



Investment & Financial Services Association Ltd

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Committee Secretary
Senate Standing Committee on Economics
PO Box 6100
Parliament House
Canberra ACT 2600
Australia

Email: economics.sen@aph.gov.au

Dear Sir/Madam

Re: Inquiry into the Trade Practices Amendment (Australian Consumer Law) Bill 2009

We refer to the Senate Inquiry into the *Trade Practices Amendment (Australian Consumer Law) Bill 2009*. We note that the Bill is a first step towards the Council of Australian Governments' goal of replacing state-based legislation with a national consumer law. IFSA welcomes the opportunity to provide comments on the Bill.

By way of background, the Investment and Financial Services Association (**IFSA**) is a national not-for-profit organisation which represents the retail and wholesale funds management, superannuation and life insurance industries. IFSA has over 145 members who are responsible for investing over \$1 trillion on behalf of more than ten million Australians. Members' compliance with IFSA Standards and Guidance Notes ensures the promotion of industry best practice.

IFSA members support COAG's proposal for the inclusion as part of the new consumer policy framework, the introduction of national unfair contract terms law. Members are, however, concerned that the broad scope of the proposed new law will undermine arrangements in the already highly regulated funds management, superannuation and life insurance industries. We note, in particular, the fiduciary and common law obligations on superannuation and managed investment scheme trustees and the statutory obligations on life insurance companies to prefer the interests of policy owners to that of their shareholders.

We make the following comments in relation to the scope and operation of the proposed unfair contract terms.

1. SCOPE

The proposal is expressed to apply to **unfair terms of standard form contracts**. It is intended that Australian Consumer Laws (**ACL**) be implemented as an applied laws regime and for the Commonwealth to include provisions in the Trade Practices Act and the *Australian Securities and Investments Commission Act 2001* (**ASIC Act**). It is noted that the provisions are intended to apply to a standard form contract that is a financial product or for a financial service.

The limited focus on unfair contract terms and the broad scope of the proposal will introduce a significant element of uncertainty in commercial dealings in this financial product and services sector. Introducing these requirements into the *Australian Securities and Investments Commission Act 2001* (**ASIC Act**) will not remove issues and uncertainty created by an overlap of concepts fundamental to the design for the offer of financial products and services under the Corporations Act.

The ACL proposal gives rise to issues reminiscent of those resulting from the overlap which previously existed between the operation of Part V of the Trade Practices Act and the Corporations Law. The rationale for removal of the overlap was set out in the September 1996 Report of the Corporations Law Simplification Task Force - *Section 52 Trade Practices Act and Dealings in Securities*. The Task Force observed that:

In 1992, the Prospectus Law Reform Subcommittee of the Companies and Securities Advisory Committee reported that this overlap created uncertainty and that this was detrimental to the efficient operation of the capital markets⁽³⁾. The Subcommittee report recommended that the Corporations Law rules on prospectuses should prevail over section 52 where there was an overlap.

Additionally, the Task Force recommended “that conduct in relation to fundraising, takeovers and other dealings in securities be governed by the Corporations Law and not by the provisions in Part V of the Trade Practices Act (which include section 52), **nor by the equivalent provisions in the Fair Trading Acts of each State and Territory.**” The Executive Summary of that Report is attached (Attachment A).

IFSA submits that the scope of the proposal should be modified. It is our recommendation that

- (1) clause 5 of the exposure draft which excludes certain terms in a standard form contract should be expanded beyond the use of certain terms to exclude specified types of documents. They would include, but should not be limited to, a standard form document:
 - (i) that is required by law to be provided to a consumer/investor in relation to the provision of a financial product or service; and
 - (ii) the content of which is prescribed by law; and
 - (iii) that is subject to regulatory supervision under the relevant law; and
 - (iv) in respect of which the consumer/investor has statutory right of redress.

(2) that business to business negotiations should be excluded from the ACL.

The following comments provided by IFSA members identify in part the potential impact of the unfair contract term proposals.

2. APPLICATION TO FINANCIAL SERVICES

With the current extensive regulation of the financial services industry, it is submitted that additional regulation via the ACL is unwarranted and in fact creates an additional burden that stymies the ability of organisations to provide products and services in a competitive environment. Below are some examples of how the ACL will, in some cases in an unintended fashion, adversely impact financial services providers without any additional benefit to investors using such services.

2.1 Financial services and investing in managed schemes

In signing an application form, an investor in a managed scheme generally makes certain declarations, including to be bound by the terms and conditions of the product disclosure statement and the managed investment scheme (**Scheme**) constitution. If investments in a scheme or trust are not specifically excluded from the ACL and are considered to be of a contractual nature (noting that the constitution is legally enforceable between the RE and the members - s. 601GB of the Act), given all investors will complete the application form attached to the current Product Disclosure Statement (**PDS**), one can assume that such investments are on the basis of a 'standard form contract', and therefore fall within the ambit of the regime.

2.2 Fees charged

The Consultation paper at page 16 (under the 'Upfront Price') notes that the, "[D]efinition makes it clear that the upfront price covers...an interest rate for credit..." Draft subsection 12BI (3) provides, "To avoid doubt, if a standard form contract...is a contract under which credit is provided...this...includes the total amount of principal that is owed under the contract." We would suggest, for the avoidance of doubt, that this be amended to note that it includes the total amount of principal and interest that is owed under the contract.

A PDS will disclose the range of fees applicable to a scheme (e.g. entry, exit, ongoing management, performance etc) which will be based on the terms of the constitution. Often in practice, the actual fee disclosed in the PDS and charged will be less than the maximum allowable under the constitution. In such a case, the RE has the discretion to increase the fees within the amount allowable under the terms of the constitution on any notice period (including no notice) it decides. However, such increases are contingent on the occurrence of particular events (the management, investment performance, and the investor's ultimate exit), thus possibly being subject to the ACL. If the RE uses this discretion to increase the ongoing management, performance and/or exit fees, and assuming the Schemes to be illiquid, investors will have no option but to remain in the investment and be subject to the higher fees. It is foreseeable that an argument could be made that the new regime will apply to this scenario. It is submitted that the application of the regime to such situations is an unintended consequence and is inappropriate in a sector subject to significant disclosure obligations such as Financial Services.

2.3 Constitution – General Discretions and Restrictions

The constitution for a Scheme established pursuant to Chapter 5C of the Corporations Act will generally provide a broad power on the RE to operate the Scheme, which is required to be exercised in the best interests of members, and members will often be restricted under the terms of the constitution from interfering with or questioning the rights, powers, authority, obligations or discretion of the RE. Once again, the RE requires these broad powers and restrictions in order to reasonably protect its (and thereby the members') legitimate interests, however if the exercise of discretion by the RE is detrimental to one or more particular investors, there is a risk that the terms in the constitution could be held to be void in relation to that one or more particular investors. Therefore, the RE's ability to act in the best interest of its members as a whole may be potentially jeopardised by allegations from one or more particular investors that its actions have been based on 'unfair' terms. This position is clearly untenable.

2.4 Constitution – Prospective Investors

The Corporations Act requires that the RE send a copy of the constitution for the Scheme in which a person is invested to members in prescribed circumstances (subsection 601GC (4)). The Act does not require that a copy of the constitution be provided to non-members. If the terms of the contract under which members make an investment in a scheme are located in the PDS and the constitution, but the constitution is not provided to the prospective investor, it is arguable that the terms found in the constitution are not 'transparent', as is required under the ACL. This potentially exposes the entire constitution to challenge.

3. BUSINESS TO BUSINESS

ACL covers all standard form contracts, including those negotiated between businesses, and operates regardless of the sophistication or size of the parties. It is submitted that business to business negotiations should be excluded from the ACL (or there should be some mechanism of assessment as to the sophistication or size of the parties; or alternatively an ability of the parties to 'opt out' of the requirements), as these parties often have the capacity to review, seek appropriate legal advice, and negotiate appropriate commercial outcomes.

To extend the scope of the ACL to all business transactions imposes an additional burden and unduly restricts commerce. For example, in relation to real property held by a scheme that a responsible entity (**RE**) manages, the RE holds the property on trust for the members of the scheme (being the beneficial owners of the freehold). When negotiating a lease with a commercial tenant, each party will have legal representation and be fully aware of their respective rights and obligations. The RE's standard form lease will have been drafted with a clear understanding of its fiduciary obligation to operate in the best interest of its members and necessarily must contain terms for the protection of these beneficial owners of the property. Application of the ACL to these arrangements may force REs to water down these protective terms or risk having entire clauses struck out as void, which may further expose REs to allegations by members that they have not acted in the members' best interests.

There is already a range of legislation already in place to protect tenants; adding to this via the ACL threatens the ability of REs to adequately protect its schemes'

members (to which it owes a fiduciary obligation) and to operate effectively in this capacity.

Further, there are numerous existing State and Commonwealth legislation that differentiate the rights of small and large businesses and also between retail and sophisticated investors. Such existing legislation can be drawn up in determining the appropriate application of the ACL in relation to business-to-business dealings.

We would be pleased to assist the Committee in its consideration of these matters and to provide any further information required.

Yours sincerely

A handwritten signature in black ink, appearing to read 'D O'Reilly', with a stylized flourish at the end.

David O'Reilly
Director – Policy and Regulations