisions in respect of which a contravention will constitute a breach of the law;
- that ASIC may take into consideration whether particular provisions of an industry code of conduct have been designated as 'enforceable code provisions' in determining whether to approve a code;
- for remedies, modelled on those now set out in Part VI of the Competition and Consumer Act, for breach of an 'enforceable code provision'; and
- for the establishment and imposition of mandatory financial services industry codes.

[1] FSRC, Final Report, vol 1, 20,recommendation 1.2.
[2] Australian Government Treasury, Restoring Trust in Australia's Financial System, 6.

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Question 1: What are the benefits of subscribing to an approved industry code

While FBAA has a code of conduct, it has not been formally approved by ASIC. Accordingly, the FBAA has not experienced any benefit from an "approved industry code".

In the FBAA's view, industry codes are valuable because they enable industries to co-regulate and develop specific expectations. This is vitally important in a broad industry such as the financial services sector where the objectives and functions of one segment differ from another. For example, it is inappropriate to have an industry code of conduct for the entire financial services industry because the functions of a bank are different from the functions of finance broker.

Self-developed industry codes are also more malleable and able to be more finely tuned than larger scale prescribed codes.

Question 2: What issues need to be considered for financial services industry codes to contain "enforceable code provisions"

The FBAA considers that only the core components of the relationship between a finance broker and their client should become subject to enforceable code provisions. Treasury's basis for enforceable code provisions appears to be such that they would allow a regulator to take action in circumstances where the consumer is unable to act further.[3] In an industry segment as populated as finance broking, if there are too many enforceable code provisions, then regulators may be faced with insufficient resources to pursue all matters that may come within their purview. Consequentially, this will undermine the overall effectiveness of implementing these provisions in the first place.

In the FBAA's view, in a finance broking context only, provisions which would be suited to becoming an enforceable code would include:

- providing legislatively-mandated disclosure;
- prescribing the making of reasonable enquiries of a client's income, assets, liabilities and repayment history; and
- maintaining adequate records of advice given to clients.

The obligation to act in the best interest of the client should not be an enforceable code provision because it is difficult to ascertain with precision what are the best interests of the client, particularly where a finance broker is not provided with all of the information required. In the FBAA's view, the penalty associated with this sort of obligation would be unfair.

Question 3: What criteria should ASIC consider when approving voluntary codes?

In the FBAA's view, ASIC should consider the following factors when approving voluntary codes:

[3] Australian Government Treasury, *Enforceability of financial services industry codes: Taking action on recommendation 1.15 of the Banking, Superannuation and Financial Services Royal Commission – Consultation Paper*, 5.

- whether the code does not merely repeat the obligations imposed by legislation – there is little benefit to be gained in allowing consumers to enforce, by way of contract, a provision of a code of conduct, where they may be able to prosecute or report the same obligation already.

- Whether the code itself sets out criteria to determine whether the obligation within the code has been breached – as most codes will not be drafted in a legislative fashion, it is crucial that each code is as self-contained as possible to avoid the need to review extrinsic materials to assist in interpretation; and

- Whether the code of conduct is procedurally fair – industry codes do not go through the same rigour as legislation so it is crucial than any approved codes have been considered from all sides.

The FBAA considers that the process for approving authorisations as conducted by the Australian Competition and Consumer Commission may be used to inform this process.

Question 4: Should the Government be able to prescribe a voluntary financial services industry code?

No, a voluntary industry code is designed to be voluntary. Any decision to prescribe such a code to make it mandatory undermines the purpose for its drafting. Additionally, as identified above, industry codes do not undergo the same drafting rigour as legislation so any attempt to prescribe a code could be considered a "short-cut" in place of ordinary legislative process.

Question 5: Should subscribing to certain approved codes be a condition of certain licences?

In the FBAA's view, this question is not specific. In an industry as broad as the financial services industry there may be circumstances where this is appropriate and circumstances it is not. Generally, the FBAA considers that should the Government decide to create further licence conditions then it should do that rather than mandating a code. A code should not be used as a "short-cut" in place of proper legislative process.

Question 6: When should the Government prescribe a mandatory financial services industry code?

Similarly, the FBAA does not consider a prescribed mandatory code of conduct for the entire financial services industry to be plausible given the size, breadth and scope of the industry. In respect of specific sectors of the industry, a prescribed mandatory code of conduct may be possible but only once all of the amendments and changes in response to the Royal Commission have been made. The FBAA consider this to be on and from 1 July 2020.

Question 7: What are the appropriate factors to be considered in deciding whether a mandatory code ought to be imposed on a particular part of the financial sector by Government?

The following factors should be considered:

1. Whether the constituents of that sector are predominantly corporations or individuals;

2. Whether the sector is already self-regulated;

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3. Does the code operate in respect of all functional levels of that sector of the market;

4. The number of regulators already involved; and

5. The number of participants in that sector.

Question 8: What level of supervision and compliance monitoring for codes should there be?

The level of supervision and monitoring for codes depends upon the sector, the number of participants and the number of regulators or other authorities already involved. If there are a large number of regulators or authorities already (such as in the finance broking sector where there is not only ASIC but also industry associations with codes of conduct and disciplinary processes – some of which have received authorisation from the ACCC already, and ombudsman services, then any further supervision and compliance monitoring would be an inefficient use of resources.

Question 9: Should code provisions be monitored to ensure they remain relevant, adequate and appropriate? If so, how should this be done and what entity should be responsible?

The party that is ultimately responsible for the code should be responsible for monitoring the code. In the case of a voluntary, industry developed code, the industry association responsible for the code should monitor its compliance. In the case of mandatory or ASIC-approved codes, ASIC should be responsible for monitoring and amending the code.

Question 10: Should there be regular reviews of codes? How often should these reviews be conducted?

The FBAA reviews its code of conduct every year. In its view, this is an appropriate time period for reviews to occur.

Question 11: Aside from those proposed by the Commissioner, are there other remedies that should be available in relation to breaches of enforceable code provisions in financial service codes?

In a finance broking context, the FBAA observes that some of the enforcement provisions and remedies are not appropriate. For example, disqualification from managing a corporation would be inappropriate as a finance broker does not need to manage a corporation in order to function. It can carry on business as an individual.

The FBAA considers that the other enforcement action available to the ACCC to manage its industry codes should be equally applicable to ASIC. In particular, the ability to investigate matters is crucial.

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Question 12: Should ASIC have similar enforcement powers to the Australian Competition and Consumer Commission (ACCC) in Part IVB of the Competition and Consumer Act in relation to financial services industry codes?

Yes, the FBAA considers that the other enforcement action available to the ACCC to manage its industry codes should be equally applicable to ASIC. In particular, the ability to investigate matters is crucial. It is noted that ASIC already has resources in that regard.

Question 13: How should the available statutory remedies for an enforceable code provision interact with consumers' contractual rights?

In circumstances where the statutory remedy and the contractual remedy can arise out of the same circumstance, the consumer should be put to an election of priority. For example, the consumer should be required to elect that it seeks statutory remedies or, in the alternative, the contractual remedy, or vice versa. A right to claim privilege arises if a party is being pursued for criminal or quasi-criminal conduct and in such cases a defendant would seek to plead privilege in any civil proceedings until any criminal quasi-criminal, civil penalty proceedings are concluded.

Question 14: Should only egregious, ongoing or systemic breaches of the enforceable provisions of an industry code attract a civil penalty?

No, in the case of finance broking, some companies may engage a series of consultants that are not employees and allow them to operate under that company's Australian Credit Licence. In this context, it would be unfair to the directors of the company where the ongoing or systematic breach is attributable to a non-employee in circumstances where the director is not aware of the behaviour.

Question 15: In what circumstances should the result of an external dispute resolution (EDR) process preclude further court proceedings?

Where a settlement arises, such settlements should always include a release so as to preclude further court proceedings. In the FBAA's view, financial service providers will refuse to participate, or will not genuinely participate, in dispute resolution if they are aware that settlement under the EDR process will not conclude the matter.

Question 16: To what matters should courts give consideration in determining whether they can hear a dispute following an Australian Financial Complaint Authority (AFCA) EDR process?

A court should consider the following matters when deciding whether to hear a dispute following an EDR process:

1. Whether one party was legally represented in the EDR process where the other was not (in other words, where there may have been an unfair process adopted - if both parties are not represented or both are represented then this should persuade the Court not to hear the dispute.

2. Whether there was a suitable disclosure of material information to the other in the EDR process - if one party withheld information in the process which was important then this should persuade the Court to intervene.

Question 17: What issues may arise if consumers are not able to pursue matters through a court following a determination from AFCA?

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Consumers may decide to pursue matters to a Court directly rather than seek a determination from AFCA thereby increasing costs.

Closing Remarks

The FBAA will continue to monitor the Government's response to the outcomes of the Royal Commission. If Treasury has any queries on the crucial issues that impact the finance broking sector, please do not hesitate to contact our organisation.

Yours faithfully,

Peter White
Managing Director, Finance Brokers Association of Australia.