

FOLEY'S | LIST

TERMS OF REFERENCE: SCOPE AND IMPLICATIONS

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Terms of Reference: scope and implications

The Financial Services Royal Commission has the potential to affect a wide range of clients operating in the financial sector.

Key dates are:

Appointment of Commissioner by letters patent	14 December 2017
Initial public hearing	12 February 2018
Interim report due (if chosen)	30 September 2018
Final report due	1 February 2019

The Commission's website is up and running and invites submissions which can be made online.¹

Key things to note in the Terms of Reference are:

1. The enquiry is not just into banks but a range of "financial services entities".
2. The enquiry is not just into "misconduct" but also conduct below community expectations.
3. The enquiry is also into whether any misconduct found arises from the culture and practices in an entity, a subsector or the industry.

1. Which financial services entities are affected?

Not just banks. Financial services entity is defined with five sub-parts:

- (i) Authorised deposit taking institutions.
- (ii) Insurers – general insurers and life insurers.
- (iii) Australian Financial Services Licensees and their authorised representatives.
- (iv) Licensees of registrable superannuation entities, and any entity with a non-incidental connection with such an entity. This limb would include industry, company and retail super funds but not self-managed super funds.
- (v) Intermediaries between borrowers and lenders. (Not in the draft terms of reference.) This limb would include operators such as mortgage brokers.

Credit providers under an Australian credit licence are not included.

¹ <https://financialservices.royalcommission.gov.au/Pages/default.aspx>

2. What conduct is relevant?

The Commissioner must investigate “misconduct”. It is defined to include:

- (i) offences;
- (ii) misleading and/or deceptive conduct;
- (iii) breach of trust;
- (iv) breach of duty or unconscionable conduct; or
- (v) breach of a professional standard or benchmark.

As a separate task (in paragraph (b)), the Commissioner must investigate conduct, practices or business activities “fall[ing] below community standards and expectations.” This concept is not defined.

Thirdly, the Commissioner must investigate particular conduct in relation to superannuation savings, specifically, whether use of those savings for any purpose is not in the members’ best interests or is below community standards and expectations (paragraph (c)).

3. Whose conduct is relevant?

Misconduct by:

- (i) directors
- (ii) officers
- (iii) employees of those entities
- (iv) anyone acting on behalf of those entities. Could include:
 - receivers and managers
 - debt recovery agents

4. Culture and practices

The Commissioner is required to look at the relationship between misconduct findings under paragraphs (a) to (c), and broader culture and practices. The culture and practices may be of the entity, industry or the subsector. The Commissioner must enquire into whether its findings:

- (i) are attributable to “particular culture and governance practices” (paragraph (d)(i)); or
- (ii) result from “other practices, including risk management, recruitment and remuneration practices” (paragraph (d)(ii)).

5. Redress and regulation

The Commissioner must investigate the effectiveness of mechanisms for redress for consumers who suffer detriment due to misconduct (paragraph (e)).

The Commissioner must investigate, among other things, the adequacy of the internal systems of financial services entities and forms of industry self-regulation (paragraph (f)).

6. What is the Commissioner not going to investigate?

There are two carve outs plus an exclusionary discretion:

- (i) The Commissioner is not required to investigate matters already being sufficiently dealt with by another enquiry, investigation or proceeding. The Commission will publish a paper including a list of the enquiries it has identified, on its website.
- (ii) The Commissioner is not required to enquire into matters relating to macro-prudential regulation.
- (iii) Also, the Commissioner may choose not to investigate a matter otherwise within paragraphs (a) to (f) of the Terms of Reference.

The first carve out is potentially wide-ranging. Financial services entities should explore whether particular allegations they are facing are the subject of other enquiries or proceedings.²

7. What is the Commissioner likely to investigate?

The Commissioner must give priority to matters which have the potential for greater harm if not addressed expeditiously.

It has been reported that the Commissioner has already issued a Request for Information to various banks, insurance companies and super funds to provide information regarding all misconduct cases and behaviour that fell short of community expectations since 2008.

8. Examples of clients (or potential clients) who may be affected

- Big banks and insurance companies
- smaller banks and branches of foreign banks

² Examples of completed or ongoing enquiries include:

- 2009 Inquiry into Financial Products and Services in Australia;
- 2016 (Senate) enquiry into forestry managed investment schemes;
- 2016 (House of Representatives) Review of Four Major Banks which included enquiry into consumer protections (house standing committee on economics);
- 2017 ASIC review of mortgage broker remuneration;
- 2017 ASIC report on financial advice and conflicts of interest in vertically integrated institutions;
- and
- ongoing (Senate) Inquiry into consumer protection in the banking, insurance and financial sector.

Recent civil proceedings include bank fees class actions; various managed investment scheme class actions; and miscellaneous individual civil proceedings involving allegations of misconduct against banks or other financial services entities; and various proceedings brought by ASIC.

- credit unions
- registered superannuation entities licensees (135 listed on the APRA website acting as trustees of around 2,300 funds)
- those non-incidentally connected to such licensees, eg:
 - sponsors of funds – unions, employers, employer associations
 - banks
 - service providers to funds
 - life insurance companies
- Australian Financial Services Licence Holders and the authorised representatives of those licence holders, eg:
 - fund managers
 - financial advisors
 - stock brokers
 - operators of managed investment schemes
- directors, officers and employees of financial services entities – who may want their own representation
- those acting on behalf of financial services entities, potentially including:
 - receivers and managers
 - debt recovery
- Potential witnesses – those who have advised financial services entities regarding, for example, governance, risk management, recruitment or remuneration, eg. lawyers, accountants and other consultants.

Given the breadth of the Terms of Reference and the scope of the ‘carve outs’, the direction the Commission takes and its focus will likely take some time to develop.

9. What can affected clients do now?

- Review complaints
- Review policies (eg. governance, risk management, complaints handling)
- Check insurance policies (eg. D&O)

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