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19 May 2023

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

Dear Sir or Madam,

Next Level Corporate P/l (AFSL 223191) submission in relation to Proposal 5 of AFCA Rules and Operational Guidelines

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

1. 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)).

These, by default, are wholesale clients that have sufficient expertise and wherewithal to look after themselves.

We note that since the AFSL rules have been in place, financial services licensees that provide financial product advice to and/or deal with wholesale clients only, have not been required to join an external dispute resolution scheme, nor more recently, become AFCA members.

This is consistent with their clients not being retail clients and therefore not requiring the protections afforded to retail clients.

The clear intention regarding the compulsory financial services alternative dispute resolution schemes was always that retail clients could access them and that wholesale clients (i.e., clients that are not retail clients), could not.

2. Conflicts and perverse outcomes

However, licensees that service both retail and wholesale clients are required to be AFCA members and to comply with the mandatory FICS/FOS/AFCA Rules.

And because the Rules are not consistent with the complex provisions of the Corporations Act (as they apply 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.

Whereas a wholesale client that is serviced by a licensee that has authorisations to service both wholesale and retail clients can access AFCA.

Additionally, AFCA has the discretion to exclude wholesale investors but as we understand it, rarely exercises this discretion and where a financial firm is a member of AFCA, AFCA will very likely hear a complaint from a wholesale client of that financial firm.

There are a number of issues that arise from these outcomes (which appear to be inconsistent with the legislative intention) and lead to an unlevel playing field.

For example, 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 (e.g., $20,000- $50,000 in AFCA and legal fees plus management time and PI deductibles).

There is no risk or cost to the complainant client, and this can easily lead to an unfair burden being placed on a financial firm and sophisticated parties seeking to 'game' the system.

All of these costs 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.

On top of that, the complainant can choose whether or not to accept an AFCA Determination whereas the financial firm has no such choice and has no ability to appeal an AFCA Determination.

Worse still, a complainant can fail in AFCA, having caused substantial financial and other costs to the financial firm, and then proceed to a regular court.

This creates 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.

In short, the financial firm and its authorised representatives are real people, seeking to provide honest and efficient advice and they should not have to pay the costs of access to AFCA by wholesale investors, nor be the innocent party that has to shoulder the cost of certain wholesale actors seeking to 'game' the system.

3. Proposal 5- proposed wording 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.

This means the current Proposal 5 will mean that blame is wrongly placed on the financial firm where a client has been incorrectly classified, perhaps due to an incorrect accountant's certificate.

However, 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 ASIC that nominated 'accountants' to be the single source of truth via their sign-off.

As a result, 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. This means the financial firm can be (severely) penalised for the errors of others.

Put simply, given the law, a financial firm should be able to rely upon an accountant's certificate because the accountant is deemed by ASIC to be the single source of truth in relation to this class of wholesale client.

4. 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.

5. Access to the courts

If a client does not have access to AFCA, they are not without redress.

Virtually all complaints regarding professional negligence are made through the courts or settled out of court.

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 court system is 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.

6. Conclusion

The ability of clients to access AFCA gives them access to a forum heavily weighted against the financial services provider because amongst other things, 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, and to ensure wholesale clients do not seek to 'game' the system, it is appropriate that access to AFCA should be limited to retail clients.

Clearly this was and is the government's intention since it has never been mandatory for licensees whose ASIC-issued authorisations provide that they service wholesale clients only, to join an independent dispute resolution scheme and/or to become AFCA members.

Clients that are not retail clients have access to the courts and often specialist legal representation.

In place of the wording in AFCA Proposal 5, NextLevelCorporate recommends 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 wholesale client as a direct result of actions by the financial firm."

Yours sincerely

Michael Ganon, Managing Director

Next Level Corporate P/L