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Design and distribution obligations and product intervention power finally legislated

Legislation for the long awaited financial product design and distribution obligations and ASIC product intervention power has finally been passed by the federal Parliament.

Legislation for the long awaited financial product design and distribution obligations and ASIC product intervention power has finally been passed by the federal Parliament. Partner, Andrea Beatty, and lawyer, Gabor Papdi, provide an overview of the new legislation.

The *Treasury Laws Amendment (Design and Distribution Obligations and Product Intervention Powers) Bill 2019 (Bill)* was passed by both houses of the federal parliament on 3 April 2019. It introduces two long-awaited consumer protection measures into the Corporations Act and NCCP Act:

1. design and distribution obligations for offerors of financial products to retail clients, and
2. a power for ASIC to make orders in relation to financial products (including credit products) to prevent significant detriment to consumers and retail clients.

These powers have long been called for by ASIC and an initial exposure draft Bill was published for consultation by the Treasury as early as 2017. After several revisions between the initial exposure draft and the Bill as passed, these measures have finally been passed by the Parliament at almost the last opportunity before the upcoming election. They represent a significant shift away from a disclosure-centric model of regulation towards a paternalistic model.

Design and distribution obligations

The design and distribution obligations are contained in a new Part 7.8A inserted into the Corporations Act. They require offerors (issuers and certain sellers) of financial products intended for retail clients to consider the intended clients of their products, design products to be appropriate for their intended clients and to take steps to ensure that products are not offered to persons outside their target market. They apply to financial products that must be offered under a Part 6.2D disclosure document or a Product Disclosure Statement, or which are issued to retail clients. As passed, the definition of 'financial product' has been expanded to include financial products within the meaning of the ASIC Act.

The design and distribution obligations commence operation two years after the Bill receives Royal Assent. At the time of writing, the Bill had not yet received Royal Assent.

The objective of the design and distribution obligations is to 'assist consumers to obtain appropriate financial products by requiring issuers and distributors to have a customer-centric approach to designing, marketing and distributing financial products' (Revised Explanatory Memorandum at [1.5]).

The key obligations on regulated persons are:

- for financial product offerors, to prepare a 'target market determination' in relation to a product, identifying the class of persons at whom the product is directed, limitations on its distribution and conditions for reviewing the target market determination (s 994B)
- to not engage in any retail product distribution activity unless and until a target market determination has been made (s 994D)

- to take reasonable steps to ensure that a financial product is distributed consistently with its target market determination (s 994E), and
- to notify ASIC upon giving aware significant dealings in a financial product that are inconsistent with the target market determination (s 994G).

A target market determination for a financial product must be such that if the product were to be issued or sold to a retail client in accordance with the target market determination, the retail client is within the target market and the product would be appropriate for a retail client in the target market – that is, it is consistent with the likely objectives, financial situation and needs of the client (s 994B(8)). Whilst this obligation is phrased as if an offeror identifies a target market given particular product specifications, in practice offerors will need to identify their target retail clients at the outset and then design the financial product to be appropriate to those clients.

If ASIC is satisfied that a design and distribution obligation has been contravened, it may order a regulated person to not engage in specified conduct in relation to retail clients. However, prior to making such an order, ASIC must hold a hearing and allow any interested person to make submissions (unless any delay in making the order would be prejudicial to the public interest, in which case ASIC may make a 21 day interim order).

Product intervention power

The Bill amends the Corporations Act (by inserting a new Part 7.9A) and the NCCP Act (by inserting a new Part 6-7A) to give to ASIC a power to order persons to not engage in specified conduct in relation to a financial product or credit product if ASIC is satisfied that the product has resulted in, or will or is likely to result in significant detriment to retail clients or consumers (as the case may be) (Corporations Act s 1023D(1); NCCP Act s 301D(1)). The provisions inserted into the two statutes are substantially the same, except for the use of legislation-specific jargon (e.g. ‘retail clients’ in the Corporations Act and ‘consumers’ in the NCCP Act). For the purposes of the power in the Corporations Act, ‘financial product’ is defined to include financial products as defined in the ASIC Act, and therefore includes credit facilities.

Product intervention orders are subject to the following limitations:

- they cannot apply to persons in their capacity as consumers or retail clients (Corporations Act s 1023C(2); NCCP Act s 301C(2))
- they cannot require a person to satisfy a training or professional standard that they are not otherwise required to satisfy under legislation
- they cannot require a person who is not required to hold a financial services or credit licence to become a member of an external dispute resolution scheme
- they cannot impose conditions on a person’s remuneration, other than the part of a person’s remuneration that is conditional on the achievement of objectives directly related to the product, and
- they can only cover conduct in relation to retail clients or consumers (Corporations Act s 1023D(4)-(5); NCCP Act s 301D(4)-(5)).

Prior to making a product intervention order, ASIC will be required to consult persons who are reasonably likely to be affected by the proposed order and, if the order will apply to an APRA-regulated body, ASIC will also be required to consult APRA. The consultation requirement in relation to affected persons can be met by ASIC publishing the proposed order (or a description of the proposed order) on its website and inviting the public to comment on the proposed order (Corporations Act s 1023F; NCCP Act s 301F).

A product intervention order can remain in force for a maximum period of 18 months (Corporations Act s 1023G(2); NCCP Act s 301G(2)), unless the Minister has given ASIC approval in writing to extend the operation of the order (Corporations Act s 1023H; NCCP Act s 301H).

Acting contrary to or failing to comply with a product intervention order is both an offence and a civil penalty provision (Corporations Act s 1023P; NCCP Act s 301P).