

12 April 2019

Manager
Financial Services Reform Taskforce
The Treasury

By Email: enforceablecodes@treasury.gov.au

Dear Sir/Madam,

Re: Enforceability of financial services industry codes

Industry Super Australia (ISA) welcomes the opportunity to comment on Treasury's consultation on the enforceability of financial services industry codes and the action to be taken as a result of recommendation 1.15 of the Banking, Superannuation and Financial Services Royal Commission.

ISA's response will cover generally Treasury's proposals and questions regarding the benefits of mandatory industry codes, their enforcement and some important considerations in their design.

Commissioner Kenneth Hayne stressed the importance of industry code enforceability, identifying it as one of his six general rules informing his response to the misconduct that had been revealed¹. He also echoed statements made by Treasury on the limitations and difficulties of enforcing existing codes, noting inadequate standards, their non-binding nature, the limitations of monitoring and enforcement, and a lack of consequences for breaches².

ISA generally agrees with the limitations identified by Commissioner Hayne. Industry codes require mandatory elements if they are to be of any benefit to the industry and consumers, and a robust monitoring, review and enforcement regime needs to be applied in support. Voluntary or unenforceable codes cannot be relied on to provide protection or clarity to consumers.

The criteria that should be applied by regulators regarding the enforcement of industry codes should be consumer interest and industry stability. Where minimum standards of conduct in these areas has not been achieved, ASIC should enforce industry codes, in the same way as the Australian Competition and Consumer Commission (ACCC) enforces its codes³.

The benefits of mandatory codes are demonstrated in the ACCC environment. The ACCC enforceable code provisions were implemented to raise the standard of business conduct through targeted regulation⁴. In the last 20 years the Franchising Code of Conduct has led to 33 litigated matters and 16 court enforceable undertakings. This has also allowed the ACCC to conduct regular compliance checks and gather information on common issues and developments in the industry⁵.

¹ Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, February 2019, pp 11-12

² Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, February 2019, pp 104-108

³ Treasury, 'Industry codes of conduct policy framework', November 2017, p 4

⁴ Australian Competition and Consumer Commission, 'Industry codes of conduct', November 2017, p 1

⁵ Australian Competition and Consumer Commission, 'Submission to the Inquiry into the operation and effectiveness of the Franchising Code of Conduct', 11 May 2018, p 1-2, 20

An enforceable industry code with mandatory elements facilitates minimising consumer harm and provides its members with a standard to adhere to without needing to wait for changes in the law.

Flexibility and Adaptability

While statute and regulation provide industry with greater clarity and are generally more readily enforceable, they are not able to be easily or quickly amended in response to changes in the industry. This relative immutability emphasises the potential benefits of mandatory industry codes in providing protection in areas where the law may be slow or unwilling to respond to frequent change.

Attempting to extend the application of statute and regulation beyond the core principles of acceptable behaviour in an industry could therefore lead to inefficiencies and consumer harm. An industry code may be adapted with relative ease to meet changing market conditions.

Mandatory and Aspirational Provisions

An effective industry code should have two distinct elements: mandatory elements and aspirational elements.

The mandatory elements of a code should, as recommended by the Royal Commission, be enforceable⁶. Additionally, the rights and obligations of an entity should be mandatory and enforceable. An example of a mandatory provision would be that the entity is required to have suitable policies, procedures and training in place regarding the treatment of customers in financial hardship. Conversely, the aspirational elements could encourage a higher standard of behaviour in the industry. The aspirational element for example, could encourage members of the industry to treat customers with dignity or aim for a certain level of customer service. Designed in this way, codes can aid the improvement of industry standards without necessarily waiting for law reform.

Once established such codes can be instrumental in facilitating positive law reform. For example, the aspirational provisions may become mandatory provisions, and current mandatory provisions may be reflected in legislation or regulation. Using this method, new industry code provisions can be used to deal with problems arising from changing market conditions in the short- and medium-term and, in the long-term, become permanent through statute or regulation should they still be relevant and effective over time.

Enforcement of Mandatory Codes

The mandatory elements of a code need to be enforceable by statute. It is reasonable for financial services entities that are signatories to an industry code to be obliged to abide by that code and that breaches of the code are enforceable. Otherwise codes create a false sense of security for consumers.

Situations in which a membership association requires entities to be a signatory to an industry code as a condition of membership provide some protection for consumers and can be helpful, but the revocation of an association membership cannot be the only method used to enforce code provisions. There should be ramifications for any entity that opts to not be covered by a relevant code.

⁶ Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, February 2019, pp 11-12, 108-111

For example, where a financial services entity has obtained a licence to operate (such as ASIC approval), and that approval was conditional upon the subscription to an industry code; it follows that the failure to comply with the code puts the licence in jeopardy.

Additionally, entities that wish to leave the coverage of an industry code should be required to explain their reasons for doing so to ASIC. Moreover, ASIC should be satisfied why the entity should still be allowed to maintain their licence. If ASIC finds such explanations to be unreasonable or unconvincing, the entity should be given the option of losing their licence or remaining members of the code.

To be effective at consumer protection and as a deterrent against misconduct in the financial services sector, an industry code needs to be pro-actively enforced by ASIC. Enforcement by ASIC should include compliance monitoring, supervision and regular reviews to ensure that code owners and subscribers are taking appropriate action (such as reporting to the regulator) on discovering breaches.

For codes authorised and enforced by ASIC, a breach by a financial services entity of the code should be considered a breach of the general obligation to do all things necessary to ensure that financial services are provided efficiently, honestly and fairly⁷.

Uniformity of Industry Codes

As the number of industry codes increases across the financial services sector it will become necessary for them to have certain common features to make them easier for consumers to navigate.

Features such as complaints processes, dispute resolution processes, sanctions, and timeframes should be as similar as possible across codes. While by necessity there will be some differences across codes due to conflicts with state and federal laws and regulations these factors should be limited. Consistency across codes provides greater benefit for consumers, as well as providing some relief to entities with regards to compliance.

Other observations

Some may argue, that voluntary codes do not play a role in advancing the interests of consumers and that a regulatory and/or legislative response to poor business conduct is more appropriate. Advocates against the utilisation of codes to drive change and consumer benefit refer to the failure of existing banking codes which did not protect consumers from inappropriate activity. It has also been suggested that even mandatory codes are of limited utility if they are not enforced and that consumers are better protected by enforceable legislation rather than industry self-regulation. While these arguments have some force, they fail to recognise the benefits that codes can deliver. Codes that can be enforced by regulators are preferred, as enforceable code provisions can be an adaptable and flexible way of providing clarity and confidence to consumers and inform future regulation and law.

Conclusion

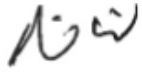
ISA considers the use of codes as an important element in improving industry standards and consumer protection. Codes can be adaptable and facilitate timely consumer protection changes. However, for codes to drive real change in industry and enhance consumer protection they must include mandatory elements (which are enforceable). The ability to enforce the mandatory elements of the codes should not be restricted.

⁷ *Corporations Act 2001*(Cth), s 912A(1)(a)

We appreciate Treasury providing ISA with an opportunity to comment on the future implementation of recommendation 1.15 of the Banking, Superannuation and Financial Services Royal Commission.

If you have any questions, please do not hesitate to contact me on 03 9657 4339.

Yours sincerely



Nick Williams
Legal Counsel