ALRC Inquiry into the Financial Services Regulatory Framework

Additional comments – Background Paper 9 and Interim Report B

Nicola Howell
School of Law, Queensland University of Technology

April 2023

Introduction

In March 2022, Dr Brown and I provided a submission on the ALRC's Interim Report A.

This second submission provides some additional comments on (i) the amended proposals A22 and A23 in Background Paper FSL9 and (ii) a suggested new regulatory framework, one that would be consistent with Proposal B1 in the ALRC's Interim Report B.

Comments on Background Paper FSL9: All roads lead to Rome: unconscionable and misleading or deceptive conduct in financial services law

In our previous submission, Dr Brown and I suggested that one solution to the complexity resulting from different definitions of 'financial product' and 'financial service' in the *Australian Securities and Investments Commission Act 2001* (Cth) ('*ASIC Act*') and *Corporations Act 2001* (Cth) ('*Corporations Act*') was to remove the current carve-out of financial products and financial services from the *Australian Consumer Law* ('*ACL*') as a Commonwealth law. I expanded on this proposal in an article published in the Company and Securities Law Journal, and in that discussion, I noted that this proposal would have the following benefits:

- Reduce the confusion created by having separate definitions of financial product and financial service in the *ASIC Act* and *Corporations Act*.
- Ensure that the general consumer protection rules are uniform across the economy.
- Where one matter involves both financial products/services and non-financial products/services, reduce the needs for formal referral of powers between ASIC and the ACCC, and for both agencies to become parties to litigation.
- Minimise litigation costs in cases where there is uncertainty about whether the *ASIC Act* or the *ACL* applies.
- Eliminate the need for separate amendment of the *ASIC Act* when the *ACL* is amended.
- Reduce the complexity that arises from the fact that the carve-out in s 131A *Competition and Consumer Act 2010* (Cth) is only a partial carve-out.[1]

Implementing this proposal would also address the problem identified by the ALRC in its Interim Report A and expanded on in it Background Paper FSL9. The problem identified by the ALRC is the

[1] Nicola J Howell 'Addressing the contrasting definitions of financial product and financial service in Australian financial services and consumer legislation' (2022) 39 *Company and Securities Law Journal* 86, 104.

existence of multiple statutory prohibitions dealing with unconscionable conduct and misleading or deceptive conduct, such that simplification of the law could be achieved by 'reducing unnecessary particularisation and removing overlapping provisions that are subject to different and highly technical thresholds'.[2]

In relation to the unconscionability provisions and the misleading or deceptive conduct provisions, Background Paper FSL9 amends the initial proposals from Interim Report A to minimise the risk of losing protections or enforcement options currently available through the more expansive suite of statutory provisions. However, as the ALRC has acknowledged, adopting these proposals would result in greater divergence between the *ASIC Act* and the *ACL*.

I am supportive of the ALRC's proposals to reduce the current proliferation of misleading or deceptive conduct and unconscionable conduct provisions in the financial services legislation. However, in my view, these objectives could equally be achieved by removing the carve out of financial services from the *ACL*, repealing the *ACL*-equivalent provisions in the *ASIC Act*, and instead making the ALRC's proposed changes to the misleading / deceptive conduct and unconscionable conduct provisions to the equivalent *ACL* provisions. The proposed deletions of equivalent provisions in the *Corporations Act* could also proceed.

I acknowledge that this proposal is outside the ALRC's terms of reference, as it requires changes to legislation other than the financial services legislation. However, to the extent that the ALRC is able to flag that this alternative proposal would also be a path to achieving legislative simplicity, I encourage it to do so.

In relation to the amended proposals A22 and A23, I also note the following:

- The ALRC's proposals would not necessarily eliminate the possibility that litigation against financial firms could plead several of the misleading or deceptive conduct or unconscionable conduct provisions. This is because the *ACL* provisions continue to apply to financial firms in their capacity as laws of the States and Territories. It is only the *ACL* operating as a law of the Commonwealth that does not apply to financial services.[3] The likelihood of regulators taking action against a financial firm under the relevant State or Territory *ACL* may be low, however, this does not seem to preclude the possibility of private action under, for example, ss 19 or 20 under the *ACL* as a State or Territory law. Where there is an expanded divergence between the *ASIC Act* and the *ACL*, this risk may be greater.
- To the extent that the ALRC can consider issues relating to the credit legislation, there are also several prohibitions in the *National Consumer Credit Protection Act 2009* (Cth) ('*NCCPA*'), with differing scope, thresholds, defences and enforcement options – for example, ss 160D and 225 in the *NCCPA* and ss 154 and 179 in sch 1 *NCCPA* (the *National Credit Code* ('*NCC*')).

[2] Australian Law Reform Commission, *Financial Services Legislation: Interim Report A (ALRC Report 137),* November 2021, 500.

[3] In the Final Report of the Review of the Australian Consumer Law, it was noted that the operational arrangements between ASIC (financial services and credit) and the ACCC (other parts of the economy) 'do not affect the jurisdiction of state and territory regulators in relation to financial services under their local application laws': Consumer Affairs Australia and New Zealand, *Australian Consumer Law Review Final Report*, March 2017, 74 (footnote 84).

A Financial Consumer Protection Act

Removing the current bifurcation

Related to my suggestion that the financial services carve-out from the ACL be removed is the suggestion for a consolidation of the consumer/investor protection provisions in the *Corporations Act* and in the *NCCPA*.

The possibility of consolidating consumer / investor provisions in the *ASIC Act* and *Corporations Act* has been identified by the ALRC, in some academic commentary, and in some submissions to the ALRC. In this additional submission, I would like to suggest that (i) a consolidation of relevant consumer / investor protection legislation should include the *NCCPA*; and (ii) such a consolidation would work well with the ALRC's proposed hierarchical approach to the regulatory framework (as set out in Proposal B1).

The Australian financial services regime is a bifurcated one, where consumer financial services (including deposit-taking, insurance, superannuation, and investment products and services are subject to a different regulatory regime than are consumer credit products and services. Credit products and services have traditionally been considered to be of a different character compared to other financial services, with a different nature and level of risk to the consumer. Also, until 2009, credit products and services were regulated only by the state and territory governments, as the Commonwealth government does not have a constitutional head of power to make laws with respect to credit. Previous inquiries into the financial system and consumer policy have noted this bifurcation, but did not make any recommendations for change.

However, the landscape has changed since that time. Consumer lives have been 'financialised', and participation in economic and social life in Australia almost necessitates access to, and use, of a range of credit and other financial products and services. There are significant consumer risks associated with using poorly regulated consumer credit products and services. This is reflected in the significant increase in obligations imposed on credit providers and intermediaries with the introduction of the *NCCPA*, and continued expansion of those obligations since its first introduction, including with more recent proposals to extend the application of the *NCCPA* to 'Buy Now Pay Later' products.[4]

In this context, the arguments for continued bifurcation of the regulation of credit and other financial products and services are weakened. In addition, many financial firms provide both credit and other financial services. Separate regulatory regimes for the two groups of products / services can impose unnecessary costs, especially where there are many similarities in the substantive content of those regulatory regimes (for example, many of the licensing, disclosure, and conduct obligations).

As part of its inquiry, the ALRC should therefore consider the merits of a Financial Consumer Protection Act that incorporates relevant consumer / investor protection obligations from Chapter 7 of the *Corporations Act* and the *NCCPA*.

Mindful of the timeframe associated with major regulatory changes, and also the limitations on the ALRC's ability to recommend changes to the policy settings, such a change could be achieved through two main stages.

[4] Australian Government The Treasury *Regulating Buy Now, Pay Later in Australia* (Options Paper), November 2022.

Stage One – Move existing provisions into one piece of legislation

In a **first stage**, new, stand-alone, Financial Consumer Protection statute could be introduced, where the focus of the Act is to *consolidate* the existing consumer protection regulation (subject to changes to technical detail proposed by the ALRC in its review). This new statute could incorporate, in one part, the existing relevant consumer protections in chapter 7 of the *Corporations Act*, and in another part, the existing provisions in the *NCCPA*.

This proposal would involve no substantive change to the existing policy settings. The substantive provisions in the *Corporations Act* and *NCCPA* would remain, as would the relevant definitions of the persons who are to be protected by the two independent sets of obligations. Instead, the proposal would consolidate the existing financial services consumer protection legislation into one instrument. In turn, this could facilitate a reduction in the size of the *Corporations Act* (one of the largest pieces of Commonwealth legislation).

I note that some have proposed the creation of a consumer financial services statute that incorporates relevant parts of the *ASIC Act* and *Corporations Act*. Such a statute could have the following main parts:

- General consumer protection obligations (the provisions currently in Part 2, div 2 *ASIC Act*);
- Relevant consumer protections for financial services (currently in Ch 7 *Corporations Act*); and
- Consumer credit protections (the existing *NCCPA*, including the *NCC*).

However, as discussed above and in my CSLJ article, in my view, it would be preferable to have the general consumer protections applicable to financial services in the *ACL* and to repeal Part 2, div 2 *ASIC Act* and s 131A *Competition and Consumer Act*. If this approach were followed, a new Financial Consumer Protection statute could have two main parts:

- Relevant consumer protections for financial services (currently in Ch 7 *Corporations Act*); and
- Consumer credit protections (the existing *NCCPA*, including the *NCC*).

Stage two – examine opportunities for consolidation

In a **second stage**, consideration could be given to identifying opportunities for consolidating the obligations across the financial services – credit divide.

There are already some significant similarities in the regulatory approaches to disclosure and conduct in the financial services and credit sectors, such that, for some existing provisions, it appears (at least on the face of it) that there would be minimal change to the *content* of the policy settings if some of these obligations were consolidated into a single obligation applying both to financial products / services and consumer credit products / services.

For example, the new Product Intervention Orders, found in Part 6-7A of the *NCCPA* and Part 7.9A of the *Corporations Act* have similar wording, and the Design and Distribution Obligation in Part 7.8A of the *Corporations Act* already applies to both credit and non-credit financial products. There are similar licensing regimes under Ch 7 *Corporations Act* and Ch 2 *NCCPA*, with similar application

criteria and duties of licensees, including the obligation to provide an internal dispute resolution process and to belong to AFCA.[5]

There are also similarities in the mandatory disclosure documents in Ch 7 of the *Corporations Act* and the *NCCPA* / *NCC*. For example, in both Acts, relevant providers must give consumers / retail investors a disclosure document giving information about the person with whom the consumer or retail investor is dealing: in the *NCCPA*, this is a Credit Guide;[6] in the *Corporations Act*, it is a Financial Services Guide.[7] Enforcement options and remedies is also an area where there are great similarities and potential scope for consolidation.

Of course, there are also some areas of Ch 7 *Corporations Act* and the *NCCPA* that appear similar on their face, but on more detailed examination, may show more significant differences. These might include the disclosure documents setting out key terms and conditions of products,[8] the best interests' duties applicable to financial advisers and to brokers, and obligations imposed on financial advisers, credit issuers, and credit advisers to understand the consumer's requirements and objectives before making a recommendation or issuing a product.[9]

There are also many obligations that are unique to one or the other of Ch 7 *Corporations Act* or the *NCCPA*. For example, the financial services regulation has no equivalent of the hardship protections in the credit legislation,[10] and issuers in the financial services sector (who are not advisers) do not have obligations to assess the suitability of the products for a particular consumer, whereas credit providers do have such an obligation.[11] These unique obligations would not be suitable for consolidation efforts, at least in the short to medium term.

A consolidated Financial Consumer Protection statute might also include relevant norms-based obligations that are needed to supplement the general consumer protections in the *ACL* (if the financial services carve-out is removed), or to mirror the general consumer protections in the *ACL* (if the financial services carve-out remains). It could also incorporate additional, or alternative, norms-based regulation specific to the financial services sector. One option might be a 'Treating Customers Fairly' regime as exists in the United Kingdom[12] and South Africa.[13] New Zealand is also implementing a TCF-like regime, with a new 'fair conduct principle' being introduced from 2025.[14]

---

[5] As discussed in Cindy Davies, Samuel Walpole, and Gail Pearson, 'Australia's Licensing Regimes for Financial Services, Credit, and Superannuation: Three Tracks toward the Twin Peaks' (2021) 38(5) *Company and Securities Law Journal* 332 ('Australia's Licensing Regimes for Financial Services, Credit, and Superannuation').
[6] See *National Consumer Credit Protection Act 2009* (Cth) ('*NCCPA*') ss 113 (credit guide for credit assistance providers), 126 (credit guide for credit providers).
[7] See *Corporations Act 2001* (Cth) ('*Corporations Act*') s 942B (FSG main requirements).
[8] Compare the PDS requirements in the *Corporations Act* (s 1013C) with the pre-contract disclosure requirements in the *NCCPA* (in sch 1 ('*National Credit Code*'), ss 16, 17).
[9] Compare the best interests obligations for financial advisers in *Corporations Act* s 961B; and the responsible lending obligations for credit providers (*NCCPA* pt 3-2, div 3, 4) and credit assistance providers (*NCCPA* pt 3-1, div 4, 6).
[10] *National Credit Code* ss 72-75.
[11] See *NCCPA* pt 3-2, div 3, 4.
[12] See Financial Conduct Authority (UK) *FCA Handbook*, PRIN 2.1 The Principles, principle 6: 'A firm must pay due regard to the interests of its customers and treat them fairly'.
[13] Andrew Schmulow, 'Treating Customers Fairly (TCF) in the South African Banking Industry: Laying the Groundwork for Twin Peaks' (2022) 30 *African Journal of International and Comparative Law* 25-38.
[14] The *Financial Markets (Conduct of Institutions) Amendment Act 2022* (NZ) has inserted a new Part 6, subpart 6A 'Regulating conduct of financial institutions' into the *Financial Markets Conduct Act 2013* (NZ).

The focus here would be on areas where there is potential for consolidation with minimal changes to the *content* of existing policy settings, providing benefits to consumers and firms in relation to consistency of standards.

The table below provides a possible structure for a Consumer Financial Services Protection statute.

Part	Title	Content examples	Applicable to
1	Introductory material	Definitions, administration, regulator, etc	Financial services and credit
2	Norms-based regulation applicable to financial services and consumer credit	Product intervention orders, design and distribution obligations, treating customers fairly obligation. Also, if the carve out of financial services from the *ACL* remains, the general consumer protections currently in found in Part 2, Div 2, *ASIC Act* (eg, prohibitions against unconscionable/misleading conduct and unfair terms).	Financial services and credit
3	Licensing of providers and advisers	Application criteria and process, licensing obligations.	Financial services and credit
4	Common disclosure documents	Perhaps starting with the Financial Services Guide / Credit Guide, but other disclosure documents might also be relevant.	Financial services and credit
5	Unique financial services obligations	Remaining consumer protection parts of Ch 7 *Corporations Act* (including any enforcement / remedial provisions that only have applicability to financial services)	Financial services
6	Unique credit obligations	Remaining parts of *NCCPA* / *NCC* (including any enforcement / remedial provisions that only have applicability to credit)	Credit
7	Enforcement and remedies	Where there are common approaches / remedies (e.g., penalties, offences, damages / compensation, injunctions, community service orders, etc)	Financial services and credit

In her submissions to the ALRC, Professor Hanrahan has noted that focusing on the financial consumer law in the *Corporations Act* would allow the Commission to provide a model that 'allows for the future integration of all the financial consumer law (including consumer credit)'.[15] The suggested model above takes this further step, by excising the relevant consumer provisions from the *Corporations Act* (Professor Hanrahan's Book 6 (Financial services providers, other than the current Ch 5D) and Book 7 (Financial consumers), and combining them with the consumer credit provisions into a new statute, along with the necessary administration, definition, enforcement and remedial provisions.

Consolidation of the financial consumer protections currently found in the *Corporations Act* and *NCCPA* does require some further attention to the scope of the person who is protected by these obligations. The protected person is currently described differently in the *Corporations Act* and *NCCPA*, as a person who is a 'retail investor' for the purpose of the *Corporations Act* protections will not necessarily be a 'consumer' for the purpose of the *NCCPA* protections. A key difference is that

[15] Pamela Hanrahan, *Submission to the ALRC's Interim Report B – Financial Services Legislation* (2022), 3.

small businesses can be protected by the *Corporations Act* provisions, but the *NCCPA* protections do not apply to small business borrowers.

Any consolidation of obligations across the financial services – credit divide will therefore necessarily involve a change to the policy settings as to who is to be protected by the obligations. Extending 'consumer' protection to small business borrowers has been flagged in previous inquiries and was the subject of exposure draft legislation.[16] Although the government at the time decided not to proceed with the small business changes, some protections for small business borrowers are included in the Banking Code of Practice and Customer-Owned Banks Code of Practice, and the Financial Services Royal Commission also highlighted concerns around the treatment of small business borrowers, albeit not supporting the extension of the *NCCPA* to small businesses.[17] The extension of 'consumer' protections to small businesses is well established in the general consumer protection law,[18] and in other sectors, and consideration of the merits of consolidating some of the financial services and consumer credit protections may be an opportune time to revisit this question. In addition, the concerns around the extension of the *NCCPA* to small business seem to focus on the responsible lending aspect. However, in terms of the proposed model above, it may be that these responsible lending obligations could be included in the part dealing with unique credit obligations, where application could be restricted to borrowing for consumer purposes. For some other provisions where there is greater potential for consolidation of financial services and credit obligations (eg, licensing, disclosure through a credit guide), it may be appropriate for these protections to also be available to small business.

Such a consolidation exercise could also fit well with the ALRC's proposed legislative hierarchy. In the example above, the primary obligations would be contained in the Act. Exclusions and exemptions could be contained in a Scoping Order, including, for example, an exclusion of small business from responsible lending obligations. And detailed requirements for disclosure, advice, and other matters could be set out in specific Rulebooks.

Future reform

The discussion above refers only to consolidation of relevant provisions in Chapter 7 of the *Corporations Act* and the *NCCPA* into a new statute. However, future reform could also examine the potential for greater consolidation across the financial services – credit divide, and also incorporation of other product specific consumer protections, for example, those that are current found in the insurance or superannuation legislation.

[16] Exposure Draft National Consumer Credit Protection Amendment (Credit Reform Phase 2) Bill 2012; see also Australian Government The Treasury, *National Credit Reform: Enhancing confidence and fairness in Australia's credit law* (Green Paper, July 2010), Chapter 1 (Credit for Small Business).

[17] *Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* (Final Report, February 2019) vol 1, 94 – 104.

[18] For example, the unfair contract terms protections apply to small business contracts – see *Australian Consumer Law* s 23; *Australian Securities and Investments Commission Act 2001* (Cth), s 12BF. For a discussion of the need for an expanded definition of consumer, see also Lynden Griggs, Aviva Freilich and Eileen Webb, 'Challenging the notion of a consumer : time for change' (2011) 19 *Competition & Consumer Law Journal* 52–77.

Conclusion

The ALRC's inquiry provides a unique opportunity to propose a simpler and more coherent and regulatory design for consumer protection in financial services, one that takes into account the financialisaton of consumers' lives across the spectrum of financial and credit products and services. A separate Financial Consumer Protection statute that incorporates the key consumer protections for financial services and credit would be one mechanism for modernising the regulatory framework in this area. If appropriate, this could be achieved through a staged approach, with a first stage simply incorporating existing provisions into a single statute (and incorporating any recommendations of the ALRC for changes to the content of the current legislation); and a second stage involving consideration of merging obligations across the financial services-credit divide, where those obligations are already very similar in practice. Future stages could examine the potential for (i) further consolidation across the financial services – credit divide where current obligations are more diverse, and (ii) incorporation of existing consumer protections for other financial products and services.

Thank you for the opportunity to contribute to the Inquiry. I would be happy to discuss any of the points raised above, and I wish the ALRC well in the preparation of the forthcoming reports.

Nicola Howell
School of Law, Queensland University of Technology
Contact: [redacted]