

Product intervention power

Submission in response to ASIC's consultation
paper 313

Australian Financial Complaints Authority

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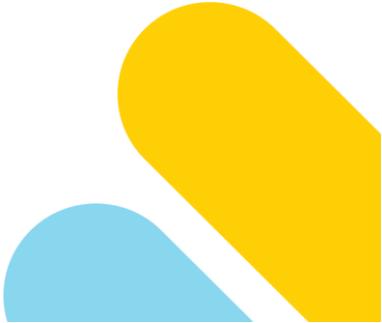
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Introduction

The Australian Financial Complaints Authority (AFCA) is the independent external dispute resolution (EDR) scheme for the financial sector. AFCA's purpose is to provide fair, independent and effective solutions for financial disputes. It does this not only by providing fair dispute resolution services, but also by working with financial firms to improve their processes and improve industry standards of service, thereby minimising complaints.

In addition to providing solutions for financial complaints, AFCA has responsibilities¹ to identify, resolve and report on systemic issues and to notify the Australian Securities and Investments Commission (ASIC), and other regulators, of serious contraventions of the law. More broadly, AFCA plays a key role in restoring trust in the financial services sector.

AFCA welcomes the opportunity to provide a submission² in response to the consultation by ASIC on its proposed guidance around when and how it may exercise its product intervention power.

This submission is informed by the experience of AFCA and its predecessor schemes. It focuses on issues that go to the effectiveness of EDR as a mechanism of redress for consumers, both individual and small business.

Key points

In response to the consultation paper³, the key points of our submission are:

- AFCA strongly welcomes the addition of the product intervention power to ASIC's regulatory toolkit. We believe that this will enhance ASIC's ability to make proactive interventions in response to:
 - > financial and credit products that deliver poor consumer⁴ outcomes, irrespective of whether the financial firm has complied with legislative or regulatory requirements
 - > gaps or unintended consequences in the current regulatory architecture.
- As an outcome focused regulatory tool, the product intervention power allows ASIC to apply a fairness lens over the conduct of financial firms in their assessment of whether a product has, will, or is likely to result in significant consumer detriment.

¹ Refer to Part C, Reporting Requirements, of [ASIC Regulatory Guide 267: Oversight of the Australian Financial Complaints Authority](#).

² This submission has been prepared by the staff of AFCA and does not necessarily represent the views of individual directors of AFCA.

³ [ASIC Consultation Paper 313, Product intervention power](#)

⁴ In this submission, consumer means both a retail client for a financial product as defined by the *Corporations Act 2001* and a consumer for a credit product as defined by the *National Consumer Credit Protect Act 2009*, unless otherwise specified.

- We consider that AFCA will have an increased and evolving role in working with ASIC regarding the identification and reporting of conduct that may warrant regulatory intervention through the exercise of the product intervention power.

Our submission will focus on part B of the consultation paper, *Proposed guidance on when and how ASIC may exercise the product intervention power*, in particular, factors that ASIC may consider when assessing if a product has, will or is likely to cause significant consumer detriment and determining an appropriate response.

Our submission is informed by our complaints handling experience and dispute resolution process, which is underpinned by fairness; an established principle for industry-based customer dispute resolution schemes.

1 Overview

Product intervention power enables ASIC to take proactive steps to minimise risk of significant consumer harm

The product intervention power is a regulatory tool which provides ASIC with the ability to intervene when a financial product⁵ has, will, or is likely to result in significant consumer detriment⁶.

Intervention is proactive and prospective, by way of a product intervention order issued by ASIC, which can apply to a specific person or persons in relation to a product, or it can be market wide. Intervention orders can require or prohibit certain conduct in relation to a financial product or products, for example, stopping its or their sale.

The significance of the product intervention power as a regulatory tool is that the exercise of the power, or the intervention by ASIC, is based on consumer outcomes. These outcomes are considered in the context of financial products that have, will or may result in significant harm to consumers.

This means that irrespective of whether a financial firm⁷ has complied with its legal obligations, ASIC can still exercise its product intervention power if it is considered that the product itself is harmful to consumers.

AFCA considers the product intervention power to be a welcome enhancement to ASIC's regulatory toolkit. It enables ASIC to act quickly in response to financial products that have been identified as actually or potentially causing harm to consumers.

It also enables ASIC to take action where a legislative or regulatory gap may exist within financial services, or where there may be unintended legislative or regulatory consequences which may be detrimental to consumers.

A major benefit is that ASIC can now take proactive steps to minimise the risk of harm to consumers without the need for legislative or regulatory change or having to use the court system. These mechanisms, while necessary and essential for particular regulatory action, are very time consuming and resource intensive. A lengthy process to take action in response to identified harmful financial products is not in the best interests of consumers who are acquiring, or may acquire, those financial products.

⁵ In this submission, financial product means a financial product as defined by the *Corporations Act 2001* and the *Australian Securities and Investments Commission Act 2001*, and a credit product as defined by the *National Consumer Credit Protection Act 2009*.

⁶ Section 1023E of the *Corporations Act 2001* outlines specific criteria which must be considered, including the nature and extent of the detriment, the actual or potential financial loss resulting from the product, the impact the detriment has, will or likely to have and other matters prescribed by regulations.

⁷ In this submission, financial firm means any firm who provides a financial product.

2 Considering significant consumer detriment

Fairness is a critical element in considering if a financial product has or will cause significant consumer detriment

In order for ASIC to be able to intervene and use the product intervention power, it must be satisfied that the financial product either has, will, or is likely to cause significant consumer detriment.

There are certain factors that ASIC must consider, which include the nature and extent of the detriment, the actual or potential financial loss and the impact of the detriment.⁸

AFCA believes that the principle of fairness is linked to the legislative considerations that ASIC is required to give in assessing the nature and extent of the detriment and its impact. We think ASIC's regulatory guidance should incorporate fairness as an explicit consideration as to whether a financial product has, will, or is likely to cause significant consumer detriment.

The community has a right to expect to be treated fairly by financial firms that offer financial products. The Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry demonstrated that even if the conduct of a financial firm is lawful, and they are offering regulated and permitted financial products, it can still fall well below community standards and expectations.

In order to determine the extent of any harm or detriment that a consumer has or may have suffered as a result of a financial product, it is essential to take into account and understand all of the circumstances of the relationship between a consumer and a financial firm, and the financial deal between them.

This consideration transcends throughout the lifecycle of the relationship that a consumer has with a financial firm and the financial product. This includes during the sale and contracting period, the delivery and use of the product and any remediation when things go wrong.

In applying the principle of fairness to an investigation to determine if an outcome was fair in the circumstances, we think that there are some key considerations which need to be made. These include:

- Did the parties obey the law?
- Did the parties make promises or representations they did not meet?
- Did the parties act honestly, reasonably and in good faith with their dealings with each other?

⁸ Section 1023E, *Corporations Act 2001*

- Did one party take unfair advantage of another? Were specific circumstances or vulnerabilities considered?
- Did the financial firm provide the product or service ethically, with reasonable care and skill and in accordance with industry and professional practice?
- Did the financial firm meet the consumer's reasonable expectations about the product or service?
- Did the product or service perform as expected and provide a fair value or benefit?
- When acting for a consumer, did the financial firm act in the interests of the consumer or group of consumers as a whole?
- How did the parties treat each other during their relationship or after concerns were raised?
- What was the impact on the consumer and their experience of the service?

AFCA's fairness jurisdiction

Fairness is one of the underlying principles for an industry-based customer dispute resolution scheme⁹ and requires both procedures and decision-making to be fair and to be seen to be fair.

When we investigate complaints, we are required to do so in a way that is impartial and fair.¹⁰ When we make a decision in regard to a complaint, under our Rules we must do what we consider is fair in all the circumstances.

This includes having regard to:

- legal principles
- applicable industry codes or guidance
- good industry practice
- previous relevant decisions¹¹

but also, the broader circumstances of the complaint, including the relationship between the complainant and the financial firm. It is this additional consideration that enables us to go beyond what was required of the financial firm by way of regulation and consider what was fair in the particular circumstances of the complaint.

We consider a good test of fairness in all the circumstances to be whether the parties would still enter into the financial deal if they fully understood its implications. AFCA is currently undertaking work developing a framework which outlines how AFCA makes decisions that are fair under our Rules. We look forward to consulting with financial firms, consumers and other stakeholders in relation to this work.

⁹ The Benchmarks and their underlying principles, [Benchmarks for Industry-based Customer Dispute Resolution](#), pg. 7

¹⁰ A.2.1 c), [AFCA Rules](#), pg. 2

¹¹ A.14.2, [AFCA Rules](#), pg. 11

3 Measuring significant consumer detriment

Considerations for the measurement of loss suffered by a consumer to inform an appropriate remedy

In order for ASIC to intervene using the product intervention power, it must be satisfied that a financial product has caused or is likely to cause significant consumer detriment.

The interpretation of what is 'significant' in the context of consumer detriment is, and will always be, subjective. An underlying consideration that AFCA believes should be applied in determining the extent of loss, detriment or harm is the position that the consumer would be in but for the conduct of the financial firm. For example, the sale of a harmful financial product. Loss is therefore measured by comparing their position after suffering the loss, detriment or harm with their position or likely position had that conduct not occurred.

When we consider a complaint, we will generally only provide a remedy if we decide that a consumer incurred loss or harm that was caused by a financial firm. If we do decide there has been a loss suffered by a consumer the type and extent of any remedy we provide will always depend on the circumstances of the complaint and we will have regard to established legal principles and consider both financial and non-financial loss suffered by the consumer.

Financial loss can be considered in two parts:

- direct financial loss is financial loss caused directly by the conduct
- indirect financial loss is financial loss which is incidental to the conduct.

Financial loss might result from default charges or enforcement costs that could have been avoided if the credit provider complied with its obligations.

Non-financial loss relates to the practical or emotional effects relating to the conduct of a financial firm. Non-financial loss might include unnecessary stress caused by an error of the financial firm.

We will generally only award compensation for non-financial loss where there has been an unusual amount of physical inconvenience, time taken to resolve a situation, or interference with the complainant's expectation of enjoyment or peace of mind. When considering an award for non-financial loss, we consider the severity and impact of the financial firm's conduct on the particular consumer.

We look at all of the consumer's circumstances when assessing the impact of the financial firm's conduct. If, for example, there is a delay in the financial firm's response to a consumer's reasonable request for documents, it may have a greater impact if the complainant is also in financial difficulty. If a consumer is young,

inexperienced and vulnerable, a financial firm's inappropriate debt collection activity may have a more significant impact on their peace of mind than it would on an experienced business person.

A consumer may be under significant stress and experiencing significant inconvenience for reasons unrelated to the financial firm's conduct, for example, a marriage break-up. In these circumstances, we will weigh up the additional stress the conduct caused the complainant and if appropriate, award compensation for it. Inconvenience can lead to non-financial loss, but we would not award compensation for a level of inconvenience that is a normal part of doing business.

However, as we are neither a regulator of the financial services industry or a court, our Rules limit our ability to consider and award compensation for non-financial loss. We believe that ASIC, as the conduct regulator within the financial services industry, does have the authority and mandate to focus equally on financial and non-financial loss that consumers have or may suffer due to the products that financial firms provide.

4 AFCA's role continues to evolve

AFCA sees an increased role in supporting ASIC's informed use of the product intervention power

AFCA commenced on 1 November 2018 as the single EDR scheme for the financial services industry.

Our role is to assist consumers, both individuals and small businesses, to resolve complaints they have with their financial firm. If the complaint is not resolved between the parties, we will decide an appropriate outcome. We can award compensation for losses suffered because of a financial firm's error.

Since our commencement, our role has evolved, and it continues to do so. Following the release of the final report of the Royal Commission, the Government announced that a compensation scheme of last resort will be established, and that this will be part of AFCA. We have recently expanded our jurisdiction to be able to consider complaints for conduct dating back to 1 January 2008¹². We will also play an increased role in remediation.

We also see the possibility of an increased role for AFCA to play in the context of informing ASIC's use of the product intervention power. There is potential for AFCA to act as a facilitator in informing ASIC of problem areas within the financial services industry that may warrant intervention using the product intervention power. This could be achieved through intelligence gathering, informed by our complaints handling processes and experience, and our systemic issues and serious contravention

¹² Our extended jurisdiction to be able to consider complaints for conduct dating back to 1 January 2008 is limited.

reporting functions. Further consideration will need to be given in relation to the detail of how AFCA's role may operate in this area.

We look forward to our continued work with ASIC the conduct regulator, to help consumers who have suffered, or are at risk of suffering, harm because of the harmful products offered by financial firms.