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**Enforceability of financial services industry codes -- Taking action on recommendation 1.15 of the Banking, Superannuation and Financial Services Royal Commission -- Consultation Paper**

To Whom It May Concern,

FINSIA thanks Treasury for the opportunity to provide feedback on its consultation paper, *Enforceability of financial services industry codes*. Broadly speaking, we support Treasury's proposals.

In our response to the questions raised in the consultation paper, we recommend, among other things, that when considering whether to approve an industry code, ASIC should also consider whether:

- the code requires subscribers to ensure individuals who act on behalf of a subscriber and are under their control adhere to principles that represent the general norms of professional conduct and competence that underlie the general and statutory law; and
- these principles are stated in the code.

In addition, ASIC should consider whether this provision is an enforceable code provision.

We also recommend that where individuals subscribe to a code (for example, a professional code), those individuals should be listed on a publicly available register of subscribers. Where a subscriber commits an egregious breach of a mandatory code, they should be able to be removed from the register. (The effect of the individual being removed from the register for a mandatory code would be to prevent the individual from working in the industry.) Where a subscriber commits a breach of a voluntary code provision, they should be able to be removed from the register.

Further, in the case of code subscribers that are organisations, each subscriber should nominate individuals responsible for ensuring the code is adhered to by the subscriber. Those organisations and individuals should be listed on a publicly available register. Where the subscriber commits an egregious breach of a mandatory code, the organisation or nominated individual should be able to be removed from the register. (The effect of being removed from the register for a mandatory code would be to prevent the organisation or individual (as applicable) from operating in the industry.) Where a subscriber commits a breach of a voluntary code provision, the organisation or nominated individual should be able to be removed from the register.

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Other specific concerns are addressed in our detailed response, which follows, to the paper.

### **1. What are the benefits of subscribing to an approved industry code?**

We agree that a firm subscribing to a code that has been approved by a regulator is beneficial to consumers and firms because the approval signals to consumers that they can be confident in the code and that it can be relied on.

### **2. What issues need to be considered for financial services industry codes to contain 'enforceable code provisions'?**

Issues that need to be considered include:

- Does a provision that is proposed to be an enforceable code provision set a clear expectation of behaviour?
- Is the provision consistent with existing general and statutory law?
- Do consumer contracts made before an enforceable code provision is introduced as part of a code, automatically incorporate the enforceable code provision when it is introduced?
- Where a consumer contract incorporates an enforceable code provision, is the provision automatically replaced if and when the enforceable code provision is upgraded in the code?
- Is it practicable for a court, tribunal or similar adjudicative body to enforce the provision or would the provision be more appropriately enforced by a regulator or another body?
- Can an appropriate remedy be provided for contractual breach of the provision or is disciplinary action being a better way to provide redress for the breach?
- Should enforceable code provisions be a source of legal rights of consumers who are not party to a contract or similar legal instrument (for example, where in breach of their code obligations a bank harms a non-customer).

### **3. What criteria should ASIC consider when approving voluntary codes?**

We support the existing criteria in ASIC's regulatory guidance, and, in addition, the additional criteria identified in the Final Report:

In applying its discretion to approve a code under that section, ASIC has produced regulatory guidance around what codes must include. To meet the ASIC threshold, a code must:

- require subscribers to be contractually bound by the code (either by contracting with the enforcement body or with consumers or both);
- have an independent person or body that is empowered to administer and enforce the code, including imposing any appropriate sanctions;
- provide that consumers have access to internal dispute resolution and an appropriate external dispute resolution scheme for any code breaches resulting in direct financial loss; and
- give consumers broad standing to complain about any other code breach to the independent body.

The Final Report's discussion on codes raises the issue of whether ASIC should consider adopting additional criteria when considering whether to approve a code. These include

considering whether the code contains:

- a comprehensive body of rules developed in consultation with stakeholders;
- adequate provisions for dispute resolution, remedies and sanctions; and
- effective and independent administration – including compliance monitoring.

This is in addition to the Final Report's recommendation 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.

The Commissioner also emphasised that it is important to have in place appropriate procedures to support industry to develop voluntary codes, and only have government prescribe mandatory codes where necessary. Equally, in approving a code, the effects on competition should be considered.

[source: <https://treasury.gov.au/sites/default/files/2019-03/cp-c2019-t368566.pdf>, p 6, notes omitted]

When considering whether to approve an industry code, ASIC should also consider whether:

- the code requires subscribers to ensure that individuals who act on behalf of a subscriber and are under their control adhere to principles that represent the general norms of professional conduct and competence that underlie the general and statutory law; and
- these principles are stated in the code.

In addition, ASIC should consider whether this provision is an enforceable code provision.

#### **4. Should the Government be able to prescribe a voluntary financial services industry code?**

Prescribing a code would mean that breaches of the code breach public law and have consequences beyond those available for breach of private instruments. For example, a pecuniary penalty could be imposed for breach of an applicable provision of a prescribed code. We support this broader approach because it has the potential to provide stronger disincentives against code breaches than mere damages.

While certain conduct should be strongly disincentivised, we nevertheless take the view that codes should be voluntary unless the problem the code seeks to address is unlikely to be effectively addressed without a mandatory code. For example, if vulnerable consumers would choose firms subscribing to prescribed codes over firms subscribing to a non-prescribed code or firms not subscribing to any code, a prescribed voluntary code should be preferred to a mandatory code. This is because a prescribed voluntary code effectively addresses the industry problem and has additional benefits:

A prescribed voluntary code may have the advantage of fostering a stronger commitment for signatories to comply with the spirit and substance of a code compared to one that is mandated. The cooperative nature of voluntary codes may lead to more robust and enduring behavioural changes that can strengthen business relationships within the supply chain. Voluntary codes may also lend themselves to greater flexibility and scope for the parties to compromise in order to arrive at mutually acceptable terms. If parties are unwilling to reach

an agreement on a voluntary code, it may influence the Government's decision on the necessity to implement a mandatory code.

<https://treasury.gov.au/sites/default/files/2019-03/p2017-t184652-5.pdf>, p 5]

We note that, even where there is a prescribed code, it may be difficult for consumers to identify codes that meet their ethical values and those that do not. We would suggest that the more widely those values are shared within the community, the stronger the case for a mandatory code. This is because the cost of imposing a code on firms who would not voluntarily subscribe to it is more likely to be outweighed by the gain to the community from ensuring their ethical values are met.

### **Should subscribing to certain approved codes be a condition of certain licences?**

Making subscribing to certain approved codes a condition of a licence is similar to mandating a code. Even if there is an approved code that the licensee can subscribe to that is not a prescribed code, licensees are required to subscribe to a code that they would not control (for example, because they can't change the code in a way that would result in the loss of its approved status).

In our view, subscribing to certain approved codes should be a condition of a licence if all the following criteria are met:

- There is an identifiable problem in the group of licensees to which the condition would apply
- The problem is more appropriately addressed by a code than law or regulation
- Self-regulation using voluntary codes to address the problem has already been tried
- There is likely to be a net public benefit

Imposing a condition on certain licensees that they subscribe to a code that is on an approved list of approved codes is likely to be justified where there is a substantial imbalance of knowledge between the licensee and the consumer. This is because, in this case, consumers may find it prohibitively difficult to identify whether a firm meets the consumer's ethical values – even where there is a prescribed voluntary code. Further, a code that complements existing law and regulation is likely to be more effective in addressing the problem that needs to be addressed than just law and regulation. This is because, generally, codes respond more quickly and practically than law and regulation to market circumstances.

## **6. When should the Government prescribe a mandatory financial services industry code?**

Prescribing a mandatory code is likely to be justified where there is a substantial imbalance of knowledge between the licensee and the consumer. This is because, in this case, consumers may find it prohibitively difficult to identify whether a firm meets the consumer's ethical values. Further, a code that complements existing law and regulation is likely to be more effective in addressing the problem that needs to be addressed than just law and regulation. This is because, generally, codes respond more quickly and practically than law and regulation to market circumstances.

**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?**

We support the approach set out in Treasury's *Industry Codes of Conduct Policy Framework*, which sets out five relevant criteria to be considered when prescribing codes:

- Is there an identifiable problem in the industry?
- Can the problem be addressed using existing laws or regulations?
- Has industry self-regulation been attempted?
- Is an industry code the most suitable mechanism for resolving the problem?
- Is there likely to be a net public benefit? There may be other factors to consider when prescribing a mandatory code in relation to financial services.

We also support the following observations about applying those criteria:

For example, the Commissioner made a number of recommendations in his Final Report directed at industry bodies on how their codes should be amended or updated. If those changes were not made and submitted for approval within the timeframes set out in the Final Report, the Government may consider prescribing those industry codes, or particular terms of them. Similarly, where an industry has not put forward an existing code for approval in a timely way, and this lack of approval creates doubt about whether the code's provisions are enforceable by consumers, it may be appropriate for Government to consider prescribing the code.'

[source: <https://treasury.gov.au/sites/default/files/2019-03/cp-c2019-t368566.pdf>, p 10]

**8. What level of supervision and compliance monitoring for codes should there be?**

Where sharply asymmetrical knowledge between industry and consumers makes it prohibitively difficult for consumers to identify breaches of the code, there is a strong argument that codes should be carefully supervised and monitored by a reputable body that is separate from any individual subscribers to the code.

A consumer might consider seeking redress for harms that they feel acutely, such as the loss of life savings. However, they might not realise that they have experienced a harm when they don't feel it; for example, the extra cost to a consumer because they've been sold a loan in breach of code obligations might be substantial, and yet the consumer doesn't realise their suffering is caused by the misconduct.

**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?**

In our view, code monitoring should be undertaken by the regulator or another reputable and independent body. The regulator or other body will need to monitor prescribed and approved codes to determine if that status should be withdrawn.

In addition, a condition of approval of a code should be the owner of the code monitors it to ensure it remains relevant, adequate and appropriate. We would suggest there should be

sanctions, in addition to withdrawal of approved status, for code owners who do not meet this condition.

**10. Should there be regular reviews of codes? How often should these reviews be conducted**

Again, knowledge asymmetries may mean that consumers are ineffective at promoting revisions of the code in their interests. However, unless the criteria for mandating codes, identified in Treasury's *Framework* are met, there is an argument that code development should not be mandated by government.

Government should withdraw the prescribed and approved status for codes that are no longer relevant, adequate or appropriate. Where there is an identifiable problem in an industry, best addressed by a code and there would be no relevant, adequate and appropriate code, the Government should be credibly expected to intervene by mandating a code. This threat will motivate the industry to ensure it always has codes that are relevant, adequate and appropriate.

In our view, where code development should be mandated, the regulator should mandate that the code be revised, but should do so in consultation with industry. The regulator should mandate that the code be reviewed:

- at least every three years; or
- if sooner than three years, as soon as practicable after there has been a relevant material change in the industry

**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?**

We also recommend that where individuals subscribe to a code (for example, a professional code), those individuals should be listed on a publicly available register of subscribers. Where a subscriber commits an egregious breach of a mandatory code, they should be able to be removed from the register. (The effect of the individual being removed from the register for a mandatory code would be to prevent the individual from working in the industry.) Where a subscriber commits a breach of a voluntary code provision, they should be able to be removed from the register.

Further, in the case of code subscribers that are organisations, each subscriber should nominate individuals responsible for ensuring the code is adhered to by the subscriber. Those organisations and individuals should be listed on a publicly available register. Where the subscriber commits an egregious breach of a mandatory code, the organisation or nominated individual should be able to be removed from the register. (The effect of being removed from the register for a mandatory code would be to prevent the organisation or individual (as applicable) from operating in the industry.) Where a subscriber commits a breach of a voluntary code provision, the organisation or nominated individual should be able to be removed from the register.

**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?**

We support ASIC having in relation to financial services industry codes, similar enforcement powers to the ACCC in Part IVB of the Competition and Consumer Act. In addition, we would support other reputable independent bodies being code monitors and enforcers; and would also support these other bodies having, like ASIC, a wider range of investigative and enforcement powers than available for breach of agreement. For example, professional associations could monitor and enforce professional codes, subject to oversight by the regulator.

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

The consumer's total entitlement to compensation under all remedies combined, should not exceed the total financial value of the harm caused.

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

In our view, the code itself should identify which provisions are civil penalty provisions. The provisions identified might involve egregious, ongoing or systematic breaches but might cover a broader range of breaches.

For a code to be approved by the regulator, we would expect that enforceable code provisions would generally attract civil penalty provisions and that there would be a range of penalties available depending on the severity of the breach.

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

If the compensation awarded under EDR process is not less than what could be awarded by the court, court proceedings should be able to be excluded.

**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?**

We suggest the following matters be considered:

- Does the dispute involve a dispute that would help clarify the law?
- Does the dispute involve a potential systemic issue?
- Does the case involve an egregious breach of obligations that requires punitive sanctions not available elsewhere?
- Was the consumer capable of appreciating the practical effect on them of choosing EDR over a court?

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

If consumers cannot pursue matters through a court following a determination from AFCA, there is a risk that their legal rights will not be protected. While it could be argued that consumers make a choice to pursue proceedings through AFCA rather than a court, ordinary consumers may find it prohibitively difficult to weigh up the consequences of the alternative avenues for redress.

Should there be any queries or comments relating to this submission, please contact Dimitri Diamantes SA Fin, Head of Policy: [d.diamantes@finsia.com.au](mailto:d.diamantes@finsia.com.au).

Kind regards,

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