

Additional remarks from Government Senators

1.1 The Labor and Greens Political Party References inquiry into *The ability of consumers and small businesses to exercise their legal rights through the justice system, and whether there are fair, affordable and appropriate resolution processes to resolve disputes with financial service providers*, (the Inquiry) has attempted to duplicate the work the Hayne Royal Commission into *Misconduct in the Banking, Superannuation and Financial Services Industry*¹ (the Royal Commission) but has done so without meaningful effect and without the resources and expertise available to the Royal Commission.

1.2 As with many politically-motivated Senate references inquiries, this one raised questions regarding the intent behind the reference, bearing in mind that reforms to the system have not had the chance to become operationally effective. Government Senators note that the Royal Commission was conducted by one of Australia's most eminent jurists, the Honourable Kenneth Madison Hayne AC QC, from 14 December 2017 and 1 February 2019. Seven (7) rounds of public hearings were held, each round consisting of approximately two weeks of hearings. 10,323 written submissions were received. The Royal Commission handed down its 530-page final report on 1 February 2019 and since then the Government has accepted—and has begun the process of applying—all 76 recommendations made in the final report. This References Committee Inquiry, by contrast, was conducted from 14 February 2019 to 8 April 2019, with only one public hearing and after receiving only 127 written submissions.

1.3 Government members of the committee endorse a collaborative approach to the resolution of disputes with, and the dispensation of grievances against, the financial services sector. Working towards outcomes that offer suitable protections to consumers and lenders alike, and that promote economic activity, growth and innovation should be the objective of all interested parties.

1.4 Government members of the committee make further remarks on the recommendations of the Majority Committee Report.

1.5 **Recommendation 1** calls on the Australian Government to *'establish an industry levy, to apply to the largest financial institutions on the ASX, that would raise funds for the legal assistance and financial counselling sectors to enable these sectors to provide assistance to consumers and small businesses that have disputes with financial service providers.'*

1.6 Paragraph 2.3(a) of the Australian Financial Complaints Authority (AFCA) constitution relevantly provides that:

The Company's (AFCA's) income is to be derived from contributions made by Members in an amount and manner as determined by the Company.²

1 February 2019, <https://financialservices.royalcommission.gov.au/Pages/default.aspx>

2 <https://www.afca.org.au/about-afca/corporate-information/constitution/>

1.7 The 'Members' section of the AFCA website provides that:

All Australian financial services licensees, Australian credit licensees, authorised credit representatives and superannuation trustees are required to be a member of the Australian Financial Complaints Authority (AFCA) under their financial services licence conditions, in accordance with ASIC Regulatory Guide RG 165.

Our members include banks, insurers, credit providers, financial advisers, debt collection agencies, superannuation trustees and many more. We have over 35,000 members across the country, most will never have a complaint lodged against them. For those that do, we offer fair, independent and effective solutions for financial disputes facilitated by professional and experienced staff.³

1.8 The 'What we do' page of the AFCA website provides that:

Our role is to assist consumers and small businesses to reach agreements with financial firms about how⁴ to resolve their complaints. We are impartial and independent. We do not act for either party to advocate their position. If a complaint does not resolve between the parties, we will decide an appropriate outcome.

1.9 Coalition members of the committee are satisfied that the financial sector (that is, 'all Australian financial services licensees, Australian credit licensees, authorised credit representatives and superannuation trustees'—as above) contributes substantially to the cost of dispute resolution through membership of AFCA. The scope of any further contributions that may be contemplated, and the services to which such contributions should be devoted, would require careful and consultative consideration.

1.10 Coalition members of the committee also note that Recommendation 1 is vague, particularly regarding the architecture of the proposed levy scheme. The recommendation is silent regarding the intended recipients of the funding that would be raised by the levy, the proposed criteria for assessing and making funding grants, and the proposed mechanism for distribution.

1.11 **Recommendation 2** recommends that *'the Australian Government improve access to legal assistance services for small businesses.'*

1.12 It should be noted that in the 2019-20 budget the Government delivered a baseline funding boost and guaranteed long-term financial commitments for frontline legal services. This included the announcement of the development of a single National Mechanism to deliver legal assistance funding.

1.13 Government members of the committee are conscious of the challenges faced by small businesses in court proceedings involving large financial institutions and agree with the sentiment of Recommendation 2. The recommendation is, however, as

3 <https://www.afca.org.au/members/>

4 <https://www.afca.org.au/about-afca/>

vague as Recommendation 1 in that it calls for a course of action without providing context, costing, meaning or any specificity.

1.14 **Recommendation 3** recommends that the Australian Government '*require Australian Credit Licence holders to comply with model litigant obligations throughout the internal and external dispute resolution processes, as well as any proceedings in the courts.*'

1.15 Government members of the committee agree with the sentiment of the recommendation, however, the Model Litigant Rules, or Model Litigant Obligations, are guidelines for how a government body ought behave before, during, and after litigation with another government body, a private company, or an individual. Application of the Model Litigant Rules or Model Litigant Obligation to non-government legal entities would require a re-assessment and adjustment of settled areas of the justice system, which re-assessment and adjustment was not canvassed in the conduct of the Inquiry or in the Inquiry report.

1.16 **Recommendation 4** calls on the Australian Government to '*immediately implement recommendation 4.11 of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry.*'

1.17 Recommendation 4.11 of the Royal Commission reads:

Section 912A of the Corporations Act should be amended to require that AFSL holders take reasonable steps to co-operate with AFCA in its resolution of particular disputes, including, in particular, by making available to AFCA all relevant documents and records relating to issues in dispute.⁵

1.18 It is noted that the Government introduced and passed the *Treasury Laws Amendment (AFCA Cooperation) Regulations 2019* that implement recommendation 4.11 of the Royal Commission. As such this recommendation is unnecessary.

1.19 Indeed, in the Budget Speech on April 2, 2019 the Treasurer remarked:

We also provide additional resources to our financial regulators following the Banking Royal Commission. This will strengthen the financial system and deliver better outcomes for all Australians.⁶

1.20 **Recommendation 5** recommends that the Australian Government '*amend the Bankruptcy Act 1966 to prevent causes of action relating to consumer credit protections from vesting in the trustee of bankruptcy.*'

1.21 Government members of the committee found the evidence presented to the Inquiry by Maurice Blackburn to be persuasive and would suggest that this issue be referred to the Attorney-General's Department for further inquiry and consideration, and that an advice be provided to Government on the implications of this evident ambiguity. The ambiguity in question relates to a bankrupt who pursues a cause of

5 Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, *Final Report: Volume 1*, February 2019, p. 34.

6 The Hon Josh Frydenberg MP, the Treasurer, *Proof Hansard*, 2 April 2019, pp. 78–79.

action against an 'irresponsible lender' for contributing to or precipitating the bankruptcy. According to s116(2)(g) of the *Bankruptcy Act 1966* 'any right of the bankrupt to recover damages or compensation for personal injury or wrong done to the bankrupt is excluded from the property that is divisible among creditors. If the entity from which a remedy in damages is sought is, however, a creditor of the bankrupt, then this entity will have an interest in the cause of action against itself. The 'irresponsible lender', as both a defendant and a creditor in this scenario, could exert influence upon the trustee in bankruptcy as to whether such a cause of action should be pursued at all. As submitted by Maurice Blackburn and noted in the majority committee report:

This means that the wrongdoer, for example the irresponsible lender that caused the bankruptcy, may have an interest in the cause or action against itself, which it may use to influence the determinations of the trustee in bankruptcy including whether the cause of action should be pursued or assigned.⁷

1.22 This legal ambiguity requires resolution.

1.23 **Recommendation 6** recommends that the Australia Government '*improve home repossession processes by requiring that creditors engage with customers at an earlier stage. This could involve:*

- (a) *establishing a new mediation section at the Australian Financial Complaints Authority (AFCA) to conduct farm debt mediations, and a new bank-initiated mediation stream for consumer and small business loans;*
- (b) *requiring banks to initiate a mediation through this new AFCA process before bringing repossession proceedings against a family home; and*
- (c) *requiring banks to give preference and due consideration to reasonable proposals put forward by customers to restructure debts, pay down parts of debts and/or trade out of temporary financial difficulty when a customer is in financial difficulty and a loan secured by or guaranteed by a family home is in default.'*

1.24 Government members of the Committee agree that engagement between borrowers and lenders should occur at the earliest possible time where such engagement has the potential to preclude or delay repossession. As the Law Council remarked in evidence to the Inquiry:

..the more that can be done at that front end and at that early point, the less we will see at that very difficult end when somebody is in the Supreme Court.⁸

1.25 This was a feature of the new AFCA regime and Government members suggest the recommendation is premature.

7 Maurice Blackburn, *Submission 47*, p. 9.

8 *Proof Committee Hansard*, Thursday 21 March 2019, p. 13.

1.26 **Recommendation 7** calls on the Australian Government to:

- *increase the current compensation cap available to consumers through the Australian Financial Complaints Authority (AFCA) to \$2 million, including for credit, insurance and financial advice disputes; and*
- *remove the sub-limit on compensation available to consumers through AFCA for indirect financial loss and for non-financial loss.*

1.27 AFCA has been in place since November 2018 and the Government has announced that a review will take place at eighteen months from that time. The call at paragraph 3.28 of the Committee majority's Report for a review to take place now, rather than at the pre-arranged juncture, is premature and unnecessary.

1.28 Government members of the committee support a fulsome review of AFCA's operations, including compensation caps and sub-limits, at eighteen months from November 2018 as planned.

1.29 It is noted—as it was in evidence to the Inquiry—that AFCA compensation limits impact directly on the professional indemnity insurance costs of small businesses who represent an overwhelming percentage of AFCA's 35,000 members.

1.30 **Recommendation 8** recommends that the Australian Government '*extend the membership of the Australian Financial Complaints Authority to:*

- *debt management firms;*
- *registered Debt Agreement Administrators;*
- *'buy now pay later' providers;*
- *FinTechs and emerging players;*
- *Small business lenders; and*
- *Professional indemnity insurers of financial providers.'*

1.31 Government members of the Committee agree in principle that AFCA membership should be as wide as is useful and practicable but caution that proper consideration should be given to the financial and administrative burdens that are placed upon AFCA members before making any formal proposal to expand membership. Many of the entities captured by the list in Recommendation 8 are likely to be small or even individual operations that may not be able to absorb the additional costs associated with membership. Government members are mindful that most operators in the financial services space conduct their businesses lawfully and fairly and do not take undue advantage of their customers, suppliers or competitors. It is important to acknowledge the distinction between oversight and over-regulation.

1.32 Financial sector reforms have been implemented by the Government to encourage fin-techs and start-ups, and to remove barriers to entry for new businesses. Many jobs in Australia exist in new sectors and new businesses. It would be unfortunate if attempts to regulate financial services were to have a cooling effect on other aspects of the economy, costing jobs and economic activity. It would also be undesirable to reduce competition and see only large financial services providers able

to operate because they are the only ones who can afford to do so under the applicable regulatory scheme.

1.33 **Recommendation 9** calls on the Australian Government to *'consider extending the loan facility limits for small businesses and farmers who wish to make a claim through the Australian Financial Complaints Authority (AFCA), in consultation with AFCA and other relevant stakeholders.'*

1.34 Once again, the AFCA review will take place at the allotted time.

1.35 Any change to the risk profile of lenders must be managed with great caution lest it impacts either the flow of credit, or the cost of credit.

1.36 The Government manages changes to the financial sector, and regulation of the financial sector, very carefully due to the potential for any misstep to have economy-wide implications. Any proposed changes may have complex impacts and must be considered with caution and only following extensive consultation.

1.37 **Recommendation 10** recommends *'the establishment of a retrospective compensation scheme independent of the Australian Financial Complaints Authority to allow victims of alleged misconduct by banks who received a past external dispute resolution determination or court judgement that was manifestly unjust to apply to the scheme to have the matter reviewed with the consent of the bank.'*

1.38 This recommendation is convoluted and ambiguous. It appears to be calling for a compensation scheme, a review/appeal mechanism, and a collaborative mediation scheme (between lending institutions and aggrieved borrowers) all at the same time.

1.39 It is of concern that the recommendation calls for a retrospective scheme without offering any detail as to the extent of this retrospectivity. It is also concerning that the term 'manifestly unjust' is used without any suggestion as to what might constitute a 'just' or 'unjust' determination, or whom may be called upon to make such a judgement.

1.40 Government members of the Committee would point to remarks from the Australian Banking Association which highlight the importance of the Rule of Law:

...where there has been a determination made by a court, we believe that any process to reopen those cases would need to be considered very carefully, with particular regard to the community's trust and confidence in the certainty of court determinations and the process of appeal that's available to citizens under our justice system.⁹

Senator the Hon Ian Macdonald

Deputy Chair