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By email to: ProductRegulation@treasury.gov.au

Manager
Financial Services Unit
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The Treasury
Langton Crescent
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Dear Ms Moore

Design and Distribution Obligations and Product Intervention Powers

Thank you for the opportunity to comment on the exposure draft of the *Treasury Laws Amendment (Design and Distribution Obligations and Product Intervention Powers) Bill 2018* (**the Bill**).

The following organisations have contributed to and endorsed this submission:

- Australian Shareholders' Association
- Care Inc Financial Counselling Service and the Consumer Law Centre of the ACT

- CHOICE
- Consumer Action Law Centre
- Consumer Credit Legal Service (WA) Inc.
- Consumer Credit Law Centre SA
- Consumers Federation of Australia
- COTA Australia
- Financial Counselling Australia
- Financial Rights Legal Centre

Details about each contributing organisation are contained in **Appendix A**.

Executive Summary

We strongly support the integrated package of reforms proposed in the Bill, which we believe would significantly improve consumer[1] outcomes and improve trust and confidence in the financial system. The design and distribution obligations (**DADOs**) should help to achieve a cultural shift within financial firms away from simply ‘selling’ financial products towards designing and distributing suitable products that meet customer needs. Further, equipping the Australian Securities and Investments Commission (**ASIC**) with the product intervention powers would allow the regulator to intervene before consumer harm occurs and deter misconduct by financial firms.

Where this submission is silent on proposed reforms, we can be taken as being supportive. While we are supportive of the proposed reforms, we consider that the Bill should be strengthened in several key areas. Most importantly, we recommend that the new DADOs and product intervention powers apply to ‘financial products’ as defined in the *Australian Securities and Investments Commission Act 2001* (Cth) (**ASIC Act**). This would ensure that a broader range of financial products is captured by the reforms, including regulated and unregulated consumer credit.

We have made additional recommendations relating to DADOs, which include:

- strengthening the definition of ‘appropriate target markets’;
- specifying maximum target market determination review periods;
- reducing the transition period, particularly for existing products;
- extending ASIC’s stop order powers to a broader range of contraventions; and
- extending the civil liability regime to ensure that consumers are adequately compensated for loss or damage.

In relation to ASIC’s product intervention powers, our recommendations include:

- permitting interventions to continue until deemed appropriate to remove by ASIC or the Minister;
- empowering ASIC to make a broader range of interventions, particularly in relation to remuneration and training;
- specifying that the extent of ASIC’s consultation is to be commensurate with the assessed risk of detriment to consumers and the need for prompt intervention; and

[1] ‘Consumers’ include reference to ‘investors’ where appropriate. Indeed, we note that the objects of Chapter 7 are to be expanded by section 706A(a) “the provision of suitable financial products to consumers of financial products”; however, the word “consumer’ is not used in this sense elsewhere in the Bill, but ‘investors’ is (and more appropriately). The notion of consumer does not suit investment; since the regime is to cover investment products, we believe that the objects clause should refer to ‘consumers of and investors in financial products’.

- ensuring that affected consumers are appropriately notified in the event of an intervention.

We have provided further comments and recommendations below.

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DESIGN AND DISTRIBUTION OBLIGATIONS

Products subject to the obligations

Under the Bill, the obligations apply to offers of financial products that require a Product Disclosure Statement (**PDS**) or fundraising disclosure under the *Corporations Act 2001* (Cth) (**Corporations Act**) or which are exempt from such disclosure under a mutual recognition scheme. Additional financial products are specifically exempted from the new regime, including MySuper products, margin lending facilities and ordinary shares.[2] Consumer credit products are also excluded from the new DADOs regime.

While we support the Minister's ability to add new products by regulation,[3] in our view exemptions to the DADOs should be extremely limited. Exemptions would only create regulatory gaps and provide incentives for firms to structure their products in order to avoid the obligations. Regulatory arbitrage has already been seen with financial and credit products, such as consumer leases, because of exemptions to classes of products. It is also unclear whether the Minister would be able to add products not regulated by the Corporations Act, such as credit, by regulation.

Linking the application of the new obligations to disclosure requirements in the Corporations Act unnecessarily narrows the scope of the DADOs. Instead, we recommend that the obligations apply to financial products as defined in the ASIC Act.[4] Adopting the ASIC Act definition would ensure that the obligations apply to all retail financial and credit products, including products that fall outside regulation under the Corporations Act or the *National Consumer Credit Protection Act 2009* (Cth) (**Credit Act**).[5] This would include complex and often not well targeted products such as expenses-only funeral insurance products, dealer-issued warranties and unregulated credit (which includes, for example, so-called 'buy now, pay later' products and small business credit). This approach would also ensure that the regime is aligned with the definitions and consumer protections in Part 2 Division 2 of the ASIC Act.[6]

Further, the disclosure nexus appears to provide a wide loophole for the DADOs to be circumvented in respect of securities, via section 708(10) of the Corporations Act.

'Buy now pay later': Harriet's story

Harriet contacted our lawyers for advice in January 2018 after her 15-year-old daughter bought a $250 handbag with Afterpay. Harriet told us that her daughter has a part time job and had $120 in her bank account at the time of purchasing the handbag. According to Harriet this was only the second time Harriet's daughter had gone shopping without her.

[2] Schedule 1, item 3, paragraph 993DB.
[3] Schedule 1, item 3, paragraph 993DB(1)(c).
[4] *Australian Securities and Investments Commission Act 2001* (Cth) s12BAA.
[5] *Australian Securities and Investments Commission Act 2001* (Cth) s12BAA; *Australian Securities and Investments Commission Regulations 2001* (Cth) Reg 2B.
[6] *Australian Securities and Investments Commission Act 2001* (Cth) s12BAA.

Harriet said she had previously explained the dangers of Afterpay to her daughter, but it was so easy that her daughter signed up anyway.

Harriet said that her daughter saw the Afterpay sign in the Mimco store window, and simply downloaded the Afterpay mobile app and input her age as over 18. Harriet said her daughter then purchased the handbag over the counter. Harriet said that there appeared to be no identity or age verification by Afterpay or the store. Harriet has contacted Afterpay, Mimco and the Credit and Investments Ombudsman with her concerns about minors being signed up so easily, but her complaint is yet to be resolved to her satisfaction. Harriet says that according to Afterpay her daughter remains liable for the $250 handbag, despite her account being closed.

Expenses-only funeral insurance: Monica's story[7]

Ballina woman Monica Kapeen was caring for three young relatives under eight years old when she started buying expenses-only funeral insurance for herself and the three children. "Everyone was talking, there'd been a lot of deaths in our community, you know," Ms Kapeen said.

The policy cost $40 per fortnight, which she paid for three years before it became unaffordable.

"I was lucky to meet the bills I had, and I couldn't, so I've lost $3, 500," Ms Kapeen said." When you only get $440 for a fortnight and out of that money you've got to pay rent, run a car ... that $40 is a lot of money. I couldn't afford it."

After missing four payments, Ms Kapeen said her policy, and all the money she had paid, was lost.

We have provided additional comments in relation to consumer credit, MySuper, ordinary shares, margin lending and other investment products below.

Consumer credit

As set out in our initial and supplementary submissions, we strongly support both regulated and unregulated credit being subject to the DADOs. This would be achieved by adopting the ASIC Act definition of 'financial product'. The Proposals Paper justified the exemption for regulated credit products on the basis that there is a 'potential overlap with the responsible lending obligations that already apply to credit products'. However, we reiterate that

[7]Originally published by Josie Taylor, ABC, *Babies among thousands of Aboriginal children signed up to 'shocking' funeral insurance schemes,* 21 November 2015, available at: http://www.abc.net.au/news/2015-11-21/aboriginal-babies-being-signed-up-to-shocking-insurance-schemes/6958342.

responsible lending obligations offer different (and lesser) protections to consumers than the DADOs.

Responsible lending obligations apply only at the point of sale and are limited to assessing whether a product is 'not unsuitable' for a consumer. In contrast, the DADOs would apply during product design, distribution and post-sale. The obligations would require firms to design safe and suitable credit products and distribute them accordingly—this would be an important additional protection for borrowers.

As noted above, we also have serious concerns about unregulated credit products being exempted from the obligations. This would exclude common consumer credit products such as 'buy now pay later',[8] certain types of consumer leases[9] and pawnbroking[10]. These products have caused significant consumer harm, and should be covered by the obligations.

MySuper

Introduced in late 2017, MySuper specific legislation, which would deliver more targeted outcomes for superannuation consumers, has so far failed to gain the support of Parliament. The *Treasury Laws Amendment (Improving Accountability and Member Outcomes in Superannuation Measures No.1) Bill 2017* includes annual MySuper outcomes assessments and complementary Australian Prudential Regulatory Authority (**APRA**) powers. The protections in this Bill would make funds more transparent and accountable in how they deliver best interest financial outcomes to members. It also gives further powers to APRA to cancel the authority of a fund to offer a MySuper product where that fund was not meeting its obligations. Combined, this reform would likely lead to MySuper products being far better designed to meet the needs of consumers.

The proposed exclusion of MySuper products from the DADOs adds further weight to the need for a solution which ensures products are designed to meet consumers' actual needs. Unless this legislation specifically addressing MySuper is passed by Parliament, we consider the current exemption for MySuper from the DADOs is inappropriate. MySuper should remain included in the DADOs unless and until legislation along the above lines is passed.

Ordinary shares

According to the Explanatory Memorandum, ordinary shares have been excluded from the Bill 'as they are fundamental to corporate fundraising and because there is a level of understanding regarding such securities among consumers'. However, while many consumers would be comfortable investing in shares in the ASX100 (and perhaps the ASX200), outside the ASX200 the risk, transparency and governance issues become more pronounced. The proposed exemption for ordinary shares appears to be very broad. This has

[8] Many 'buy now pay later' services appear to avoid regulation by not technically 'making a charge' for credit, and therefore fall outside *National Consumer Credit Protection Act 2009* (Cth) s6.

[9] Section 171 of the National Credit Code exempts short term leases (those for four months or less) and indefinite leases from regulation.

[10] Pawnbrokers are expressly excluded from the operation of most consumer credit laws under *National Consumer Credit Protection Act 2009* (Cth) s6(9).

the potential to expose consumers to risky low-cap shares, not just less volatile blue-chip shares.

The extent of the proposed exemption for ordinary shares is also unclear, as the Bill fails to provide a definition of the term 'ordinary shares'. The Explanatory Memorandum says that the 'term is to take its ordinary meaning', and is 'intended to distinguish such shares from other types of shares, particularly preference shares'. The anti-avoidance provisions, while important, only add to the definitional confusion, as ordinary shares in listed investment companies (**LICs**) appear to be covered by the new obligations. We understand from Treasury that the exemption is only for listed ordinary shares that are offered in Australia. We strongly agree with the requirements of 'listed' and 'offered in Australia', as we believe that the regime should be as comprehensive as possible to have maximum effect. We understand, moreover, that listed unit trusts (MIS), ETPs, ETFs, and equity warrants will not be exempt from the regime. We acknowledge that there are good grounds not to exempt ETFs, ETPs and warrants (extending Treasury's rationale for not exempting LICs). However, we note that listed unit trusts are a significant part of the primary equity market, and we consider that their absence from the share exemption is paradoxical and may attract strong industry objections.

As set out in our initial submission, we recommend that the exemption (if any) for ordinary shares be limited to fully paid ordinary shares in listed Australian companies traded on the ASX (not on a junior exchange). Secondary listings (for example, for NZSE50 stocks) could be considered for exemption by ASIC on a case-by-case basis. This would ensure that low-cap shares traded on alternative exchanges are not covered by the exemption.

We assume that standard rights issues and share purchase plans of listed shares would also be exempted from the Bill.

The Bill seems to aggregate DADOs together as a single regime, meaning a product appears to be subject either to all the obligations or none of them. If so, that is problematic for the exemption of (at least) ordinary shares. We concede that there are reasonable grounds to exempt the *issue* of fully paid ordinary shares listed on ASX, to avoid interfering with standard capital raising practice and burdening it with excessive costs or delays, to little benefit. However, the *distribution* channels should not be exempt (except for wholesale underwriting and placements). Stockbrokers and other parties involved in distributing these issues (not the secondary sales on market) should be required to ensure that the shares are offered only to suitable retail clients.

Margin lending

We note that the Proposals Paper stated that margin lending facilities would be captured by the DADOs, but these loans have been excluded in the Bill as 'these products are currently subject to product-specific regulations that negate the need to apply the new regime' (see para 1.17). The reasoning behind this change is unclear, particularly given that the protections under Division 4A of Part 7.8 of the Corporations Act do not protect 'sophisticated investors'.[11]. Section 761GA says that "sophisticated investors" are not "retail clients'. This creates a no

[11]Sophisticated investors are defined in section 761GA of the *Corporations Act 2001* (Cth).

mans land between retail and wholesale. We do not of course object to wholesale clients and professional investors being exempted. However, since clients can qualify as sophisticated investors by virtue of their assets or income, rather than investment expertise, it is undesirable that investment products that may be specifically targeted to them would be exempted.

The proposals paper discussed defining target markets for margin loans according to 'whether the consumer is approaching retirement age and therefore does not have an extended working life to recover from a significant financial loss (as illustrated by the storm financial case).' it does not appear that this risk of consumer harm outlined in the proposals paper has been addressed, and we therefore do not consider the exemption to be appropriate. We also note that, even years after Division 4A took effect, ASIC encountered problems with non-standard margin lending.[12]

Other investment products

We would welcome explicit confirmation from Government and/or ASIC whether the following products will be captured by the DADOs and PIP regime: Corporate Collective Investment Vehicles **(CCIVs)** *Comprehensive Income Products for Retirement* **(CIPRs)**; Complex Products as identified (but not defined) in ASIC's Report 384.

We understand that self managed superannuation Funds **(SMSFs**) have been excluded (at present) from the Bill, on the grounds that they are conceptually too different from other financial products. We concede that, although it could be only a matter of expanding the scope of ASIC Act s12BAA(7)(f). The SMSF sector is now worth over $600 billion,[13] and is subject to two material problems: promotion of loans to buy properties, which is not covered by responsible lending laws, in the case of SMSF trustees; and aggressive selling of SMSF services to individuals whose super balances are far too low for an SMSF to be cost effective. This is a missed opportunity, and we urge Government to act swiftly on these problems.

Recommendation 1: Apply DADOs to 'financial products' as defined in the *Australian Securities and Investments Commission Act 2001* (Cth) s12BAA, which would include regulated and unregulated credit.

Recommendation 2: The exemption to ordinary shares (if any) be limited to fully paid ordinary shares in listed Australian companies traded on the ASX.

Recommendation 3: Remove the proposed exemption for margin lending.

[12] Australian Securities and Investments Commission, *16-010MR Margin lenders improve lending standards following ASIC Review*, 21 January 2016, available at: http://asic.gov.au/about-asic/media-centre/find-a-media-release/2016-releases/16-010mr-margin-lenders-improve-lending-standards-following-asic-review/.
[13] SuperGuide, *SMSFs surge towards 600,000 controlling $700bn in* assets, 19 September 2017, available at: https://www.superguide.com.au/smsfs/smsfs-lead-the-super-pack-again.

Design obligations

We are broadly supportive of the design obligations set out in paragraph 1.33 of the Explanatory Memorandum. However, we suggest strengthening the provisions in several areas below.

Definition of 'responsible person'

The design obligations are imposed on the person who is responsible for preparing the disclosure for the product.[14] For financial products requiring a PDS, under section 1013A of the Corporations Act this is the person 'making the offer to sell the financial product' who is referred to as the 'responsible person'.

As noted above, we are concerned that linking the DADOs to disclosure obligations unnecessarily narrows the scope of the reforms. Instead, we recommend defining issuers as the entity that is responsible for the obligations owed under the terms of facility that is the product, in line with the definition of issuers in the Corporations Act.[15] In relation to credit, we recommend that the definition of 'issuers' reflect the definition of 'credit providers' in the National Credit Code.[16] These definitions would also align with the ASIC Act definition of 'financial product'.

Definition of 'appropriate' target markets

We support the proposed broad definition of 'appropriate' in the Bill,[17] but are concerned by the phrase 'generally meet the likely objectives, financial situations and needs of the persons in the target market'. Given that the new obligations are intended to ensure that 'financial services providers appropriately promote the provision of *suitable* financial products to consumers of those products' [emphasis added],[18] we believe that the phrase 'generally meet' should be replaced with 'suitable for'. This would arguably provide stronger protections to consumers, and better reflect the intent of the legislation.

We also recommend that ASIC provide industry-specific guidance to financial services providers about appropriate target markets, including guidance for certain product categories if necessary. This should include guidance on what ASIC considers to be inappropriate or 'non-target' markets to provide some constraint on industry setting unreasonably wide target markets. We note that the Proposals Paper suggested that issuers be required to indicate target and non-target markets, which we supported.

Although it is understandable that the Bill does not require an individual suitability test, we believe that the decision not to proceed with non-target markets is wrong. There is no general obligation on issuers to design safe and suitable products, as opposed to the obligation to determine a target market. This distinction makes it even more important that the issuer should

[14] Explanatory Memorandum [1.36]; Schedule 1, item 4 and 5, subparagraphs 1018A(1)(c)(ii) and 1018A(2)(c).
[15] *Corporations Act 2001* (Cth) s761E. We note that this was the initial proposal in the Proposals Paper.
[16] A credit provider is defined as 'a person that provides credit, and includes a prospective credit provider': National Credit Code s204.
[17] Schedule 1, item 3, paragraph 993DB(10).
[18] Explanatory Memorandum [1.5]; Schedule 1, item 1, paragraph 760A(aa).

be required to state and publicise a non-target market. The target and non-target markets might overlap, for a small part of the public, or there could be a grey area between them. If anything, it is more important that the issuer determines and publicise the non-target market, rather than the target, to steer away people who probably should not buy the product. That is not to prohibit it, but a warning *against* a product is more persuasive than an invitation to buy it. We believe defining a non-target market in addition to the target market would assist consumers to identify whether they fall outside of the target market. We do not think that this adds any complexity other than stating explicitly what is implied in the target market determination.

In relation to investment products, we note paragraph 1.38 of the Explanatory Memorandum, which states "…This formulation provides flexibility in determining what is appropriate for a particular product in particular circumstances. For example, it would enable an issuer to conclude that it is appropriate to distribute a product to an investor as part of balanced portfolio, even if it would not otherwise be appropriate for the investor."

We believe ASIC guidance is needed to avoid this latitude being abused, especially where the client is not receiving personal advice. Such a product might for example be appropriate for up to 5% or 10% of a balanced portfolio, but not at 20% or above. The guidance also needs to discuss concentration risk and diversification, to help prevent a client acquiring several similar products from different issuers.

Obligation to review a target market determination

We generally support the obligation for an issuer to review a target market determination as necessary to ensure it remains appropriate, including the obligation to identify 'review triggers' and the maximum period between reviews.[19] However, there is a risk that issuers will set unreasonably lengthy maximum review periods. We therefore recommend that the legislation provide for a maximum review period, for example once every 12 months. The obligation should remain scalable to allow shorter review periods if appropriate, for example for complex or higher risk products or vulnerable target markets.

Recommendation 4: Define 'issuer' as the entity that is responsible for the obligations owed under the terms of facility that is the product, in line with the definition of issuers in s761E of the Corporations Act. In relation to credit, we recommend that the definition of issuers reflect the definition of 'credit providers' in the National Credit Code.

Recommendation 5: Replace the phrase 'generally meet' with 'suitable for' in the definition of appropriate target markets in subsection 993DB(1).

Recommendation 6: Provide a maximum period between reviews of target market determinations, which should remain scalable to allow shorter review periods if appropriate (for example, for complex or higher risk products or vulnerable target markets).

[19] Explanatory Memorandum [1.43]-[1.49].

Distribution obligations

‘No advice’ distribution models

It is proposed that the distribution obligations would apply to ‘regulated persons’ that deal or provide financial advice in relation to financial products covered by the DADOs.[20] We support the broad application of the obligations to all types of dealing and providing financial advice. Given that the obligations would apply to all types of dealing (including arranging to deal),[21] we are confident that ‘no advice’ distribution models would be covered. However, it would be useful for the ASIC to clarify this in any guidance provided to industry about the new obligations.

It is common for poor value financial products, such as add-on insurance, to be sold under ‘no advice’ or ‘general advice’ models. This means that the distributor is not considering the consumer’s personal circumstances, such as their objectives, financial situation and need. In the add-on insurance sector, these distribution models and excessive commission payments have resulted in widespread mis-selling of insurance that is unsuitable for the people buying it.[22] We therefore consider it is critically important that the DADOs apply to the distribution of financial products through no advice and general advice models.

Definition of a ‘regulated person’

The definition of a ‘regulated person’ under section 1011B of the Corporations Act is very broad when considered in isolation, which we support. However, we raise similar concerns to those above on page 6 that linking the application of DADOs to disclosure obligations under the Corporations Act unnecessarily narrows the scope of the reforms and application of the DADOs to ‘regulated persons’.

Obligation not to distribute where target market determination may not be appropriate

We consider the obligation not to distribute a financial product where a target market determination may not be appropriate as a key protection under the new law. In our view, there is a greater risk of financial firms making inappropriate target market determinations (for example, by determining an unreasonably broad target market) than there is of not making determinations at all. For this reason, we recommend amending subsection 993DC (3)(b)(i) to remove the requirement for ‘an event or circumstance [to have] occurred’ that would reasonably suggest that the target market determination is no longer appropriate. Instead, we recommend that the section simply apply where a person knows, or reasonably ought to know, that the target market determination is no longer appropriate.

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[20] Explanatory Memorandum [1.56]; Schedule 1, item 3, section 993DA.

[21] Arranging to deal is also dealing under section 766C(2) of the *Corporations Act 2001* (Cth); See also Australian Securities and Investments Commission, *RG36 Licensing: Financial product advice and dealing*, June 2016, available at: http://asic.gov.au/regulatory-resources/find-a-document/regulatory-guides/rg-36-licensing-financial-product-advice-and-dealing/.

[22] For further information, see Consumer Action Law Centre, *Submission to Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry - Part 1*, 22 January 2018, pp. 9-13, available at: https://policy.consumeraction.org.au/2018/01/22/royal-commission-into-misconduct-in-the-banking-superannuation-and-finance-sector-consumer-action-submission-part-1/.

Record keeping obligations

We strongly support the obligation for distributors to collect distribution information, and to notify issuers of significant dealings that are not consistent with a product's target market determination.[23] We consider that there is scope to strengthen these obligations by requiring distributors to provide distribution information to issuers upon request. We also recommend requiring distributors to notify ASIC of significant dealings that are not consistent with a product's target market determination, which would complement the similar obligation that applies to issuers[24] and the current mandatory breach reporting regime.

We also believe there would be merit in disclosing target market determinations and distribution information to the public. This would assist consumers and their representatives to determine whether products are suitable to their needs, and whether breaches have occurred. Currently, the Bill would only require information about target markets to be included in advertising and promotional material—rather than being generally available to consumers.[25]

Recommendation 7: ASIC provide regulatory guidance that clarifies the design and distribution obligations apply to 'no advice' distribution models of financial products.

Recommendation 8: Amend subsection 993DC(3)(b)(i) to apply where a person knows, or reasonably ought to know, that the target market determination is no longer appropriate.

Recommendation 9: Require distributors to provide distribution information to an issuer upon the issuer's reasonable request.

Recommendation 10: Require target market determinations and distribution information to be made available to the public, via additional avenues such as being prominently featured on the issuer's website.

Promotional material

We support amendments to section 1018A of the Corporations Act to require advertising and promotional material for a financial product to refer to the product's target market. However, this section only applies to financial products requiring a PDS. Consistent with our recommendations above, we suggest that the advertising and promotional material obligations apply to all financial products as defined in the ASIC Act, which would cover a much broader range of financial and credit products.

We also recommend that any disclosure of target markets in advertisements and promotional material be consumer tested for effectiveness, including with respect to behavioural economics. Consumers can be subject to 'information overload', particularly in the financial services market, meaning that information contained in mandatory disclosures often goes

[23] Explanatory Memorandum [1.67]-[1.74].
[24] Explanatory Memorandum [1.53]; Schedule 1, item 3, section 993DG.
[25] Explanatory Memorandum [1.75].

unnoticed.[26] Issuers should ensure that disclosure of target markets is not simply an exercise in 'tick box' compliance, but is consumer tested to ensure that it is effective.

While we support information about target market determinations being included in advertisements and promotional material, we also recommend that this information be available generally to consumers (for example, on the issuer's website) - -see Recommendation 10 above.

> **Recommendation 11:** Apply advertising and promotional material obligations to 'financial products' as defined in the ASIC Act.
>
> **Recommendation 12:** Disclosure of target markets in advertisements and promotional material be consumer tested for effectiveness.

ASIC powers

We support new ASIC powers to request information, issue stop orders, and make exemptions and modifications to the new regime.[27] However, ASIC's stop order powers are limited to contraventions relating to failure to make a target market determination, dealing in or providing advice on a product without a determination, and failing to take reasonable steps to comply with a determination. This seems unnecessarily limited and exposes consumers to a risk of harm, particularly where the target market determination may not be appropriate.

We recommend that ASIC's stop order powers be extended to apply to all contraventions under the new law, particularly contraventions relating to distributing products where target market determinations may be inappropriate.[28]

We understand from discussion with Treasury that it is implied in the Bill that a target market determination must be 'appropriate' to be deemed a 'target market determination'. If this is the intended approach, this must be clarified in the legislation. This approach would mean that an issuer that makes an inappropriate target market determination would breach the requirement to determine a target market, and would face penalties and civil liability. If this is the case, and it is the sole basis for ensuring that those who make inappropriate target market determinations face consequences for doing so, this needs to be explicit in the Bill.

> **Recommendation 13:** ASIC's stop order powers be extended to apply to all contraventions under the new law, particularly contraventions relating to distributing products where target market determinations may inappropriate. This must be explicit in the legislation, rather than implied.

[26] For example, see Prof Lauren Willis, Loyola Law School, *Against financial literacy education,* 2008, available at: http://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=1198&context=faculty_scholarship.
[27] Explanatory Memorandum [1.79].
[28] Schedule 1, item 3, paragraph 993DC.

Civil and criminal penalties

We support strong penalties for contraventions of the DADOs and PIP. We also support additional resourcing for ASIC to ensure the new obligations are appropriately and promptly enforced. We note that the ASIC Enforcement Review Taskforce is currently reviewing penalties, and suggest that penalties in the Bill be consistent with those recommendations.

> **Recommendation 14:** Ensure penalties are consistent with the recommendations of the ASIC Enforcement Review Taskforce when these recommendations are released.

Civil liability

We strongly support consumers who suffer loss or damage because of contraventions of the new laws being entitled to recover that loss or damage by civil action. However, the proposed causes of action in the Bill are extremely limited and would unduly restrict consumers' ability to recover their losses.

Under the current Bill, consumers would only be able to recover loss or damage if the relevant contraventions related to distributing a product without a target market determination, and failing to take reasonable steps to comply with a target market determination.[29] We recommend that these causes of action be extended to apply to all contraventions under the new law, particularly contraventions relating to distributing products where target market determinations may be inappropriate.[30] This is arguably where the greatest risk of consumer harm lies, and where consumers are most likely to incur losses.

It also appears that standing to apply for injunctive relief would be limited under section 1324 of the Corporations Act, rather than the broader standing provisions under the ASIC Act and Credit Act.[31] We would prefer that standing to apply for injunctive relief against breaches of the new law reflect the standing provisions under the ASIC Act and Credit Act. This would enable consumer organisations to take action to protect the public interest.

We also suggest providing other remedies, such as the right to rescind or void the relevant contract with the financial services provider. Relying on this remedy is often more straightforward and practical than pursuing loss or damages, or an injunction, through a dispute resolution process.

> **Recommendation 15:** Civil liability causes of action be extended to apply to all contraventions under the new law, particularly contraventions relating to distributing products where target market determinations may inappropriate. Other remedies, such as the right to void the relevant contract in the event of a breach, should also be considered.

[29] Explanatory Memorandum [1.96].
[30] Schedule 1, item 3, paragraph 993DC.
[31] See *Australian Securities and Investments Commission Act 2001* (Cth) s12GD; *National Consumer Credit Protection Act 2009* (Cth) s177.

Recommendation 16: Standing to apply for injunctive relief against breaches of the new law reflect the standing provisions under the ASIC Act and Credit Act, rather than section 1324 of the Corporations Act.

Transition period

We consider the transition period for new and existing financial products (12 and 24 months after the date of Royal Assent respectively) is far too generous. These reforms were first recommended in the Financial System Inquiry Final Report in December 2014, and accepted by Government in October 2015.[32] The industry has had ample notice of the proposed changes and time to adjust its policies and processes accordingly. The lengthy transition period for existing financial products means that the consumer harm intended to be mitigated by these reforms would continue for at least another 2 years, which is unacceptable.

We recommend the obligations apply to new financial products on the day after Royal Assent, and to existing products 12 months after the date of Royal Assent. This would also complement the transition period for the ASIC PIP, which commences the day after Royal Assent.

Recommendation 17: Apply the obligations to new financial products on the date of Royal Assent, and to existing products 12 months after the date of Royal Assent.

PRODUCT INTERVENTION POWER

Products subject to the intervention power

We strongly support the intervention power applying to both financial products and credit products. However, similar to our recommendation above, we recommend that the intervention power apply to financial products as defined in the ASIC Act, rather than financial products and credit products regulated under the Corporations Act and Credit Act.

This would ensure that products such as dealer-issued warranties, expenses-only funeral insurance, small business credit, pawnbroking and 'buy now pay later' finance were covered by the intervention power. These products are widely available to consumers and have the potential to cause significant consumer harm, and have done so, but are not regulated by the Corporations Act or Credit Act. As the case studies below demonstrate, these products are also commonly sold where they are not appropriate for the consumer. Given the wide availability of these products to consumers, it is critical that ASIC is empowered to intervene when such products pose a significant risk to consumers.

[32] The Treasury, *Government response to the Financial System Inquiry,* 20 October 2015, available at: https://treasury.gov.au/publication/government-response-to-the-financial-system-inquiry/.

‘Buy now pay later’: Tara’s story

Tara (name changed) called the National Debt Helpline in January 2018 as she was struggling with her bills. Tara told us that she works casually earning around $80 per week and is looking for other work. She says that she used to work full time but was bullied at work by her boss. Tara said she owns a car worth approximately $5,000 and is currently driving uninsured.

Tara told us that she currently has debts to Radio Rentals, FlexiRent, Telstra and Afterpay. She estimates her debt to Afterpay as approximately $700. Tara said she is on a payment plan of $30 per week but she has been struggling to make these payments. Afterpay is not regulated by the Credit Act, so is not subject to the same responsible lending, financial hardship and dispute resolution obligations as other credit providers.

Dealer-issued warranties: Jemima’s story

Jemima (name changed) and her husband bought a second-hand car. Jemima told us that the salesperson advised them that the manufacturer’s warranty would last three years, but they could purchase an extension for a further two years after that. They agreed. Jemima also said that the salesperson told them that servicing would need to be completed through a certain dealership, but that these dealerships were located Australia wide. This turned out to be incorrect. Jemima and her husband were in South Australia when they realised the car was due for a service. There were no affiliated dealerships in the whole state. After moving interstate for family reasons, they realised that the closest dealership was two and a half hours' drive away. Jemima explained to us that she rang the warranty provider to check to see if the requirement could be waived due to their personal circumstances but the warranty provider said no. With our assistance, the matter has now been resolved.

Applying the intervention power to the ASIC Act definition of financial products would also ‘future proof’ the legislation in an era of fintech and open data. We anticipate new ‘innovative’ products will continue to enter Australia’s financial services market. These may seek to exploit loopholes in regulations in the Corporations Act and Credit Act, and would therefore fall outside the current scope of the intervention power despite posing risks to consumers.

Recommendation 18: Apply the intervention power to the ASIC Act definition of financial products.

Using the intervention power

The new intervention power can be used where ASIC is satisfied that a product or class of products has resulted, or is likely to result, in significant detriment to consumers. In considering whether the risk of harm is 'significant', we support the flexibility provided to ASIC to consider factors other than those listed in section 1022CD.

We also support the acknowledgement in the Explanatory Memorandum that 'detriment' can cover a broad range of harm or damage that may flow from a product. However, we believe that there is merit in the Bill also explicitly stating that consumer detriment should not just be determined by reference to individual loss, but also where large numbers of consumers might suffer relatively small (individual) losses.[33] This is particularly the case where the class of consumers impacted is vulnerable or disadvantaged.

Recommendation 19: The Bill specify that consumer detriment should not just be determined by reference to individual loss, but also where large numbers of consumers who might suffer relatively small (individual) losses.

Type of interventions

ASIC would be able to make a range of temporary orders under the new law, including banning a person from issuing a product, directing that a product only be sold to certain consumers or in particular circumstances, and requiring appropriate warnings or labels. We support ASIC being empowered to make a broad range of orders, as this would allow ASIC to tailor its interventions to ensure they are appropriate and effective.

However, we are concerned that the Bill explicitly denies ASIC the power to make interventions in relation to training or remuneration under section 1020CC(6).[34] While the Bill provides that ASIC would be able to intervene where the remuneration arrangement is contingent upon the achievement of objectives 'directly related' to the financial product, it is unclear what circumstances this would cover. Conflicted remuneration and poor training standards are clear drivers of misconduct and poor consumer outcomes in the financial system.[35] We therefore strongly recommend that these limitations be removed from the Bill.

Recommendation 20: ASIC be permitted to make interventions in relation to training and remuneration.

Duration of intervention orders

We strongly oppose interventions being restricted to an initial duration of up to 18 months with no ability for extensions. We recommend that intervention orders continue until ASIC, or the

[33] See our initial joint submission at pp. 44-45: http://policy.consumeraction.org.au/wp-content/uploads/sites/13/2017/03/FINAL-Joint-Consumer-Submission-DADOs-and-PIPs-15032017.pdf.
[34]Ibid, pp. 43-44.
[35] A summary of this research is available in Consumer Action Law Centre's submission to the Retail Banking Remuneration Review, pp. 3-5, available at: https://consumeraction.org.au/wp-content/uploads/2017/02/170212-Consumer-Action-Submission-Sedgwick-Review-Issues-Paper-FINAL.pdf.

Government, decides that the risk of consumer harm has been addressed and the intervention order is safe to remove.

As set out in our initial submission, the Financial Conduct Authority in the United Kingdom is empowered to make temporary interventions without consultation for up to 12 months, but is able to make permanent rules with consultation with affected parties.[36] The watered-down version proposed in the Bill would require ASIC to undertake extensive consultation without any power to make permanent rules. The proposal is, in a sense, the worst of both worlds.

Recommendation 21: Intervention orders continue until ASIC, or the Government , decides that the risk of consumer harm has been addressed and the intervention order is safe to remove.

Procedural requirements

While we acknowledge the need for procedural fairness, we caution against requiring ASIC to consult extensively with affected parties or to conduct lengthy public consultations. The delays associated with lengthy consultations would fundamentally undermine the purpose of the power, and would hinder ASIC's ability to respond to risks to consumers in a timely fashion. Consultations are time-consuming and can be used by industry to stave off much-needed reforms or harm mitigation. Requiring extensive consultation would detract from the pre-emptive, preventive and timely aims of the powers identified as necessary by the Financial System Inquiry.[37]

We therefore recommend that the Bill specify that the extent of ASIC's consultation is to be commensurate with the assessed risk of detriment to consumers and the need for prompt action. We also suggest removing the requirement for consultations between ASIC and other regulators. These consultations should be permitted but determined on a case-by-case basis by ASIC, rather than mandated.

Recommendation 22: The Bill specify that the extent of ASIC's consultation is to be commensurate with the assessed risk of detriment to consumers and the need for prompt action.

Recommendation 23: Remove the requirement for consultations between ASIC and other regulators. These consultations should be permitted but determined on a case-by-case basis by ASIC, rather than mandated.

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[36] Financial Conduct Authority, *FSA confirms approach to using temporary product intervention rules that will be used by the FCA,* 31 March 2013, available at: https://www.fca.org.uk/news/press-releases/fsa-confirms-approach-using-temporary-product-intervention-rules-will-be-used.
[37] Financial System Inquiry Final Report, *Chapter 5: Regulatory System*, 7 December 2014, available at: http://fsi.gov.au/publications/final-report/.

Transition period

We support the intervention powers commencing on the day after Royal Assent.[38] However, we are concerned that ASIC can only intervene in relation to products that are made available for acquisition after the commencement of the new power. This could be particularly problematic for longer-term products such as home loans and life insurance, which may have been purchased months or years before the new laws commence.

We recommend that ASIC be empowered to intervene in relation to products that were acquired by consumers before the commencement of the new power. At a minimum, consumers who were previously sold products that are later subject to an intervention order should be personally notified and advised that they can make a complaint to an external dispute resolution scheme, if applicable.

Recommendation 24: ASIC be permitted to intervene in relation to products that were acquired by consumers before the commencement of the new power.

Please contact Senior Policy Officer Katherine Temple at Consumer Action Law Centre on 03 9670 5088 or at katherine@consumeraction.org.au if you have any questions about this submission.

Yours sincerely

Gerard Brody
Chief Executive Officer
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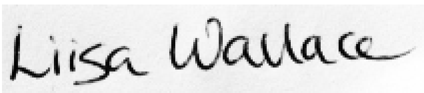

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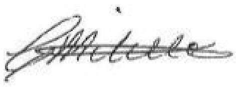

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[38] Explanatory Memorandum [2.75]; Table item 3 of section 2 to the Bill.

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APPENDIX A: ABOUT THE CONTRIBUTORS

Australian Shareholders' Association

The Australian Shareholders Association (ASA) is an independent, not-for-profit, member-funded organisation that has grown to be the major autonomous body representing Australian retail investors. Its advocacy promotes the interests of retail shareholders. ASA also helps its members improve their investment knowledge through its educational offerings.

Care Inc Financial Counselling Service and the Consumer Law Centre of the ACT

Care Inc. Financial Counselling Service has been the main provider of financial counselling and related services for low to moderate income and vulnerable consumers in the ACT since 1983. Care's core service activities include the provision of information, counselling and advocacy for consumers experiencing problems with credit and debt. Care also has a Community Development and Education program, provides gambling financial counselling as part of the ACT Gambling Counselling and Support Service in partnership with lead agency Relationships Australia; operates outreach services in the region and at the Alexander Maconochie Centre and makes policy comment on issues of importance to its client group. Care also operates the ACT's first No Interest Loans Scheme, which was established in 1997, and hosts the Consumer Law Centre of the ACT.

CHOICE

Set up by consumers for consumers, CHOICE is the consumer advocate that provides Australians with information and advice, free from commercial bias. By mobilising Australia's largest and loudest consumer movement, CHOICE fights to hold industry and government accountable and achieve real change on the issues that matter most.

Consumer Action Law Centre

Consumer Action Law Centre is an independent, not-for-profit consumer organisation based in Melbourne. We work to advance fairness in consumer markets, particularly for disadvantaged and vulnerable consumers, through financial counselling, legal advice and representation, and policy work and campaigns. Delivering assistance services to Victorian consumers, we have a national reach through our deep expertise in consumer law and policy and direct knowledge of the consumer experience of modern markets.

Consumer Credit Law Centre SA

The Consumer Credit Law Centre South Australia (**CCLCSA**) was established in 2014 to provide free legal advice and financial counselling to consumers in South Australia in the areas of credit, banking and finance. The Centre also provides legal education and advocacy in the areas of credit, banking and financial services. The **CCLCSA** is managed by Uniting Communities who also provide an extensive range of financial counselling and community legal services as well as a large number of services to low income and disadvantaged people including mental health, drug and alcohol and disability services.

Consumer Credit Legal Service (WA) Inc

Consumer Credit Legal Service (WA) Inc. (CCLSWA) is a not-for-profit charitable organisation which provides legal advice and representation to consumers in WA in the areas of credit, banking and finance, and consumer law. CCLSWA also takes an active role in community legal education, law reform and policy issues affecting consumers. In the 2016/2017 financial year, CCLSWA provided 2677 pieces of legal advice to 1088 new clients.

Consumers' Federation of Australia

The Consumers' Federation of Australia is the peak body for consumer organisations in Australia. CFA represents a diverse range of consumer organisations, including most major national consumer organisations. Our organisational members and their members represent or provide services to millions of Australian consumers.

COTA Australia

COTA Australia is the national consumer peak body for older Australians. Its members are the State and Territory COTAs (Councils on the Ageing) in each of the eight States and Territories of Australia. The State and Territory COTAs have around 30,000 individual members and more than 1,000 seniors' organisation members, which jointly represent over 500,000 older Australians.

COTA Australia's focus is on national policy issues from the perspective of older people as citizens and consumers and we seek to promote, improve and protect the circumstances and wellbeing of older people in Australia. Information about, and the views of, our constituents and members are gathered through a wide variety of consultative and engagement mechanisms and processes.

Financial Counselling Australia

FCA is the peak body for financial counsellors. Financial counsellors provide information, support and advocacy for people in financial difficulty. They work in not-for-profit community organisations and their services are free, independent and confidential. FCA is the national voice for the financial counselling profession, providing resources and support for financial counsellors and advocating for people who are financially vulnerable.

Financial Rights Legal Centre

Financial Rights is a community legal centre that specialises in helping consumers understand and enforce their financial rights, especially low income and otherwise marginalised or vulnerable consumers. We provide free and independent financial counselling, legal advice and representation to individuals about a broad range of financial issues. Financial Rights operates the Credit & Debt Hotline, which helps NSW consumers experiencing financial difficulties. We also operate the Insurance Law Service which provides advice nationally to consumers about insurance claims and debts to insurance companies. Financial Rights took close to 25,000 calls for advice or assistance during the 2016/2017 financial year.