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Executive General Manager Jurisdiction
Australian Financial Complaints Authority
GPO Box 3
Melbourne VIC 3001
Email: consultation@afca.org.au

Dear Sir or Madam,

We refer to the AFCA Rules and Operational Guidelines - Proposed Amendments - Consultation Paper dated March 2023.

This is our submission in respect of the Proposals by AFCA.

Proposal 1 – paid representatives

This proposed new rule is not appropriately drafted.

Where a paid representative behaves badly, the period for which they may be prevented from representing clients should be substantially longer than a maximum of 12 months. Financial planners can be banned permanently from the industry – badly behaved paid representatives should be prevented from representing clients in AFCA for periods ranging from 12 months to permanently, depending on how bad their conduct is. For example, we submit that what is effectively a 12-month "suspension" which (in AFCA's words in the Consultation Paper) could allow the paid representative to "put in place processes, resources or training" is not an appropriate response to a person that has a record of intentionally misleading or engaging in intentional deceptive conduct towards AFCA or other parties to the dispute.

Where paid representatives operate on a success fee basis, they should need to declare that in writing to AFCA, and that information be shared with the financial firm, before they take any action for a client. There should also be a requirement that written disclosure of the fee arrangements and the client's signed consent to the fees be obtained and provided to AFCA. The potential for conflicts of interest by solicitors as a result of success fees is well known, and that conflict clearly applies even more so to paid representatives who operate on a success fee basis in respect of AFCA complaints. This is because all solicitors in Australia are subject to strict professional standards and conduct obligations – including the requirement for full disclosure of and written consent to solicitor's fees. There is nothing similar in respect of paid representatives.

Our society creates rule-based frameworks to protect potentially unskilled people when they are arguably most vulnerable. This would typically be the case with respect to complainants appearing before AFCA. These may be persons who may have already faced the trauma of

substantial financial losses and now must navigate a dispute resolution process where unregulated persons are seeking to extract fees from them (in many cases at percentage rates far in excess of the fees charged by the financial advisers against whom they are complaining).

It may be possible that AFCA does not see this as its responsibility. If that is the case, it is incorrect and inappropriate. AFCA has created a jurisdiction in which untrained and unregulated individuals can enter into contractual arrangements with unregulated disclosure obligations, unregulated fee levels and no set framework to ensure that clients can seek redress for poor service or conduct with no guarantee that these persons carry appropriate professional indemnity insurance.

AFCA's obligations in this area should derive from the fact that AFCA has created the dispute resolution scheme that permits these untrained and unregulated individuals to "access" and potentially prey on naive and vulnerable consumers.

The courts and legal practice boards in the jurisdictions protect the naive and vulnerable by regulating advocates that appear before them. To the fullest extent possible, AFCA should apply broadly similar standards to protect those persons that seek to rely on AFCA to assist them in their vulnerable state.

One way in which this could be done is for AFCA to exclude a paid representative where that paid representative operates in a jurisdiction where it is against the law for such a person to provide legal services for reward. The work undertaken representing a client in AFCA is fundamentally legal work. Being a solicitor brings with it important protections for clients, including maintaining a trust account and being required to hold professional indemnity insurance. There are currently paid representatives who are managing claims totalling millions of dollars, and yet these people have no appropriate qualifications, no requirement for professional indemnity insurance, and no mandatory professional standards.

Finally, it should not be AFCA's discretion to exclude paid representatives who are either operating illegally or behaving badly – AFCA should be required to exclude those paid representatives.

(AFCA has for example had the discretion to exclude wholesale clients from AFCA for many years, but in our experience has so infrequently exercised that discretion that having a discretion is not helpful to financial firms. For this reason, it is a recurring theme in this submission that AFCA should have fewer discretions and more mandatory requirements.)

Proposal 2 – discretion for AFCA to exclude complaints where the complainant is acting inappropriately

This proposed new rule is not appropriately drafted.

Again, this should not be a discretion but should be a requirement. Access to AFCA confers an enormous benefit to the complainant. It is a jurisdiction that does not impose costs on complainants and instead imposes all of those costs on the financial firm whether or not the financial firm is at fault. It also disposes of various strict rules of evidence to make the process more complainant friendly. In effect, it comes at a substantial cost for both the financial firm and often the authorised representative. The very least that should be expected from the complainant is appropriate behaviour.

Further, while the concept of protection for AFCA's staff has merit, this protection should be extended to also protect the staff of the financial firm. Those staff should not be subject to bullying, harassment, discrimination or intimidation by a complainant.

Where a complainant is acting inappropriately, they should be warned once about this in writing. If they continue to so behave, their complaint should be excluded from AFCA.

Proposal 3 – discretion for AFCA to exclude a complaint where there has been no loss

This proposed new rule is not appropriately drafted.

This should not be a discretion but should be a requirement. Where the Complainant has suffered no loss, the financial firm should not be required to continue incurring costs, time and stress dealing with a complaint.

Proposal 4 – discretion for AFCA to exclude a complaint where the complaint has been the subject of a full and final settlement between the parties

This proposed new rule is not appropriately drafted.

Again, this should not be a discretion but a requirement. Where the matter has previously been settled, the financial firm should not be required to continue incurring costs, time and stress dealing with a complaint, (unless that settlement was achieved by fraud, misleading conduct, duress or unconscionable conduct).

Proposal 5 – discretion to exclude complaints by non-retail clients

This proposed new rule is not appropriately drafted.

We have provided more detail on this more complex issue in Appendix A. In summary, all non-retail clients should be excluded from AFCA (a requirement and not a discretion), and the financial firm should not be penalised when other entities (for example, qualified accountants issuing accountant certificates) have caused a misclassification.

Proposal 6 – forward looking review

We make no comment about this Proposal.

It is our view generally that there should be a broader ability for a financial firm to seek review from the traditional courts of AFCA determinations over a certain monetary limit (perhaps the monetary limit used for the compensation scheme of last resort would be a suitable amount).

Proposal 7 – effect of determinations

We make no comment about the actual wording of this Proposal.

Otherwise, we repeat our comment in respect of Proposal 6.

Proposal 8 – the slip rule

This proposed rule is appropriately drafted.

Otherwise, we repeat our comment in respect of Proposal 6.

Proposal 9 – consistency of language about AFCA's limits

We make no comment about this Proposal.

Proposal 10 – clarifying the objection process for rule A.8.3

Based on the information we have, this proposed new rule is not appropriately drafted. It is not clear why the financial firm should be denied the ability to make a submission in respect of an objection. For example, it may be acceptable that the financial firm is not entitled to obtain confidential information about the terms of the paid representative's retainer for privacy or commercial confidentiality reasons. However, the financial firm may typically have had considerable direct contact with the paid representative and may be directly aware of the paid representative's conduct that is relevant to the decision to exclude the paid representative. In that context, the ability of the financial firm to share that information as part of an objective process of determining whether the paid representative should be excluded, is not only relevant but necessary for fairness. The financial firm would share that information by way of the ability to make formal submissions.

In a system that prides itself on transparency and the ability of relevant parties to be heard, this proposed rule is not only inappropriate but also perverse.

This position equally applies to a complainant who is objecting to their exclusion from the system because of their adverse conduct. Again, it is appropriate that adverse conduct against the financial firm's staff should also form the basis of a decision to exclude the relevant complainant. In that context, if that complainant objects, in the name of fairness, transparency and the right of all relevant parties to be heard, this proposed rule is not only inappropriate but also perverse.

Proposal 11 – banking and finance panels

We make no comment about this Proposal.

Proposal 12 – definition changes

This proposed rule is appropriately drafted.

Proposal 13 – annual reporting

We would support a situation where AFCA is required to report on how frequently it exercises its discretions. The Proposals referred to in this submission show that AFCA has many important discretions. Yet it remains unknown as to how often AFCA exercises those discretions, and in whose favour the discretions are exercised. Our experience is that AFCA rarely exercises its discretion to exclude complaints by wholesale clients. It would be helpful to have statistics on the exercise of particular discretions, in the interests of transparency and fairness.

Yours sincerely

Fiona Halsey
Director

Mark Halsey
Counsel

APPENDIX A

Background

Chapter 7 of the Corporations Act 2001 (Cth) has various definitions for persons who do not fall within the definition of retail clients (section 761G(4)). The term wholesale clients encompass all clients that are not retail clients. The greatest number by far of people who are classified as wholesale are so classified because of an accountant's certificate. Two smaller categories of wholesale clients are professional investors and sophisticated investors. The expression professional investors generally refer to professionals, financial services businesses, and investors who control at least $10 million. Sophisticated investors are in general terms people with enough experience with relevant financial products and services so it is thought they can look after themselves.

The intention regarding the compulsory financial services alternative dispute resolution schemes was always that retail clients could access AFCA. This proposition is clearly evidenced by the fact that applicants for financial services licences that deal with and service wholesale clients exclusively are not required to become AFCA members.

Licensees that service both retail and wholesale clients are required to be AFCA members. When these licensees join AFCA (and its predecessors FICS and FOS) they are and were required to comply with the mandatory FICS/FOS/AFCA Rules. The complexity of the provisions of the Corporations Act has meant that the Rules are not consistent with the legislative framework as it applied to the distinction between retail and wholesale clients. This has perverse consequences. For example, a wholesale client that is serviced by a licensee that has authorisations to service wholesale clients only, cannot access AFCA because the licensee is not a member of AFCA. However, a wholesale client that is serviced by a licensee that has authorisations to service both wholesale and retail clients can access AFCA.

AFCA has the discretion to exclude wholesale investors but rarely exercises this discretion. Where a financial firm is a member of AFCA, AFCA will very likely hear a complaint from a wholesale client of that financial firm.

Being a member of AFCA means that a client can make a complaint to AFCA, and all of the costs of that complaint will be paid for by the financial firm. There is no risk or cost to the complainant client. A complaint can easily cost a financial firm $20,000 - $50,000 in AFCA and legal fees. These are the direct costs. There are also major indirect costs. Substantial staff and proprietor time are almost always lost dealing with AFCA complaints. Professional indemnity insurance premiums increase. There is an effect on the morale of the proprietor and the staff involved. All of these are incurred whether the complaint is worthy or not. If the complaint is not worthy, there is no compensation for the financial firm, and there are no consequences for the complainant. The complainant can choose whether or not to accept an AFCA Determination. The financial firm has no such choice and has no ability to appeal an AFCA Determination. A complainant can fail in AFCA, having caused substantial financial and other costs to the financial firm, and then proceed to a regular court.

It is an unlevel playing field.

Some of that can be justified when there is a power imbalance between a retail client and a financial firm. It cannot be justified when the dispute is between a financial firm and a wholesale client. The vast bulk of AFCA members who are financial advisers are small businesses. They are mum-and-dad businesses, and the proprietors and staff work hard every day to stay in business.

Even the large businesses which are members of AFCA will often seek indemnity from an individual adviser of the amounts awarded by AFCA, or at the very least, the excess from the professional indemnity insurance policy.

The assets of wholesale clients are often greater than the assets of the financial firm, or the authorised representative who will frequently be required to indemnify the financial firm.

The financial firm and the authorised representatives are real people, and they should not have to pay the costs of access to AFCA by wholesale investors.

Proposed wording of Proposal 5 does not require AFCA to exclude wholesale investors

The proposed wording of Proposal 5 will not require AFCA to exclude wholesale clients, sophisticated investors or professional investors.

Proposed wording of Proposal 5 would mean blame is wrongly placed on the financial firm where a client has been incorrectly classified due to an incorrect accountant's certificate

As set out above, there are 3 ways that a client can be classified as not being a retail client (i.e., wholesale, sophisticated or professional.)

The clear intention of the legislation (Section 761G(7)(c) of the Corporations Act 2001 (Cth)) is that a financial firm should be able to rely on a certificate issued by an accountant. It is not the financial firm that makes the important decisions as to whether the client has net assets of $2.5 million, or gross income in each of the last 2 years of $250,000. It is the accountant.

Proposal 5 however will have the effect that where the client has been incorrectly classified, even when this is not the result of any failure by the financial firm, the client should still be able to access AFCA. When we say this, it's important to remember that most of these financial firms are small businesses. The costs imposed on these small businesses through the AFCA process are real costs, both in money, time and stress. This means that the financial firm will be penalised for the errors of others. A financial firm should be able to rely upon an accountant's certificate.

Government response supports the exclusion of wholesale clients, sophisticated investors and professional investors

We note from the Government Response to The Review of the Australian Financial Complaints Authority dated November 2021, the government believes that non-retail clients (including wholesale clients) should be excluded. This is clear by the references to the certificate from a qualified accountant. The government clearly believes that where a certificate has been provided by a qualified accountant the client should be excluded from AFCA.

Access to the courts

If a person does not have access to AFCA, they are not without redress. Virtually all complaints regarding professional negligence are made through the courts. For example, where an accountant, an architect, a surveyor or a doctor makes an error to the disadvantage of a client, the client may take action through the courts. The courts are a fair system, where the rights of both plaintiff and defendant are protected through a system developed over hundreds of years. All Australians have access to the courts. Wholesale

clients, sophisticated investors and professional investors should use that system, where the rights of the plaintiff and defendant are balanced, and each side bears the costs and consequences of their actions.

Conclusion

The ability of clients to access AFCA gives them access to a forum heavily weighted against the financial service provider as all costs of the process are borne by the financial firm. There is no disincentive of any kind for a client to make a complaint to AFCA. Because of this, it is appropriate that access to AFCA should be limited to retail clients which was always the government's intention since it has never been mandatory for licensees whose ASIC-issued authorisations provide that they service wholesale clients only to become AFCA members. People who are not retail clients have access to the courts.

In place of the wording in AFCA Proposal 5, I recommend the following

"AFCA should exclude complaints from persons who are not retail clients unless there is evidence that they have been incorrectly classified as a result of actions by the financial firm."