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Financial Services Unit (CSU)
Financial System Division
The Treasury
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Via Email: ProductRegulation@treasury.gov.au

The Australian CFD & FX Forum ("CFD & FX Forum") response to the Proposals Paper regarding Design and Distribution Obligations and Product Intervention Power

1. Preamble

The CFD & FX Forum is pleased to provide comments on the Proposals Paper regarding Design and Distribution Obligations and Product Intervention Power.

The CFD & FX Forum and each of its members ("Members") are committed to enhancing the efficient operation, transparency and overall investor understanding and confidence in CFDs and FX within Australia, and in the Australian CFD and FX industry as a whole.

Representing 64%¹ of Australian CFD & FX providers by market share, the CFD & FX Forum has established Best Practice Standards ("Standards") for the purpose of continuously improving existing CFD and FX industry standards and addressing specific CFD and FX industry issues and investor concerns, building upon existing legislation to deliver additional benefits to investors and elevating investor perception and understanding in dealing in CFD and FX products.

The CFD & FX Forum considers the response to this paper as an opportunity to work with ASIC in implementing best practice across the wider industry.

2. Introduction

The CFD & FX Forum has the following comments to make regarding the proposals outlined within the paper. These comments are considered further below when addressing the questions posed by the paper.

- When defining distributors there needs to be further clarity regarding exactly what it means to 'advertise a product' and 'receive a benefit'. The definition appears to be broad and could define numerous entities as distributors unnecessarily;
- The suggested use of needs-based analysis when selling products may go beyond the scope of general advice;
- The frequency of any product reviews undertaken by issuers should be at the discretion of the issuers. This is due to the fact the proposals cover a wide range of products across the financial markets and some products will not need as much scrutiny as others;

¹ June 2016 Investment Trends Report

- The process for determining the scale of detriment to consumers is necessarily broad however further clarity should be given regarding this process in guidance notes. In particular, examples of metrics that could be used should be provided in guidance, such as percentage of total assets lost;
- We consider the duration for an intervention proposed in the paper to be excessive and concur with the view of the FSI;
- Product intervention powers, specifically the power to ban the distributing of a product should only be invoked by ASIC as a last resort. Before invoking any such powers, less restrictive measures should be considered and all supervisory and/or enforcement actions must be exhausted, thereby preventing the need to ban the distribution of the product by all product issuers. Additionally, there should be a full consultation with the impacted industry sector before banning the distribution of a product, with ASIC being required to provide a thorough justification of its actions based on quantifiable evidence and accurate assumptions about the knowledge and trading behaviour of Australian retail clients, in order to give the relevant industry sector an opportunity to challenge ASIC's decision. The consultation should be appropriately scaled to the level of detriment incurred by the consumers, e.g. for matters affecting consumers on a market-wide bases, consultation with the market as a whole should occur;
- In order to avoid the unintended consequence of Australian consumers moving their business to product distributors and issuers in offshore, unregulated jurisdictions, thereby losing the protections provided by ASIC and external dispute resolution bodies such as the Financial Ombudsman Service ("FOS"), any product design and distribution rules, and product intervention powers, must not be overly restrictive;
- The proposals should not inhibit consumer choice and stifle competition between product issuers. Such an outcome would inhibit the objective of promoting effective competition in the interests of consumers; and consideration should also be given to how other ongoing industry initiatives and regulatory changes (such as client money reform) would impact the degree of intervention required and the overall risk profile of the products and issuers in question.
- We view these proposals as an opportunity to work with ASIC in implementing industry best practice across the wider industry.

3. Responses to the Questions posed:

Question 1. Do you agree with all financial products except for ordinary shares being subject to both the design and distribution obligations and the product intervention power? Are there any financial products where the existing level of consumer protections means they should be excluded from the measures (for example, default (MySuper) or mass-customised (comprehensive income products for retirement) superannuation products)?

Yes, we agree with the proposal that all financial products except for ordinary shares should be subject to the design and distribution obligations.

We do not consider there to be any other products that should be excluded from the measures.

Question 2. Do you agree with the design and distribution obligations and the product intervention power only applying to products made available to retail clients? If not, please explain why with relevant examples.

Yes, we agree with the design and distribution obligations and the product intervention power only applying to products made available to retail clients.

Question 3. Do you agree that regulated credit products should be subject to the product intervention power but not the design and distribution obligations? If not, please explain why with relevant examples.

Yes, we agree that regulated credit products should be subject to the product intervention power but not the design and distribution obligations due to the potential regulatory overlap.

Question 4. Do you consider the product intervention power should be broader than regulated credit products? For example, 'credit facilities' covered by the unconscionable conduct provisions in the ASIC Act. If so, please explain why with relevant examples.

No, we do not consider it necessary for the product intervention power to be broader than regulated credit products.

Question 5. Do you agree with defining issuers as the entity that is responsible for the obligations owed under the terms of the facility that is the product? If not, please explain why with relevant examples. Are there any entities that you consider should be excluded from the definition of issuer?

Yes, we agree with the definition as it is proposed. We do not consider there to be any other entities that should be excluded.

Question 6. Do you agree with defining distributors as entity that arranges for the issue of a product or that: (i) advertise a product, publish a statement that is reasonable likely to induce people as retail clients to acquire the product or make available a product disclosure document for a product; and (ii) receive a benefit from the issuer of the product for engaging in the conduct referred to in (i) or for the issue of the product arising from that conduct (if the entity is not the issuer).

In general, we agree with the definition of distributors as it stands, particularly that it includes those that are actively inducing retail clients to acquire the products in question. However, we consider that further clarity should be provided on what it means to 'advertise a product' and 'receive a benefit'. As noted in the paper the definition is not intended to include media companies engaged to advertise products, which is consistent with other exclusions for media companies in the Corporations Act. We do not consider it necessary for the definition of 'Distributor' to include those that passively promote the product in question. An example of such passive advertising would be banner advertisements placed upon the websites of partner entities. These banner advertisements simply direct consumers to the website of the issuer and nothing else, but a fee is received depending upon how many consumers are redirected. We consider it to be onerous to impose the distributor obligations upon such entities that are passively advertising the products in question as opposed to those actively inducing clients to acquire the product. We consider banner advertisements on third party websites to fall into the exclusions noted in the Corporations Act.

Question 7. Are there any situations where an entity (other than the issuer) should be included in the definition of distributor if it engages in the conduct in limb (i) but does not receive a benefit from the issuer?

No.

Question 8. Do you agree with excluding personal financial product advisers from the obligations placed on distributors? If not, please explain why with relevant examples. Are there any other entities that you consider should be excluded from the definition of distributor?

Yes, we agree with the proposed exclusion.

Question 9. Do you agree with the obligations applying to both licensed and unlicensed product issuers and distributors? If they do apply to unlicensed issuers and distributors, are there any unlicensed entities that should be excluded from the obligations (for example, entities covered by the regulatory sandbox exemption)? Who should be empowered to grant exemptions and in what circumstances?

Yes, we agree with the proposed obligations applying to both licensed and unlicensed issuers and distributors. Any exemptions to this should be considered by ASIC who would then advise the relevant minister to grant exemptions from the provisions of the Corporations Act as necessary.

Question 10. Do you agree with the proposal that issuers should identify appropriate target and non-target markets for their products? What factors should issuers have regard to when determining target markets?

Yes, we agree that issuers should identify appropriate target and non-target markets for their products. For the products the CFD & FX Forum members provide the factors to be used when determining the target market would likely mirror those already used by member firms to assess client suitability during the on-boarding process. This includes using information such as experience, work status, wealth and income in determining whether the client is suitable to trade on the products available. It would be sensible to use those factors already in use to identify the target markets.

In addition, the paper considers a needs-based analysis when selling products, monitoring products to ensure they continue to meet the needs of consumers and identifying what the maximum percentage of the portfolio that should be invested in a product. The Forum considers consumers themselves to be in the best position to evaluate this and such a requirement for a needs-based analysis goes beyond the scope of general advice.

Question 11. For insurance products, do you agree the factors requiring consumers in the target market to benefit from the significant features of the product? What do you think are significant features for different product types (for example, general insurance versus life insurance)?

Yes, we agree with the proposal as it stands.

Question 12. Do you agree with the proposal that issuers should select distribution channels and marketing approaches for the product that are appropriate for the identified target market? If not, please explain why with relevant examples.

In principal we agree that issuers should select appropriate distribution channels for the target market. However, the Forum asserts that it is incorrect to assume “*Distribution channels whereby consumers can acquire the product without active engagement are also unlikely to be appropriate regardless of the target market.*” This does not take into consideration current requirements for client qualification, disclosure, risk management tools and other client suitability factors that occur during the onboarding process.

Question 13. Do you agree that issuers must have regard to the customers a distribution channel will reach, the risks associated with a distribution channel, steps to mitigate those risks and the complexity of the product when determining an appropriate target market? Are there any other factors that issuers should have regard to when determining appropriate distribution channels and market approach?

Yes, we agree that issuers should be aware of the customers a distribution channel will reach and the associated risks.

Question 14. Do you agree with the proposal that issuers must periodically review their products to ensure the identified target market and distribution channel continues to be appropriate and advise ASIC if the review identifies that a distributor is selling the product outside of the intended target market?

Yes, we agree that some form of periodic review should be conducted by issuers and any adverse findings reported to ASIC. However, the scope and frequency of the review should be determined by the issuer due to the large number of products that the proposed legislation will cover. The CFD & FX Forum offers products that rarely change, with distribution channels that also do not vary frequently. As such, we suggest that frequent reviews for the products we provide would be unnecessary and onerous.

Question 15. In relation to all the proposed issuer obligations, what level of detail should be prescribed in legislation versus being specified in ASIC guidance?

As noted in the response to question 14, given the wide range of products that the legislation will cover, we suggest that much of the detail should be provided in ASIC guidance rather than a prescriptive piece of legislation. Having such detail in the guidance will allow for differences across product types and also provide the scope for types of issuers to determine the most appropriate course of action that suits the products that they offer. The legislation should only detail the high level obligations and allow for the guidance to provide some flexibility regarding its implementation.

Question 16. Do you agree with the proposal that distributors must put in place reasonable controls to ensure that products are distributed in accordance with the issuer’s expectations?

Yes, we agree that distributors should have controls in place to ensure products are distributed in line with the issuer’s expectations.

Question 17. To what extent should consumer be able to access a product outside of the identified target market?

A consumer should be able to access any product, even if they are considered outside the target market, as a matter of choice. It should not be for distributors to decide if a consumer wants to use a particular product.

Question 18. What protections should there be for consumers who are aware they are outside the target market but choose to access a product regardless?

In spite of the consumer being able to exercise freedom of choice when accessing products there should be minimum standards in place to ensure consumers understand all features of the products. These are largely in place already with Product Disclosure Statements, Financial Services Guides and Statements of Advice. However, for certain types of product which are considered outside of the target market for the individual consumer, then additional disclosure should be given on the specifics of the product and personal advice must be provided regarding the nature of the product, which includes a clear explanation of why the consumer is outside of the target market and consequently the reasons why the product is not suitable.

Question 19. Do you agree with the proposal that distributors must comply with reasonable requests from the issuer related to the product review and put in place procedures to monitor the performance of products to support the review? Should an equivalent obligation also be imposed on advised distributors?

Yes, we agree that distributors should comply with requests from the issuer related to product review and this should form part of the agreement between the issuer and distributor.

Question 20. In relation to all the proposed distributor obligations, what level of detail should be prescribed in legislation versus being specified in ASIC guidance?

As noted in the response to question 15, given the wide range of products that the legislation will cover, we suggest that much of the detail should be provided in ASIC guidance rather than a prescriptive piece of legislation. Having such detail in the guidance will allow for differences across product types and also provide the scope for types of issuers to determine the most appropriate course of action that suits the products that they offer. The legislation should only detail the high level obligations and allow for the guidance to provide some flexibility regarding its implementation.

With specific regard to the relationship between issuers and distributors it may be reasonable to mandate specific minimum terms in the agreement between the two regarding the design and distribution obligations.

21. Do you agree with the obligations applying 6 months after the reforms receive Royal Assent for products that have not previously been made available to consumers? If not, please explain why with relevant examples.

Yes, we agree with the proposal.

22. Do you agree with the obligations applying to existing products in the market 2 years after the reforms receive Royal Assent? If not, please explain why with relevant examples and indicate what you consider to be a more appropriate transition period.

Yes, we agree with the proposal.

23. Do you agree that ASIC should be able to make interventions in relation to the product (or product feature), the types of consumers that can access a product or the circumstances in which a consumer can access the product? If not, please explain why with relevant examples.

In principal, we agree that ASIC should be able to make interventions in certain circumstances, in particular where the aim is to provide a consistent minimum standard regarding advertising and marketing of certain products. However, care should be taken when approaching how ASIC is able to execute such interventions. There is significant difference between ASIC imposing minimum risk warning standards on certain products and being able to ban an entire class of products. As such, careful consideration should be given to whether interventions should be graded on the scale of impact to the market and consequently, those ASIC interventions that may have a greater impact should be subject to some form of independent review prior to ASIC exercising such powers. Alternatively, the intervention should only be on an individual basis due to non-compliance with legislative requirements rather than an industry wide ban. Banning products is an unnecessarily blunt instrument that restricts consumer choice and such arrangements in other jurisdictions have seldom been used. Other jurisdictions support self-commitment rather than banning products, such as BaFin in Germany using ten principles to improve transparency and investor protection. In addition, it needs to be clear that any intervention will only apply to retail clients, as is the case with product design and distribution.

The Forum also considers that all actions should be proportionate. In many cases the issue resides with the provider of the product rather than the nature of the product itself. For example, the Forum makes up circa 64% of the Australian CFD retail market and ensures good standards, conduct and market practice by its members. Problems in the sector usually reside with other providers and not in the nature of the product itself.

The Forum is an example of how a self-regulatory body can lift the standards of the industry without regulatory intervention. Given self-regulatory bodies generally operate to standards above and beyond the relevant laws and regulations, with common aims such as promoting integrity, transparency, and best practice, it is our submission that ASIC should have regard to, and consult with, self-regulating bodies before invoking any product intervention powers.

Adopting alternative, less restrictive measures, would significantly help to improve transparency and investor protection, while avoiding the need for the creation of new market-wide product intervention powers, which may prove complicated to implement and lead to possible unintended consequences. For example, a market-wide ban on a particular product would likely lead to consumers taking their business to offshore, unregulated product issuers, thereby losing the protections afforded to them by ASIC and the access to external dispute resolution forums, such as FOS.

ASIC must be required to provide complete and thorough justification for their decision to ban a product, in order to give the industry sector an opportunity to respond. The scope of the consultation process should be proportionate to the scope of detriment incurred by consumers.

For example, for matters affecting consumers on a market-wide basis, consultation with the market as a whole should occur. In assessing whether a proposed intervention is proportionate to the level of consumer detriment, consideration should be given by ASIC to the scale of impact of the intervention to the market. We would suggest that those ASIC interventions that may have a greater impact should be subject to some form of independent review prior to ASIC exercising such powers. Moreover, before ASIC is able to invoke any product intervention powers, all supervisory and/or enforcement actions must be exhausted, thereby likely eliminating the need to ban all product issuers. Furthermore, while product intervention may be temporary, the impact on product issuers would likely be significant and in some cases irreversible.

24. Are there any other types of interventions ASIC should be able to make (for example, remuneration)?

ASIC may wish to consider increasing the level of regulatory capital required to be able to provide such products. This creates a higher barrier to entry and also encourages a higher standard of conduct given greater funds are at risk.

25. Do you agree that the extent of a consumer detriment being determined by reference to the scale of the detriment in the market, the potential scale of the detriment to individual consumers and the class of consumers impacted? Are there any other factors that should be taken into consideration?

Yes, we agree that the extent of consumer detriment can be determined by reference to the scale of detriment to the market, individual consumers and class of consumer. However, whilst this should form the basis for determining the extent of consumer detriment, and it should be flexible to cover all circumstances, some metrics should be identified and discussed in the guidance provided by ASIC on the subject. These may include percentage of income affected, number of consumers affected compared to the market as a whole, and whether detriment was caused by a specific product issuer or by a group of product issuers.

26. Do you agree with ASIC being required to undertake consultation and consider the use of alternative powers before making an intervention? Are there any other steps that should be incorporated?

Yes, we agree that ASIC should be required to undertake consultation prior to any intervention taking place. ASIC should also thoroughly review its alternative powers prior to making any intervention. ALL other supervisory or enforcement actions should be exhausted prior to an intervention occurring. As noted in the proposals paper, the level of consultation should be scaled dependent upon the nature of the intervention. Any intervention that is market wide and involving a class of product should be subject to industry consultation. When consulting ASIC should clearly outline the factors considered when proposing the intervention, the scale of detriment occurring, why alternative powers are not appropriate and also the nature of the intervention i.e. a full rationale for the decision needs to be provided.

27. Do you agree with ASIC being required to publish information on intervention, the consumer detriment and its consideration of alternative powers? Is there any other information that should be made available?

Yes, we agree that ASIC should be required to publish information on the intervention. The publication should be in a standardised format and include a minimum level of information for each intervention. As noted this should include information on the intervention, including entities affected and the duration of the intervention, the scale of consumer detriment and a clear explanation of what alternate powers were considered and why they were not appropriate. The publication should also detail the consultation that occurred prior to the intervention taking place.

28. Do you agree with interventions applying for an initial duration of up to 18 months with no ability for extensions? Would a different time frame be more appropriate? Please explain why.

No, we do not agree that the initial duration of an intervention apply for up to 18 months. We concur with the view of the FSI that 12 months is sufficient time for the relevant practices to be remediated. In circumstance where the intervention may result in legislated policy change, which we suggest would occur only in limited circumstances, this could be identified when the intervention is first made and the extended time period applied.

29. What arrangements should apply if an ASIC intervention is subject to administrative or judicial appeal? Should an appeal extend the duration that the Government has to make an intervention permanent?

If an ASIC intervention is subject to an administrative or judicial appeal then the intervention should cease until the appeal has been finalised. However, when an appeal is made this should also lead to an extension of the time the government have to make the intervention permanent. The extension should be equal to the duration of the appeal.

30. What mechanism should the Government use to make interventions permanent and should be mechanism differ depending on whether it is an individual or market wide intervention? What (if any) appeal mechanisms should apply to a Government decision to make an intervention permanent?

In the case of individual interventions, the Government could direct ASIC to use its powers to make the intervention permanent. Any such permanent intervention should be subject to appeal within the AAT. Permanent market wide interventions should be addressed through legislative change as it is likely that any such intervention which needs to be made permanent will involve policy change.

31. Are there any other mechanisms that could be implemented to provide certainty around the use of the product intervention power?

ASIC should thoroughly engage with affected parties prior to making an intervention, and allow time for remediation if possible. Where ASIC identifies an issue and exercises its product intervention powers, ASIC should also set a clear series of actions and timeframe which, if adhered to by the relevant market participants, will result in the lifting of the intervention.

32. Do you agree with the powers applying from the date of Royal Assent? If not, please explain why with relevant examples.

Yes, we agree with the powers applying from the date of Royal Assent.

33. What enforcement arrangement should apply in relation to a breach of the design and distribution obligations or the requirements in an intervention?

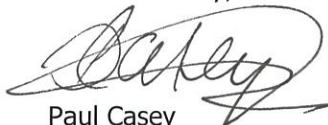
We consider a breach of the design and distribution obligations to be less significant than a breach of the requirements of an intervention. Consequently, only administrative actions should be used for breaches of the design and distribution obligations, whilst for breaches of the requirements of intervention injunctions, civil and criminal penalties should also be available.

34. What consumer rights and redress avenues should apply in relation to a breach of the design and distributions obligations or the requirements of an intervention?

We consider the current provisions available to protect and enforce consumer rights as detailed in the proposals paper to be sufficient when applied to breaches of the design and distribution obligations or the requirements of an intervention.

Please contact us for any further assistance.

Yours sincerely,



Paul Casey
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