



Law Council
OF AUSTRALIA

Legal Practice Section

13 August 2021

Financial System Division
Treasury
Langton Crescent
Parkes ACT 2600

By email: CSLR@treasury.gov.au

Dear Sir / Madam

Financial Services Royal Commission - Compensation Scheme of Last Resort

These comments have been prepared by the Australian Consumer Law Committee of the Law Council of Australia's Legal Practice Section (**the Committee**).

The Committee takes a specific interest in legal and policy matters affecting consumers. Members of the Committee are lawyers with extensive professional experience and expertise in consumer protection law and provide legal advice and representation to consumers from all walks of life in Australia, ranging from investors in sophisticated financial products to socially and economically disadvantaged people in remote communities.

Accordingly, the Committee welcomes the opportunity to comment on the Treasury's draft bills regarding the Compensation Scheme of Last Resort (**CSLR**). The CSLR has been contemplated for many years, including during the *Review of the financial system external dispute resolution framework (Ramsay Review)*¹ in 2017 prior to the Financial Services Royal Commission. It is important for consumers that the CSLR is introduced and effective as soon as possible.

On balance, the Committee supports the introduction of the CSLR, but provides some further commentary below in respect of certain aspects of the proposed CSLR which we believe may be enhanced in a way that prevents unfair consumer outcomes.

The Committee makes the following recommendations to the proposed bill to ensure fairness for consumers, in particular consumers who are vulnerable to financial exploitation. We provide the commentary below under the same headings as those which appear in the consultation paper.

¹ *Review of the financial system external dispute resolution and complaints framework: Supplementary Final Report*, 6 September 2017 ('Ramsay Review').

Scope

The Committee supports the increased scope of the CSLR, beyond disputes relating to only personal advice failures as proposed by the Ramsay Review.² By extending the coverage of the scheme to include personal advice on relevant financial products to retail clients, credit intermediation, securities dealing, credit provision and insurance product distribution, the proposed CSLR is more likely to achieve an increase in confidence across the sector. An all-encompassing scheme with fewer rule deviations results in a simplicity that will be more comprehensible to consumers.

Voluntary AFCA members

The Committee disagrees with the statement that “the inclusion of financial products and services of voluntary AFCA members in the CSLR would create a disincentive for voluntary AFCA membership and would add to CSLR complexity”.

To best achieve the scheme’s purpose, it should be designed with a consumer focussed lens. Consumers ought to have access to redress regardless of whether a firm is a voluntary or mandatory member of the AFCA. It is unlikely in the extreme that a consumer at the point of obtaining a financial product would be aware of whether the Financial Services Provider is a compulsory or voluntary member. Under the present proposed model, that could lead to unusual and unfair outcomes where consumers who have suffered detriment due to the conduct of a Financial Services Provider are disentitled to any compensation under the scheme merely due to the membership category of the Financial Services Provider.

Whilst the Committee acknowledges the comments made in respect of a possible reluctance for voluntary membership, it is the view of the Committee that consistency in outcomes for consumers is critical in the design of a scheme such as the CSLR. To do otherwise, and exempt voluntary members of AFCA, would lead to inherently unfair outcomes for consumers which are significant. If a voluntary member of AFCA has caused detriment towards a consumer, which detriment has not been able to be recovered, there doesn’t appear to be any clear reason why a consumer ought not be able to recover any detriment from the CSLR, and in the Committee’s submission the mere category of the membership of the Financial Services Provider isn’t a sound reason for the exclusion from eligibility from the scheme.

The Committee recommends the CSLR be extended to include voluntary AFCA members.

Court and Tribunal decisions

The Committee notes the Treasury’s position on the inadequate data available for unpaid court and tribunal decisions. The Committee has concerns about the complete exclusion of these decisions from the scheme on these grounds, particularly in light of the accompanying lack of commitment to collect relevant data. This is not a new problem and the exclusion of court and tribunal decisions from the CSLR runs the risk of distorting consumer choice away

² Ibid.

from litigation and towards AFCA. This in turn runs the risk of impacting current statistics in relation to unpaid AFCA claims. Further, AFCA determinations are limited in their precedential value. Reduced litigation in the financial services sector could prevent necessary law reform through our judicial system.

A further issue that arises is the grossly unfair outcome posed to consumers who elected to pursue court proceedings rather than go through AFCA. Once a complaint has already been dealt with by a court or tribunal, a consumer is not able to lodge a complaint with AFCA.³ This leaves consumers in a position where they are prejudiced from accessing the CSLR due to a choice to bring court or tribunal proceedings prior to the scheme's introduction.

The Committee recommends:

- (a) the Treasury make a commitment to collecting data on unpaid court and tribunal decisions between periodic reviews; and
- (b) the CSLR should respond to court and tribunal decisions where the consumer would have been otherwise eligible for AFCA coverage at the time the court or tribunal proceedings commenced.

Paying claims

Whilst we appreciate the long-term sustainability of the scheme is a factor for consideration, we recommend the proposed compensation cap of \$150 000 be increased to align with AFCA's compensation caps. This is in line with the Ramsay Review's recommendation that the compensation caps of the CSLR and AFCA be aligned.⁴

We make this recommendation with a view to reduce the significant losses experienced by consumers affected by financial advice scandals. Many lose their life savings or their family home and are subsequently placed at risk of further disadvantage and exploitation. \$150 000 is not sufficient to cover the damages awarded. We note this group is likely to represent a minority of consumers accessing the scheme.

We agree that where the CSLR pays an amount of compensation to the claimant, the relevant financial firm runs a risk of having its licence suspended or cancelled by ASIC. This is likely to improve the compliance of financial firms with AFCA determinations, ensuring payments are made promptly.

Governance

The present proposal sees the inclusion of one of AFCA's industry directors, one of AFCA's consumer directors, a person with actuarial qualifications or expertise and a person with expertise in claims handling. If the purpose of the CSLR is to be achieved, it is vital the consumer's voice is not overpowered within the governance structure of the scheme by

³ AFCA rule C. 1. 2 (d).
⁴ Ramsay Review, p 19.

membership skewed in favour of the industry. The current proposed governance structure leaves room for a situation to arise in which AFCA's consumer director is the only voice for consumers on the board.

The Committee recommends an amendment of s 106(3)(f) of the draft legislation to align the CSLR with AFCA's governance model and legislate a board that is independently chaired with an equal number of members with consumer and industry experience.

Funding the scheme

The most important aspect of the funding of the scheme is that the funding is sufficient to ensure that the CSLR is an enduring and lasting feature in the financial services industry in Australia. That is, it must be sustainable.

The Committee notes that in this submission above, we have called for the caps in the scheme to be increased to those levels which are equal to the limits of the AFCA compensation caps. Whilst we strongly believe this should occur, we recognise a need to ensure that the funding obtained supports the scheme at this level without affecting scheme sustainability. The Committee strongly believes that any funding shortfalls should not be borne by consumers. There should be appropriate measures available to the minister to ensure that the scheme remains sustainable. Those measures should include ensuring that the funding in any given year has a surplus so that in the event of a 'black swan' event or a major financial crisis where claims experience upon the CSLR deteriorates, there is a surplus pool of funds to be drawn upon. To that end, we believe that the Capital Reserve is a sensible measure, but we query whether the \$5 million limit will be sufficient in the event of a major financial disaster. We welcome the fact that the Capital Reserve may be amendable through regulations to enable revisions to be made as appropriate. In addition to that, depending upon the levels drawn down from the scheme, it may be appropriate for some claims to be paid over more than one (but not many) financial years. It is noted by the Committee that this recommendation was also made by the Ramsay Review.⁵

The Committee believes that the overall funding measures recommended are reasonable, and that there are appropriate measures which enable flexibility for the scheme. One matter which may be worth considering is whether it is appropriate for there to be a mechanism by which in the event of a major financial disaster, the Minister may make a contribution to the CSLR from general revenue so as to ensure scheme sustainability in the rare event of a major financial industry scheme. Such a measure would ensure that the CSLR remains sustainable in the event of a catastrophe, and ensures that consumers won't be unfairly disadvantaged in such an event. Any contribution made by the Federal Government could be recovered in subsequent years via the levy mechanism currently proposed.

The Committee congratulates Treasury on putting together the currently proposed CSLR scheme which is a critical missing piece of consumer protection in our financial services industry. Such a scheme if implemented properly will assist in providing consumers greater confidence in the financial sector.

⁵ Supplementary Final Report Review of the financial systems external dispute resolution and complaints framework pg 94

The Committee would welcome the opportunity to discuss this submission with the Department. In the first instance, please contact the Committee Chair, Ben Slade at BSlade@mauriceblackburn.com.au.

Yours sincerely



Michael Tidball
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