

Design and Distribution Obligations and Product Intervention Power

Legal Aid NSW Submission
to The Treasury

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NEW SOUTH WALES

Table of Contents

Introduction	3
Chapter 2: Products to be captured by these measures	3
<i>Question 1: all products except shares?</i>	3
<i>Question 2: products made available to retail clients</i>	3
<i>Question 3: regulated credit products</i>	3
<i>Question 4: coverage for credit facilities</i>	6
Chapter 3: Design and distribution obligations	9
<i>Question 5: defining “issuers”</i>	9
<i>Question 6: defining “distributors”</i>	9
<i>Question 7: distributors that do not receive a benefit</i>	11
<i>Question 8: excluding personal financial product advisers</i>	11
<i>Question 9: application of obligations</i>	11
<i>Question 10: identifying target markets</i>	12
<i>Question 11: benefit to consumer from insurance product</i>	14
<i>Question 12: appropriate distribution channels</i>	15
<i>Question 13: appropriate distribution channels</i>	15
<i>Question 14: periodic review of products</i>	17
<i>Question 15: issuer obligations in legislation or guidance</i>	18
<i>Question 16: reasonable controls on distribution</i>	18
<i>Question 17: access for consumers outside target market</i>	18
<i>Question 18: protections for consumers outside target market</i>	19
<i>Question 19: reasonable requests from the issuer</i>	19
<i>Question 20: distributor obligations in legislation or guidance</i>	19
<i>Question 21: commencement of obligations</i>	20
<i>Question 22: application to existing products</i>	20
Chapter 4: Product Intervention Power	20
<i>Question 23: product intervention power</i>	20
<i>Question 24: other interventions</i>	20
<i>Question 25: determining consumer detriment</i>	21
<i>Question 26: consultation before intervention</i>	22
<i>Question 27: requirement to publish</i>	23
<i>Question 28: duration of intervention</i>	24
<i>Question 29: interventions subject to appeal</i>	24
<i>Question 30: making interventions permanent</i>	24
<i>Question 31: providing certainty</i>	25
<i>Question 32: commencement of powers</i>	26
Chapter 5: Enforcement and consumer redress	26
<i>Question 33: enforcement arrangements</i>	26
<i>Question 34: consumer rights and redress</i>	26

About Legal Aid NSW

The Legal Aid Commission of New South Wales (Legal Aid NSW) is an independent statutory body established under the *Legal Aid Commission Act 1979* (NSW) to provide legal assistance, with a particular focus on the needs of people who are socially and economically disadvantaged.

Legal Aid NSW provides information, community legal education, advice, minor assistance and representation, through a large in-house legal practice and private practitioners. Legal Aid NSW also funds a number of services provided by non-government organisations, including 32 community legal centres and 28 Women's Domestic Violence Court Advocacy Services.

The Legal Aid NSW Civil Law Division focuses on legal problems that impact most on disadvantaged communities, such as credit, debt, housing, employment, social security and access to essential social services. Consumer issues constitute the largest category of service for our Civil Law Division.

In 2014-15 Legal Aid NSW provided 4,887 in house advice and 5,477 minor assistance services in consumer law

matters. More than one quarter of these matters dealt with credit products, including consumer leases. This submission draws on the casework experience of civil law solicitors in providing these services.

Legal Aid NSW welcomes the opportunity to provide a submission to the Design and Distribution Obligations and Product Intervention Power proposals that are being considered by the Treasury. Our submission follows the numbering of the questions outlined in the Proposals Paper.

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Introduction

Legal Aid NSW broadly supports the proposals to create new design and distribution obligations for issuers and distributors of financial products, and to create a new power for ASIC to intervene if a product is creating a risk of significant consumer detriment. These measures should reduce the number of consumers buying products that do not match their needs, promote fair treatment of consumers and build confidence in the financial system. There should be broad coverage of financial products, issuers and distributors to avoid any incentive to design products or distribution models that avoid the obligations. The product intervention power should be designed so that ASIC can act swiftly and proactively to prevent consumer detriment rather than waiting until harm has occurred.

Chapter 2: Products to be captured by these measures

Question 1: all products except shares?

Do you agree with all financial products except for ordinary shares being subject to both the design and distribution obligations and the product intervention power? Are there any financial products where the existing level of consumer protections means they should be excluded from the measures (for example, default (MySuper) or mass-customised (comprehensive income products for retirement) superannuation products)?

Yes. Legal Aid NSW supports broad coverage of all financial products in respect of the new measures.

If certain financial products are to be excluded from the measures, it should only be where existing consumer protections have been demonstrated to effectively protect consumers.

Question 2: products made available to retail clients

Do you agree with the design and distribution obligations and the product intervention power only applying to products made available to retail clients? If not, please explain with relevant examples.

Legal Aid NSW clients are ordinarily retail clients, and so we are not in a position to comment on the application of the new measures to products made available to wholesale clients.

Question 3: regulated credit products

Do you agree that regulated credit products should be subject to the product intervention power but not the design and distribution obligations? If not, please explain why with relevant examples.

No. Legal Aid NSW considers that regulated credit products should be subject to both the product intervention power and the design and distribution obligations. We are concerned

that the exclusion of regulated credit products would create a regulatory gap with the effect of lessening protections for consumers, in particular vulnerable consumers.

Responsible lending obligations

Legal Aid NSW does not agree that there is an overlap between the responsible lending obligations in the *National Consumer Protection Credit Act 2009* (Cth) ('the Credit Act') and the design and distribution obligations.

The Credit Act requires a credit provider to assess that each loan is "not unsuitable" for an individual consumer at point of sale. The responsible lending obligations, unlike the design and distribution obligations, do not place any burden on the credit provider before the point of sale. Specifically, the credit provider is not required to identify target and non-target markets of consumers during the product design phase, or to tailor product design to the target market. Further, the credit provider is not required to target distribution and marketing of the credit product to consumers who would benefit from the product.

Our casework experience shows that the responsible lending obligations, and other obligations in the Credit Act, do not go far enough in protecting vulnerable consumers from entering into harmful and unsuitable credit products. Our work assisting hundreds of consumers with small amount credit contracts (SACCs) and consumer leases provides many examples of this. Many of these matters involve the credit provider:

- targeting a vulnerable class of consumers, such as Aboriginal people living in remote areas of NSW, or people experiencing financial hardship
- failing to consider consumers' individual financial circumstances
- breaching their obligations under the Credit Act, and
- providing credit products to consumers that further entrenches their financial hardship.

The case studies of Cindy and Kylie, below, demonstrate that responsible lending obligations are not effectively preventing harm to vulnerable consumers. If design and distribution obligations were in force, sales practices would have to change and some of these products would not have been sold at all. Design and distribution obligations are a form of early intervention that could prevent harm to consumers.

Case Study – Cindy

Cindy is a young Aboriginal woman and a single mother to four children. Cindy was referred to Legal Aid NSW by a community organisation after she sought assistance with food and energy vouchers. Cindy believed her housing provider had been overcharging her on rent because she had such large deductions from her Centrelink benefit. After talking to Cindy about her circumstances it became clear that she was renting four household items. Cindy had signed up with two different rental providers and had already completed payment for rental contracts for an additional three

household items. Cindy did not realise how much of her Centrelink benefit had been paid towards her consumer lease contracts.

Cindy is in receipt of Centrelink benefits that amount to \$650 per fortnight. Cindy's rent is \$260, with an additional \$211 per fortnight deducted for her consumer lease contracts. This left Cindy with \$179 per fortnight to pay for electricity, food, transport and other expenses for her and her four children. Now that Legal Aid NSW has assisted Cindy to cancel her consumer lease payments, she is in a position to meet her living expenses without difficulty.

Case Study – Kylie

Kylie is a 48-year-old Aboriginal woman who lives in a remote community. She works on a part-time basis at a local community organisation and receives minimal Newstart and Carer payments from Centrelink. When Kylie started using SACC loans she had:

- a \$10,000 loan, for which she is now on a hardship arrangement
- a credit card debt of \$2,000
- a debt of \$3,706 following a car accident

Kylie struggled to manage her limited income and regularly borrows money from SACC providers to make ends meet. In the past two years, Kylie has had eight loans from two SACC providers, ranging from amounts from \$100 to \$1,900. On three occasions Kylie was granted a third loan in a 90-day period. The lender has been unable to demonstrate how they rebutted the presumptions of unsuitability.

In our view, the design and distribution obligations are a necessary protection for consumers of credit to close gaps in the current regulatory framework.

We also submit that unregulated credit products should be subject to both the design and distribution obligations and the product intervention power. This would prevent consumer harm from poorly designed unregulated credit products, and avoid creating further incentives for credit providers to design products that avoid Credit Act obligations. See further our response to Question 4 below.

Recommendation

- **Legal Aid NSW recommends that regulated and unregulated credit products should be subject to both the product intervention power and the design and distribution obligations.**

Question 4: coverage for credit facilities

Do you consider the product intervention power should be broader than regulated credit products? For example, 'credit facilities' covered by the unconscionable conduct provisions in the ASIC Act. If so, please explain why with relevant examples.

Yes. Legal Aid NSW strongly supports the product intervention power applying to both regulated and unregulated credit products. As stated at our response to Question 3, we also support the application of the design and distribution obligations to all credit products. At a minimum, Legal Aid NSW supports the product intervention power applying to credit facilities, as that term is used in Part 2, Division 2 of the *ASIC Act 2001* (Cth) ('the ASIC Act').

Legal Aid NSW regularly assists consumers who have been sold products designed by providers to avoid regulation and membership of external dispute resolution schemes. With this in mind, we consider that the power should have as broad an application as possible.

The case studies below provide examples of products designed to avoid regulation, and leading to consumer detriment, in respect of pawn-broking, rent to buy arrangements, "no interest" credit and funeral expenses funds.

Case Study – Aziz

Aziz went to a pawnbroker who offered him a \$1,600 loan. The pawnbroker took Aziz's car as security. Aziz's car is worth approximately \$6,000. The pawn ticket states that Aziz would pay "Interest: 25% Amount: \$400 per month". The terms and conditions of the pawn ticket were confusing. Aziz thought that he was paying 25% per annum interest for the three-month redemption period only. Aziz made three payments of \$500, \$400 and \$400.

Aziz did not understand that he was in fact paying 300% per annum interest, and each time he made a payment; the pawnbroker extended his redemption period by a further three months. Aziz returned to pay off the balance of his loan but was told that he could not redeem his car until he paid \$1800 in interest. The term of Aziz's loan has three months remaining, which means he risks accruing a further \$1200 in interest.

Aziz has no rights under the *Credit Act*. Legal Aid NSW is considering whether Aziz may have a claim under the *ASIC Act*, such as for misleading and deceptive conduct and unconscionable conduct. However, as the Proposals Paper notes, these remedies are for extreme misconduct and can be onerous to establish.

Case Study – Joan and Matthew

Joan and Matthew are an Aboriginal couple who live in regional NSW. They could not get a loan from a bank because of their poor credit history. Joan and Matthew entered into a rent to buy arrangement to purchase a property with Red House Pty Ltd.

Joan and Matthew signed an option to purchase and a residential tenancy agreement. Joan and Matthew paid option fees and rent. Rob, a director of Red House Pty Ltd, explained to Joan that she would have to pay a deposit, option fees and double market rent for four years. Rob said that all money paid above market rent would be put towards the deposit. After the four years, Rob would help Joan and Matthew obtain finance to exercise the option.

Joan and Matthew did not get legal advice and did not understand the terms of the option. According to the option, the money paid under the residential tenancy agreement was not being applied towards the deposit.

After three years, Joan and Matthew had difficulties making payments. Joan and Matthew could not exercise the option to buy the house because they were ineligible for finance. Mainstream lenders refused to give them a loan due to their bad credit history and because they do not lend for rent to buy arrangements.

Joan and Matthew spent \$140,000 on trying to buy the house. Joan and Matthew had to move out because they could not purchase the house. Joan and Matthew are considering their legal options, and may have to go to the Supreme Court to recover money paid under the Option.

Case Study – Janette

Janette is 63 years old and is unable to work due her anxiety and depression. Janette's sole income source is the Newstart payment from Centrelink. In early 2016, Janette was approached unsolicited by a company to have her home cladded for \$23,657. To pay for the cladding, Janette was offered a \$17,580 "no interest" loan with Easy-Pay loans. In approving the loan, Easy-Pay were aware that the client was not working but approved the loan based on her ability to pay previous debts with them. Easy-Pay obtained one months' worth of bank statements to verify the client's financial circumstances.

In the middle of 2016, Janette sought advice from Legal Aid NSW due to her severe financial hardship. In addition to the Easy-Pay debt, Janette had the following debts:

- \$180,000 home loan
- \$2,000 on an ANZ Credit Card
- Two \$10,000 debts on Commonwealth Bank Mastercards and

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- a \$531 debt on her ANZ Visa Card.

Janette saw a financial counsellor who estimated that Janette was in deficit of \$1,142 per fortnight. Janette was forgoing food to pay her bills. Legal Aid NSW was ultimately able to negotiate a hardship arrangement with Easy-Pay but it is unclear what rights, if any, Janette had under the Credit Act.

The case study below is one of approximately 100 that Legal Aid NSW is dealing with currently. It illustrated the risk of unsolicited sales of unregulated products targeting vulnerable consumers.

Case Study – Candice

Candice is an Indigenous woman. She has good literacy skills but does not work and relies on Centrelink for an income. She does not have any children but has at various times cared for many of her nieces and nephews.

In 2004, she was undertaking a Centrelink training program at the Aboriginal Medical Service. During one lunch break there was a presentation in the staff room from someone from Aboriginal Funeral Funds.

Candice had the impression that the organisation was an Aboriginal organisation and that it would be for the benefit of Aboriginal people. Because of this impression, she felt she could trust the organisation and was confident that in signing up her best interests would be looked after. Candice also thought the product was a fund, in the sense of a savings plan. She thought she was agreeing to put money aside for her various relatives' funerals. She thought she could get the money back if she pulled out of the fund.

Candice signed up herself and ten relatives over the next few years. Six of the nominees were children when they were signed up and two of the six were less than one year old. Upon hearing that the policies would cancel on her death (as the premiums would not be maintained), Candice sought legal advice. She had a very poor understanding of the product and she was at that time paying \$175 per fortnight to Aboriginal Funeral Fund. Prior to ceasing payments, Candice had paid in excess of \$40,000 to the company.

The above examples show that unregulated credit products and financial products can cause significant harm to consumers, especially vulnerable consumers. In our view, it would seem contrary to the purpose of the product intervention power that unregulated credit products be excluded from its scope. We are concerned that, under the terms of the current proposal, the product intervention power could not be used to intervene in respect of a number of harmful products. Unregulated credit products, rent to buy arrangements and funeral expenses funds already enjoy a regulatory gap, making it difficult for consumers to obtain a remedy when they are treated unfairly. As demonstrated in the case studies, these products create large consumer detriment and specifically target

vulnerable consumers, such as people living in remote indigenous communities. Failure to extend the intervention powers to these products misses a vital opportunity for ASIC to address some of the most exploitative products on the market and weakens the possible impacts of these powers.

Recommendations

Legal Aid NSW recommends that the product intervention power apply to

- **all financial products (as defined under Part 2, Division 2 of the ASIC Act) which are offered to retail consumers, which may then include wholesale products**
- **regulated and unregulated credit products, including credit facilities under Part 2, Division 2 of the ASIC Act, and**
- **real property as it relates to arrangements involving a residential home purchase.**

Chapter 3: Design and distribution obligations

Question 5: defining “issuers”

Do you agree with defining issuers as the entity that is responsible for the obligations owed under the terms of the facility that is the product? If not, please explain why with relevant examples. Are there any entities that you consider should be excluded from the definition of issuer?

Yes. Legal Aid NSW agrees with the proposed definition of issuers as defined in the *Corporations Act 2001* (Cth). With respect to credit products, we recommend that issuers be defined in relation to the definition of credit providers in the Credit Act.

Given that the intention is to cover the market as comprehensively as possible, Legal Aid NSW does not support excluding entities from the definition of issuer. Any exclusions stand to create inconsistencies in regulation which may motivate some issuers to structure their business model in a way that avoids the obligations.

Question 6: defining “distributors”

Do you agree with defining distributors as entity that arranges for the issue of a product or that:

(i) advertise a product, publish a statement that is reasonable likely to induce people as retail clients to acquire the product or make available a product disclosure document for a product; and

(ii) receive a benefit from the issuer of the product for engaging in the conduct referred to in (i) or for the issue of the product arising from that conduct (if the entity is not the issuer).

No. Legal Aid NSW recommends that the definition of distributor should be expanded to cover entities that distribute products via any means. We further recommend that the definition should not be restricted to entities that receive a benefit from the issuer.

Limb (i) of proposed definition: Conduct

The current definition covers entities that:

- advertise a product
- publish a statement to induce consumers to acquire a product, or
- make available a product disclosure document for a product.

Entities can engage in many other forms of conduct that are equally likely to induce a consumer to acquire the product. Examples of such conduct by entities include assistance to:

- apply for a product
- acquire a product, or
- vary the terms of a product.

Limb (ii) of proposed definition: Benefit

The proposed definition requires the distributor to receive a benefit from the issuer. We consider that this requirement is too restrictive. Entities with business models such as fee-for-service or vendor finance may not receive a benefit from the issuer for distributing the product. Alternatively, some entities may receive a benefit from an issuer, but receipt of the benefit is extremely difficult for the consumer to establish. We consider that these entities directly influence consumers' decisions to acquire a product and should be covered by the obligations.

Legal Aid NSW recommends that the receipt of a benefit should not be an element of the definition of distributor. In the alternative, the second limb of the definition could be redrafted to be less restrictive and allow for a "likely or perceived benefit". Please see our response to Question 7 for further detail.

Recommendation

- **Legal Aid NSW recommends that limb (i) of the definition be expanded to include entities that help consumers apply for a product, acquire a product or vary the terms of a product.**
- **Legal Aid NSW recommends that the requirement of receipt of a benefit in limb (ii) of the definition be removed.**
- **In the alternative, Legal Aid NSW recommends that the requirement in limb (ii) be redrafted to allow for a "likely or perceived benefit".**

Question 7: distributors that do not receive a benefit

Are there any situations where an entity (other than the issuer) should be included in the definition of distributor if it engages in the conduct in limb (i) but does not receive a benefit from the issuer?

Yes. As noted at our response to Question 6, there are situations where an entity engages in conduct that causes a consumer to acquire a product but the entity does not receive a benefit from the issuer. Further, there are situations where it is difficult for the consumer to establish that a benefit has been received by the entity. The rent to buy business model is one example of such a situation.

Rent to buy: Unclear if benefit received

Rent to buy business models can be structured in many different ways but often involve an entity who matches a vendor with a purchaser. All representations about the product are made by the rent to buy entity, including engaging the prospective purchasers and providing the relevant contracts to the purchasers. The parties to the contract, however, are only listed as the vendor and the purchaser.

The rent to buy business structure means that it is a complex and expensive task for the consumer to uncover if the rent to buy entity has in fact received a benefit in the transaction. We are concerned that entities such as rent to buy businesses would avoid the design and distribution obligations if the proposed definition of distributor was maintained. As noted at Question 6, we consider that the drafting of limb (ii) is too restrictive and may create an exemption for many entities which are intended to be covered by the obligations.

Question 8: excluding personal financial product advisers

Do you agree with excluding personal financial product advisers from the obligations placed on distributors? If not, please explain why with relevant examples. Are there any other entities that you consider should be excluded from the definition of distributor?

No. Legal Aid NSW notes the intention is for the obligations to have a broad application and any exception stands to limit the application of the obligations.

Question 9: application of obligations

Do you agree with the obligations applying to both licensed and unlicensed product issuers and distributors? If they do apply to unlicensed issuers and distributors, are there any unlicensed entities that should be excluded from the obligations (for example, entities covered by the regulatory sandbox exemption)? Who should be empowered to grant exemptions and in what circumstances?

Yes. Legal Aid NSW strongly agrees that the obligations should apply to both licensed and unlicensed issuers and distributors. Imposing the obligations on all entities provides consistency within the market, discourages efforts to avoid the obligations and strengthens consumer protections.

We again note that the intention is for the obligations to have a broad application. If exemptions are to be made, Legal Aid NSW submits that ASIC should be empowered to grant exemptions. Legal Aid NSW recommends that there be a prescribed and transparent process for granting exemptions, which could include establishing the rationale for exclusion and allowing feedback from stakeholders about the effectiveness of the existing protections.

Recommendations

- **Legal Aid NSW recommends that the obligations apply to licensed and unlicensed issuers and distributors.**
- **Legal Aid NSW recommends that ASIC be empowered to grant exemptions, after following a prescribed and transparent process.**

Question 10: identifying target markets

Do you agree with the proposal that issuers should identify appropriate target and non-target markets for their products? What factors should issuers have regard to when determining target markets?

Yes. Legal Aid NSW strongly supports the proposal that issuers should identify appropriate target and non-target markets for their products.

Identifying market: Product design phase

We note that the Financial System Inquiry (FSI) commented that issuers should identify target and non-target markets during the product design phase, taking into account the product's intended risk/return profile amongst other characteristics.

The FSI also commented that in some circumstances, issuers should stress-test the product to assess how consumers may be affected in different circumstances, and consumer-test products to make key features easy to understand.

Legal Aid NSW recommends that issuers should identify target and non-target markets during the product design phase, and tailor their product design to the target market. This approach has benefits for industry, consumers and the regulator, including:

- encouraging industry to be more consumer-focused in product design
- reducing the number of consumers buying products that do not match their needs, thus reducing consumer detriment, and
- limiting future regulatory intervention.

Identifying market: Overcoming difficulties

Legal Aid NSW acknowledges that defining target and non-target markets is a complex exercise. Introducing an individual suitability test is one approach that could help to overcome the practical difficulties with identifying target markets. However, we note the FSI's comments that this approach may be too onerous to implement.

As an alternative, we propose that ASIC provide clear guidance to industry about how to define target and non-target markets. This will be important to ensure that markets are not identified so broadly as to make the exercise meaningless.

Identifying market: Factors to consider

There is a wide range of factors that issuers should have regard to when determining markets. Consumer-related factors include:

- age
- income
- proximity to retirement
- financial literacy, and
- particular vulnerabilities (such as disability, Aboriginality, limited English skills).

Product-related factors include:

- the complexity of the product
- the cost of the product with regard to the consumer's financial circumstances
- suitability for the target market and the benefit that the consumer will obtain from the product, and
- the level of risk to the consumer.

Identifying market: Disclosure to consumer

Once the issuer has identified the target market, the consumer should be made aware, through marketing, advertising and any relevant Product Disclosure Statements: who the target market is and why; and equally importantly, who is not the intended target market and why.

Identifying market: Periodic review

After the product has been sold, Legal Aid NSW recommends that the issuer and distributor should periodically review whether the product still meets the needs of the target market. The results of the reviews should inform future product design processes.

Recommendations

- **Legal Aid NSW recommends that consumers should be made aware of who the target market is and why, and who the target market is not and why.**
- **Legal Aid NSW recommends that ASIC should issue clear guidance about how to define target and non-target markets.**
- **After the product has been sold, Legal Aid NSW recommends that the issuer and distributor should periodically review whether the product meets the needs of the target market. The results of the reviews should inform future product design processes.**

Question 11: benefit to consumer from insurance product

For insurance products, do you agree the factors requiring consumers in the target market to benefit from the significant features of the product? What do you think are significant features for different product types (for example, general insurance versus life insurance)?

Yes. Legal Aid NSW strongly supports a requirement that product issuers must target their products at consumers who will benefit from the significant features of a product. We also recommend that a target claims ratio should be set for each product so that there will be quantitative evidence that the target market does in fact benefit from the significant features of the product.

Our experience: Limited benefit to target market

Legal Aid NSW regularly assists clients in circumstances where the target market has been sold a product, which contains exclusions contrary to the characteristics of the market. In the context of home and contents insurance, some examples include:

- pensioners or seniors denied cover because they have “failed to maintain” properties that they have owned for several years, and
- grossly inadequate levels of cover provided to consumers living in disaster-prone areas, with the result that in the event of a total loss, the consumer is left to bear the cost of rebuilding the family home.

Our experience: Misunderstanding of product

In the context of general and life insurance, consumers regularly report a misunderstanding of what the salient features of the product are. The table below shows examples from our casework about the mismatch of the consumer’s understanding of the features of the product compared with their actual level of cover:

Product	Consumer understanding	Actual level of cover
Salary Continuance - Consumer Credit Insurance	Consumer told that in the event he became ill and could not work that he would be covered.	Consumer, as a casual worker, was excluded from any cover.
General Insurance - Building	Consumers believed that if they lost their home, the cash settlement would be for the sum insured.	Cash settlement was calculated using a complicated depreciation formula.
General Insurance - Building	Consumer believed that they were covered for the amount that it would cost them to rebuild their home.	Cover was for the amount that the insurer could rebuild the home for.
Add-on Insurance - Used Cars	Consumer believed that they were covered in the event that anything	Extremely limited cover provided.

	happened to the car in the year following purchase.	
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A common theme that emerges from these examples is that consumers expect to benefit from the significant features of the product that they have purchased. The proposal outlined at Question 11 will assist to align community expectation with industry practice.

Recommendations

- **Legal Aid NSW recommends that consumers in the target market should benefit from the significant features of a product.**
- **Legal Aid NSW recommends that a target claims ratio should be set for each product so that there will be quantitative evidence that the target market does in fact benefit from the significant features of the product.**

Question 12: appropriate distribution channels

Do you agree with the proposal that issuers should select distribution channels and marketing approaches for the product that are appropriate for the identified target market? If not, please explain why with relevant examples.

Yes. Legal Aid NSW strongly agrees with the proposal that issuers should select distribution channels and marketing approaches for the product that are appropriate for the identified target market.

We note our recommendation at Question 10 that issuers should identify target and non-target markets during the product design phase as well, and tailor their product design to the target market.

Question 13: appropriate distribution channels

Do you agree that issuers must have regard to the customers a distribution channel will reach, the risks associated with a distribution channel, steps to mitigate those risks and the complexity of the product when determining an appropriate target market? Are there any other factors that issuers should have regard to when determining appropriate distribution channels and market approach?

Yes. Legal Aid NSW strongly agrees that issuers must have regard to: the customers that a distribution channel will reach, the risks associated with a distribution channel, steps to mitigate those risks, and the complexity of the product when determining an appropriate target market.

Issuers must be aware of the way their distributors actually operate in the market place, particularly in relation to their sales and marketing techniques. Issuers should avoid distribution channels that pose a risk to and are detrimental to consumers. These channels could include door-to-door sales, unsolicited and high-pressure sales tactics and incentives to induce the consumer to purchase the product. The case studies below

indicate the harm that can result when complex financial products are sold after an unsolicited approach is made, an inducement is offered, and high-pressure sales tactics are employed.

Case Study – Mr and Mrs Robbo

Mr and Mrs Robbo are middle-aged consumers from a regional area. Mr Robbo receives the Disability Support Pension. During a holiday on the Gold Coast, the Robbos obtained a 'scratchie' from a stall at Dreamworld after being told they could win money or a holiday. The scratchie indicated that they had won so they returned to the stall and were told that all they had to do to claim their prize was attend a presentation and that there was no obligation to sign anything further.

The Robbos attended the presentation in offices at a nearby shopping centre. They told the sales agent that they were not going to sign anything on that day. The sales agent took the Robbos to see an apartment that 'would be just like the ones' they could stay at through the holiday club he was pitching. The Robbos were also taken through a one page 'holiday planner' that determined their dream holiday were they ever to have the money. They were told that if they signed up on that day only, they would get a special offer of 30 points and would accrue more points each year they were in the club.

The Robbos understood that if they signed up, their payments would be going towards the payment of future holidays, or accommodation points that could be exchanged for accommodation at any time. It was not explained that they were actually purchasing membership of a club and that they would be required to outlay more money to purchase accommodation points. Mrs Robbo asked the sales agent if they could get out of the agreement if they changed their mind. The sales agent said 'make sure you are sure, once you sign you cannot change your mind. It is a legally binding contract'. Within an hour of attending the presentation the Robbos signed up to a \$9,350, 15-year membership of a timeshare holiday club and a linked credit contract with a credit provider. The contract will ultimately cost them \$12,426 over five years.

After leaving the offices, the Robbos felt sick about the commitment they had made. They wanted to undo the contract, but remembered what the sales agent had told them. When the Robbos approached Legal Aid NSW for advice, we discovered that the complete contract was never disclosed, referencing 'general terms and conditions' that were not provided at any time. The contract also did not indicate that the Robbos would be provided the 30 accommodation points promised on the day of signing. The Robbos were not informed of their cooling-off rights and were shocked to learn that they had entered a time-sharing interest. Had this been disclosed, the Robbos never would have signed up, given its association with being an expensive and complex financial product.

Case Study – Mr Sulli

Mr Sulli is from a non-English speaking background. He is employed but his income is modest and he has a low level of financial literacy. While walking down the street on holiday with his wife and young children, Mr Sulli was approached by a sales representative who asked if he wanted ‘free tickets to the theme parks’. Mr Sulli agreed and was told he needed to attend an information seminar before he could obtain the tickets.

Mr Sulli attended the seminar and was subjected to a high level, high-pressure sales pitch for a time-sharing interest. He was told that if he signed up for membership he would be able to take a holiday at any time he wanted for the rest of his lifetime. Mr Sulli was in fact sold a very complex holiday club membership product which was financed by a linked credit contract. The credit contract was for a period of ten years and the total cost was over \$44,000. It was not adequately explained to Mr Sulli that he was entering into a credit contract, he had no opportunity to obtain independent legal advice and the actual cost of the product was not fully disclosed to him.

Mr Sulli did not receive any free theme park tickets either; he only received a 50% discount on the entry fee.

Recommendations

- **Legal Aid NSW recommends that issuers should be aware of how distribution channels actually operate in the marketplace.**
- **Legal Aid NSW recommends that issuers avoid distribution channels that involve any form of door-to-door sales, unsolicited sales, inducements and high-pressure sales tactics.**

Question 14: periodic review of products

Do you agree with the proposal that issuers must periodically review their products to ensure the identified target market and distribution channel continues to be appropriate and advise ASIC if the review identifies that a distributor is selling the product outside of the intended target market?

Yes. Legal Aid NSW strongly supports the proposal for periodic review by issuers and that issuers must advise ASIC if such a review identifies that a distributor is selling a product outside of the intended target market. We suggest that this could be incorporated into the mandatory breach reporting obligations of Australian Financial Services licensees.

Legal Aid NSW recommends that the periodic review occur with reasonable frequency and transparency. We also recommend that ASIC publish information in circumstances where the review identifies that a distributor is selling outside the target market.

This proposal should not interfere with ASIC's ability to intervene before a review takes place, in the event that ASIC becomes aware of a risk to consumers due to a distributor selling a product outside the intended target market.

Recommendations

- **Legal Aid NSW recommends that any periodic review process occur with reasonable frequency and be transparent.**
- **Legal Aid NSW recommends that ASIC should publish data in relation to the review process.**

Question 15: issuer obligations in legislation or guidance

In relation to all the proposed issuer obligations, what level of detail should be prescribed in legislation versus being specified in ASIC guidance?

Legal Aid NSW submits that a reasonable level of detail is required in the legislation to clearly identify and define the broad principles of issuer and distributor obligations.

Recognising that ASIC guidelines are more flexible, dynamic and easier to amend than legislation, detailed guidance should also be provided by ASIC.

Recommendations

- **Legal Aid NSW recommends that legislation include a reasonable level of detail to clearly identify and define the broad principles of issuer and distributor obligations.**
- **Legal Aid NSW recommends that ASIC guidelines provide more detailed guidance, including how the legislation will be enforced.**

Question 16: reasonable controls on distribution

Do you agree with the proposal that distributors must put in place reasonable controls to ensure that products are distributed in accordance with the issuer's expectations?

Yes. Legal Aid NSW agrees with this proposal. Legal Aid NSW recommends that issuers should review these controls as part of their periodic review, as noted in Question 14. Again, we suggest that this could be incorporated into the mandatory breach reporting obligations of Australian Financial Services licensees.

Question 17: access for consumers outside target market

To what extent should consumer be able to access a product outside of the identified target market?

Legal Aid NSW does not oppose consumers outside the target market accessing a product, but considers that there should be safeguards in place. One option is an opt-in model where the consumer is not contacted by the provider for a period of 48 hours after

initial contact, after which the consumer can elect to sign up to the product. This approach could be coupled with information in plain English provided to the consumer about:

- the product's features
- the risk to the consumer
- why the consumer is not within the target market, and
- the benefit (or lack of benefit) to the consumer.

Recommendations

- **Legal Aid NSW recommends that safeguards be in place where a consumer outside the target market wants to purchase a product, including:**
 - **an opt-in model, and**
 - **informing the consumer in Plain English about the product's features, the risks, the benefit or lack of benefit to the consumer and why the consumer does not fall within the target market.**

Question 18: protections for consumers outside target market

What protections should there be for consumers who are aware they are outside the target market but choose to access a product regardless.

Please see our response to Question 17.

Question 19: reasonable requests from the issuer

Do you agree with the proposal that distributors must comply with reasonable requests from the issuer related to the product review and put in place procedures to monitor the performance of products to support the review? Should an equivalent obligation also be imposed on advised distributors?

Yes. Legal Aid NSW agrees that distributors should comply with reasonable requests from the issuers related to the product review and put in place procedures to monitor the performance of products to support the review. We recommend that the procedure process be transparent and that the results of product review be made public.

Please see Question 8 for our comments about personal financial product advisers and advised distributors.

Question 20: distributor obligations in legislation or guidance

In relation to all the proposed distributor obligations, what level of detail should be prescribed in legislation versus being specified in ASIC guidance?

Please see our response to Question 15.

Question 21: commencement of obligations

Do you agree with the obligations applying 6 months after the reforms receive Royal Assent for products that have not been previously made available to consumers? If no, please explain why with relevant examples.

Yes. Legal Aid NSW agrees with the timeframe for implementation in relation to new products.

Question 22: application to existing products

Do you agree with the obligations applying to existing products in the market 2 years after the reforms receive Royal Assent? If not, please explain why with relevant examples and indicate what you consider to be a more appropriate transition period.

No. Legal Aid NSW disagrees with the timeframe for implementation in respect of existing products. We consider that providers should have a firm understanding of their existing products, and that a long implementation period of two years is unnecessary.

We recommend that the obligations apply to existing products one year after the reforms receive Royal Assent.

Recommendations

- **Legal Aid NSW recommends that the obligations apply to existing products one year after the reforms receive Royal Assent.**

Chapter 4: Product Intervention Power

Question 23: product intervention power

Do you agree that ASIC should be able to make interventions in relation to the product (or product feature), the types of consumers that can access a product or the circumstance in which a consumer can access the product? If not, please explain why with relevant examples.

Yes. Legal Aid NSW strongly supports the product intervention power proposal. We consider that the power will improve market integrity and enhance consumer protections, particularly in respect of vulnerable consumers who are often the target of inappropriate products that are ill suited to their needs. We note that the power has been in use in a number of international jurisdictions for some years, and would be a very welcome addition to ASIC's current powers.

Question 24: other interventions

Are there any other types of interventions ASIC should be able to make (for example, remuneration)?

Yes. Legal Aid NSW supports the interventions outlined in the Proposals Paper which cover disclosure obligations, warning statements, advertising and marketing documents, product features, product banning and distribution restrictions. However, we consider that the product intervention power should be aligned with ASIC's current approach to enforceable undertakings. This would increase the scope of possible interventions, including in relation to training and remuneration for financial products.

In our view, the harm stemming from many financial products relates to issues of mis-selling, which we submit is often intrinsically related to:

- knowledge of the products held by staff of distributors or issuers, and
- the sales incentives to staff of issuers or distributors.

Failing to allow ASIC the power to intervene on those issues may lead to uneven responses to harmful products, and may limit the systemic impact that the power may have on industry practice. We acknowledge the view that these issues could be addressed by legislative reforms to professional standards and life insurance remuneration, but submit that the intervention power is a more effective and consistent way to limit consumer harm.

Recommendation:

- **Legal Aid NSW recommends that the product intervention power be extended to training and remuneration.**

Question 25: determining consumer detriment

Do you agree that the extent of a consumer detriment being determined by reference to the scale of the detriment in the market, the potential scale of the detriment to individual consumer, and the class of consumers impacted?

Legal Aid NSW agrees that in determining whether there is a risk of significant consumer detriment, ASIC should consider

- the potential scale of the detriment in the market
- the potential scale of the detriment to individual consumers, and
- the class of consumer likely to be affected, in particular whether those consumers are likely to be experiencing hardship or vulnerability.

Risk of consumer detriment

Legal Aid NSW agrees that an intervention should be permitted where there is a risk of consumer detriment, rather than a breach of a law or actual detriment. In our view, this approach aligns with the intended proactive, preventative and pre-emptive nature of the product intervention power. We note that this view reflects the position taken by the UK's Financial Conduct Authority (FCA) and the European Union.

Value of loss

We agree with the suggestion in the Proposals Paper that ASIC should be able to intervene in circumstances where the risks to consumers are not necessarily significant in terms of the value to the individual consumer, but rather involve small losses to multiple consumers.

Vulnerable consumers

We agree with the suggestions in the Proposals Paper that:

- exercise of the power should take into account whether a particular class of consumers is vulnerable or more likely to experience hardship as a result of the product, and
- a detriment affecting a particularly vulnerable class of consumers is more likely to warrant investigation by ASIC.

Question 26: consultation before intervention

Do you agree with ASIC being required to undertake consultation and consider the use of alternative powers before making an intervention? Are there any other steps that should be incorporated?

No. Legal Aid NSW's preferred approach is that taken by the UK's FCA. The FCA can make temporary product intervention rules without consultation which lapse after 12 months. During this period, the FCA consults on and makes permanent rules.

We endorse this approach. It would overcome any risk of delay caused by a consultation process. We consider that the FCA approach reflects the FSI's comments that:

ASIC should be equipped to take a more proactive approach to reducing the risk of significant detriment to consumers with a new power to allow for *more timely and targeted intervention*.¹ (emphasis added)

We note the FSI's comments that the product intervention power should be used as a "last resort or pre-emptive measure."² In our view, it should always be used as the latter. This is consistent with the FSI's rationale that the product intervention power should facilitate targeted early intervention to reduce harm to consumers rather than waiting until detriment has occurred.³ With this in mind, we do not agree that ASIC should be required to consider the use of alternative powers before making an intervention. Instead, ASIC should select the most appropriate power to alleviate consumer harm in the circumstances, as is already its practice.

In the alternative, we recommend that ASIC consider engaging in a consultation process on a case-by-case basis depending on the level of consumer detriment.

¹ Financial System Inquiry Final Report, December 2014, 206.

² Financial System Inquiry Final Report, December 2014, 206.

³ Financial System Inquiry Final Report, December 2014, 209.

Recommendations

- **Legal Aid NSW recommends that ASIC be able to make temporary product intervention rules, without consultation, which lapse after 12 months.**
- **In the alternative, Legal Aid NSW recommends that ASIC consider the level of consultation necessary on a case-by-case basis depending on consumer detriment.**
- **Legal Aid NSW recommends that ASIC should exercise the product intervention power if it is the most appropriate power to alleviate consumer harm in the circumstances.**

Question 27: requirement to publish

Do you agree with ASIC being required to publish information on intervention, the consumer detriment and its consideration of alternative powers? Is there any other information that should be made available?

Yes. Legal Aid NSW agrees that ASIC should be required to publish information on intervention and the consumer detriment. Following from our response to Question 26, we consider that ASIC should publish information about its consideration of the most appropriate power to use in the circumstances.

ASIC should also publish information about particular traders subject to the intervention, where possible.

ASIC should be empowered to direct traders subject to the intervention to take steps to notify their customers of the intervention, its implications and any avenues for redress.

Recommendations

- **Legal Aid NSW recommends that ASIC should be required to publish information on intervention, the consumer detriment and its consideration of the most appropriate power to use in the circumstances.**
- **Legal Aid NSW recommends that ASIC publish information about particular traders, where possible.**
- **Legal Aid NSW recommends that ASIC be empowered to direct traders to take steps to notify their customers of the intervention, its implications and any avenues for redress.**

Question 28: duration of intervention

Do you agree with interventions applying for an initial duration of up to 18 months with no ability for extensions? Would a different time frame be more appropriate? Please explain why.

We agree with this approach, as long as ASIC has the power to make a permanent intervention (discussed further in Question 30).

If this approach is not taken, ASIC should have the power to extend the operation of the intervention after the 18-month period until the Government has made a decision as to whether to confirm the intervention. This exercise could be subject to safeguards such as the protocols surrounding ASIC's sunset class orders.

Recommendations

- **Legal Aid NSW recommends that ASIC should have the power to make permanent rules.**
- **In the alternative, ASIC should have the power to extend an intervention until the Government has made a decision about its permanency.**

Question 29: interventions subject to appeal

What arrangements should apply if any ASIC intervention is subject to administrative or judicial appeal? Should an appeal extend the duration that the Government has to make an intervention permanent?

Legal Aid NSW recommends that if an ASIC intervention is subject to an appeal, whether judicial or administrative, that the intervention should remain in place until such time as the appeal is resolved.

Recommendation:

- **Legal Aid NSW recommends that if an ASIC intervention is subject to an appeal, the intervention should remain in place until such time as the appeal is resolved.**

Question 30: making interventions permanent

What mechanism should the Government use to make interventions permanent and should the mechanism differ depending on whether it is an individual or market wide intervention? What (if any) appeal mechanisms should apply to a Government decision to make an intervention permanent?

Our preferred approach is for ASIC to have the power to make both initial interventions and permanent rules for individual and market-wide matters.

We note that Professor Dimity Kingsford Smith and Dr Marina Nehme, in their response to Recommendation 22 of the Financial System Inquiry Final Report, said:

There should be a power to extend the temporary rules or orders and to make permanent PIPs rules. Accountability for proper making of temporary and permanent PIPs rules should be through registration under the Legislative Instruments Act 2003 and application for judicial review to the Federal Court of Australia. Accountability for exercise of the power to make PIPs temporary intervention orders should be under the Administrative Appeals Tribunal Act 1975.⁴

This would mirror the UK model where the FCA has the power to make permanent rules, following consultation, about a wide range of matters including banning products or services.⁵ ASIC has the power to make legislative instruments under the Corporations Act, and should also have such powers under the Credit Act. It could be required to consult with stakeholders before making a permanent rule. These could be disallowable instruments.

Recommendations

- **Legal Aid NSW recommends that ASIC be provided with powers to make permanent rules for individual and market-wide interventions.**

Question 31: providing certainty

Are there any other mechanisms that could be implemented to provide certainty around the use of the product intervention power?

Yes.

Transparency

Transparency of information around the product intervention power is vital. Consumers and consumer advocates should be able to access information surrounding the circumstances of when, how and against which trader the power is being used.

Legal Aid NSW recommends that a public register be kept that reports when the product intervention power has been used. The public register could be made accessible online via the ASIC website.

Guidance

ASIC should publish guidance available to industry and consumers about how the product intervention power can be used.

⁴ Professor Kingsford Smith, Dr Nehme, *Product Intervention Powers: a Legal, Comparative & Policy Analysis*, <http://download.asic.gov.au/media/3251548/product-intervention-powers-a-legal-comparative-and-policy-analysis.pdf>

⁵ *Financial Services and Markets Act 2000* (UK) ss 137A, 137D, 137E.

Recommendations:

- **Legal Aid NSW recommends that a public register be kept that reports when the product intervention power has been used.**
- **Legal Aid NSW recommends that ASIC publish guidance about how the product intervention power can be used.**

Question 32: commencement of powers

Do you agree with the powers applying from the date of Royal Assent? If not, please explain why with relevant examples.

Yes. Legal Aid NSW agrees with the proposed start date on the basis that the powers relate to all relevant financial products.

Chapter 5: Enforcement and consumer redress

Question 33: enforcement arrangements

What enforcement arrangement should apply in relation to a breach of the design and distribution obligations or the requirements in an intervention?

ASIC must be given authority to select from all of its enforcement powers, including administrative actions, civil penalties, criminal penalties and injunctive actions. Each breach should be dealt with on a case-by-case basis and the appropriate penalty determined based on the circumstances surrounding the breach.

Importantly, ASIC should be fully resourced and well equipped to be able to effectively enforce the obligations and use the product intervention power.

Recommendations

- **Legal Aid NSW recommends that ASIC have the authority to select from all of its enforcement powers depending on the circumstances of the breach.**
- **Legal Aid NSW recommends that ASIC be adequately resourced to effectively enforce the design and distribution obligations and exercise its product intervention powers.**

Question 34: consumer rights and redress

What consumer rights and redress avenues should apply in relation to a breach of the design and distribution obligations or the requirements of an intervention?

Consumers should be afforded all the rights and redress avenues that have been described in the Proposals Paper including:

- compensation

-
- remedies for refunds or replacement products at no additional cost
 - contracts to be voidable at the option of the consumer
 - the option to seek orders declaring the whole or part of a contract void or terms varied and
 - the option of participating in civil litigation and class actions.

Consumers should also have the right to participate in external dispute resolution (EDR) as a means to resolve their dispute. We note, however, that unlicensed providers would need to become members of EDR to ensure consumers have this option as a redress avenue.

Further, traders should be required to notify consumers when there has been an action against their provider. If a consumer has a product with a certain provider and that provider has been found to have breached the obligations or a requirement in an intervention, then all customers of that provider must be notified in writing of the breach and avenues for redress. ASIC should oversee the notification to ensure that it is accurate, in plain English, and provides information on options for redress. Transparency of information will be a powerful tool for consumer choice and may act as a further deterrent to providers.

Recommendations

- **Legal Aid NSW recommends that consumers be afforded the following redress avenues:**
 - **compensation**
 - **remedies for refunds or replacement products at no additional cost**
 - **contracts to be voidable at the option of the consumer**
 - **the option to seek orders declaring the whole or part of a contract void or terms varied, and**
 - **the option of participating in civil litigation and class actions.**
- **Legal Aid NSW recommends that consumers should have a right to participate in external dispute resolution as a result of a breach of the new measures, even where the provider is unlicensed.**
- **Legal Aid NSW recommends that traders be required to notify their consumers in writing when they have breached the design and distribution obligations or a requirement in an intervention.**