



7 October 2022

Ms Mohita Zaheed
Financial System Division
Treasury
Langton Crescent
PARKES ACT 2600
Submitted via email to: FAR@treasury.gov.au

Dear Ms Zaheed,

Treasury Consultation - Financial Services Compensation Scheme of Last Resort

The Australian Finance Industry Association (AFIA)¹ appreciates the opportunity to respond to Treasury's consultation on the Financial Services Compensation Scheme of Last Resort (CSLR).²

AFIA is the only peak body representing the entire finance industry in Australia. We represent 158 members, including bank and non-bank lenders, neobanks, finance companies, fintechs, providers of vehicle and equipment finance, car rental and fleet providers, and service providers in the finance industry.

We are the voice for advancing a world-class finance industry, with our members who are at the forefront of innovation in consumer and business finance in Australia. Our members finance Australia's future.

We collaborate with our members, governments, regulators and customer representatives to promote competition and innovation, deliver better customer outcomes, and create a resilient, inclusive and sustainable future.

¹ www.afia.asn.au

² www.treasury.gov.au/consultation/c2022-311520

INTRODUCTORY COMMENTS

AFIA supports the introduction of a CSLR. We firmly believe customers who have received a determination from the Australian Financial Complaints Authority (AFCA), finding they are entitled to compensation under the scheme, should justly receive that compensation.³

We have strongly indicated our support for this policy in previous submissions on the matter.⁴

There are two sets of draft Regulations on which consultation is sought:

- The Financial Services Compensation Scheme of Last Resort Levy Regulations 2022 ([‘the CLSR Regulations’](#))
- The Corporations Amendment (Financial Services Compensation Scheme of Last Resort) Regulations 2022 ([‘the Corporations Regulations’](#)).

The CSLR will operate under three bills introduced to introduced by the Assistant Treasurer and Minister for Financial Services, Hon Stephen Jones MP, on 8 September 2022.⁵ These bills are:

- The Financial Services Compensation Scheme of Last Resort Levy Bill 2022 ([‘the CSLR Bill’](#))
- The Financial Services Compensation Scheme of Last Resort Levy (Collection) Bill 2022 ([‘the CLSR Collection Bill’](#))
- Schedule 3 of the Financial Sector Reform Bill 2022 ([‘the FSR Bill’](#)).

Our submission will refer to the bills as necessary to contextualise the scheme under which the Regulations operate.

AFIA welcomes the proposed CSLR insofar as it implements recommendation 7.1 the *Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* (‘the Royal Commission’).⁶

AFIA notes the proposed CLSR builds on the important work of the *Review of the financial system external dispute resolution and complaints framework*, chaired by Professor Ian Ramsay (‘the Ramsay Review’).⁷

We also applaud the fact that this legislation has been pursued in a spirit of bipartisan co-operation.

³ Explanatory Memorandum, Financial Sector Reform Bill 2022, 72[2.41].

⁴ Australian Finance Industry Association, *Submission to Treasury on Establishing a Compensation Scheme of Last Resort* (7 February 2020): [070220_AFIA_Submission- Treasury_CSLR- Submission.pdf](#).

⁵ Commonwealth Parliamentary Debates, House of Representatives, 8 September 2022, 5 (The Hon. Stephen Jones MP, Assistant Treasurer and Minister for Financial Services).

⁶ Commonwealth, Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, *Final Report* (4 February 2019) vol 1, 41 (‘Royal Commission Final Report’).

⁷ Supplementary Final Report of the Review of the financial system external dispute resolution and complaints framework (‘The Ramsay Review’).

AFIA is committed to ensuring all Australians have continued access to finance, while enhancements to consumer protections are made following the Royal Commission.

There are three core elements of the CSLR on which AFIA would like to comment, these are:

1. The eligibility criteria and \$150,000 cap on the CSLR⁸
2. The funding structure for the levy under the CSLR⁹
3. The purported cap on CSLR levies and how it can be waived by ministerial determination.¹⁰

Our specific comments on the details of the proposed CSLR are contained in **Attachment A**.

CLOSING COMMENTS

AFIA welcomes further dialogue on the CSLR legislation and the Regulations.

Should you wish to discuss our submission or require additional information, please contact Sebastian Reinehr, Senior Policy Adviser, at Sebastian.Reinehr@afia.asn.au or 0474 704 992.

Yours sincerely



Diane Tate
Chief Executive Officer

⁸ Explanatory Memorandum, Financial Sector Reform Bill 2022, 70[2.30] and at 72[2.44].

⁹ Explanatory Memorandum, Financial Sector Reform Bill 2022, 70[2.30], 81[2.108] and at 90[3.20].

¹⁰ CSLR Bill, clause 14(4) on individual sub-sectors and 15(5) on the whole scheme. See too CSLR Regulations section 14 and 15. respectively. See too Explanatory Statement, Financial Services Compensation Scheme of Last Resort Levy Regulations 2022, 3-4.

ATTACHMENT A: DETAILED COMMENTS ON THE CSLR LEGISLATION AND REGULATIONS

EXECUTIVE SUMMARY

AFIA will first outline and then comment upon the following aspects of the CSLR.

1. The eligibility criteria and \$150,000 cap¹¹
2. The funding structure for the levy¹²
3. The purported cap on CSLR levies and how it can be waived by ministerial determination.¹³

Part 1 - The eligibility criteria and cap appropriately limit on the CSLR

1.1 Outlining the proposed CSLR's limits

AFIA supports carefully defined eligibility criteria under the scheme, as suggested by the Ramsay Review, and advocated in our last submission on this matter.¹⁴

The FSR Bill inserts into the *Corporations Act 2001* ('the *Corporations Act*'), a new section 1064, limiting the conditions under which a consumer may access the CSLR.

To be eligible for the scheme, a consumer must meet **all** the following criteria:¹⁵

- They have received a relevant AFCA determination, requiring compensation
- The determination has not been paid after twelve months, or any longer period decided by AFCA
- AFCA has taken appropriate steps to require the amount to be paid and the determination remains unpaid
- The consumer is not eligible to receive payment under another statutory scheme
- The CSLR operator reasonably believes the relevant entity that is or was an AFCA member, having regard to their financial position, is unlikely to fully pay the amount.

¹¹ Explanatory Memorandum, Financial Sector Reform Bill 2022, 70[2.30] and at 72[2.44].

¹² Explanatory Memorandum, Financial Sector Reform Bill 2022, 70[2.30], 81[2.108] and at 90[3.20].

¹³ CSLR Bill, clause 14(4) on individual sub-sectors and 15(5) on the whole scheme. See too CSLR Regulations section 14 and 15 respectively. See too Explanatory Statement, Financial Services Compensation Scheme of Last Resort Levy Regulations 2022, 3-4.

¹⁴ Australian Finance Industry Association, *Submission to Treasury on Establishing a Compensation Scheme of Last Resort* (7 February 2020), 2: [070220_AFIA_Submission-_Treasury_CSLR-_Submission.pdf](#).

¹⁵ Explanatory Memorandum, Financial Sector Reform Bill 2022, 70[2.30].

Further, to be covered by the CSLR, the AFCA determination **must** relate to these products:¹⁶

- A 'credit activity' under the *National Consumer Credit Protection Act 2009* (NCCPP)¹⁷
- Certain personal financial advice
- Dealing in securities for a person as a retail client, other than issuing securities.

The maximum amount of compensation is also capped at \$150,000, under the proposed new section 1067 of the *Corporations Act* inserted by the FSR Bill.¹⁸

1.2 AFIA recommendations on the proposed CSLR's limits

AFIA supports these clearly defined eligibility criteria, and the \$150,000 cap on compensation.

However, Treasury should carefully consider the application of the scheme to AFCA members and credit products, as outlined above. Firstly, this may deter uptake of voluntary AFCA membership where it is not a legal requirement.¹⁹ Secondly, Treasury should remain cognisant that credit providers are only responsible for 11% of unpaid AFCA determinations, compared with 53% relating to financial planners and advisers.²⁰

Part 2 - Funding of the CSLR and levy caps

2.1 The proposed funding arrangements

It is proposed the scheme will be funded in the following way:

- Outstanding AFCA unpaid AFCA determinations accrued before the day the CSLR bills were introduced to the House of Representatives, will be funded by a 'one-off levy' on the 'top ten banking and insurance groups in Australia'.²¹ The process for this is outlined in clause 16(1) of the CSLR Bill and section 18 of the Regulations²²
- The Commonwealth will fund the CSLR for the 'first levy period'.²³ The first levy period is financial year 2023/24²⁴
- From financial year 2024/25 onwards, the CSLR levy will be funded in accordance with the formula in section 11 of the CSLR Regulations, as provided for under clause 12(1) of the CSLR Bill.²⁵

¹⁶ Explanatory Memorandum, Financial Sector Reform Bill 2022, 70[2.30], 71[2.36].

¹⁷ Ibid. See too section 6 of the *National Consumer Credit Protection Act 2009*, which defines 'credit activity'.

¹⁸ Ibid, 72[2.44].

¹⁹ Australian Finance Industry Association, *Submission to Treasury on Establishing a Compensation Scheme of Last Resort* (7 February 2020), 2: [070220_AFIA_Submission_-_Treasury_CSLR_-_Submission.pdf](#).

²⁰ Australian Securities and Investments Commission (ASIC), *ASIC's Response to the Supplementary Issues Paper of the Ramsay Review*, 7[20]: [ASIC - Submission to the EDR Review Supplementary Issues Paper \(treasury.gov.au\)](#).

²¹ Explanatory Memorandum, Financial Sector Reform Bill 2022, 70[2.30].

²² See too *ibid*, 98[3.57].

²³ *Ibid*, 81[2.108].

²⁴ As defined under section 9 of the CSLR Bill.

²⁵ Explanatory Memorandum, Financial Sector Reform Bill 2022, 90[3.20].

The relevant formula for calculating levies payable from 2024/25 onwards is:²⁶

$$\left[\text{Sub-sector costs} - \left(\frac{\text{Minimum levy component}}{\text{Sub-sector population}} \right) \right] \times \frac{\text{Graduated entity metric}}{\text{Sub-sector metric}}$$

The effect of this formula is that smaller financial institutions within a given sub-sector will be liable to pay smaller levies and larger financial institutions will be liable to pay larger levies.²⁷

AFIA supports this graduated approach.

Under clause 8 of the CSLR Bill and section 6 of the CSLR Regulations, financial institutions operating in the following sub-sectors are liable to pay the levy:

1. credit intermediaries
2. credit providers
3. licensees that provide personal advice on relevant financial products to retail clients
4. securities dealers.

AFIA supports the fact that this scheme does not apply to the deposit-taking activities of authorised deposit-taking institutions (ADIs), which are separately protected by the Financial Claims Scheme (FCS).²⁸

2.2 The purported levy caps for the CSLR

The CSLR Bill suggests levies charged in any single levy period are capped at:²⁹

- \$250 million for the whole CSLR³⁰
- \$20 million, or another amount as determined by the Regulations, for each sub-sector.³¹

2.3 AFIA recommendations on the suggested funding arrangements and levy caps

AFIA supports the suggested proportional approach to funding the scheme, outlined in Part 2.1 of this submission. However, we seek more information on the method used to calculate

²⁶ CSLR Regulations, section 11, with terms further defined under section 4 of those Regulations.

²⁷ Explanatory Statement, Financial Services Compensation Scheme of Last Resort Levy Regulations 2022, 3-4.

²⁸ Australian Prudential Regulatory Authority, *Financial Claims Scheme*: www.apra.gov.au/about-financial-claims-scheme.

²⁹ See the definitions of 'scheme levy cap' and 'sub-sector levy cap' in clause 7 of the CSLR Bill.

³⁰ CSLR Bill, clause 17(1).

³¹ CSLR Bill, clause 17(2).

the 'one-off' levy on Australia's 'top 10 banking and insurance groups' to fund outstanding unpaid AFCA determinations.³²

AFIA also strongly supports capping the total amount of levies charged in a single levy period.

We request further information on how the caps of \$250 million for the whole scheme, and \$20 million for each sub-sector were determined as appropriate for the scheme.

This information is especially important, given the Explanatory Memorandum of the CSLR Bill estimates that the total amount of funding the government will have to provide to fund the CSLR, including its funding of the whole amount of the levy for 2023/24, is \$3.9 million.³³

Therefore, it is unclear why the levy caps of \$250 million for the whole CSLR and \$20 million for each sub-sector are appropriate. AFIA seeks further detail on how these figures were calculated and, if appropriate, AFIA requests the lowering of these caps as the empirical data establishes as suitable for such a scheme.

Lowering these caps would ensure they function as a real ceiling on the amount to be raised by the CSLR levy, which is justified using data and costings, instead of being an arbitrary statutory cap that may not actually function as any real ceiling in practice for the scheme.

Furthermore, concerns regarding moral hazard and other similar distortions associated with the scheme remain relevant, with the scheme by its very nature requiring financial institutions to contribute towards compensation for the failure of other and/or future institutions' poor conduct.

AFIA is also significantly concerned that the CSLR Bill and Regulations allow the caps for both the whole scheme and individual sub-sectors to be effectively removed by Ministerial determination.³⁴ This can be done through the imposition of a so-called 'special levy'.³⁵

AFIA notes that elements of the Regulations attempt to mitigate this concern by requiring various notice and reporting requirements be met prior to the imposition of a special levy.³⁶

³² Explanatory Memorandum, Financial Sector Reform Bill 2022, 70[2.30].

³³ Explanatory Memorandum, Compensation Scheme of Last Resort Bill 2022, 3.

³⁴ CSLR Bill, clause 14(4) on individual sub-sectors and 15(5) on the whole scheme. See too CSLR Regulations section 14 and 15 respectively.

³⁵ Explanatory Statement, Financial Services Compensation Scheme of Last Resort Levy Regulations 2022, 3-4.

³⁶ *Corporations Amendment (Financial Services Compensation Scheme of Last Resort) Regulations 2022*, sections 7.10B.50 and 7.10B.55. See too Explanatory Statement for these Regulations, 3-4.

However, it is AFIA's view these attempts at mitigation are insufficient to provide the necessary certainty to entities which may be affected by such uncapped and unplanned 'special levies'.

Levies should be capped at an amount justified by rigorous data and analysis. They should also be lower than the current caps in Clause 17 of the CSLR Bill, as outlined above.

Any requirement for additional 'special levy' payments should require additional legislation to pass the Parliament, rather than being permitted by Ministerial determination. Alternatively, 'special levy' determinations should be made by an independent expert panel. Such a panel should be required to issue written reasons, hear submissions from affected parties and undertake public consultations. Their decisions should also be subject to the *Administrative Decisions (Judicial Review) Act 1977* ('the ADJR Act').

Part 3 – Summary of all AFIA recommendations

AFIA supports the following aspects of the proposed CLSR legislation and Regulations:

1. The introduction of a CSLR, to the extent it implements recommendation 7.1 of the Royal Commission and the Ramsay Review³⁷
2. The eligibility criteria proposed under the new section 1064 of the *Corporations Act*³⁸
3. The capping of maximum compensation payments under the scheme at \$150,000³⁹
4. The government's funding of the first normal levy period for the scheme in 2023/24⁴⁰
5. The graduated approach to funding the scheme from 2024/25 onwards, so levies are proportional to the size of the affected entity⁴¹
6. The principle of capping levies for the whole CSLR and individual sub-sectors⁴²
7. This scheme not applying to the deposit-taking activities of ADIs, which are separately protected by the FCS.⁴³

AFIA has the following concerns, outlined above, with the CSLR legislation and Regulations:

1. AFIA recommends that, in applying the CSLR, Treasury should remain cognisant that ASIC estimates credit providers are only responsible for 11% of unpaid AFCA determinations. This compares to 53% related to financial planners and advisers⁴⁴

³⁷ Royal Commission Final Report, 41.

³⁸ Explanatory Memorandum, Financial Sector Reform Bill 2022, 98[3.57]

³⁹ Ibid, 70[2.30].

⁴⁰ Ibid, 72[2.44].

⁴¹ Ibid, 81[2.108]. See too CSLR Regulations, section 11.

⁴² CSLR Bill, clauses 7 and 17.

⁴³ Australian Prudential Regulatory Authority, *Financial Claims Scheme*: www.apra.gov.au/about-financial-claims-scheme.

⁴⁴ Australian Securities and Investments Commission (ASIC), *ASIC's Response to the Supplementary Issues Paper of the Ramsay Review*, 7[20]: [ASIC - Submission to the EDR Review Supplementary Issues Paper \(treasury.gov.au\)](http://ASIC-Submission-to-the-EDR-Review-Supplementary-Issues-Paper-(treasury.gov.au)).

2. AFIA seeks more information on the method used to calculate the 'one-off' levy to fund accumulated unpaid AFCA determinations prior to the introduction of the CSLR⁴⁵
3. AFIA recommends the lowering of the levy caps of \$250 million for the whole CSLR and \$20 million for each sub-sector. AFIA seeks further information on how these figures were decided as appropriate caps⁴⁶
4. AFIA does not support the capacity of the levy caps, both for the whole CSLR and individual sub-sectors, to be removed by Ministerial determination.⁴⁷ The caps should only be able to be removed by new legislation or determinations made by an independent, expert panel. Such a panel should be required to issue written reasons, hear submissions from affected parties and undertake public consultations. Their decisions should also be subject to the *ADJR Act*.

⁴⁵ CSLR Bill clause 16(1) and CSLR Regulations, section 18.

⁴⁶ CSLR Bill, clause 17, cf Australian Government funding of \$3.9 million per Explanatory Memorandum, Compensation Scheme of Last Resort Bill 2022, 3.

⁴⁷ CSLR Bill, clause 14(4) on individual sub-sectors and 15(5) on the whole scheme. See too CSLR Regulations section 14 and 15 respectively. See too Explanatory Statement, Financial Services Compensation Scheme of Last Resort Levy Regulations 2022, 3-4.