Law Council
OF AUSTRALIA

*Legal Practice Section*

# Enforceability of Financial Services Industry Codes

**The Treasury**

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# Table of Contents

# About the Law Council of Australia

The Law Council of Australia exists to represent the legal profession at the national level, to speak on behalf of its Constituent Bodies on national issues, and to promote the administration of justice, access to justice and general improvement of the law.

The Law Council advises governments, courts and federal agencies on ways in which the law and the justice system can be improved for the benefit of the community. The Law Council also represents the Australian legal profession overseas, and maintains close relationships with legal professional bodies throughout the world.

The Law Council was established in 1933, and represents 16 Australian State and Territory law societies and bar associations and the Law Firms Australia, which are known collectively as the Council's Constituent Bodies. The Law Council's Constituent Bodies are:

- Australian Capital Territory Bar Association
- Australian Capital Territory Law Society
- Bar Association of Queensland Inc
- Law Institute of Victoria
- Law Society of New South Wales
- Law Society of South Australia
- Law Society of Tasmania
- Law Society Northern Territory
- Law Society of Western Australia
- New South Wales Bar Association
- Northern Territory Bar Association
- Queensland Law Society
- South Australian Bar Association
- Tasmanian Bar
- Law Firms Australia
- The Victorian Bar Inc
- Western Australian Bar Association

Through this representation, the Law Council effectively acts on behalf of more than 60,000 lawyers across Australia.

The Law Council is governed by a board of 23 Directors – one from each of the constituent bodies and six elected Executive members. The Directors meet quarterly to set objectives, policy and priorities for the Law Council. Between the meetings of Directors, policies and governance responsibility for the Law Council is exercised by the elected Executive members, led by the President who normally serves a 12 month term. The Council's six Executive members are nominated and elected by the board of Directors.

Members of the 2019 Executive as at 1 January 2019 are:

- Mr Arthur Moses SC, President
- Mr Konrad de Kerloy, President-elect
- Ms Pauline Wright, Treasurer
- Mr Tass Liveris, Executive Member
- Dr Jacoba Brasch QC, Executive Member
- Mr Tony Rossi, Executive Member

The Secretariat serves the Law Council nationally and is based in Canberra.

# About the Section

The Legal Practice Section of the Law Council of Australia was established in March 1980, initially as the 'Legal Practice Management Section', with a focus principally on legal practice management issues. In September 1986 the Section's name was changed to the 'General Practice Section', and its focus broadened to include areas of specialist practices including Superannuation, Property Law, and Consumer Law.

On 7 December 2002 the Section's name was again changed, to 'Legal Practice Section', to reflect the Section's focus on a broad range of areas of specialist legal practices, as well as practice management.

The Section's objectives are to:

- Contribute to the development of the legal profession;
- Maintain high standards in the legal profession;
- Offer assistance in the development of legal and management expertise in its members through training, conferences, publications, meetings, and other activities.
- Provide policy advice to the Law Council, and prepare submissions on behalf of the Law Council, in the areas relating to its specialist committees.

Members of the Section Executive are:

- Ms Maureen Peatman, Chair
- Mr Michael James, Deputy Chair
- Mr Geoff Provis, Treasurer
- Ms Tanya Berlis
- Mr Dennis Bluth
- Mr Mark Cerche
- Ms Peggy Cheong
- Mr Philip Jackson SC
- Dr Leonie Kelleher OAM
- Ms Christine Smyth

# Acknowledgement

In the preparation of this submission, the Law Council is grateful for the assistance of the Australian Consumer Law Committee of the Legal Practice Section.

# Executive Summary

1. The Law Council of Australia's Consumer Law Committee (**ACL Committee**) welcomes the opportunity to provide the following submission to The Treasury in relation to the Consultation Paper entitled *Enforceability of Financial Services Industry Codes*.

2. The Committee is one of the eight specialist committees of the Legal Practice Section. Each of these Committees approach issues of law reform and practice from a different perspective, which reflects their respective primary focus.

3. The recent Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (**Royal Commission**) revealed significant instances of misconduct, much of which occurred despite the fact that there were relevant codes of practice in place in relation to those entities. It is therefore timely to revisit the design of codes of practice to ensure that the learnings of the Royal Commission are acted upon.

4. A code of practice is a useful mechanism for providing industry and consumers with a set of accepted standards which will be abided. However, it is important in setting a code of practice that the code of practice has enforceability, accountability and transparency.

5. There has been much discussion in relation to the life insurance code of practice and the voluntary superannuation code of practice which have been introduced in the last few years. Whilst the introduction of a code of practice was a step forward in life insurance, there was some concern from the consumer movement about the first iteration of the life code, and the voluntary superannuation code.

6. If the industry, in signing up to a code, is agreeing to be bound to a set of standards, then it follows that the industry should also accept that a failure to abide those standards should result in sanctions for not meeting those standards. If there were no consequences for failures to meet the agreed standard set out in the code, then there would be little incentive for industry to meet those standards. Accordingly, without appropriate sanctions and real consequences there is a risk of undermining the effect of the code.

7. There is also an existing issue in relation to life and general insurance whereby a re-insurer is not covered by the code, but the primary insurer is. It is the view of the ACL Committee that if a re-insurer wishes to participate by re-insuring a particular line of insurance, it must be a signatory to the relevant code to ensure consistency and compliance and to prevent any gaps in regulation.

# Responses to Consultation Paper

## The benefits of subscribing to an approved industry code

8. It is in the interests of industry and consumers alike to ensure that there is a robust code of practice. In the area of life insurance, a robust code of practice should provide confidence to consumers that they can buy life insurance in the full knowledge that they can expect to be treated fairly and that the insurer can be held to account for their conduct, where their conduct falls short.

9. Industry will have a clear guideline as to how they ought to conduct themselves in selling, designing and handling insurance claims.

10. Importantly, for the code to achieve its objectives, there needs to be genuine consultation between the industry and consumer representatives. Inadequate consultation by industry risks undermining the code altogether.

## Enforceable code provisions

11. As stated above in the Executive Summary, if the industry is agreeing to be bound to a certain standard of conduct, there doesn't appear to be any persuasive reason why a failure to meet such standards shouldn't have consequences.

12. Such consequences may include:

    (a) civil penalties;

    (b) compensation; and

    (c) licensing consequences.

13. The *Corporations Act 2001* (Cth) (**Corporations Act**) already provides obligations on financial services providers (**FSP**) to act honestly efficiently and fairly.[1] An FSP who is in breach of their own code of conduct seems logically to be capable of being framed as a breach of the FSP's obligations under the Corporations Act. In the view of the ACL Committee, there is merit in making that explicit by legislation.

## The criteria to be considered when approving voluntary codes

14. Voluntary codes of practice carry some risk. First, there is a risk to consumers that a proportion of the industry will not sign up to the code. Secondly, there is a risk to competition in the industry that those who do sign up to the code may be at a commercial disadvantage to those who don't.

15. Accordingly, before approving any industry code, the Australian Securities and Investments Commission (**ASIC**) should consider at least the following:

    (a) the existing legislative framework and whether such a framework provides adequate protection to consumers;

    (b) whether there has been any systemic misconduct in the industry;

[1] *Corporations Act 2001* (Cth) s 912A.

(c) the extent, if any, of a power imbalance between consumers and the industry;

(d) the extent to which the industry has consulted in the consumer movement; and

(e) the proportion of the industry which has signed up to the code.

16. In relation to point (d) above, in considering the consultation with the consumer movement, ASIC needs to undertake a qualitative, not merely quantitative, assessment. That is, ASIC should require that industry produce a statement or letter from the consumer organisations which supports the proposition that the industry has conducted the consultation in good faith and in a genuine way. If such a statement or letter is not able to be produced, that should weigh heavily on ASIC's consideration of whether to approve a code.

## Prescribing a voluntary financial services industry code

17. The Royal Commission highlighted some widespread issues in the financial industry. There will be more Royal Commissions and other enquiries in the future in relation to other issues.[2] When such misconduct is revealed, it should be open to Government to prescribe a code of conduct as a requirement for participating as a business in that particular industry.

## Voluntary financial services industry code as a condition to financial services license

18. There is a significant power imbalance between the financial services industry and consumers. Given the findings of the Royal Commission, it would be timely to now require all financial services industries to adhere to appropriate codes of practice as a condition of their financial services license.

## Mandatory financial services industry code

19. The ACL Committee submits that a general financial services industry code may be too broad to be effective. That is, the insurance industry is very different to the banking industry, and the financial advice industry is different again.

20. It is the view of the ACL Committee that work should be undertaken to identify each of the relevant financial services that exist and to ensure that all financial services have their own code of conduct that is sufficiently particular to the services that each particular FSP provides.

21. Most importantly, there should not be any financial services which should not be covered by a relevant code of practice.

## Level of supervision and compliance monitoring for codes

22. As indicated in the Executive Summary to this submission, it is critical in relation to codes of practice to ensure that breaches of the code carry consequences.

23. A code of practice is a method of self-regulation of an industry and it should be recognised that there is significant underreporting of breaches of existing codes of

[2] See, eg., the recent Royal Commission into violence, abuse, neglect and exploitation of people with a disability.

practice. That is so because, in most instances, consumers do not lodge complaints to code administrators, and often don't know that a code administrator exists.

24. It is the view of the ACL Committee that a code of practice needs to have an audit and compliance monitoring function, which may consist of random audits of industry participants to ensure compliance with the relevant code. Code administrators must be appropriately funded to ensure that there are sufficient resources to undertake the audit and compliance monitoring function rather than simply reviewing the self-reporting of industry.

25. In addition, the ACL Committee believes that the code administrator should be required to report annually as to the performance of industry participants. Such a report should not be de-identified. That is, organisations who frequently breach the accepted norms of behaviour set out in the code of practice should not have the benefit of remaining anonymous. By ensuring such organisations are publicly named, there is incentive for organisations to adhere to the code.

## Regular reviews of codes

26. In the view of the ACL Committee, it is necessary to regularly review and update industry codes of practice. Codes of practice should have mandatory reviews every 4 years.

27. The ACL Committee does not have a view as to who should conduct the review other than to say that, as previously stated, is important in the development and review of any code of practice that there is suitable consultation that occurs with the consumer movement. The ACL Committee would assume that the consultation would occur between the industry peak body, whoever that might be, ASIC and relevant consumer representatives.

## Available remedies

28. In setting remedies relating to breaches of a code of practice, it is important to recognise that sometimes a breach of the code of practice may occur which does not necessarily cause any detriment to the consumer. However, there will be many circumstances in which a breach of the relevant code of practice will give rise to significant detriment to a consumer.

29. Accordingly, it is important that the remedies available in relation to a code of practice provide remedies which will put consumers right in circumstances where they have suffered detriment, and which will appropriately sanction/punish a financial services entity which has breach the code such as to create a deterrent for any similar future conduct.

30. The ACL Committee would recommend at least the following remedies be available:

    (a) civil penalties;

    (b) compensation/damages;

    (c) punitive orders (such as public naming and shaming);

    (d) enforceable undertakings; and

    (e) additional license requirements (such as further staff training/education obligations).

31. The ACL Committee notes that this list should not be considered as exhaustive.

## Interaction between statutory remedies for an enforceable code provision and consumers' contractual rights

32. The ACL Committee considers that statutory remedies for an enforceable code provision should be a binding term of the contract and able to be enforced by the consumer.

## Civil penalties

33. Civil penalties should be available as an option in respect of all enforceable provisions, not only in cases of egregious, ongoing or systemic breaches of the enforceable provisions of an industry code.

34. That is not to say that a civil penalty should be the automatic penalty. However, there will be some instances where an individual breach of the code will be egregious and accordingly, civil penalties should be available as an option.