Attn: Consumer Law Team

Submitted online

Review of the Amended Unfair Contract Terms Protections

The Australian Financial Markets Association welcomes the opportunity to comment on the Review of the Amended Unfair Contract Terms Protections ('the Review').

AFMA's engagement with the Government in 2023 resulted in a 'class no-action letter' for many Industry Standard Form Contracts in wholesale financial markets. We again thank ASIC and the Government for this important temporary addition to the regime.

This relief broadly addressed the main concern that the broad wording used in the legislation exposed those engaged in the regular activities of wholesale markets to heightened and unclear levels of regulatory risk, however, as discussed below, it was not a perfect fix.

The Review presents an opportunity to further refine the regime and properly build in the protections for wholesale markets into the design of the regime rather than leaving them as an imperfect add-on.

This is important because while the class no-action letter gives assurance that ASIC will not pursue action under the amended regime in relation to the listed Industry Standard Form Contracts, as ASIC notes in their relief the 'no-action letter does not preclude third parties (including the Director of Public Prosecutions) from taking legal action in relation to the conduct the subject of this letter.'[1] The letter itself is a 'policy decision, not a legal opinion'[2] and is a statement of ASIC's 'present regulatory intentions'[3]. That is, it is subject to the potential for a change of policy by ASIC.

We note that should the Review result in changes to the legislation the relief will cease. The relief terminating at 'the end of the day on which any amendments to the ASIC Act commence, where those amendments respond to the review referred to in section 80 of Schedule 2 of the UCT Reforms.'[4] Even in the event no changes are made the relief will terminate at the end of 9 November 2027 unless remade.

We trust Treasury would agree that leaving the legislative provisions such that a class no-action letter is still required would be self-evidently sub-optimal.

[1] https://download.asic.gov.au/media/wj0j54t5/20240205_final-class-uct-no-action-letter_publish-version_05022024.pdf
[2] *Ibid.*
[3] *Ibid.*
[4] *Ibid.*

Preferred adjustments

1- *Wholesale/Retail*

In terms of how best to approach the issues that are partially dealt with via the class no-action relief, our preferred course of action remains that proposed in our original letter:

> Apply the section 761G 'retail client' definition of the Corporations Act 2001 to contracts in respect of financial products and services covered by Schedule 2 of the legislation.

This would align with the substantive intent of the UCT Regime to 'to provide greater protections for small businesses from unfair contract terms'[5].

There is a proliferation of definitions of wholesale vs retail in the Australian law. The Australian Law Reform Commission reported that 'There are 29 regulations that affect the meaning of "retail client" and "wholesale client"'[6], more recently even interpretations by authorities have created more definitions. ALRC noted that 'a definition so complex and with many exceptions is vulnerable to regulatory arbitrage'[7].

AFMA supports a single, logical, and consistent definition. The s761G definition is the core retail/wholesale definition in the Corporations Act. It sets a clear distinction that has been in place since 2002, that in our view should be consistently used and amended from time to time as required.

The creation of multiple competing versions of the retail/wholesale distinctions does not support the conditions needed for international investors to have confidence to engage with the Australian market.

It is also antithetical to the Government's Simplification Agenda, a key priority of the Government, that aims to simplify the regulatory experience and reduce such burdens on business.

AFMA suggests that the Review presents an opportunity to reverse course from the increasing number of retail/wholesale distinctions and begin the process of reducing the number of these tests.

As discussed below, the test currently used in relation to unfair contracts unduly includes often multinational wholesale businesses that manage large asset portfolios into a regime of protections intended for true retail clients.

2- *Professional Investor Test*

In the event the Treasury is not minded to support the Corporations Act's standard wholesale/retail distinction, we would then suggest that the Professional Investor test be applied, as defined in Section 9 of the Corporations Act.

This test has control of $10 million in assets as a key provision. It is another 'bright line test' that is already in the legislation, is well understood, and would address the concerns about the existing legislation affecting wholesale markets without the need for a list of standard contract carve outs.

With the benefit of the over two years of experience of the regime, we suggest that confidence should now be in place to move away from the 100 employee test.

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[5] ParlInfo - BILLS : Treasury Laws Amendment (More Competition, Better Prices) Bill 2022 : Second Reading

[6] ALRC-FSL-Interim-Report-A.pdf

[7] *Ibid.*

Currently a contract is a 'small business contract' if either party "employ[s] fewer than 100 persons" or 'the party's turnover… is less than $10,000,000', and the upfront price payable under the contract does not exceed $5,000,000'.

In financial services there are many firms (and special purpose vehicles) that control sizeable assets yet have relatively few staff, these can be, for example, the lightly staffed local operations of large multinationals. Similarly, the $10,000,000 test should apply at the group level, as application at the party level also results in such firms having their contracts deemed as 'small business'.

We do not expect that these current outcomes accord with public expectations around who should gain additional contractual protections for being 'small business'. We would be pleased to assist Treasury develop wording and guidance to ensure group structures are treated appropriately.

3- *Industry Standard Form Contracts*

In the event that Treasury or the Government is not minded to support the Corporations Act standard wholesale/retail distinction in s761G, or the Professional Investor definition of section 9, then we would suggest that changes be made to properly exclude a wider range of Industry Standard Form Contracts from the regime in the revised legislation.

We would suggest this should be done by setting up a flexible exemptions mechanism that would provide both the Australian Consumer and Competition Commission (ACCC) and the Australian Securities and Investments Commission (ASIC) administrative discretionary powers to exempt out specific types of contracts to deal with unintended consequences as they arise.

The initial register of exempted contracts should be populated with:

(1) The industry standard documents currently covered by the ASIC class no-action letter.
(2) Standard documentation that has been developed in the intervening period including:
- Due Diligence Process Outline (DDPO)
- Block Trade Agreement

Link: [Standard Documentation | AFMA]

(3) Other categories of contracts not currently covered in the relief but that warrant similar exemption including:
- Contracts for the purpose of close-out netting.

This register should be regularly updated to ensure the functioning of wholesale markets remain unimpeded without compromising the protections for retail customers and genuine small businesses.

Regardless of how the wholesale markets carve out is addressed practical guidance and model clauses could still materially assist with broader implementation across large contract libraries.

Extraterritoriality

While we understand that the Government has been supportive of a wide extraterritorial application of the regime in a recent case, the current extraterritorial extension goes beyond what is typical of extraterritorial regimes.

We understand that in *Karpik v Carnival plc* [2023] HCA 39 a foreign company dealing with foreign clients was in scope merely because the company also conducted related business in Australia. This is an unusually limited basis to trigger extraterritorial application.

We would suggest the Government review this result from a whole of Government perspective with a view to determining whether it is a desirable outcome, particularly given the government might not support a similar outcome being reciprocated. For example, an Australian company dealing with Australian customers being caught by the laws of a foreign jurisdiction merely because the company also dealt with customers in that jurisdiction.

Upfront price

Finally, we note that the $5 million upfront price is a poor fit for transactions involving financial products and services for which there may be no upfront price despite the transfer of large amounts of risk.

We suggest that sensible clarifications be developed in line with those elsewhere in the Corporations Act to accommodate financial products and services.

Conclusion

We note again that the Review is a welcome opportunity to refine the Unfair Contracts Regime to better align with the Government's objectives.

AFMA played a key role in ensuring the wholesale markets were not unduly impacted by unintended consequences of the original update to the regime. We trust our letter assists Treasury in further improving the design of the regime and moving protections for the wholesale markets to a more principles-based and permanent basis.

We would very much welcome the opportunity to meet with Treasury to discuss our submission.

Yours sincerely

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