AUSTRALIAN
RETAIL
CREDIT
ASSOCIATION

7 October 2022

Financial System Division
Treasury

Dear Madam/Sir,

ARCA RESPONSE– FINANCIAL SERVICES COMPENSATION SCHEME OF LAST RESORT (CSLR) REGULATIONS 2022

Thank you for the opportunity to provide a response to Treasury in relation to the *Financial Services Compensation Scheme of Last Resort Levy Regulations 2022* (**the Regulations**). We note that the Regulations have been developed pursuant to section 19 of the *Financial Services Compensation Scheme of Last Resort Levy Act 2022* (**the Act**).

The Act provides that the Governor-General may make regulations prescribing matters required or permitted by the Act to be prescribed, or necessary or convenient to be prescribed for carrying out or giving effect to the Act. As the Regulations deal with matters required or permitted by the Act, ARCA's response in relation to the Regulations is of relevance to both the Regulations and the Act.

On this point, we note that the Act has been referred to the Economics Legislation Committee for inquiry and report (due by **20 October 2022**) and that the Committee is currently accepting submissions in relation to this enquiry. Given the relevance of ARCA's submission to the matters dealt with by the Act, a copy of this submission has also been provided to the Committee for its consideration.

ARCA & our previous submission

By way of background, ARCA is the peak industry association for businesses using consumer information for risk and credit management. Our Members include Australia's leading banks, credit unions, finance companies, fintechs, and credit reporting bodies.

Collectively, ARCA's Members account for well over 95% of all consumer lending in Australia.

ARCA has previously provided a submission to Treasury in relation to Treasury's earlier CSLR discussion paper. A copy of ARCA's submission dated 7 February 2020, has been provided with this correspondence.

ARCA's response to the Regulations is set out below and you will note that our response reflects and elaborates upon a number of the matters set out within our earlier submission.

Inclusion of credit providers within the CSLR

By way of background, ARCA is supportive of the introduction of a CSLR provided it is implemented in a manner which reflects and which addresses the recommendations of the Ramsay Review and which is thereby restricted to financial advice failures exclusively.

In this regard, we note that at part 2, section 6 of the Regulations the four sub-sectors that are in-scope of the annual levy are described as follows:

- credit intermediaries sub-sector;
- credit providers sub-sector;
- licensees that provide personal advice on relevant financial products to retail clients sub-sector; and
- securities dealers sub-sector.

As noted in the explanatory memorandum to the Regulations, if a person meets both the criteria for these sub-sectors (as outlined in the ASIC Regulations) during the qualifying period for a levy period, and also the general conditions for the annual levy, they will be liable to pay the annual levy.

ARCA maintains that the imposition of the annual levy upon the credit provider and credit intermediary sub-sector is unwarranted and fails to take into account the significantly reduced potential for consumer detriment arising as a result of unpaid AFCA determinations, (as compared to licensees that provide personal advice in relation to financial products).

In particular, we continue to hold the view that the insolvency of a credit provider is, generally, less likely to lead to an unpaid determination, when compared to the risk which arises as a result of the insolvency of a licensed financial advice firm.

This view is supported by data provided by AFCA on its website and which is accessible at: https://www.afca.org.au/news/latest-news/complaints-paused-due-to-firm-insolvency.

For instance, as stated on AFCA's website, as at 1 June 2022, of the total number of financial firms which;

- are impacted by insolvency, and

- have open claims against them,

the top 7 primary business types, are described as follows:

- Foreign exchange dealer
- Funeral insurance provider
- Managed investment scheme operator
- Financial advisor/planner
- Derivatives Dealer
- Corporate Advisor
- Securities Dealer

It is notable that 'credit provider' or 'credit representative' does not feature within the list of the top 7 primary business types.

Similarly, of the 28 financial firms against which an AFCA determination remained unpaid as at 1 June 2022, the top 7 primary business types were described as follows (with the number of firms set out in brackets next to each description)

- funeral insurance provider (4 firms)
- Managed investment scheme operator (5 firms)
- Financial advisor/planner (8 firms)
- Derivatives dealer (3 firms)
- Securities dealer (3 firms)
- Foreign exchange dealer (1 firm)
- Mortgage broker (2 firms)

You will note that only 'mortgage broker' would potentially fall within the description of 'credit intermediary' or otherwise relate to the provision credit services, whereas the remainder of firms referred to fall within non-credit activities.

Inclusion of ADIs within the CSLR

As noted in our previous submission, in respect of ADIs, given the strict prudential requirements which already apply, ADIs are highly unlikely to become insolvent and should always have the capacity to pay a determination amount (including by loan reduction).

In fact, the application of the CSLR to an ADI would indicate that an issue exists with the Australian Prudential Regulation Authority's (APRA's) capital adequacy requirements, such that these requirements are insufficient to protect against the risk of an ADI becoming insolvent.

On this basis, we strongly recommend that the Regulations be amended so that the description of the sub-sectors which will be subject to an annual levy is amended to exclude those credit providers which are ADIs.

Exclusion of voluntary AFCA Members within the CSLR

We note that the Regulations make it a condition that for a person to be subject to the payment of an annual levy under the Regulations, a law of the Commonwealth must require (directly or indirectly) the person to be a member of the AFCA scheme (refer Part 2, sections 7 & 8).

ARCA is supportive of the inclusion of this condition within the Regulations and we consider that this requirement appropriately addresses the issues which were raised in our earlier submission in relation to the potential consequences arising from the inclusion of voluntary AFCA members within the CSLR.

Uncertainty in relation to costs

While there is certainty in relation to a portion of the annual levy which will be payable by a person who falls within one of the designated sub-sectors, we are of the view that there remains a significant amount of uncertainty as to the potential total liability for individual persons under the CSLR.

In particular, we note that the annual levy payable by a person who falls within an applicable sub-sector for the levy period is the sum of the minimum levy component and the graduated levy component. The minimum levy component for each sub-sector is $100.

This means that the leviable person in each sub-sector will have certainty in relation to the flat minimum fee which will be applied as part of the annual levy. However, what is uncertain, is the total amount of other levies or fees which may be imposed upon persons subject to the CSLR.

For instance, we note that the CSLR operator has the discretion (at any time during a levy period), to recalculate the amounts included in the initial estimate of claims, fees and costs and determine a revised estimate of claims, fees and costs for the levy period and a sub-sector (subject to certain procedural and legal requirements).

Whilst the revised estimate of claims, fees and costs must not exceed the sub-sector levy cap of $20 million for a particular sub-sector for the relevant levy period, this does not address the potential for individual participants to encounter significant unexpected additional costs, at any time during the relevant levy period.

For smaller businesses which do not have the substantial resourcing of larger or more established organisations, unexpected costs and multiple levy amounts can have a significant impact upon a business. We would therefore encourage consideration to be given to the removal or, alternatively to the imposition of further individual limits, to those levies and fees which may be applied separate to the annual levy.

If you have any questions or comments in relation to this submission please contact me via email.

Yours sincerely,

Mary Vancea
General Manager – Legal & Policy