Law Council OF AUSTRALIA

Business Law Section

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Dear Ms Sykes

Treasury Laws Amendment (Measures for Consultation) Bill 2023: Rationalisation of ending ASIC instruments (Tranche 2)

1. This submission has been prepared on behalf of the Financial Services Committee and the Corporations Committee (collectively, the **Committees**) of the Business Law Section of the Law Council of Australia in response to the consultation on:

   (a) the exposure draft *Treasury Laws Amendment (Measures for Consultation) Bill 2023: Rationalisation of ending ASIC instruments (Tranche 2)* (the **Bill**) and accompanying exposure draft Explanatory Memorandum; and

   (b) the exposure draft *Treasury Laws Amendment (Measures for Consultation) Regulations 2023: Rationalisation of ending ASIC instruments (Tranche 2)* (the **Regulations**) and accompanying Explanatory Statement.

2. The consultation period is brief, being only open for a month to 16 March 2023, but the Committees are taking the opportunity to comment in some detail on the Bill because the content proposes substantive policy changes that go beyond the apparent scope of routine maintenance of financial services laws.

3. The Committees strongly support both the work of Treasury in stewardship of financial services legislation to keep laws current and fit-for-purpose, and the work of the Australian Law Reform Commission (the **ALRC)** in making recommendations to simplify the *Corporations Act 2001* (Cth) (the **Corporations Act**) and related legislation, and to draw relevant materials together for ease of access and clarity. One of these recommendations is for significant obligations imposed on the regulated community to be located in statute, rather than instruments made by the Australian Securities and Investments Commission (**ASIC**).

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4. To this end, as ASIC instruments of that kind reach the end of their 10-year life, they are being considered for inclusion in the Corporations Act itself. While this is a worthy objective, the translation into the Corporations Act would only be uncontroversial if the meaning and effect were broadly the same. However, in this case, in relation to at least one of the Parts of the Bill, the Committees consider the Bill makes fundamental changes that they are firmly of the view will cause serious difficulties, if implemented in its draft form.

5. The Committees seek only to comment on those of the legislative changes within the Bill covering subject matters in which members of the Committees have expertise and wish to comment.

Part 1—Acquisitions of relevant interests in voting shares

General comments

6. The Corporations Committee generally supports and welcomes Treasury's proposal to substantively incorporate the terms of Class Order [CO 13/520] into the Corporations Act and repeal that ASIC Class Order.

7. In addition, the Corporations Committee submits that the same approach should be taken with respect to the other takeovers class orders (**Takeovers Class Orders**) on which ASIC recently consulted in ASIC Consultation Paper 365, as these are generally not controversial and have been operating effectively for a considerable period.

Additional amendments

8. The Corporations Committee recently made submissions on ASIC's proposed modifications to [CO 13/520] (and to the other Takeovers Class Orders) in response to ASIC Consultation Paper 365[1] (**CP 365 Response**). While the Corporations Committee was largely supportive of the instrument being remade in its current form, the Corporations Committee had a number of suggestions for improvement. We similarly submit to Treasury that, consistent with our CP 365 Response (a copy of which is available through the link set out in footnote 1 below), Part 1 of the draft Bill be amended to reflect the Committee's responses to:

    (a) B3Q2—regarding class relief for non-IPO voluntary escrow arrangements; and

    (b) B3Q3—regarding the modification of subsection 609(3).

9. In addition, to the extent that Treasury proposes to adopt any of the other changes to [CO 13/520] (or the other Takeovers Class Orders) which ASIC has consulted on, please also refer to our comments in respect of those in our CP 365 Response.

10. See also paragraphs 11 to 18 below for our additional submissions with respect to the proposed amendments to section 615.

[1] A copy of the Corporations Committee's CP 365 Response to ASIC is available at https://www.lawcouncil.asn.au/publicassets/fd158cbb-87b1-ed11-947a-005056be13b5/2022%2001%2023%20-%20S%20-%20ASIC%20Consultation%20Paper%20365.pdf

Amendments to section 615 - background

11. Section 615[2] recognises that the relevant rights issue exception under item 10 (or item 10A) of section 611 should be available even if foreign holders do not receive an offer of securities or rights, but cash realised from the sale of those securities or rights (if any). Section 615:

    (a) sets out a procedure that facilitates foreign participation;

    (b) while permitting non-foreign holders to rely on the relevant exceptions to the general prohibition under section 606.[3]

12. Under the procedure in section 615, the issuer must appoint a nominee for foreign holders who is approved by ASIC and is required to undertake certain tasks in connection with that role ("**Nominee**").

13. Item 6(i) of Class Order [CO 13/520] amends section 615 so that the issuer does not need to use the Nominee process for every foreign holder (i.e. it can extend offers to those foreign holders where a prospectus is not needed).

Amendments to section 615—the proposed changes

14. The proposed new legislation seeks to amend section 615 to build in the amendments under item 6(i) of Class Order [CO 13/520]. We agree that it generally does so.

15. We understand that Treasury has a focus on increasing efficiencies by reducing red tape and regulatory spend. Given this, in our view one area for reform would be the Nominee appointment process itself.

16. In the Committees' experience, the Nominee appointment process takes up a significant amount of ASIC's time and increases the issuer's expenses when it does not need to. Both issuers and underwriters find the process time-consuming and it often causes issuers to choose other paths to a rights issue.

17. The Committees see two possible avenues for reform here:

    (a) **eligibility criteria:** a standard set of eligibility criteria being determined for Nominees (either in the legislation or in a legislative instrument) which if a Nominee meets, means that ASIC approval is not required. The eligibility criteria could encompass the following:

        (i) the Nominee has an Australian financial services license that permits it to undertake the activities contemplated under section 615;

        (ii) the Nominee is not the subject of an order from ASIC prohibiting them from being a section 615 nominee;

        (iii) the Nominee has entered into arrangements with the relevant issuer that allow it to carry out the role contemplated under section 615; and

        (iv) the Nominee undertakes to provide full details of its activities and the foreign holders on behalf of whom it disposed of the ineligible securities

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[2] As amended by ASIC Instrument 2015/1069 in the case of accelerated rights issues.
[3] As noted in the Explanatory Statement to Class Order [CO 13/520].

to ASIC on request and retains records to this effect for a minimum of six years; or

(b) **standing approval:** underwriters and other Australian financial services license holders that would seek to operate in the capacity of a section 615 nominee engage directly with ASIC for approval. The approval process would be based on that entity's ability and suitability to be a section 615 nominee, without this being linked to any particular capital raising. So as to not increase the burden on ASIC, an entity would only need to seek approval from ASIC to be a section 615 nominee every three years. ASIC would, of course, have the power to revoke a standing approval in certain circumstances.

18. In the Committees' opinion, this small change would remove a significant inefficiency from the capital raising process, would reduce ASIC's workload and would increase the willingness of issuers to utilise rights issues as a means of raising capital.

Part 2—Constitutions of registered schemes

19. This section sets out the concerns of the Committees with the substantive changes made by the proposed amendments in Part 2 of the Bill, and then provides brief responses to the specific consultation questions.

Background

20. The existing ASIC instruments that the text in Part 2 seeks to replace are:

(a) ASIC Class Order [CO 13/655] *Provisions about the amount of consideration to acquire interests and withdrawal amounts not covered by ASIC (Managed investment product consideration) Instrument 2015/847);*

(b) ASIC Class Order [CO 13/657] *Discretions affecting the amount of consideration to acquire interests and withdrawal amounts*; and

(c) ASIC Corporations (Managed investment product consideration) Instrument 2015/847[4].

21. Those instruments were promulgated by ASIC as an overlay on section 601GA of the Corporations Act, which states in subsection (1)(a) that "The constitution of a registered scheme must make **adequate provision** for the consideration that is to be paid to acquire an interest in the scheme". Subsection 601GA(4) states that if members are to have a right to withdraw from the scheme, the scheme's constitution must, among other things, specify the right, set out **adequate procedures** for the mechanics of withdrawals and the provisions must be **fair to all members** (emphasis added).

22. When these provisions were legislated in the *Managed Investments Act 1998* (Cth) (which amended the Corporations Law, which has since been replaced by the Corporations Act, to insert Chapter 5C), ASIC could have simply provided guidance as to how a responsible entity (**RE**) should interpret these terms in drafting constitutions. Instead, ASIC chose to interpret the expression "adequate provision" very strictly, essentially considering that only a fixed price for an interest hard-wired

[4] This governs pricing for schemes registered before October 2013 and, for those schemes, preserves the provisions of the previous Class Order [CO 05/26] *Constitutional provisions about the consideration to acquire interests*.

in the constitution would meet the requirement without ASIC relief. The relief is given based on conditions, including strictly limiting the types of discretions the RE can exercise and requiring detailed documentation in a "pricing discretions policy" covering the exercise of each discretion (**Pricing Policy**).

23. The experience of members of the Committees is that this approach has always been in tension with the reality of operating a registered scheme, in which prices of interests in the scheme are determined *by reference to* net asset value (for schemes of which the interests are not traded on a financial market) and market price (for interests in schemes which trade on financial markets). There are necessarily variable inputs into prices, including:

    (a) making estimates to fairly attribute costs such as brokerage to members joining and leaving a scheme;[5]

    (b) making appropriate discounts to the entry price to encourage reinvestment or raise capital; and

    (c) simple administrative aspects such as rounding numbers to an appropriate number of decimal places.

    As there are also challenges in obtaining valuations of assets which make up scheme property at precise times, prices at which applications and withdrawals of interests are transacted will rarely, if ever, represent the exact value of an interest in the scheme at the time of issue or withdrawal.

24. While the Committees agree that discounting of prices of interests should not be allowed to unfairly dilute the interests of existing members, the Committees are of the view that general obligations for the RE to determine prices in a way that is fair to both existing members and those members entering and leaving a scheme, and consistent with its duty to act in the best interest of members, should be sufficient to provide adequate member protection without the high level of prescription that has applied under the ASIC instruments to date. The Committees note that neither the legislature nor ASIC has sought to impose similar limitations on companies where, presumably, best interests and other obligations imposed on directors are seen as sufficient fetters.

25. For a retail corporate collective investment vehicle (**CCIV**), which is a closely comparable structure to a registered managed investment scheme, under the content rules for the CCIV constitution set out in sections 1223G and 1223H of the Corporations Act, there are no corresponding requirements regarding constitution provisions or discretions for the issue of shares in the CCIV. Section 1223H requires the constitution to "set out a price, or a method for determining a price, at which shares in the CCIV are to be redeemed" while the relevant sub-fund of the CCIV is liquid. There is a requirement for the redemption provisions to be "fair and reasonable".

26. For registered managed investment schemes, 18 pages of ASIC's Regulatory Guide 134 *Funds management: constitutions* (**RG 134**) are devoted to a highly prescriptive interpretation of the simple requirements in the Corporations Act that there be adequate provision, adequate procedures and, for withdrawals, fairness to members. The Committees submit that the difficulties presented to REs by the ASIC instruments and ASIC's prescriptive approach to interpretation are illustrated by the fact that a search of the Federal Gazette reveals that instruments modifying section 601GA of

[5] This is generally referred to as the transaction cost factor in the price.

the Corporations Act have been made on 452 occasions, which presumably represent circumstances where REs have had to go to the expense and trouble of seeking a modification of the requirements from ASIC because of the impracticality of rigid prescriptive rules relating to pricing of interests. The processing of the relief applications and issuing of these instruments obviously also consumes considerable ASIC resources. Unless Part 2 is modified, the Committees would expect that burden to continue or increase.

27. The Committees believe that reconsideration of the ASIC instruments provides a welcome opportunity to consider the utility of prescriptive rules in this area. The Committees suggest that Treasury consider making laws that will still provide the appropriate level of member protection but will be simpler to apply and administer, and not require REs to change their current processes.

The proposed changes—civil penalty provision

28. It is important to note that the existing regime under Class Order [CO 13/655] only sets out conditions of relief from a requirement of the Corporations Act as to the content of a scheme constitution. It does not impose statutory duties or specific penalties. The consequence of failing to meet the conditions of relief is that ASIC may potentially consider that the constitution does not meet the requirements of section 601GA. The Corporations Act does not provide that contravention of section 601GA is an offence, nor is that section a civil penalty provision.[6]

29. The Bill, by stark contrast, makes it a statutory duty of the RE not to exercise discretions in pricing interests in the scheme outside strict rules and attaches civil penalties to any breach.

30. If the Bill were to be passed in the form of the exposure draft, the effect of the proposed legislation would be that any pricing error, no matter how immaterial, would be a deemed "reportable situation" requiring a breach report to be submitted to ASIC under section 912DAA of the Corporations Act. Minor pricing errors occur frequently in the managed funds industry, often due to circumstances outside the RE's control, such as a temporarily incorrect price feed from a data supplier. The fact that the error may be corrected and remediated within days, and may involve a variation of only a few dollars, would not erase the reportable situation, the obligation to report the breach to ASIC and the potential imposition of a civil penalty. ASIC may therefore be swamped with breach reports relating to pricing errors which are of very low significance. The Committees consider that reviewing such reports represents an unjustified distraction and diversion of finite ASIC resources which would be better utilised addressing more egregious breaches.

31. The exercise of discretions by an RE relating to its powers and duties under a scheme constitution is a normal part of the day-to-day operation of a registered scheme, and, in exercising all discretions, the RE must act in accordance with its statutory duties in section 601FC of the Corporations Act. The Committees are of the view that the imposition of a civil penalty in relation to the exercise of discretions specifically in relation to pricing of interests is disproportionate and is not an appropriate way to regulate the problems that the legislation is purportedly trying to solve—the risk that

[6] See section 1317E of the Corporations Act.

interests may be issued at discounted prices in a way that is unfairly dilutive to existing members, and a perceived challenge in interpreting the term “adequate provision”[7].

32. The Committees submit that the draft legislation should be amended to return the exercise of discretions under a constitution to its proper place as a compliance step, rather than an obligation which is comparable to statutory duties such as requirements to act honestly, exercise care and diligence, and act in members' best interests. There is already a statutory duty in subsection 601FC(1)(f) that requires an RE to ensure that a scheme's constitution meets the requirements of sections 601GA and 601GB. Considered together, the Committees submit that these duties should be sufficient to require the RE to act properly when setting prices of interests in the scheme.

33. As to the purported purpose of the Bill to aid in the interpretation of the expression “adequate provision”, the Committees consider that this could be achieved within the existing section 601GA by making a brief amendment providing that the application price clauses in the constitution should be fair and reasonable to members[8]. The Committees submit that it need not be spelled out that any discretion should be exercised in members' best interests, because that duty already applies under section 601FC(1)(c). The Committees consider that the entirety of the proposed new sections 601FCA to 601GE could be omitted in favour of this simple and clear amendment requiring the relevant provision of the constitution, with which the RE will be bound to comply, to be fair and reasonable. The guidance as to interpretation of the terms in section 601GA could reside in RG 134. To adopt this much simpler approach would, in the Committees' view, be consistent with the ALRC's efforts to simplify the Corporations Act, and would be unlikely to allow any untoward conduct by REs because of the existing requirements imposed on REs to exercise discretions in members' best interests, and (in the case of schemes structured as trusts) as trustee with the applicable fiduciary duties.

34. Finally the Committees note that if, contrary to this submission, different requirements for pricing interests in the scheme are imposed, REs will need assurance that existing requirements are “grandfathered”, so that existing scheme constitutions do not require amendment. There may also need to be a substantial implementation period if computer systems by REs, registry service providers and custodians for processing applications and withdrawals have to be reconfigured to accommodate new rules. REs will also need to update their compliance systems. The Committees cannot perceive any policy justification for the additional implementation costs which this (apparently unintended) substantive policy change would impose.

Pricing Policy

35. The Committees commend the proposal to omit the requirement imposed on an RE, currently located in Class Order [CO 13/657], to prepare a Pricing Policy that sets out all possible discretions the RE may exercise under the constitution, and keep related records of the exercise of discretion. ASIC has imposed a requirement to state in a product disclosure statement for a scheme that the Pricing Policy is available from the RE on request. To the best of Committee members' knowledge, in practice, members

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[7] The Treasury consultation web page refers to the purpose of “making it easier for stakeholders to identify their rights and obligations”. A perceived need for explanation of an existing law does not justify the imposition of a harsher law.

[8] Alternatively, the requirements for registered schemes could be put on an equal footing with the CCIV, and the issue price requirements removed entirely (see paragraph 25).

do not request the policy, so the Committees are of the view that it provides no demonstrable benefit to members.

36. Committee members' experience is that the REs of schemes which are listed on financial markets find the requirement for a Pricing Policy particularly pointless, as member approval requirements for substantial issues and withdrawals of interests are set under the Listing Rules, and Class Order [CO 13/655] already allows the issue of interests at significant discretionary discounts to market prices in certain circumstances.

Technical issues with the existing drafting

37. The Committees note the following specific problems with the drafting of Part 2 (assuming it is retained, which is not the Committees' preferred outcome, for the reasons outlined above):

    (a) Section 601FCA:

        (i) The application of subsection (1) is unclear. Do the rules in this Part not apply if, for example, the constitution is drafted so that it does not meet the requirements of subsection 601GE(1)? Is that a way for the rule to be avoided (see (b)(i))?

        (ii) Subsection (2) prohibits exercising a discretion to set a particular price on application or withdrawal of an interest. It is not clear to the Committees what this drafting is seeking to achieve. So long as the price is not unfairly dilutive and has been set in the best interests of members, what regulatory mischief is avoided by this prohibition? Why could the price not be a specific amount? Arguably, any calculation, even in line with existing requirements of ASIC instruments allowing the exercise of certain discretions, results in a specific price at which the interests are actually issued.

        (iii) Subsections (3) and (4) broadly mirror existing requirements and the Committees believe it would be more sensible to include them in regulatory guidance or, if they must remain in the legislation, frame them as a "safe harbour" for compliance with section 601GA, not attracting any additional sanction. The language in section 601GD(2) to the effect that the constitution "is taken to make adequate provision" could also be applied here.

        (iv) Subsections (5) and (6) impose the duty and civil penalty about which the Committees have expressed serious concerns at paragraphs 28 to 32 above.

    (b) Section 601GD(4): This provision imposes a requirement that does not currently exist, and the Committees consider that it would be impossible for an RE to fully comply with it. Currently, section 601GAE(2)(a) (inserted into the Corporations Act by Class Order [CO 13/655]) requires that, for schemes with interests that are not market-traded, a **formula in the constitution must be based on** the value of scheme property attributable to interests in the scheme at the time of issue. The proposed new drafting requires that the **<u>result</u> of using the formula must be that the price is equal to the value of scheme property at the time of issue** less liabilities divided by the number of interests on issue.

The Committees submit that this more restrictive requirement is not practical and is not consistent with the way market practice and computer systems are currently configured in the managed funds industry. For a typical scheme which invests in equities which trade on financial markets, the RE sets a cut-off time during a business day (say 2 pm) for acceptance of applications to issue new interests. The constitution will generally say that the issue price is the price calculated at the next "valuation time" after acceptance of an application, and that a transaction cost factor is applied[9]. The valuation time for assets of the scheme which are Australian market traded securities will be set after market close and applied to those applications received during the day, but where the scheme includes assets which are securities traded on markets outside Australia, the prices of those assets will be moving overnight and in some cases around the clock. It is therefore not achievable for the value of the scheme property to always be calculated **at the time** the interests are issued. For schemes which hold assets which are less liquid, such as those investing in property or infrastructure, valuations are done as regularly as practical, but third-party valuations are expensive and time consuming and may only be done on the portfolio on a rolling basis, and at less frequent intervals than the periods for processing applications or withdrawals. Unless a scheme holds only cash, it is impossible for the RE to be certain that the value of the scheme property is the value exactly "at the time". The Committees submit that, at the least, the drafting of this provision should instead reflect the wording currently used in Class Order [CO 13/655].

Class Order [CO 13/655] expressly provides for two important reasons to vary from issuing interests at the market price for interests in a listed scheme; namely pro rata rights issues and institutional placements. There are no corresponding provisions in the Bill. If the intention of the Bill is to reproduce the same policy approach as in the Class Order in the Corporations Act, then the Committees submit that provision should be made for these normal market practices. If the Bill does not reproduce these Class Order provisions in the Corporations Act, then an RE may need to hold a members' meeting to vote on an amendment to the scheme constitution to insert a specific price to cover these situations, or potentially apply to ASIC for relief, neither of which is practical in a time-sensitive capital raising environment.

38. The Committees have also observed a minor error in the exposure draft Explanatory Memorandum. Table 1.2 refers to the "Chi-X Limited" financial market. The Committees believe that the reference to "Chi-X Limited" should be "Cboe Australia Pty Ltd" (which was previously known as Cboe Australia Ltd before Chi-X Asia-Pacific Holdings Ltd and its subsidiaries were acquired by Cboe Global Markets, Inc.). Subsection 601GC(3)(b)(i) in the Bill correctly refers to Cboe Australia Pty Ltd.

[9] See paragraph 23 and footnote 5.

Responses to specific consultation questions:

Question	**Committees' response**
The class of scheme targeted by subsection 601GD(6) is intended to be the same class of scheme targeted by notional subparagraph 601GAE(2)(a)(ii) inserted by ASIC Class Order [CO 13/655]. The definition of exchange traded fund has been partially incorporated on the basis that elements of the definition are unnecessary to appropriately target the same class of scheme. The definition of managed fund has not been incorporated on the same basis. Is this appropriate?	For an exchange traded fund (**ETF**) that is not listed on the main board of ASX (but is instead traded on one or both of the AQUA or Cboe markets), the pricing for applications and withdrawals is similar to that for a scheme with interests that are not quoted on a financial market, so ETF pricing requirements can be the same. Generally, only stockbrokers can apply for and withdraw interests in an ETF. Other investors can only acquire and dispose of these interests on-market. There are also market prices for an ETF determined by trading on the relevant exchange, and those prices apply to transfers of interests on-exchange, as opposed to applications and withdrawals administered through the RE. Some exchange-traded managed funds also allow both applications and withdrawals through the RE, and market trading, including for retail clients. The Committees find it difficult to respond to the specific question here, because the meaning and purpose of subsection 601GD(6) is unclear due to the use of negative drafting, which refers to disregarding a discretion under the constitution, without making clear what the consequence of it being disregarded will be. Is the consequence that the constitution will not be taken to make adequate provision? All discretions must necessarily be given to the RE under the constitution, because generally a trustee has no powers or discretions unless they are specified in the document establishing the trust.

Question	Committees' response
Is repeal of the documentation requirements appropriate?	Yes
1.1 In particular, do the documentation requirements provide consumers with important information or safeguards, the repeal of which would cause harm?	No. Please see the comments at paragraphs 35 and 36.
1.2 Do the documentation requirements place an unnecessary administrative burden upon responsible entities?	Yes
1.3 Are there any appropriate alternative approaches?	The scheme constitution should be the governing document for how prices of interests are to be calculated, supplemented as appropriate by disclosure in product disclosure statements or similar.

Question	Committees' response
Is ASIC Corporations (Managed Investment product consideration) instrument 2015/847 still necessary? Could it be repealed? Would any transitional provisions be required?	This instrument should remain on foot while Class Order [CO 13/655] and Class Order [CO 13/657] remain in force. This instrument carried forward the terms of the original Class Order [CO 05/26] when it came to the end of its 10-year life (in 2015. When Class Order [CO 13/655] and Class Order [CO 13/657] were issued, REs with existing schemes as at 1 October 2013 had a choice whether to continue to operate their pricing systems under Class Order [CO 05/26] or opt into the approach under the new Class Order [CO 13/655] by a notice on their website. Many REs of listed schemes chose to change their systems because the provisions of Class Order [CO 13/655] are more flexible for them, having arisen out of the need for heavily discounted capital raising during the global financial crisis. For those REs who have still not opted in to Class Order [CO 13/655], revoking the instrument may make their pricing policies and processes non-compliant although they would not have done anything wrong or injurious to members. If new rules are legislated which would require different policies and processes, the Committees strongly recommend that all REs—whether they are operating under Class Order [CO 13/655] or ASIC Corporations (Managed Investment product consideration) instrument 2015/847–be given a substantial transition period, in particular to allow adequate time to adapt computer systems. However, for the reasons given above, the Committees consider that less prescription in the rules is preferable. If a principles-based approach to the legislation requiring only fairness and best interests were adopted, as opposed to the current highly prescriptive and punitive draft legislation, then the Committees expect that REs could continue to use their existing systems and no transition period would be necessary.

Part 3—Exemptions from requirement to provide Financial Services Guide (FSG)

39. This amendment seems uncontroversial, and the Committees support making these amendments to the Corporations Act to enshrine long-standing ASIC exemptions from the obligation to provide an FSG in the Corporations Act, which are currently in ASIC Corporations (Superannuation and Schemes: Underlying Investments) Instrument 2016/378.

40. The Committees consider, however, that it is desirable to include a provision that applies the same treatment to CCIVs, in addition to superannuation entities and registered schemes.

Part 4—Precontractual statements and information statements (*National Consumer Credit Protection Act 2009* (Cth))

41. The Financial Services Committee supports any initiative to consolidate ASIC instruments into regulation as a general principle. However, the Financial Services Committee believes that there is an opportunity to improve outcomes for credit providers and consumers beyond what has been contemplated by the proposed changes, for the reasons set out below.

Background

42. The exposure draft Regulations seek to incorporate the provisions of *ASIC Credit (Electronic Precontractual Disclosure) Instrument 2020/835 (***ASIC Instrument 2020/835***)* into the *National Consumer Credit Protection Regulations 2010* (Cth) (the **Credit Regulations**). The provisions of Part 4 of the Bill establish the legislative foundation for these amendments by making amendments to the *National Consumer Credit Protection Act 2009* (Cth) (the **Credit Act**).

43. The predecessor to ASIC Instrument 2020/835 was ASIC Class Order [CO 10/1230] *Clarification of credit disclosure obligations—including commencement*. At the time of its sunset, it was the subject of ASIC Consultation Paper 331 *Remaking ASIC class orders on unlicensed COI lenders and credit disclosure obligations* (**CP 331**). Paragraphs 29 to 30 of CP 331 stated as follows:

> "The exemption in paragraphs 5 and 6 of the class order replicates reg 28L for pre-contractual disclosure under s16 of the National Credit Code.
>
> One effect of the declaration and exemption is that a credit provider may give pre-contractual disclosure in the same way it gives other disclosure documents under reg 28L if it chooses to comply with the requirements in the class order.
>
> Note: Alternatively a credit provider can provide precontractual disclosure under s16 of the National Credit Code, either by traditional methods of delivery, or by electronic disclosure (see paragraphs 34–38), by complying with the relevant conditions."
>
> (paras 29–30)

Simplification and Alignment

44. The proposed provisions seek to preserve the current position: different requirements apply in respect of documents to be provided under section 16 of the National Credit Code (which is located in Schedule 1 of the NCCPA) (the **Credit Code**) than to other documents which a credit provider must give under the Credit Code or the Credit Act. However, the Financial Services Committee notes that the requirements of regulation 28L of the Credit Regulations and proposed regulations 72B and 72C do not align, and the assertion in CP 331 that they may be given 'in the same way' is true only in the broadest sense (that the communication method may be electronic).

45. In addition, these inconsistent provisions are not comprehensive, and there is nothing which expressly allows credit providers to provide information which the Credit Code requires them to provide, other than documents to be provided under section 16 of the Credit Code, via an electronic document retrieval system, and on one view they cannot be provided in that way. Information which falls into that category includes account statements. This situation exists because, with effect from 30 July 2020, the *Electronic Transactions Regulations 2020* (Cth) repealed the *Electronic Transactions Regulations 2000* (Cth), regulation 10(2) of which had provided for the possibility of a credit provider being able to use that method. The repealed regulation 10(2) has not been reproduced elsewhere, and the Financial Services Committee submits that this leaves credit providers in an unsatisfactory situation.

46. Section 187 of the Credit Act applies the provisions of the *Electronic Transactions Act 1999* (Cth) (the **Electronic Transactions Act**) to the Credit Act. The Explanatory Statement to ASIC Instrument 2020/835 and the note in CP 331 extracted above confirm the view that the procedure for electronic precontractual disclosure it sets out is an alternative to the procedure under the Electronic Transactions Act, however the Financial Services Committee considers that doubt remains as whether these provisions apply to the giving of disclosure documents under the Credit Act and the Credit Code.

47. The Financial Services Committee is not convinced that there is a need to maintain two procedures for the giving of electronic precontractual disclosure and responsible lending disclosure under regulation 28L, in parallel with the Electronic Transactions Act (as a third mechanism which may apply to both).

48. The Financial Services Committee suggests that Treasury may wish to consider an alternative approach, which would involve:

    (a) repealing both ASIC Instrument 2020/835 and regulation 28L of the Credit Regulations; and

    (b) taking any steps necessary, both by legislative amendments and have ASIC clarify in the appropriate regulatory guidance that the Electronic Transactions Act, subject to the exceptions contained in the Credit Regulations, applies to the giving of the relevant disclosure documents.

49. The Financial Services Committee submits that the financial services disclosure regime could be further simplified by aligning the procedures for electronic disclosure under Chapter 7 of the Corporations Act with the corresponding procedures under the Credit Act and the Credit Code. The current broad approach taken in relation to electronic provision of documents and information for the purposes of the Credit Act and the Credit Code differs materially from the approach under Chapter 7 of the

Corporations Act, which applies to financial products which are not credit. See for example *ASIC Corporations (Facilitating Electronic Delivery of Financial Services Disclosure) Instrument 2015/647*. The Financial Services Committee is not aware of any policy reason for these differences and submits that the procedures should be aligned at least with one another, if not also with the Electronic Transactions Act.

Technical issue—the Bill

50. Subsection 26(10) of the Bill begins with the words:

> "The giving of a document by a credit provider to a debtor for the purposes of this section is to be disregarded if …"

51. The Financial Services Committee considers that the meaning and intended effect of the term 'disregarded' in this context is unclear. The Financial Services Committee submits that it might be more appropriate to use "have no effect" in place of "be disregarded" or to redraft the provision to the following effect:

> "A document is deemed not to have been given for the purposes of this section if …"

Technical issues—the Regulations

52. Assuming that Treasury proceeds with the implementation of proposed regulations 72A–72C, the Financial Services Committee has the following comments.

53. The drafting of these regulations should, in the Financial Services Committee's view, as far as possible be consistent with the approach taken to the same issue. The Financial Services Committee has observed some differences between regulation 72A, on the one hand, and regulation 28L and regulation 72C, on the other. This is discussed below.

54. For example, the use of the term 'physically' and 'personally' in proposed regulation 72A(1) appears to be redundant and confusing. Regulation 28L(6) provides a model for this provision which the Financial Services Committee would support over the current proposed approach.

55. Another example is the use of 'received' in proposed regulation 72A(3) and 'retrieved' in proposed regulation 72C and regulation 28L. It appears to be the intent that a document 'retrieved' by means of a regulation 72C document retrieval mechanism is deemed to be 'received' for the purposes of regulation 72A. The Financial Services Committee considers that this would be clearer if the references in regulation 72A to documents being 'received' were changed to 'received or retrieved'. Alternatively, the link provided in regulation 28L(8) could be duplicated in proposed regulation 72C.

56. The effect of proposed regulation 72A(4)(a) is that, if a debtor tells the credit provider that the debtor has not received the document, then the credit provider will be deemed to have not given the document, taking into account regulation 72A(3) and the proposed section 26(10)(c) of the Credit Code. The Financial Services Committee notes that this would result in the credit provider being in breach of section 16 of the Credit Code, which is a criminal offence of strict liability (see section 22 of the Credit Code). The Financial Services Committee believes that this provision could allow a debtor to falsely tell the credit provider that the debtor has not received or retrieved

the document (for example, when the debtor is seeking to delay or evade enforcement of the contract), which could occur well after the event.

57. The Financial Services Committee submits that the creation of what amounts to a non-rebuttable presumption that the debtor didn't receive the document simply because the debtor asserts that they did not receive it, with the consequence that the credit provider is not only unable to recover the debt but is also potentially subject to criminal prosecution and a civil penalty, is a disproportionate safeguard to protect against the potential for an IT failure. The equivalent provision of ASIC Instrument 2020/835 (s 6(e)) and the substantially similar regulation 28L(8) don't give rise to this non-rebuttable presumption. As they stand, the Financial Services Committee notes that the provisions would have the effect of a credit provider always having to obtain an acknowledgement of receipt before it could rely on electronic delivery.

58. The Financial Services Committee considers that current technology offers much more effective and efficient solutions to this issue. The Financial Services Committee considers that the proposed provisions should, at a minimum, be modified to address this issue, for example by returning to the drafting utilised in regulation 28L(8) and ASIC Instrument 2020/835 (s 6(e)).

59. Proposed regulation 72B(1) preserves the existing requirement that the debtor consents to electronic provision of documents. The Credit Act, and the Credit Code, however, do not address how consent may be given, or whether it may be implied. The Financial Services Committee suggests that there is an opportunity to align the requirements of the Credit Act and the Credit Code with other provisions which are designed to facilitate electronic delivery of documents, such as:

    (a) the definition of "consent" in section 5(1) of the Electronic Transactions Act -providing that "consent" includes consent that can reasonably be inferred from the conduct of the person concerned; or

    (b) the approach taken to the electronic delivery of financial services disclosures under the Corporations Act, as reflected in ASIC Corporations (Facilitating Electronic Delivery of Financial Services Disclosure) Instrument 2015/647.

60. Proposed regulation 72B(2) preserves the requirement also found in regulation 28L(4) that a debtor be given certain information (regulation 72B(2)) before the debtor provides consent. The view of the Financial Services Committee is that, as the disclosure documents which are the subject of the consent are given only once, telling consumers that they might not get precontractual documents in paper form in future is at best baffling, and that they 'should regularly check' for their documents is self-evident.

61. The Financial Services Committee submits that providing this information no longer has value to consumers and there is no longer any good reason for it to be given. The Financial Services Committee notes that electronic delivery is becoming the norm, rather than the exception, and is well understood by consumers generally. The giving of information of this type is not required by the Electronic Transactions Act, and the Financial Services Committee is not aware of any justification for the additional disclosures. The Financial Services Committee submits that the opportunity to dispense with the requirement, and similarly amend regulation 28L(4), should be taken as part of this law reform process.

62. Proposed regulation 72B(2)(c) also preserves the (implied) position that a debtor is able to withdraw consent after it has been given. In the Financial Services Committee's view, there is no good reason to allow consent to be withdrawn in the context of pre-contractual documents that will only be provided once. The withdrawal of consent after it is given has the potential to create particular difficulties for credit providers who offer low-cost credit through solely digital channels. A consumer could apply for a loan in circumstances where the credit provider makes it clear that it only communicates using digital methods, consent to electronic provision of documents as part of that process and then, after the loan has been approved (but before a contract is entered into), the consumer could withdraw that consent and leave the credit provider with no means of communication provided for in its business model. The credit provider would then have to either withdraw its loan approval (which would not be in the interests of either party) or manually provide the pre-contractual documents in paper form (which it may not be set up to do).

63. For the reasons outlined above, in the Financial Services Committee's view, the benefits to the consumer of being able to withdraw consent for electronic delivery of these one-off disclosure documents are illusory, and would be likely to increase costs to all consumers without any apparent benefit.

64. If you have any questions, please do not hesitate to contact Pip Bell, Chair of the Financial Services Committee (pbell@pmclegal-australia.com) (regarding Parts 2 to 4) or Robert Sultan, Chair of the Corporations Committee (robert.sultan@nortonrosefulbright.com) (regarding Parts 1 and 2).

Yours faithfully

Philip Argy
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Business Law Section