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Attention: Amanda Fairbairn, Policy Lawyer
The Behavioural Unit
Australian Securities and Investments Commission
GPO Box 9827
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Dear Ms Fairbairn

Norton Rose Fulbright Australia – Response to ASIC Consultation Paper 335

1 Introduction

1.1 Norton Rose Fulbright Australia (**NRF**) welcomes the opportunity to provide our response to the Australian Securities and Investments Commission's (**ASIC**) Consultation Paper (**CP**) 335 on the proposed update of Regulatory Guide 256 (**RG 256**).

1.2 NRF is broadly supportive of the various proposals made in CP 335. We set out in the proceeding paragraphs the matters of most significance for ASIC's consideration.

2 When to initiate a remediation (Section B, CP 335)

2.1 We agree with ASIC's proposal to remove reference to systemic issues and the suggestion that it may not be appropriate to remediate product failures (paragraph 28, CP 335).

Tier 1

2.2 We note ASIC's observation that "the types of failures that have caused consumer loss and fall under Tier 1 will generally involve a breach of the law or a contractual failing" (paragraph 31, CP 335). To the extent that the proposed Tier 1 involves a breach of law or contract, we agree with the proposal.

Tier 2

2.3 Regarding the proposed Tier 2, we note that it is not intended to go beyond what is reasonable to expect (paragraph 34, CP 335). According to Figure 1 which appears under paragraph 26, Tier 2 is triggered where there are failures causing loss that breach:

(1) industry codes of conduct;

(2) the standards and expectations of the licensees' consumers;

(3) other external standards and expectations; and

(4) the licensees' business values.

2.4 While we do not dispute that licensees are required to comply with obligations that are broad in nature, including the general obligations under s912A(1)(a) of the *Corporations Act 2001* (Cth) (**Corporations Act**), we consider that Tier 2 raises uncertainty from a practical perspective. In particular, it is our submission that the reference to "expectations" is too vague, potentially subjective and overly broad for licensees to ensure ongoing compliance.

2.5 We would like to highlight the following issues:

(1) What segment do these "expectations" relate to? Figure 1 makes reference to "*other* external standards and expectations" (emphasis added) which we submit is overly broad. Expectations are constantly changing and it seems unreasonable and unfair to require licensees to remediate in circumstances where the goal posts are potentially constantly (and even regularly) shifting. It will be very difficult for licensees to understand, and embed across their vast organisations, trigger points for a Tier 2 breach.

(2) The reference to "consumers' standards and expectations" is also unclear: is it the impacted consumers of the impacted product(s) or service(s) that these standards and expectations relate to, current consumers of those product(s) or service(s), or community standards and expectations more broadly?

(3) It is also unclear from the existing wording what timeframe is intended for Tier 2 to be triggered. As mentioned, "expectations" constantly change and can be anticipated to change in response to various external factors including prevailing sentiment. For instance, are licensees expected to consider "expectations" at the time when the consumer entered into the agreement with the licensee to obtain products or services or at the time that something goes wrong? It is noted that the developments in recent years may have substantially altered the "expectations" of consumers and the wider community in general, compared to consumer expectations prior to the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (**Royal Commission**).

(4) Similarly, the "business values" of the licensees may well have changed post Royal Commission. It is unclear whether, for instance, under the proposed changes licensees are expected to remediate consumers under Tier 2 for not meeting its *current* business values even though it has met its then business values for the lifetime of the product and/or services.

2.6 An additional issue relates to the ambiguity around how the two-tiered approach to initiating a remediation (Proposal B1) is intended to operate in the context of the new breach reporting regime. The *Financial Sector Reform (Hayne Royal Commission Response) Act 2020* (Cth) (**Hayne Act**) defines a "reportable situation" to include situations where the licensee breaches a "core obligation". Such core obligations are defined to include a wide range of obligations, including:

(1) the obligation to do all things necessary to ensure that the financial services covered by the licence are provided efficiently, honestly and fairly (s912A(1)(a) of the Corporations Act); and

(2) the obligation to comply with the financial services laws ((s912A(1)(c) of the Corporations Act), so far as it relates to the provisions of the Corporations Act or the *Australian Securities and Investments Commission Act 2001* (Cth) (**ASIC Act**) as defined in s761A of the Corporations Act. This includes the sections of the ASIC Act which deal with unconscionable conduct.

2.7 ASIC suggests that "[t]ier 2 may cover failures causing loss that are not formally reported to ASIC under s912D of the Corporations Act…" (paragraph 32, CP 335). However, this suggestion does not seem to align with the new breach reporting regime. Due to the broad definition of "core obligations" under the Hayne Act, it is arguable that Tier 2 breaches may technically be captured as a "reportable situation" (by virtue of a breach of an obligation under s912A(1)(a) of the Corporations Act). Given

that s912EB(8) of the Hayne Act requires licensees to remediate certain clients upon completion of an investigation into a "reportable situation", we query whether licensees would be obliged to remediate certain Tier 2 breaches which would effectively turn them into Tier 1 breaches (where remediation is mandated). This obscures ASIC's proposed delineation between the two tiers. Given the lack of clarity as to how the two-tiered approach operates in the context of the new breach reporting regime, licensees can also be expected to err on the side of caution which may result in a material increase in the number of breach reports submitted.

2.8 A potential result of the lack of clarity is different licensees applying different interpretations as to when Tier 2 would be triggered. This is likely to compromise the objective of the updated guide in achieving consistency across licensees and the industry generally.

3 **The review period for a remediation (Section C, CP 335)**

3.1 ASIC has proposed that, as a starting point, the relevant start date for a remediation period should begin on "the date a licensee reasonably suspects the failure first caused loss to a consumer" (Proposal C1).

3.2 We agree with ASIC that some remediation may go back more than seven years. We also share the view that the time period referred to in RG 256.85 may have created an impression that licensees are only required to remediate customers seven years from the date the licensee discovered the issue (paragraph 38, CP 335).

3.3 ASIC's proposal on the starting date means that the remediation period will not be anchored to a seven-year timeframe (paragraph 40, CP 335).

3.4 We agree that, where a licensee has records to support a timeframe beyond seven years, the review period for remediation should not be cut off at the seven-year point by default, but should be consistent with the overarching principle being to return consumers, as closely as possible, to the position they would have otherwise been in. This is consistent with the licensees' general obligations, and resonates with the various guidelines included in the recent practical field guide released by ASIC titled "Making it right: How to run a consumer-centred remediation".

3.5 However, we submit that the proposed text in its current form under Proposal C1 goes beyond the existing legal obligations of licensees. We highlight some key issues below:

(1) The first issue relates to the apparent inconsistency with licensees' document retention obligations. By way of example, section 286 of the Corporations Act places an obligation to retain financial records for seven years after the transactions covered by the records are completed. The proposal therefore goes beyond what is required by law, raising practical questions as to whether all licensees are now obligated or at least *expected* to keep records for as long as they could, noting that strict compliance with the legal provisions may still result in a Tier 2 breach given the broad reach extended by the current wording of Tier 2.

(2) The second issue relates to the apparent inconsistencies with consumers' rights in the context of limitation periods, with the proposal going beyond what licensees can legitimately rely on in terms of limitation periods. For example, the limitation period under section 14 of the *Limitation Act 1969* (NSW) is six years from the date on which the cause of action founded on contract or breach of statutory duty first accrues. Reliance on limitation periods in the context of remediation is discussed in the recent case of *Australian Securities and Investments Commission v Australia and New Zealand Banking Group Ltd (No 3)* [2020] FCA 1421. In finding that the licensee became aware from about 11 July 2011 of the risk that it was not contractually entitled to charge certain fees, Allsop CJ stated the following in relation to the decision of ANZ not to remediate earlier affected customers (2003-2007) at [67]:

> If 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, unless there were other circumstances which would make that conduct inappropriate; hence the legitimacy of the regulator confining the

> remediation contravention to the period from 11 July 2005 and not August 2003, when the conduct actually began…

(3) Related to this issue is the potential inconsistencies with the Hayne Act. The Hayne Act amends the Corporations Act to include an obligation to remediate consumers where there are reasonable grounds to believe the affected consumer has a "legally enforceable right to recover the loss or damage" from the licensee (s912EB(8)). The Explanatory Memorandum to the bill explains that:

> [a] client 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. However affected clients may still have rights that they are able to pursue through internal dispute resolution and through AFCA. Licensees should take this into account in determining whether they should extend the breadth of their remediation consistent with ASIC's regulatory guidance.

3.6 Additionally, it is our submission that further guidance is desirable where the wording "reasonably suspects" will be adopted in the updated RG 256. Considering the structure of financial institutions and, in particular, where institutions often adopt the model of distributing decision making power across the business, the current use of "reasonable suspicion" as a threshold may raise practical implementation issues as reasonable minds may differ as to when this threshold is met even within the same organisation.

4 Using beneficial assumptions (Section D, CP 335)

4.1 With respect to beneficial assumptions, we agree that the use of appropriate assumptions can generally lead to good consumer outcomes and save licensees a considerable amount of time and resources (paragraph 46, CCP 335). We also agree that:

(1) there is a need to provide guidance for licensees that can be applied to a variety of remediation programs regarding when and how to use these assumptions in a way that leads to fair and efficient outcomes (paragraph 47, CCP 335); and

(2) the application of beneficial assumptions needs to be evidence-based, well documented and monitored to ensure that it continues to achieve the overarching goal (i.e. to return all affected consumers as closely as possible to the position they would have otherwise been in) (paragraph 48, CCP 335).

4.2 We consider that it is desirable for licensees to be able to achieve a level of consistency in their application of beneficial assumptions to a range of remediation programs.

4.3 However, we submit that this section provides overly detailed guidance on what a licensee needs to factor into consideration when deciding whether they are justified to rely on beneficial assumptions, which potentially places too high a threshold for licensees to meet. This is especially the case where the remediation is small-scaled and/or the remediation amounts are relatively small. In those circumstances, it may well be the case that proceeding without beneficial assumptions is more time and cost effective. The current proposed guidance may potentially reduce the number of remediation programs that seek to apply these assumptions given the vast array of issues they need to first take into account.

4.4 By way of illustration, the proposed guidance in CCP 335 contains the following considerations that should be taken into account including:

(1) Whether the assumption aims to meet the overarching goal (paragraph 48(a));

(2) Whether it is evidence-based and well documented (paragraph 48(b));

(3) Whether it is monitored to ensure that it continues to achieve the overarching goal throughout the remediation (paragraph 48(c));

(4) The nature of distribution of losses caused and whether an averaging approach works (paragraph 50);

(5) In the context of scoping assumptions, whether the assumptions widen the net to capture more consumers than less (paragraph 52);

(6) In the context of refund assumptions, whether they err on the side of overcompensation and whether they are used to justify limiting or preventing consumers from exercising their rights with respect to internal dispute resolution systems or lodging complaints with the Australian Financial Complaints Authority (paragraph 53);

(7) In the context of applying beneficial assumptions to account for absent records, whether data may be sourced from across the organisation or from service providers, what the data could indicate about the consumers, and how it may inform assumptions (paragraphs 61-62); and

(8) In the context of applying beneficial assumptions to increase efficiency, whether the remediation is properly resourced (paragraph 54), and whether the assumptions are applied in a way to benefit them commercially rather than the consumer (for instances, not giving due weight to the impact of the licensees' conduct) (paragraph 70).

4.5 Further, although ASIC's proposed guidance is detailed, given the variability in remediation, the current guidance is unlikely to be able to "cover the field" in terms of circumstances when assumptions may be appropriate. Accordingly, licensees will still be required to make judgments about when and how to use assumptions, in line with their existing obligations and the overarching goal to return all affected consumers as closely as possible to the position they would have otherwise been in.

4.6 Additionally, it is unclear if it is ASIC's intention under Proposals D2 and D3 to require all licensees to go through the process of considering whether or not to use beneficial assumptions, regardless of size and complexity, and potentially be able to justify why no beneficial assumptions were used. Proposal D2 states that "[w]e propose that licensees *should* apply beneficial assumptions if they need to make up for absent records…" (emphasis added) while Proposal D3 states that "[w]e propose that in certain circumstances it *may be appropriate* to use beneficial assumptions to increase the efficiency of a remediation" (emphasis added). The guidelines are unclear as to whether considering the use of beneficial assumptions is a default position such that licensees who determine not to do so would have to be able to justify why they have not.

4.7 For the reasons above, we are of the view that the guidance in its current form may not be necessary or desirable. While we agree that all assumptions for any remediation program should be carefully thought through and monitored as the program proceeds and amended as needed (for instance, in response to consumer feedback or complaints), it may be preferable from a practical perspective for ASIC to keep the guidelines high level and principles based and, upon engaging with the individual licensees for specific remediation programs, object or provide no objection to the use of beneficial assumptions.

5 Settlement deeds (Section H, CP 335)

5.1 Regarding the proposed clarification around the use of settlement deeds, we urge ASIC to consider any potential unintended consequences for licensees, in particular, in the context of insurance payouts.

5.2 We note that it is common practice of insurers to require from the insured licensees executed settlement deeds when considering whether it is entitled to a payout.

6 Other issues

6.1 We set out below for ASIC's consideration other issues that it may wish to consider when formulating the updated RG 256.

6.2 We note there are instances where the remediation methodology or rules have had to change to become more streamlined towards the latter part of a project for consumers whose files do not seem to be materially different from the previous cohort of customers in terms of data availability and/or consumer circumstances. This appears to be mainly driven by the need to increase output.

6.3 We submit that this is likely to result in inconsistency with respect to the treatment of customers and potentially raises issues of unfairness. We are supportive that a licensee's methodology should be finalised at the start of any remediation program, and for the fine tuning of rules to only occur where it does not result in unfairness or inconsistency. As licensees continue to gain more experience in remediation, it can be expected that different business units or programs will share their learnings and try to maintain consistency.

6.4 Accordingly, we submit that it might be worthwhile for ASIC's updated guideline to provide some clarity around the expectation of consistency *within* a program, as well as consistency across the licensee. A suggested approach might be to require senior members of the program to consider and assess the impact of potential inconsistent treatment when material rule changes are proposed (and not over-emphasise the time saving element of that rule change), and document any reasons for proceeding despite potential or apparent inconsistency.

We are happy to discuss any of our comments above if that would be of assistance.

Yours faithfully

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