FSC FINANCIAL SERVICES COUNCIL

ASIC Consultation Paper 335: consumer remediation

FSC Submission

March 2021

FSC FINANCIAL SERVICES COUNCIL

Contents

1. About the Financial Services Council

The FSC is a leading peak body which sets mandatory Standards and develops policy for more than 100 member companies in one of Australia's largest industry sectors, financial services.

Our Full Members represent Australia's retail and wholesale funds management businesses, superannuation funds, life insurers, financial advice licensees and licensed trustee companies. Our Supporting Members represent the professional services firms such as ICT, consulting, accounting, legal, recruitment, actuarial and research houses.

The financial services industry is responsible for investing $3 trillion on behalf of more than 15.6 million Australians. The pool of funds under management is larger than Australia's GDP and the capitalisation of the Australian Securities Exchange, and is the fourth largest pool of managed funds in the world.

2. Introductory Remarks

The FSC welcomes the opportunity to provide a submission to the Australian Securities & Investments Commission (**ASIC**) relating to Consultation Paper (**CP**) 335 *Consumer remediation: Update to RG 256* released on 3 December 2020.

The FSC acknowledges the importance of an appropriate remediation framework in financial services to improve confidence in the financial services system, by providing customers with appropriate recompense where relevant laws and regulations are not met.

As an overall comment, the FSC is broadly supportive of ASIC's proposals in the consultation paper and considers in most cases it is in line with current remediation practices.

The FSC's members wish to ensure our affected customers are put back in the position they would have been in had the event not occurred. However, we encourage ASIC to consider the proportional impact of costs and certainty of the rules when licensees perform remediation.

We are concerned that the effect of CP335 and its proposed amendments to RG256 may have effects on industry that may lead to increases in remediation complexity for industry while creating more ambiguity and uncertainty for industry and consumers. FSC members have had experience in addressing remediation with increased frequency and cost in recent years and our comments reflect a strong focus of members to help lift efficiency of remediation in the FSC's areas of membership, namely superannuation, life insurance, investments and financial advice.

The FSC's members continue to face a number of practical issues that make it difficult for registrable superannuation entities and fund managers to expedite efficient resolution including the following:

- Access by entities to client files that are held by financial advisers particularly where they're no longer aligned with the product issuer that receives a matter for remediation assessment.
- Existing privacy obligations such that customer details aren't shared between advisers and the fund manager/superannuation fund.
- Expectations of the regulator to review third party remediation programs where it has been conducted by an independently owned and managed advice business.

While it is in the interests of customers and licensees to remediate on a timely basis, the current settings and those proposed do not appear likely to achieve the goal of doing so in the way all stakeholders would prefer; namely as fast and as fairly as possible.

The FSC submits that any changes to remediation guidance, and response to submissions, should be assessed independently within 12 months after the revised guidance commences, including the impact on customers and businesses, and any economic, competition, consumer and policy implications.

2.1. ASIC monitoring

The FSC acknowledges ASIC's concern that monitoring remediation programs is resource-intensive, and that one of the objectives of updating RG256 is to enable ASIC to reduce the resources it currently devotes to remediation. In the introduction to CP355, ASIC observed that "there is a lack of transparency as to how remediations more broadly are being carried out". While we agree with the majority of ASIC's proposals in CP355, it is unclear how updated guidance will address this lack of transparency.

The advice industry is currently undergoing a multifaceted transformation, including significant adviser migration away from the corporate groups which were the subject of ASIC Report 515. To the extent that ASIC is monitoring breach reporting and remediation activity, there is value in ASIC monitoring the activities of all industry participants, not just those that were, or remain, affiliated with the companies the subject of ASIC's wealth management project.

2.2. Whole of Government consistency

The FSC considers it very important for the efficiency of remediation that there be consistency in the views of Government and government agencies on customer remediation. The FSC submits that, before the commencement of any changes in remediation guidance:

- ASIC liaise with other relevant agencies, including APRA, ATO, AFCA and the Privacy Commissioner to coordinate a common whole-of-government approach to remediation;
- ASIC's approach to remediation should align with that common whole-of-government approach; and
- ASIC should not require a particular approach to remediation if this approach does not work in the context of requirements of other agencies.

3. Section B: when to initiate a remediation

The FSC agrees in principle with the removal of the term "systemic" issue and replacing that with a requirement that a remediation must be initiated when "a licensee has engaged in a misconduct, error or compliance failure" as it is a more accurate indicator of the types of issues that are typically remediated by licensees.

The FSC submits there is a need for more clarity to understand the intersection between a revised RG256 and RG271 and ensuring alignment with AFCA expectations including their recent fairness guidance. While we appreciate ASIC referencing the scalability of the remediation undertaken by a licensee, we have additional concerns that without clear guidance that this will create unnecessary administrative and compliance burdens which are likely to result in delays in members receiving timely outcomes.

In the case that ASIC's expectation is for all remediation activities to be covered under the revised RG256, sufficient time from when the guidance is finalised will be required to assess potential impacts within members companies including the time required to conduct appropriate change management and implementation.

3.1. B1Q1 Do you agree with our proposed two-tiered approach to initiating remediation? If not, why not?

We do not agree with ASIC's proposed two-tier approach and consider that a licensee should only be required to remediate a customer when it has breached a legal or regulatory obligation or a contract with the customer, causing loss or detriment to a customer. Tier 1 sufficiently captures this requirement. We do not consider it practical or appropriate to go beyond that and extend the obligation to "community expectations" which may be more aspirational and/or were never intended to be mandatory.

We submit that the Tier 2 obligations are inherently vague, amorphous, subjective and difficult for licensees to interpret when a customer may consider their standards or expectations have not been met. We have concerns that the current articulation of Tier 2 has the potential to add significant complexity of remediation, in particular:

- A licensee may have breached an industry code by not sending certain correspondence to the customer due to a system fault. We agree that the licensee should be required to report a significant breach of a code or standard to an industry compliance committee, investigate and fix the cause of the issue, but it may not be appropriate to remediate the customer in this circumstance, other than by re-sending the relevant correspondence and providing an apology.
    - This example may fall under the 'detriment' arm of ASIC's 'loss, detriment and disadvantage' framework. We submit that ASIC should provide further clarity about these terms, clarifying that this type of example does not fall within the framework for remediation.
- The range of considerations in Tier 2 may (a) cause delays in deciding whether to initiate remediation (extending the overall time taken to remediate) and (b) may be applied inconsistently across the industry which could lead to different outcomes for consumers.
- Customers can suffer loss or detriment for many reasons and not all of them are attributable to the licensee they have engaged with. When a licensee is at fault, it is generally because there has been misconduct, error or compliance failure (Tier 1).
- Community standards and expectations change over time, can be subjective, and are informed by prevailing sentiment. They are also rarely documented or determined based on consensus. Attempting to apply these concepts to trigger that determination would likely lead to significant inconsistency and inefficiency.
- The structure of the Tier 1 and Tier 2 approach to initiating a remediation is unclear. The layout and use of the word "and" between Tier 1 and Tier 2 on pages 12 and 44 suggests that there must be a breach of Tier 1 and Tier 2 to trigger a remediation, and may cause confusion and inconsistency across licensees.

- The scope and implications of adding Tier 2 remediations are broad and policy in nature, and are arguably outside the scope of industry guidance.
- Issues relating to compensation money subject to Tier 2 remediations, including differing payment pathways (such as ex-gratia or another form) as well as the appropriate tax treatment where the payment relates to superannuation payments. We strongly encourage more clarity and ASIC to work with the ATO as appropriate to resolve such issues.

Licensees must ensure that their financial services are provided efficiently, honestly and fairly under section 912A of the Corporations Act (Cth) (**the Act**). If there is a case where, due to the facts, not meeting a community expectation or breaching an industry code, happened to also constitute a breach of section 912A, then such conduct would be captured by Tier 1 in any case.

Licensees need to be fair and consistent in their remediation approaches: across classes, unitholders and products. In some instances, this may translate to remediation of what the CP256 defines as a Tier 2 failure, but this should not be required as a matter of course. The FSC recommends ASIC provide clarity that the ASIC/APRA Good Practice Guide for Unit Pricing is still considered best practice.

The inherent subjectivity and vagueness of Tier 2 will increase the volume of breaches reported to ASIC, especially in light of the new breach reporting obligations to commence this year, and will increase ASIC's involvement in licensee remediations. Licensees should do all things necessary to put the customer back into the position that they would have been had the breach not occurred and the regulatory guide should support this principle but not include additional obligations on licensees that go beyond the legal and regulatory framework, specifically Tier 2.

Given the above, we submit that Tier 2 events (involving no breach of law, legislation or contract) should not automatically be matters for remediation. If a Tier 2 event occurs, then it ought to remain a matter for the licensee's discretion as to whether it decides to provide a response involving remediation or compensation. Where a breach of a code constituted a breach of law or legislation (for example, those provisions of any industry code which are designated as an enforceable code provision) then those provisions would fall within Tier 1 in any case.

In the event a two-tiered approach is adopted, assessment of whether the failure warrants remediation should be based on what is objectively reasonable to expect in the circumstances. The FSC submits further guidance should be provided to set clear expectations of what may be considered reasonable, including ASIC working with industry to develop examples of Tier 2 remediation that do not meet the Tier 1 requirement.

3.2. Single customers

ASIC's proposal that customer remediation might need to be initiated for a single customer will result in additional compliance and operational obligations and may delay the speed at which the customer is redressed. Single customer remediation is currently addressed as part of other processes, including complaints handling.

To set the threshold for remediation at only one customer will significantly increase the number of remediations a licensee is required to complete, thus reducing efficiency and timeliness of customer outcomes.

When it is identified that an individual customer has been impacted by misconduct, error or compliance failure, the FSC submits that customer impact should not be governed by ASIC guidance on remediation. The impact should be addressed on a case-by-case basis, informed by the processes and values of the organisation, either directly with the customer or, where a complaint has been made, through IDR and/or EDR. We note ASIC's comment on the scalability of remediation and, while we believe approaches can be scaled, it is still likely to be significantly more onerous than finding and fixing an individual customer impact due to the additional processes, steps and procedural requirements to govern remediation.

A complaint that is investigated and resolved should not be considered an automatic trigger for a broader remediation. Whether a broader investigation is required should be left to the discretion and judgment of the business.

Please see also discussion below on beneficial assumptions in relation to remediation by a single customer.

3.3. Other comments on Section B

The FSC makes the following additional points on Section B:

- While CP 335 aims to provide flexibility by proposing that once a remediation is initiated, it may be tailored and scaled for every circumstance, the FSC requests more clarity about the concept and application of scalability, such as ASIC providing some factors as to what constitutes a material customer remediation activity.
- There may be value in ASIC developing concise and clear definitions for customer impact (failures), including loss, detriment and disadvantage. This will particularly assist large organisations where remediation decisions are distributed across the business.
- The requirement to remediate is triggered when a business has engaged in a misconduct, error or compliance failure that has caused consumers to have suffered potential or actual loss, detriment or disadvantage (loss) as a result. This should be limited to financial loss. It is unclear what is meant to be captured by 'disadvantage', and in the absence of specific guidance, we suggest this be removed from the explanation of when a remediation should be initiated.
- In relation to fund managers and remediating potential loss, it is challenging to implement a consistent or sustainable remediation methodology based on 'potential' loss. For the majority of errors relating to Managed Investment Schemes (**MISs**), there is a clear financial loss that is suffered directly by the fund or by clients. There may also be compensation for the time value of money for any potential or actual loss of performance, however this is in addition to a clear, identifiable loss. It is unclear how the introduction of 'potential' loss provides clarity for fund managers.

4. Section C: The review period for a remediation

4.1. C1Q1 Do you agree with this proposal? If not, why not?

The FSC agrees with ASIC that some remediations may go back more than 7 years and that paragraphs in the current RG256 may have created an impression that licensees and product issuers are only required to remediate customers 7 years from the date the licensee discovered the issue.

The FSC agrees that the review period for a remediation should begin on the date a licensee or product issuer reasonably believes the failure first caused loss to a customer, and should not be limited (or there be an impression that it is limited) to just 7 years in every case, especially where the licensee or product issuer has records to support a longer timeframe.

However, there are two important caveats which should be recognised and addressed in the revised guidance.

The first relates to the application of limitation periods, a topic on which CP 335 is silent. The application of limitation periods is, for many remediations, a legitimate and in some cases a necessary step in considering the relevant review period. This should be expressly recognised, with guidance provided, in the revised guidance.

The legitimacy of the application of limitation periods to a remediation is underscored by two recent events:

1. In October 2020, the decision in *Australian Securities and Investments Commission v Australia and New Zealand Banking Group Ltd (No 3)* [2020] FCA 1421 was delivered. In that case Allsop CJ considered a licensee's reliance on a limitation period in a remediation relating to the licensee's unauthorised charging of certain fees. The Chief Justice's finding was that the unauthorised charging began in 2003, with the licensee becoming aware of the risk of the unauthorised charging in 2011. On that basis he stated, at [67] of the judgment, '[i]f characterised as a breach of contract, there would be no apparent reason why a party in the position of the Bank should not apply a statute of limitations period to such circumstances', noting the 'legitimacy' of ASIC confining the remediation contravention to the period from 2005 (ie applying a 6-year limitation period back from 2011) rather than from 2003.

2. In December 2020, the *Financial Sector Reform (Hayne Royal Commission Response) Act 2020* (Cth) became law. The Act amends the *Corporations Act 2001* (Cth) to include an obligation to remediate customers who have received personal advice (see new ss912EA and 912EB). The obligation is said to apply only where there are reasonable grounds to believe the affected customer has a 'legally enforceable right to recover the loss or damage' from the licensee. The relevant Explanatory Memorandum explains, at [12.33], '[a] customer would not have a legally enforceable right where, for example, the underlying cause of

action has been extinguished or barred as not enforceable by expiry of the relevant limitation period'.

As a role for limitation periods in remediations appears to be accepted in case law and contemplated by the Corporations Act, we submit that the revised RG 256 should acknowledge the relevance of limitation periods in remediations.

This is not to say limitation periods should limit the look back period for all remediations. We recognise some licensees and product issuers may choose to remediate customers even where those customers, due to a limitation period, do not have a legally enforceable right to recover loss or damage suffered.

Related to limitation periods, ASIC should provide guidance on how licensees and product issuers should identify the appropriate cause of action in respect of the loss or damage for which the remediation is seeking to compensate, recognising as Allsop CJ did in the ANZ case referred to above that a failure may give rise to multiple causes of action, potentially with different applicable limitation periods.

The second important caveat relates to the document retention obligations and practices of licensees and product issuers.

In some cases, as ASIC recognises, a licensee and product issuer will have documents to enable a review period of a timeframe longer than 7 years. However, the revised guidance should recognise the obligation to retain documents is normally for a maximum period of 7 years. It should also recognise licensees' and product issuers' legitimate interest in having finite document retention periods.

We submit the guidance should state that when a licensee and product issuer has complied with its document retention obligations and does not hold records before that point, its remediation need only include those customers for whom it has relevant records or for whom it would be reasonable in the circumstances to make a beneficial assumption to include them.

Furthermore, we submit that if ASIC proceeds with the position that a remediation should begin on the date a licensee reasonably suspects the failure first caused loss to a consumer, it should clarify and provide worked examples of how this might work in practice where there are insufficient records.

4.2. C1Q2 Are there any practical problems associated with this proposal? Please give details.

The FSC notes that the quality of records may degrade over time for a variety of a reasons and the reduced availability of records beyond seven years can make it difficult to efficiently and effectively assess customer impact.

ASIC's proposal states that gaps in records should be filled by making "beneficial assumptions". However, where no, or limited records are available, this process poses resourcing and decision making challenges. Further, its inherent uncertainty and subjectivity

may lead to significant inefficiency, remediation delay and cost, as well as potentially inappropriate outcomes.

For example, if a business has a record that a person was a customer more than seven years ago but holds no other information on the customer, it is not reasonable on this basis alone to make the beneficial assumption that the customer should be paid remediation.

In addition, the Australian Privacy Principles require an organisation to take reasonable steps to destroy or permanently de-identify personal information once it is no longer needed. If the view is taken that information should be retained indefinitely because it possibly may at some point in the future be in some way relevant to customer remediations, this would run counter to privacy considerations and also increase the risk of misuse or unauthorised access.

ASIC have commented at paragraph 39 that some issues have arisen due to legacy products and systems, and the difficulties these cause in relation to accessing records to facilitate appropriate and timely remediation. In 2015 the Government made a commitment to a comprehensive product rationalisation scheme for legacy products in financial services (life insurance and funds management), however, this has yet to be acted on. Implementation of such a scheme would assist to resolve the remediation difficulties associated with legacy products (and systems).

The default position should not be that in the absence of records outside of the legislated record-keeping periods, a licensee should be assumed to have to remediate a customer(s).

The FSC notes the expectations of large licensees/firms should not be different to those of smaller organisations, for this provides no incentive for smaller organisations to improve record keeping and modernise systems etc, and creates inconsistent outcomes for consumers. The approach is currently unclear about whether it creates lower expectations for smaller licensees. While there are practical challenges of smaller licensees in conducting remediation activities, it is unclear why superannuation members who are advised by smaller licensees should have a lower standard.

4.3. C1Q3 Are there any other matters that we should consider to help us provide appropriately scalable guidance?

We note that advice and investment remediations generally require records to be provided by third parties, for example product issuers or former advisers. The FSC submits that ASIC should consider the best approach to ensuring third parties engage with and support requests for records relating to remediation and provide guidance for the industry (noting the importance of maintaining privacy).

5. Section D: Using beneficial assumptions

5.1. D1Q1 Do you agree with our proposal for assumptions to be beneficial and that they should satisfy certain considerations. If not, why not?

The FSC notes the use of an appropriate assumption can help drive efficiency and speed of remediation execution.

The FSC submits the regulatory guide should make it clear that licensees and product issuers can elect to make a beneficial assumption in respect to a refund, efficiency or scoping assumption at its discretion and should not be obligated to use beneficial assumptions as a default position.

Instead, the FSC submits that the basis for an assumption in remediation is what is appropriate and reasonable in the circumstances. We recommend adopting the term "reasonable assumptions" for these purposes. We recommend this change in approach because:

1. We consider that the definition of a beneficial assumption provided in the consultation is too broad and vague for practical purposes.
2. There can be a variety of assumptions that will need to be made in a remediation which do not benefit or disadvantage a customer but which are important for efficiency purposes – for example, it may be assumed that the only conduct being assessed is the identified misconduct and that the remediation is not undertaking a full re-assessment of compliance with law and regulations. Other assumptions may not always be beneficial but are reasonable, for example, where there is some evidence of compliance with the law but not full evidence. Focussing on beneficial assumptions raises the question of the legitimacy of these other assumptions.
3. This may lead to potential complexity and delays in the execution of remediation, as a firm will have to not only make an assumption, but evidence and document that the assumption is beneficial.
4. Where there are multiple clients/individuals/cohorts, an assumption that benefits one may in some cases disadvantage another.
5. The FSC submits clarity is needed on where an assumption may be 'generally' fair and reasonable, particularly where it is otherwise possible that an applied assumption may result in a number of affected customers being undercompensated.
6. In large scale remediations (ie unitholders in a fund) there may be instances where an assumption may not be beneficial to every unitholder. In this instance it would be better if the wording made it clear that the beneficial assumption could be made in respect of those impacted individuals as a collective (the class of individuals impacted). It would not be possible to always determine in a large-scale remediation that it was a beneficial assumption for every individual and therefore would be of limited use in large scale remediations if this is not clarified.

In addition to these points, ASIC's guidance is intended to apply to all remediations, however, the requirement for evidence-based and documented assumptions and to monitor those assumptions do not translate well outside formal remediation projects (for example, compensating a small number of customers for an error).

We submit that it is unclear what ASIC intends when it refers to monitoring an assumption. The FSC submits ASIC should provide examples and/or further guidance to show licensees what evidence of assumptions or monitoring would be required.

Further, the FSC requests clarity from ASIC about how licensees and product issuers will be expected to evidence that the assumptions are 'beneficial' for customers. For example, how would an assumption of future earnings or CPI in the future be evidence-based? Would sampling be permitted and can licensees propose the approach and methodology? Further clarity on ASIC's preferred sampling approach would be welcome. We also recommend providing more information and examples as to what ASIC has in mind about future earnings and CPI in the future.

If the extent of evidence required means specific remediation calculations effectively need to be completed for all in-scope customers, this would defeat the purposes of enabling licensees to complete their customer remediation activities efficiently.

Given they have the obligation and expertise in this area, licensees should be empowered to determine reasonable assumptions that expedite the completion and reduce the complexity of remediation while seeking to return all affected consumers as closely as possible to the position they would have otherwise been in.

5.2. D1Q3 Is it appropriate to use an assumption based on an average (e.g. in calculating loss, using the average premium or the average fees charged over a relevant period?) If not, why not?

This may be appropriate to increase of the efficiency of remediation in certain situations, for example, where records are not available and customer impact is likely low and in a narrow band (that is, having a small tail/low variance) or where appropriate sampling has identified the customer failure rate and the cost of individual file assessments is not commensurate with the average customer's loss.

However, it is unclear as to how an averaging approach — which by its nature will result in some members being worse off — aligns with ASIC expectations that beneficial assumptions should result in *all* affected customers being returned to the position that they would have otherwise been in. This is ambiguous and arguably inconsistent, potentially leading to uncertainty for both industry and as to what customers might expect.

We encourage ASIC to develop examples that are provided in the guidance making use of averages and failure rates assessed through appropriate sampling to illustrate this approach further.

5.3. D2Q2 Are there any practical problems associated with this proposal? Please give details.

If licensees and product issuers are required to make only 'beneficial assumptions' if records are absent and this is outside of record-keeping obligations, this will result in significant over remediation. Licensees and product issuers should be required to utilise the records available to ensure as many customers impacted by a failure are restored. However, the FSC has concerns with a proposal for licensees to develop a series of beneficial assumptions when they have met their record-keeping requirements. Rather, we submit aligning regulatory guidance with legal obligations will allow licensees to remediate more efficiently and provides a more comprehensible and consistent point of reference.

There are additional issues with beneficial assumptions in relation to failures that have impacted only one customer. While this is contemplated by RG271, we note that licensees will need to take great care if a solitary customer alleges an historic failure (outside record-keeping obligations), with significant operational impacts potentially triggered by this event if a licensee doesn't know if further disputes might arise. In these instances, we submit that customers should be required to produce records to support their claim, otherwise licensees may be required to make 'beneficial assumptions' where there is no evidence of any failure.

The FSC also notes that concerns have been raised that the ATO in particular can take a tough line with beneficial remediation assumptions that can effectively act as a discouragement to the use of these assumptions. For example:

- the ATO requiring detailed breakdowns of remediation amounts to determine where the payer of remediation is being 'generous' to the customer by using a beneficial assumption, thus slowing down remediation programs; and
- the ATO arguing a remediation into a super account involving a beneficial assumption should be treated as a superannuation contribution, thus having a detrimental effect on some customers.

This approach by the ATO appears to be operating counter to ASIC's preferred approach to beneficial assumptions. This indicates the importance of FSC's recommendation that ASIC work with other agencies to ensure a consistent whole-of-government approach to remediation (see introductory remarks).

5.4. D2Q3 Are there any other matters that we should consider to help us provide appropriately scalable guidance?

In many cases, an assumption may require a licensee to perform a significant amount of investigation and testing, to ensure no customer is worse off. We seek ASIC's guidance and worked examples of what is appropriate if licensees will be required to utilise assumptions to increase the efficiency of remediation.

We submit that ASIC should consider working with industry to set reasonable assumptions across the industry, regulators and EDR schemes. An agreed set of assumptions will aid licensees to effectively and efficiently restore customers and mitigate the risk of an obligation which is imprecise and/or unclear and fails to achieve its objective.

In relation to unit pricing (UP) rectifications, the purpose of these is to put the client in the position they would have been had the error not occurred. This is important as UP has flow on impacts to other decisions and calculations such as entry price in to the fund for new investors, performance fees and management fees, and valuations for other trusts in some cases, therefore we query whether using beneficial assumptions may impact some processes or stakeholders that have not fully been considered. This may have the impact of disadvantaging other stakeholder groups or processes.

6. Section E: Calculating foregone returns

6.1. E1Q1 Do you agree with this proposal to set out a three-step framework for calculating returns or interest? If not, why not?

Step 3 includes underlying assumptions as to what is 'fair and reasonable', for example, daily compounding of interest and a 'reasonably high' rate. At the current time, ASIC has expressed a preference for the RBA cash rate + 6% per annum.

These assumptions may be applicable to equity products or similar risky investments where customers anticipate an equity related return on investments. However, this assumption should be questioned for other products, particularly those that provide stable/capital guaranteed returns. A rate of cash +6%, with daily compounding, could not be considered 'fair and reasonable' for many fixed interest products, bond funds, cash management, or all deposit products.

In addition, members note that the terms 'if it is appropriate to do so in the circumstances' and 'reasonably practical' are arguably ambiguous and may encourage licensees to move straight into Steps 2 and 3 without attempting to calculate foregone returns or interest rates without the use of assumptions. We would appreciate clarity from ASIC as to when it may be appropriate to move to Steps 2 and 3, particularly in cases where the licensee has the data available to calculate actual foregone returns but has elected not to do so.

6.2. E1Q3 Should our guidance clarify whether the rate compounds (and at what interval) or whether it should be based on simple interest? Please give reasons

In general, the compounding basis should be aligned to that of the relevant product to provide the most appropriate outcome for consumers.

In addition, the FSC submits ASIC should provide further clarity around the use of the prescribed rate under the *Life Insurance Act 1995* (i.e. bond rate plus 3 per cent per annum) for certain insurance matters as there may be different practices across the industry, including differing views between insurers and trustees.

In relation to Step 3, it would be useful if ASIC could confirm that using the Federal Court Post Judgement Interest Rate is consistent with ASIC's expectations of using a rate that is "reasonably high, relatively stable and objectively set".

7. Section F: How to approach finding and automatically paying customers

7.1. General comments on section F

The FSC agrees that guidance in respect to what is considered an appropriate approach to finding customers would assist licensees. For example, the current RG256 briefly mentions that licensees should make "reasonable efforts" to contact a customer when they don't respond to communications that ask the customer to respond within a specific timeframe. Some remediation communications may request the customer contact the licensee or product issuer to receive a refund but do not impose a timeframe. Therefore, removing the reference to a specified timeframe would provide more clarity.

In general terms, "best endeavours" is a high standard and may lead to uncertainty and be unduly onerous as to how far a licensee's approach needs to go. A standard of "best endeavours" is potentially fraught as a point of reference. It is submitted that the extent of the obligation should be governed by, and expressed as, what is reasonable in the circumstances.

If ASIC intend to provide guidance as to what constitutes "reasonable efforts" or "best endeavours" the FSC submits this guidance should be practical and measurable, and the cost involved to the licensee or product issuer should be commensurate with the actual loss suffered by the customer.

The FSC also requests that ASIC provide guidance for 'return to sender' scenarios. For example, when remediation letters are sent to customers and the licensee or product issuer receives a 'return to sender' notification and the licensee or product issuer is unable to contact the customer in any other way (and they have exhausted best endeavours) because there is no email, phone numbers or any other viable method to contact the customer.

It would also assist if ASIC could provide guidance that confirms that any monetary compensation should be sent to the relevant unclaimed monies register.

There would be substantial value in the Government facilitating the sharing of information, particularly from the ATO, to enable direct payment to customers who do not have an open, suitable account. By allowing licensees and product issuers to share records and access records through the ATO, solely for the purposes of remediation, we submit this is likely to substantially increase a licensee's and product issuer's ability to find and directly pay compensation to customers.[1]

In relation to reuniting lost superannuation members, see the comments on *The Treasury Laws Amendment (Reuniting More Superannuation) Bill 2020* under section 8.1 below.

[1] For superannuation products, this could possibly be achieved by extending the terms of use of the ATO Provision of Details Service to allow this to be used for exited members (currently this can be used to obtain contact details for members who are lost or at risk of becoming lost).

7.2. F1Q4 Do you agree that cheques should be paid as a last resort? If not, why not?

When customers do not have an open, suitable account to receive compensation, appropriately endorsed cheques offer a pragmatic solution for both the customer and licensee or product issuer. When supported by robust follow up processes, sending cheques can be an appropriate method to compensate customers.

7.3. F1Q7 If you are a superannuation trustee, what challenges do you have in accepting and/or facilitating remediation payments from third-party licensees? Please give details.

The following response is on behalf of FSC members that are superannuation trustees.

As indicated in this submission's introductory comments, the role of the superannuation trustee in third party remediations is unclear. This creates considerable legal and financial uncertainties in the sector that we submit should be addressed. As trustees are the source of the original payments and the recipient or facilitator of remediation payments, it may be appropriate for them to understand the amounts paid to clients but the third party may not always be willing or able to provide that information. It is also unclear what role the superannuation trustee should take if they disagree with the third party's approach to remediation. For example, if the trustee seeks to have compensation calculated on actual loss and the third party insists on RBA + 6%. The FSC recommends that ASIC provide guidance in this area.

We submit guidance on superannuation trustee legal responsibilities to members will assist trustees develop better and more robust processes consistent with their duties.

For superannuation trustees, it can also be unclear when it is appropriate for compensation payments involving superannuation to be paid as cash directly to the member. Payments should generally be made back to the superannuation fund to make the fund 'whole', regardless of whether a condition of superannuation release (such as retirement) has been met. Further, where an individual is no longer eligible to contribute to super or has fully utilised contribution caps, making a cash payment removes the ability for the person to retain the amount in the super system. As a general principle, licensees should seek to retain remediation payments within the superannuation system where this is practicable.

In addition, we submit that ASIC should provide guidance about when it is likely to be appropriate for remediation monies in relation to superannuation to be paid out directly as cash, including where a recipient has already met a condition of release.[2] We recommend ASIC consult with APRA, ATO and DSS to ensure a consistent approach (consistent with comments in the introduction to this submission).

[2] See also page 3 of joint APRA-ASIC letter to RSE Trustees, dated 10 April 2019, entitled "Oversight of fees charged to members' superannuation accounts", which indicates ASIC and APRA would take action in some cases against practices where remediation is paid outside of super.

If payment is made outside of superannuation, a degree of comfort would be required about the rights and obligations of the superannuation fund – while the fund member has been remediated the superannuation fund has not been remediated and there is an argument the fund might still have a cause of action against the payer of remediation. Further, the superannuation trustee may not always be able to access the necessary information in order to defend such a claim.

Therefore, further guidance from ASIC would be welcome confirming how compensation involving superannuation may be treated.

7.4. Removing the low-value compensation threshold: F2Q1 Do you agree with our proposal? If not, why not?

We respectfully disagree with the removal of the $20 low value threshold for former customers, however we agree that this should not provide an opportunity for windfall gains for licensees. The low-value compensation threshold provides clarity, consistency and efficiency to licensees. We submit that by removing the threshold, this may delay remediation for customers as licensee resources would be diverted to attempt compensation payments for small amounts.

We recommend that the updated guidance clarify that the low value threshold only applies to customers who no longer hold a policy or account but are suitable to receive compensation from the licensee as it is not a financially sustainable option for a licensee to include former customers in a remediation where the value of the refund or compensation is less than $20. In addition, from a customer perspective, it is unlikely to be appropriate to be contacting former customers asking them to action a $5 refund.

We understand that the value of compensation differs from individual to individual, for example a $100 refund to one person may be significant whereas to another its immaterial. However, given the difficulty and cost of contacting former product holders, we think a reasonable compromise (as acknowledged in ASIC guidance – see ASIC RG 94) is that licensees not be obligated to contact former customers where the remediation is $20 or less and instead:

- donate such money to a charity,
- lodge the payment into unclaimed monies where that regime applies for such nominal amounts, noting it may not apply in some cases, or
- pay these amounts to the superannuation fund or MIS for the benefit of all current members, noting remediation amounts for superannuation funds and MIS are trust money and any money belonging to former members should either remain in the fund/ MIS for the benefit of all existing members and or paid according to unclaimed monies.
    - The payment to unclaimed monies may require that the super fund/MIS to make attempts to pay the amounts to members/unitholders in the first instance. The current unclaimed money processes may not alleviate the administration burden for small amounts.

The FSC considers that having a low value threshold is useful and practical when a licensee is conducting a scoping exercise for affected customers. If that threshold is removed, then licensees are able to use a subjective judgment call to determine what they consider is low value compared to the cost of contacting former customers. That value will vary between licensees and create inconsistencies. We agree that the starting point should be to return all money to current customers, but the $20 low value threshold should not be removed for customers who do not hold current policies or accounts suitable to receive compensation. This is in line with ASIC's current rationale in the consultation paper and explanation in the current regulatory guidance. Even if ASIC keeps the low value threshold in the regulatory guide for former customers, this does not stop the licensee including these customers in their remediation if they choose to.

We submit that the actual remediation cost (staff and operational costs) to the licensee to remediate a former customer who is owed a $20 refund is disproportionate to the customer's loss. An example of these costs to the licensee include the following:

- Identifying potentially affected customers;
- Consideration of what is fair and appropriate;
- Calculating the loss suffered and any interest;
- Investigating contact details;
- Drafting a communication plan and relevant correspondence;
- Drafting follow up correspondence or building webforms; and
- Management of unresponsive customers and the unclaimed money process.

In such cases, the licensee does not benefit, as the amount due to former customers would either be paid to a charity or for a community benefit, or else (where unclaimed monies legislation applicable allows for such nominal amounts to be sent to unclaimed monies) paid in accordance with the applicable unclaimed monies requirement (which differs depending on the type of product or remediation).

Case study

Background: An issue was identified whereby the APRA Levy (charge to a member account to cover a levy imposed on super funds by APRA) was over collected across products held by a superannuation fund for FY2018 and part of 2019. The levy was reduced to zero within the registry system for part of 2019 to reduce the member impact. However, as the levy was charged across all members within the fund, the issue effectively impacted all active and exited members who were members of the fund throughout the impact period.

Remediation: The resulting investigation identified ~$1.4m in overpayments needing to be reunited with 133,000 members. ~$1.27m was returned from overpayments held in the fund operations account where it had been accumulating and a further $141k was paid in interest separately by the Trustee.

Of the above remediation, $1.33m was paid and communicated across 101,000 members who were either active members or exited members whose remediation payment was >$20.

An amount of ~$88k was paid to the fund reserves to cover 32,000 exited members owed <$20 in line with trustee's Compensation Policy. The average member impact in this cohort inclusive of interest was $2.72.

The above remediation provides a practical example of what the impact would be in a similar circumstance if there was the removal of the low-value compensation threshold.

Removing the <$20 threshold would introduce nearly 14 times the amount of exited member interactions that were completed for the APRA levy. This would have created a significant increase in the time required to test and execute account creation (to house the refunds), posting of adjustments, exit payments and member communications. Additionally, this would also have resulted in a greater number of payments out that failed, could not be processed or members who could not be communicated with due to being lost and uncontactable. (Note: Our research shows nearly 25% of members fall into this cohort. This would mean that ~8,000 members would not have their remediation paid immediately and would likely wait for 16 months before the amount could be moved to the ATO).

It should be noted also that the timeframe for investigation to completion of this issue, that is all to the point where all were processed, took ~6 months. This timing would likely have been greater if exits less than $20 were to have been included.

Member expectation: In addition to the above, we also noted that our members do not respond positively to low value remediations with negative commentary received from members who have received small remediation amounts for example ***'Mate you just spent 50c posting a letter that said you had made a 1c error. Don't waste either of our time with this')***

While this does not suggest that for active members we should cease paying any remediation amount, it does demonstrate that community and member expectations are that members will receive fair compensation where due, but also that their fees are put towards resources that improve outcomes for them as members.

Again, the above is based entirely on current guidance, we must re-iterate the point that paying exits under $20, based on current guidance, does not produce favourable member outcomes. However, were remediation legislation to be implemented that allows funds to make payments directly to the ATO, or at least when a payment fails would certainly deliver better member outcomes as the ATOs visibility across the industry and resulting repatriation capabilities far outweigh those of individual industry participants.

7.5. F2Q2 Do you think that any licensee using a low-value compensation threshold should have to disclose it? If not, why not?

We submit that if regulatory guidance provides sufficient clarity and sets a standard low-value compensation threshold, then disclosure will not be required. If disclosure is required, we note it is unclear in the guidance who the disclosure needs to be made to. If the

disclosure is to be made individually to those impacted by the low value threshold then it is likely to limit any savings or benefits from this approach.

8. G: remediation money that cannot be returned

8.1. G1Q1 Do you agree with our proposal

We agree that remediation payments in general should not be paid using the assets of a pooled investment scheme; however if it is identified that the fund has incorrectly benefited from the error, compensation may be paid from the fund to ensure both the fund and clients are in the position they should have been had the error not occurred.

8.2. G1Q2 Is it appropriate for ASIC to provide guidance that any money that cannot be directly returned to consumers be lodged in an unclaimed money regime? If not, why not? G1Q3 What challenges are there in lodging unclaimed money? Please give details.

FSC members would welcome further guidance from ASIC on payment to unclaimed money systems, as these systems and processes generally do not specifically contemplate remediation compensation. Some issues include:

- When does compensation payments to customers become legally payable to the customer? From the date the licensee knew the funds were owing to the customer or the date the first communication is sent to the customer?
- When does an unclaimed money regime's holding requirement commence in the context of remediation compensation? Should holding requirements apply at all?
- To what point should a rate of return be applied to a principal compensation amount when compensation will be sent to an unclaimed money regime, particularly where significant effort and follow-up has occurred in an attempt to contact and pay the customer?
- What is an appropriate threshold for 'best endeavours' to find and pay customers?
- If a licensee sends a bank cheque, how and when can the licensee unilaterally cancel the bank cheque (as these cheques do not automatically expire), before sending the compensation to an unclaimed money regime?
- Can licensees deal with compensation below the relevant unclaimed money regime's threshold after a reasonable follow up process?
- In context of superannuation, when can compensation be paid to the fund to benefit all existing members, or is this considered profiting from the failure?

We note that Parliament has very recently passed *The Treasury Laws Amendment (Reuniting More Superannuation) Bill 2020* which includes provisions to allow superannuation funds to voluntarily transfer amounts to the ATO in circumstances where the trustee believes it is in the best interests of that member. These provisions could help with remediations involving lost superannuation members.

The FSC considers it would be useful if the ASIC guidance set out that in these circumstances it would be considered to be in members best interest to transfer the amount directly to the ATO under this provision.

9. Settlement deeds

9.1. H1Q1 In what circumstances, if any, are settlement deeds essential to protect your legitimate interests?

ASIC's is proposing to clarify their guidance about the appropriateness of using settlement deeds and sought feedback as to the circumstances where settlement deeds are essential to protect the licensees' legitimate interests.

FSC members have raised concerns around any proposed change to the licensees' ability to use settlement deeds. We note that it is standard practice in the context of insurance for insurers to require copies of signed settlement deeds before they would consider whether they would be making a pay out under the terms of a policy. Settlement deeds are therefore essential to protecting the interests of licensees where insurance policies are involved, without which the licensees' interests may be adversely impacted.

We also note that fund managers use settlement deeds with institutional investors or third party providers which provides a useful avenue for limiting liability between corporate entities.

10. Other Feedback

The FSC provides this additional feedback on CP 335.

- CP 335 does not contemplate the source of funds that can be used to remediate clients. There remains some ambiguity on this approach, with ASIC seemingly permitting some industry participants to remediate cohorts of members using other members money, or operational reserves, while other industry participants are required to remediate out of shareholder capital. Whilst the FSC interprets recent legal precedent in the superannuation context as indicating that member reserves cannot be used to remediate members, it appears this remains standard practice in some sectors. The FSC submits that ASIC should clarify its position on whether members and customers savings and/or administrative reserves can be used to fund some or all of a remediation program, and apply a consistent approach across all participants in the financial services sector.

- To the extent allowed by law, ASIC should make it clear that electronic delivery and electronic signatures are the preferred method if customers are required to sign and return forms to receive compensation. The regulatory guide should set out that paper forms and wet signatures should be avoided in respect to remediation and only used as a last resort to make it easier to remediate customer efficiently.

- The breach reporting paragraphs at RG256.65 to RG256.67 will need to be updated in the regulatory guide in line with the new Royal Commission breach reporting legislation due to commence on 1 October 2021.

- We request that the updated guidance should not have retrospective application. This approach would be consistent with the approach taken by ASIC when RG 256 was originally issued (i.e. RG 256.12 provided that the guidance only applied to client review and remediation initiated on or after the RG 256 issue date). Should the revised guidance have retrospective application, it could expose licensees to considerable risk if the new RG 256 amendments were not applied to ongoing client remediation, or significantly impact the timeliness and cost (including re-work) if the RG 256 amendments were to be incorporated into ongoing client remediation.