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Productivity Commission

Review of Australia's Consumer Policy Framework

Productivity Commission
Inquiry Report

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Contents

Abbreviations	VI
A summary of the Commission's proposals	IX
Recommendations	XV
1 Why this inquiry?	1
1.1 Setting the scene	2
1.2 The Commission's task	9
1.3 The Commission's approach	9
1.4 A road map to the rest of the report	15
2 Overview of the current consumer policy framework	17
2.1 Background	17
2.2 The current framework	18
2.3 What happens in other countries?	23
2.4 What problems need to be addressed?	24
3 Objectives for a future consumer policy framework	27
3.1 The role of consumers, effective competition and consumer policy	28
3.2 When should governments intervene?	29
3.3 Government intervention is not costless	36
3.4 Objectives for the consumer policy framework	38
3.5 Identifying and evaluating policy instruments	43
4 Generic consumer regulation	47
4.1 The need for a more nationally coherent approach	48
4.2 The case for a new national generic consumer law	58
4.3 Who should enforce the new generic law?	63
4.4 Other matters	74
5 Industry-specific consumer regulation	81
5.1 When is an industry-specific approach warranted?	82
5.2 Reviewing specific consumer regulation	88

5.3	National regimes for credit and energy services	98
5.4	Other issues in key specific areas	112
6	Supporting institutional changes	129
6.1	Elevating the importance of consumer policy	130
6.2	Any potential role for financial incentives?	132
6.3	Facilitating timely and effective policy changes	133
7	Unfair practices and conduct	139
7.1	Introduction	140
7.2	A general provision relating to unfair practices?	140
7.3	Variations and a national generic consumer law	142
7.4	Misleading or deceptive conduct	143
7.5	Unfair contract terms legislation	149
8	Defective products	171
8.1	Introduction	171
8.2	Merchantable quality and fitness for purpose	173
8.3	Product liability arrangements	177
9	Access to remedies	191
9.1	Introduction	192
9.2	Criteria for assessment and some principles	192
9.3	Making a complaint	194
9.4	Alternative dispute resolution	199
9.5	Court action	210
9.6	Consumer representation	213
10	Enforcement	225
10.1	Introduction	225
10.2	Outline of the current enforcement landscape	227
10.3	Suitability of current enforcement powers	231
10.4	Regulatory consistency	251
11	Empowering consumers	257
11.1	Introduction	258
11.2	Disclosure issues	258
11.3	Consumer information and education initiatives	269
11.4	Consumer input into policy making	274

11.5	Consumer policy research needs	283
11.6	Institutional arrangements for funding consumer advocacy and research	284
12	Vulnerable and disadvantaged consumers	293
12.1	What is consumer vulnerability and disadvantage?	295
12.2	Current approaches to the needs of vulnerable and disadvantaged consumers	296
12.3	Improving outcomes for vulnerable and disadvantaged consumers	299
13	Other considerations for the future framework	305
13.1	Consumer policy and trans-Tasman economic integration	306
13.2	E-commerce	310
13.3	Small business considerations	318
14	How big would the net benefits be?	323
14.1	Placing the costs and benefits into a framework	324
14.2	Looking at the impacts in more detail	325
14.3	Some implications of the qualitative analysis	330
14.4	Quantifying these costs and benefits	332
14.5	Experimental estimates of the costs and benefits of the suite of reforms	334
14.6	The judgment in perspective	355
A	Public consultations	359
B	Behavioural economics and consumer policy	373
C	International approaches	389
D	Unfair contract terms	403
E	Credit regulation	443
F	Utility services	463
G	Occupational licensing	489
	References	497

Abbreviations

ABA	Australian Bankers Association
ABS	Australian Bureau of Statistics
ACCC	Australian Competition and Consumer Commission
ACID	Australian Communications Industry Forum
ACMA	Australian Communication and Media Authority
ADR	alternative dispute resolution
AER	Australian Energy Regulator
AFCO	Australian Federation of Consumer Organisations
APRA	Australian Prudential Regulatory Authority
ASFA	Association of Superannuation Funds of Australia
ASIC	Australian Securities and Investments Commission
BFSO	Banking and Financial Services Ombudsman
CAV	Consumer Affairs Victoria
CFA	Consumers' Federation of Australia
CGA	<i>Consumer Guarantees Act 1993 (NZ)</i>
COAG	Council of Australian Governments
CUAC	Consumer Utilities Advocacy Centre
CFA	Consumer Federation of Australia
DJIR	Department of Justice and Industrial Relations (Tasmania)
EDR	early/external/effective dispute resolution
ERAA	Energy Retailers Association of Australia
ESCSA	Essential Services Commission of South Australia
FCAA	<i>Federal Court Act of Australia 1976</i>
FISC	Financial Industry and Complaints Service
FOS	Financial Ombudsman Service

FRC	full retail contestability
FTA	Fair Trading Act
GDP	Gross Domestic Product
IC	Industry Commission
MCCA	Ministerial Council on Consumer Affairs
MFAA	Mortgage and Finance Association of Australia
NCC	UKs National Consumer Council
NCP	National Competition Policy
NZ CCCFA	<i>Credit Contracts and Consumer Finance Act 2003</i>
NZ FTA	<i>New Zealand Fair Trading Act 1986</i>
OBPR	Office of Best Practice Regulation
OECD	Organisation for Economic Cooperation and Development
OFT	Office of Fair Trading
PC	Productivity Commission
PDS	Product Disclosure Statement
RBA	Reserve Bank of Australia
REIA	Real Estate Institute of Australia
RIS	Regulatory Impact Statement
SCAV	<i>Supreme Court Act 1986</i> (Victoria)
SCLAJ	Standing Committee on Law and Justice
SCOCA	Standing Committee of Officials of Consumer Affairs
TIO	Telecommunications Industry Ombudsman
TPA	Trade Practices Act
TTMRA	Trans-Tasman Mutual Recognition Agreement
UCCC	Uniform Consumer Credit Code
UCCCMC	Uniform consumer Credit Code Management Committee
WA DOCEP	Western Australia Department of Consumer and Employment Protection

A summary of the Commission's proposals

<i>Current problem</i>	<i>Proposed response</i>	<i>Main benefits of change</i>
Objectives for the future policy framework		
Lack of agreed overarching objectives contributes to differences in regulatory interpretation and enforcement, and to tensions with other policies aimed at assisting consumers.	All Australian Governments to adopt common objectives for consumer policy, with the overarching objective being to 'improve consumer wellbeing by fostering effective competition and enabling the confident participation of consumers in markets in which both consumers and suppliers can trade fairly and in good faith.' New policy initiatives to be designed and implemented in accordance with 'best practice' principles.	Improved consumer policy design and application, enhanced responsiveness to changing circumstances, and better policy evaluation.
Institutional reform		
Current delineation of responsibilities for consumer policy among Australian Governments makes levels of protection for consumers partly dependent on where they live; adds unnecessarily to business compliance costs and thereby to prices for consumers; reduces the responsiveness of policymaking to changing consumer needs; and detracts from the further development of national markets.	Facilitation of a nationally coherent consumer policy framework through: <ul style="list-style-type: none"> • introduction of a single national generic consumer law (applying to all sectors, including financial services); • making the Australian Government, through the ACCC, responsible for enforcing the product safety provisions of the new law nationally, but possibly with scope for States and Territories to issue interim product bans; and scope for individual jurisdictions to refer all their enforcement powers for the new law to the Australian Government; • streamlining industry-specific consumer regulation, including through the transfer of responsibility for some areas to the Australian Government (see below); and • increasing the profile of consumer policy within government and improving the effectiveness of MCCA. 	More effective, efficient, consistent and responsive policy and regulation, leading to better outcomes for consumers and greater certainty and lower costs for business. Contribution to the further development of a national commercial regulatory framework.
Industry-specific regulation		
Jurisdictional variations in industry-specific consumer regulation add to business compliance costs. Need to supplement generic law with specific statutes not always established. Ad hoc reform likely to be a slow process.	CoAG, in consultation with MCCA, to oversight a program to: repeal unnecessary specific consumer regulation; and determine how costly divergences and lack of policy responsiveness in other areas should be reduced — including through transfer of policy and/or enforcement responsibility to the Australian Government, and harmonisation of jurisdictional requirements.	A more streamlined and less costly specific regulatory regime, with price savings for consumers. Added impetus to the development of national markets and a national commercial policy framework.

(continued)

<i>Current problem</i>	<i>Proposed response</i>	<i>Main benefits of change</i>
Industry-specific regulation (continued)		
<p>Deficiencies of jurisdiction-based regulation of consumer credit well established.</p> <p>Gaps in the regulation of credit providers and intermediaries providing advice on credit products mean that some consumers face excessive risks and have no guaranteed access to alternative dispute resolution.</p>	<p>Transfer responsibility for regulating consumer credit to the Australian Government, with enforcement by ASIC. The new regime to:</p> <ul style="list-style-type: none">• cover all credit products and intermediary services;• retain the Uniform Consumer Credit Code within the broader financial services regulatory (FSR) regime;• incorporate changes to regulatory requirements already agreed to by MCCA;• incorporate other <i>appropriate</i> State and Territory credit regulation;• include a licensing system for finance brokers, and a licensing or registration system for credit providers (with both requiring participation in an approved ADR scheme); and• allow, over time, for streamlining of current credit regulation, given requirements in the broader FSR.	<p>More effective protection for those acquiring and seeking advice on credit products.</p> <p>More timely adjustment of policy settings to changing requirements.</p>
<p>Despite the move to national energy markets, some key aspects of energy-related consumer policy will continue to be subject to divergent State and Territory regulation.</p>	<p>Australian Governments to agree to the longer term goal of a single set of consumer protection measures for energy services to apply across Australia.</p> <p>State and Territory Governments to agree to implement the new non-price regulatory requirements for retail energy services with minimal jurisdictional variations to enable a smooth transition to a uniform national regime at a later date.</p>	<p>Lower regulatory compliance costs for energy retailers putting downward pressure on energy prices.</p>
<p>Unnecessary retail price regulation of contestable utility services, with some potential for unintended adverse consequences.</p>	<p>Abolish retail price regulations applying to telecommunications services and contestable energy services.</p> <p>Assist disadvantaged consumers through community service obligations and supplier hardship policies.</p>	<p>Removal of redundant regulation which involves some risks to longer term supply, and which is not a good or transparent way of helping disadvantaged consumers.</p>

(continued)

<i>Current problem</i>	<i>Proposed response</i>	<i>Main benefits of change</i>
Industry-specific regulation (continued)		
Protection for consumers in the home building sector is inadequate in most jurisdictions.	The current national review of 'last resort' Builders Warranty Insurance to also examine how to improve 'early stage' protection, including through providing guaranteed consumer access to ADR; and more effective licensing arrangements for builders.	Greater and more uniform protection across Australia for those having a home built or renovated.
Unfair contract terms		
The capacity for businesses to use one-sided contract terms can sometimes unfairly and inefficiently cause detriment to consumers.	The new national generic consumer law to include a provision to address the use of 'unfair' contract terms. This provision to allow regulators or consumers to take action where detriment has been suffered as a result of the use of an unfair term.	More timely and cost-effective redress for those suffering detriment related to the use of these terms. Better incentives for fairer contracts that assign risks efficiently between consumers and suppliers.
Defective products		
Lack of understanding about the rights conferred by the statutory warranty provisions in the generic consumer law.	Regulators to devote more resources to publicising these rights, and to ensuring compliance by suppliers. The need for changes to the legislation itself to be examined in developing the new national generic consumer law.	Raised consumer and business awareness, with fewer consumers purchasing possibly unnecessary extended warranties from suppliers.
Lack of information on the incidence and costs of product-related injury.	Implement all of the remedial measures proposed in the Productivity Commission's Consumer Product Safety study.	Improved design and application of product safety requirements; insights on any impacts of civil liability reforms and other factors on the incentives to supply safe products.
Redress		
Consumers are sometimes confused about where to seek help, and information on complaints is not always effectively used by regulators.	All jurisdictions to participate in the national consumer complaints database (AUZSHARE). Improve the ACCC's web-based information tool — <i>Consumers Online</i> . A somewhat wider role for the telecommunications ombudsman; processes to encourage further integration of financial sector ADR services; investigation of how best to give effect to an ADR service for general consumer complaints; and a process for periodically reviewing whether the structure of ADR services remains appropriate to consumer needs.	Better access to help for consumers where they suffer detriment; greater incentives for suppliers to meet legitimate consumer needs; and improved intelligence about the nature of emerging serious complaints.

(continued)

<i>Current problem</i>	<i>Proposed response</i>	<i>Main benefits of change</i>
Redress (continued)		
Procedures for pursuing small claims in courts and tribunals vary by jurisdiction and can be onerous for consumers.	Standardise arrangements, including claim ceilings and fee waivers for disadvantaged consumers. Court processes to allow for judgements based on written submissions and other forms of non 'in-person' testimony.	Equal treatment of consumers across jurisdictions; more cost-effective access to redress for smaller problems; and better access to the court/tribunal system for disadvantaged consumers.
Representative and class actions face practical obstacles.	Allow regulators to take representative actions on behalf of consumers, whether or not they are parties to the proceedings, and examine workability of private class action arrangements.	More effective redress when many consumers suffer modest detriment from the misconduct of a single supplier.
Resource constraints for legal aid and financial counselling make it harder to assist disadvantaged consumers.	Provide additional funding for these services.	More equitable outcomes for disadvantaged consumers.
Enforcement tools		
Gaps in the tool kit for enforcing the generic law impede a layered approach linked to the seriousness of the breach, and may reduce incentives for suppliers to comply with the law.	The new national generic consumer law to include provision for: civil pecuniary penalties (including recovery of profits from an unlawful activity); banning orders; substantiation notices for questionable claims made to consumers; and infringement notices for minor breaches of the law. Further examination of the case for including 'naming and shaming' powers.	More efficient, cost-effective, deterrence and redress through regulatory action better tailored to the nature of particular breaches.
Promoting consistent enforcement		
Reporting requirements for consumer regulators do not always assist in promoting consistent and coordinated enforcement.	Greater focus on reporting on problem areas/coordination difficulties and how they have been solved.	More prompt and effective attention to enforcement gaps. Less likelihood of overlapping or inconsistent enforcement.
Empowering consumers		
Disclosure documents are overly long and complex, confusing some consumers and being ignored by many.	Require 'layering' of disclosed information to enhance its comprehensibility and relevance to consumers. Greater evaluation of the effectiveness of mandatory disclosure requirements, prior to and/or post implementation.	Enhanced consumer decision making.
Insufficient evaluation of the effectiveness of consumer information and education campaigns.	Cross-jurisdictional review of a sample of existing campaigns by the recently established MCCA taskforce on consumer education issues.	More accessible, effective and better targeted education campaigns.

(continued)

<i>Current problem</i>	<i>Proposed response</i>	<i>Main benefits of change</i>
Empowering consumers (continued)		
Funding constraints limit the ability of many general consumer advocacy bodies to contribute to policy debate. A paucity of information needed to properly assess consumer policy issues.	Additional taxpayer support for the operating costs of a peak national consumer body; for networking between consumer advocacy groups; and for specified research, including through the establishment of a National Consumer Policy Research Centre. Guidelines and governance arrangements to help ensure that this support delivers high quality advocacy and policy research in priority areas, and that the national interest is appropriately represented.	Higher quality consumer input into policy making, including through better access to the views of front-line consumer agencies. A richer information base on which to anchor future consumer policy development.

Recommendations

Chapter 3 — Objectives for consumer policy

RECOMMENDATION 3.1

Australian Governments should adopt a common overarching objective for consumer policy:

‘to improve consumer wellbeing by fostering effective competition and enabling the confident participation of consumers in markets in which both consumers and suppliers trade fairly and in good faith’.

To provide more specific guidance to those developing and implementing consumer policy, this overarching objective should be supported by six operational objectives.

The consumer policy framework should efficiently and effectively aim to:

- *ensure that consumers are sufficiently well-informed to benefit from, and stimulate effective competition;*
- *ensure that goods and services are safe and fit for the purposes for which they were sold;*
- *prevent practices that are unfair or contrary to good faith;*
- *meet the needs of those who, as consumers, are most vulnerable, or at greatest disadvantage;*
- *provide accessible and timely redress where consumer detriment has occurred; and*
- *promote proportionate, risk-based enforcement.*

Chapter 4 — A new national generic consumer law

RECOMMENDATION 4.1

Australian Governments should implement a new national generic consumer law to apply in all jurisdictions. The new law should be based on the consumer protection provisions of the Trade Practices Act (TPA), amended to:

-
- *reflect other recommendations in this report;*
 - *incorporate additional provisions from State and Territory Fair Trading Acts in those cases where the TPA is generally agreed not to be adequate to deal with a particular generic issue; and*
 - *ensure that the new law covers non-corporate entities and accommodates jurisdictional differences in court and tribunal arrangements.*

RECOMMENDATION 4.2

The new national generic consumer law should apply to all consumer transactions, including financial services. However:

- *the Australian Securities and Investments Commission (ASIC) should remain the primary regulator for financial services, with any involvement by the Australian Competition and Consumer Commission or State and Territory consumer regulators in this area only occurring after prior consultation with ASIC; and*
- *financial disclosures currently only subject to ‘due diligence’ requirements should be exempted from the misleading or deceptive conduct provisions of the new law.*

RECOMMENDATION 4.3

Responsibility for enforcing the consumer product safety provisions of the new national generic consumer law in all jurisdictions should be transferred to the Australian Government and be undertaken by the Australian Competition and Consumer Commission (ACCC).

If the Council of Australian Governments determines that the States and Territories should retain the power to issue interim product safety bans, these should lapse after 30 days if not extended nationally by the responsible Australian Government Minister, on advice from the ACCC.

RECOMMENDATION 4.4

The remainder of the new national generic consumer law should be jointly enforced by the Australian Competition and Consumer Commission (ACCC) and State and Territory consumer regulators. However, individual States and Territories should have the option to refer their enforcement powers for all of the new law to the Australian Government, with enforcement to be undertaken by the ACCC.

The enforcement arrangements for the new national generic consumer law should be subject to an independent review within ten years, with explicit consideration of the benefits and costs of moving to a single national regulator model for all of the law, having regard to:

- *any evidence that differing enforcement practices or regulatory ‘break-out’ are leading to divergent outcomes for consumers and businesses across Australia;*
- *experiences and outcomes in any jurisdictions that have referred their powers of enforcement for the new national generic consumer law to the Australian Government; and*
- *the implications of any shifts in enforcement responsibility for industry-specific consumer policy to the national level (see recommendations 5.1 to 5.3).*

Chapter 5 — Industry specific consumer regulation

CoAG’s Business Regulation and Competition Working Group, in consultation with the Ministerial Council on Consumer Affairs, should instigate and oversee a review and reform program for industry-specific consumer regulation that, drawing on previous reviews and consultations with consumers and businesses, would:

- *identify and repeal unnecessary regulation, with an initial focus on requirements that only apply in one or two jurisdictions;*
- *identify other areas of specific consumer regulation where unnecessary divergences in requirements, or lack of policy responsiveness, have significant costs; and*
- *determine how these costs would be best reduced, whilst maintaining protections for consumers, with explicit consideration of:*
 - *the case for transferring policy and, where appropriate, regulatory enforcement responsibilities to the Australian Government and how this transfer might be best pursued; and*
 - *a process and timetable for harmonising and streamlining currently divergent specific regulation that remains the responsibility of the States and Territories.*

RECOMMENDATION 5.2

Responsibility for the regulation of credit providers and intermediaries providing advice on credit products ('finance brokers') should be transferred to the Australian Government, with enforcement to be undertaken by the Australian Securities and Investments Commission (ASIC).

Amongst other things, the new national credit regime should:

- *cover all consumer credit products and all intermediaries providing advice on such products (including through electronic or other arms-length means);*
- *retain the Uniform Consumer Credit Code (UCCC) as a self standing set of requirements within the broader financial services regulatory regime; incorporating changes to the Code that have been agreed to by the Ministerial Council on Consumer Affairs (MCCA), but not yet implemented;*
- *incorporate requirements from state and territory credit legislation outside of the code, where these pass a benefit-cost test;*
- *include a national licensing system for finance brokers, and a licensing or registration system for credit providers that would give consumers guaranteed access to an approved dispute resolution service; and*
- *allow, over time, for the streamlining of the current UCCC in the light of requirements within the broader financial services regime, where net benefits are likely.*

Also, CoAG should give consideration to implementing the new national regime in a phased way, including as initial steps:

- *importing into the Australian Government's jurisdiction the current UCCC — modified to reflect changes agreed to by MCCA, but not yet implemented — and making ASIC responsible for its enforcement; and*
- *introducing an interim, ASIC enforced, national licensing arrangement for finance brokers, based on the draft proposal developed by MCCA.*

RECOMMENDATION 5.3

Through the Ministerial Council on Energy (MCE), Australian Governments should agree to the longer term goal of a national consumer protection regime for energy services, with a single set of requirements to apply in all jurisdictions participating in the national energy market. Those requirements should be enforced by the Australian Energy Regulator.

The specific requirements for that regime should be developed under the auspices of the MCE after the Australian Energy Market Commission has completed its reviews of the effectiveness of competition in each of the jurisdictional retail energy markets.

Through the MCE, State and Territory Governments should also agree to implement the new non-price regulatory requirements for retail energy services, scheduled for introduction around 2010, with minimal jurisdictional variations so as to enable a smooth transition to a uniform national regime at a later date.

RECOMMENDATION 5.4

The Australian Government should remove all retail price regulation applying to telecommunications products and services.

Also, where the Australian Energy Market Commission finds a jurisdictional retail energy market to be fully contestable, the State or Territory Government concerned should remove all retail price regulation in that market as soon as practicable.

Ensuring that disadvantaged consumers continue to have sufficient access to utility services at affordable prices should be pursued through transparent community service obligations, supplier-provided hardship programs, or other targeted mechanisms that are monitored regularly for effectiveness.

RECOMMENDATION 5.5

In examining how to improve 'last resort' home builders' warranty insurance, the Senate Economics Committee should also consider how to enhance the effectiveness of earlier stage consumer protection measures in the home building sector, including through:

- *providing for guaranteed access to effective ADR across Australia; and*
- *better linking licensing schemes to actual builder performance.*

Chapter 6 — Supporting institutional changes

RECOMMENDATION 6.1

As part of the transfer of greater responsibility for consumer policy to the national level, the Australian Government should ensure that there are effective arrangements in place to:

- *facilitate enhanced coordination between Treasury and other relevant government portfolios;*

-
- *promote consistent consumer policy approaches and outcomes across portfolios; and*
 - *enhance the profile of consumer policy across government generally.*

States and Territory Governments should similarly ensure that their current governmental structures promote coordinated and consistent consumer policy approaches and outcomes and give sufficient profile to consumer policy across all relevant portfolio areas.

RECOMMENDATION 6.2

The Australian Government should enhance the capacity of the Commonwealth Consumer Affairs Advisory Council to advise the Minister on emerging, nationally significant, consumer policy issues and on other consumer matters requiring further research (see recommendation 11.3). Specifically the Government should:

- *provide additional resourcing to support the Council’s advisory role; and*
- *ensure that membership of the Council is selected to provide the necessary core consumer policy expertise and to bring a national perspective to its advisory functions.*

RECOMMENDATION 6.3

Australian Governments should agree to the following changes to improve the effectiveness of the Ministerial Council on Consumer Affairs (MCCA).

- *The Council’s voting rules should be altered such that future policy changes would only require the agreement of the Australian Government and three other jurisdictions (a similar arrangement to those for competition and corporations law).*
- *The MCCA secretariat should be sufficiently resourced to carry out policy development work (including the preparation of regulation impact statements) as well as administrative functions.*
- *MCCA should be made more accountable for its performance through improved public reporting of meeting agendas and outcomes. It should also seek greater stakeholder input on its strategic agenda and performance.*

Chapter 7 — Unfair contracts

RECOMMENDATION 7.1

A provision should be incorporated in the new national generic consumer law that addresses unfair contract terms. The Commission's preferred approach would have the following features:

- *a term is established as 'unfair' when, contrary to the requirements of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract;*
- *there would need to be material detriment to consumers (individually or as a class);*
- *it would relate only to standard form, non-negotiated contracts;*
- *it would exclude the upfront price of the good or service; and*
- *it would require all of the circumstances of the contract to be considered, taking into account the broader interests of consumers, as well as the particular consumers affected.*

Where these criteria are met, the unfair term would be voided only for the contracts of those consumers or class of consumers subject to detriment, with suppliers also potentially liable to damages for that detriment. The drafting of any new provision should ensure the potential for private (and regulator-led) representative actions for damages by a class of consumers detrimentally affected by unfair contract terms.

Transitional arrangements should be put in place after enactment, which would give businesses the time to modify their contracts.

The operation and effects of the new provision should be reviewed within five years of its introduction.

Chapter 8 — Defective products

RECOMMENDATION 8.1

Australia's consumer regulators should:

- *raise awareness among consumers and suppliers about the statutory rights and responsibilities conferred by the implied warranties and conditions in the generic consumer law; and*
- *where appropriate, take specific enforcement action against misleading marketing and sale of extended warranties.*

The adequacy of existing legislation related to implied warranties and conditions should be examined as part of the development of the new national generic consumer law.

RECOMMENDATION 8.2

Consistent with the recommendations in the Productivity Commission’s Review of the Australian Consumer Product Safety System, Australian Governments should:

- *develop a hazard identification system for consumer product incidents;*
- *introduce mandatory reporting requirements for voluntary product recalls; and*
- *require suppliers to report products associated with serious injury or death or products which have been the subject of a successful product liability claim or multiple out-of-court settlements.*

Ideally, these measures should be implemented as part of the development of the new national generic consumer law (see recommendation 4.1).

RECOMMENDATION 8.3

Drawing on the mechanisms proposed in recommendation 8.2 and on the baseline study examining product related accidents prepared for the Ministerial Council on Consumer Affairs, Australian Governments should monitor trends in product safety, including any impacts of the civil liability reforms, with a view to assessing whether the incentives to supply safe products continue to be adequate.

Chapter 9 — Access to remedies

RECOMMENDATION 9.1

To facilitate more effective referral of complaints to the right body and sharing of information on complaints:

- *all consumer regulators should participate in the shared national database of serious complaints and cases, AUZSHARE; and*
- *the Australian Competition and Consumer Commission should provide an enhanced national web-based information tool for guiding consumers to the appropriate dispute resolution body, as well as providing other consumer information. It should be subject to consumer testing to ensure that it is easy to use and has the appropriate content.*

Australian Governments should improve the effectiveness of alternative dispute resolution (ADR) arrangements for consumers by:

- *extending the functions of the Telecommunications Industry Ombudsman to pay TV and reviewing options for further consolidation, including through a single consumer entry point for communication services complaints, or an umbrella arrangement (similar to that proposed below for financial services) encompassing all individual dispute resolution services in this area;*
- *reducing the inconsistencies in the complaint-handling and reporting processes used by energy ombudsman and assessing the scope for some jurisdictions to immediately combine their energy ombudsman offices on a bilateral basis, prior to the ultimate formation of a national energy ombudsman;*
- *further enhancing financial ADR services through:*
 - *integration of the existing bodies into a single umbrella scheme to provide one referral and complaint pathway, while allowing independent governance of its subsidiary schemes;*
 - *the requirement that any new industry ADR services, including for credit, be accessed through the gateway service, the Financial Ombudsman Service;*
 - *timely and coordinated revision of ceilings on the value of transactions subject to ADR, with ceilings differentiated according to the relative risks of consumer detriment for the relevant classes of products; and*
 - *allowing a consumer with a claim exceeding any given ceiling to waive the excess and have their claim met up to the limit;*
- *ensuring there are effective, properly resourced, government-funded ADR mechanisms to deal consistently with all consumer complaints not covered by industry-based ombudsmen; and*
- *establishing a formal cooperative mechanism between the various regulators, ADR schemes and other stakeholders to re-assess every five years the nature and structure of ADR arrangements to achieve best practice and address redundancies or new needs.*

Australian Governments should improve small claims court and tribunal processes by:

-
- *introducing greater consistency in key aspects of those processes across jurisdictions, including:*
 - *common higher ceilings for claims;*
 - *common criteria for fee waivers for disadvantaged consumers; and*
 - *allowing small claims courts and tribunals to make judgments about civil disputes based on more flexible forms of testimony, including written submissions and video-conferencing, unless either of the disputing parties requests otherwise.*

RECOMMENDATION 9.4

In the light of the Victorian Law Reform Commission’s Civil Justice inquiry and recent decisions by the Federal Court of Australia regarding third-party financing of private class actions, Australian Governments should assess the desirability of clarification (or amendment) of the relevant legislation and the use of other policy approaches to facilitate appropriate private class action, taking into account any risks of excessive litigation or other unintended effects.

RECOMMENDATION 9.5

Australian Governments should ensure a provision is incorporated in the new national generic consumer law that allows consumer regulators to take representative actions on behalf of consumers, whether or not they are parties to the proceedings.

RECOMMENDATION 9.6

Australian Governments should provide enhanced support for individual consumer advocacy through increased resourcing of legal aid and financial counselling services, especially for vulnerable and disadvantaged consumers.

Chapter 10 — Enforcement

RECOMMENDATION 10.1

The new national generic consumer law should give consumer regulators the capacity to:

- *seek the imposition of civil pecuniary penalties, including the recovery of profits from illegal conduct, for all relevant provisions;*
- *apply to a court to ban an individual from engaging in specific activities after the court has found that a breach of consumer law has occurred;*

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- *issue notices to suppliers requiring them to reasonably substantiate the basis on which claims or representations are made; and*
 - *subject to guidelines informed by the current Treasury review of infringement notice powers under corporations law, issue infringement notices for minor contraventions of consumer law.*

The possible inclusion of naming and shaming powers in the new law should be the subject of further examination and consideration by the Australian and State and Territory Governments under the auspices of the Ministerial Council on Consumer Affairs.

RECOMMENDATION 10.2

The Australian Government should commission a review by an appropriate legal authority of the merits of giving consumer regulators the power to gather evidence after an initial application for injunctive relief has been granted, but prior to substantive proceedings commencing.

RECOMMENDATION 10.3

Australian Governments should ensure that all of their consumer regulators are required to report annually on the nature of specific enforcement problems, their consequences, steps taken to address them (including enforcement strategies and priorities) and the impact of such initiatives. Such reporting should be informed by input from stakeholder groups.

Chapter 11 — Empowering consumers

RECOMMENDATION 11.1

Where a need for mandatory information disclosure requirements has been established, the regulator concerned should require that:

- *information is comprehensible, with the broad content, clarity and form of disclosure consumer tested prior to and/or after implementation, and amended as required, so that it facilitates good consumer decision-making; and*
- *complex information is layered, with businesses required to initially provide only agreed key information necessary for consumers to plan or make a purchase, with other more detailed information available (including by electronic means) by right on request or otherwise referenced.*

Also, the respective roles and responsibilities of regulators and businesses in regard to such matters as consumer testing, content and amendment should be understood and agreed at the outset.

Consistent with these principles, prospective reform of mandatory disclosure requirements for financial services should be progressed as a matter of urgency.

RECOMMENDATION 11.2

Through the National Education and Information Advisory Taskforce, Australian Governments should commission a cross-jurisdictional evaluation of the effectiveness of a sample of consumer information and education measures, and the prospects for improving them. The evaluation should focus on campaigns in areas where the benefits from changing consumer (or supplier) behaviour are likely to be most significant. It should also include an evaluation of the proposed school-based financial literacy program, drawing on evidence from similar programs overseas.

RECOMMENDATION 11.3

Within the broader consumer policy implementation framework agreed to by CoAG, the Australian Government, in consultation with MCCA, should take the lead role in developing arrangements to provide additional public funding to:

- help support the basic operating costs of a representative national peak consumer body;*
- assist the networking and policy functions of general consumer advocacy groups; and*
- enable an expansion in policy-related consumer research.*

Part of the latter funding component should be used to establish and support the operation of a dedicated National Consumer Policy Research Centre (NCPRC), with the remainder provided as contestable grants for research on specified consumer policy issues. An independent review of the effectiveness of the NCPRC in delivering beneficial research outcomes should be conducted after 5 years.

The new funding arrangements should be subject to appropriate guidelines and governance requirements to help ensure that taxpayer support contributes to high quality advocacy and policy research in priority areas, and that the national interest is appropriately represented.

1 Why this inquiry

Key points

- There are a suite of government policies that deal with the purchase and use of consumer goods and services.
- Though these policies are very important in promoting consumer welfare, many other economic and social policies are also ultimately directed at this end.
 - The linkages and complementarities between consumer and competition policies are particularly important in this context.
- Various interrelated market and other developments are influencing the appropriate level and nature of government involvement to protect and empower consumers. Key developments include:
 - greater market competition and internationalisation of supply;
 - a wider range of more complex goods and services (leading, amongst other things, to reliance on standard form contracts, and a need for effective information disclosure);
 - greater consumer spending on services;
 - technological change that is influencing what people buy and how they buy it;
 - reforms to the provision of essential services; and
 - growing awareness of the direct and indirect costs of consumer regulation and the need for evidence-based policies.
- Some aspects of Australia's consumer policy framework do not appear to have been subject to sufficiently rigorous scrutiny prior to their introduction, or to adequate subsequent evaluation. Good policy making has been further complicated by the dual responsibilities of the Australian and State and Territory Governments.
- In reporting on ways to improve Australia's consumer policy framework, the Commission has:
 - focused on a forward looking assessment of high level issues, with a view to mapping out a robust and flexible framework able to respond in a timely way to future market and other developments;
 - had regard to recent CoAG decisions to promote enhanced national approaches in the consumer policy area;
 - looked in some detail at consumer policies in a few key specific sectors; and
 - had regard to the interests of consumers, the sometimes competing interests of businesses and the wider community, and to potential tradeoffs between short and long term outcomes and those for different groups of consumers.

1.1 Setting the scene

What is the consumer policy framework?

There are a suite of government policies that deal with the purchase and use of consumer goods and services. These seek to directly promote better outcomes for consumers by creating a framework that:

- protects them from unconscionable or deceptive conduct, and from unsafe or defective goods and services;
- provides them with remedies when they suffer loss from such conduct or products; and
- assists them in making better purchasing decisions by ensuring that they receive appropriate product information, or in some cases by changing the terms and conditions of transactions (such as cooling off periods).

By making consumers more confident about participating in markets, and penalising inappropriate business conduct, these measures also assist reputable suppliers. Put simply, effective competition is stimulated by empowered consumers and responsive suppliers that trade fairly.

Key elements of the consumer policy framework are the generic provisions in the Trade Practices Act (TPA), State and Territory Fair Trading Acts (FTAs) and Sale of Goods Acts.¹ There are also many specific industry regulations protecting consumers, as well as ombudsman arrangements, some co- and self-regulation and various consumer education initiatives.

Consumer policy has social and distributional as well as economic dimensions. It frequently distinguishes outcomes for different types of consumers — such as by their level of likely vulnerability when purchasing goods and services. It also often codifies community norms about what is fair or ethical in consumer transactions, entailing judgements that go beyond narrow interpretations of economic efficiency.

The relationship with competition and other policies

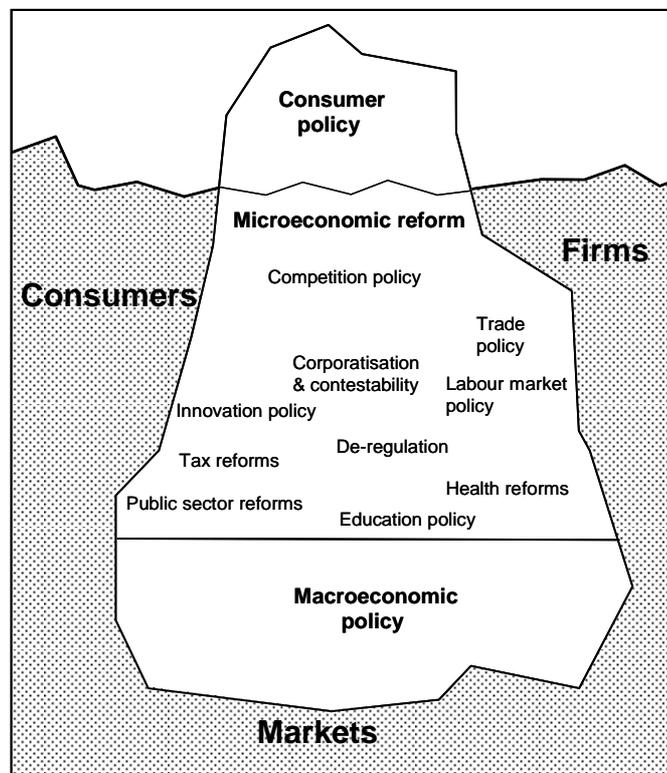
While consumer policy is highly important and visible as a mechanism for promoting consumer welfare, it is only one of many policies aimed at this end (figure 1.1). For example, competition policy seeks to improve outcomes for

¹ Unless otherwise specified, references in this report to the FTAs should be read as also encompassing the various Sale of Goods Acts.

consumers through preventing anti-competitive business practices, and increasing the number of suppliers and the range of goods and services available in markets.

Indeed, almost all economic policies — macro and microeconomic — are ultimately aimed at improving consumer wellbeing. Thus, while not explicitly protecting or empowering consumers, sound macroeconomic policies and widespread competition and trade reforms have delivered large gains to them over the last few decades by containing inflation, improving resource allocation and increasing productivity and economic growth.

Figure 1.1 **Many policies influence consumer wellbeing**



This broader consumer policy context is also important because the different policy strands often reinforce each other. For example, in enabling consumers to operate more effectively in markets, successful consumer education policies can increase the potency of competition and productivity-oriented policies. In this vein, the direct leverage exerted by consumers on economic activity is huge: final household consumption accounts for about 60 per cent of GDP. Hence, many inquiry participants pointed to the important role of effective consumer policies in ‘activating’ competition and thereby enhancing productivity and growth.

Equally, there can be tensions and trade-offs between the different policy strands that ultimately aim to promote consumer wellbeing. For instance, consumer policies

that help consumers in one facet of their dealings with business, may create compliance burdens or dull incentives for productivity improvement, which then rebound on consumers through increased prices or as reduced incomes.

The broader policy environment affecting consumer welfare is also relevant because action in any given area uses government resources and political commitment that may reduce the capacity for action in others. As Professor Chris Field (sub. 102, p. 4) remarked in the context of policies designed to protect vulnerable consumers:

... governments and regulators might also potentially inefficiently misdirect scarce resources on addressing small, retail issues that appear to obviously harm vulnerable consumers, at the expense of allocating resources to address monopolistic wholesale market and other upstream issues, cartel behaviour and broad market design, which may be equally harmful (if not more so) to vulnerable consumers (but less immediately obvious to see).

This highlights the need when evaluating a specific consumer policy proposal to examine its wider repercussions for consumers and to consider the potential gains in the context of other policy options that might not always be conceived of as ‘consumer policy’.

Who are consumers?

The main focus of the consumer policy framework, and thus of this report, is on individuals making purchases of goods or services for private use. This concept of a consumer is central to the definitions employed in both the TPA and the FTAs.

Notably, however, the definitions in these (and other) statutes vary somewhat, and mean that for purchases below designated spending ceilings, businesses sometimes have access to similar protections as individual consumers. Indeed, specific provisions have been added to the TPA to protect small businesses from unconscionable behaviour in their dealings with larger corporations.

In this report, the Commission has endorsed a continuation of the thrust of current generic consumer law in regard to the definition of a consumer, meaning that some business transactions would continue to be covered (see chapter 13). However, in looking at other aspects of the consumer policy framework, and proposing changes to it, the Commission has not delineated any issues arising primarily for businesses.

The changing policy environment

Various changes to markets, institutions and consumers themselves have influenced the nature and scope of consumer policy and will continue to do so in the future.

A more competitive market environment

Reductions in trade barriers, microeconomic reform and the growth of the Internet as a mechanism for informing and undertaking transactions have contributed to much more competitive markets in Australia than when most of the current consumer policy framework was formulated. More intense competition suggests that businesses that fail to respond effectively to consumers' preferences will be disadvantaged in the marketplace. Of itself, this will reduce the extent of policy intervention required to protect and empower consumers.

An associated feature of stronger market competition is *greater internationalisation* of supply. Many more products purchased in Australia are ultimately sourced from overseas (the import to GDP ratio nearly doubled from 1971-72 to 2005-06). As well, consumers are more often transacting directly with suppliers overseas — especially through the Internet — as are foreign consumers with Australian suppliers. Such developments raise new and sometimes complex issues for protecting domestic consumers. They also mean that consumer policy frameworks may play a role in the international competitiveness of firms if they bolster (or retard) a country's reputation for probity in its dealings with foreign consumers.

A greater variety of goods and services

Partly as a result of the more competitive market environment, the range of products available to consumers has increased. Allied to this has been an acceleration in the importance of 'dynamic' goods and services — such as toys, mobile phones and computer technology — whose characteristics change frequently (Bils and Klenow 2001). These trends have been accentuated by an increase in consumer responsibility for buying services that in the past were more often provided, without choice, by governments (such as health, retirement income and education services).

This growth in choice has been of major direct benefit to many consumers. It has also helped to make consumers more demanding and thereby reinforced the competitive disciplines on suppliers. But at the same time, it has increased the investment that consumers must make to compare alternatives and gather information on products, which may disadvantage some.

Growing product complexity

Associated with greater product variety, many goods and services have become more complex. Amongst other things, this has led to:

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- the increased use of intermediaries. Skilled intermediaries can greatly reduce the difficulties confronting consumers in complex markets. Equally, as experience in the financial services area indicates, choosing an intermediary raises new issues for consumers, including conflicts of interest;
 - widespread use of standard form contracts, especially in areas like telecommunications, financial services and car rentals. The associated cost savings can result in lower prices for consumers. But perceptions that suppliers have used these contracts to shift excessive risks onto consumers, together with the inability of consumers to vary terms, have raised unfairness concerns; and
 - more emphasis on (often regulated) information disclosure. However, the length and complexity of many product disclosure statements has given rise to questions about their usefulness.

In conjunction with increased product variety, greater complexity has also created an environment in which there is the potential for sometimes costly industry-specific consumer regulation to proliferate.

Changes in spending patterns

Reflecting demographic, lifestyle and other factors, the pattern of consumer spending continues to change. In particular, a greater share of household income is spent on services — close to 80 per cent, compared to around 60 per cent forty years ago. In contrast to many goods, gauging potential deficiencies in services is often difficult prior to purchase. And in some cases — for example, certain health, building, financial or education services — deficiencies may still be hard to identify after the event, let alone credibly verify where third parties are making judgments about redress. Hence, service transactions are likely to put a greater premium on consumer confidence and trust in the supplier.

The influence of technological change

Ongoing technological change and convergence has been an important contributor to the greater range of products and services available and the accompanying shifts in spending patterns, as well as to the increase in product complexity. It has also empowered consumers by giving many of them better access to information on products and services via the Internet, and expanded the opportunities for them to make purchases outside of the traditional retail environment. But though benefiting many consumers, the latter has simultaneously:

- increased the challenges for those seeking redress — especially for transactions with overseas (or even interstate) suppliers via the Internet;

-
- created new opportunities for fraud; and
 - heightened related consumer problems such as unsolicited approaches (spam) and the privacy and security of personal information.

More generally, the growth in Internet-based transactions has added to the global dimensions of consumer policy.

Reforms to the provision of essential services

The introduction of competition to the provision of energy, water and telecommunications services has delivered significant benefits for consumers. In particular, while the need to put provision on a commercial footing has sometimes led to upward pressure on prices, this pressure has often been more than offset by the productivity gains that have ensued from the more competitive market environment. Moreover, consumers now have much greater capacity to purchase service ‘bundles’ that meet their particular requirements.

However, these benefits have sometimes been diluted by high ‘switching’ costs, and complex customer contracts. And the corporatisation and privatisation of suppliers has raised issues about the best means of ensuring that vulnerable and disadvantaged consumers continue to have appropriate access to these services.

Greater consumer heterogeneity and higher expectations

Consumers themselves are changing. As a result of better education and greater access to information and guidance through the Internet, many are now more able to judge the merits of even complex products and services. But the increasing complexity of markets and demographic changes — such as population ageing and the greater proportion of consumers from non-English speaking backgrounds — may have simultaneously increased the pool of vulnerable and disadvantaged consumers at risk of suffering detriment. So too may have the increasing market participation of young people, especially in the telecommunications area.

Community norms about minimum acceptable levels of safety and information disclosure also appear to be rising. This is leading to demands for ‘less risky’ products, including through the imposition of more stringent minimum safety standards, the mandatory provision of a range of new information (for example, whether a food product contains genetically modified ingredients), and even to calls by some for bans on goods not meeting certain values-based production standards.

Impacts on policy and policy making so far

In the face of these developments, Australia's consumer policy framework has been evolving. For example, there have been additions and modifications to the relevant generic provisions in the TPA and FTAs. The range of industry-specific consumer regulation has also expanded significantly. And there have been various self regulatory and non-regulatory initiatives, including the introduction of voluntary codes of conduct in particular sectors and an array of consumer education measures.

Moreover, like the market landscape, policy making has become more sophisticated. For instance:

- There is now a greater recognition that some regulatory measures to protect and empower consumers can have significant and often unintended costs — not only for businesses, but also for consumers in terms of higher prices, more restricted choice and less responsive suppliers. This has variously led to the repeal or reconfiguration of some consumer regulation, and more exploration of non-regulatory approaches for promoting consumer policy goals.
- There is increasing acceptance that consumer policies should be evidence-based, and thus, among other things, take account of how consumers, businesses and regulators actually behave. The insights provided by behavioural economics have been helpful in this regard — though as discussed later in the report, its contribution lies in enriching existing analytical frameworks and improving the design and implementation of specific policies, rather than in providing a superior alternative framework.

However, it is not clear that all of the changes to the consumer policy framework have been subject to appropriate prior scrutiny. Indeed, some appear to have been 'quick fixes' for particular problems, rather than properly considered policy responses. And where evaluation of existing policies has occurred, it has often been piecemeal, rather than part of a broadly-based assessment of the sort of policy approaches required to deliver the best outcomes for consumers and the community.

Also, good policy making has been further complicated by the dual responsibilities of the Australian and State and Territory Governments in the consumer area. This has variously led to inconsistencies in the generic policy framework provided by the TPA and FTAs, and to overlaps and further inconsistencies between the generic framework and specific industry regulations. In addition, it has rendered the process of making changes to the policy framework more difficult — even when there is general acceptance that change is required. As a consequence, the scope to consolidate policy responsibility, or at least to promote greater uniformity in regulatory requirements, has been the subject of much discussion.

1.2 The Commission's task

It is against this backdrop that the Commission has been asked to report on:

- ways to improve the policy framework to assist and empower consumers, including disadvantaged and vulnerable consumers;
- options for promoting harmonisation and coordination of consumer policy across jurisdictions;
- any areas of consumer regulation that are unlikely to provide net benefits and that could be revised or repealed;
- the scope for more effective use of self-regulatory, co-regulatory, and consumer education and information approaches and principles-based regulation; and
- changes to the consumer policy framework to facilitate greater economic integration between Australia and New Zealand.

In undertaking its assessments, the Commission is to have regard to a range of matters including: the benefits of well-targeted consumer policy for consumer wellbeing, efficiency and productivity; the burden on consumers and businesses, including small business, of unnecessary or poorly configured regulation; the need for consumer policy to be evidence-based; complementarities between Australia's competition and consumer protection laws; and recent developments in consumer policy overseas.

The full terms of reference (and correspondence advising of extensions to the Commission's reporting date) are set out at the front of volume 1 of this report.

1.3 The Commission's approach

A forward looking focus on 'core' consumer policy areas

The Commission has concentrated on those policies explicitly designed to protect and empower consumers. Thus, for example, it has not reviewed the various provisions in Parts IV and VII of the Trade Practices Act designed to prevent harm to consumers from anti-competitive business practices.

Moreover, as this is a forward looking inquiry, the Commission has not looked only at the adequacy of the policy framework to deal with existing consumer issues. Rather, it has sought to map out a framework that can both better address current circumstances and accommodate new market developments and policy pressures

over the next decade and beyond. Given past experiences, those developments and pressures are likely to be substantial.

And though the Commission has focussed on consumer policy as it relates to the market sector of the economy, many of the principles and good practice measures that underlie its analysis and recommendations could have application in the provision of government and other non-market services.

An emphasis on procedures, institutions and generic regulation

In making its assessments and formulating recommendations, the Commission has concentrated heavily on key institutional and procedural aspects of the policy framework. Effective and responsive institutional arrangements will be paramount in dealing with future developments and pressures impacting on policy settings. But even in the absence of such pressures, institutional and procedural reform would be warranted to address the sort of contemporary problems alluded to above.

Consistent with this high level approach, in discussing regulatory issues, the Commission has given most attention to the generic provisions in the TPA and FTAs that create the overarching regulatory framework protecting consumers. Indeed, given the array of industry-specific consumer regulation at both the State and Federal level, it would not have been feasible to examine every existing statute. Moreover, over the last decade or so, some of these statutes have been reviewed, and in several cases revised with the aim of making them more effective.

That said, the Commission has drawn on these analyses of specific regulatory areas in considering how the general policy framework might be improved and to help shed light on the circumstances in which augmentation of the generic provisions with industry-specific measures is likely to be appropriate. It has also had regard to the findings of its own recent report on consumer product safety regulation (PC 2006) — an integral part of the generic regulatory framework — and to the developments that have ensued in response to that report.

In addition, the Commission has looked in more detail at the specific consumer regulations and policies applying to credit provision, utility services and home building.

- Borrowing decisions made by consumers can have pervasive and long lasting effects on their wellbeing, and the financial products they purchase are changing rapidly and becoming increasingly complex.
- Utility or ‘essential’ services similarly have several characteristics that, in combination, make them very important from a consumer policy perspective:

they are necessary to provide for a basic standard of living, with disconnection reducing consumers' capacity to undertake a range of other tasks and potentially posing risks to their health; billing is usually lumpy, increasing the risk of financial stress for low income households; in some areas supply is still less than fully competitive; and price menus and product bundling can be very complex.

- A home will typically be the largest purchase consumers will ever make, with those having that home built required to deal with an additional range of issues and complexities. Though it is up to consumers to take care in choosing the right builder for the job, and ensure that they understand the implications of the contract they sign, there have been ongoing concerns about the adequacy of protection for them when things go wrong in the building process. As well, there are claims that aspects of the consumer protection regime can unfairly penalise reputable builders.

The Commission has also identified occupational licensing as an area where there is ostensibly considerable scope to reduce burdensome regulation. And it has looked at some particular consumer issues raised by the growing importance of electronic and mobile commerce. These are likely to be relevant to both generic consumer regulation and policy, and various specific industry arrangements.

Recognition of recent CoAG decisions on the consumer policy framework

At its most recent meeting, the Council of Australian Governments (CoAG 2008) agreed, in principle, to the Australian Government assuming greater regulatory responsibilities in some key areas of the consumer policy framework — including for consumer product safety, the provision of mortgage credit and related advice and some other lending activities. The objective is to 'remove inconsistencies in consumer policy across jurisdictions and remove overlaps and gaps between Commonwealth and State and Territory responsibilities.' CoAG has further proposed to agree to enhanced national approaches to the consumer policy framework in October of this year, drawing on this report.

As elaborated on in subsequent chapters of the report, the thrust and goals of these proposed changes are in accord with several of the Commission's key recommendations (and with the parallel recommendations in the draft report (PC 2007b) released some months before the CoAG meeting). In a number of cases, the Commission has spelt out some specific requirements that it considers should be encompassed within the broad approach agreed to by CoAG. It has also identified a range of other issues that could warrant further attention in giving effect to the agreed approach.

A concern with the long term wellbeing of the community as a whole

The Commission's primary benchmark for assessing the current policy framework and alternatives to it is the wellbeing of the community as a whole.

This is not to downplay the importance of consumers' rights which, for many, are the starting point for assessing a desirable policy framework (chapter 3). However, while broadening those rights may be in the interests of the wider community, the associated costs must always be considered as part of the policy formulation process. For example, the costs of more stringent labelling requirements to meet 'right to know' goals will be passed on to all consumers — some of whom may derive little benefit from the information provided.

Recognising the trade-offs that arise when there are significant divergences in consumers' preferences and capacities to make informed purchasing decisions is especially important in gauging the degree to which policy should cater for vulnerable and disadvantaged consumers. Though difficult to define precisely (see box 1.1), vulnerable and disadvantaged consumers are a particular target group for consumer policy. In this case, the trade-offs are further complicated by the typically greater weight given to protecting vulnerable and disadvantaged consumers on social justice grounds. But even here, the interests of consumers overall cannot be ignored — raising a range of policy targeting issues, as well as the broader question of whether consumer policy is necessarily the best way of assisting those in the vulnerable and disadvantaged group. Thus, for example, price regulation of utility services is likely to be a more costly way for the community as a whole of meeting distributional goals than, say, targeted hardship support.

In looking at the impacts of policy changes, potential differences in short term and longer term outcomes also need to be considered. For instance, introducing a new regulation to deal with a problem affecting consumers may provide an immediate net benefit for them and the wider community. But, if that regulation stifles competition and innovation then, over the longer term, a net cost may be imposed on both. Unless otherwise indicated, the Commission has taken a longer term perspective in its policy assessments.

Finally, in assessing what would be in the best interests of the community, the Commission has taken account of the previously noted social and distributional dimensions of consumer policy and the insights from behavioural economics. Though the Commission has often not explicitly separated behavioural rationales from other reasons for policy intervention, it sees the findings of behavioural economics as relevant to the design of consumer policies in a range of specific areas.

Box 1.1 Which consumers are vulnerable and disadvantaged?

There have been various definitions of ‘vulnerable and disadvantaged’ consumers put forward by regulatory and other bodies, with Consumer Affairs Victoria (CAV 2004b) providing the most sophisticated analysis of its possible dimensions.

Broadly speaking, *disadvantage* can be seen as reflecting a set of (generally persistent) individual traits — such as poverty, low education, disability, or poor English proficiency — that increase the risk of a consumer experiencing detriment or/and intensify the adverse consequences of that detriment. For example, a person with low income and educational status is likely to be more susceptible to experiencing detriment, less able to bear it if it occurs and less able to seek redress.

Vulnerability is a broader term relating to the susceptibility of consumers to detriment based on both their personal characteristics and the specific context in which they find themselves (market features, product attributes, the nature of the transaction, the regulatory environment). A disadvantaged consumer is a vulnerable one, but not necessarily vice versa. For instance, in markets where the quality of services is hard to discern and convey to consumers, many will be vulnerable, but not disadvantaged. Indeed, virtually all consumers can be vulnerable in some situations — so-called ‘situational’ vulnerability.

The application of these concepts to policy formulation is further complicated by the fact that individuals’ circumstances often change over time. For example:

- A consumer may exhibit a short-lived characteristic — such as trauma following the death of a loved one — that gives rise to temporary vulnerability in many situations.
- Someone who is initially vulnerable in a particular situation may learn strategies that reduce future susceptibility in a repeat situation.
- Changes in income/employment status will see some consumers shift in or out of the disadvantaged grouping.

The implication is that neither vulnerability nor disadvantage can be defined precisely in terms of a particular risk of detriment. Rather, these groups will include consumers experiencing a spectrum of risks. This in turn suggests that if the term ‘vulnerable and disadvantaged’ consumers is to be used to delineate a narrower group for policy purposes, it is best thought of as encompassing those at particular risk of being misled or making poor purchasing decisions, either generally or in specific situations.

A high level approach to tackling regulatory divergence

As documented in a consultancy paper prepared for the Commission by Professors Stephen Corones and Sharon Christensen from the Faculty of Law at the Queensland University of Technology (and available through the inquiry website), there are many variations in the detailed generic consumer provisions in the TPA

and the FTAs. There are similarly a multitude of differences in State and Territory industry-specific consumer regulations.

Most of these variations are minor, meaning that their individual impacts on the protections afforded to consumers and on business compliance costs are generally small. But collectively they are likely to be more of a burden. Hence, the Commission has mapped out some high level procedural and institutional reform approaches to promote uniformity in regulatory requirements in the broad across jurisdictions.

Also, in those cases where it has proposed changes to the *content* of regulations, it has not attempted to suggest specific legislative amendments, concentrating instead on spelling out the nature of the required changes. If the thrust of those proposals is accepted, the drafting of revised legislation and any supporting guidance in Explanatory Memoranda, would be part of the next stage of the process. That said, in commenting on the substance of regulations and possible changes to them, the Commission has had regard to relevant legal and other input in submissions and to the aforementioned consultancy paper (Corones and Christensen 2007).

Provision for extensive public input

The issues raised by this inquiry are relevant to a wide cross section of the community. Accordingly, in preparing this report, the Commission has sought to provide all of the interests with a range of opportunities to contribute.

It held public hearings prior to and after the release of the draft report (PC 2007b), received over 250 written submissions and met informally with more than 70 organisations and individuals across Australia (appendix A). Through these processes, it has been able to capture the views of government entities responsible for developing and applying consumer policy, consumer organisations — including those providing support and advice to vulnerable and disadvantaged consumers — and businesses that must comply with consumer policies. In this latter regard, it also conducted a small scale survey of some major firms to elicit more detailed information on the compliance burdens of consumer regulation.

As well, the Commission met with government, consumer and business interests in several other countries to help inform itself on possible alternatives to current approaches employed in Australia, and on market trends and developments that will influence consumer policy in the coming decades.

1.4 A road map to the rest of the report

The remaining chapters elaborate on the analysis and findings set out in the self contained summary of this report. They are followed by a suite of appendices providing additional background and supporting information for those requiring more detail on particular issues.

The chapters fall into two groups. The first briefly outlines how the current consumer policy framework operates (chapter 2) and then sets out some core objectives and guiding principles that should underpin the future framework (chapter 3).

The second group of chapters examines ways to enhance the effectiveness and responsiveness of the framework, specifically:

- the creation of a single generic consumer law applying across Australia (chapter 4);
- a nationally oversighted review process directed at enhancing the contribution of industry-specific consumer regulation in the broad (including through the removal of outdated or redundant requirements), as well as identification of changes to improve the effectiveness of some key specific regulatory requirements (chapter 5);
- some supporting institutional initiatives to facilitate timely implementation of the revamped generic and industry-specific regulatory regimes, and of any further modifications or augmentations to those regimes necessitated by changing market circumstances in the future (chapter 6);
- changes to the generic consumer law to deal with unfair contract terms (chapter 7);
- measures to improve the effectiveness of the generic ‘merchantable quality’ provisions and those addressing product safety (chapter 8);
- ways to enhance consumers’ access to remedies where they suffer loss from products or services that do not comply with regulatory requirements (chapter 9), and to improve the associated enforcement strategies and tools available to regulators (chapter 10);
- means to create more confident and informed consumers, including through improved disclosure requirements and consumer education programs, better research on consumer policy issues, and more effective consumer input into the policy making process (chapter 11);

-
- dealing with the particular consumer issues faced by vulnerable and disadvantaged groups such as older Australians, young people, those with disabilities, and Indigenous Australians (chapter 12); and
 - some other considerations relevant to future policy settings, namely:
 - the role of an efficient and responsive consumer policy framework in promoting economic integration with New Zealand and global integration more generally;
 - the consumer policy challenges arising from the growth in electronic and mobile commerce; and
 - the implications of policy reform for small business in both its consumer and supplier roles (chapter 13).

Finally, in chapter 14, the Commission has provided some indicative estimates of the likely magnitude of the net benefits for consumers and the community from its proposed reform package.

2 Overview of the current consumer policy framework

Key points

- The consumer policy framework consists of a mix of generic and industry-specific regulation and non-regulatory measures. Both the Australian and State and Territory Governments have responsibilities for policy development, administration and enforcement.
- Although precise approaches in the consumer policy area vary from country to country, there is no fundamental divergence between the Australian regime and that in other developed countries. The key elements of the Australian framework are most similar to those in New Zealand and the United States.
- In a number of respects, Australia's consumer policy framework is sound. It provides a broad platform for consumer protection for most products and services. But it has some systemic deficiencies which impair its effectiveness and which will limit its capacity to adapt to emerging issues, namely:
 - the absence of clearly specified objectives guiding policy development, implementation and evaluation;
 - an inappropriate delineation of responsibilities between the Australian and State and Territory Governments that has led to jurisdictional inconsistencies, gaps and overlaps in the framework;
 - a lack of policy responsiveness to changing market circumstances;
 - inadequate evaluation processes for assessing consumer regulation; and
 - missing or deficient policy instruments.

2.1 Background

Until the 1970s, consumer protection in Australia was largely provided through the common law and, at the State level, Sale of Goods legislation. The *Trade Practices Act 1974* (TPA) was the first national legislation specifically designed to provide consumer protection. The TPA introduced prohibitions against misleading or deceptive conduct and unfair practices, and imposed certain non-excludable terms and conditions into all consumer contracts.

Those provisions were subsequently expanded. In 1986, the TPA was amended to include a prohibition against businesses engaging in unconscionable conduct, and again in 1998 to strengthen the rights of small business in their dealings with larger

enterprises. New provisions were added to regulate product liability and country of origin labelling in 1992 and 1998 respectively.

However, the reach of the TPA was, and is, subject to the limitations imposed by the Constitution, which means it generally only applies to corporations and enterprises trading across state or international borders. Recognising this, in 1983, the Australian, State and Territory governments agreed to consistent consumer protection across the jurisdictions. Subsequently, between 1987 and 1992, each State and Territory introduced consumer protection provisions broadly equivalent to those in the TPA through the Fair Trading Acts (FTAs).

The TPA and FTAs are supplemented by an array of industry-specific consumer regulation, self and co-regulatory schemes and non-regulatory options (such as consumer education campaigns). The result is a framework that is broad ranging but complex — involving all levels of government and a wide variety of policy tools.

2.2 The current framework

Generic legislation

The generic consumer provisions in the TPA and State and Territory FTAs form the basic framework for consumer policy in Australia. These provisions fall into three main categories:

- prohibitions on certain types of conduct, including misleading or deceptive conduct¹ and unconscionable conduct.
- imposition of non-excludable conditions and warranties into consumer contracts², including that:
 - the supplier has the right to sell the good, and the consumer has the right to own the good outright;
 - goods will comply with their description or, if provided, their sample;
 - goods will be of merchantable quality (that is, meet a basic level of quality and performance) and be reasonably fit for purpose; and
 - manufacturers will take reasonable action to ensure that a good can be repaired and that spare parts are available.

¹ Complementing the general prohibition on misleading or deceptive conduct is a list of specific prohibited practices, including false representations and harassment and coercion.

² In some States and Territories, these provisions are included in Sale of Goods Acts rather than the Fair Trading Acts.

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- provisions relating to product safety and product information, including those which enable governments to:
 - ban or recall unsafe goods;
 - require goods to be produced in a certain way or have information marked on or included with goods (safety and information standards); and
 - issue notices about potentially unsafe goods (warning notices).

Other generic consumer protection measures include legislation regulating trade measurement, business names registration, sale of goods and pricing behaviour. The *Corporations Act 2001* also has some provisions equivalent to those in the TPA, primarily relating to unconscionable conduct.

Variation across jurisdictions

Although the State and Territory laws generally parallel the TPA, the provisions are not uniform. For example, inconsistencies arise in relation to:

- the definition of a ‘consumer’ and hence coverage of the statutes across jurisdictions;
- standards for what constitutes harassment or coercion and definitions of pyramid selling schemes;
- requirements for door-to-door selling and telemarketing activities;
- enforcement powers available to regulators. (For instance, some have the power to issue warning and infringement notices and notices requiring a trader to substantiate claims or representations); and
- redress mechanisms for consumers and fines and penalties for breaches of the law.

There are also variations in how intensively each jurisdiction applies consumer laws. For example, more than 80 per cent of consumer product bans apply in only two states (PC 2006, p. 343). In addition, some States and Territories have consumer protection provisions in their FTAs that go beyond those in the TPA. For instance, in 2002 the ACT introduced a requirement for credit providers to undertake an assessment of a borrower’s capacity before offering credit card limit increases, while in 2003 Victoria introduced unfair contract provisions (discussed in chapter 7 and appendix D).

Enforcement and access to redress

Primary responsibility for the administration and enforcement of consumer protection laws rests with the Australian Competition and Consumer Commission (ACCC) and the state and territory Fair Trading Authorities. Enforcement occurs through a range of strategies including court action, administrative settlements, and enforceable undertakings. Private individuals and firms can also bring civil actions under consumer laws — in fact, private parties initiate the majority of actions.

The Federal Court has primary jurisdiction to hear matters under the TPA, with the Federal Magistrates Court having concurrent jurisdiction for some consumer protection provisions. For the FTAs, matters are ordinarily heard in the Supreme Court or, in the case of smaller claims, in the District or Small Claims Court. Parties can seek injunctions, damages, rescission or variation of a contract, refund and non-punitive orders (such as probation orders), community service orders and corrective advertising orders. In addition, the ACCC and Fair Trading Authorities can seek criminal penalties, including fines, for breaches of some generic consumer protection provisions³. These regulatory authorities also provide general assistance in resolving disputes, often through referral to dispute resolution mechanisms in specific industries.

Industry-specific regulation

As noted above, industry-specific consumer regulation supplements generic consumer laws in a large number of areas. At the Australian Government level, those sectors covered by specific regulation include:

- financial services, administered by the Australian Securities and Investments Commission (ASIC);
- telecommunications, administered by the Australian Communications and Media Authority and the ACCC;
- food safety, administered by Food Standards Australia and New Zealand; and
- therapeutic goods, administered by the Therapeutic Goods Administration, a unit of the Department of Health and Ageing.

³ Criminal penalties are not available for breaches of the unconscionable conduct provisions nor, with the exception of Tasmania, for contraventions of the prohibition on misleading or deceptive conduct.

At the state and territory level, several hundred statutes cover an array of activities and providers, (including home building, retail energy supply, credit providers, vehicle sales, retirement villages, travel agents, pawnbrokers and second-hand dealers, and various professional occupations). Much of this legislation is administered by the Fair Trading Authorities, but there are also a significant number of industry-specific regulators, including licensing authorities and safety regulators.

Industry-specific arrangements may include explicit dispute resolution mechanisms and there are several industry-specific ombudsmen (such as the Telecommunications Industry Ombudsman, the Banking and Financial Services Ombudsman and the state and territory energy ombudsmen). In addition, specialised administrative tribunals have been established in some jurisdictions to resolve disputes between businesses and consumers in relation to tenancy, building and credit issues.

Regulation applying specifically to financial services is particularly complex. Partly reflecting their nature and importance to consumer wellbeing, financial services are subject to several different regulatory arrangements administered by a number of government agencies at the national and state level. Specifically:

- As well as administering the consumer protection provisions in the *ASIC Act 2001*, which broadly replicate those of the TPA, ASIC is responsible for administering the licensing and disclosure requirements of the *Corporations Act 2001*.
- However, lending products, such as credit cards, loans and hire purchase agreements are exempted from the *Corporations Act*. These products are subject to the provisions of the Uniform Consumer Credit Code (UCCC), administered by the States and Territories.
- There is also separate regulation in some jurisdictions imposing interest rate caps and licensing credit providers.

Despite this complexity, some financial services fall outside the regulatory net. For example, small business loans and loans to consumers for investment purposes are not regulated by the *Corporations Act* or the UCCC, and finance brokers do not need to be licensed or registered in most jurisdictions.

(Regulation of financial services is discussed in more detail in chapter 5 and appendix E.)

Other policy tools

In addition to the main regulatory tools, the consumer policy framework encompasses various self-regulatory and co-regulatory schemes and non-regulatory tools such as education campaigns.

- Self-regulation is developed, administered and enforced by industry. It can include service charters, accreditation, certification, standards, codes of conduct and dispute resolution schemes. Examples include the Australian Retailers Association Scanning Code of Practice, the Banking Code of Practice, the voluntary advertising codes administered by the Advertising Standards Bureau, and professional accreditation of accountants.
- Under a co-regulatory model, industry typically develops and administers its own arrangements, but government provides legislative backing to enable the arrangements to be enforced by the industry concerned (the therapeutic goods advertising code is one such example).
- Governments can mandate codes under the TPA and FTAs. Mandatory codes also exist under industry-specific regulation in areas such as telecommunications and retail energy supply.
- All governments provide information to educate and assist consumers. This includes publications on key consumer issues and alerting the public to product safety concerns and scams.

Consumer representative bodies also play a significant role in the latter area. For example, the Australian Consumers' Association publishes Choice magazine, which provides an independent source of information on goods and services. In addition to providing general advocacy, some of these groups also offer advice and assistance to consumers on an individual basis (for example, through legal aid and financial counselling).

Policy development

At the federal level, the Treasury is responsible for general consumer policy advice and development. At the state and territory level, responsibility for policy development lies primarily with the Fair Trading Authorities. However, other areas of government play an important role in the formulation of specific consumer regulation. And there are some dedicated bodies involved in aspects of policy development (for example, Food Standards Australia New Zealand).

Higher level policy input and coordination is provided through the Ministerial Council on Consumer Affairs (MCCA), which consists of Ministers responsible for

fair trading, consumer protection and credit laws from the Australian, New Zealand and State and Territory Governments. The role of MCCA is to consider consumer affairs and fair trading matters of national significance and, where possible, develop a consistent approach to these issues.

In addition, governments have a range of advisory bodies and consultative committees to feed into general consumer policy development. For example, the Commonwealth Consumer Affairs Advisory Council (CCAAC) provides independent advice to the Minister for Competition Policy and Consumer Affairs on consumer issues. CCAAC currently has 13 members appointed by the Minister — though it is not clear that the current membership is best suited to providing advice on emerging policy issues that are of national significance (see chapter 6).

2.3 What happens in other countries?

All OECD countries have some sort of consumer policy framework. However, while the broad goals are very similar, there are differences in legal and institutional approaches. And, there are differing emphases on consumer ‘protection’ versus consumer ‘empowerment’.

- At one end of the spectrum, some countries have a strong emphasis on risk prevention, direct regulatory controls and state-led enforcement.
- At the other end, some countries focus on enforcement by consumers of their rights through an established legislative framework, supported by various consumer education measures.
- Most countries sit somewhere along this continuum.

More specifically, and as elaborated on in appendix C:

- almost all countries have some form of dedicated consumer legislation;
 - primarily, this legislation prohibits certain conduct (eg misleading or deceptive conduct) or imposes certain rights and obligations on consumer contracts;
- the amount of industry-specific regulation varies;
 - although most countries have specific regulation for high risk areas (eg medical professions), some tend to rely on generic laws to cover most consumer issues, while others have a suite of industry and occupational regulation (such as Australia and the United States);
- a mix of public and private enforcement of consumer laws is typical;
 - however, some countries, such as the Netherlands and Japan, rely almost exclusively on consumers to enforce their own rights. And these countries

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- tend to provide greater access to small claims courts, tribunals and alternative dispute resolution than countries with strong government enforcement;
- federal systems, such as the United States and Canada, have both national and state/provincial consumer legislation;
 - consequently, consumer policy can vary within these countries, raising consistency and harmonisation issues similar to those arising in Australia; and
 - there is no predominant model for consumer advocacy.
 - in the United States there are several well established private advocacy groups; while the United Kingdom publicly funds the National Consumer Council to represent consumers. In addition, the European Union funds a separate body to represent consumers in standards development processes.

The key elements of the Australian framework are most similar to those in New Zealand and the United States.

2.4 What problems need to be addressed?

As outlined in detail in subsequent chapters, the Commission considers that in a number of respects the current consumer policy framework is sound. The key elements of this framework, operating through the TPA and state FTAs, provide a broad platform for consumer protection for most products and services.

However, input to the inquiry and the Commission's own assessment have highlighted a number of systemic deficiencies with current arrangements which impair the effectiveness of consumer protection measures and add unnecessarily to compliance and administration costs, and which will limit the capacity of the framework to adapt to emerging issues.

- *A lack of clear objectives* for the framework to guide policy development, implementation and evaluation.
- *An inappropriate delineation of responsibilities between the Australian and State and Territory Governments.* This has led to inconsistencies, gaps and overlaps in the policy framework and its enforcement. It has also meant that protection for Australian consumers is partly dependent on where they live. And it has increased compliance costs for business, with these imposts passed on to consumers in the form of higher prices, lower quality and/or reduced product choice.
- *A lack of policy responsiveness to changing market circumstances.* Long delays in implementing change are often experienced even where there is general

agreement among decision makers that action should be taken. The current delineation of responsibilities across governments has been a contributing factor.

- *Inadequate evaluation processes.* While there are procedures in place in all of the jurisdictions for assessing new or amended regulation and periodically reviewing existing regulation, these have not always been applied in a sufficiently rigorous or comprehensive manner. As a result, it has proved difficult to prevent quick fix responses to particular consumer problems and get seemingly outdated or redundant consumer regulation off the statute books.
- *Missing or deficient policy instruments.* Timely and cost effective application of the generic consumer law is made more difficult by gaps in the regulatory tool kit, as well as by deficiencies in alternative dispute resolution and other redress mechanisms where consumers suffer detriment from breaches of that law. This has reduced the effectiveness of the generic regime in protecting consumers and thereby increased the likelihood that more prescriptive industry-specific measures will be employed. Also, mandatory information disclosure requirements have not worked well — sometimes confusing rather than informing consumers. And current approaches on consumer advocacy, education and policy research require modification if they are to better meet the needs of consumers and the community in the years ahead.

Taken together, these deficiencies have reduced the effectiveness of the consumer policy framework and increased the costs associated with its implementation. But the current problems and costs are only part of the story. Given the increasingly national focus of consumer markets, greater product complexity and growing consumer expectations, without remedial action, the costs associated with the current arrangements will continue to grow over time. It is with an eye to the future as well as to the present, that the Commission has concluded that aspects of the framework are in need of an overhaul. (Some quantitative estimates of the potential gains are provided in chapter 14.)

3 Objectives for a future consumer policy framework

Key points

- Competition between firms, responding to signals sent by well-informed and confident consumers, leads to a more dynamic and efficient economy and promotes consumer well-being.
- However, in some circumstances, competition alone may be insufficient to deliver these benefits. Intervention may be required to correct market failures (information gaps, cognitive limitations or social externalities). Governments may also intervene to achieve more equitable outcomes. For the most part, these rationales are consistent with a case for intervention based on promoting appropriately defined consumer rights.
- Of course, intervention has various costs. Hence, establishing a rationale for intervention is not sufficient to justify a policy response. Benefits to the community must outweigh the costs.
- A set of objectives for the consumer policy framework will provide greater guidance to policymakers, regulators, consumers and suppliers and facilitate evaluation of the effectiveness of the framework. An appropriate overarching objective is *to improve consumer wellbeing by fostering effective competition and enabling the confident participation of consumers in markets in which both consumers and suppliers trade fairly and in good faith.*

This overarching objective should be supported by a set of operational objectives — namely, that the consumer policy framework should efficiently and effectively aim to:

- ensure that consumers are sufficiently well-informed to benefit from, and stimulate, effective competition;
 - ensure that goods and services are safe and fit for the purposes for which they were sold;
 - prevent practices that are unfair or contrary to good faith;
 - meet the needs of those who, as consumers, are most vulnerable, or at greatest disadvantage;
 - provide accessible and timely redress where consumer detriment has occurred; and
 - promote proportionate, risk-based enforcement.
- In giving effect to these objectives, the requirements in the consumer policy framework should be based on best-practice principles of policy design and implementation.

3.1 The role of consumers, effective competition and consumer policy

The role of consumers in facilitating competition, and promoting well-functioning markets, has long been recognised. In seeking the ‘best’ value (the good or service and price/quality combination most appropriate for them) consumers not only advance their own self-interest, but also provide signals to suppliers on the product characteristics they require. Competition between suppliers, who respond to these signals, can variously lead to lower costs, improved product quality, greater innovation and higher productivity (see, for example, OECD 2007b, p. 8).

However, poorly informed consumers send weak and confused signals to the market, limiting the benefits they receive from transactions and reducing gains from competition more generally. As pointed out by Vickers (2003), informed choice has two dimensions — knowing the alternatives on offer and having the ability to judge their price and quality differences.

In addition to having access to relevant information, consumers need to be sufficiently confident to act on it (box 3.1). Confident consumers have the skills needed to deal effectively with suppliers, and obtain what they expect from a transaction, or, if not, to access effective redress mechanisms.

Of course, it is not necessary for *all* consumers to be well informed and confident to encourage effective competition between firms. Competition will still be robust if there is a sufficient proportion of informed, ‘marginal’ consumers who are willing to switch suppliers to secure a better deal. That said, as a general rule, competition works best when the bulk of consumers are reasonably well-informed and willing to act on that information.

To this end, a key goal of consumer policy is to overcome significant information failures that can hinder effective competition. However, it is important to emphasise that competition is a means to achieving an improvement in consumer wellbeing rather than an end in itself. In addition, it is only one means. Where competition is limited (or absent), consumer policy can still achieve improvements in consumer wellbeing through other policy responses such as business or product regulation, improved access to redress mechanisms, and support measures (such as legal aid and financial counselling).

It is also important to note that good consumer policy benefits good businesses (and their shareholders) as well as consumers. To the extent that consumer policy makes it more difficult for rogue operators to survive, those who do the right thing benefit.

Box 3.1 **Creating confident consumers**

In identifying the appropriate outcome for consumer policy as ensuring that ‘consumers transact with confidence’, the New Zealand Ministry of Economic Development observed:

Confidence in transacting is important. When consumers are not confident:

- they may avoid transacting in the future so they don’t have to face the possibility of a bad deal and its consequences
- it may result in consumer inertia — they may opt for an existing supply arrangement because of the perception that they will face risks/costs by switching to another supplier or means of supply, even though another supplier or means of supply may offer a better deal or
- they may spend considerable time and effort investigating or will accept higher costs attempting to avoid a bad deal.

In other words, consumers may incur additional costs, or competition may be adversely affected through consumers transacting less and suffering from inertia.

Consumer confidence comes from:

- having the skills and knowledge to be able to transact effectively
- having ready access to information about the characteristics of the products and services consumers intend to purchase
- not being subjected to concealed risks, either from hazardous goods or from rogue suppliers
- having effective access to redress when the market fails
- having robust market rules and institutions that govern consumer transactions.

Source: New Zealand Ministry of Economic Development (2003, pp. 28-9).

3.2 **When should governments intervene?**

Information gaps and poor decision making by some consumers are features of most markets. But they do not automatically warrant a government response. This is especially the case given that mechanisms to address obstacles to good decision making will often emerge in the market. And, by learning from their experiences, consumers become more confident and capable over time.

Imperfect, but nevertheless reasonably functioning, competitive markets may well deliver better outcomes for the community than would be achieved through additional government intervention. In many situations, individual consumers are best placed to decide what purchases to make in their own private interest, and importantly, able to take responsibility for their decisions, even when they do (sometimes) make mistakes.

However, in certain circumstances, intervention may be warranted to correct significant market failures (gaps in information provision, cognitive limitations or those relating to social externalities), or to achieve social justice goals. In the main, these rationales are consistent with a goal of promoting generally-accepted and appropriately-defined consumer rights (see below).

Information failures

Information failures, which can prevent efficient market operation, fall in two broad categories, namely:

- limitations on the ability of consumers to access information; or
- on their capacity to effectively use that information in transactions.

Information imbalances between buyers and sellers

For the most part, suppliers will have better information than consumers about the quality of the goods and services that they offer for sale. A lack of information about relevant product characteristics increases the likelihood of consumer detriment and reduces the effectiveness of signals sent to suppliers (box 3.2).

In many cases, the consequence of a poor consumer choice can be rectified by choosing a different product next time. Indeed, this process of learning from mistakes made in earlier purchases is a crucial part of the information gathering process. By altering their purchasing decisions, consumers can impose penalties on those suppliers who do not conform to reasonable expectations (and by so doing precipitate the exit of those firms or changes in their behaviour). However, this adjustment process takes time during which consumers may be exposed to the risk of loss. Reliance solely on such a process can be especially problematic for costly products, or those for which design faults can result in significant harm.

There are various market responses to these potential problems which will often limit the actual detriment suffered by consumers.

Suppliers of good quality products have incentives to distinguish themselves from those selling poorer quality items.

- They may offer guarantees of quality, extended warranty periods, or to refund the purchase price if the consumer is not satisfied.
- Service providers may enter into contracts that specify that payment is conditional on the quality of the service.

Box 3.2 Sources of potential information problems in markets

Experience goods

Experience goods and services (Nelson 1974) are those for which quality can be difficult to fully establish until after purchase (for example, meals, hairstyling, concerts, and used cars). This gives rise to the prospect of detriment in circumstances where quality differs from that anticipated by the consumer.

Experience goods can also impair the efficient operation of the market through what is known as the problem of adverse selection. Where consumers cannot distinguish quality, the probability of receiving low quality is reflected in the market price. As the price declines, high quality sellers may leave the market, potentially perpetuating a cycle of declining quality and prices until only poor quality products remain. Of course, market responses that enable suppliers to signal quality to consumers (see text) can partly or completely short-circuit this process.

It is important to note that the problem here is not the availability of poor quality products as such, but the inability of consumers to distinguish these from higher quality items. In a market with full information, there may be consumers who are prepared to accept lower quality in return for a lower price.

Credence goods (or post-experience goods)

Credence goods and services (Darby and Karni 1973) are those for which verification of quality may not be possible even after purchase. This is because:

- it may be difficult to determine whether an unsatisfactory outcome is due to the lack of ability or effort on the part of the supplier (for example, legal services, financial counselling, medical services and some trades); or
- some product characteristics are difficult to verify (such as whether food is organic or whether medicinal products will have the promised effect).

Establishing quality can be further complicated in circumstances where problems only emerge over time. Credence attributes are typical of many services, particularly those provided by specialists, who consumers may rely on to diagnose and provide solutions to problems.

In such circumstances, there are a number of ways in which consumers may be disadvantaged. The provider may have an incentive to recommend unnecessary services, or provide a lower standard than agreed with the customer, particularly where the consequences of poor service may not become apparent for some time. Further, due to the infeasibility of precisely specifying quality before the transaction is undertaken, the consumer is required to take some aspects of performance on trust (Byron, Gropp and Gusberti 2000, p. 180).

Whenever establishing quality is difficult, the extent of problems which arise for consumers will depend on whether market responses emerge. The bigger the quality perception problem, the stronger will be the incentives for a market response. That said, there are a number of impediments to these responses emerging (see text).

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- Firms often distinguish themselves from others through branding and reputation. Repeat purchases provide sellers with the opportunity to build and maintain reputations for high quality supply.

Intermediaries may also offer information services to consumers (pre-purchase mechanical inspections for cars are an example).

As well, there are common law avenues available for consumers to obtain relief for faulty products or misrepresentation.

However, as Hadfield et. al (1998, pp. 155-6) note, there are a number of market features which may reduce the likelihood of a market-based solution emerging, in particular where:

- repeat transactions are rare, reducing the benefits to firms of having satisfied customers;
- entry and exit costs to the industry are low, leading to the possibility of ‘fly-by-night’ operators with little to lose from a poor reputation; and
- there are limits to the ability of consumers to obtain common law remedies, including where:
 - sellers are outside the consumers’ jurisdiction;
 - sellers have few assets against which a judgement can be enforced;
 - the costs to consumers of an unwise decision are delayed or potentially catastrophic, making a court judgment an unsatisfactory resolution; and
 - the cost of obtaining a resolution through the courts is likely to be high, reducing the incentive for consumers to pursue the issue.

Fraudulent or deliberately misleading supplier conduct is an extreme manifestation of information asymmetry which prevents the benefits of competition from being fully realised and undermines confidence in the market concerned.

Limitations on the ability of consumers to effectively use information

More recently, behavioural economists have drawn on longstanding insights into human behaviour to question whether consumers always behave in what standard economic analysis suggests is in their best interests, even where they are adequately informed¹. This raises a range of challenges for policy making, including whether

¹ Obviously producers are also subject to behavioural biases, but for the purposes of this inquiry such biases do not appear to have major unaddressed policy implications.

the provision of more information to consumers will necessarily be an effective way of improving market outcomes.

The view that some consumers may lack the ability to interact effectively with suppliers is not new. It is well-accepted that certain groups in the community (such as children) lack the cognitive capacity to assess all the implications of entering into a transaction and are therefore prevented by law from doing so. Examples include:

- dangerous products which, if used by children, might endanger themselves or others;
- products which have the potential to cause emotional damage (such as certain movies);
- products of addiction; or
- products requiring a long-term financial commitment.

However, the recent work in the behavioural economics area suggests that limitations on the ability of consumers to effectively use product information might be more pervasive than previously recognised by economists. As discussed in appendix B, behavioural characteristics which can lead to consumers making poor decisions include:

- the *endowment effect* — consumers may persist with options they have chosen, even when better value alternatives are available;
- *choice overload* — consumers may avoid making decisions when there are too many alternatives on offer, or where those options appear too complicated to evaluate;
- simple *rules of thumb* — consumers may inappropriately apply these decision-making techniques to complex situations; and
- *framing effects* — the way in which the product is presented can influence choice.

All of these behaviours (which are partly acknowledged by the current consumer policy framework) may be particularly problematic in markets for complex products (FEMG, sub. DR122, pp. 9-10; ACCC, sub. 80, pp. 157-8; ASIC, sub. 103, pp. 16-17). For example, choosing between alternative financial products might require an understanding of the time value of money; or, in the utilities sectors, product bundling can add an extra dimension of complexity. These problems can sometimes be reduced by drawing on the experience of more knowledgeable friends and relatives, or alternatively, by paying for published comparative information about such products, where it is available. However, these options will not always

be available. Nor will consumers subject to behavioural biases necessarily use them even when they are available.

The ability to make well-informed decisions can also be impaired by the circumstances under which the decision is made. As noted in chapter 1, there are situations in which most consumers will be vulnerable to poor decision-making (for example, following a bereavement). Time constraints may also limit the ability of consumers to fully inform themselves, with constraints sometimes being imposed by ‘high pressure’ sales techniques. This, in turn, can provide a rationale for ‘cooling-off’ periods to provide consumers with time to reflect on the decisions that they have made.

The social costs of consumer choices

Consumption externalities are the costs imposed by a consumer’s choice on members of the consumer’s family or the wider community. These costs include those involved in remedying the adverse consequences of that decision (such as taxpayer-funded medical services where injury has resulted).

Governments sometimes intervene to overrule consumer choices that they judge would have significant negative impacts on the wider community (such as by regulating the consumption of tobacco products). In other cases, government policy may be directed towards promoting socially desirable choices (for example, information campaigns to promote healthy lifestyles).

Moreover, behavioural economics suggests that individual consumers can sometimes benefit from restrictions on their ability to choose. For example, restricted access to addictive products (such as alcohol or gambling) may improve the welfare of some individuals, as well as reducing social costs for the wider community. From this perspective, the information failure and social externalities rationales for intervention overlap.

Achieving social justice outcomes

There is a widely held view that, to promote social justice, disadvantaged or otherwise vulnerable consumers should be assisted to participate effectively in markets, and to prevent them from falling victim to scams and other inappropriate trading practices.

More generally, the concept of ‘fair’ or equitable treatment is fundamental to both consumers’ and producers’ expectations about what is reasonable market behaviour. The findings of behavioural economics (appendix B) suggest that most people in

society value fairness. This is possibly both because they have an inherent regard for the welfare of those who are treated unfairly and out of concern that they might receive the same treatment themselves.

Policy makers have acknowledged the importance of such considerations. According to the Office of Best Practice Regulation (OBPR 2007, p. 129), while standard cost-benefit analyses focus on the efficiency implications of intervening in a market, the

... way in which benefits and costs are distributed among various groups, and over time, can also be important to decision makers. While [cost benefit analysis] cannot resolve equity issues, it can draw attention to them by quantifying the impacts of proposed policies on different groups. If the information is available, a [cost-benefit analysis] can identify potential winners and losers and the magnitude of gains and losses. It is then up to decision makers to decide whether distributional impacts/equity issues are important and need addressing.

To this end, policy makers may sometimes explicitly give greater weighting to losses experienced by lower income earners to reflect the fact that such losses will normally impact on these individuals more than equivalent losses suffered by wealthier consumers. (For an example of this approach, see UK OFT 2000.)

In addition to achieving important social justice objectives, intervention on behalf of vulnerable and disadvantaged consumers can also improve the confidence with which these consumers interact with suppliers, encouraging greater market participation and enhancing overall efficiency.

Protecting consumer rights

In keeping with the approach of Consumers International (box 3.3), a number of inquiry participants argued that the rationale for consumer policy should be based on protection of consumer rights (box 3.4).

Discussion of consumer rights can provide a useful basis for identifying sources of potential consumer detriment. For example, the view that consumers have a fundamental ‘right to know’ is consistent with the previous discussion that consumer welfare can be reduced where adequate product information is not available. As noted above, consumer confidence in the ability to undertake a transaction, including having any perceived rights protected, is fundamental to well-functioning markets. Similarly, a ‘right to safety’ is consistent with policy intervention to correct market failures associated with hidden product risks.

Moreover, there is a substantial overlap between the rights-based approach and the social justice arguments outlined in the previous section. As noted by the Victorian Government (sub. 92, p. 27), while some consumer rights

... can be interpreted in an economic context they also focus on access to justice, fairness and prohibiting levels of harm or disadvantage that the Australian community believes are unacceptable.

In these respects, a rights approach represents a different ‘point of entry’ to the discussion about when governments should intervene to improve efficiency and promote social justice, rather than a completely separate rationale.

Box 3.3 **Consumer rights and responsibilities**

Consumer policy promotes the establishment of legislation, institutions and information that improve quality of life and empower people to make changes in their own lives. It seeks to ensure that basic human rights are recognised, and promotes understanding of people's rights and responsibilities as consumers. These are:

- the right to satisfaction of basic needs
- the right to safety
- the right to be informed
- the right to choose
- the right to be heard
- the right to redress
- the right to consumer education
- the right to a healthy environment.

Consumers also have responsibilities to use their power in the market to drive out abuses, to encourage ethical practices and to support sustainable consumption and production.

Source: Consumers International 2007.

3.3 Government intervention is not costless

Establishing an in-principle rationale for intervention — based on either market failure or social justice grounds — is not by itself sufficient to justify a policy response. Intervention has costs which can be significant and take various forms.

- Businesses incur compliance costs in altering their activities to meet regulatory and other requirements. Variations in these requirements across jurisdictions will magnify these burdens.
- Policies that involve a lessening of market competition (for example, licensing requirements) are likely to diminish incentives for efficiency and innovation.

Box 3.4 Consumer rights: views of inquiry participants

Consumers' Federation of Australia (sub. 83, p. 5) said that:

Our starting point is that consumers in Australia are entitled to:

- fair, effective and sustainable markets;
- affordable and equitable access to essential services;
- protection from unsafe or unfit products and services;
- products and services that are sustainable in terms of their environmental effects;
- fairness in transactions and conduct;
- information and education to assist them in making choices in an increasingly complex market place;
- accessible and effective remedies for failures and breaches of the law;
- active monitoring and enforcement of consumer protection laws;
- input through representative bodies to policy-making that affects their interests.

These rights in effect, become the objectives of consumer policy. Particular focus is required to ensure these principles are a reality for disadvantaged and vulnerable consumers.

Western Australian Community Organisations (sub. 76, pp.16-17), argued that consumer policy could be based on the UN Guidelines for Consumer Protection:

- (a) The protection of consumers from hazards to their health and safety;
- (b) The promotion and protection of the economic interests of consumers;
- (c) Access of consumers to adequate information to enable them to make informed choices according to individual wishes and needs;
- (d) Consumer education, including education on the environmental, social and economic impacts of consumer choice;
- (e) Availability of effective consumer redress;
- (f) Freedom to form consumer and other relevant groups or organisations and the opportunity of such organisations to present their views in decision-making processes affecting them;
- (g) The promotion of sustainable consumption patterns.

The Centre for Credit and Consumer Law (sub. 93, p. 1) argued that consumer policy should be based on the rights identified by Consumers International (see box 3.3) and have fairness, social justice and distribution objectives. It should focus on:

- Facilitating and supporting universal access to essential services on a fair and reasonable basis, including through pricing mechanisms, but also through specific consumer protection measures such as fair practices in the event of default or non-payment.
- Protection from exploitation, unfair practices and unsafe goods and services.
- Facilitating the development of skills to make effective choices, and to identify and avoid unfair practices.
- Clear, concise, comparable and timely information on products and services.
- Access to redress and effective independent complaints and dispute resolution processes.

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- Policies that involve regulating quality can reduce the range of products available in the marketplace.
 - There may also be unintended or perverse outcomes where consumers or suppliers do not behave as expected. (For example, regulated tariffs for energy services may have inadvertently discouraged some consumers from investigating potentially cheaper alternatives — chapter 5).
 - If the institutional and procedural arrangements giving effect to the policy framework are poorly configured, the framework itself can be a source of considerable cost. Lack of responsiveness to changing market and other circumstances and wasted effort in policy formulation and related activities are but two examples.

Ultimately, most of these costs will be borne by consumers in the form of higher prices, less choice and, to the extent that productivity is diminished, through lower incomes. The upshot is that even where an in-principle case for government involvement can be made, these costs may sometimes more than offset the potential benefits of that involvement.

Hence, as elaborated on below, even with commonly agreed objectives, assessing the future benefits and costs of proposed policy interventions will be central in determining whether those interventions would in fact serve to promote the interests of consumers and the wider community.

3.4 Objectives for the consumer policy framework

Clear specification of objectives is fundamental to good regulation. Those responsible for implementing and enforcing regulation — including the judiciary — are guided by its objectives. The more clearly specified the objectives, the more effective the guidance. As previously noted by the Commission (PC 2004c, p. 162):

Decision makers facing conflicting objectives need to exercise discretion to assess the tradeoffs. In matters of law, the judiciary often has to weigh up a range of factors in making a judgment. However, the larger the number of conflicting objectives, the greater is the discretionary element involved in their resolution. As this tends to increase the potential for inconsistent judgements, there are advantages in narrowing the range of, and clearly specifying, objectives.

Clearly-specified objectives are particularly important where there is potential for divergence between the intent of the regulation and the interpretation of its operational criteria (which can occur where, as in the case of consumer policy, implementation involves different regulators and enforcement mechanisms).

Significantly, the Trade Practices Act and individual State and Territory Fair Trading Acts, have differently specified objectives².

Clear objectives, with observable outcomes, also facilitate assessment of the effectiveness of the policy framework and the performance of regulators. And, in addition to providing guidance to regulators and others responsible for enforcement, clear objectives provide greater certainty to consumers and suppliers by identifying behaviours and circumstances which might trigger intervention.

In reinforcing the importance of soundly based objectives in the consumer policy area, AGL Energy commented that:

... a clearly enunciated set of objectives will provide much needed guidance to all stakeholders, particularly regulators and policy makers, leading to a more transparent and consistent consumer protection framework. Such objectives will form a constant reference point against which proposed regulatory and legislative developments can be measured for appropriateness and effectiveness. (sub. DR149, p. 1)

Energywatch UK similarly said that developing a set of clear objectives would be helpful in developing a common understanding of the aims of consumer policy among those making decisions and also those affected by decisions:

We wholeheartedly agree that a set of clear objectives and supporting principles is required to anchor the future development of consumer policy. Much effort and expense can be wasted by the creation of a plethora of regulators and regulations to deal with specific problems. Good consumer policy, we believe, seeks to prevent consumer detriment from occurring and provide speedy remedy when it does. Policymakers, regulators, suppliers and consumers should have a common understanding of what is meant by fair trading in competitive markets and what would constitute a proportionate response when that is not achieved. (sub. DR197, p. 4)

In the draft report, having regard to objectives for consumer policy regimes in other countries, suggestions from participants in initial submissions, and its own analysis of the key issues that the future consumer policy framework should address, the Commission proposed that the overarching objective should focus on ‘promoting the confident and informed participation of consumers in competitive markets in which both consumers and suppliers trade fairly and in good faith’. It further proposed six supporting operational objectives, namely to:

- ensure that consumers are sufficiently well-informed to benefit from, and stimulate effective competition;
- ensure that goods and services are safe and fit for purpose;

² Currently, only the TPA and the FTAs in Queensland and Victoria have a specific objects clause. In other jurisdictions objectives are implied by the long title of the legislation. (Corones and Christensen 2007, p. 25)

Box 3.5 Consumer policy objectives: participants' views

Choice (sub. DR194, pp. 4-5)

Based on the current objectives of the Trade Practices Act, we suggest the following alternative objective for the future policy framework:

“To enhance the wellbeing of all Australian consumers through the promotion of effective competition and fair trading.”

In light of the alternative overarching objective proposed above, it would be appropriate to acknowledge consumer confidence in the operational objectives:

“ensure that consumers are sufficiently well informed and sufficiently confident to benefit from, and stimulate effective competition.”

Finally, despite devoting considerable discussion in the report to the field of behavioural economics...the importance of evidence about how consumers actually behave is not to be found in the proposed operational objectives or supporting principles.

Real Estate Institute of Australia (sub. DR172, p. 3)

... REIA asserts that these objectives should also enshrine common consumer rights and responsibilities. While there is much discussion of consumer protection and empowerment within the Draft Report (which each result in an onus on either business or the regulatory system to facilitate some form of consumer redress), there is precious little examination of the basic responsibilities that should be borne by consumers.

Energywatch UK (sub. DR 197, p. 4)

An alternative formulation of the (overarching) objective is:

“To equip confident and able consumers, acting in fair and informed markets, to look after their own interests and to act on behalf of those who can not protect their own interests.”

Australian Food and Grocery Council (sub. DR150, p. 4)

The AFGC concurs with the key operational objectives described in the Draft Report, but considers further operational objectives should be added:

“flexibility of response measures;
evidence-based foundations for action;
minimal imposition of regulatory burden; and
industry-specific approaches where appropriate.”

Optus (sub. DR173, p. 4) and Australian Mobile Telecommunications Association (sub. DR175, p. 3)

... recommends the inclusion of a seventh formal operational objective:

“Ensure that new regulations are enacted only if they are based on evidence, where cost benefit analysis has determined that a problem exists and that the introduction of regulation would assist, manage or resolve the problem, and where it does not duplicate or overlap with existing regulation.”

Telstra (sub. DR156, p. 2)

... submits that an additional operational objective... should be:

“To encourage investment in products and services that meet consumer needs.”

-
- prevent practices that are unfair or contrary to good faith;
 - meet the needs of vulnerable and disadvantaged consumers;
 - provide accessible and timely redress where detriment has occurred; and
 - promote proportionate, risk-based enforcement.

There was widespread support for the thrust of these proposals in submissions on the draft report, notwithstanding various suggestions to change particular emphases. Moreover, there were many suggestions for additions — a sample of which are reproduced in box 3.5.

After reflecting on this input, and being cognisant of the need to avoid excessive complexity, the Commission has concluded that with some minor reworking, the objectives enunciated in the draft report are fundamentally sound. However, there is merit in the suggestion from several participants (Choice, sub. DR194; Victorian Government, sub. DR226; Joint Consumer Groups, sub. DR228) for explicitly bringing the notion of consumer welfare into the higher level objective. The Commission also supports evidence-based policy development (Australian Food and Grocery Council, sub. DR150; Optus, sub. DR173; Choice, sub. DR194). But this notion is encompassed by the reference in the lead-in to the operational objectives on the need for efficient and effective policy approaches (see below).

The Commission therefore proposes that the following common set of objectives be introduced to guide and shape Australia’s future consumer policy framework.

RECOMMENDATION 3.1

Australian Governments should adopt a common overarching objective for consumer policy:

‘to improve consumer wellbeing by fostering effective competition and enabling the confident participation of consumers in markets in which both consumers and suppliers trade fairly and in good faith’.

To provide more specific guidance to those developing and implementing consumer policy, this overarching objective should be supported by six operational objectives.

The consumer policy framework should efficiently and effectively aim to:

- ***ensure that consumers are sufficiently well-informed to benefit from, and stimulate effective competition;***
- ***ensure that goods and services are safe and fit for the purposes for which they were sold;***

-
- *prevent practices that are unfair or contrary to good faith;*
 - *meet the needs of those who, as consumers, are most vulnerable, or at greatest disadvantage;*
 - *provide accessible and timely redress where consumer detriment has occurred; and*
 - *promote proportionate, risk-based enforcement.*

The overarching objective focuses on the role of consumer policy in delivering better outcomes for consumers; the operational objectives aim to promote interventions that are effectively targeted to the identified problem, minimise costs and unintended side-effects, and have special regard for the needs of vulnerable and disadvantaged consumers.

In the main, these objectives should be uncontroversial since they represent the ‘common ground’ on which the consumer policy framework in Australia currently rests. But they are also consistent with, and supportive of, those reforms — discussed in subsequent chapters — that the Commission considers necessary to carry an effective consumer protection regime into the future.

Specifically:

- *ensuring that consumers in general are sufficiently well-informed to participate in, and benefit from, competition* includes consideration of how to effectively enhance the knowledge base of consumers and remove any obstacles to use of that knowledge (such as those identified by behavioural economics);
- *ensuring that goods and services are safe and fit for the purposes for which they were sold*, encompasses all of the issues surrounding the creation of an effective set of implied terms and conditions and product safety. It involves preventing detriment arising from ‘hidden risks’ or unknown product characteristics;
- *preventing practices that are unfair or contrary to good faith* addresses behaviour by suppliers that fails to meet generally accepted standards and which leads to consumer detriment or otherwise reduces consumer confidence;
- *meeting the needs of vulnerable and disadvantaged consumers* recognises that some consumers face specific obstacles to effective market participation. It also encompasses consumer policy’s social equity goals;
- *providing accessible and timely redress where consumer detriment has occurred* ensures that, where consumers’ reasonable expectations are not met, effective remedies are available; and

-
- *promoting proportionate, risk-based enforcement* involves the effective and efficient enforcement of regulations designed to encourage appropriate supplier behaviour.

And, the requirement that the framework should promote these outcomes in an efficient and effective way encapsulates the notions that the benefits of intervention cannot be considered in isolation from its costs, and that policy makers should have regard to the evidence on how consumers and businesses actually behave.

In many respects, the protections offered by the current regime are comprehensive and many of the tools and policies required to give effect to these objectives are already in place. Indeed, the reach of the framework is illustrated by the extension of its protections beyond household consumers to cover many of the purchases made by small (and other) businesses (see chapter 13).

But as noted above and in chapter 2, significant changes to the current framework are required. In order to further the proposed objectives, these policy changes should be guided by the best-practice principles of policy design and implementation outlined in the next section. These principles should also inform the development and application of consumer policy that involves non-legislative approaches (eg various self-regulatory schemes and non-regulatory tools such as education campaigns).

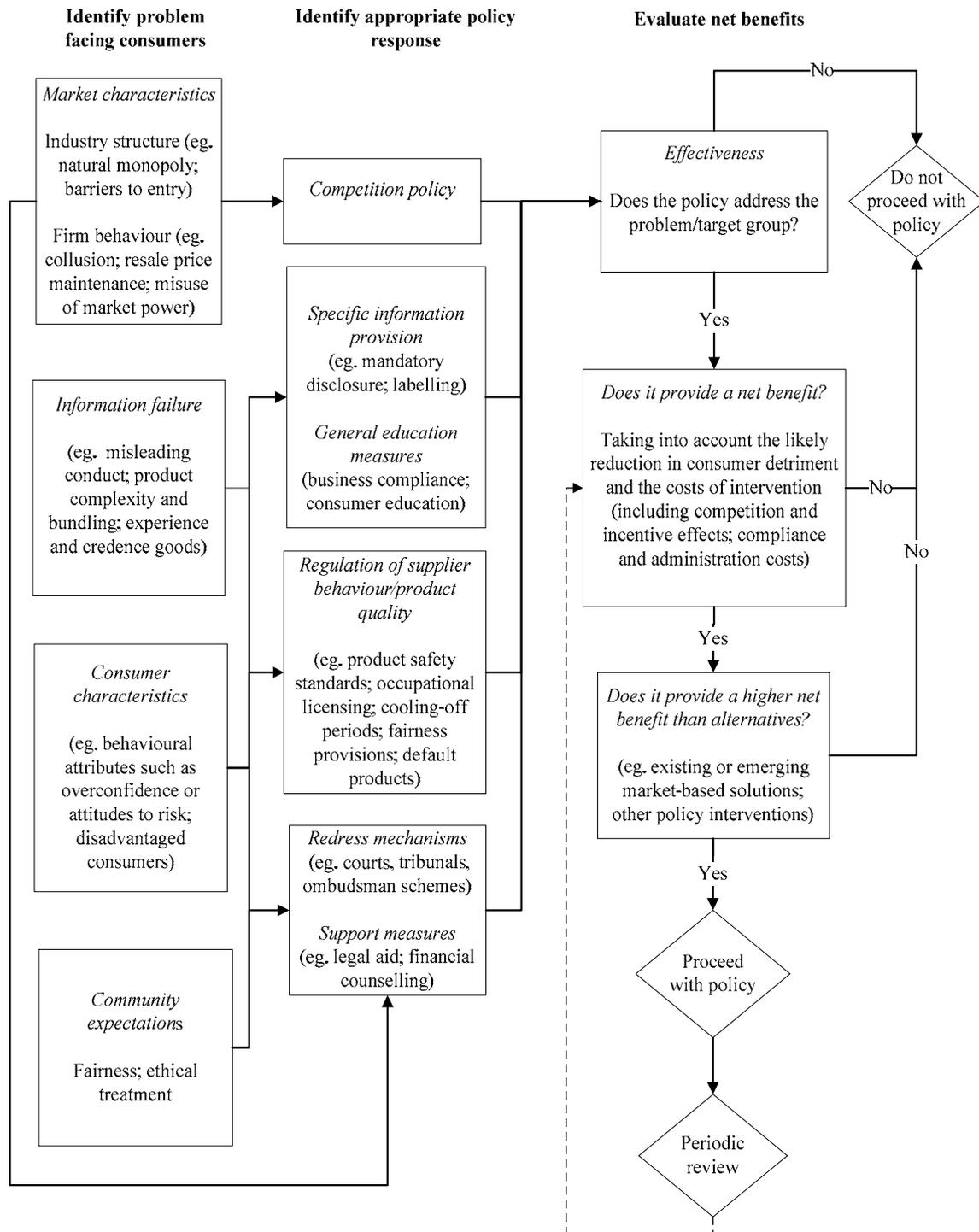
3.5 Identifying and evaluating policy instruments

Broad requirements for identifying effective and efficient policy instruments have been widely explored and documented. The OECD has recently applied these to the specific requirements of consumer policy (see, for example, OECD 2007b). Building on this OECD work, figure 3.1 outlines the approach regulators should take to ensure that any intervention proposed to address a consumer problem is likely to provide a net benefit to the community, and where it passes this test, represents the most effective policy response.

The first step is to carefully evaluate the problem facing consumers. Where possible, estimates of the associated detriment should also be provided. In outlining the features of best practice regulation, the OBPR (2007, p. 58) observed:

To design appropriate and well targeted solutions, the problem should be clearly specified and put in perspective. Otherwise, unnecessary or inappropriate regulation may result or the problem may not be solved. Specification of the problem should include details of its nature and magnitude.

Figure 3.1 Identifying and evaluating policy instruments



While measuring the associated consumer detriment can be difficult (see chapter 14), there are a number of sources of evidence that can be drawn on. These include complaints data, consumer surveys, focus groups and ‘shadow shopping’ exercises such as those recently conducted by ASIC (sub. 103, p. 6). Though not definitive, such measures can at least help to indicate whether the direct costs to consumers — when their reasonable expectations are not met — are significant enough to consider a policy response.

Proper specification of the problems facing consumers, and the objectives of any government action, will in turn assist in identifying appropriate policy responses. Assessment of policy effectiveness should be based on a comparison of relevant alternatives (OBPR 2007, p. 64), including those from outside consumer policy. For example, the most effective response to assist consumers disadvantaged by virtue of low income will typically be through income support — which can be targeted directly at those consumers — rather than through intervening to change the terms or conditions under which goods and services are supplied.

The final step in choosing an appropriate policy intervention is establishing whether it provides a net benefit for the community (taking into account economic, social, environmental and equity impacts) and, if so, whether it provides a higher net benefit than alternative policy responses. This should include consideration of whether the intended objective could be efficiently achieved through more effective enforcement of existing laws rather than through introducing new regulation.

There also needs to be periodic review to ensure that regulation implemented according to these requirements continues to be appropriate as consumer and supplier behaviour adjusts and markets evolve. The importance of regular policy evaluation was acknowledged by CoAG (2006a) in recent amendments to regulation review processes (see chapter 5).

Drawing on the policy development process embodied in figure 3.1, the Commission considers the operation of the consumer policy framework should be based on best-practice principles of policy design and implementation. These include that policy intervention should:

- support and complement the role of competition in improving consumer welfare through:
 - preserving and promoting incentives for consumers to enhance their purchasing capabilities; and
 - reinforcing market incentives for suppliers to effectively meet consumers’ needs.

-
- engender the flexibility required for timely and appropriate adjustment of policies to meet changing market circumstances and consumer and business requirements; and
 - be soundly-based by:
 - focusing on addressing material shortcomings in market outcomes at the lowest possible cost to consumers, businesses and regulators, and with minimum risk of unintended or perverse consequences;
 - providing for cost-effective enforcement, through a layered regulatory response according to the risk/severity of the problem, and ensuring that consumers have reasonable access to alternative low cost dispute resolution; and
 - fostering good regulatory and administrative process, including through periodic review of all policy measures, and avoiding regulatory inconsistencies.

At the operational level, whenever a new policy initiative is contemplated, or an existing measure reviewed, there should be:

- clear identification of the nature and source of the underlying problem;
- quantification, to the extent reasonably possible, of the associated detriment, or prospective detriment, for consumers, or groups of consumers; and
- a comparison of the benefits and costs of all feasible options for dealing with the problem, including relying on market solutions, or employing approaches from outside 'consumer' policy.

4 Generic consumer legislation

Key points

- Greater responsibility for the consumer policy framework should reside with the Australian Government:
 - Australia’s consumer markets are becoming more national in character, with variations in consumer laws and enforcement practices across jurisdictions resulting in unnecessary compliance burdens for businesses and differences in protection for consumers.
 - Mechanisms to promote responsive policy making within the current multi-jurisdictional regime have often been ineffectual, leading to lengthy delays in progressing worthwhile consumer reforms.
 - Given rapidly changing consumer markets, these costs will increase over time.
- Australian Governments should implement a new national generic consumer law. This law should be based on the consumer provisions in the Trade Practices Act, augmented to address areas where the Act is generally agreed not to be adequate to deal with particular generic issues. It should apply in all jurisdictions to all consumer transactions, including financial services.
- The enforcement approach adopted for the new generic law should be the one most capable of delivering effective, consistent and efficient enforcement outcomes.
 - The Australian Government, through the Australian Competition and Consumer Commission (ACCC), should assume responsibility for enforcing the product safety component of the new law as soon as practicable, though possibly with the States and Territories retaining the power to issue interim, time limited, product safety bans.
 - The remainder of the new law should be jointly enforced by the ACCC and State and Territory consumer regulators. But individual States and Territories should have the option of referring their enforcement powers to the Australian Government, with enforcement undertaken by the ACCC.
- These enforcement arrangements should be reviewed within ten years, with explicit consideration of the case for moving to a single national regulator model for all of the generic consumer law, having regard to:
 - any evidence that differing enforcement practices or regulatory ‘break-out’ are leading to divergent outcomes for consumers and businesses across Australia;
 - outcomes in any jurisdictions that have referred their enforcement powers for all of the generic law to the Australian Government; and
 - the implications of shifts in enforcement responsibility for specific consumer regulation to the Australian Government.

Responsibility for the development and enforcement of Australia’s consumer laws is split between the Australian and State and Territory Governments. This delineation of responsibility has some advantages. However, as highlighted in many submissions to the inquiry (box 4.1), it also gives rise to problems and costs for consumers and businesses, including inconsistencies in regulatory requirements and their enforcement and a lack of policy responsiveness to changing market circumstances and consumer needs.

Against this backdrop, the next three chapters outline the case for the creation of a more nationally-coherent consumer policy framework.

- This chapter examines the broad case for a greater emphasis on national policy approaches to consumer regulation and sets out how this should be achieved for the generic consumer law.
- Chapter 5 maps out a process for reviewing industry-specific consumer regulation directed at:
 - identifying and repealing unnecessary specific consumer regulation;
 - identifying other areas of State and Territory specific consumer regulation where differences in regulatory requirements, or lack of policy responsiveness, are particularly costly for consumers and businesses; and
 - determining how these costs should be reduced, with explicit consideration of the case for transferring policy responsibilities to the Australian Government.
- Chapter 6 looks at some additional measures that could help to build support for the new framework, and to facilitate timely implementation of the proposed reforms and more responsive future policy development.

4.1 The need for a more nationally coherent approach

In considering future arrangements for both generic and industry-specific consumer law, the appropriateness of the current division of responsibilities between the Australian and State and Territory Governments is a paramount issue.

There are advantages from State and Territory involvement

As in other policy areas, consumer policy priorities and requirements will sometimes differ across jurisdictions. For example, catering for Indigenous consumers will be a greater issue in Queensland, Western Australia and the Northern Territory than elsewhere; building standards will necessarily vary across the country depending on climatic factors; and jurisdictional differences in the use of some consumer products and services, or in their method of sale, may similarly call for divergent policy and/or enforcement approaches.

Box 4.1 **Participants' views on the current delineation of responsibility**

State Governments, in particular, pointed to the benefits of the current sharing of responsibility for consumer policy development and enforcement. For example, the Victorian Government emphasised that:

The consumer policy framework in Australia needs to take into account the national nature of many consumer markets and subsequently balance nationally consistent approaches with the need for policies that can engage directly with individual consumers and respond quickly and flexibly with innovative solutions when new problems emerge. (sub. 92, p. 6)

And the Queensland Government said that:

... the current framework provides the flexibility for Queensland to respond to regional, industry or marketplace specific issues where necessary. There is also a culture of competitive regulation allowing States and Territories the ability to adopt regulatory innovations from other jurisdictions where necessary and tailor regulation to suit local conditions. ... broad administrative networks ... enable local State and Territory officials to quickly detect and respond to emerging problems such as a dangerous product entering the market. (sub. 87, pp. 28-29)

However, many other participants contended that the current division of responsibilities has led to slow policy development and unnecessary compliance costs for businesses, leading to higher prices for consumers.

Australia's consumer policy framework has failed to develop to reflect the fact that our market is now overwhelmingly national in character. Federal/State responsibilities in this area are by and large accidents of history rather than sensible divisions based on careful assessment of consumer markets and regulatory capacities. The Federal/State split of responsibilities slows policy making processes and frustrates businesses and consumers. In general, inconsistencies between different jurisdictions are undesirable as inconsistency causes uncertainty and confusion for business and consumers. For businesses trading across State boundaries – many of the major players in key consumer industries – this means additional compliance costs which in turn means increased prices for consumers. (Choice, sub. 88, p. 42)

The pace of legislative change ... has been painfully slow. ... there are numerous examples of changes which have been agreed to in principle and have unilateral support but which have taken, or are taking years to implement. (Consumer Credit Legal Centre, sub. 95, p. 40)

The developmental process and timeliness of government policy development in consumer protection is of particular concern to the REIA. ... the ... process is generally much too slow to respond to rapidly emerging consumer issues, sometimes resulting in a 'stop gap' piecemeal approach by various jurisdictions awaiting outcomes. Despite being on the [Ministerial Council for Consumer Affairs] MCCA agenda, there is sometimes no practical solution implemented for many years ... (Real Estate Institute of Australia, sub. 39, p. 9)

Currently consumer regulation is extremely burdensome for retailers with myriads of enforcement agencies, multiple statutes, inconsistencies across states, and multiple licensing systems. Poorly designed regulation not only leads to excessive compliance costs, but in some cases may be the cause of non compliance. (Australian Retailers Association, sub. 71, p. 4)

As the South Australian Minister for Consumer Affairs (sub. DR219, p. 3) amongst others emphasised, the current sharing of policy responsibilities can also facilitate policy experimentation and learning (see box 4.2).

Box 4.2 Policy experimentation in the consumer policy area

Some previous important innovations in consumer policy have emerged from single jurisdictions. For example, the consumer provisions of the Trade Practices Act (TPA) and the Contracts Review Act (NSW) provided real-world evidence on the impacts of enhanced consumer protections. Subsequently, the new provisions of the TPA were adopted by the States and Territories, and the Contracts Review Act influenced the later enactment of unconscionability provisions in the TPA. More recently, some have argued for wider application of Victoria's unfair contract provisions, which are themselves based on UK laws (see chapter 7). Also, as the Victorian Government (sub. DR226, p. 20) noted, failed policy experiments can sometimes provide useful policy guidance and prevent widespread application of inappropriate requirements.

Given rapidly changing consumer markets, there could in future potentially be further benefits from policy experimentation at the jurisdictional level.

But the divergences in regulatory requirements that ensue from such experimentation have costs for businesses and ultimately consumers (see text). Because of this, the current system is heavily geared towards maintaining consistent policy approaches. Indeed, given the increasingly national nature of consumer markets, businesses will often respond on a nationwide basis to new regulations introduced in a single jurisdiction (Samuel 2007, p. 7). Hence there is probably now less scope to conduct significant policy experiments at the jurisdictional level, or to isolate their impacts in policy evaluation exercises.

In addition, while some national consumer regulators such as the ACCC have a presence at the regional level, a number of participants perceived that state-based regulators will be able to apply consumer laws to local issues in a more timely fashion. And, there are synergies between the generic and industry-specific enforcement functions of State and Territory consumer regulators, and also with other State and Territory bodies involved in the application of those laws. In the latter case, for example, criminal prosecutions for contraventions of consumer laws require the assistance of police and judicial services. And even more 'routine' enforcement matters may sometimes be assisted by cooperation with other State and Territory agencies.¹

¹ For instance, the Victorian Government reported that in early 2007, faulty valves were identified on a number of LPG gas tanks. The majority of the faulty valves were distributed in Victoria, so in conjunction with VicRoads, Consumer Affairs Victoria issued public warning notices and sent letters to all owners of LPG vehicles (sub. 92, p. 95).

These sorts of advantages are recognised in various aspects of the current consumer policy framework. In particular, in enforcing the generic consumer law, the State and Territory Fair Trading Authorities largely focus on local issues, while the ACCC concentrates on more nationally significant issues. As the Chairman of the ACCC, Graeme Samuel, recently said:

... many consumer issues arise on an individual or local basis, whether the issue is one of breach of the law or resolvable misunderstandings between consumers and traders. In aggregate these issues are no less important to the overall well being of consumers. Accordingly within a uniform legislative framework there's still an important role for State and Territory Fair Trading Agencies, particularly in dealing with local issues and assisting consumers to obtain fast effective justice in individual cases. (2006, pp. 7-8)

But this does not mean that the current framework is appropriate

The benefits of policy development and enforcement by lower level governments often leads some to presume that responsibility should reside with the lowest level of government able to effectively meet policy objectives. This is commonly known as the subsidiarity principle (see Victorian Government, sub. 92, p. 92).

Yet, on its own, the subsidiarity principle cannot give a definitive answer on what level of government should have responsibility for consumer policy. The subsidiarity principle recognises that lower level governments should only have responsibility if they can deliver effective policy. This requires an examination of the benefits and costs of alternative arrangements. Overseas experience suggests no obvious default level of government responsibility: in the United Kingdom and New Zealand a national government is primarily responsible; while in the United States and Canada, state and federal governments have overlapping responsibilities.

Accordingly, in assessing how Australia's future consumer policy framework would be best configured, the choice is not between two polar extremes. Rather, the issue is whether it would be desirable to alter the current balance of policy and enforcement responsibilities across the two levels of government — and, in particular, whether shifting more responsibility to the Australian Government would mitigate some of the costs of the current regime, without putting the welfare of consumers at risk. In the Commission's view, there are good reasons to believe that such a shift would be beneficial.

Australia's consumer markets are becoming more national

A sizeable share of goods and services (in 2007 around 48 per cent, measured by turnover) is supplied by firms that operate across jurisdictions. This proportion ranges from 21 per cent in personal and other services to 87 per cent in communication services. Moreover, in the retail trade sector, for which substantial

time series data is available, the proportion has increased from 47 per cent to 53 per cent since 1998 (ABS, unpublished data). And since 2003, the number of businesses operating in every State and Territory has increased by over 70 per cent (ABS 2007c).

In large part, the increasingly national nature of consumer markets reflects the broad similarities in consumer demands across Australia and hence the opportunities for suppliers to realise economies of scale by operating in multiple jurisdictions. An indication of these demand similarities is that consumers' spending patterns are much more influenced by factors such as age, income and family type than by where they live (figure 4.1). (Some other reasons for the continuing trend towards national markets are discussed in box 4.3.)

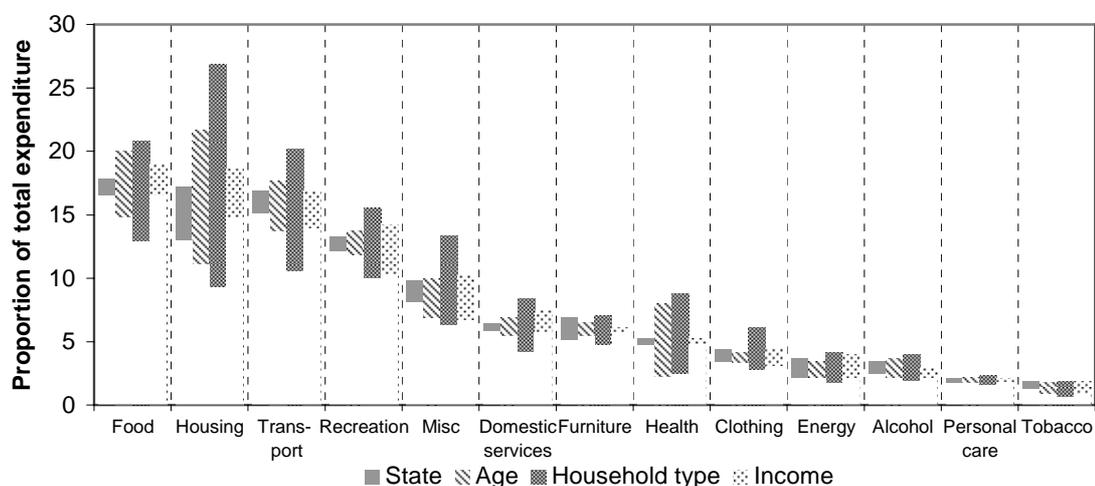
The 'mismatch' in markets and policy responsibility raises costs

While multiple consumer policy regimes that facilitate tailored application may benefit some consumers, in an increasingly national market environment, they also impose costs on consumers as a whole. In particular, superimposing multi-jurisdictional and somewhat divergent policy regimes on those suppliers servicing the Australian market (or large parts of it) raises their costs of doing business. Apart from the added compliance costs, variations in requirements may reduce opportunities to realise economies of scale through centralising functions. A large part of these cost increases will be passed on to consumers in the form of higher prices.

Various examples of needless variation or prescriptive differences in requirements are provided later in this chapter, in subsequent chapters and the appendices to the report. Suffice to say, that the problems arise across a wide range of consumer goods and services. For example, the Australia New Zealand Working Group on Trans-Tasman Competition & Consumer Issues (ANZTTCCI, sub. DR179, p. 2) pointed to compliance costs burdens from divergent regulatory requirements for food, tobacco, lay-by sales, charitable fundraising, lotteries and trade promotions, telephone marketing, door-to door-sales and trade stamps. Indeed, in some cases, suppliers apparently must choose between competing requirements. According to the Australian Compliance Institute (sub. DR128, p. 2):

This is most prevalent within the food retailing sector of the economy. This in turn gives rise to a form of 'regulator roulette' where organisations are forced to choose which state based agency to comply with and which to be in breach of. This decision is usually made on a risk minimisation basis by electing to comply with the regulator that can inflict the most 'harm' on the organisation in question by way of penalties for the infringement.

Figure 4.1 **Ranges of average consumer expenditure as a percentage of total expenditure^a**



^a The expenditure shares in the figure portray the range of spending across different categories of consumers. In the case of food, for example, the range of expenditure shares by State is around 1.5 per cent of total average spending, compared to variations of 5 per cent, 7 per cent and 3 per cent by age, household type and income, respectively. Figures reported for States only. Household types include single person, couple with no children, couple with dependent or non-dependent children and retirees.

Data source: ABS 6530.0 Household Expenditure Survey, Summary of Results.

Box 4.3 **Other contributors to more national consumer markets**

In addition to similarities across Australia in the nature of consumer demand, several other factors have played a role in the trend towards national consumer markets:

- The removal of foreign trade barriers has led to a large expansion in imports of consumer goods and services. (Since 1988, the value of imported consumer products has nearly tripled in real terms, ABS 2007a.) These imported products will typically be supplied nationally, or at least to the eastern states.
- Technological changes have added to the economies of scale available to larger suppliers. For instance, innovations in supply chain management (enabled by the greater use of computers) have led to an expansion in national chain stores that supply groceries, white goods and hardware (Johnston et al 2000, p. 8).
- In some sectors, barriers to multi-State operations have been removed or reduced. For example, in the 1990s, the Australian Government assumed responsibility for corporations regulation, competition policy and the regulation of financial institutions.

Moreover, even in the large majority of cases where the substance of the law is common across jurisdictions, differences in regulatory interpretation, or in enforcement priorities, can have similar cost raising effects. For example, several energy service providers referred to the costs ensuing from differences in ‘quasi’ regulatory guidelines governing the activities of jurisdictional regulators.

For individual suppliers, such costs may often be quite modest and therefore difficult to separately identify — though Woolworths (sub. DR180, p. 1) said that its experience in the retailing area was that the compliance cost burden of divergent and sometimes inconsistent regulatory requirements is significant, with no apparent consumer benefit. And even if the costs for individual firms are often modest, this does not mean that the collective imposts from variations in the consumer law can be dismissed as unimportant, with some referring in this context to the ‘tyranny of small differences’.

Further, businesses must first grapple with these differences either when they are beginning a business or expanding into new markets. Given the other matters that they must deal with at these times, the opportunity cost of determining the substance of numerous small differences and what, if any, variations in compliance strategies are required, can be high. Even where there are no regulatory differences, some suppliers confronting multiple policy regimes may still incur costs in satisfying themselves that this is in fact the case.

There may also be some less direct costs of jurisdictional differences in consumer law or its interpretation and enforcement. As well as potentially reducing compliance with the law, divergent requirements:

- may have greater proportionate effects on small businesses (with the Small Enterprise Telecommunications Centre claiming that they make interstate transactions a ‘nightmare’ (sub. DR168, p. 2)); and
- could conceivably deter new entry and thereby diminish competition in the markets concerned. Though no specific examples were provided to the Commission, especially for overseas suppliers with choices about where to focus marketing effort, even a small added burden may be influential on decision making at the margin. Notably, New Zealand businesses have reported that variations in State and Territory consumer laws increase their costs considerably (ANZTTCCI, sub. 105, p. 2).

The current arrangements penalise consumers in other ways

A further consequence of the current division of responsibility for consumer policy is that the protections and redress options for consumers confronting the same problem can depend on where they live. Anecdotally, the per capita costs of

applying consumer regulations are sometimes higher in smaller jurisdictions than in larger ones, contributing to observed differences in enforcement ‘intensity’ around Australia. Such differences detract from fairness in outcomes and also from consistency in the signals to consumers and businesses about their rights and responsibilities. And the duplication of overheads inherent in any multi-jurisdictional regulatory regime is an additional burden on consumers as taxpayers.

Most importantly, under the current regime, there is often a need to secure agreement from nine jurisdictions for changes to policy settings. Through MCCA and related coordination mechanisms, governments have sought to ensure that this requirement does not unduly impede responsive policy making. However, a widely held view is that these arrangements have often been ineffectual, with the ensuing lack of policy responsiveness creating the potential for significant detriment for consumers across Australia. In pointing to this lack of responsiveness, the Real Estate Institute of Australia (trans. p. 284) observed:

... in August of 2003 as a result of the Henry Kay activities, MCCA, quite rightly in our view ... decided to review licensing of property investment advisers ... in March 2007 we are still waiting on the report from MCCA, nearly four years after the event. This is simply not good enough, and the reasons for this inactivity should be addressed.

Similarly, Choice (sub. 88, p. 92) said:

Even reasonably simple changes have taken far too long. For example, the low threshold for hardship variations in the credit code, originally set in 1996 at \$125 000, took many years to be adjusted despite the rapid increase in housing prices throughout Australia ... for eight years only consumers with mortgages or other consumer loans below \$125 000, well below average house prices, were eligible to apply for hardship relief or postponements of enforceable proceeding under the credit code.

In fact, many of the specific issues that have been raised in MCCA meetings over the last decade ostensibly remain unresolved (table 4.1), in some cases several years after they were first considered².

The Victorian Government (sub. DR226, p. 35) said that while not reported in MCCA communiqués, some of the matters listed as unresolved in table 4.1 have in fact been finalised, and that some others are of an inherently ongoing nature. Along with several State and Territory Governments, it also pointed out that MCCA must contend with a range of external constraints on timely decision making even when, as is often the case, there is agreement on the nature of the policy change required.

² For example, after referring the issue of credit card overuse to the Uniform Consumer Credit Code Management Committee in 2000, MCCA did not comment on the matter again until 2006, when it stated that it would soon announce some proposed regulatory options (MCCA 2006a). In 2007, MCCA said that it was still consulting stakeholders on this issue (MCCA 2007a).

Table 4.1 MCCA's progress on consumer issues

<i>Meeting</i>	Jul 2000	Jul 2001	Aug 2002	Aug 2003	Aug 2004	Apr 2005	Sep 2005	May 2006	Sep 2006	May 2007
Antique cots	⊖									
Auzshare						⊖				
Baby walker standard			⊖							
Banking issues	→	⊖								
Car rental	→		→							
Commonwealth Games						⊖				
Comparison rates	→		→							
Consumer policy review									→	→
Consumer research						→	→	⊖		
Cooperatives legislation							→	⊖		
Credit cards	→	→						→	→	→
Credit providers and EDR								→		
Cross jurisdictional issues		⊖						⊖		
Education and information										⊖
Electronic equipment review									⊖	
Electronic/mobile commerce	→		→		⊖			⊖		
Enforcement consistency					⊖					
Ethanol in fuel				⊖						
Event ticketing		→								
Finance brokers				→	→				→	→
Frequent flyer points	⊖									
Fundraising									⊖	
Future directions								→		
GST	⊖									
Home building insurance		→	→					⊖		
Inbound tourism operators							→			
Indigenous consumers			→	→	→	→	⊖			
Infomercials			⊖							
Mobile phone contracts		→	→	⊖						
Mobile phone radiation	⊖									
National trade measurement					→			→	→	⊖
Overseas mail scams		→	⊖							
Pay day/Fringe credit	→	→	→							
Personal property securities										⊖
Petrol		⊖								
Prams and strollers										⊖
Premium rate telephone services						→	⊖			
Product safety policy				→	→	→	→	→	→	→
Property investment advice				→	→	→	→	→		
Residential tenancy databases				→					→	
Reverse mortgages										→
Smash repairs							⊖			
Telemarketing								⊖		
Temp. compensation for petrol		→	⊖							
Travel agents	→									
Travel compensation fund			⊖					⊖	→	⊖
Two-part pricing						⊖				
Unfair contract terms			→	→	→	→	→	→		
Victorian credit review								⊖		
Weighting instruments	⊖									
Wine labelling						→				
Youth education					→	→	⊖			

Key: → Matter raised and future consideration proposed
 ⊖ Decision made/No future action required (Note: decisions on electronic/mobile commerce, homebuilding insurance, mobile phone contracts, and prams and strollers were taken out of session)

Sources: MCCA (2000, 2001, 2002, 2003, 2004c, 2005b,c, 2006a,b and 2007c).

These governments also argued that, on occasion, the Australian Government or national regulatory impact statement requirements, have been the source of delays.

But while such explanations could well be accurate, they are unlikely to be of much consolation to those consumers who have suffered detriment as a result of MCCA's shortcomings — shortcomings that were conceded by the Victorian Government (sub. DR226, p. 32). Quite simply, unless the various constraints on timely decision making by the Council can be significantly reduced (see section 6.3), then policy inertia will continue to be a significant cost for consumers under the current institutional and regulatory framework.

A more nationally coherent approach is needed

The most appropriate *precise* delineation of responsibility for the future consumer policy framework between the Australian and State and Territory Governments is a matter that can be reasonably debated. In some areas, fine judgements will be involved.

But what is clear, is that the benefit-cost calculus for the current delineation of responsibilities is now different from even a decade ago. The increasingly national nature of consumer markets; the gradual — but now substantial — shift away from the largely consistent generic consumer law agreed to in the 1980s; and the often ineffectual processes to facilitate timely policy change; together mean that the current framework has become more costly for consumers and businesses, with few or no counterbalancing benefits.

Moreover, these costs will almost certainly continue to rise.

- The trend towards more national consumer markets means that the burden imposed by divergent regulatory requirements will grow.
- The increasing pace of change in many of those markets means that the detriment for consumers from unresponsive policy making will escalate.

Indeed, it is notable that the current approach in the consumer policy area stands apart from the largely national approach for many other key arms of policy governing the commercial operations of firms — such as corporations law, business taxation and industrial relations arrangements, and anti-competitive conduct rules. As such, it is likely to detract to some extent from the role of these other policy arms in fostering the further development of national markets and the attendant price, choice and productivity benefits that this will deliver for consumers.

The need for a nationally coherent policy framework to accommodate these sorts of developments has been recognised by MCCA (2007c) which has committed to,

‘nationally coordinated and consistent policy development and implementation by all jurisdictions.’

Yet despite this commitment, based on past experience, the likelihood of a nationally coherent consumer framework emerging under the current delineation of responsibilities and associated regulatory apparatus is not promising.

- In the absence of change, there will almost certainly be new divergences in policy approaches and regulatory requirements across the jurisdictions, adding to the unnecessary costs imposed on consumers, businesses and the community.
- Given past difficulties of progressing even quite minor policy reforms, the capacity of the current regime to deliver timely responses to the significant policy challenges that lie ahead is highly questionable. And without such timely responses, there is the risk that some governments will rely on unilateral changes to their consumer laws, adding further to divergences in approach.

Accordingly, in the Commission’s view, a more nationally coherent policy framework is required, with the location of greater responsibility for the framework with the Australian Government being a pre-requisite for achieving this. In the next section and the subsequent two chapters, the Commission has mapped out what it considers is required in this regard for both generic and industry-specific consumer regulation.

4.2 The case for a new national generic consumer law

The generic consumer law is currently implemented through nine separate pieces of legislation (the TPA provisions plus those in the eight State and Territory Fair Trading Acts) and enforced by nine regulators (the ACCC plus the eight lead State and Territory consumer regulators). In addition, the *Australian Securities and Investments Act 2001* (ASIC Act) — enforced by ASIC — applies the generic law to financial services.

Much of this law is broadly consistent. In some form, all jurisdictions include provisions relating to misleading or deceptive conduct, implied terms and conditions and related enforcement powers.

Nonetheless, a report commissioned for this inquiry demonstrates that there are a large number of small differences in these generic requirements, including across the definitions of a consumer and the application of implied terms (box 4.4).

Box 4.4 Variations in the generic consumer law

For this inquiry, the Commission engaged two legal experts to compare generic consumer laws across Australia. Their report (Corones and Christensen, 2007) demonstrated that Australian consumer laws are far from uniform. For example:

- Only three of the generic consumer acts (the TPA, and the Victorian and Queensland Fair Trading Acts) have a formal objects clause guiding the application of consumer laws.
- The definition of a 'consumer' varies between jurisdictions. Some of the legislation relies on an ordinary use test, where a person who acquires a good or service is a consumer if the price is under \$40 000 or, if the price exceeds \$40 000, the good or service is of a kind ordinarily acquired for personal, household or domestic use. In other cases, a purpose test is applied, and a consumer is anyone who acquires a good or service that is not re-sold or used in a production or manufacturing process.
- Only the TPA and the New South Wales and Northern Territory Fair Trading Acts expand implied conditions and warranties to consumers who may not have a contractual relationship with the supplier.
- In Queensland, Tasmania and the ACT, implied conditions and warranties apply to 'sales', rather than supply, of goods, so leased goods may not have implied conditions and warranties in some circumstances.
- Unlike most State and Territory regulators, the ACCC does not have the power to require the substantiation of claims made in the promotion of goods and services.

Moreover, recently, some significant differences have emerged. For example:

- In 2003, Victoria unilaterally enacted legislation prohibiting unfair contract terms (chapter 7).
- Recent changes to the regulation of telemarketing sales have led to substantial inconsistencies between New South Wales and Victorian regulation, including in relation to variations in the scope of the regulation, permitted call times, disclosure requirements, cooling-off periods and penalties.

Differences in enforcement intensity and/or priorities at the jurisdictional level (see section 4.3) can similarly lead to divergent requirements for businesses (and variable outcomes for consumers).

The costs of divergences in the requirements or application of the generic law should not, of course, be overstated. Even the more significant differences may not require businesses to employ tailored compliance strategies. Anecdotally, many businesses comply with most of the generic law by simply adhering to ethical standards. And where specific compliance measures are called for, meeting the most stringent provision may avoid the need for differential strategies.

Nonetheless, as recognised above, the cumulative costs of even individually small differences can be material. And because many of them are seemingly needless, they can also be a source of significant frustration for businesses. For example:

- In Victoria, the definition of merchantable quality includes a range of non-exhaustive considerations (such as price or the terms of supply) that are not explicitly identified in the TPA or other Fair Trading Acts.
- In South Australia, businesses are prohibited from advertising goods with a purchasing limit (eg, 3 per customer).
- Though companies engaging in door-to-door selling must in all jurisdictions give consumers a form outlining their scope to cancel a contract, in the ACT, this form must additionally be read aloud to the consumer.

More importantly, a continuation of the recent regulatory ‘break-outs’ will see the compliance burden increase in the future. The burden may inimically also increase as unnecessary specific consumer regulation is repealed (see recommendation 5.1) and the generic law becomes the sole means of protecting and empowering consumers in a wider range of areas.

In any event, the considerations in section 4.1 suggest that there is little reason for *any* variation in the content of the generic consumer law.

- The generic law reflects broad notions of efficiency, fairness and equity, which the vast majority of consumers and businesses would regard as appropriate and reasonable irrespective of where they live or trade.
- The broad, principles-based, nature of the generic law allows for its application to a wide variety of particular circumstances. This largely removes any case for variations in the *law* itself to account for specific local requirements.

Indeed, the desirability of a uniform generic consumer law is not controversial. The first review of the TPA (the Swanson review of 1976) argued that:

... uncertainty and confusion arises when different laws ... attempt to deal with the same matter, even if in a slightly different manner only. ... Marketing of goods in Australia is commonly organised on national, or at least multistate, basis. The costs of current legal compliance programs, are unnecessarily high. Marketers should not need to consult up to nine different authorities to plan their compliance programs. (Swanson et al. 1976, p. 59)

These propositions led to efforts to harmonise generic consumer laws in the 1980s and all governments continue to agree to the principle of consistency, summed up by one of MCCA’s strategies, which is to facilitate and encourage:

... nationally coordinated and consistent policy development and implementation by all jurisdictions, including legislative consistency of major elements of consumer protection law and emerging policy issues. (MCCA 2007c, p. 1)

Taking all of these factors into account, in the Commission's view, the intrinsic case for introducing a single national generic consumer law applying across Australia is compelling. Importantly, this would be a readily implementable first step in developing a regulatory regime that better matches the increasingly national nature of consumer markets and commercial arrangements generally. It could also facilitate efforts to deliver the same sort of national focus in industry-specific requirements — a much more complex and time consuming process (see chapter 5).

Responses to the draft report

Responses to the draft report indicated that there is strong support from consumer, business, legal and regulatory interests for the introduction of a new national generic law. (See for example, ACCC, sub. DR176, p. 3; AGL Energy, sub. DR149, p. 2; Anglicare, sub. DR191, p. 3; Choice, sub. DR194, p. 3; Joint Consumer Groups, sub. DR228, p. 4; Law Council of Australia, sub. DR225, p. 2; Optus, sub. DR173, p. 4; and Suncorp, sub. DR171, p. 5.) And while the South Australian Minister for Consumer Affairs (sub. DR219, p. 6) argued that a new national generic law is unnecessary to 'ensure appropriate consistency', the Victorian Government said that:

... needless variation in the generic laws across jurisdictions does not benefit anyone. For these reasons, the Victorian Government supports the introduction of a national generic consumer law. (sub. DR226, p. 19)

The ACT Government (sub. DR250, p. 3), the Department of Consumer and Employment Protection of Western Australia (WA DOCEP — sub. DR248, attachment p. 2) and the New South Wales Government (sub. DR251, p. 2) similarly supported implementation of a new national law.

However, a number of participants emphasised that the new law should be based on 'best practice'.

- Most of these were concerned to avoid a lowest common denominator approach that diminished the protections currently provided to consumers in some jurisdictions, with the Victorian Government saying that the new law should be 'the best of breed'. In a similar vein, the Joint Consumer Groups (sub. DR228, p. 14) argued that protection for consumers across Australia should be 'brought up to the standards achieved in proactive jurisdictions.'

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- Businesses including Telstra (sub. DR156, pp. 2-3) also argued for a best practice set of requirements — though in their case with the goal of avoiding a highest common denominator approach.

And, while supporting a national generic law, the Victorian Government (sub. DR226, p. 21) advocated scope within that law for jurisdictional experimentation ‘in approved circumstances’.

The TPA should be the ‘stepping off’ point for the new law

The Commission considers that, for the most part, the thrust of the current generic law is broadly appropriate and not in need of major overhaul. For the most part, its provisions are formulated in a sufficiently general way as to provide considerable scope to deal with changing market circumstances and consumer needs. Hence, the Commission does not accept the contention from WA DOCEP (sub. DR248, attachment p. 3) and some others that the current law is outdated. Rather, as outlined in subsequent chapters, what is required is some augmentation and other modification in a relatively small number of specific areas.

The Commission agrees that the new law should embody the most appropriate regulatory principles and requirements rather than simply replicating those in any one of the contemporary pieces of generic law. Equally, it would not be sensible to develop the new law through a ‘line by line’ consideration of the existing pieces of multi-jurisdictional legislation. Given the myriad of minor differences in that legislation, this would be a time consuming and costly process, with minimal impact on the effectiveness of the new requirements.

A more practical approach would be to start with the TPA — the foundation for all of the existing generic laws — and then augment or modify its requirements where there is general agreement that they are not adequate to deal with particular issues. Thus, in addition to the proposed inclusion of a new provision governing unfair contract terms (see chapter 7), the Commission is recommending that the new law include a wider range of enforcement tools than provided for in the TPA (see chapter 10). (As a single law, it would also eliminate the current variations in penalties for regulatory breaches.)

Moreover, some other augmentations to reflect existing requirements in State and Territory Fair Trading laws may be warranted. Provisions to deal with mock auctions (see chapter 7) and door-to-door selling are possible examples — though the Commission has not looked in any detail at the latter. In addition, consideration should be given as to whether the new national law should include the product liability provisions contained in the TPA, but not in the State and Territory Fair

Trading Acts. Though inclusion would extend the application of these provisions to non-corporate entities and others currently falling outside the remit of the TPA, in the Commission's view, this could be appropriate.

But whatever the precise requirements agreed to for the new law, it is critical that those requirements are uniform across Australia. Quite simply, there is no place for policy experimentation by individual jurisdictions in relation to these overarching regulatory requirements. And, as emphasised by several participants, implementation of the law should seek to avoid regulatory overlays and conflicts with other regulation impacting on firm conduct. Specific implementation approaches to promote these objectives are considered in section 4.4.

4.3 Who should enforce the new generic law?

Consistent with the high level objectives for consumer policy enunciated earlier, the enforcement approach adopted for the new national generic consumer law should be the one most capable of delivering effective, consistent and efficient enforcement outcomes. Against these criteria, the two broad options — a single national regulator or the current approach of separate regulators in each State and Territory plus the ACCC — each have pluses and minuses. The choice between the two is finely balanced.

The competing considerations and trade-offs

The main advantages of the one regulator model are that it should help to:

- ensure that the intent of the single law in promoting consistent treatment for consumers and businesses across the country was not undermined by unwarranted variations in enforcement approaches or intensity at the jurisdictional level. Though the extent of variation in enforcement approaches with respect to the generic law has been debated by inquiry participants, it seems clear that enforcement intensity differs somewhat across jurisdictions;
- preclude wasteful duplication of regulatory effort where the same issue is needlessly pursued by more than one regulator. For example, a national retailer told the Commission that the New South Wales Office of Fair Trading had raised a misleading or deceptive conduct matter, unaware that the issue had already been resolved with the ACCC; and
- allow for the linkages between consumer and competition policy to be reflected in all enforcement of the generic consumer law, rather than only in the ACCC's more limited current enforcement remit in the consumer policy area.

Further, the Commission is sceptical about the contention that a single national regulator would be intrinsically less well placed or inclined to apply the new national generic law to local issues. Under the current regime, the ACCC's focus has sensibly been on applying the consumer provisions in the TPA to nationally significant issues. But there is no inherent reason why an appropriately tasked and resourced national regulator could not effectively apply the new law at the local level.

- There are many instances where this happens overseas — in some cases, in countries with many more consumers than in Australia.
- Within Australia, national dispute resolution services such as the Banking and Financial Services Ombudsman deal with local problems, apparently successfully.
- And in delivering government services, Australian Government entities such as the ATO, Centrelink and Medicare have a strong local presence.

Indeed, the ACCC indicated that it has sometimes taken enforcement action on local issues where lack of resourcing has prevented a State and Territory from doing so (trans., p. 716).

However, the multiple regulator model does have one important advantage. There are synergies (economies of scope) between the role of State and Territory Fair Trading Authorities in enforcing the generic consumer law and their other regulatory roles, including the enforcement of various industry-specific laws. For example, the current regime allows for the combination of investigative actions where breaches of more than one set of laws are involved. In elaborating on the benefits of such combination, WA DOCEP commented that:

In practice many enquiries and complaints involve both generic and industry specific laws. Often the most effective redress for an industry specific matter (eg a motor vehicle complaint) will be under generic law, not the industry specific law. The separation of responsibility for the administration of generic and industry specific laws would create new problems in coordination and cooperation between the ACCC and DOCEP (problems that would be reflected in other jurisdictions) and work against the concept of a one-stop shop for consumers and businesses. (sub. DR248, attachment p. 5)

When such combination of investigative action gives regulators access to a wider range of enforcement tools to deal with a breach, the likelihood of a successful outcome may also be increased. Some specific examples of these synergies, provided by the New South Wales Government, are shown in box 4.5.

Box 4.5 Examples of actions taken under the New South Wales FTA and an industry-specific statute

The New South Wales Government provided the following examples of actions taken under both an industry-specific statute and the FTA, with the latter used to deal with those elements of the misconduct that may not have been in contravention of the specific legislation.

1. A licensed swimming pool builder was convicted of breaches of the Home Building Act for receiving an excessive deposit (10% instead of the statutory 5%) and carrying out residential building work without a contract of insurance. The builder was also convicted under the Fair Trading Act for making a false and misleading representation. He had told the consumers that the local council would not approve a concrete pool and convinced them, against their wishes, to build a fibreglass pool. The local council had made no such decision.
2. An unlicensed motor dealer was convicted under the Motor Dealers Act of several counts of unlicensed dealing and odometer interference. The dealer had falsely advertised cars as if they were for private sale, had only one owner, were registered, had a low odometer reading etc, and was also convicted under the Fair Trading Act for making false representations that goods are of a particular standard, quality, grade, composition, style or model or have had a particular history or particular previous use.
3. A licensed motor dealer who displayed second-hand cars for sale with notices that falsely stated no statutory warranty applied (thus misleading potential purchasers into thinking the dealer was not obliged to repair or make good any defect which may exist or occur in the car) was convicted under the Fair Trading Act for making a false or misleading representation concerning the existence, exclusion or effect of any condition, warranty, guarantee, right or remedy. He was also found guilty of breaches of the Motor Dealers Act as he had not made the required entries in his register or used the correct forms.
4. A finance broker advertised personal loans and other finance, took details from prospective borrowers over the phone, subsequently advised them that the loan had been approved and demanded a loan fee of \$300-\$500. The loans were not advanced and he refused to refund the fees. He was convicted of multiple breaches of the Consumer Credit Administration Act for not entering into a finance broking contract and for accepting a commission without securing the credit. The court ordered refunds as provided by the Act. The finance broker was also convicted under the Fair Trading Act for falsely representing that services have approval or benefits they do not have and for accepting payment without intending to supply services.

Source: New South Wales Government, sub. DR251, pp. 10-11.

There can similarly be synergies between the consumer education and business compliance programs undertaken by State and Territory consumer regulators for their generic and industry-specific laws. And, as noted earlier, effective and timely enforcement may sometimes be facilitated by the linkages between these regulators and other State and Territory entities.

As well as potentially contributing to better outcomes for consumers, such synergies may provide cost savings for taxpayers. In particular, for as long as the States and Territories have a major role in enforcing industry-specific consumer law (see chapter 5), making a national regulator solely responsible for enforcing the generic law would inevitably entail some additional regulatory overheads. As the ACCC observed:

There would likely be considerable duplication in terms of physical presence across the country as both the national regulator and agencies implementing other state and territory legislation would need a regional office network to enforce their laws. (sub. DR176, p. 5)

Constitutional issues

Further, as elaborated on in box 4.6, there are some restrictions on the scope of the Australian Government's activities that would need to be addressed as part of any move to a one regulator model for the new national generic consumer law.

- Tribunals and small claims courts are not replicated at the Australian Government level, and constitutional restrictions might limit consumers' access to State and Territory bodies under a solely national system. There does not appear to be any obvious accessible and low cost alternative for enabling redress for consumers in such situations. And while the constitutional limitation may be resolvable, the possible options for doing so would take time to work through.
- There would also be some potential constitutional issues requiring resolution before a national regulator could enforce the consumer law for transactions involving entities currently outside the purview of the TPA.

Resourcing issues

The eight State and Territory generic consumer regulators collectively have an annual budget of more than \$300 million and employ some 2500 people. While these regulators together administer more than 300 statutes, maintenance of an 'equivalent' enforcement and related educative capacity under a one regulator model for the new national generic law would ostensibly necessitate a considerable transfer of enforcement resources.

It was put to the Commission that, based on the current experience with shifting responsibility for trade weights and measures to the national level, these transfer costs could be considerable. Such costs could be reduced through a staged process, drawing on the experiences from similar transfers that occurred in the 1990s in the corporations and financial services areas. But this does not negate the more general point that the transactions costs of the resource transfers required to ensure effective

application of the new generic consumer law to local issues under a one regulator model (or to deal with constitutional issues), must be factored into the overall benefit cost calculus.

Box 4.6 Constitutional issues bearing on the enforcement issue

Under a one regulator model for the new national generic consumer law, some constitutional restrictions on the Australian Government may make it difficult to precisely replicate the consumer protections that are currently available at the State and Territory level.

First, the Australian Government cannot replicate State and Territory consumer tribunals and small claims courts. This is because the Constitution restricts Commonwealth bodies belonging to the executive from undertaking judicial functions.

Accordingly, Commonwealth tribunals are restricted to reviewing the administrative decisions of the Government and other non-judicial functions. Moreover, the Constitution also prevents the Commonwealth from vesting powers in State tribunals. Thus, section 77(iii) only permits the Commonwealth to make laws ‘investing any *court* of a State with federal jurisdiction’ (emphasis added).

Second, the Constitution (section 51) restricts the Commonwealth’s regulatory scope to a set of prescribed powers. The Commonwealth has used some of these powers to enact and enforce existing consumer laws (such as over the activities of corporations and interstate commerce). However, legal issues arising from the recent challenge to the enforcement of corporations laws³ raise a question about whether the Commonwealth would be able to comprehensively enforce consumer laws against all entities (in the absence of a State referral of powers).

That said, these constraints may well be resolvable. For example, it might be possible for the States and Territories to vest their own tribunals and small claims courts with powers to hear consumer matters under a national generic consumer law. Further, the ACCC has so far been able to enforce State and Territory implemented competition laws for non-corporate entities through the extension of its powers in the TPA (see s. 44ZZM) and related State legislation.

The role and make-up of the ACCC

In the Commission’s view, the ACCC would be the logical choice as the regulator for the new national generic law under a one law, one-regulator, model. It has extensive experience in enforcing the TPA — on which much of the new generic law would be based — across all jurisdictions.

The Commission notes the arguments from some that enforcement of consumer policy at the Australian Government level should in future be housed in a separate

³ *The Queen v Hughes* (2000) 171 ALR 155.

body, rather than combined with competition policy within the ACCC. In discussing this alternative approach, David Cousins, Director of Consumer Affairs Victoria, said that:

There has been some international debate as to whether competition and consumer protection functions are best co-located or separated. Whilst these policy areas are complementary to the extent that they both seek to enhance consumer welfare, they are doing so from different perspectives. In practice, competition and consumer protection matters are readily distinguished when it comes to enforcement. (Cousins 2007, p. 33)

Similarly, WA DOCEP contended that :

... the balance that initially existed in the ACCC's functional obligations has been eroded by a continuing practice of increasing the ACCC's responsibilities in structural industry regulation. Organisations reflect their functions. Issues such as staff recruitment, corporate culture, internal resource allocation and agenda setting all reflect the functions of the organisation. The ACCC's functional obligations are now significantly weighted against consumer regulation. (sub. 99, p. 53)

However, in the Commission's view, such an approach would be undesirable — irrespective of whether or not a one law, one regulator model, is implemented for the new national generic law. In particular, as elaborated on in box 4.7, housing the enforcement of consumer policy at the Australian Government level in a separate body would see the loss of some important synergies with the enforcement of competition policy and in related policy development in these areas.

But while breaking up the ACCC would not be appropriate, some changes to its governance arrangements might well be a necessary precursor to the implementation of a single regulator model for the new national generic consumer law. Specifically, there is clearly some scepticism about its likely preparedness to assume and appropriately prioritise the sort of local enforcement functions currently undertaken by the State and Territory generic consumer regulators.

For the reasons set out earlier, provided that the ACCC was adequately resourced and motivated to take on a local enforcement role, such perceptions do not appear to be well founded. Nevertheless, if not acknowledged and addressed in some way (see box 4.8), they could make it very difficult to secure consensus for a one regulator model. Again, the costs of doing so need to be factored into the decision making calculus. So too must be the costs of any new mechanisms that would be required to allow the States and Territories to convey their enforcement concerns and priorities to the ACCC.

Box 4.7 **Why would splitting up the ACCC be damaging?**

The current combination of competition and consumer policy within the ACCC has several important benefits.

- It helps to ensure that the ACCC is mindful of the benefits of competition for consumers when enforcing consumer policy (and hence is wary of action that may lessen competition). Indeed, as noted in chapter 3, competitive markets are the first line of defence for consumers against bad business behaviour and will often be more effective than consumer laws in delivering good outcomes for them.
- Enforcement can sometimes be greatly assisted by knowledge of competitive pressures in different markets; uncompetitive markets will generally require a greater consumer policy focus.
- Consumer policy expertise helps to ensure that the end goal of competition policy (higher welfare for consumers) is not overlooked. As the Chairman of the ACCC, Graeme Samuel, recently stated:

The nature of competition laws as an aspect of consumer policy is illustrated by the fact that many competition matters involve direct consideration of consumer issues. (2007, p. 11)

- Competition reform often entails the establishment of parallel consumer protection measures (such as industry codes and ombudsmen). Indeed, the recognition of these complementarities long pre-dates the establishment of the ACCC: they were also reflected in the development of the TPA, which combined both consumer and competition laws.

Moreover, the Commission has not received any concrete evidence that the ACCC gives insufficient attention to nationally significant consumer issues — the focus of its consumer responsibilities under the current enforcement arrangements. Indeed, the vast majority of the ACCC's enforcement actions relate to consumer protection matters.

The draft report proposals

In the draft report, after weighing up all of these considerations, the Commission concluded that early implementation of a one regulator model for all of the proposed national generic consumer law would be problematic. But given its view that the one regulator model should remain on the longer term policy agenda, it proposed that the Australian and State and Territory Governments jointly explore the scope and means to overcome any obstacles to, and potential risks of, the approach.

It further argued that:

- this exploration should not preclude making the Australian Government, through the ACCC, the sole regulator for the product safety provisions as soon as the

new law is implemented — noting that product safety issues are generally national in nature, and with potentially severe consequences for some consumers if not promptly addressed; and

- pending the possible across-the-board adoption of a single regulator model in the future, individual States and Territories should have the option of referring their enforcement powers for all of the new national generic consumer law to the Australian Government.

Box 4.8 Dealing with perception problems

Concerns about the ACCC's likely preparedness to assume and appropriately prioritise the application of a new national generic law to local issues mirror those that were evident when ASIC was made responsible for the national enforcement of the corporations and financial services law.

To address these concerns, the resulting Corporations Agreement contained a number of provisions that guaranteed a continued role for the States and Territories in policy development — including that the Commonwealth consult with States and Territories on all major policy changes and before implementation secure the agreement of three State and Territory Ministers (two of which must be State Ministers).

It also set out requirements to help ensure that the previous levels of investor protection at the State and Territory level were maintained, including that:

- ASIC maintain offices in the capital cities of the States and the Northern Territory and, in consultation with the States and Territories, appoint Regional Commissioners that consult with the local community and help to set ASIC priorities;
- ASIC develop a system of performance indicators that it will report against in its annual report; and
- State and Territory Ministers be able to complain about levels of service at a Ministerial Council and that the Commonwealth Minister be obliged to provide a written response to such a complaint within a month.

Source: Attorney General's Department (2006).

Responses to the draft report

A significant number of participants saw considerable merit in the making a single national regulator responsible for administering the new national generic law, especially if the aforementioned obstacles can be overcome. For instance, the Australian Food and Grocery Council contended that:

Consumer protection is a broad and complex area interfacing with many industries, community sectors, regulatory and legal systems. The AFGC recognises that there are generic issues which cross broad areas of consumer interest. It is appropriate for these

issues to be dealt with centrally and nationally. Indeed, the consumer protection provisions of the Trade Practices Act and activities of the Australian Consumer and Competition Commission ... illustrate that some fundamental issues such as prevention of fraud and deception and anti-competitive behaviour can be provided for at a foundation level by national legislation enforced by a national agency. (sub. DR150, pp. 4-5)

Others to voice support included AGL Energy (sub. DR149, p. 2), Anglicare Tasmania (sub. DR191, p. 5), Australian Compliance Institute (sub. DR128, p. 2), Australian Toy Association (sub. DR161, p. 2), Choice (sub. DR194, p. 4), Commerce Commission NZ (sub. DR193, p. 1) and Optus (sub. DR173, p. 4).

However, an equally significant number either opposed a change to the current delineation of enforcement responsibilities between the ACCC and State and Territory regulators, or expressed considerable reservations about the scope to introduce an effective single regulator model, especially in the short term. For example, the South Australian Minister for Consumer Affairs said that:

Even if there were to be a national generic law (which is not supported) it would not be appropriate for this law to be administered by a single national regulator ... consumers' needs are best met by having a local regulator who has a grass roots understanding of local issues and who can respond sensitively and quickly to issues that arise. This does not preclude improving methods of information sharing through engagement, accountability and cooperation ... (sub. DR219, p. 7)

Kildonian Uniting Care (sub. DR206, p. 5) questioned whether the interests of vulnerable and disadvantaged consumers would be served by the one regulator model. And the ACCC itself said that:

Setting aside the constitutional and infrastructure difficulties, the proposal for a single regulator turns on the assumption that the associated benefits arising from a consistent application of the generic consumer law to local consumer issues are greater than the benefits associated with having a range of consumer and related laws enforced by local regulators who can utilise a full range of compliance tools associated with these laws to deliver outcomes for consumers. The ACCC does not believe the [Productivity Commission] has convincingly made this case in its draft report. (sub. DR176, p. 6)

Others to express opposition or reservations included the ACT Government (sub. DR250, p. 3), ANZTTCCI (sub. DR179, p. 1), WA DOCEP (sub. DR248, attachment p. 3), Energywatch UK (sub. DR197, p. 4), Foundation for Effective Markets and Governance (sub. DR122, p. 4), New South Wales Government (sub. DR251, p. 2), Redfern Legal Centre (sub. DR150, p. 7), Telstra (sub. DR156, p. 6) and the Victorian Government (sub. DR226, p. 7).

In some cases, those opposing the one regulator model in the broad were similarly opposed to the early transfer of responsibility for enforcing the product safety

component of the new law to the Australian Government. However, the ACCC argued that enforcement by a single national regulator is appropriate in this particular area.

Because the vast majority of goods supplied in the Australian economy are supplied nationally, the ACCC considers the enforcement of product safety laws to be a national issue and believes these laws should be enforced by a single regulator. A rapid and national response is often required to deal with immediate and significant threats to public health and safety posed by unsafe products, which does not allow the time otherwise needed for inter-jurisdictional coordination and cooperation. Moreover, there are significant benefits associated with maintaining public confidence across the country in having product safety messages delivered by a single voice. (sub. DR176, p. 4)

And, as elaborated on below, all State and Territory Governments, through CoAG, have recently agreed to the Australian Government assuming greater responsibility for regulating product safety.

The way ahead

A contingent approach with a referral of powers option

While the current delineation of enforcement responsibilities for the generic law has some benefits, there is clearly considerable dissatisfaction amongst consumers and businesses about the outcomes it is delivering in many parts of Australia. Though implementation of a national generic law may address some of the concerns, there is clearly a risk that, under a multiple regulator model, inconsistent enforcement will continue to detract from consumer wellbeing and remain a source of unnecessary cost and frustration for businesses. Accordingly, the Commission remains of the view that the option of making the Australian Government, through the ACCC, solely responsible for enforcing the new national generic law has intrinsic merit, especially in the longer term.

Equally, the Commission accepts that there are some good reasons to persist with a multiple regulator approach. In particular, while the States and Territories remain responsible for enforcing a large body of specific consumer regulation, the loss of regulatory synergies and the costs of creating a parallel regional office network are powerful arguments against implementation of the one regulator model.

More pragmatically, in the face of considerable jurisdictional opposition to the one regulator model, there is a real possibility that packaging it with the implementation of a new national generic law, could put the latter at risk. As argued earlier, the Commission considers that implementation of this new law is a critical first step in

creating a more nationally coherent consumer policy framework that could deliver more efficient and effective outcomes for consumers and the wider community.

The Commission has therefore concluded that, for the time being — and with the important exception of the product safety provisions (see below) — the new national generic law should be jointly enforced by the Australian Government and the States and Territories.

However, individual States and Territories should have the option to refer their enforcement powers to the Australian Government, with enforcement undertaken by the ACCC. The benefit-cost trade-off for the one regulator model will not be the same across jurisdictions. Thus a consensual referral option could potentially be attractive to some smaller jurisdictions where enforcement overheads are proportionately more significant. In supporting this approach, the Victorian Government (sub. DR226, p. 31) suggested that it could have wider application in the consumer policy area.

Moreover, if it transpires that the intent of the new law in delivering uniform and effective outcomes for consumers and businesses across Australia is undermined by inconsistencies in enforcement, then the option of one national regulator should be revisited. It should also be revisited if the review process detailed in chapter 5 leads to a significant reduction in the role of the States and Territories in enforcing industry-specific consumer laws. In these circumstances, one of the key arguments for maintaining a multi-jurisdictional enforcement model — regulatory synergies and avoiding duplication of regulatory overheads — would carry less weight.

Indeed, to ensure that there is appropriate future consideration of these matters, there should be an independent review of the enforcement regime no later than ten years after the new national generic law is implemented. That review would be informed by the outcomes of improved reporting of enforcement performance (see recommendation 10.3); by the experiences in any jurisdictions that take up the voluntary referral of powers option; and outcomes in areas of industry-specific consumer regulation where enforcement responsibility is transferred to the Australian Government (see chapter 5).

Enforcement of the consumer product safety provisions

While moving to a one regulator model for the entirety of the new national generic consumer law would not be appropriate at this juncture, the Commission is still strongly of the view that the Australian Government, through the ACCC, should become the sole regulator for the product safety provisions as soon as the new law is implemented. It reiterates that product safety issues are generally national in

nature, with most products being imported and sold across Australia. Product safety problems can also have potentially severe consequences for some consumers if not promptly addressed. Hence, the risks to consumer wellbeing under a system that requires nine jurisdictions to take quick and effective action are likely to be higher than for other parts of the generic law. (The arguments for a single national regulator in this area are elaborated on in the Commission's recent study (PC 2006) into Australia's consumer product safety system.)

Reflecting these arguments, CoAG (2008) recently agreed that the Australian Government should assume greater responsibility for regulating product safety — with MCCA, through CoAG's Business Regulation and Competition Working Group, to develop a detailed implementation plan for a national system by July 2008. CoAG has further indicated that, under this national system, States and Territories could retain the power to impose interim product safety bans (an 'intermediate' model that was not examined by the Commission in its consumer product safety study).

Within an otherwise national enforcement model, an interim ban arrangement would have some advantages. In particular, it would cater for any imperative for a State or Territory to take remedial action when a product safety issue arises in their jurisdiction. In so doing, it could also provide a way of moving forward on what has so far been a contentious reform area.

However, any state-based interim product safety ban arrangement would need to be carefully crafted to ensure that it did not become the source of significant and ongoing differences in product safety requirements across jurisdictions. Accordingly, the Commission is recommending that if the States and Territories are given the power to issue interim product safety bans, these should lapse after 30 days if not extended nationally by the responsible Australian Government Minister on advice from the ACCC. This would facilitate prompt, but still nationally consistent, responses — in contrast to the current arrangements that have been characterised by a multiplicity of jurisdictionally-based permanent bans and standards.

4.4 Other matters

Application of the generic law to financial services

In a number of areas, the application of generic consumer law overlaps with that of industry-specific regulation. For example, in therapeutic goods and telecommunications regulation, the ACCC shares responsibility with other

Australian Government regulators. There are further overlaps between the ACCC's responsibilities and the enforcement of some State and Territory industry-specific regulations (in areas such as health, food and electrical products).

In contrast, financial services are expressly exempted from the consumer protection provisions of the TPA. This exemption was introduced in response to the Wallis inquiry that recommended the creation of a separate industry-specific regulator for financial services (Wallis 1997, p. 32). (However, the Wallis inquiry did not recommend that financial services be exempted from the generic law.)

In its initial submission, ASIC (sub. 103, p. 74) contended that the 'carve-out' of financial services is not causing significant problems and that cooperation mechanisms with the ACCC are working well. It also said that any moves to concurrent jurisdiction could require costly new coordination procedures and prevent it from taking action with some of the additional enforcement tools that it has at its disposal. The Australian Bankers Association (sub. DR245, p. 8) similarly supported a continuation of the current arrangements to avoid any potential for confusion in regulatory roles.

However, according to the ACCC, the carve-out has introduced some uncertainty as to its ability to take action in certain cases:

While on its face the delineation between the respective jurisdictions of the ACCC and ASIC appear quite clear, in practice, there is a significant degree of overlap and uncertainty. In some cases it is unclear which agency has jurisdiction and it may be the case that in some situations one agency will have responsibility for some aspects of a transaction, whereas the other agency will have responsibility for other aspects.

Examples of areas of overlap and uncertainty include debt collection, investment seminars, loyalty schemes and periodic or deferred payments of utility accounts. (ACCC, sub. 80, p. 139)

It further noted (p. 141) that uncertainty about the definition of a financial service and therefore which legislation applies, has raised procedural costs in some cases.

In the Commission's view, there is a strong underlying rationale for the new national generic law to encompass all sectors. There are always risks that statutory carve-outs will create uncertainty and thus give unscrupulous businesses scope to escape regulation by operating in the cracks. Concurrent jurisdiction avoids this problem, with cooperation arrangements minimising the risk of duplicated enforcement effort.

Moreover, notwithstanding ASIC's initial concerns, the Commission is unaware of any evidence suggesting that cooperation arrangements between the ACCC and industry-specific regulators in other areas are more costly than the current

arrangements for financial services, or are delivering inferior outcomes. Indeed, in a subsequent submission, ASIC said that it:

... is confident that the two agencies can work together to develop and implement effective arrangements to coordinate regulatory activity, avoiding unnecessary overlaps or gaps and ensuring that it is clear for consumers and other stakeholders which agency to take up their complaint or issue with in the first instance. (sub. DR174, p. 4)

Under such arrangements, the presumption should be that ASIC would have primary enforcement responsibility, with any involvement by the ACCC or State and Territory consumer regulators in this area being the exception rather than the rule, and only occurring after prior consultation with ASIC.

Application of the misleading or deceptive conduct provisions

In bringing financial services within the remit of the new national generic law, the question arises as to whether certain disclosures required by the Corporations Act or other financial services legislation should be subject to the misleading or deceptive conduct provisions. Currently, financial services regulation requires that some such disclosures only be made on reasonable grounds (eg section 670A of the Corporations Act), and exempts providers from the misleading or deceptive conduct provisions.

The reason for this is that the latter provisions impose strict liability on firms engaging in misleading or deceptive conduct, even if such conduct could not reasonably have been avoided. Such a stringent requirement could pose difficulties for those preparing documents relating to raising equity capital or acquiring assets, where there is often a significant amount of uncertainty and judgement required. As the Wallis inquiry stated:

Among the risks that investors may be rewarded for bearing are those deriving from imperfect information. It is vital to economic efficiency that regulation not unduly interfere with this risk allocation function of the financial system. In the areas of the law which have provided specific due diligence defences, explicit balances have been struck between consumer protection and market efficiency objectives, and these should not be interfered with by other laws. (1997, p. 251)

The Commission considers that there is a good prima facie case for replicating these exemptions in the new national generic law and notes that few participants have argued strongly against this approach. This endorsement of current practice does not of course imply that current financial disclosure requirements cannot or should not be improved. In chapter 11, the Commission has mapped out some general requirements for improving mandatory disclosure requirements, as well as indicating that research may be warranted on how best to address conflicts of interest in financial disclosure statements. As suggested by Dr Luke Nottage

(sub. DR114, p. 6), further research on the most appropriate treatment of this particular *sub-set* of financial disclosures under the new national generic law might also be desirable.

However, pending any evidence of major costs to consumers from the current treatment of this sub-set of financial disclosures, changing that treatment does not seem warranted and could well be counterproductive. That is, the imposition of stricter requirements in these cases might well lead to even longer disclosure documents or prospectuses as firms attempted to ensure that they were not subject to action for misleading or deceptive conduct. This would increase costs for financial service providers and thereby prices for consumers, and could also (further) inhibit some consumers' understanding of investment products.

Legislative arrangements for implementing the new generic law

In other areas, two broad approaches have been used to replace overlapping or divergent jurisdictional legislation with a nationally uniform law.

- *Applied law arrangements.* These arrangements require one jurisdiction to enact a 'template'. Other jurisdictions then pass application legislation that automatically adopts this law and any subsequent changes made to it. The Competition Code is an example of applied law arrangements.
- *Referral of powers.* Section 51(xxxvii) of the Constitution permits the States, either severally or individually, to refer powers over a particular area to the Commonwealth. Corporations law is an example where a referral of powers approach was employed.⁴

In this case, given that the Commission is recommending that the States and Territories retain their current enforcement responsibilities for most aspects of the new national generic law (at least for the time being), an applied law approach would *prima facie* be preferable. Moreover, the use of an applied law arrangement would not preclude the option for an individual jurisdiction to voluntarily refer its enforcement powers (see above).

That said, the Commission emphasises that these legislative instrument issues are complex. For example, if an applied law arrangement is used, minor variations in the legislation at the jurisdictional level may be required to ensure that the new

⁴ These are not the only options for coordinating or harmonising consumer legislation. For example, the current generic consumer law is the result of a model legislation process. This process requires jurisdictions to enact laws that are as close as possible to a model act. However, as past experience indicates, this approach does not guarantee uniformity in what are intended to be national laws. Accordingly the Commission has not considered it further.

national generic law extends to non-corporate entities and to reflect differing judicial arrangements among the States and Territories. The Commission also notes that whatever legislative instrument is employed, there may be a need for supporting protocols (or a like mechanism) specifying the basis for reviewing and making changes to the law.

Guarding against future regulatory ‘break-out’

Even with a uniform national generic consumer law in place, supported by arrangements which ensure that future changes to it are implemented in an identical fashion across Australia, the risk of regulatory divergence cannot be completely removed. For example, variations could still emerge if jurisdictions were to introduce self-standing generic provisions in separate legislation. And under the proposed multi-jurisdictional enforcement model, there remains some risk that individual jurisdictions could promulgate divergent guidelines for applying the new law (or other forms of varying ‘grey letter law’).

The Commission is hopeful that the general consensus on the benefits of a nationally uniform generic consumer law, improved Ministerial Council processes (see section 6.3) and the various informal processes through which consumer policy makers and enforcement agencies engage with each other, will keep any such break-out to a minimum. But if the sort of regulatory break-out that has characterised the previous model legislation approach were to be evident in the future, this would increase the case for moving to a one-law one-regulator model.

Interface with other ‘consumer’ legislation

Legislation such as the Privacy Act, the Spam Act and the Do Not Call Register Act, has a strong consumer protection focus. As GE Money (sub. DR208, pp. 4-5), Suncorp (sub. DR171, p. 2), and the Australian Finance Conference (sub. DR216, p. 2) pointed out, inconsistency between such legislation and the generic consumer law and industry-specific consumer regulation (see next chapter), can impose unwarranted compliance costs and thereby penalise business and consumers.

Such interface issues may well merit detailed investigation and possibly even some legislative change. However, such investigation is for another inquiry rather than for this review focussed on the TPA, the Fair Trading Acts and key industry-specific consumer statutes.

RECOMMENDATION 4.1

Australian Governments should implement a new national generic consumer law to apply in all jurisdictions. The new law should be based on the consumer protection provisions of the Trade Practices Act (TPA), amended to:

- *reflect other recommendations in this report;*
- *incorporate additional provisions from State and Territory Fair Trading Acts in those cases where the TPA is generally agreed not to be adequate to deal with a particular generic issue; and*
- *ensure that the new law covers non-corporate entities and accommodates jurisdictional differences in court and tribunal arrangements.*

RECOMMENDATION 4.2

The new national generic consumer law should apply to all consumer transactions, including financial services. However:

- *the Australian Securities and Investments Commission (ASIC) should remain the primary regulator for financial services, with any involvement by the Australian Competition and Consumer Commission or State and Territory consumer regulators in this area only occurring after prior consultation with ASIC; and*
- *financial disclosures currently only subject to ‘due diligence’ requirements should be exempted from the misleading or deceptive conduct provisions of the new law.*

RECOMMENDATION 4.3

Responsibility for enforcing the consumer product safety provisions of the new national generic consumer law in all jurisdictions should be transferred to the Australian Government and be undertaken by the Australian Competition and Consumer Commission (ACCC).

If the Council of Australian Governments determines that the States and Territories should retain the power to issue interim product safety bans, these should lapse after 30 days if not extended nationally by the responsible Australian Government Minister, on advice from the ACCC.

RECOMMENDATION 4.4

The remainder of the new national generic consumer law should be jointly enforced by the Australian Competition and Consumer Commission (ACCC) and State and Territory consumer regulators. However, individual States and Territories should have the option to refer their enforcement powers for all of the new law to the Australian Government, with enforcement to be undertaken by the ACCC.

RECOMMENDATION 4.5

The enforcement arrangements for the new national generic consumer law should be subject to an independent review within ten years, with explicit consideration of the benefits and costs of moving to a single national regulator model for all of the law, having regard to:

- *any evidence that differing enforcement practices or regulatory ‘break-out’ are leading to divergent outcomes for consumers and businesses across Australia;*
- *experiences and outcomes in any jurisdictions that have referred their powers of enforcement for the new national generic consumer law to the Australian Government; and*
- *the implications of any shifts in enforcement responsibility for industry-specific consumer policy to the national level (see recommendations 5.1 to 5.3).*

5 Industry-specific consumer regulation

Key points

- Industry-specific regulation can be an effective means of providing consumer protection where the risk of consumer detriment is high and/or the quality of the product or service is difficult to establish prior to purchase.
- However, there are problems with the way that specific consumer regulation is currently developed and employed. Jurisdictional differences add unnecessarily to business compliance costs. Also, some of this regulation is:
 - unnecessary given the generic consumer law;
 - overly prescriptive; and/or
 - primarily designed to protect existing businesses from competition.
- A nationally oversighted review and reform program should be initiated to:
 - identify and repeal unnecessary specific consumer regulation, with an initial focus on requirements applying in only one or two jurisdictions;
 - identify other areas of specific consumer regulation where unnecessary divergences in requirements, or lack of policy responsiveness, have significant costs; and
 - determine how to reduce these costs, while continuing to protect consumers, with explicit consideration of the case for transferring policy, and where appropriate enforcement, responsibilities to the Australian Government.
- Responsibility for regulating credit providers and intermediaries providing advice on credit products should be transferred to the Australian Government, with enforcement undertaken by the Australian Securities and Investments Commission.
 - Amongst other things, this new credit regime should cover all credit products and intermediaries (including those providing advice through electronic or other arms-length means); and provide for licensing of finance brokers and registration or licensing of credit providers, giving consumers guaranteed access to an approved dispute resolution service.
- To improve the effectiveness and/or efficiency of some other key areas of industry-specific consumer regulation:
 - Australian Governments should agree to a single, uniform, consumer protection regime for energy services once the national energy market is further developed.
 - In fully contestable utility markets, all retail price regulation should be removed, with assistance to disadvantaged consumers provided through targeted community service obligations and company-provided hardship programs.
 - The current national review of ‘last resort’ home builders’ warranty insurance should also consider how to enhance the effectiveness of early stage consumer protection measures in the home building sector, including in relation to dispute resolution and the licensing of builders.

As outlined in chapter 2, the generic provisions of the Trade Practices Act (TPA) and the Fair Trading Acts are frequently supplemented by consumer regulations specific to a particular market or industry. This specific regulation tends to define acceptable trader behaviour or product characteristics and is therefore more prescriptive than the generic law (examples include occupational licensing and safety standards for certain products). And it usually focuses on the identification and prevention of unacceptable behaviour, rather than providing remedies to consumers in the event that such behaviour occurs (and through those remedies adding to the incentives for suppliers to act appropriately).

In this chapter, the Commission has assessed the role of industry-specific regulation within a more nationally coherent consumer policy framework. It has not undertaken a detailed examination of every aspect of such regulation. Rather, the Commission has focussed, in the first instance, on how to ensure that:

- there is the right mix of generic and industry-specific consumer regulation; and
- the division of responsibility for specific consumer regulation between the Australian and State and Territory Governments is compatible with a nationally coherent policy framework.

However, the Commission has made some recommendations to improve the specific consumer protection arrangements in the key areas of consumer credit, utility services and home building.

5.1 When is an industry-specific approach warranted?

Industry-specific consumer protection ranges from self-regulatory arrangements, which suppliers comply with on a voluntary basis, to more prescriptive controls on supplier behaviour or product characteristics. Among the latter are mandatory information disclosure requirements, licensing requirements for service providers and direct controls on price and product quality.

There are relatively few significant areas of consumer spending that are not subject to specific consumer protection regulation. Such arrangements apply to:

- everyday purchases (such as food);
- routine periodic transactions undertaken by almost all households (for example, purchases of financial or utility services);
- a broad range of professional and trade services (for instance, those supplied by medical practitioners, real estate agents and plumbers); and
- more significant episodic purchases (such as buying a home or motor vehicle).

The intent is to provide more effective and certain consumer protection than could the generic provisions alone (box 5.1). In particular, taking action after the event under generic law may not provide adequate consumer protection where:

- the risk of consumer detriment is relatively high and/or the detriment suffered if things go wrong is potentially significant or irremediable (the primary reason why specific regulation is employed in the medical and consumer credit areas); and/or
- the suitability and quality of services is hard to gauge before or even after purchase — the ostensible rationale for many other professional licensing regimes and ‘objective’ standards for technically complex products.

Box 5.1 Some views on the benefits of industry-specific regulation

Queensland Government (sub. 87, pp. 50-1):

... industry specific regulation can provide targeted solutions, can be easier to enforce and can address problems before they arise. Such regulation tends to work best for industries that can be clearly defined and are relatively static, where there are specific or technical problems that cannot be dealt with through general regulation and where there are significant consequences for consumers if problems do arise.

... Because it applies to a single industry or sector, industry-specific regulation often imposes more prescriptive rules or conditions of participation in a market, such as relating to competency and standards of conduct. Such provisions can be more effective than general law in preventing or reducing the risk of serious harm. Potential problems may be addressed when a trader enters a market as through a licensing process, rather than depending on the effectiveness of action taken by the regulator after the fact under general law.

Targeted regulation can greatly improve confidence in a market, particularly when there are significant risks of participation. It provides consumers and traders with certainty about their rights and obligations and better equips the parties to resolve disputes when they do arise.

Industry specific regulation is usually easier to enforce than general regulation because it is easier to demonstrate when specific rules have been broken. Unlike actions under general law, prosecution is less dependent on proving that the intention of the action would damage consumers.

Industry specific models may also provide regulators with a more effective means of monitoring business behaviour against compliance requirements.

ACCC (sub. 80, pp. 137-8):

... introduction of an industry-specific regime in some cases may have substantial benefits for consumers and be necessary to achieve the objectives of consumer policy.

It may be necessary to provide a higher level of protection than generic laws, for instance a licensing regime, or a different type of protection in certain situations, for instance specific disclosure requirements or standard form terms and conditions.

While well-designed industry-specific regulation can enhance consumer wellbeing and provide greater certainty to suppliers of goods and services about their obligations, reliance on generic law alone has some important advantages. It:

- facilitates consistency in approach across consumers and markets;
- allows regulators to deal with emerging problems without the need for new statutes — an especially important feature given that many consumer markets are evolving rapidly; and
- imposes relatively few costs on the overwhelming majority of suppliers who do the right thing by consumers.

Moreover, apart from typically higher compliance burdens, specific consumer regulation can also have indirect costs, including restricting the entry of new suppliers or products to a market, or impeding process innovation.

In recognition of these costs, it is important that the need for specific consumer regulation is carefully established and its appropriateness assessed. Consistent with the decision-making tree described in chapter 3, such an assessment should include an evaluation of viable alternatives, including the scope to employ self-regulation or co-regulation (box 5.2). Though having some significant limitations, when viewed along the spectrum of policy alternatives, such approaches may nonetheless provide a less costly way of augmenting generic consumer protection measures than ‘black-letter’ specific regulation. (The Consumers Telecommunication Network (sub. DR211, p. 6), for example, contended that the co-regulatory model in the telecommunications sector is the most ‘workable’.)

Also, once a need for industry-specific regulation is established, it should conform to some fundamental design principles, including that:

- the activities which are covered are clearly identified; and
- its requirements complement, rather than duplicate, generic provisions, and are sufficiently flexible to accommodate changes in the market concerned.

Current concerns

As in other policy areas, evidence of unnecessary or overly prescriptive specific consumer regulation has, over the last decade or so, led to the review and rationalisation of aspects of this regulation. Box 5.3 provides some commentary on these reform processes and examples of specific consumer regulations that have been modified or abolished.

Nonetheless, there continue to be problems with the way that specific regulation is developed and employed in the consumer area which should be remedied as part of the implementation of a nationally coherent consumer policy framework.

Box 5.2 **Self-regulation**

Self-regulatory codes of behaviour may be voluntary or enforced (through legislation or as a condition of operating in the industry) as 'co-regulation'.

- *Voluntary* codes in the consumer area include the Australian Retailer's Association Scanning Code of Practice, the voluntary advertising codes administered by the Advertising Standards Bureau, and various professional accreditation schemes.
- *Enforced* codes, which will usually include a binding dispute resolution mechanism, include those in the telecommunications and banking sectors, and the therapeutic goods advertising code.

Codes are normally developed by suppliers, often in consultation with consumers. Given the direct involvement of both groups in the market concerned, problems can often be quickly identified and rectified and changes made to the codes, if required. Indeed, voluntary codes can sometimes provide for more immediate redress than formal regulatory provisions. For example, the Scanning Code of Conduct provides a transparent and quick way for consumers to resolve issues relating to overcharging at supermarket checkouts.

Suppliers also have an incentive to ensure that self-regulatory arrangements minimise adverse impacts on market activity (though such incentives may also lead to less effective consumer protection mechanisms).

The major disadvantage of pure self-regulation is that suppliers will only comply with it when in their interests to do so. This is more likely to be the case when industry members receive significant reputation benefits as a result of compliance. In the absence of these benefits, or if breaches are difficult to detect, incentives to comply are clearly reduced. Even where there is a commitment from an industry body to enforce a code, supported by the bulk of its membership, application to 'rogue traders' may not be possible. Also, effective enforcement can be problematic where a self-regulatory arrangement lacks a binding, independent dispute resolution mechanism.

Such enforcement problems can sometimes be effectively addressed through a co-regulatory regime where an industry-developed code is enforced by government. And because such an arrangement continues to draw on industry knowledge, it may retain some of the advantages of a self-regulatory regime, including minimising unintended consequences and costs. However, the benefits of co-regulation will largely depend on the circumstances of the industry. Ultimately, there may be only a limited distinction between co-regulation and 'black-letter' regulation introduced by the government after extensive consultation with consumers and the sector concerned.

Box 5.3 Rationalisation of industry-specific consumer regulation

- The Victorian Government has indicated its intent to rely more on the generic provisions of its Fair Trading Act. It has repealed a number of pieces of industry-specific legislation and incorporated some specific regulations (for example, those relating to hire purchase agreements) into more general legislation:

By emphasising the Fair Trading Act as our key enforcement tool it is considered that there will be greater consistency in conduct regulation across industries and lower compliance costs for business, especially if some industry-specific regulation can be avoided. (CAV 2004a, p. 6)

It has also commenced a review of all consumer-related licensing regimes to ensure that 'the consumer problems, regulation objectives and government interventions are consistent and appropriate'. (sub. 92, p. 74)

- The Queensland Government has undertaken to:
... continue its program of significant legislative review, including a comprehensive review of current legislation to reduce the future need for lengthy and complex industry-specific legislation. (Minister for Tourism, Fair Trading and Wine Industry Development (Queensland) 2004, pp. 1-2)
- Under the National Competition Policy Legislative Review Program, occupational licensing schemes which were reformed or abolished, included: arrangements in some jurisdictions for hairdressers; employment agents; podiatrists; real estate agents; dentists; veterinarians; and conveyancing services (PC 2005b, pp. 79-80).

Inconsistent requirements across and within jurisdictions

There are a plethora of inconsistencies in State and Territory specific consumer regulation (see box 5.4).

In some instances, differences in jurisdictional requirements are warranted. For example:

- A Productivity Commission (2004c) study found that climatic factors provide a rationale for some variations in building standards (although it argued that these could sometimes be made on a regional, rather than a jurisdictional, basis).
- Regulation in certain consumer markets is targeted at social problems such as excessive gambling or liquor consumption that are more evident in some jurisdictions (eg, gambling rates differ markedly among jurisdictions).

And even where the intrinsic case for variation is weak, if the goods or services concerned are mainly supplied by businesses operating in single jurisdictions, then the added compliance cost burden from differing requirements may be modest.

Box 5.4 Variations in industry-specific regulations

Some of the more significant differences across the States and Territories in industry-specific consumer regulation include:

- *Credit.* Western Australia has a positive licensing regime for credit providers, while other jurisdictions only register providers or have the capacity to ban miscreant providers (so-called 'negative licensing'). Further, three jurisdictions impose interest rate caps (which also vary in their detail) — see appendix E.
- *Energy.* The arrangements to institute a national energy market provide for the retention of some jurisdictionally divergent energy-related consumer protection measures (see section 5.3).
- *Food.* Individual jurisdictions continue to depart from nationally set standards at the implementation stage (Regulation Taskforce 2006, p. 58).
- *Tobacco.* A range of regulations require different display and signage requirements (see text). The regulations also change regularly in different jurisdictions.
- *Electrical products.* According to AEEMA (sub. 84, p. 2), there are variations in electrical product standards, and enforcement efforts are not well coordinated, leading to delays in removing unsafe products from the market.
- *Therapeutic goods.* Variations in the classification of poisons mean that the conditions of sale for some pharmacy only medicines differ between jurisdictions. (ASMI 2005, p. 5).

However, given the trend towards national markets, these variable requirements are increasingly a source of unwarranted added cost and frustration for businesses operating across Australia, or large parts of it, to the ultimate detriment of consumers. Moreover, because industry-specific laws are often more prescriptive than the generic consumer law, there may be less scope for businesses to circumvent needless regulatory differences through simply operating in an ethical way or, alternatively, complying with the most stringent requirement. For instance, the Australian National Retailers Association (sub. 60, p. 9) reported that variations in tobacco regulation across States require the production of different signage and display labels. The Commission's survey of a number of major suppliers who operate across jurisdictional boundaries (see chapter 14) similarly suggests that the compliance burden from such inconsistencies are far from trivial.

In some cases, there are also variations and inconsistencies in the requirements within jurisdictions, or between national and jurisdictional regulatory measures. Putting its perspective on the regulatory framework for mobile telecommunications, the Australian Mobile Telecommunications Association stated:

... the mobile telecommunications industry operates under a complex regulatory model [with] different degrees of industry and government initiation of 'self-regulatory' initiatives, significant use of government delegated legislation, overlapping and

inconsistency between jurisdictional and agency responsibilities, and numerous bodies developing policy without adequate reference to, or knowledge of, initiatives or regulatory responses developed by other bodies or agencies.

This kind of duplication and overlap can lead to confusion among suppliers and their customers as to their obligations and rights. Consumers particularly may find the complaints procedures and processes across different jurisdictions, for the same services and products, confusing and leading to a perception of less than satisfactory or timely resolution of issues. (sub. DR175, pp. 2-3)

Poor design and implementation procedures

There are also more fundamental deficiencies in the specific regulatory component of the policy framework that are detracting from good outcomes for consumers and the community.

- A need to supplement the generic consumer law is not always clearly demonstrated — with industry-specific consumer regulation sometimes introduced mainly because of a reluctance to enforce the generic law and/or a lack of resources to do so; or to provide quick responses to problems raised by vocal interest groups (CAV 2006b, pp. 4-5).
- Notwithstanding recent reform efforts, some specific regulation is overly prescriptive, reducing the responsiveness of suppliers to the changing needs of consumers and increasing costs and therefore prices. (Examples include areas of occupational licensing discussed below.)
- As noted by some participants, including Choice (sub. 88, p. 76), certain regulations appear to be primarily designed to protect existing businesses from competition, rather than to assist consumers.

Moreover, as discussed in chapter 4, the involvement of multiple jurisdictions in some key areas of specific regulation has led to a lack of policy responsiveness, giving rise to the potential for significant detriment to consumers.

5.2 Reviewing specific consumer regulation

The role of regulatory assessment

Robust regulatory assessment is the key to ensuring that any new industry-specific consumer regulation is genuinely required, is well-targeted to meeting the needs of consumers and does so at low cost. Periodic review of existing measures is also

important to ensure that they remain appropriate in the light of changing market conditions and consumer behaviour, and of improvements to the generic law.

The importance of robust regulation review has been acknowledged in recent commitments by COAG to strengthen and broaden the scope of regulatory assessment processes (box 5.5). And as the commentary reported earlier in box 5.3 illustrates, it has also been explicitly endorsed in some State and Territory Government input to this review. As another example, the Director of Consumer Affairs Victoria (Cousins 2007, p. 30) recently observed:

Two key ways to avoid bad regulation are to ensure the process of developing regulation is rigorous and that the process is subject to independent assessment. It is essential at the outset that the problems of concern are properly identified and their underlying causes fully understood. This requires good research and evidence gathering. Too often, ‘solutions’ to problems assumed to exist are proposed before the problems are fully explored.

Consumer-specific considerations call for sophisticated evaluation

But while acknowledging the need for robust evaluation, several participants contended that aspects of current review guidelines are not well suited to assessing consumer policy. For example, the Queensland Government (sub. 87, p. 38) claimed that implementation of Regulatory Impact Statement (RIS) guidelines has underplayed the indirect benefits of regulation (such as for vulnerable and disadvantaged consumers and for equity more generally). Others perceived a bias towards considering those impacts that can be quantified (Choice, sub. 88, p. 45; Consumer Action Law Centre, sub. 94, p. 57; ASIC sub. 103, p. 77), with the latter stating:

We note though that to date the focus of OBPR’s processes has been on the costs to industry. The other side of the equation, the benefits (and costs) to consumers, has not been adequately focused upon.

The Commission understands these concerns, but notes that RIS processes do provide scope to take account of indirect benefits and costs, including those which cannot be readily quantified. Moreover, though adverse impacts on competition are a key review trigger, the fundamental determinant of the worth of a regulation has always been whether it provides a net public benefit. In assessing this, policy makers must have regard to a range of non-exhaustive factors, including the ‘interests of consumers generally or a class of consumers’ and ‘social welfare and equity’ (NCC 1998).

It is true that the nature of the problems that are targeted through consumer policy raise some particular issues and challenges for the application of the RIS process.

For example, the process will need to recognise that the behaviour of consumers can at times substantially depart from the behavioural models used to analyse firm behaviour. As noted in appendix B, such behavioural insights can sometimes help improve regulatory design.

Box 5.5 Reviews of regulation assessment processes

Three recent reports (Regulation Taskforce 2006; IPART 2006 and VCEC 2007b) evaluating Australian Government, New South Wales and Victorian regulation review processes recommended changes to improve regulatory institutions, including:

- greater use of risk assessment and business compliance costing tools;
- the use of more rigorous consultation to inform RISs;
- strengthening the oversight and the incentives for compliance with RIS guidelines;
- better targeting regulation review processes to the most important areas;
- tightening the tests for determining an adequate RIS and preventing regulation which is inadequate from proceeding to Cabinet; and
- the development of mechanisms to encourage the timely development of standards.

Following the Taskforce's report, all jurisdictions agreed (COAG 2006a) to develop stronger regulation review requirements, including:

- integrating gatekeeping mechanisms into decision-making processes and increasing transparency;
- improving the quality of regulation impact analysis by, where appropriate, using cost-benefit analysis and more detailed measurement of compliance costs;
- broadening the scope of RISs to explicitly recognise the effect of regulation on individuals and the cumulative burden of regulation on businesses; and
- undertaking reviews (at least annually) to review priority areas where regulatory reform could provide significant gains to business and the community.

And at its most recent meeting, CoAG indicated that its Business Regulation and Competition Working Group will be examining whether further reforms are needed to ensure that jurisdictions have in place best practice regulation and review processes.

Sources: Regulation Taskforce (2006), IPART (2006), VCEC (2007b) and COAG (2006a; 2008).

That said, there is nothing in the current RIS processes that precludes consideration of behavioural factors. Moreover, while explicit quantification of some of the impacts of consumer regulation will not be possible, there are other metrics that can be employed to help guide decision making — including the use of risk analysis. Consulting with a broad range of stakeholders to ensure that all of the benefits and costs of a proposed regulation are at least identified, can also contribute to an effective RIS process. Notably, concerns about the extent of consultation were voiced during this inquiry (see for example, Consumers' Federation of Australia, sub. 83, pp. 7, 10; Choice, sub. 88, p. 48 and Australian National Retailers Association, sub. 60, p. 5).

In sum, the key goal of regulation review processes is to ensure that regulations are well targeted at the problem identified and that they achieve their objectives at least cost. Provided they are applied in a sophisticated and flexible way, rigorous consumer policy review processes should be unobjectionable: they are aimed at improving the benefits of regulation to the community while minimising the costs to businesses, consumers and taxpayers.

A dedicated review program is required

Over time, application of robust regulatory assessment processes should help to ensure that industry-specific consumer regulation is more judiciously and effectively used. So too will application by consumer regulators of the more specific decision making tree set out in figure 3.1. Also, the Commission's proposals to add to the suite of enforcement tools available to generic consumer regulators (see chapter 10) may reduce the incentive to use specific regulation on the grounds that application of the generic law is too slow and costly.

But without some overarching driver, dispensing with unnecessary or outdated statutes, and improving the efficiency, effectiveness and jurisdictional consistency of the remaining stock of specific consumer regulation, could be a slow process.

Further, such assessments would not of themselves provide a vehicle for examining whether responsibility for some, or much, of the large body of State and Territory specific consumer regulation that remained in place would better reside with the Australian Government. In many areas, commonality in consumer issues across Australia, the national nature of the markets concerned, the costs of current jurisdictional variations in regulatory requirements and a lack of policy responsiveness arising from the involvement of up to nine governments, might well provide a compelling case for single national regimes. Examination of the arguments for transferring responsibility for more specific consumer regulation to the Australian Government, and the ways in which this might be achieved, should therefore be an integral part of the development of a nationally coherent consumer policy framework.

Accordingly, in the draft report, the Commission proposed that CoAG oversee a review and reform program for industry-specific consumer regulation akin to the processes for reviewing anti-competitive legislation under NCP. Specifically, it suggested that this program should:

- identify and repeal unnecessary specific consumer regulation, with a particular focus on requirements that only apply in one or two jurisdictions;

-
- identify other areas of specific consumer regulation that apply in all or most jurisdictions, but where needlessly divergent requirements or a lack of policy responsiveness impose significant costs on consumers and/or businesses; and
 - determine how these costs would be best reduced, including explicit consideration of the case for transferring policy and enforcement responsibilities to the Australian Government and how this transfer might be best pursued.

It went on to argue that occupational licensing (box 5.6) should be an early priority for review under this program, noting that while the need for licensing in some areas is not in dispute:

- licensing has costs, meaning that it should not be overused; and
- there are significant differences across jurisdictions in the use of occupational licensing (figure 5.1 and table 5.1), raising doubts about the need for a considerable part of the current occupational licensing apparatus in the consumer area.

Responses to the draft report proposal

Many participants expressed broad support for a CoAG-oversighted review process to streamline and improve industry-specific regulation. However, several suggested that the primary focus of this review process should be narrower — namely, on removing specific regulation addressing matters that can be adequately dealt with by the generic law. (See, for example, Communications Alliance, sub. DR185, p. 4; Telstra (sub. DR156, pp. 8-9; and Woolworths, sub. DR180, p. 1.) And the Victorian Government (sub. DR226, p. 49) called for a more ‘manageable’ program, though beyond referring to the relevant review work that has already been undertaken, did not indicate what this would entail.

In contrast, the Real Institute of Australia (sub. DR172, p. 7) advocated an even broader remit for the review program — arguing that transfers of responsibility to the Australian Government are only one means of addressing the costs of jurisdictionally divergent consumer regulation. It proposed the development and application of guidelines to promote harmonised requirements for that specific regulation which remains the responsibility of the States and Territories.

Box 5.6 **The benefits and costs of occupational licensing**

An occupational licence imposes a range of conditions on service providers, often specifying: educational and professional qualification requirements; the tasks that a licensed provider can undertake; proscribed forms of conduct; and sanctions for breaches of the requirements.

Compared to reliance on the generic law, licensing can be targeted at identified problems in specific industries; be activated or modified relatively quickly; and increase consumer confidence in the operation of the industry. It is most likely to confer net benefits where the potential consumer detriment from making a poor choice is significant and:

- the costs of obtaining product information are high; and/or
- verification of quality by the consumer or other third parties is difficult.

For example, the difficulty for consumers of establishing the quality of medical services before and even after the event, and the potentially severe consequences of poor services, suggest that licensing of medical providers is highly desirable.

However, by restricting entry to the market, licensing schemes can limit competition, reducing choice and raising prices for consumers. They also impose compliance costs on all suppliers (including those who 'do the right thing' by consumers), with these imposts again at least partly passed on to consumers. Hence, it is important that licensing is not over-used.

Negative licensing

Negative licensing is a less costly form of licensing arrangement that has been employed in some industries. Examples include the arrangements for land valuers in South Australia, and introduction agents in Victoria. Under this sort of arrangement, suppliers do not require regulatory approval before entering the industry, but can be fined or suspended from trading if they fail to comply with certain obligations.

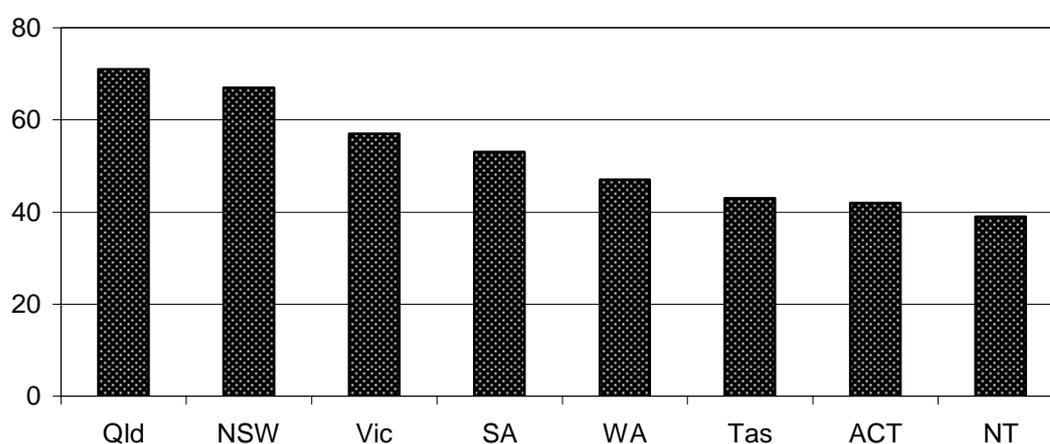
As well as having lower administration and ongoing compliance costs, by removing the need for prior approval, negative licensing schemes can reduce business set-up costs. However, such schemes will not be universally appropriate. Apart from the need to take court action to ban non-compliant suppliers, breaches of licence conditions will usually only come to light when a consumer has suffered detriment and reported it to the regulator. Thus, negative licensing arrangements may be inappropriate when the potential consumer detriment from inappropriate supplier behaviour is high.

Focussing on the outcomes of the review program, Anglicare (sub. DR191, p. 6) and Legal Aid NSW (sub. DR215, p. 4) contended that any harmonisation initiatives or transfers of regulatory responsibility should maintain the 'higher' standards of protection. And in supporting and emphasis on specific regulation applying in only one or two jurisdictions, Choice (sub. DR194, p. 3) said that there

should not, however, be a presumption that such regulation is necessarily inappropriate.

Figure 5.1 Occupational licensing

number of consumer-related occupations/activities licensed by jurisdiction



Source: Appendix G.

Table 5.1 Occupations licensed in only one or two jurisdictions

Aboriginal health worker	Hydraulic services designer	Property inspector (pre-purchase)
Acupuncturist	Inbound tourism operator	Quantity surveyor
Chinese medical practitioner/dispenser	Introduction agent	Rehabilitation provider
Energy Assessor	Kit home supplier	Shopfitter
Engineer (building industry)	Marine designer	Site classifier
Entertainment industry agent/manager	Marine surveyor	Specialised contractor
Firearms instructor	Motor vehicle repairer	Speech pathologist
Firearms repairer	Optical dispenser	Steel fixer
Floor finisher and coverer	Passive fire equipment installer	Strata manager
Hairdresser	Plumbing plan certifier	Structural landscaper
Hawker	Professional engineer – chartered	Venue consultant
	Property developer	Wool, hide and skin dealer

Source: Appendix G.

This presumption was also the main concern of those opposing or expressing reservations about the proposed review. For example, the National Consumers' Roundtable on Energy commented that:

We suggest that the requirements applying in one or two jurisdictions may represent best practice and result from the experience of markets over time that may be replicated at the national level. The fact of some regulation being particular to one or two jurisdictions should not be sufficient recommendation for its repeal. (sub. DR199, p. 5)

More generally, the ACT Government (sub. DR250, p. 4), the New South Wales Government (sub. DR251, p. 4) and the Western Australian Department of Consumer and Employment Protection (WA DOCEP — sub. DR248, attachment pp. 5-6) questioned the need for such a review program — referring to both recent review and reform activity, especially in the area of occupational licensing, and prospective CoAG action to deal with regulatory ‘hotspots’. And the South Australian Minister for Consumer Affairs (sub. DR219, p. 8) said that any review and reform program should be oversighted by MCCA rather than CoAG.

The terms of reference for the review

The preceding commentary serves to illustrate the difficulty of drawing neat boundaries around an exercise aimed at ensuring that more appropriate use is made of industry-specific regulation within a nationally coherent consumer policy framework.

It is clearly important that a concerted effort is made to remove unnecessary specific regulation — especially that dealing with matters that could otherwise be well handled using the generic law. This applies to areas for which the Australian Government is responsible, as well as those where responsibility resides at the State and Territory level.

But this is only part of the task. Ensuring that policy and enforcement responsibilities for soundly-based specific consumer regulation reside at the right level of government is also very important. So too is eliminating unwarranted divergences in areas where regulatory responsibility remains with the States and Territories.

Equally, it would not be sensible or practical to encompass every piece of specific consumer regulation within a ‘fast-tracked’ review process. That is, some of the less significant regulation would be better left to existing regulatory assessment processes. Nor would it be sensible to include those more important statutes that have been comprehensively assessed in recent reviews, with explicit consideration of the issue of which level of government should have policy responsibility. And yet other regulations may be better assessed on a stand-alone basis. For example, while the Commission has previously signalled that pharmacy regulation requires further national review and reform, it has suggested that this would best occur as a precursor to the renegotiation of the Australian Community Pharmacy Agreement in 2010 (PC 2005b, p. 265).

With these sorts of considerations in mind, the Commission remains of the view that a focus on specific consumer regulations applying in only one or two jurisdictions is a useful *starting point* for rationalising the current regulatory regime.

- There will of course be some regulations that apply in all or the majority of jurisdictions that are probably unnecessary given the protections available in the generic consumer law.
- And, as noted above, there may sometimes be good reasons for requirements that apply in only one or two jurisdictions. Hence contrary to the presumption of some participants, it is not the Commission's intention that such *worthwhile* regulation be repealed as part of this review and reform process.

However, with common sense application, a focus on regulatory 'outliers' seems more likely to offer the prospect of some early regulatory streamlining than other potential identification mechanisms.

The Commission also remains of the view that attention in this context on occupational licensing is not unreasonable. Of the total of nearly 100 occupations licensed by the States and Territories for consumer policy reasons, more than 30 are licensed in only one or two jurisdictions (table 5.1). While in some instances there are good reasons for this (eg. Aboriginal Health Workers), in others (eg hairdressing) the *prima facie* case for specific requirements seems very weak. Of course, in the many specific areas that the Commission has not considered in this inquiry, there are likely to be 'one-off' regulations that warrant scrutiny. Hence, the occupational licensing area is again only a starting point for investigation.

The other critical component of the review process which the Commission has in mind, is an assessment of whether shifting responsibility for some aspects of specific consumer policy development, and as appropriate enforcement, from the States and Territories to the Australian Government would enhance outcomes for consumers. Indeed, it is this component of the review process that distinguishes it from the legislation review process under National Competition Policy (NCP). While the latter process provided scope for national reviews, for those specific consumer regulations that were assessed, the reviews were mainly conducted at the State and Territory level. Hence 'the which level of government' issue was not examined. The Commission's expectation is that a review program which explicitly addressed this issue, would identify various areas of specific consumer regulation where the interests of consumers and the community would be better served by moving to single national regimes (see, for example, box 5.7)

Finally, as some participants argued, the review process should assist in harmonising that specific consumer regulation which remains the responsibility of the States and Territories. Accordingly, where a review concludes that a transfer of

regulatory responsibility to the national level would not be appropriate, it should outline a process and timetable for achieving harmonisation in jurisdictional requirements.

Box 5.7 Some areas where nationally-based regimes may be warranted

In addition to consumer credit and energy market regulation (see section 5.3), participants in this inquiry, or previous reviews, have identified several areas of industry-specific consumer regulation where national rather than state-based regulatory regimes may be beneficial, including:

- *electrical products*: as noted in box 5.4, regulatory variations between jurisdictions have contributed to delays in removing unsafe products from the market (though the current state-based regime is supported by the electrical regulatory authorities (ERAC, sub. DR143, p. 4));
- *legal services*: the CoAG Standing Committee of Attorneys-General released a national model for regulation of legal professionals in May 2004; and
- *real estate*: the Real Estate Institute (sub. DR172, pp. 8-9) pointed to various gaps, overlaps and inconsistencies in current state-based regulation, suggesting that the area is a 'prime candidate' for a national regulatory approach

In addition, the scope for consolidation of responsibility for consumer protection regulation in the chemicals and plastics sector, including through greater use of national regimes, is among the matters being considered by the Commission in a concurrent research study — a draft report for which was recently released (PC 2008).

Evidently, the success of this proposed review process will depend on the support and cooperation of all Australian Governments, as well as effective consultation with consumers, businesses and other stakeholders. As the NCP process showed, reform of specific regulation — national or state — in a federal system is not an easy task.

However, the arrangements that have recently been agreed to by CoAG to improve the consumer policy framework could be particularly helpful in facilitating a rigorous and effective review process. As discussed further in the next chapter, one of the newly formed CoAG working groups — the Business Regulation and Competition Working Group (BRCWG) — is to be responsible, in consultation with the Ministerial Council on Consumer Affairs (MCCA), for developing enhanced national approaches, drawing on this report. For this particular reform initiative, such an arrangement would both provide for the necessary national oversight of the review program and take advantage of MCCA's more detailed consumer policy expertise in the development and conduct of the program.

RECOMMENDATION 5.1

CoAG's Business Regulation and Competition Working Group, in consultation with the Ministerial Council on Consumer Affairs, should instigate and oversee a review and reform program for industry-specific consumer regulation that, drawing on previous reviews and consultations with consumers and businesses, would:

- *identify and repeal unnecessary regulation, with an initial focus on requirements that only apply in one or two jurisdictions;*
- *identify other areas of specific consumer regulation where unnecessary divergences in requirements, or lack of policy responsiveness, have significant costs; and*
- *determine how these costs would be best reduced, whilst maintaining protections for consumers, with explicit consideration of:*
 - *the case for transferring policy and, where appropriate, regulatory enforcement responsibilities to the Australian Government and how this transfer might be best pursued; and*
 - *a process and timetable for harmonising and streamlining currently divergent specific regulation that remains the responsibility of the States and Territories.*

5.3 National regimes for credit and energy services

At its most recent meeting, CoAG agreed in principle to the Australian Government assuming greater regulatory responsibility for consumer credit and to a process and timetable to give effect to this. Hence, the Commission's proposed general review process for industry-specific consumer regulation will not be required in this particular area. Also, the Commission considers that the in-principle case for a similar transfer of responsibility for energy market regulation is sufficiently strong as to make further investigation unnecessary, though there are some short term impediments to doing so.

A framework for a national regime for consumer credit

Financial products include financial investments (such as in shares or superannuation), loans and other forms of credit, mechanisms for managing financial risk (such as insurance) and facilities providing for non-cash payments

(such as cheque or savings accounts). Financial services involve the sale of these products, including the provision of advice.

The purchase of financial services can entail significant monetary commitments, sometimes over long periods of time. Hence, where the behavioural traits identified in appendix B lead to imprudent decisions, the consequences for consumers can be particularly costly. Moreover, purchasing decisions will often involve complex product comparisons, with consumers frequently relying on intermediaries to make these comparisons on their behalf. However, assessing the quality of such advice, even after the event, can be problematic. Accordingly, effective consumer protection measures are particularly important for these services.

In furthering the development of a nationally coherent consumer policy framework, the Commission considers that future arrangements in the financial services area should aim to ensure that:

- product/service coverage is comprehensive such that there are no gaps that can be exploited by unscrupulous providers;
- there is an appropriate balance between protecting and empowering consumers and providing them with efficient access to a wide range of products and services;
- there is consistency in the regulatory requirements applying to different financial services and service providers and in the enforcement of those requirements across Australia; and
- policy making and enforcement is responsive to changing circumstances in what is a highly dynamic market, with new products and services being introduced all the time.

How are financial services regulated at present?

Most financial services are regulated at the national level by the Australian Securities and Investments Commission (ASIC). As well as applying the generic consumer law, which is replicated in the ASIC Act, it also administers the licensing regime and related disclosure requirements for those providers regulated under Chapter 7 of the Corporations Act. This licensing regime requires, among other things, that a provider belongs to an ASIC-approved Alternative Dispute Resolution (ADR) scheme.

However, credit providers and many of those providing advice on credit products are outside ASIC's remit. Rather, as well as being subject to the generic consumer

law through the TPA and State and Territory Fair Trading Acts, credit providers in particular are separately regulated by the States and Territories¹.

- The overarching piece of regulation is the Uniform Consumer Credit Code (UCCC), implemented through template legislation. As elaborated on in more detail in appendix E, its main focus is on promoting truth in lending through prescribed disclosure requirements. It also prohibits ‘unjust’ terms, requires the provision of ‘comparison rates’ of interest (incorporating most fees and charges) in designated credit contracts, as well as covering such matters as default procedures and provision for hardship applications. Responsibility for enforcing the code lies with the State and Territory Fair Trading Authorities.
- There are also various separate pieces of State and Territory credit regulation. For example, three States have introduced caps on interest rates and Western Australia has a positive licensing regime for credit providers and intermediaries advising borrowers on the merits of competing credit products (hereafter referred to as finance brokers).

Deficiencies in the current State-based regime

Against the criteria for an effective consumer policy regime for financial services, the current arrangements governing consumer credit fall short in several important respects.

First, there are gaps in service coverage. The absence of a comprehensive national approach for regulating finance brokers is widely acknowledged to be a major deficiency in the current regime. As the Finance Brokers Association (sub. DR177, p. 6) pointed out, in the last few years, changes in the housing market have seen consumers rely much more heavily on finance brokers when considering their lending options. The Association went on to say:

As consumers continue to turn toward mortgage and finance brokers to assist in their borrowing needs, the FBAA recognizes and is supportive of the need for a regulatory regime to be established which governs the activities of finance and mortgage brokers that has national consistency.

There are also some generally acknowledged loopholes in the UCCC which can be used by unscrupulous credit providers to circumvent its requirements. And lack of coverage under the code for small business and investment loans (including margin

¹ It appears that the bulk of credit by value is in fact provided by financial service providers who, by virtue of their other activities, are subject to the regime administered by ASIC. However, ASIC (sub. DR174, p. 9) cautioned that while a credit provider may belong to a corporate group which holds an Australian Financial Services Licence, the provider itself may not be licensed.

lending), is seen by some as another significant gap in the current regime, as is the absence of regulation for web aggregation services (see appendix E).

Second, the state-based arrangements have resulted in differential protection for credit consumers and have imposed added burdens on service providers which will ultimately be passed on to consumers in the form of higher prices.

- While the UCCC notionally provides for consistent requirements across Australia, it has not prevented jurisdictions from unilaterally introducing additional requirements as part of, or separate from, the Code. This means that the protections available to consumers acquiring credit partly depend on where they live.
- As a result of these differential requirements, service providers operating nationally or in multiple jurisdictions incur additional costs from the need to vary their business practices, use different paperwork etc.
- There are also further costs from duplicated requirements for the many credit providers who supply other financial services that are regulated at the national level by ASIC.

Thirdly, the inter-jurisdictional processes for changing the Code have often seen prolonged delays in implementing necessary reforms (appendix E). Given that the adverse consequences for consumers of ill-judged use of credit or poor quality advice on credit products can be very significant, and that products and market practices are evolving rapidly, this lack of policy responsiveness is a major demerit in the current arrangements.

Coverage gap problems could potentially be rectified within the existing regulatory framework. Indeed, there are various initiatives in train to do so (see box 5.8).

However, the costs for consumers and businesses from inconsistent and overlapping requirements are a direct consequence of the current delineation of responsibilities. And while not all of the delays in achieving changes to the UCCC can be sheeted home to the multi-jurisdictional approach, it has evidently been a major contributor.

The case for a national regime is compelling

Reflecting these deficiencies in the current approach, there has been widespread support from both consumer groups and financial service providers for transferring responsibility for regulating consumer credit and finance broking to the Australian Government. The Commission concurs with a recent House of Representatives Parliamentary Committee (SCEFPA, 2007, p. 48) examining home lending which

argued that such a transfer of responsibility would ‘remove the arbitrary and illogical division of powers that currently exists’.

Box 5.8 Work in train to improve current credit market regulation

As elaborated on in appendix E, through MCCA, a variety of measures to strengthen or otherwise improve credit regulation are being progressed. For example:

- On behalf of MCCA, in late 2007, New South Wales released an exposure draft Finance Broking Bill for public consultation. The proposed legislation is intended to provide the basis for a uniform regulatory regime for finance brokers across Australia. Apart from a requirement for brokers to be licensed and to participate in an ASIC-approved ADR scheme, the proposed arrangements stipulate educational standards and various ‘best practice’ conduct rules. (Aside from the licensing regime in Western Australia, the only specific requirements currently applying to finance brokers are a registration system in the ACT and disclosure requirements in New South Wales, Victoria and the ACT when a broker deals in consumer credit (sub. DR178, p. 4).)
- Various measures have been agreed to, or are under consideration, to close regulatory loopholes in the UCCC (such as in relation to the treatment of bills of exchange); ensure that all consumers of credit have access to dispute resolution; consumer test pre-contractual disclosure requirements; explore issues related to responsible lending; and revamp the comparison rate requirements (see sub. DR226, pp. 51, 53).

Many of these initiatives will help to inform the configuration of the new national regime for consumer credit, recently agreed to in principle by CoAG (see text), though there has been considerable debate on the merits of some (see appendix E).

In the Commission’s view, the experience of ASIC in relation to other financial services makes it the logical choice to be the national regulator for credit products and advice. Indeed, ASIC (sub. DR174, p. 5) noted that, notwithstanding the primary role of the States and Territories in the credit area, it has sought to play a significant role in relation to emerging credit issues through ‘a targeted combination of research, compliance and enforcement work, work with industry bodies and consumer education’. Provided that ASIC was proactive in addressing the full range of credit provision and intermediary issues, and appropriately resourced to do so, then such a shift in responsibility has the potential to significantly improve the effectiveness of protection for consumers, and provide some cost savings to credit providers/advisors and their customers.

CoAG has agreed in principle to a transfer of responsibility to the Australian Government

At its most recent meeting, CoAG (2008) agreed in principle to the Australian Government assuming responsibility for regulating the following credit/financial services products and advisory services:

- mortgage credit and advice, including persons and corporations engaged in mortgage broking;
- margin lending; and
- lending by non-deposit taking financial institutions.

The BRCWG, in consultation with MCCA, is to develop detailed proposals by October 2008, drawing on this report.

CoAG has also requested the BRCWG to identify any other financial services providers that best sit within the Australian Government's responsibility, citing as possible examples pay day lenders and 'fringe' credit providers. The BRCWG is to report back to CoAG by July and develop implementation plans by October.

This decision is in line with the Commission's proposal in its draft report to transfer responsibility for regulating all credit providers and finance brokers to the Australian Government, with those regulatory requirements enforced by ASIC — a proposal that was welcomed by many participants. (See, for example, ACT Government, sub. DR250, p. 4; Anglicare Tasmania, sub. DR191, p. 6; ANZ Banking Group (ANZ), sub. DR178, p. 2; the Australian Bankers Association (ABA), sub. DR245, p. 2; Banking and Financial Services Ombudsman, Financial Industry Complaints Service and the Insurance Ombudsman Service, sub. DR170, p. 2; Cash Converters, sub. DR144, p. 6; Choice, sub. DR194, p. 4; WA DOCEP, sub. DR248, attachment p. 8; Finance Brokers Association of Australia, sub. DR177, p. 5; the Financial Planning Association of Australia, sub. DR212, p. 2; Financial Sector Union National Office, sub. DR157, p. 1; Legal Aid NSW, sub. DR215, p. 5; Mortgage and Finance Association of Australia, sub. DR119, p. 3; and Westpac Banking Corporation, sub. DR247, p. 1.)

The devil is in the detail

Most participants also supported the draft report proposal to keep the requirements for consumer credit separate from those for financial services that are already administered by ASIC. In many cases, this was because credit was seen as being different from other financial services and therefore requiring targeted regulatory treatment. Also, the ABA (sub. DR245, p. 12) and some individual banks expressed

concern that any attempt to dispense with the UCCC and instead rely on new arrangements within the broader financial services regime could entail significant compliance costs for mainstream credit providers — with the ABA noting that the banks have ‘invested very considerable sums of money and resources’ in complying with the code’s requirements.

More broadly, however, the responses to the draft report highlighted the complexities involved in transferring responsibility for consumer credit and advice to the Australian Government, as illustrated by the following list of issues drawn mainly from the submission by ASIC (sub. DR174):

- whether, given the ostensibly lower consumer and compliance risks attaching to credit provision relative to many other financial products, there is scope, over time, to simplify and streamline current credit requirements. (Such streamlining could also ensue from the introduction of more layered disclosure requirements — see chapter 11);
- whether less stringent quality of advice requirements should apply to credit products, given that the ‘appropriateness of advice in credit does not raise difficult questions around attitude to risk and overall long term financial needs to the same degree’ (p. 11);
- the merits of differential licensing/registration requirements for finance brokers and credit providers in the light of the trade-off between a ‘proportionate’ regulatory response and the problems that can arise under a dual system when there is service convergence, or where the one entity engages in both activities;
- whether and how the prohibition in the Corporations Act on ‘acting for more than one licensee’ should be applied to finance brokers; and
- whether the new regime should extend to products such as small business and investment loans, and also to property investment advice (see appendix E).

There were also some significant differences of opinion amongst participants about:

- whether the UCCC should be modified before or after the transfer of responsibility to the Australian Government; and
- what specific modifications (additional to any streamlining) should be made to the requirements in the UCCC. For example:
 - Some consumer groups voiced concern about a lowest common denominator approach and supported incorporation of the separate credit legislation sitting outside the code in some jurisdictions, as well as adoption of the measures developed by MCCA to close coverage loop holes and otherwise strengthen the stringency of the code.

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- Conversely, the ABA (sub. DR245, pp. 3-4) and ANZ (sub. DR178, pp. 3-4) claimed that the current MCCA proposals to deal with fringe lending could adversely affect activities in mainstream credit markets, with ANZ going on to argue that, more generally, there is a risk that the transfer process could easily become one predicated on the highest common denominator. Similarly divergent views were evident in regard to the merits of MCCA’s proposed finance broking regime. (See, for example, Mortgage and Finance Association of Australia, sub. DR119, p. 3; the Finance Brokers Association of Australia, sub. DR177, p. 5; Australian Finance Conference, sub. DR216, p. 7, and the ABA, sub. DR245, p. 4.)

And several participants, including the Victorian Government (sub. DR226, p. 53), raised concerns that too rapid a transition process could result in the ‘sidelining’ of work done within MCCA to improve the UCCC and related state-based regulation.

Some key requirements for the new national regime

Given the CoAG process that is now in train, it would not be appropriate or sensible for the Commission to try to develop a detailed implementation plan for the new national regime for consumer credit. However, drawing on the responses to the draft report and its own further analysis, the Commission considers that the new regime should have the following features.

- First and foremost, it should cover all consumer credit products and all intermediaries providing advice on such products (including through electronic or other arms-length means); not just those advising on mortgage products. While dealing with advice on mortgage products may be the biggest and most pressing issue, advice on a range of other credit products can raise similar concerns about service quality, disclosure of interests etc. Also, any attempt to restrict the coverage of the advisory component of the new regime would inevitably give rise to ‘boundary line’ problems.
- The UCCC should be retained as a self standing set of regulatory requirements within the broader financial services regulatory regime, sitting beside the mirror TPA provisions and the requirements of the Corporations Act. Credit products are different in character from other financial services, as are the nature and level of the associated risks. Hence it is appropriate that ASIC should have access to some specific credit-related measures that appear to have worked reasonably well, or that could do so with further modification. For example:
 - Regulatory guidance on permissible credit instruments may help to limit the use of potentially detrimental credit arrangements, and may make it easier for the regulator to take action against rogue credit providers.

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- Some specific indication of what summary information should be provided in all credit contracts may be helpful in promoting a layered approach to disclosure matters (see chapter 11).
 - These credit-specific requirements should incorporate changes to the code that have been agreed to by MCCA but not yet implemented. As elaborated on in appendix E, this group of agreed modifications includes changes to: narrow the bills of exchange exemption; better address fringe lending issues; and deal with some particular issues relating to e-commerce and vendor financing. Also, a decision is apparently imminent on whether to continue with the mandatory comparison rate requirements, or to introduce alternative measures.
 - The requirements should also incorporate generally agreed provisions from state and territory credit legislation outside of the code, where these pass a benefit-cost test.
 - The new regime should include a national licensing system for finance brokers, and a licensing or registration system for credit providers that would give consumers guaranteed access to an approved ADR service, either as part of the finance brokers regime or as a separate regulatory arrangement. In the Commission's view, access to effective dispute resolution should be an integral component of consumer protection arrangements in the credit area.
 - As a general principle, ADR will often provide for a cost-effective means of consumer redress (see chapter 9).
 - For disputes involving consumer credit, recourse to the services of expert third parties is likely to be particularly helpful given both the complexity of many credit products and advice on those products, and the substantial detriment that some consumers experience when things go wrong.
 - And the process of transferring responsibility for consumer credit regulation to the Australian Government should allow, over time, for the streamlining of the current UCCC in the light of requirements within the broader financial services regime, where net benefits are likely. In particular, removing any needlessly or overly prescriptive credit-related provisions could help to minimise inconsistencies in outcomes across different financial products, and reduce compliance costs for the many entities who provide both credit and other financial products and services.

There may also be benefits from implementing the new regime in a phased way. For example, immediately bringing the UCCC within the Australian Government's jurisdiction, and introducing an interim national licensing system for finance brokers, based on the draft proposal developed by MCCA, and enforced by ASIC, would give credit consumers some early additional protections. As well, it might be possible to quickly implement those changes to the UCCC that have been agreed to

by all jurisdictions. Indeed, seeking to resolve all of the detailed issues prior to the transfer of broad responsibility for consumer credit and advice to the Australian Government could lead to further protracted delays in addressing some matters that have now been under consideration for several years and for which the general direction of change required is broadly agreed.

The CoAG process will also evidently need to consider the resourcing implications of the transfers of enforcement responsibility to ASIC and whether any changes to its governance arrangements are required — for example, to facilitate the involvement of the States and Territories in the ongoing development of credit policy. However, the Commission notes that the processes and protocols agreed to when responsibility for financial services was transferred to the Commonwealth (see box 4.7) may well prove adequate for this purpose.

RECOMMENDATION 5.2

Responsibility for the regulation of credit providers and intermediaries providing advice on credit products (‘finance brokers’) should be transferred to the Australian Government, with enforcement to be undertaken by the Australian Securities and Investments Commission (ASIC).

Amongst other things, the new national credit regime should:

- ***cover all consumer credit products and all intermediaries providing advice on such products (including through electronic or other arms-length means);***
- ***retain the Uniform Consumer Credit Code (UCCC) as a self standing set of requirements within the broader financial services regulatory regime; incorporating changes to the Code that have been agreed to by the Ministerial Council on Consumer Affairs (MCCA), but not yet implemented;***
- ***incorporate requirements from state and territory credit legislation outside of the code, where these pass a benefit-cost test;***
- ***include a national licensing system for finance brokers, and a licensing or registration system for credit providers that would give consumers guaranteed access to an approved dispute resolution service; and***
- ***allow, over time, for the streamlining of the current UCCC in the light of requirements within the broader financial services regime, where net benefits are likely.***

Also, CoAG should give consideration to implementing the new national regime in a phased way, including as initial steps:

- ***importing into the Australian Government’s jurisdiction the current UCCC — modified to reflect changes agreed to by MCCA, but not yet implemented — and making ASIC responsible for its enforcement; and***

-
- *introducing an interim, ASIC enforced, national licensing arrangement for finance brokers, based on the draft proposal developed by MCCA.*

The Commission further notes that there are linkages between the regulation of financial services providers and consumers' access to credit products. Hence, those tasked with the detailed development of the new national regime for consumer credit should consider how 'responsible lending' issues might impact on the regulatory arrangements.

And, as outlined in appendix E, there are several other matters that might warrant consideration by CoAG, in consultation with MCCA, in the development of the new national credit regime, or in making any parallel changes to the broader financial services regulatory regime. These include whether:

- small business loans should be covered by the credit regime;
- property investment advice and web aggregation services should be covered by the financial services regulatory regime;
- specific regulatory provisions are needed to address reverse mortgage issues; and
- debt collection should be regulated at the national level.

A national consumer regime for energy services should be the goal

There are good reasons to supplement the generic consumer law with specific measures to protect and empower energy consumers. They are essential services, with disconnection having potential harmful effects; billing is lumpy increasing the risk of financial stress for low income households; price menus and product bundling can be complex; and some areas of supply are not yet fully competitive. An overview of the current specific regulatory regime is provided in box 5.9, with further elaboration in box 5.10, chapter 9 and appendix F.

Responsibility for these measures lies with the States and Territories — a consequence of the historic arrangements that saw separate State-based monopolies provide services in different jurisdictions. However, the process of creating national energy markets and laws to overcome the costly fragmentation of the previous jurisdictionally separate frameworks is now underway.

- The Ministerial Council on Energy (MCE) is currently developing national electricity laws and has established a national regulator — the Australian Energy Regulator (AER) — to enforce these laws in participating jurisdictions.
- Moves to develop a national gas market are less well advanced (appendix F). But it is planned that it should proceed along similar lines to the development of the national electricity market.

Box 5.9 Consumer protection for utility services

Consumer protection arrangements for utility services — energy, telecommunications and water — aim to secure a basic level of access for all consumers, to facilitate informed choice, to encourage ‘fairness’ in contracts and to minimise and deal with disputes effectively. To this end, and supplementing generic consumer law, there is a mix of ‘black letter law’ and co/self-regulatory approaches, including retail price regulation, community service obligations (CSOs), universal service obligations (USOs), hardship provisions and dispute resolution schemes.

In the case of telecommunications, policy and enforcement responsibilities lie with the Australian Government. In contrast, the States and Territories are responsible for consumer protection in the energy and water sectors.

Given the essential nature of many of these services, as well as the complex service offerings which can make informed choice difficult, many of these measures are clearly warranted. Hence, overall, the Commission considers that the specific consumer protection regime for utility services is broadly sound — a view generally shared by both consumer advocates and utility suppliers.

However, the jurisdictionally-based process for introducing competition reforms to energy service provision has contributed to duplication and inconsistency in what are broadly similar regulatory approaches for protecting consumers. In the Commission’s view, there is a strong in-principle case for addressing this fragmentation in the regulatory regime by developing a single set of consumer protection requirements for energy services to apply across Australia (see text).

In addition, while utilities-specific ombudsmen schemes appear to operate reasonably well, there are changes that could be made to them to improve their efficiency and effectiveness. For instance, once national energy markets are well developed, replacing the network of jurisdictional ombudsmen with national dispute resolution arrangements would offer the prospect of cost savings, more consistent treatment for consumers and the opportunity to consolidate and build regulatory expertise (see chapter 9).

And, as retail markets for utility services become fully contestable, there should also be changes to the way that support for low income and other disadvantaged consumers is provided (see section 5.4).

Yet despite these moves to consolidate energy markets, the current intention is to leave some key consumer protection measures at the State and Territory level. Certain measures — including retail price regulation, alternative dispute resolution and service performance standards — will not be covered by a new ‘national’ consumer policy framework scheduled for introduction around 2010. Moreover, detailed implementation of some of the measures encompassed by that framework will be left to individual States and Territories. And though not explicitly a consumer protection measure, renewable energy requirements designed to shift

consumers' spending patterns, also vary considerably across the States and Territories.

The continuation of such divergent arrangements will add to regulatory compliance costs for national energy suppliers and thereby to the price of energy, and can also be expected to lead to different levels of protection for consumers depending on where they live. As AGL Energy remarked:

... the current complex generic and energy specific regulatory requirements impose significant costs on energy retailers, in terms of multiple business systems and processes, and personnel training. We also believe that the current framework leads to jurisdictional inconsistencies with respect to customer rights and obligations.
(sub. DR149, p. 2)

The draft report proposal and responses to it

Given such costs, in the draft report, the Commission argued that it is now a logical time to implement a single consumer protection regime encompassing all jurisdictions participating in the national market arrangements, with uniform requirements across those jurisdictions. It further suggested that there be scope for those jurisdictions not currently part of the national energy market to choose to participate in this national consumer protection regime.

This proposal was endorsed by a number of major energy suppliers. (See for example, AGL Energy, sub. DR149, p. 2; Energy Retailers Association, sub. DR184, p. 1; Origin Energy, sub. DR158, p. 2; Synergy WA, sub. DR155, p. 2; and Tru Energy, sub. DR164, p. 1.) It was also supported by the Australian and New Zealand Energy and Water Ombudsman Network (sub. DR187, p. 2) and, in principle, by the National Consumers' Roundtable on Energy (sub. DR199, p. 8).

However, the latter went on to say that improving access to services is critical to those in rural and regional communities and that jurisdictional governments tend to be more responsive to these needs. It therefore concluded (p. 9) that to support a move to a national framework it would need:

... considerably more reassurance that the national regulators, the AEMC and AER, had the mandate and authority to drive investment in distribution networks that was in the broader public interest.

In a similar vein, the ACT Essential Services Consumer Council (sub. DR204, p. 2) pointed to the divergences in regional hardship levels and the adverse consequences that could ensue from a uniform lowest common denominator approach.

Some participants also questioned whether, at this early stage of the process of creating national energy markets, jurisdictional supply arrangements are too

divergent to warrant a uniform suite of consumer protection measures — even if that may be appropriate in the longer term. More bluntly, the New South Wales Government (sub. DR251, p. 12) indicated that its policy is to retain certain jurisdictional controls consistent with the current agreement between the jurisdictions on this matter. And the Victorian Government similarly stated that it is:

... important for jurisdictions to be able exercise some discretion over consumer protections in the energy sector in their state in order that optimal consumer outcomes can be achieved. (sub. DR226, p. 55)

A national regime in this area may not be feasible immediately

The Commission remains of the view that, within a national energy market, the specific consumer protection regime should also be nationally-based. As in other areas, the maintenance of divergent state requirements within a national market environment will lead to higher costs for consumers and differing levels of protection for them. And while there may well be regional differences in service access needs, hardship levels and the like, it is far from clear that these differences are delineated by state boundaries. Moreover, access to essential services in rural areas is not a matter that can be efficiently addressed through consumer policy.

However, the Commission accepts that a national regime for consumer-related energy market regulation may not be feasible in the short term. In the face of evident opposition from some jurisdictions, seeking to move in this direction now could undermine support for, and further slow progress in implementing, national energy market arrangements in the broad. This could be costly for consumers. Furthermore, differences in supply arrangements across jurisdictions, and in the extent to which electricity and gas supply have been deregulated, could make it difficult to develop a workable set of national arrangements that went much beyond enunciation of desired outcomes.

Accordingly, the Commission is proposing that Australian Governments agree to the longer term goal of a single set of consumer protection measures for energy services to apply across Australia, but leave their development and implementation until the process of creating national energy markets is further progressed. An appropriate time to revisit the issue could be when the Australian Energy Market Commission (AEMC) has completed its assessments of the degree of contestability in the energy markets of each of the participating jurisdictions and made recommendations on any price regulation that remains in force (see section 5.4). In the meantime, through the MCE, State and Territory Governments should agree to implement the new non-price regulatory requirements for retail energy services, scheduled for introduction around 2010, with minimal jurisdictional variations so as to enable a smooth transition to a uniform national regime at a later date.

RECOMMENDATION 5.3

Through the Ministerial Council on Energy (MCE), Australian Governments should agree to the longer term goal of a national consumer protection regime for energy services, with a single set of requirements to apply in all jurisdictions participating in the national energy market. Those requirements should be enforced by the Australian Energy Regulator.

The specific requirements for that regime should be developed under the auspices of the MCE after the Australian Energy Market Commission has completed its reviews of the effectiveness of competition in each of the jurisdictional retail energy markets.

Through the MCE, State and Territory Governments should also agree to implement the new non-price regulatory requirements for retail energy services, scheduled for introduction around 2010, with minimal jurisdictional variations so as to enable a smooth transition to a uniform national regime at a later date.

5.4 Other issues in key specific areas

Support for low income and other disadvantaged consumers of utility services

As alluded to in section 5.3, because of the difficulties that low income and other disadvantaged consumers can face in paying for utility services, Australian governments provide explicit support through a variety of CSO and USO arrangements. In addition, many suppliers have in place hardship programs that provide for flexible payment options and procedures to minimise the risk of disconnection (box 5.10). In Victoria it is mandatory for retail energy providers to provide such programs.

Though a detailed assessment of these CSO/USO and hardship arrangements would undoubtedly reveal scope for improvement in their content and configuration², for the most part, they are a sound way of assisting ‘at risk’ consumers. Hence, the Commission sees such arrangements as being an integral component of the consumer protection regime for utility services in the years ahead.

² See, for example, Telstra, sub. DR156, p. 10.

Box 5.10 Helping vulnerable and disadvantaged consumers of utility services

Community service and universal service obligations

CSOs are government requirements for service providers to engage in non-commercial activities to promote affordability and access objectives. They apply in a range of sectors and take two principal forms:

- Those that are directly funded by governments, including concessions for low income earners (for example, in energy and water) and the provision of 'uneconomic' services (for example, certain rail services).
- Universal service obligations, such as standardised service requirements for some basic postal and telecommunication services. These obligations are ultimately funded by cross-subsidies between different groups of consumers, despite the commitment by Australian Governments, as part of the NCP process, to fund CSOs directly from consolidated revenue.

Hardship programs

Supplier-provided hardship programs typically offer low income and other disadvantaged consumers payment flexibility, including through payment plans and additional time to pay; and advice on how to reduce service usage and to access a financial relief agency or financial counsellor. While it is mandatory in Victoria for retail energy providers to have hardship programs, there are in fact incentives for suppliers to provide these programs voluntarily. In particular, they can help suppliers to:

- recoup some payment in situations where a customer is simply unable to pay immediately, thus reducing the costs of debt collection; and
- identify potential problem customers and apply preventative measures before substantial debts accrue.

Retail price regulation

But the future role for retail price regulation in containing utility prices is much more problematic.

Retail price regulations for telecommunications and energy services were introduced as a transitional measure following the deregulation of service provision, subject to review and removal once full contestability had been established. Yet though some of these markets are now very competitive, many of these interim price regulations remain in place.

There is little dispute that well designed price regulation can be a useful means of curbing monopoly pricing in utility markets that are not contestable. Given that

many low income consumers have less ‘price elastic’ demand than other service users, they may be particularly disadvantaged by such monopoly pricing.

Equally, retail price regulation can have some unintended costs for consumers:

- Overly stringent price controls may adversely affect the longer term supply of the services concerned. (The most extreme manifestation of this sort of outcome were the interruptions to electricity supply in California in 2000 and 2001.)
- And even where price regulation is limited to specified ‘default’ service contracts — generally the case in Australia — if consumers presume that a control on prices means that the regulated service must be a ‘good deal’, then they may be discouraged from ‘switching’ to potentially cheaper unregulated services. (As well as the adverse impacts for those consumers who remain with a higher cost service, lower levels of switching will potentially lessen competition in the marketplace to the detriment of consumers overall.)

However, to date, the Australian experience has been that retail price regulation has provided sufficient ‘headroom’ to both minimise any risks to longer term supply and to encourage entry by competitors. Thus there are now many licensed retailers in most price-regulated utility markets (see table F.1, appendix F).

There is evidence that some energy consumers could acquire services more cheaply were they to switch from a regulated tariff contract to a non-regulated, ‘market’ contract. For example, in South Australia, one analysis suggested that consumers could save up to 9 per cent on their electricity bills by switching (ESCOSA 2006). That analysis also suggested that a disproportionately large number of consumers on apparently more costly regulated contracts had low incomes.

But there are other reasons why consumers opt to remain on regulated tariffs — including greater simplicity in tariff structures and the costs of investigating the pros and cons of the alternatives. Thus, as the National Consumers Roundtable on Energy (sub. DR199, p. 12) amongst others argued, sticking with the price regulated default contract may be a rational and sensible choice for some consumers.

The Commission therefore concludes that retail price regulation has played a useful role in the introduction of competition to utility service markets. In short, without ostensibly having had any major unintended costs, it has provided a constraint on monopoly pricing in the transition to fully contestable markets.

Equally, once full contestability is achieved, retail price regulation will have little role to play. As in other markets, competition amongst suppliers will best serve to keep prices in check. And while some low income and other disadvantaged consumers will still need help to pay for utility services, this support will be best

delivered through appropriately funded CSO arrangements and supplier-provided hardship programs (see above).

Consistent with this conclusion and the original intent of price regulation, in the draft report, the Commission proposed that:

- remaining retail price controls in the telecommunications sector be immediately removed (reflecting its view that these markets are now fully contestable);
- retail price regulation in fully contestable energy markets also be removed; and
- CSOs and supplier-provided hardship programs be monitored regularly for effectiveness.

There was extensive commentary on this draft recommendation variously supporting its intent; reiterating the underlying arguments for and against retail price regulation; debating the extent of contestability in energy markets and therefore whether it would be premature to remove price regulation at this time; and emphasising the general need for adequate support for low income and other disadvantaged consumers. Significantly, the suggested removal of retail price regulation in the telecommunications sector attracted much less commentary than the energy market component of the proposal, with the ACCC (sub. DR176, p. 7) noting that such regulation has been progressively relaxed as competition between telecommunications providers has taken hold.

Also, several submissions, including some from those supporting the removal of retail price regulation in the energy sector, emphasised that there is already an AEMC process in train for examining the extent of contestability in jurisdictional retail energy markets (see appendix F). The AEMC has now completed its review of the Victorian retail energy market, where it found that competition is effective, and has proposed to the Victorian Government that price controls on services for residential customers be phased out (or removed) from the beginning of 2009 (sub. DR226, p. 56).

In the light of this input, the Commission sees no reason to alter the thrust of the draft report proposal. It reiterates that effective support for low income and other disadvantaged groups should remain a centrepiece of consumer policy in the utilities area. But this is not the role of price regulation. Hence, once utility markets are fully contestable — as the telecommunications market evidently already is — retail price regulation should be abolished.

The Australian Government should remove all retail price regulation applying to telecommunications products and services.

Also, where the Australian Energy Market Commission finds a jurisdictional retail energy market to be fully contestable, the State or Territory Government concerned should remove all retail price regulation in that market as soon as practicable.

Ensuring that disadvantaged consumers continue to have sufficient access to utility services at affordable prices should be pursued through transparent community service obligations, supplier-provided hardship programs, or other targeted mechanisms that are monitored regularly for effectiveness.

Action needed on food regulation

The primary objectives of food regulation in Australia are to protect consumers by ensuring food is safe and suitable, to provide enough information to enable consumers to make informed choices, and to prevent misleading or deceptive conduct.

In 2000, COAG endorsed an intergovernmental agreement to harmonise food standards in Australia and New Zealand, with the Australian and New Zealand Food Regulation Ministerial Council established to oversight food regulation policy. Food standards are set by Food Standards Australia and New Zealand, an independent bi-national statutory authority, and incorporated into the Food Standards Code. The Code is then reflected to varying degrees in the various State and Territory Food Acts, and enforced largely at the state level (the Australian Quarantine and Inspection Service has certain responsibilities at the national level). Also, the ACCC and State and Territory Fair Trading Authorities can invoke provisions in the generic consumer law, such as those relating to misleading or deceptive conduct, for food matters.

A number of reviews in recent years have highlighted problems with the current food regulatory system, as have participants in this inquiry. These issues can be summarised as (Regulation Taskforce 2006):

- overlap and inconsistencies between State and Territory Food Acts, and the Food Standards Code;
- inconsistencies in enforcing standards across jurisdictions;
- lack of enforcement of some elements of the Code; and

-
- protracted timeframes and procedural complexity in developing and amending food standards.

The Australia Food and Grocery Council (sub. DR150, p. 6) submitted that these inconsistencies in regulations and enforcement across jurisdictions lead to ‘unnecessary costs and competitive disadvantages [being] imposed upon food companies that operate across borders’. And Choice (sub. DR194, p. 10) stated that there are ‘serious consumer issues (eg food labelling, obesity) that require consideration’.

In 2007, the Australian Government established the Bethwaite Review of Food Regulation to address many of these issues. Specifically, the review was to draw upon findings of existing reviews and undertake consultations to examine, among other matters:

- alignment of enforcement levels (including penalties) across jurisdictions;
- the future role of the Australian Government in the food regulatory system, including whether it could play a greater role in enforcing standards;
- possible improvements to the mechanisms available to change the food regulatory system, including Ministerial Council processes; and
- reducing the compliance burden on business.

Though there has as yet been no publicly advised outcome from that review process, CoAG recently announced that it has asked the BRCWG to look at how to deliver a more efficient food regulatory regime. Specifically, the BRCWG is to report to CoAG by July 2008 on ‘options for reducing the regulatory burden on businesses and not-for-profit organisations in relation to food regulation, without compromising public health’ (CoAG 2008).

Significantly, many of the concerns relating to food regulation are common to other key industry-specific consumer regulations discussed elsewhere in this chapter. Hence, the intent of the Commission’s proposed review program for industry-specific consumer regulation (see recommendation 5.1) is equally applicable to food regulation. As well as looking at options to harmonise current regulatory requirements, the BRCWG could therefore usefully examine whether the current delineation of responsibilities between the Australian and State and Territory Governments in this area is conducive to delivering effective and responsive food regulation for consumers.

Better consumer protection in the home building sector

A home will typically be the largest purchase consumers will ever make. And for those having that home built, there are an additional range of issues and complexities to negotiate. Hence, consumers need to take great care in choosing the right builder for the job and ensure that they understand the implications of the contract that they sign.

In the majority of cases, domestic building projects are completed with no major problems for the consumer. However, disputes between builders and consumers can arise, both in regard to the quality of workmanship, and to contractual matters. For example, in 2006-07, there were some 1 500 domestic building disputes in Victoria — around 2 per cent of the number of domestic building permits issued (Building Commission 2007).

Consumer protection mechanisms

The generic TPA and FTA provisions relating to merchantable quality and fitness for purpose apply in the home building sector. In addition, the industry is subject to various specific regulation at the state and territory level:

- *Licensing of building practitioners.* All jurisdictions require builders to be licensed, and Queensland and New South Wales also license other building trade contractors.
- *Statutory warranties.* In most jurisdictions, statutory warranties specific to home building require a building contractor to provide a product as agreed in a suitable state, and fit for its intended purpose for a set period of time. That period ranges from five years from completion in South Australia, to seven years in New South Wales. Western Australia and the Northern Territory do not have building-specific statutory warranties.
- *Access to dispute resolution mechanisms.* In Queensland, New South Wales, and Victoria, there are sector-specific ADR bodies. In these jurisdictions and in Western Australia, there are also dedicated appeals tribunals that hear building disputes.
- *Mandatory home builders' warranty insurance.* In all jurisdictions, licensed builders must have home builders' warranty insurance (HBWI)³ — although Tasmania has very recently legislated to remove this requirement. Except in Queensland, HBWI operates as a 'last resort scheme' (see below), provided by private insurers. In Queensland, the Building Services Authority has a monopoly

³ In Western Australia, the product is referred to a 'Home Indemnity Insurance'.

over the provision of HBWI (which is a ‘first resort’ scheme), in addition to acting as the government’s registrar of builders and a customer complaints bureau.

Developments in HBWI

The market for HBWI changed markedly in the mid-1990s when Victoria and New South Wales abandoned government monopoly provision of HBWI, and opened up supply of the product to private insurers. In 2000–2001, poor returns from HBWI, exacerbated by the collapse of HIH and the 2001 terrorist attacks in the United States, prompted several insurers to leave the market, and those that remained moved to limit their risk in offering HBWI. As a result, many (particularly small to medium) builders found it difficult to obtain HBWI, and as such were not able to retain their building licences. In 2002, the New South Wales and Victorian Governments, in consultation with the insurance companies, developed a 10 point plan (box 5.11) that was intended to stabilise the insurance market, while still providing protection for consumers (VCEC 2005). Since then, several insurance companies have entered the HBWI market in these states, and the ‘crisis’ in availability has eased.

The main change ensuing from the 10 point plan was that HBWI effectively became a ‘last resort scheme’, rather than a product providing earlier-stage protection against faulty workmanship, as had nominally been the case in these jurisdictions. (Western Australia and South Australia have always had last resort schemes.) As such, consumer protection now largely relies on the other planks of the consumer protection structure, namely licensing and ADR/legal mechanisms, with HBWI acting as a last resort in a limited subset of cases. Claims against HBWI policies (in all jurisdictions except Queensland) can only be made after all other avenues to have the damage or loss rectified have been exhausted, and are limited to instances where the builder dies, becomes insolvent or disappears and cannot rectify the problem. As a result, the number of claims has fallen in recent years (figure 5.2).

Concerns about consumer protection

Notwithstanding more than 30 reviews of consumer protection in the building industry in the past 10 years (Builders’ Collective of Australia, sub. 7, p. 1), submissions to this inquiry point to significant shortcomings in consumer protection mechanisms in several jurisdictions, and to individual cases of significant detriment to both consumers and builders. Most of these deficiencies relate to the dispute resolution process, and to the HBWI product.

Box 5.11 The 10 point HBWI plan

In May 2002, the New South Wales and Victorian Governments jointly announced a '10 point plan' intended to stabilise the market for HBWI, while maintaining protection for consumers. Under the revised arrangements:

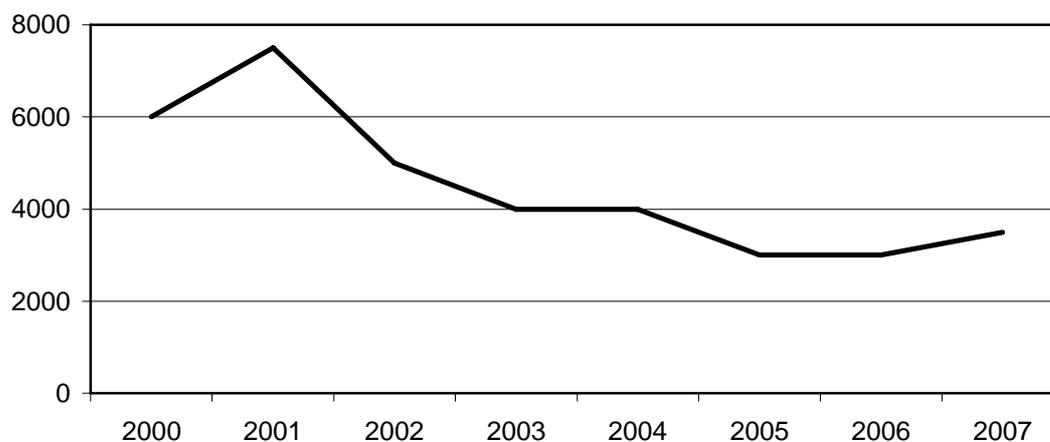
- Homeowners can claim against their policy only as a last resort, when the builder is dead, or insolvent or has disappeared and is not capable of rectifying any defective or incomplete building works.
- Non-completion claims are capped at 20 per cent of the contract price.
- There is a \$12 000 threshold for works requiring a builder to carry insurance.
- There is a \$200 000 ceiling on individual claims.
- Insurers' liability in respect of claims arising from the death, disappearance or insolvency of any single builder is capped at \$10 million.
- Buildings of more than three storeys that contain two or more separate dwellings no longer require HBWI cover.
- There is a six year minimum period of cover for structural defects.
- There is a two year minimum period of cover for non-structural defects.

In addition, the Victorian and New South Wales governments agreed to:

- attempt to harmonise their HBWI requirements in the broad; and more specifically
- harmonise their insurance reporting requirements.

Source: Allan 2002.

Figure 5.2 Number of HBWI claims, Australia, 2000 to 2007



Data source: Vero estimates, pers. comm.

Dispute resolution

As outlined earlier, three jurisdictions have ADR bodies specific to the home building sector. In New South Wales and Queensland, these bodies are able to adjudicate in disputes, while in Victoria, Building Advice and Conciliation Victoria (BACV) provides mediation services.

Submissions to the inquiry suggest that where the use of ADRs is voluntary, a significant proportion of disputes end up in court, where the costs of resolving a dispute escalate. Russell Joseph (trans. p. 68) stated that:

While the Victorian government has instigated the BACV process, consumers have nowhere other than the courts to go if their builder or insurer simply refused to cooperate. The same also applies to builders, with the result being that the winner of the dispute is the one with the deepest pockets to fund what is always a very expensive and complex litigation. I table an article in the Melbourne Age quoting Margaret Lothian, senior member at VCAT: 'It's going to be expensive, starting at \$5000 a day,' Ms Lothian says. 'Even when you win, you can lose.'

Victorian Building Commission data seem to bear this out: in 2006, of the consumers who indicated that their building project ended in serious dispute, about two-thirds required a court decision to resolve the dispute (Building Commission 2007).

Home builders' warranty insurance

Though a cost for consumers, as a last resort product everywhere except in Queensland, HBWI offers little protection to them in most circumstances. Indeed, several participants in the inquiry stated that the use of the term 'warranty' is misleading, implying as it does that it:

... is a policy against faulty workmanship. In reality, it is an insurance policy that carries the cost of finalising the unfinished construction or poor workmanship to a limited value if the builder dies, disappears or becomes insolvent. (John Fulton, sub. 14, p. 2)

And even in situations where HBWI applies, some inquiry participants contended that it does not offer sufficient protection. For example, George Korfiatis (trans. p. 123) highlighted the difficulties that some have apparently experienced in making claims:

We've discovered obviously that the insurance is not accessible until the builder is dead, disappears or is insolvent. It's forced on us and then it's highly conditional and unlikely to access it. It shouldn't be called warranty insurance the way it's currently structured because you've got to finish your court battles with the builder and then you've got to start another one with the insurer. If consumers knew the whole process,

and the legal system and the way it's set up right now, they would not bother. The commercial decision would be, 'Forget about it'.

Moreover, as well as these concerns about the protection provided to consumers, several inquiry participants claimed that the eligibility conditions for securing insurance adversely affect many builders.

Given that the incidence of insolvency in the industry has historically been quite high, insurers writing HBWI policies assess the eligibility of builders for insurance based on the assets in their business, with insurance typically capped at a certain turnover level. In addition, since the collapse of HIH, insurers have routinely sought indemnities and bank guarantees from builders before issuing certificates for insurance (Minter Ellison Lawyers 2007).⁴

Insurers claim that these processes have improved the financial viability of the building industry, and that in effect they are carrying out financial vetting on behalf of the State and Territory regulatory authorities. Vero (Suncorp, sub. DR171, p. 10) submitted that:

... the eligibility criteria for HBWI applied by prudent insurers like Vero contributes to ensuring only financially sound, technically competent builders, can access HBWI. Given that HBWI is a prerequisite to the registration/licensing process, this in turn minimises the risks of consumers dealing with at risk builders.

But Keith Atkins (trans. p. 537), a building tradesman, rejected this notion stating that:

... it was fraud in the extreme that this insurance was even called insurance, because we had to provide the backup to the actual insurance.

Additionally, several builders complained that the eligibility requirements for HBWI do not take into account the technical ability or past record of the builder, with eligibility based on capacity to pay should something go wrong, rather than on capacity to complete projects to an appropriate standard. For example, David Wilson and Associates (sub. DR127, p. 2) submitted that:

Under my FAI/ HIH warranty insurance policy 1996-2001 sold to me by the Master Builders Association of Victoria, I was able to pursue building work without major restriction within agreed job cost limits That allowed me and my business to work unhindered. I NEVER HAD A SINGLE CLAIM! ...

⁴ The legality of insurers procuring indemnities and bank guarantees from builders prior to issuing insurance certificates has been called into question by a decision in a West Australian District Court case, which suggests that insurers may be acting in contravention of the Commonwealth *Insurance Act 1973* (Harden Jones Architects, sub. DR214; Minter Ellison Lawyers 2007).

... When HIH collapsed the only warranty insurance I could obtain was via HIA Home owners warranty. The limits applied to my business were unconscionable ... This meant I was restricted to pursuing minor building works for no other reason than the self interests of the insurer.

The Commission's Draft Report

In its Draft Report, the Commission concluded that consumer protection in the home building sector is inadequate in most jurisdictions, and that changes are required. Specifically, it proposed that Australian governments should take early action to provide better and uniform protection for those having a home built or renovated, and that this should entail:

- guaranteed access for consumers to alternative dispute resolution mechanisms;
- greater scope to de-register builders who do not meet appropriate performance standards; and
- a revamping of compulsory builders' warranty insurance to ensure that it is of genuine value to consumers and that consumers understand the product.

In general, there was little demur on the draft recommendations relating to improved access to ADRs and more stringent, performance-based licensing. A notable exception was the New South Wales Government, which said that the NSW *Home Building Act 1989* already provides ample scope for the de-registration of builders who do not meet appropriate performance standards (sub. DR251, p. 13).

There was also considerable support from consumers and individual builders for the proposed revamp of HBWI arrangements. For example, Kim Booth MP (sub. DR210, p. 1) stated that:

It is reprehensible that in a modern democracy the farce of HBWI should still continue as it does in most states of Australia.

Kalida Pty Ltd (sub. DR137, p. 1) submitted that:

As a builder of some 32 years I took great umbrage at the fact that I had to give and still have in place indemnities against my house for a system that does not serve the purpose it's purported to.

And Choice (sub. DR236, p. 10) lent its 'full support' to the draft recommendation.

But there were also criticisms of that part of the Commission's recommendation relating to HBWI, most notably from the Housing Industry Association (HIA) and Vero. Firstly, these participants questioned whether the number of disputes in the home building sector is sufficient to warrant revamping what is a last resort, not a first resort, product. The HIA asked (sub. DR160, p. 5):

If consumers are highly satisfied and if only 1 per cent of domestic building projects end up in arbitration then why should all consumers bear a significant increase in premium just to revamp an insurance package that they will almost never need?

Answering this question requires an analysis of likely insurance increases from suggested revamps and a comparison of that cost compared to the benefit provided.

The Victorian Government (sub. DR226, p. 58) similarly cautioned against ‘seeking to revamp an insurance product which has apparent benefits to some consumers’, though it nonetheless indicated that it is currently considering an expansion of the grounds on which claims against HBWI can be made.

A second and related criticism was that the cost of offering consumers an insurance product triggered at an earlier point in a dispute would be high. On this matter, the HIA (sub. DR160, p. 9) noted that its:

... discussions with insurers about ways to improve HBWI without increasing costs indicate that HBWI insurers are not willing to provide insurance that is triggered simply because a builder has been ordered to rectify faulty work and failed to do so. This is because of the moral hazard involved.

And Vero (Suncorp, sub. DR171, p. 10) stated that ‘private capital would never be used to make a “first resort” HBWI market’.

As a consequence, these participants argued that the focus should be on improving other, first resort, processes such as ADR and licensing, rather than trying to provide insurance against poor workmanship. In this regard, the HIA pointed favourably to the recent developments in Tasmania, noting that it did not see the need for HBWI to be compulsory if the other parts of the consumer protection framework are well-designed. (Even so, its preferred model was to link HBWI to a strengthened licensing system (box 5.12).)

The issues are complex but changes can and should be made

The Commission accepts that the treatment in its Draft Report of the issues surrounding the particular matter of HBWI may have reinforced the misperception that the product could or should be a first line protection against faulty workmanship. Clearly this is not the case, and hence the form and scope of HBWI needs to be considered in conjunction with other, first resort, protections such as ADR and licensing requirements.

But the large number of complaints to this inquiry (citing significant individual consumer detriment) clearly indicate that, despite a multitude of past reviews and frequent changes to the various elements of the regulatory package, consumer protection in the home building sector could be better in most jurisdictions.

Box 5.12 Some proposed changes to consumer protection arrangements in the home building sector

Tasmania

In response to ongoing concerns about HBWI, the Tasmanian Government has recently legislated to make it non-compulsory as part of a suite of changes aimed at improving consumer protection in the home building sector. Other elements of the new policy package include:

- a mandatory dispute resolution process, administered by Consumer Affairs and Fair Trading (CAFT), open to both consumers and builders to initiate.
 - An independent expert adjudicator will attempt to facilitate an agreement between the parties, and will issue a ‘complaint inspection advice’ setting out the terms of the agreement. Non-compliance with this advice will result in the Director of CAFT issuing a rectification order, as will situations where agreements cannot be reached between parties.
 - There will be provision for either party to appeal to the Magistrates Court on the grounds of procedural unfairness;
- some mandated standard contract terms, in order to reduce the likelihood of contractual disputes; and
- mandatory provision of information to consumers on the protections available to them.

Housing Industry Association

In its submission to this inquiry, the HIA proposed a system that would allow an earlier ‘trigger’ point for HBWI in the event of a dispute. The HIA’s proposal would:

- allow builders or consumers to initiate the dispute resolution process, and would separate contractual disputes from factual disputes relating to workmanship. Contractual disputes would be referred to the court system, and factual disputes would be handled by expert on-site adjudication:
 - the adjudicator would be empowered to make binding determinations, underpinned by a an agreed definition of a defect in the form of a guide of tolerances for building works;
- enable appeal of a determination to an expert panel, rather than a tribunal; and
- be linked to the licensing regime. If a builder failed to rectify work determined to be defective after exhausting his/her appeal rights, then loss of licence would ensue. In this circumstance, HBWI would be triggered.

Sources: Department of Justice (Tasmania) 2008; HIA sub. DR160, p. 10.

The overriding requirement for a better regime is that, in all parts of Australia, consumers and builders have guaranteed access to effective ADR. In New South Wales and Queensland, where use of ADR is mandatory before cases can proceed

to court, there seems to be somewhat less disquiet than elsewhere. In Queensland, the QBSA resolves over 70 per cent of claims before they go to the tribunal, and 80 per cent of those without requiring formal directions to rectify works (QBSA 2006). And in New South Wales, the early intervention dispute resolution service offered by the Office of Fair Trading has reduced the volume of building complaints going to the Consumer, Trader and Tenancy Tribunal by approximately 30 per cent. (sub. DR251, p. 13).

As well, in most jurisdictions, licensing needs to be more closely linked to the actual performance of builders. Previous inquiries (such as Allan 2002; VCEC 2005) highlight that one of the main strengths of Queensland's consumer protection system in the home building area is that there are linkages between a builder's performance — in terms of the history of claims against him or her — and consideration of ongoing registration. Such linkages provide both an incentive for builders to maintain high consumer service standards, and a means to remove underperforming builders from the industry.

But while access to ADR and more effective licensing are the keys to preventing building disputes ending up in the courts, there remains a need to address the HBWI issue, which has been a running sore since the privatisation of these schemes and the (unrelated) collapse of HIH. Undoubtedly, part of the problem is a misperception about what HBWI is and what it can provide for in the event of a building dispute. However, there are valid concerns about its value to consumers, and its impacts on builders and therefore competition in the home building sector.

The Commission is not convinced that reliance on further incremental, jurisdiction-specific, improvements will be sufficient to resolve the concerns surrounding HBWI or to achieve needed improvements in other aspects of consumer protection in the sector. A national approach is required, with the recently announced Senate inquiry into HBWI providing an opportunity for achieving this. If this inquiry adopts a broad focus and looks at the linkages between the last resort HBWI product and earlier stage protections for consumers — as its terms of reference allow it to do — it could be the springboard for facilitating coordinated and nationally-consistent improvements in the overall consumer protection package. More specifically, the inquiry could usefully look at means to improve consumer awareness of what HBWI does and does not cover, and at the case for 'rebadging' the product to more accurately represent its coverage to consumers.

In examining how to improve ‘last resort’ home builders’ warranty insurance, the Senate Economics Committee should also consider how to enhance the effectiveness of earlier stage consumer protection measures in the home building sector, including through:

- *providing for guaranteed access to effective ADR across Australia; and*
- *better linking licensing schemes to actual builder performance.*

6 Supporting institutional changes

Key points

- While CoAG has announced that it will be working with the Ministerial Council of Consumer Affairs (MCCA) in developing national approaches to improve the consumer policy framework, some additional initiatives are needed to facilitate effective and timely implementation of the new framework and build support for it.
- All jurisdictions should ensure that their current governmental structures give sufficient prominence to consumer policy and that their intra-government coordination mechanisms in this area are effective and promote consistent consumer policy approaches across all relevant portfolio areas.
- The Australian Government should enhance the capacity of the Commonwealth Consumer Affairs Advisory Council to play an active role in advising on emerging, nationally significant, consumer policy issues and on other consumer matters requiring further research.
- To enable MCCA to play a more productive role in the future development of consumer policy, changes should be made to improve the Council's effectiveness and efficiency:
 - its voting rules should be altered, such that future policy changes would only require the agreement of the Australian Government and three other jurisdictions (a similar arrangement to those for competition and corporations law);
 - the MCCA secretariat should be sufficiently resourced to carry out policy development work (including the preparation of regulation impact statements) as well as administrative functions; and
 - accountability and transparency should be increased through improved public reporting of meeting agendas and outcomes. MCCA should also seek greater stakeholder input on its strategic agenda and performance.

Implementation of a new nationally coherent consumer policy framework will require considerable cooperation between Australian Governments and effective processes for keeping the reform process on track. To this end, CoAG has announced that the Business Regulation and Competition Working Group, in consultation with MCCA, will be responsible for the development of enhanced national approaches to improve the consumer policy framework. However, some additional changes to institutional arrangements, discussed in this chapter, are

necessary to build support for the new nationally coherent policy regime and facilitate more timely changes to it in the future.

6.1 Elevating the importance of consumer policy

Implementation of the Commission's framework recommendations in the two previous chapters would, over time, see the Australian Government assume progressively more responsibility for consumer policy matters. This might sometimes require specific initiatives to facilitate a more prominent role for the Australian Government in particular areas of consumer policy development and enforcement.

However, the perception in some quarters that consumer policy has been a low priority for the Australian Government could be a more general obstacle to the development of a nationally coherent policy framework. Indeed, some participants indicated that their support for transfer of more responsibility to the national level was subject to the proviso that more prominent consumer policy institutions be established within the Australian Government (eg Victorian Government, sub. DR226, p. 5).

The recent decision by the Australian Government to create a Minister for Competition Policy and Consumer Affairs — responsible for formulation, implementation and administration of competition and consumer policy, including consultative arrangements with the States and industry bodies — will be helpful in this context. These matters were previously the responsibility of the Parliamentary Secretary to the Treasurer.

Also, the portfolio linkage between consumer and competition policy has been maintained. This will preserve the important synergies and inter-relationships between the two policy arms (see box 4.6).

However, there may still be a need for changes to deliver better cross-department coordination of consumer policy issues within the Australian Government. Consistency in approaches within a government is likely to be just as important as between levels of government — especially when that government is taking on significant new policy development and enforcement roles. Some have contended that, at present, there is little such coordination (Choice, sub. DR194, p. 9; Victorian Government, sub. DR226, pp. 8, 41-42; ADMA, sub. DR231, p. 7).

Similar changes in some states and territories to raise the profile of consumer policy and improve coordination within government may also be warranted, especially while they retain responsibility for both generic law enforcement and a significant

amount of industry-specific consumer regulation. As the Australian Finance Conference (sub. DR216, pp. 2-3) indicated, a feature of the consumer affairs portfolio is that it is usually relatively junior and, depending on the jurisdiction, can sit below quite diverse Cabinet functions such as Treasury, Commerce, Attorney-Generals or Justice, each with their own policy priorities.

To further improve the prominence of consumer policy at the Australian Government level, the capacity of the Commonwealth Consumer Affairs Advisory Council (CCAAC) could usefully be enhanced. As its name suggests, CCAAC's primary role is to provide the Minister for Competition Policy and Consumer Affairs with independent advice on current and emerging consumer issues. As part of this role the Council also:

- investigates and reports to the Minister on consumer issues referred to it by the Minister; and
- considers reports and papers referred to it by the Minister and reports to the Minister on their likely consumer impacts.

CCAAC currently has thirteen members from a range of industries and backgrounds, including both an Indigenous and a youth representative.

Some participants contended that CCAAC could do considerably more than it does at present (Choice, sub. DR194, p. 9). The Commission concurs — at least outwardly, there is little to suggest that CCAAC has been particularly influential in informing consumer policy decision making at the Australian Government level. But with some modest additional resourcing, and with a membership providing greater access to core consumer policy expertise and greater capacity to bring a national perspective to bear, CCAAC could play a more influential role in advising on emerging, nationally significant, consumer policy issues. For example, it could advise the Minister:

- on areas where improved enforcement might be a better option than further regulation; and
- when an inquiry by a regulator into consumer issues arising in a particular market might be appropriate.

It could also be an important source of advice on information gaps and emerging issues which require further research.

RECOMMENDATION 6.1

As part of the transfer of greater responsibility for consumer policy to the national level, the Australian Government should ensure that there are effective arrangements in place to:

-
- *facilitate enhanced coordination between Treasury and other relevant government portfolios;*
 - *promote consistent consumer policy approaches and outcomes across portfolios; and*
 - *enhance the profile of consumer policy across government generally.*

States and Territory Governments should similarly ensure that their current governmental structures promote coordinated and consistent consumer policy approaches and outcomes and give sufficient profile to consumer policy across all relevant portfolio areas.

RECOMMENDATION 6.2

The Australian Government should enhance the capacity of the Commonwealth Consumer Affairs Advisory Council to advise the Minister on emerging, nationally significant, consumer policy issues and on other consumer matters requiring further research (see recommendation 11.3). Specifically the Government should:

- *provide additional resourcing to support the Council's advisory role; and*
- *ensure that membership of the Council is selected to provide the necessary core consumer policy expertise and to bring a national perspective to its advisory functions.*

6.2 Any potential role for financial incentives?

Transfers of responsibility to the national level sometimes have involved the Australian Government making financial payments to the states and territories. For example, under National Competition Policy (NCP), part of which established national competition laws, the Australian Government paid State and Territory Governments \$5.3 billion over 9 years (NCC 2006). And, for the transfer of responsibility of corporations and financial services, the Australian Government pays an ongoing amount of nearly \$170 million annually, indexed to inflation. More generally, the Australian Government has sometimes agreed to make payments to the States and Territories for the implementation of worthwhile reforms — recently, for the National Reform Agenda and water reforms (CoAG 2006a).

The NCP process demonstrated that financial payments can motivate sustained reform (PC 2005b, p. 380). And in elaborating on some of the impacts of incentives on the reform process, the National Competition Council (NCC) observed that:

Apart from the magnitude of the funding, tying performance to financial rewards has enabled governments to eschew pressure from lobby groups by claiming they have no

option other than to meet their NCP commitments. At the officials' level, the effect of competition payments has been to empower jurisdictional competition policy units to a far greater extent than otherwise. (NCC 2004, p. 36)

But the case for such incentives appears weaker in this instance than for these other reform programs.

A rationale for incentives could be constructed around the wider benefits of fostering national markets through greater uniformity in consumer policy approaches, at least insofar as the national benefits considerably exceeded the benefits to individual jurisdictions.

Importantly, however, in contrast to the transfers of responsibilities for competition and corporations laws, the transfer of responsibility that would result from implementation of the Commission's proposals in the consumer area would not have negative revenue implications for the States and Territories. In fact, their reduced policy development and enforcement role could result in some budgetary savings for them. This would tend to offset any arguments for incentives based on national market 'externalities'.

In addition, when the transfer of responsibility for competition policy was agreed to, the States and Territories lacked a significant tax base that grew in line with economic growth. Accordingly, the tax dividend from the increased economic activity ensuing from the reforms, disproportionately went to the Australian Government. But since then, the arrangements for distributing the revenue collected from the Goods and Services Tax to the States and Territories have somewhat addressed this issue. To the extent that the proposed consumer policy reforms increase the future income base, those gains would flow to the States and Territories consistent with the growth in GST revenues.

Accordingly, the Commission remains unconvinced that financial incentives are needed to facilitate the proposed reforms to the consumer policy framework. Significantly, the same conclusion in the Commission's draft report elicited no responses in subsequent submissions.

6.3 Facilitating timely and effective policy changes

In March 2008 CoAG agreed that the recently established CoAG Business Regulation and Competition Working Group (BRCWG — see box 6.1), in consultation with MCCA, will be responsible for the development of enhanced national approaches to improve the consumer policy framework — drawing on the

recommendations and analysis in this report. The intention is that CoAG will agree on a new national approach in October 2008.

Box 6.1 CoAG Business Regulation and Competition Working Group

The CoAG Business Regulation and Competition Working Group is one of seven working groups established by CoAG at the end of 2007. Each working group is overseen by a Commonwealth Minister, with deputies who are nominated by the States and Territories at a senior departmental level.

The objectives of the Business Regulation and Competition Working Group are:

- To accelerate and broaden the regulation reduction agenda to reduce the regulatory burden on business.
- To accelerate and deliver the agreed CoAG regulatory hot spots agenda.
- To further improve processes for regulation making and review, including exploring a national approach to processes to ensure no net increase in the regulatory burden, and common start dates for legislation.
- To deliver significant improvements in Australia's competition, productivity and international competitiveness.

Source: CoAG 2007b.

This implementation arrangement will have several benefits. It will provide necessary national oversight of the reform program; help to ensure that changes are made in a timely fashion; and take advantage of MCCA's consumer policy expertise in the many detailed implementation issues that will inevitably arise.

But though critical to implementing a more coherent consumer policy framework in the short-term, this is not all that is required. As markets and consumers' needs and characteristics evolve, further changes to the policy framework will be required. On the presumption that the States and Territories continue to have a significant policy and regulatory role, MCCA will in turn remain a potentially key player in facilitating effective and timely policy change. In particular:

- With the States and Territories and the ACCC jointly enforcing the new national generic consumer law, it will remain a high level vehicle for promoting coordinated and consistent application of those regulatory requirements.
- It will similarly be a vehicle for promoting national consistency in industry-specific consumer regulation that remains the responsibility of the States and Territories (and that does not fall within the remit of other Ministerial Councils).
- And it will be a forum in which the States and Territories can put their views on issues relating to those parts of the policy framework residing with the Australian Government, including the need for any policy changes.

However, without changes to address MCCA's generally acknowledged problems, it is unlikely to be effective and influential in this role. In particular, as discussed in chapter 4, some important issues have taken several years to progress through MCCA.

There are many reasons for this lack of timeliness in decision making and implementation, some of which reflect the vagaries of a Federal system, including:

- responsible Ministers frequently changing;
- lack of resourcing in individual sponsoring agencies undertaking cross-jurisdictional policy development;
- at least one government typically being in caretaker mode; and
- the inconsistent pace at which individual jurisdictions apply template legislation.

Some State Governments (Victorian Government, sub. DR226, p. 40; and the South Australian Minister for Consumer Affairs, sub. DR219, p. 3), and other participants like the Joint Consumer Groups (sub. DR228, p. 7), contended that another major reason for MCCA's lack of progress on some key policy issues has been the prolonged delays in receiving 'clearance' from the Office of Best Practice Regulation (OBPR) for proposals requiring a Regulation Impact Statement (RIS)¹. For example, though acknowledging the need for robust regulatory assessment, the South Australian Minister for Consumer Affairs said that the RIS process:

... has been used in practice to delay or prevent important MCCA policy projects without an appropriate evaluation of the merits. (sub. DR219, p. 3)

Moreover, the Victorian Government (sub. DR226, pp. 32, 36) and the Western Australian Department of Consumer and Employment Protection (WA DOCEP, sub. DR248, p. 2), amongst others, claimed that in some areas where delays have occurred, it has been mainly due to the difficulty in securing Australian Government agreement to policy proposals.

But irrespective of the source of delays, consumers continue to suffer detriment because of policy inertia.

In the Commission's view, there are changes that could be made to improve the timeliness of MCCA's decision making.

¹ The OBPR assesses whether a RIS has fulfilled the *CoAG Best Practice Regulation Guidelines*. While it does not have any power over decisions made by Ministerial Councils, CoAG has directed the Office to provide independent advice to it on the adequacy of regulation impact statements prepared for Councils.

Currently, decision making within MCCA involves consultation between Ministers and senior officials of all Australian Governments and the New Zealand Government, with policy changes only progressed on a consensus basis. Moving to an alternative voting arrangement which did not give each individual jurisdiction a veto power would be one way to facilitate more timely outcomes. Notably, the transfer of responsibility for competition and corporations law to the national level was accompanied by such a change in voting rules. Specifically, the arrangements in these two areas require that all changes receive the assent of the Australian Government and three other States and Territories (under corporations arrangements two of these three must be States). In the draft report, reflecting the proposed transfer of responsibility to the national level for some key areas of consumer policy, the Commission suggested that a similar voting arrangement should also be employed within MCCA.

A number of participants, including several State Governments, rejected the notion that the Australian Government alone should have a veto power (Victorian Government, sub. DR226, p. 40; the South Australian Minister for Consumer Affairs, sub. DR219, p. 10; Joint Consumer Groups, sub. DR228, p. 6; WA DOCEP, sub. DR248, p. 13). Indeed, some suggested that it could perpetuate the sort of delays that have been evident in the past when only the Australian Government has been opposed to policy changes (REIA, sub. DR172, p. 12).

However, some State Governments recognised that reaching decisions by consensus can result in a stalemate, and were generally supportive of a shift to a two-thirds majority voting arrangement (NSW Government, sub. DR251, p. 20; Victorian Government, sub. DR226, p. 40; the SA Minister for Consumer Affairs, sub. DR219, p. 10). For example, the SA Minister for Consumer Affairs referred to this precedent in some other Ministerial Councils:

Several Ministerial Councils make decisions by a two thirds majority. In addition, changes to the Credit Code must not be introduced by a State or Territory unless there has been a resolution of MCCA passed by a majority comprising at least two-thirds of the members who are present and vote. (sub. DR219, p. 10)

As this commentary indicates, change to MCCA's voting rules will be a contentious issue — especially if it involves giving the Australian Government a right of veto. Nonetheless, in the Commission's view, implementing a corporations law style voting arrangement would have important advantages:

- It would be consistent with the intention of the proposed package of institutional reforms to move more responsibility for consumer policy and enforcement to the national level.
- On those occasions where there is a divergence between the national interest and State or Territory interests, it is obviously desirable that the national interest

takes precedence. This will be only possible if the Australian Government has a veto power in the Ministerial Council.

That said, such a change to voting rules will not of itself be sufficient to expedite decision making within MCCA. Often delays have occurred even where there is consensus on the nature of the policy change required. Some further steps that could be taken to improve the performance of MCCA are:

- Boosting the skills and resourcing of the MCCA secretariat to carry out policy development, including undertaking regulation impact statements.
- Improving the transparency and accountability of the operations of the Council.

A number of participants commented that MCCA is not sufficiently resourced with policy staff to drive its agenda (eg Joint Consumer Groups, sub. DR228, p. 6; Victorian Government, sub. DR226, pp. 40-41). At present, the MCCA secretariat is based permanently in the Commonwealth Treasury and does not have a policy development role. Its responsibilities are administrative in nature (ie. the preparation of agenda items and minutes for meetings, managing secretariat finances, records management, website updates, etc). Policy development, including regulatory impact assessment, is contracted out to individual State and Territory Departments of Consumer Affairs and Fair Trading on a proposal-by-proposal basis. Carrying out this work requires individual jurisdictions to re-allocate their, often limited, existing resources.

In the Commission's view, there is a case for giving the secretariat sufficient resources to do both policy development work (including where appropriate through engagement of consultants) and administration. An appropriately skilled and adequately resourced MCCA secretariat would obviate or greatly reduce the need to devolve policy work and the preparation of RISs to individual jurisdictions. This arrangement would be akin to what has recently been announced for the permanent secretariat supporting the Standing Committee of Attorneys-General².

In addition, transparency can play an important role in making organisations accountable for their performance. In the Commission's view, there is scope for MCCA to do better on this score, in particular, through improved public reporting of its meeting agendas and outcomes. For example, in criticising the Commission's assessment of MCCA's progress on consumer issues (table 4.1), the Victorian Government referred to progress that had been made in some areas but which had not been publicly reported in a communiqué (sub. DR226, p. 35). Better reporting

² See Eyers, J. 2008, 'A-G sets agenda for SCAG support unit', *The Australian Financial Review*, 28 March 2008, p. 58.

of these matters would be consistent with the intent of CoAG's broad protocols and general principles for the operation of Ministerial Councils³.

Moreover, some participants raised concerns about the level of MCCA's stakeholder consultation, particularly in regard to its strategic agenda and performance (REIA, sub. DR172, p. 12; Choice, sub. 88, pp. 47-49; GE Money, sub. DR208, p. 2). Improved transparency in policy development, through enhanced consultation, would provide added discipline on MCCA to operate efficiently and effectively. Such greater engagement with stakeholders would also be consistent with the aim of CoAG's broad protocols *'to facilitate high-quality consultative decision-making, through a robust framework that is accountable, fiscally prudent, and administratively efficient.'* (attachment E, CoAG 2004)

Of course, the proposed changes outlined above are not a panacea. Complex policy issues will still take time to work through and they will still involve consultation with nine Australian jurisdictions and New Zealand. Nonetheless, the changes should contribute to more effective and timely decision making by MCCA to the benefit of Australian consumers.

RECOMMENDATION 6.3

Australian Governments should agree to the following changes to improve the effectiveness of the Ministerial Council on Consumer Affairs (MCCA).

- ***The Council's voting rules should be altered such that future policy changes would only require the agreement of the Australian Government and three other jurisdictions (a similar arrangement to those for competition and corporations law).***
- ***The MCCA secretariat should be sufficiently resourced to carry out policy development work (including the preparation of regulation impact statements) as well as administrative functions.***
- ***MCCA should be made more accountable for its performance through improved public reporting of meeting agendas and outcomes. It should also seek greater stakeholder input on its strategic agenda and performance.***

³ See Attachments E and F, CoAG Communiqué 25 June 2004.

7 Unfair practices and conduct

Key points

- Existing consumer laws deal adequately with most instances of unfair practices and conduct.
- However, there is a gap in provisions relating to unfair contract terms.
 - There are sound economic and ethical rationales for proscribing unfair contract terms that cause consumer detriment.
 - The existing unconscionability provision of the generic consumer law prohibits the abuse of unfair terms only in constrained circumstances, is very costly and slow to use, and lacks clarity about its application in this area.
- Despite sound in-principle arguments for intervention, the cost-benefit tradeoff for a new national provision against unfair contract terms is difficult to judge.
 - The aggregate benefits of a law against unfair contract terms are hard to assess. This is because, whilst there is persuasive evidence of the prevalence of unfair terms, there is limited information on the extent of the detriment associated with them and because the nature of the problem can make it difficult to collect data.
 - On the other hand, there is little evidence in Victoria or in the other countries that have enacted laws against unfair contract terms, of significant business compliance or other burdens. Indeed, some businesses in Australia have supported such regulation and many are used to complying with provisions against unfairness in industry codes.
 - The absence of a provision dealing with unfair contract terms in the Trade Practices Act has already led to one state enacting its own law and others may introduce different laws. A uniformly adopted provision would aid in the development of a nationally consistent generic consumer law.
- The Commission considers that, on balance, a law that addresses unfair terms is warranted. The regulatory risks entailed by such a new law could be reduced by:
 - taking account of the full circumstances of the contract, including any beneficial or adverse effects of changes to unfair terms for consumers generally; and
 - excluding upfront price terms and negotiated contracts from its scope.
- Any law would need to incorporate the capacity for a class of affected consumers or a regulator to take representative actions to achieve redress since, by their nature, unfair terms can affect large groups of individuals.
- The main remaining policy issue is whether unfair terms should be addressed ex ante on the basis of their likely detriment for consumers, or ex post after establishing detriment. While the two approaches are less different than is often supposed, the key tradeoff is between greater pre-emption of unfair terms on the one hand, and an additional reduction in the risk of regulatory overreach on the other. For the interim at least, the Commission favours the ex post approach.

7.1 Introduction

Measures against unfair conduct and practices are a key element of generic consumer law. These measures adopt a dual approach. For example, under the Trade Practices Act (TPA):

- there is a prohibition of unconscionable conduct generally (part IVA); and
- Division 1 of Part V prohibits various broad kinds of unfair practices, notably misleading or deceptive conduct (s. 52), and false and misleading representations (s. 53). In addition, the TPA proscribes some specific practices that are considered deceptive or unfair (including referral selling, bait advertising, and pyramid selling).

There are similar, but not identical provisions in the State and Territory Fair Trading Acts.

This chapter is not a forensic economic or legal examination of all elements of these provisions, since the purpose of the inquiry is to lay out a framework for consumer policy in the future. Consequently, this chapter examines three broad issues, with most of the effort spent on the last:

- whether there is an advantage in having a general prohibition on unfair commercial practices;
- the implications of variations in laws against unfair conduct between jurisdictions; and
- any significant or emerging gaps in the coverage of provisions against unfair practices and conduct and especially the role that might be played by a measure to deal with unfair contract terms.

7.2 A general provision relating to unfair practices?

The prohibition of unconscionability in the generic legislation represents a general prohibition of unfairness, but usually only for unfairness that crosses a high threshold of severity. Other Australian provisions relating to unfair conduct only deal with specific instances of unfair practices, such as deceptive conduct. As a result, there is no broad prohibition on unfair practices by business in Australia, unlike the USA, which bars unfair or deceptive acts and practices, or Europe, which applies an *Unfair Commercial Practices Directive*. Several participants suggested the adoption of a similar provision in Australia (Queensland Government, sub. 87, pp. 52ff; Luke Nottage, sub. DR114, p. 7; and the Consumer Action Law Centre,

sub. DR241, p. 6), while Frank Zumbo suggested the introduction of a general standalone duty of good faith (sub. DR217, pp. 4ff).

Conceptually, a broad provision against unfairness is attractive because it can avoid prescription of specific types of unfairness and, in theory, does not need to be continually adapted as new commercial expressions of unfairness are discovered. For example, the USA has used its general provisions to bar emerging threats, such as spyware and unauthorised telephone billing.

However, in practice, the application of the US provisions — the most mature broad law against unfairness — has periodically raised major concerns, due to changing interpretations of unfairness. In the 1970s, for example, an excessively wide-reaching interpretation of unfairness was accompanied by ‘rulemaking frenzy’ by the Federal Trade Commission, which culminated in its temporary closure by Congress (Muris 2004). While that frenzy has passed, the general provision has been subject to several phases in its reach since that time (Beales 2003). In any case, the statute does not stand by itself. It is accompanied by various specific laws dealing with unfair and deceptive practices. These include provisions requiring truth in lending and fair labelling, and laws against spam. Similarly, the European Union’s *Unfair Commercial Practices Directive* is supported by 31 specific proscribed practices.

So, in fact, the differences between this general regime and current trade practices laws in Australia are not as great as might be thought, especially given the relatively broad range of instruments that are already included. The potential value of a general regime in deterring new forms of businesses misconduct (what Luke Nottage, sub. DR114, p. 7 refers to as ‘educative effects’) could arguably also be achieved by ensuring that statutes barring newly developed forms of unfair conduct are incorporated into trade practices law when the need arises. Moreover, in practice, a general fairness provision may not be as adaptable in dealing with new problems. For instance, despite its generic fairness statute, concerns about unfair contracts arise in the USA as much as here (appendix D).

In that context, introducing a general provision against unfairness might be more conceptually neat than practically useful for consumers. Nevertheless, the Commission agrees with the ACCC (sub. 80, p. 72) that it would be prudent for Australian policymakers to see how the European model develops, and only to consider the option of pursuing a general unfair practices provision at a later time if warranted by strong evidence in its favour.

7.3 Variations and a national generic consumer law

The key features of the TPA relating to unfair practices are replicated in FTAs. However, there are several variations between the Acts, set out in the research undertaken by Corones and Christensen (2007, pp. 58-63) for the Commission and identified by the ACCC (sub. 80, pp. 120-21). The implementation of a national generic consumer law to apply in all jurisdictions, as recommended by the Commission, would eliminate all such differences.

Where similar, but not identical, fairness provisions exist in the TPA and FTAs, the TPA should usually provide the basis for the provision in the new national law (chapter 4). In the one area of greatest current difference — the treatment of unfair contract terms — the Commission is proposing a new provision in the generic consumer law that would provide a national approach to this issue (section 7.5). Most of the other distinctive differences between the TPA and the FTAs arise from the fact that FTAs include prohibitions on specific instances of unfair conduct that are, in theory, already outlawed by more general prohibitions of a wider class of unfair practices.

While exclusive reliance on a general provision is often the best option, there can sometimes be a case for preserving such specific prohibitions in a broader regime. Specific prohibitions nested within general prohibitions may clarify the application of laws (Legal Aid Queensland, sub. 51, p. 2; ANZEWON, sub. 64, p. 28; and Consumer Action Law Centre, sub. 94, p. 73).¹ The Commonwealth Consumer Affairs Advisory Council (sub. 38, p. 7) observed:

Legislated broad prohibitions on unconscionable conduct or misleading conduct can look attractive on the statute books. However, until they are interpreted and applied through expensive legal process (which the size and nature of consumer claims may not justify bringing) they may have only a diffuse deterrent effect.

The prohibition of mock property auctions provides one example of this. Such auctions usually take the form of bidding at an auction by non-genuine bidders who have no real intention to buy the property and without disclosure of their interest — ‘dummy’ bidding. They are barred in most States through provisions in FTAs,² and in Western Australia and NSW as part of other specific statutes. There is no explicit equivalent in the TPA. There is a strong *prima facie* case that mock auctions undermine the probity of the auction process, to the likely detriment of consumers.

¹ Such nested provisions are already common in part V of the TPA. For instance, false representation, bait advertising and a score of other provisions can be seen as specific instances of misleading or deceptive behaviour.

² Real Estate Institute of Australia (REIA, sub. 39, attach. 1).

While usually mock auctions affect the real estate industry, their importance may be accentuated given the rising use of Internet auctions.

Samuel (2004), while approving specific State statutes against the practice, suggests that the misleading or deceptive conduct provisions of the TPA could also be used to prohibit it, as does REIA (sub. 39, p. 7). On the other hand, Corones and Christensen (2007, p. 77) observe that the only likely general provision that might outlaw mock auctions is s. 53 of the TPA, which relates to false representation of goods. They note that it might be difficult to act using this general provision because it usually relates to misrepresentation about the nature of the goods being traded, and not the conduct of the auction. Finally, mock auctions might alternatively be cast as an ‘unglorified form of collusion’ (Gans 2006), though striking it out on those grounds may be pushing the limits of part IV of the TPA.

Either way, a separate single national provision would clarify the unfair and inefficient nature of the conduct, while eliminating the significant variations in the present specific statutes identified by REIA (sub. 39, pp. 6-8 and attach. 1). The fact that the most populous states have already enacted a provision against mock auctions suggests that there may be grounds for including it in the national generic consumer law on pragmatic grounds alone.

In some other instances, the grounds for specific prohibitions in the FTAs are less clear-cut. This, for example, may apply to NSW provisions that extend a general prohibition of false representations to specific false representations relating to residential tenancy, retirement contracts and holiday occupation agreements. Since all other jurisdictions appear to deal adequately with such issues using general provisions against false representations, it appears likely that these specific approaches could be removed in a single national generic consumer law. The question of the extent to which a national uniform generic consumer law should incorporate specific features of State and territory FTAs is discussed in chapter 4.

7.4 Misleading or deceptive conduct

The key outstanding issues in a framework policy report such as this are any major deficits or gaps in protections for consumers against unfair practices and conduct. The Commission’s analysis, supplemented by the views of participants, identified two areas where concerns should be focused:

- misleading or deceptive behaviour (the subject of this section); and
- unfair contracts (section 7.5).

Assertions of misleading or deceptive behaviour are by far the most common area of complaint made to the national regulator (ACCC, sub. 80, p. 37), so it is clearly important that section 52 of the TPA operates well. Many of the concerns of participants, including the ACCC, about this section relate to its appropriate enforcement and the incapacity of the regulator to undertake effective representative actions on behalf of consumers adversely affected by unfair business conduct (issues that are addressed in chapters 9 and 10). However, there are also concerns relating to:

- the capacity of the provisions to deal with cases where lack of comprehensibility might constitute a contravention; and
- whether the provisions should also be applicable to ‘free’ goods and services.

Comprehensibility

An emerging issue is the extent to which lack of comprehensibility in contracts, advertising, signage or labelling might constitute misleading or deceptive conduct under s. 52. This raises the desirability of amendments to s. 52 or the introduction of a new ‘comprehensibility’ requirement into the national generic consumer law, as recommended by the Consumers’ Telecommunications Network (sub. 78, p. 8). Many participants urged the adoption of a particular form of comprehensibility requirement — plain English standard-form contracts — as part of reforms relating to consumer contracts generally (for example, Choice, sub. 88, p. 81 and Frank Zumbo, sub. 49, p. 4). The *Victorian Fair Trading (Amendment) Act 2003* incorporated such a requirement (s. 163) as part of a suite of changes centred on controlling unfair contracts. The Australian Communications Industry Forum (ACIF 2005b) Consumer Contracts Code for communications also mandates ‘plain language’ contracts in a similar context. However, the Commission considers that the issue of comprehensibility is broader than any requirement for plain English contracts alone and best viewed, in the first instance, as an issue distinct from unfair contracts.

Lack of comprehensibility could represent misleading or deceptive conduct under s. 52 if its effect is to hide an important provision, such as a disclaimer (ACCC 2007, pp. 17-19). Even failure to provide information — silence — can amount to misleading or deceptive conduct where there is a reasonable expectation that certain information would be disclosed.³

However, the recent *Butcher* case (box 7.1) has blurred the role of s. 52 in dealing with comprehensibility. The case was lost on the grounds that the majority of the

³ *Demagogue Pty Ltd v Ramensky* (1992) 39 FCR 31.

High Court found that a disclaimer, while very small and indistinct, could still be read and that the parties to the contract were sufficiently sophisticated (‘intelligent, shrewd and self reliant’) to take more care in what was a large transaction.

Box 7.1 The case of the small print disclaimer

In *Butcher v Lachlan Elder Realty Pty Ltd (2004) 21 ALR 357*, a real estate agent sold an expensive waterfront property to a wealthy and intelligent buyer. The marketing brochure was handed to the buyer with the assurance that this was ‘all you need to know’. It included a survey diagram that was relevant to the boundaries of the land. The brochure provided — in small and indistinct writing — a disclaimer about the accuracy of any of the information in the brochure. This was not directed specifically at the survey diagram, which indeed proved to be wrong following a change in the high water mark since the survey had been completed, with significant financial consequences for the buyer.

The buyer attempted an action under s. 52 and ultimately lost in the High Court (passed by a majority with two dissents). The loss hinged on the facts that the buyer was sophisticated and that a disclaimer was made, which while small, could still be read.

The case raised two significant questions:

- What constitutes comprehensibility? There was disagreement about the extent of comprehensibility, with the majority of judges indicating that the brochure was short and the type, while small, was still legible. The dissenting judges deplored the disclaimer because of its small (‘tiny’) and blurry character.
- To what extent should comprehensibility take account of the traits of the parties to a contract? The case suggests that a judgment about misleading or deceptive conduct must take account of the characteristics of the person/s affected by the conduct, not the general class of people who might be so affected. In this instance, this meant that the fact that the buyer was shrewd, intelligent and wealthy was given prominence, reducing the responsibility the real estate agent might otherwise have had.

Source: Pengilley (2005).

This case highlighted two issues. First, judicial interpretation of the adequate visibility and specificity of disclosure will play an important role in deciding some cases under s. 52.

Second, the *Butcher* case raises questions about the extent to which suppliers may escape prohibitions against misleading or deceptive conduct in circumstances where sophisticated buyers are involved. Sometimes the sophistication of the buyer increases their responsibility for care in transactions and therefore the threshold for action under the TPA. But in other instances, the sophistication of the buyer cannot

help them reduce the risk of being misled. As Pengilley (2005) argues, it is not clear that sophistication of a buyer would equip them with the capacity to be particularly cautious about the accuracy of a document, and the fact that the transaction was costly might equally suggest prudence in divulgence by the seller as much as the buyer.

The precedent set by the *Butcher* case is probably not one that would allow sellers generally to be confident that they could use vague, small print disclaimers, though it raises uncertainty in this area. Equally, there is now more uncertainty about the extent to which the traits of the consumer affect the coverage of s. 52.

A more explicit comprehensibility provision in the national generic consumer law (as envisioned by some inquiry participants) that required appropriate divulgence of disclaimers and clarity generally might deal with this uncertainty. Such a provision could also reduce the scope of suppliers to use complex terms to cloak unfair contractual conditions or to obscure consumers' statutory rights (for example, in relation to minimum statutory warranties — as raised by Luke Nottage, sub. DR114, p. 8). And, it is generally more efficient for suppliers to produce comprehensible contracts and other statements for consumers, than for consumers individually to attempt to interpret complex terms.

Judicial consideration of a comprehensibility requirement could be guided by some principles, such as whether the disclaimers were onerous; whether a reasonable consumer would be able to find and use the information disclosed; and the size of fonts and the clarity of language.

However, while the trend to plain English contracts is worthwhile, there are arguments against a mandated provision. First, comprehensibility requirements may lead to (potentially vexatious) claims by careless parties that they had not understood a contract. The current jurisprudence is that knowledge of a written contract is presumed if a party signs it (Clarke and Kapnoullas 2001). This creates incentives for due diligence by consumers when entering contracts that expose them to significant risks. That said, there is little evidence so far that Victorian consumers have vexatiously used the comprehensibility requirement of s. 163 of the Fair Trading Act (nor of the Consumer Contracts Code in telecommunications).

Second, a requirement for comprehensibility may not change consumers' propensity to read contracts or disclaimers enough to justify a mandated approach.

Finally, comprehensibility in complex contracts may be difficult to define. Despite the uncertainties of the existing generic consumer law arrangements, successive judgments are likely to define the appropriate extent and nature of comprehensibility in such contracts. Even with guiding principles, it may be

difficult to replicate this flexibility in a specific comprehensibility provision that relates to all contracts.

That does not, however, negate the value of explicitly requiring comprehensibility in some instances. A targeted approach would be to require that disclosures mandated by regulation are readily comprehensible (chapter 11) and to deal with instances when a supplier unfairly uses a contract term (section 7.5). Given these proposals, the Commission is wary about recommending the inclusion of provisions in the proposed national generic consumer law to require ‘comprehensibility’ of contracts in the broad.

Should ‘free’ goods be covered?

The TPA and FTA provisions relating to misleading or deceptive conduct apply to activities directly involving ‘trade or commerce’, with the consequence that these provisions will not apply where a supplier provides free goods or services in a non-commercial setting (Miller 2007, pp. 76ff).

In many instances, misconduct related to freely provided goods entails little likely consumer detriment, except inconvenience, precisely because there is no direct pecuniary loss.

Nevertheless, in some instances, misleading or deceptive conduct in the provision of free goods or services can lead to more serious adverse outcomes for consumers. In particular, services that provide one-sided or false information about irreversible lifetime decisions could have profound adverse impacts for some people. For example, Reproductive Choice Australia (sub. DR121, pp. 2-3) alleged that this issue has arisen in the provision of apparently objective pregnancy counselling services by an agency that, as a central charter, aims to avoid abortions.

Also, misconduct by non-commercial entities may be more likely to affect the vulnerable and disadvantaged because ‘free’ services are relatively more important for this group. For instance, a church may advertise free meals to the disadvantaged, but when they come to claim them, require attendance at a church service or a bible class lesson (Reproductive Choice Australia, sub. DR121, p. 3).

Therefore, in principle, there can be grounds to discourage misleading or deceptive conduct generally, even for ‘free’ goods and services, if it causes significant consumer detriment.

However, devising an approach that is workable and well targeted is difficult. Reproductive Choice Australia suggested two possible remedies for misleading or deceptive conduct in a non-commercial setting:

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- widening the ambit of the generic law to non-commercial activities and/or;
 - creating an overarching consumer advocacy body that would be able to make findings in respect of alleged misconduct and to pursue remedies.

But, in both cases, it would be hard to define the limits of these arrangements. The case law suggests that removing the current requirement that s. 52 apply only to activities directly involving ‘trade or commerce’ would make it possible to prosecute people or corporations providing any misleading or deceptive information adversely affecting another party.⁴ This would bring into scope significant and expanding activities in modern economies, such as Australia:

- Many advocacy bodies — including political parties — give one-sided advice, with possible implications for consumers’ decision-making.
- The Internet provides many free information services of a non-commercial character, some of which are evidently false or misleading, and others, at least, potentially so.

Were the scope of s. 52 to be widened this greatly, it could embrace almost any dispute involving contested information, with resourcing costs that could displace more significant consumer policy. Indeed, a wider measure may unintentionally frustrate free debate. For example, widening the ambit could allow a commercial entity to take or threaten action under s. 52 to punish or avert critical comments about their products made in good faith by non-commercial entities.

The grounds for some change to the generic consumer law would be greater were there only limited current scope to address misleading or deceptive conduct in non-commercial settings. But, in fact, there are a litany of alternative ways to avoid or resolve such problems — such as through caveat emptor, media exposure, counter-advertising, consumer education and existing tort arrangements (civil actions alleging defamation or injurious falsehood). In that context, the existing diverse ways of dealing with alleged unethical behaviour in non-commercial settings are likely to be superior to seeking new formal legal remedies.

⁴ For example, in *Orion Pet Products Pty Ltd v Royal Society for the Prevention of Cruelty to Animals (Vic)* [2002] FCA 860, 5 July), the Court found that the RSPCA had made some misleading and deceptive statements about the nature of electronic dog collars. However, it was precluded from prosecution under the TPA because, while it was trading corporation, the statements made were not made in trade or commerce.

7.5 Unfair contract terms legislation

Key issues

The TPA and the common law enshrine the concept of fairness in contractual dealings in many ways, such as avoiding unconscionable or misleading behaviour by businesses. However, many consumer groups, State and Territory Governments and some businesses have said they are concerned about unfair contract terms more generally (box 7.2). Unfair contract terms are those that disadvantage one party but that are not reasonably necessary to protect the legitimate interests of the other.

Examples of such ‘unfair’ terms include reserving the right to vary the contract at any time for any reason, or removing liability for interruptions in supply, which may have the effect of inefficiently shifting risk from suppliers to consumers. (Further examples are shown in appendix D.)

The biggest concerns arise for standard-form contracts — typically used in the supply of a broad range of services including air travel, telecommunications, energy, consumer credit, car hire, holiday packages, home improvements and software sales. Such non-negotiated contracts have advantages for consumers — in particular, in competitive markets, lower business costs will be passed on to consumers as lower prices. But, by their nature, these contract terms are offered on a ‘take-it-or-leave-it’ basis, are often complex and apparently mostly not read. The concern is that businesses sometimes use unfair terms against consumers and the public interest generally.

The UK and the EU have augmented their consumer policy framework with provisions to address unfair contract terms and (as noted above) the notion of unfairness is embedded in US law. Locally, the Victorian Government has enacted an unfair contracts provision at the State level and several industry codes embrace the notion of unfairness. Appendix D sets out the details. However, attempts by the Ministerial Council on Consumer Affairs (MCCA) to devise national, uniform legislation along the lines of the Victorian model have so far stalled, with the regulatory impact statement (RIS) not meeting the required standard. In particular, the submitted RIS only provided anecdotal evidence of detriment from the use of unfair terms.

In considering the merits of addressing unfair terms in consumer contracts, a multi-layered set of questions arise. These begin with threshold issues of assessing the nature of the perceived problem (is it due to a market failure or some other problem?), its extent, and its impacts. As appendix D demonstrates, the details of these issues are very complex and so they are simply summarised here.

Box 7.2 Participants' comments on unfair contracts

A large number of community and consumer groups, several individuals and some businesses supported national unfair contracts legislation.

Advocacy groups argued for changes, primarily on the grounds of fairness. The groups included the Consumers' Telecommunications Network (sub. 78, p. 55); WA Community Organisations (sub. 76, pp. 6-8); Consumer Law Centre of the ACT (sub. 74, p. 2); Kildonan Child and Family Services (sub. 65, p. 23); Australian Financial Counselling and Credit Reform Association (sub. 62, p. 3); Eastern Access Community Health (sub. 56, p. 4); the Tasmanian Council of Social Service (sub. 32, p. 3); and Choice (sub. 88, pp. 58ff).

The Motor Trades Association of Australia (sub. 43, p. 14), Optus (sub. DR173, p. 6), the Australian Mobile Telecommunications Association (sub. DR175, p. 4) and Telstra (sub. 35) similarly supported legislation to address unfair contract terms, though for somewhat different reasons. Telstra commented that:

... it would be beneficial for consumers to be protected by a single national regime relating to unfair terms in consumer contracts, to avoid duplication and the inefficiencies associated with administering and complying with multiple regimes and ensure a level playing field for all participants. (p. 23)

Several semi-government agencies also supported national provisions in this area, including the Australia and New Zealand Energy and Water Ombudsman Network (sub. 64, p. 13); Legal Aid Queensland (sub. 51, p. 3); and the Commonwealth Consumer Affairs Advisory Council (sub. 38, p. 1, pp. 8-9).

The latter said:

Unfair contract legislation should be implemented on a national basis as it can deal with systemic unfairness in consumer contracts without reducing consumer choice or creating additional complexity. (p. 1)

The ACCC (sub. 80, pp. 71-84) gave a detailed assessment of unfair contracts laws, but did not reach a final judgment on their desirability and called for more evidence (sub. DR176).

The Governments of South Australia (sub. DR219, pp. 11-12) and the ACT (sub. DR250, p. 8) supported the national adoption of the Victorian approach. The Queensland Government (sub. 87, pp. 52-53) observed the gap in the existing TPA in relation to a general standard of fairness, but like the NSW Government (Office of Fair Trading, sub. 73, p. 22), did not adopt a specific position on unfair contracts law.

The Victorian Government (sub. 92, p. 52) noted that it had introduced unfair contract terms provisions into its Fair Trading Act (FTA) in 2003, and that since then:

... Consumer Affairs Victoria has identified and successfully negotiated the modification or removal of many terms it considered unfair, improving both the economic efficiency and social equity of consumer contracts.

There are potential rationales for action

The Commission accepts that there is a rationale for addressing unfair contract terms. The strongest argument for doing so is ethically based — and is merely the extension of existing ethical principles about fairness in contracts, to cover substantive terms that appear to be manifestly unfair in most circumstances.

There is a conventional economic rationale too, but it is more complicated and depends on the nature of risk appraisal by consumers and the difficulties that ‘good’ firms have in signalling that they will act in good faith with their customers compared with ‘bad’ firms (appendix D).

There are also counter-arguments against a blanket ban of apparently unfair terms based on understanding why these terms are so prolific across all types of contracts, including in competitive industries (as suggested by evidence in appendix D). Such terms are certainly not specific to rogue traders. So why do businesses with strong incentives to please consumers choose to insert unfair terms into their contracts? One explanation is that ‘one-sided’ contracts can actually be beneficial to consumers as a whole by providing them — through the business — with a way of deterring problematic behaviour by small groups of consumers. In particular, just as some businesses behave in bad faith or otherwise inappropriately, so too do some consumers. For instance, they may not be careful in using their purchases, conceal damage they have done to a rented asset, or seek to extract themselves from contracts that require businesses to commit significant upfront resources. Crucially, unlike businesses, consumers do not generally have a brand name or reputation to lose from such conduct. It is hard for suppliers to foresee all the forms that such conduct might take, hence the need for disclaimers that deal with unspecified contingencies.

As a result, what appear to be one-sided contracts may sometimes better protect the bulk of customers from the behaviour of the few, than balanced contracts (Bebchuk and Posner 2006; Johnston 2005 and Gillette 2004). In that case, they may not be so one-sided. The bulk of consumers know that their implicit contract will generally be honoured, and indeed, sometimes exceeded, while those whose behaviour threatens the spirit of the contract know that the supplier has a capacity to act against them. A provision simply barring one-sided contracts may also threaten the continued availability of certain types of consumer products or services — for example, the capacity to return a rental vehicle to a convenient drop off without a vehicle inspection.

So measures against unfair contract terms have to steer a middle course, by seeking to stem acts of bad faith or otherwise inappropriate behaviour by *either* party to a contract. A one-sided contract term that is abused by a supplier would then be

construed as an unfair practice, while its use to deter rare instances of bad faith by a consumer would not. In this case, while some contract terms may be unfair in all contexts,⁵ in others, bad faith is not intrinsic to the contract term, but is revealed by its inappropriate use.

This is why an important consideration in deciding whether (and how) to act on unfair contracts is whether it is possible to strike out terms that are genuinely used unfairly (and inefficiently), while preserving the long-term benefits for the bulk of consumers that arise from suppliers being able to act against consumers who act in bad faith or otherwise inappropriately. Frank Zumbo (sub. DR217, p. 9) argues that these benefits are amply protected, as an unfair term is one that goes beyond what is reasonably necessary to protect a business's legitimate interests. However, that will depend on how subtly courts and regulators can interpret 'reasonably necessary' and 'legitimate'.

There is evidence of exploitation of unfair terms, but it is incomplete

There is persuasive evidence that notionally unfair terms are commonplace in Australian contracts not covered by the Victorian legislation (appendix D). However, the rationale for action principally rests on the unreasonable *use* of unfair terms, not their *existence*. This is because, perceptions of their inherent unfairness aside, dormant unfair terms often do not cause detriment to consumers.

The evidence about the detrimental use of unfair terms is of variable quality. Much of the cited evidence is anecdotal, a deficiency noted by the ACCC (sub. 80, p. 77) and the recent NSW inquiry into unfair contracts by the NSW Legislative Council Standing Committee on Law and Justice (SCLAJ 2006). Nevertheless, there is quantitative evidence from Victoria (box 7.3 and appendix D) and from various other countries that suggests that somewhere between about 5 and 15 per cent of consumers might be detrimentally affected by unfair terms. The wide range of these estimates underlines the uncertainty about how many consumers are adversely affected.

The evidence about the overall extent of detriment suffered by consumers is also limited. The most complete evidence for Australia is from a survey by Consumer Affairs Victoria (CAV 2007b) of the incidence of unfair terms and the nature of the consequent detriment (box 7.3). CAV does not provide an average estimate of the financial detriment, but it finds that particular consumers can face high costs, running into the tens of thousands of dollars. More generally, consumers

⁵ For example, a term that permitted clearly disproportionate penalties for a technical breach of contract.

experiencing unfair terms tend to report emotional effects, such as significant annoyance, frustration, disappointment, as well as erosion of their willingness to enter future transactions involving contracts.

Box 7.3 Unfair contracts in Victoria

Consumer Affairs Victoria undertook a telephone survey of around 1700 consumers in 2007 about their experiences with consumer contracts. This was supplemented by in-depth interviews with 20 consumers.

Among the findings were:

- Until prompted, around half of the respondents could not recall entering contracts. Even after prompting, the responses suggested that many consumers were unaware that they had actually entered contracts when buying common goods and services (such as banking).
- Around one quarter of consumers failed to read contracts at all (and around one fifth only skimmed). Nevertheless, 64 per cent of consumers asked questions about contract terms prior to signing.
- Consumers said contracts were often hard to read, and trusted (sometimes inadvisably) salespeople to explain their important facets.
- 30 per cent of consumers believed they had encountered unfair terms in contracts, including terms that resulted in changes to the types of goods/services supplied under the contract; unclear fees (the most common complaint); excessive termination charges; and increases in the quoted charges.
- Some other allegations seemed to involve problems that were less evidently indicative of the use of unfair terms. For example, some consumers regarded poor customer service as the outcome of unfair terms.
- When answers were adjusted to reflect the existing (Victorian) legal definition of unfair terms, around 17 per cent of consumers had experienced them, which is still significant.
- Consumers were most likely to encounter unfair terms in telecommunications, financial services, utilities and recreation/leisure services. This is likely to mainly reflect the fact that most households have contracts in such areas, rather than an inherently high *rate* of unfair contracts in these services.
- The financial detriment from unfair terms ranged from \$30 to tens of thousands of dollars, though the survey did not provide an average estimate. The emotional impacts tended to be high. The strongest effect was annoyance (8 on a scale of 1 to 10), frustration (7.8) and disappointment (7.6). Problems with contracts also appeared to undermine the confidence of consumers when entering new contracts (a score of 6.9 out of 10), which underlines the value of policy reforms that reduce risks for consumers (chapter 14).

Source: CAV (2007b).

An independent review of the UK arrangements by the National Audit Office (1999, p. 53) gave the example of nine contracts that were changed because of the unfair contracts law. It estimated that the changes generated annual benefits for British

consumers of at least £125 million (about \$300 million) — implying significant prior detriment in those cases. However, this is a gross estimate of the benefits, not a net one. Competition between suppliers may mean that price or other contract terms will have been subsequently adjusted in response to the elimination of the notionally unfair terms. Any such price rises would have partly eroded the ostensible benefits to consumers from reducing detriment. As Chris Field noted at the Commission’s Perth hearings:

... Put simply, the deletion of one term as unfair may see another term which the consumer values affected adversely. (trans., p. 172)

While the CAV survey provides the most systematic evidence, the Commission notes that robust quantitative evidence of the extent of detriment is inherently hard to gather (appendix D). Given these difficulties, an equally relevant question is whether the incidence of detriment is low *enough* not to be relevant for policy. In many other cases, low incidence events matter significantly for policy — such as acts of misleading or deceptive behaviour. As the ACCC notes in its submission, the uncertainty suggests that:

In such cases, the relevant consideration is whether the detriments associated with introducing such a law are significant. (sub. 80, p. 78)

There would be other, less tangible, benefits from policy action

While the direct benefits for consumers from addressing unfair contract terms are unlikely to be as large as some have maintained, other factors suggest there would be additional gains from implementing a measure.

The existing unconscionability provisions of generic consumer law — which could, in principle, tackle unfair contracts — are very costly, slow and uncertain in their application (appendix D). Actions often take years to progress and cost hundreds of thousands of dollars and sometimes millions for single cases. They set a hurdle for unconscionability that is high and their application to the use of unfair terms, while evolving, is still not clear. The *NSW Contracts Review Act 1980*, which bars ‘unjust’ contracts, is more amenable to use than provisions against unconscionability (Lovric & Millbank 2003), but still suffers significant limitations as an effective tool against the use of unfair terms (Zumbo 2006). Simplification and consolidation of the existing unconscionability provisions, as suggested by Frank Zumbo (sub. DR217, pp. 4ff) might resolve some of these difficulties. But such amended provisions are still likely to be unwieldy for dealing with even modest numbers of unfairly used terms. In contrast, measures targeting unfair contract terms are more likely to be economical, timely and provide greater clarity about the threshold and principles for action.

Secondly, a national approach to unfair contracts would reduce the risk that individual jurisdictions would adopt their own (varying) provisions. In doing so, it would more generally support the goal of a single national generic consumer law. Consumer policy also has an increasingly global dimension with the expansion of sales made directly through the Internet. This, and moves for more convergence in consumer policy internationally, reinforces the case for a unified national approach on this issue.

There are costs from policy action

Whatever their immediate benefits, barring unfair contract terms is likely to have some adverse knock-on impacts for consumers through higher prices (or lower quality goods and services). These impacts arise through three pathways.

First, an unfair contracts provision would entail enforcement costs for regulators and impose compliance burdens on businesses through re-writing contracts and dealing with the regulator. Businesses will usually pass these on to consumers. However, these costs appear unlikely to be large, especially given the learning that has taken place in the UK and Victoria, and the fact that compliance costs would be avoided on those national contracts already changed due to the Victorian legislation.

Second, barring specific terms alters the ‘complex balance of the contractual bargain’ (Field, trans., p. 173), thus affecting profits and placing upward pressure on prices. For instance, a reduced capacity for businesses to impose some contingent charges on consumers, such as certain termination fees, would lead to recovery through higher upfront charges.

Third, as noted previously, prohibition could sometimes have unintended impacts by reducing (reputable) suppliers’ discretion to act against consumers behaving in bad faith. As well as adding to the above cost and price effects, this might affect the availability or nature of products and services.

It may still be appropriate to bar the offending contract terms and, indeed, price rises associated with stripping unfair terms from contracts send a useful signal to consumers about the relative attractiveness of competing suppliers (appendix D and Frank Zumbo, sub. DR217, p. 11). Nevertheless, the implication is that the net benefits to consumers from action are not as high as might be thought by looking at the direct benefits.

Quite apart from these price effects, regulatory errors may arise, especially given that unfairness is difficult to define correctly without understanding the full context of the contract and the particular transaction involved. These uncertainties were

raised in the Commission's consultations in the UK about the British statute, as well as by several Australian participants. For example, some banks were concerned about how a new law would deal with unilateral changes in interest rates, which are essential to their business (ANZ, sub. DR178, p. 5). In fact, it is very unlikely that the unilateral right to increase interest rates would be at risk, but in other contractual contexts, the uncertainty may be higher. While firms could test what they saw as inappropriate decisions by the regulator in court (Frank Zumbo, sub. DR217, p. 12), the high costs of legal action may deter them from doing so.

Such concerns may be alleviated if there are some practical restrictions on the scope of any policy response. This could include confining the ambit of any law, careful regulatory processes based on consulting with businesses, and adoption of a layered enforcement approach. For example, in the UK, the regulator has considered only the 'key' unfair contract terms when policing the provision for small business, reflecting the proportionately greater compliance costs and the small reach of their contracts (Edwards 2003). Notably, business has not identified major costs associated with the introduction of unfair contract laws in Europe, the UK and Victoria.

Overall, the qualitative nature of the benefits makes it hard to determine *ex ante* whether a national measure would pass a cost-benefit test. This is especially so given that some of the hotspots of concern about unfair contracts — telecommunications and financial services — are already covered by codes or statutes. Moreover, the unconscionability provisions in the generic consumer law can at least deal with the most egregious exploitation of contracts. Accordingly, the question of net benefits appears to hinge on whether remedies for the residual misuse of terms and the gains from a consistent national approach are worth the costs. One option, in this context, would be to do nothing now on the grounds of uncertainty, and to collect more evidence. For example, the ACCC suggested consideration of the impacts of unfair contract laws in jurisdictions where they already exist (sub. DR176, p. 8), while Chris Field (sub. DR218, pp. 2-3) suggested a more ambitious research agenda to gather more evidence. However, it is not clear, given the nature of the issues (appendix D), that such approaches would unearth much beyond the evidence that the Commission has already gathered from its Australian and international consultations and from various existing studies.

What are the options?

In the presence of uncertainty of this kind, several alternative policy options could reduce the risks of inappropriate intervention:

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- a highly targeted, risk-management approach that quarantined policy action to hotspots through inclusion in industry-specific regulation, codes of practice, or ombudsman arrangements (as in the unjust contracts law already in the Uniform Consumer Credit Code). This option was favoured by the MBA (sub. DR111, pp. 10-11) because it could enable full recognition of existing legislation on unfair terms in specific industry sectors, such as the building industry;
 - light-handed regulatory approaches, such as better disclosure of terms likely to be a source of a problem (ACCC, sub. 80, pp. 81-82) and mandatory cooling off-periods so consumers can reflect on terms before being committed (ACCC, sub. 80, pp. 82-83);
 - adoption of a policy that deals with unfair terms across the whole economy, but that builds, explicitly or implicitly, some kind of appraisal of the community benefit into any particular application of the law. This would shift the evidential burden to a point where it can be more easily gauged. If this can be achieved, it would meet the usual ‘onus of proof’ requirement that regulatory action should only take place where net benefits are likely (a requirement emphasised by Chris Field, sub. DR218, p. 2).

The first alternative provides a degree of protection to consumers. However, it risks cementing in place the existing hotchpotch of solutions to unfair contract terms across various industries and jurisdictions. It also raises the question of where the hotspot list would stop. The European experience (appendix D) suggests that many industries outside those presently covered by specific laws/codes in relation to unfair terms have experienced significant issues with unfair contracts. Accordingly, codes might be required for many more industries, risking another layer of regulatory variations, with uncertain and varying outcomes for business and consumers, depending on the nature of the transaction. Moreover, increasingly, transactions are crossing the boundaries of industries. This is particularly evident in the convergence of telecommunications services, content and electronic devices (which can also encompass various credit arrangements). These boundary issues could create additional confusion about which code should apply to an apparently unfair term.

The light-handed approaches are similarly unlikely to represent a satisfactory solution. They are premised on consumer ignorance of the terms, when that is usually not the basis for concern. For most low-cost standard-form contracts, consumers trust suppliers and do not expect to face problems. Disclosing the terms, or allowing consumers the time to find them, would rarely make a difference. Also cooling-off periods are not feasible in many cases (such as renting a car or taking a flight without significant notice).

The third approach has significant advantages over the other two options. It targets the source of the problem more effectively and has full coverage of unfair terms whatever the industry, yet still addresses the risks of regulatory error. It would be more likely to be accepted by all jurisdictions — thus assisting in the introduction of a single generic consumer law. Its national and broad approach would reduce the possibility that new industry-specific arrangements, such as the national regime contemplated for energy, would adopt prescriptive arrangements for aspects of unfair conduct (such as in relation to unfair marketing) that could be adequately dealt with by a generic unfair contracts provision. Existing industry-specific arrangements for unfair contracts may eventually also become obsolete.

How would such a broad national approach work?

The approach could work in several ways. In the draft report, the Commission recommended an ex post model that would void unfair terms *after* they had been used by business to the detriment of consumers (box 7.4). The discussion that follows draws on the feedback from participants about this particular model — and has prompted the Commission to modify its approach in some key areas.

However, in the Commission’s view, regardless of the exact design of the model, it would need to meet a number of broad criteria.

Box 7.4 The Commission’s draft report proposal for unfair contract terms

The Commission proposed that a new provision should be incorporated in the new national generic consumer law that voids unfair terms in standard-form contracts in certain contexts. The proposal shared some features of the existing Victorian arrangements. It adopted the same definition of unfairness and required ‘all the circumstances of the contract’ to be considered when reaching a judgment about unfair terms. It also provided for the use of guidelines to help clarify unfair terms.

However, it differed in several major respects from the Victorian approach:

- it related only to non-negotiated contracts and did not cover the upfront price of the good or service;
- unfair terms would be voided only for the contracts of those consumers subject to detriment, so that the law would only operate *after* the misuse of a contract term;
- it explicitly required that there be an overall public benefit from remedial action; and
- it incorporated the capacity for business to secure regulatory approval for ‘safe harbour’ contract terms that would be immune from any action under this provision.

Providing clarity about what constitutes unfairness

Any workable law must define unfairness. The provisions against unfair contracts in the United Kingdom, the European Union more generally and Victoria adopt a common definition. The essential aspect of this is that a term is unfair if ‘contrary to the requirements of good faith, it causes a significant imbalance in the parties’ rights and obligations arising under the contract.’

Most aspects of this definition are unproblematic. However, in considering the first court proceeding involving the Victorian legislation (*Director of Consumer Affairs Victoria v. AAPT Limited VCAT 2006*), Justice Morris observed that the role of the expression ‘contrary to the requirements of good faith’ was less straightforward than the definition’s other elements. If taken literally, the expression could be seen as a redundant provision (mere ‘surplusage’ in his words).⁶ Nevertheless, on the basis of case law, he argued that the expression provides guidance about when an imbalance is ‘significant’. Its precise role has been most clearly set out by Justice Morris in the most recent application of the Victorian law (*Free v. Jetstar Airways Pty Ltd, Civil Claims*) [2007] VCAT 1405):

The phrase “contrary to the requirement of good faith” performs an adjectival role, so that it assists in the assessment of whether a contractual term causes a “significant imbalance” in the parties’ rights and obligations, to the detriment of the consumer. It does not amount to a separate element which has to be proved before the term may be regarded as unfair. What has to be proved is the “significant imbalance”.

Frank Zumbo (sub. DR217, p. 7) suggests that the term is now also clarified in NSW contract law.

Given its usefulness in guiding the application of the law, there are good grounds for retaining the principle of ‘good faith’ in any definition of unfairness. Accordingly, the Commission considers that the use of the Victorian definition should not cause any problems, though other definitions of unfair terms may be equally apt.

Achieving benefits for the public generally

The application of any law regarding unfair contract terms should be designed so that the benefits for unfairly treated consumers are not offset by any incidental costs to consumers generally. In effect, this is nothing more than the requirement to consider the overall public interest in applying the law. This is consistent with the

⁶ Others have also noted the ambiguity of good faith in Australian law when referring to contractual obligations (Harper 2004, McDougall 2006, Douglas 2006), with Justice McDougall commenting that, the concept ‘is uncertain and ambulatory.’

design of competition policy, which also has as its ultimate goal the achievement of overall benefits, not more competition for its own sake. (This is evident, for example, in the criteria for declaration of access in part IIIA of the TPA.)

Among other matters, a regulator (and any court) might be expected to take into account:

- the extent of consumer detriment (realised or likely);
- the degree to which the contract term reduced transactions costs in its current (and proposed) forms;
- any effects (adverse or favourable) on risk allocation and prices; and
- whether voiding (or changing) terms for groups of affected consumers could encourage inappropriate behaviour by some consumers to the ultimate detriment of consumers as a whole.

In other words, the regulator would need to take account of ‘all the circumstances of the contract’ and evidence of detriment. Given the recent case law outlined above, these requirements are already embodied in the Victorian legislation, but without much guidance as to their scope.

In the draft report, the Commission sought to give effect to this public benefit goal through an explicit test in any dispute relating to alleged unfair contracts. Several inquiry participants questioned the merit of this test. Luke Nottage (sub. DR114, p. 10) commented that such an explicit test has no precedent in consumer law in Australia and a range of other countries. At most, he argued that it could be expressed as a ‘good practice guideline’ or that the onus of proof be reversed, with a business subject to the law having to show that striking out an apparently offending term was not in the public interest. The ACCC also recommended the removal of an explicit public benefit test, noting that:

Courts are not experienced in applying public benefit tests. Including such a test in the proposed UCT provision may therefore lead to uncertainty regarding how it will be interpreted by the courts (sub. DR176, p. 9).

It also observed that, in any case, an explicit test would represent a ‘belts and braces’ approach to regulation, since meeting the other criteria developed by the Commission for applying an unfair contract law (box 7.4) would almost certainly guarantee that the public benefit test had been met (ACCC, trans., p. 725).

In the light of these participants’ comments, an implicit, rather than an explicit, consideration of the public benefit is likely to be appropriate. Nevertheless, it may be useful to make clear in an explanatory memorandum to a new Act on unfair contracts that gauging unfairness ‘in all the circumstances’ would include

consideration of the broader impacts of any action on other consumers (including higher prices or restricted choice).

Application to non-negotiated contracts alone

The Victorian unfair contracts provision covers negotiated as well as standard-form contracts. Conversely, the UK unfair contracts law explicitly excludes negotiated contracts from its scope.

There are several grounds for such exclusion. Negotiated contracts, by their nature, require parties to explicitly consider and tailor the terms and conditions. Parties can seek to eliminate any terms seen as unfair in such contracts. Indeed, even apparent ‘standard-form’ contracts can be negotiated contracts if parties routinely strike out or alter existing terms that they do not believe to be appropriate (MBA, sub. DR111, p. 4).

Negotiation also typically occurs for more costly products and often will involve intermediaries because they have professional competence in interpreting the terms and conditions. In that context, parties to negotiated contracts, or their agents, are usually sufficiently sophisticated to ensure acceptable contract outcomes and can reasonably be expected to have their ‘eyes wide open’. The application of an unfair contracts law in this situation would undermine parties’ diligence in considering the full terms of the contract.

Accordingly, it would only be appropriate for a court or tribunal to void negotiated terms in highly special circumstances. The Victorian Government (sub. DR226, pp. 61-62) argued that their Act (section 32X) already allows a court or tribunal to take into account whether parties negotiated a contract when determining unfairness. But this gives little guidance about the degree to which the standard of fairness would be tempered for negotiated contracts. And, as noted by the Victorian Government, the existing unconscionability provisions of the TPA already have the scope to address particularly egregious terms in such contracts. That, and the fact that most of the concerns relate to standard-form contracts (a point acknowledged by the Victorian Government, sub. DR226, p. 61), suggests that inclusion of negotiated contracts would involve risks that exceeded the likely benefits.

Exclusion of price terms

The Commission considers that the application of the new law should explicitly exclude terms dealing with (‘non-contingent’ or upfront) standard contract prices. This exclusion is a feature of the Consumer Contracts Code in communications in Australia

(ACIF 2005b) and of unfair contract terms legislation generally in the UK. In contrast, the Victorian legislation would potentially allow action against an ‘unfair’ price.

The argument for exclusion rests on the fact that prices are clearly visible to consumers and, unlike many other terms, cannot legitimately be seen as surprises veiled by a complex contract. Unless there are major barriers to effective competition, consumers can elect to avoid contracts with unfair prices. And where there are such barriers, competition policy is the more appropriate vehicle for achieving efficient prices rather than the discretionary use of unfair contracts law to impose de facto price controls. While the Victorian Government (sub. DR226, p. 63) argues that prices would not be regulated in this way, it is not clear that their Act effectively precludes this.

Charges that are less transparent should still be potentially subject to regulatory action under the new provision. For example, this could include charges triggered by various contingent events after activation of the contract — ‘contingent prices’. Accordingly, regulation would extend to such matters as unreasonable cancellation charges, but not to prices deemed as unfairly high.

Guidance for consumers and business

It would be relatively easy for regulators to provide guidance to consumers and business about indicative lists of terms that would usually fail a fairness test (ACCC, sub. 80, p. 81 and sub. DR176, p. 8). This would help prevent unnecessary claims by consumers and encourage pre-emptive action by businesses to ensure their contracts did not contain unfair terms.

The draft report also raised the use of ‘safe harbour’ or ‘pre-commitment’ arrangements as another way of promoting certainty for business, reducing the costs of regulatory change, and encouraging early action on unfair terms. Under these arrangements, the regulator could agree to codes put forward voluntarily by business for standard-form contracts on an industry basis (for example, those that might be put forward by industry associations or negotiated by the regulator with them). These ‘safe harbour’ contracts would be exempt from actions under any new regulation, thereby providing certainty to business. The only recourse for regulatory action when a business used a safe harbour contract would be when circumstances other than the terms themselves resulted in unconscionability (for example, duress). The regulator would then have to pursue that matter under the existing unconscionability provisions of s. 51AA and 51AB, which have high hurdles for action.

Some parties supported such safe harbour arrangements for the certainty they would provide and for the potential to give recognition to already developed codes (MBA, sub. DR111, p. 12; Optus, sub. DR173, p. 6; Suncorp, sub. DR171, p. 4; and the Real Estate Institute of Australia, sub. DR172, p. 12). Some provided more provisional support, seeing a need for further development. For example, the Foundation for Effective Markets and Governance (sub. DR122, p. 4) argued that the regulator might need to remove its protections if there was misrepresentation by the industry or material circumstances changed. And Choice (sub. DR194, p. 8) argued that the regulator would need to exercise discretion in approving safe harbour arrangements.

Others generally opposed a safe harbour option. The ANZ Bank considered that the arrangements would constitute another layer of superfluous regulation (sub. DR178, p. 5) though, in fact, a safe harbour arrangement would involve no additional net regulatory burden, since its use would be entirely discretionary for businesses. The Redfern Legal Centre (sub. DR151, p. 9) questioned the right of businesses to safe harbour provisions, seeing this as emasculating the role of any new law. However, as well as providing certainty for business, the intent of safe harbour provisions would be to motivate early adoption of fair contracts for the benefit of consumers. A more significant concern expressed by the ACCC was that the arrangements could place a high regulatory burden on the regulator, and if charges were imposed to get a safe harbour ruling, a disproportionate burden on small business:

The ACCC believes that if a regulatory approval procedure was included, it is likely it will have to deal with a large volume of applications for contract review from risk-averse businesses across the country seeking approval of their own ‘safe harbour’ terms. This will raise significant resource issues for the regulator. (sub. DR176, p. 8)

Using the regulator as a readily available arbiter could also undermine suppliers’ capacity and responsibility to exercise their own judgments in these areas.

These concerns would be reduced were a safe harbour arrangement quarantined to broad industry groups through model codes (for example, telecommunications services, gyms and rental car services). Nevertheless, there would be practical administrative difficulties in deciding whether a particular industry code had sufficiently broad business coverage (for example, would a code developed just for gyms in Melbourne qualify?). Overall, the regulatory resource costs identified by the ACCC may well present an obstacle to efficient safe harbour provisions.

Even so, as recommended by Choice (sub. DR236, p. 9), it would be sensible for the regulator to take account of existing codes developed by industries to ensure fair contract terms, since they may provide lessons for the development of guidelines and would provide at least interim protection for consumers. For example, in the telecommunications industry, the Communications Alliance developed the

Consumer Contracts Industry Code — administered by ACMA — to deal with unfair contracts (Optus, sub.DR173, p. 6 and the Australian Mobile Telecommunications Association (AMTA), sub.DR175, p. 4). Similarly, in the credit area, the Uniform Consumer Credit Code and the Code of Banking Practice (CoBP) at least partly address unfair contract terms (ANZ, sub.DR178, p. 6 and Australian Bankers’ Association, sub.DR245, p. 17). Over time, the appropriateness of such codes could be re-assessed in the light of the generic approach to unfair contracts. For instance, in respect of the Consumer Contracts Industry Code, AMTA argued that:

In supporting the implementation of a generic consumer law AMTA’s preference would be to review this code and determine its appropriateness in relation to a national framework. (sub. DR175, p. 4)

Implementation would have to be nuanced

Sensible implementation of policy would seek to accommodate firms’ cycles of contract document changes, accordingly reducing compliance burdens, an approach supported by the ACCC (sub. DR176, p. 9). The ACCC (p. 9) also made several other practical recommendations, which should be implemented as part of the transition to enforcement of a new law:

- There should be a transition period — of say a year — after introduction of the law — before it is enforced by regulators, so that businesses have time to adjust their contracts and the regulator can develop appropriate guidelines. There is a precedent for such delayed implementation, with the ACIF (2005b) Consumer Contracts Code requiring compliance within six months of the registration of the code.
- A grandfathering clause should be included in a new unfair contract terms law, which would exempt period contracts from legal action for the remaining duration of the contract. Where contracts have long durations or no fixed date of cessation, their grandfathering status would only persist for a reasonable period. This would allow a smooth transition to new contracts compatible with the law.

The capacity for effective representative actions

A practical concern with the application of unfair contract terms law is to ensure that consumers (or regulators on behalf of them) are able to mount effective representative actions to recoup their collective losses (ACCC, sub. DR176, pp. 8-9 and Choice, sub. DR194, p. 8). The Commission has made several proposals to improve the scope for effective representative actions in consumer law generally (chapter 9).

The wording of any unfair contracts legislation should ensure that regulators or private parties could readily use such general provisions against unfair terms. This would allow a court to provide redress for a group of consumers who had experienced generally similar detriment from unfair terms. For example, a unilateral change to a frequent purchasers' scheme that rendered credits valueless could pave the way for a class action on behalf of all the relevant creditors, without having to go into the details of each creditor.

Coordination across jurisdictions

For as long as there are multiple enforcers of generic consumer law, specific attention would need to be paid to consistency in enforcement approaches and prevention of jurisdictional overlaps for what would be a new provision in that law. Regulators would need to develop protocols to establish clear lines of responsibility for enforcement, with, for example, the ACCC dealing with matters relating to corporations that have operations across several jurisdictions.

Furthermore, while guidelines to business and consumers about what constitute unfair terms would be highly desirable (see above), there is a danger that such grey law may differ between jurisdictions, leading to added compliance burdens and greater uncertainty for business and inequality for consumers. Therefore, it will be important to ensure that any quasi-regulation in this area — charters, guidelines and codes — are also uniform and consistently interpreted by regulators.

A choice between two broad options remains

There would still be a choice to make between two broad approaches that give effect to the above requirements, each with its own advantages and limitations.

The ex ante model

An *ex ante model* would give the regulator the capacity to pre-emptively rule out unfair terms that could cause (future) detriment to consumers (that is, something along the lines of the Victorian and UK models, but subject to the criteria above). This approach would be more likely to lead to early revision of a greater number of contracts because businesses would be aware of the threat of pre-emptive regulatory action, even when evidence of detriment was unclear. Accordingly, it would also entail lower court costs. The practical feasibility of the approach has been demonstrated, since it is similar to the successfully applied models used in the UK and Victoria, and has been effectively implemented in some Australian industry codes (Choice, sub. DR236, p. 8).

On the other hand, the model involves greater risk of regulatory overreach since it would effectively place all standard-form contract terms under the gaze of the regulator and would require judgments about potential consumer detriments that have not yet materialised. Depending on the terms struck out by a regulator, it could sometimes have adverse impacts on consumers. In that context, it would be important to ensure that the regulator was itself required to act in good faith in consulting with businesses about changes to contracts.

The ex post model

Under this approach, regulators would only initiate action when a consumer (or consumers) had already suffered a detriment from an unfair term. In this case, the unfair contract term would only be voided for the consumers subject to the detrimental use of that term by the business, and not for others who were party to the same contract. As it would require evidence of detriment, this model would better target the key problems posed by unfair contracts and would be less prone to the risks of regulatory overreach.

This variant would effectively represent an extension to the consumer unconscionability provision (s. 51AB) of the TPA (though it need not be crafted that way in the generic consumer law), but allowing action on unfair terms in a broader context. To provide effective deterrence and redress, it would have to be drafted to avoid the slowness and costs besetting applications of s. 51AB (a risk noted by several participants, for example, Joint Consumer Groups, sub. DR228).

The issuing of regulatory guidelines would help clarify unfair terms for courts as well as business. This would help make the application of the new law more timely than the present unconscionability provisions. The law would also have to be framed so that the standard of proof for detriment required by courts was not set at a threshold that made action practically unfeasible.

Under this option, the threat of ex post action would still create incentives for industries to voluntarily develop fair standard-form contracts where the risks of problematic contract terms were high. As with the ex ante approach described above, media reporting of cases would also often have a salutary commercial impact. As pointed out in Appendix D, even failed cases based on unconscionability have led to widespread changes in contracts and business conduct (*ACCC v Oceana Commercial Pty Ltd & Ors [2003]*). Moreover, a sensible regulator observing ex ante an egregious contract term could always advise a business that it was running a real risk of subsequent prosecution if the business used the term. Consequently, despite its ex post form, this approach would still have a preventative role in reducing the incidence and inappropriate use of unfair terms. This should reduce the

concerns of the many participants who saw an ex post provision as too narrow and cumbersome.⁷

There are, nevertheless several limitations to an ex post approach. It would not provide a remedy for consumers who were unaware of their rights (Redfern Legal Centre, sub. DR151, p. 10). Nor would it necessarily address the intangible costs that might be experienced by consumers who act against their own interests in order to avoid triggering an unfair term (for example, not terminating a problematic contract because of excessive terminating charges). The Redfern Legal Centre also observed that a law that allowed demonstrably unfair terms to stand until they were used would send a bad, ethically unsound, signal.

However, these deficiencies are probably not as significant as they might initially appear.

- The evidence suggests that most consumers do not read standard-form contracts. In that case, the signal sent by (unused) unfair terms would be muted, with the damage to consumers emerging only *after* the surprise exploitation of an unfair term (and thereby subject to effective remedial action under the ex post approach).
- An ex post approach would still create incentives for business to eliminate many unfair terms before they are widely used to disadvantage consumers (as discussed above). In that sense, the ex post model partly replicates the capacity of the ex ante model to pre-empt the use of unfair terms.

The models are more alike than different

As the preceding discussion makes clear, the differences between the two models are not as significant as might first appear to be the case. In practice, the models may lead to similar outcomes for consumers. The key tradeoff is between readier pre-emption of unfair terms on the one hand, and the reduction in the risk of regulatory overreach on the other. For the interim at least, the Commission is inclined to the view that the ex post approach is the preferable option because it would be:

- a better-targeted measure than the ex ante approach;
- a prudent approach given the uncertainty about the severity of the problem; and

⁷ Such as Luke Nottage (sub. DR114, p. 10); Redfern Legal Centre (sub. DR151, p. 10); ASIC (sub. DR174, p. 14); Legal Aid Queensland (sub. DR202, p. 2); Kildonian Uniting Care (sub. DR206, p. 7); South Australian Government (sub. DR219, pp. 11-12); The Law Council of Australia (sub. DR227, p. 3); and Choice (sub. DR236, p. 7).

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- less prone to regulatory error, as some evidence of actual detriment would be required.

The legislation should be drafted to avoid the practical pitfalls in the existing unconscionability provisions in the generic consumer law.

There would be scope to assess whether an ex ante model might be a better approach as further information becomes available about the effectiveness of the proposed ex post model. This underlines the importance of conducting a review of the impacts of the proposed new law after it has been in operation for a reasonable period, say five years. As part of this review, it will be important to assess the effectiveness of the new law for disadvantaged and vulnerable consumers, since they may be particularly affected by unfair terms (as noted by Anglicare Tasmania, sub. DR191, p. 8).

However, regardless of how the specific model is configured, the most important requirement is to put in place an arrangement for addressing unfair contract terms. Its workability — including the extent to which it facilitates the introduction of a nationally consistent generic consumer law — its efficiency, and the risks of unintended consequences will be the key criteria in deciding the exact approach.

RECOMMENDATION 7.1

A provision should be incorporated in the new national generic consumer law that addresses unfair contract terms. The Commission's preferred approach would have the following features:

- ***a term is established as 'unfair' when, contrary to the requirements of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract;***
- ***there would need to be material detriment to consumers (individually or as a class);***
- ***it would relate only to standard-form, non-negotiated contracts;***
- ***it would exclude the upfront price of the good or service; and***
- ***it would require all of the circumstances of the contract to be considered, taking into account the broader interests of consumers, as well as the particular consumers affected.***

Where these criteria are met, the unfair term would be voided only for the contracts of those consumers or class of consumers subject to detriment, with suppliers also potentially liable to damages for that detriment. The drafting of any new provision should ensure the potential for private (and regulator-led)

representative actions for damages by a class of consumers detrimentally affected by unfair contract terms.

Transitional arrangements should be put in place after enactment, which would give businesses the time to modify their contracts.

The operation and effects of the new provision should be reviewed within five years of its introduction.

8 Defective products

Key Points

- Australia's consumer protection arrangements encompass an array of mechanisms to encourage suppliers to market products that meet reasonable standards of safety, quality and performance. These include statutory and common law rights to refunds and compensation in the event of injury or loss from defective products.
- There is evidence that many consumers, retailers and manufacturers are unaware of the legal rights and responsibilities conferred by the implied warranty conditions contained in these laws. Consumer regulators should raise community awareness about the scope of those rights and responsibilities. The adequacy of existing legislation covering implied warranties and conditions should be examined as part of the development of the new national generic consumer law.
- Recent amendments to the law of negligence and the statutory provisions of the Trade Practices Act and the State and Territory Fair Trading Acts have restricted the circumstances under which product liability actions can be taken and the scale of compensatory damages that can be sought.
- Inconsistent application of these laws across jurisdictions and differences with liability regimes for other categories of injury means that the level of compensation available to plaintiffs is dependent on the context and the location where such injury occurs. The complexity of personal injury law has increased as a result.
- Any impact of the recent amendments (or other factors) on incentives to supply safe products should be monitored, drawing on the results of the Ministerial Council on Consumer Affairs' baseline study of product related accidents and the other proposals put forward by the Commission in its recent report on consumer product safety.

8.1 Introduction

Defective products impose a range of costs on consumers and the broader community.

- In the case of unsafe products, these costs can include both physical and psychological injury, the financial burden of income lost due to incapacity and costs associated with accessing medical treatment. Broader societal impacts will also be felt through greater demands on the public health and social welfare

systems and the temporary (or permanent) reduction in the economy's productive capacity.

- For products that otherwise fail to meet reasonable levels of quality or performance, some consumers will bear the additional cost of procuring replacement products and the dissatisfaction associated with the original purchase. Economic activity may also be impeded if some consumers are less willing to purchase products whose quality and performance is uncertain.

Reputable firms do not, of course, intentionally set out to produce and market unsafe or otherwise defective goods. But some products inherently pose risks simply because of the uses for which they are designed. More generally, there is always an explicit trade-off between designing and manufacturing products that offer higher levels of product safety, quality and performance and the cost of doing so. It is the willingness of consumers to pay for enhanced characteristics that ultimately determines whether firms make the investments necessary to deliver them.

That said, for a range of reasons, governments and the legal system also play a role in ensuring consumer products meet reasonable standards of quality, performance and safety. A key reason is that the complexity of some products means that consumers will be unable to cost-effectively judge whether they meet appropriate standards. Another is to address those circumstances where a firm has little reputational capital and only a transitory commitment to a particular market.

The statutory conditions implied into contracts by the *Trade Practices Act 1974* (TPA) and the State/Territory Fair Trading Acts give consumers basic and guaranteed levels of protection for the goods and services they acquire which, in most jurisdictions, cannot be excluded by the seller.¹ But there is evidence that the rights and responsibilities conferred by these conditions are not well understood in the community. Accordingly, the level of protection they provide is compromised. This chapter presents options to address this information gap.

In addition, specific product safety laws provide for protection against the supply of defective products including through bans and recalls, mandatory product standards and the issuing of product warnings, and compensation in the event they cause injury or death. A number of sector-specific regulatory regimes also apply to more hazardous products — electrical goods providing an obvious example. The Commission's earlier review of Australia's consumer product safety system judged that these mechanisms deliver a reasonable level of product safety to Australian consumers (PC 2006).

¹ Any term of a contract that attempts to do so will be void under section 68 of the TPA.

However, it also found that recent amendments to personal injury law are likely to have weakened the incentives for businesses to supply safe goods (although at the time it was too early to tell what the magnitude of the impact might be). In addition, while it did not consider the introduction of an *ex ante* legal requirement for firms to supply safe products was justified at the time, it noted that under a broader assessment of the regulatory framework, a different conclusion could potentially be reached. The Commission's current review of consumer policy arrangements provides an opportunity to revisit both these issues.

8.2 Merchantable quality and fitness for purpose

The Trade Practices Act and provisions in the State and Territory Fair Trading Acts imply statutory conditions into contracts that guarantee a minimum level of quality and performance for goods and services. Because these rights are implied into each consumer contract, consumers must pursue their own civil actions when they consider their statutory rights have been breached.

The main route for such action is through Part V, Divisions 2 and 2A of the TPA (and the similar provisions of the jurisdictional Fair Trading Acts) which place a liability on suppliers, manufacturers and importers for the loss or damage caused by consumer goods that are (among other things) not of merchantable quality or fit for specific purposes. Merchantable quality requires that goods meet a basic level of quality and performance that would reasonably be expected given the price and the manner in which they are described. Fitness for purpose requires that goods be suitable for any particular purpose the consumer made known to the supplier when negotiating or arranging to buy them, or a purpose that is obvious from the circumstances in which the sale took place (ACCC 2004).²

While these rights appear reasonably straightforward, the application of the statutory conditions varies across jurisdictions. The main differences relate to such matters as:

- whether the conditions are excludable (the case in Queensland, Tasmania and the Australian Capital Territory);
- variations in purchase value and use thresholds for eligibility;
- factors to be considered (such as price, terms of supply and condition of goods) in determining whether the provisions apply;
- obligations on the buyer to examine goods prior to purchase;

² Accordingly, merchantable quality and fitness for purpose are not restricted to the safety features of products.

-
- the extent to which they rely on the skill or judgement of the supplier; and
 - whether the supplier could reasonably be aware of the defect or whether the defect was brought to the attention of a consumer (Corones and Christensen 2007).

These differences would be eliminated by implementing a single national generic consumer law, as recommended by the Commission (see chapter 4). But if that recommendation is not adopted, then at the very least, the ability to exclude statutory conditions should be repealed in those jurisdictions that currently provide such scope. That specific jurisdictional inconsistency serves to undermine a generally accepted community expectation in regard to Australian consumer law (that consumers should receive similar protection regardless of where they reside) with, to the Commission's knowledge, no offsetting benefits.

More broadly, there is a related concern regarding the community's (consumers, retailers and manufacturers) awareness of the scope of the implied conditions themselves. In this context, recent investigations in other countries and by the ACCC (2004) in Australia have revealed that there is a general lack of understanding of differences between the voluntary warranties offered by manufacturers and the implied (statutory) protections provided by generic consumer laws. Importantly, rights to compensation are not limited to the period of a manufacturer's voluntary written warranty.

Statutory rights (in those situations where they cannot or have not been excluded, restricted or modified) *override* voluntary warranties and, as noted above, depend on what would reasonably be expected of a product (in terms of its quality and performance), taking into account the price and the manner in which it is described and used. Thus, using an example provided by the ACCC (2004), a consumer is likely to be entitled to a refund if a TV that could be expected to last at least 10 years develops a serious fault after 12 months, irrespective of whether the manufacturer's voluntary warranty still applies.

Prima facie, the protections provided by the implied conditions raise questions regarding the benefits provided by so-called 'extended' warranties (which are not warranties as such, but service or insurance contracts to provide repair and maintenance for a specific period). In the words of the ACCC:

Consumers should check whether the likely benefits of these contracts justify the additional cost and especially that the extended warranty is not duplicating statutory rights that exist anyway.

Sellers who offer such warranties risk breaching the Act if they misrepresent either the real benefits or a consumer's need for them. (2004, p. 2)

Of course, the additional certainty provided by an extended warranty would have some value to many consumers. Thus the Commission is not suggesting such warranties do not have a legitimate role in the marketplace. However, there is clearly scope for better education of consumers in this area to help them make more informed choices. Indeed, given the apparent lack of understanding of the statutory provisions and the proliferation of extended warranty offerings across a broad spectrum of consumer goods, there could in future be a case for a stronger policy response. This could involve, for example, specific enforcement action against some suppliers with respect to any misleading marketing and sale of extended warranties.³

In responding to this suggestion in the Draft Report, regulators highlighted the range of current and prospective initiatives that are being pursued in the area. The ACCC said that in addition to future marketing campaigns that are being considered by the National Education and Information Advisory Taskforce (in which the ACCC participates), it is also independently taking other educative actions:

... the ACCC has released a range of new refund and warranty publications as part of its public education and awareness activities. In January 2008, the ACCC released a consumer fact sheet about mobile phone handset refunds and warranties issues. The ACCC is also preparing further material for publication in 2008 to educate consumers and suppliers about their statutory rights and responsibilities in relation to implied warranties and conditions. This material includes a revised version of the ACCC brochure on warranties and refunds. (sub. DR176, p. 10)

The South Australian Minister for Consumer Affairs (sub. DR219, p. 12) similarly noted involvement in awareness-raising through education and enforcement activity. And the Victorian Government pointed to its 'extensive' work in the education and compliance area, including a recent example of court-based enforcement action. But it also suggested that the legislation upon which the implied warranties regime is based needs to be reviewed (see below).

Such activity by regulators is clearly desirable. However, the Commission notes the need for education programs to be ongoing, widely available (such as through point of sale locations) and in a format (including different languages) suited to different consumer needs. In the words of Anglicare Tasmania:

To be effective, consumer education campaigns must be adequately resourced and ongoing. Many education campaigns run only for a short period, or in short bursts. Unfortunately, Anglicare financial counsellors advise that many people do not notice information unless they actually need it, and then, it may not be immediately available.

³ The Commission notes the ACCC's successful recent Federal Court action involving LG Electronics for false and misleading representations about the existence or duration of statutory conditions and warranties, and the rights and remedies available to mobile phone users (ACCC 2006a).

The solution to this is to ensure that information is provided in as many different formats and locations as possible so that when people do need the information, it is easy for them to locate. (sub. DR191, p. 11)

There is also the need for such activity to be coupled with greater enforcement action where appropriate. Dr Luke Nottage, who focused specifically on inappropriate behaviour by retailers in the extended warranty area, said that the New Zealand experience offers lessons in this context:

... there must be re-education and enforcement against retailers — beyond those who don't take advantage of ignorance by selling extended warranties — who often try to fob off buyers by claiming that they owe no duties whatsoever to consumers, telling them to claim only against the manufacturer (ie. under TPA Part V Div 2A). ... the Office of Fair Trading and ACCC should talk to their counterparts in NZ, where this practice is much less widespread. (sub. DR114, p. 11)

In addition to commentary on education and enforcement matters, some participants also discussed the adequacy of the legislative base underpinning the implied warranties regime. The Victorian Government, for example, questioned whether the current provisions are outdated and noted that the legislative approach used in New Zealand is worth considering.

... [the implied warranties] laws have been in place for many years. There are some core issues that the Productivity Commission needs to further consider. This includes the systemic non-compliance by retailers and manufacturers with the scheme; the need for a comprehensive review of the scheme; and the impact on the economy of the inability of consumers to achieve redress. The Productivity Commission may wish to consider the New Zealand Consumer Guarantees Act 1993. (sub. DR226, p. 10)

However, the Commission has not undertaken the detailed analysis necessary to reach a judgement on the adequacy or otherwise of the existing regulation in this area, or the merits of alternative models such as those adopted in countries like New Zealand. Accordingly, it considers that this issue should be examined as part of the development of the new national generic consumer law, with input from the regulators responsible for enforcing these provisions.

RECOMMENDATION 8.1

Australia's consumer regulators should:

- ***raise awareness among consumers and suppliers about the statutory rights and responsibilities conferred by the implied warranties and conditions in the generic consumer law; and***
- ***where appropriate, take specific enforcement action against misleading marketing and sale of extended warranties.***

The adequacy of existing legislation related to implied warranties and conditions should be examined as part of the development of the new national generic consumer law.

8.3 Product liability arrangements

In addition to the implied warranty provisions, there are a range of other legal avenues available to consumers to seek redress or compensation for injury, loss or damage caused by defective products. These include both statutory rights provided by provisions in the TPA and civil rights under common law. These avenues place a strong onus on suppliers to ensure their products meet appropriate standards and provide for damages in cases where this duty is breached and a consumer suffers injury or loss as a result — though the stringency of these measures has been somewhat reduced following recent amendments to civil liability laws (see below).

Trade Practices Act

The TPA contains a range of direct and indirect provisions that enable consumers to claim compensation in respect of defective (unsafe) products. The most direct are the specific *manufacturer's liability for defective goods* provisions (Part VA). Introduced in 1992, these provisions place a 'strict' liability on manufacturers (meaning a plaintiff need not prove fault on the defendant's part) to provide compensation for injury, loss or damage caused by defective goods. Successful actions under Part VA only require proof that the corporation manufactured or imported the goods; the goods had a defect and, because of this defect, the individual suffered injury.⁴

At the same time, measures were also introduced to allow plaintiffs, for the first time, the scope to commence representative proceedings in the Federal Court (pursuant to section 75AQ in the case of product liability claims). The aim was to promote access to the justice system and improve the efficiency of court resources (ALRC 1988).

⁴ The test of whether goods are defective focuses on the reasonable expectations of the community — an objective test for a court to decide. Unlike a pure strict product liability regime (where the reasonableness of a defendant's action would not be an issue), Part VA does provide manufacturers with a number of defences that inject notions of fault into liability law. Nevertheless, the onus remains on manufacturers to rely on an exclusive set of defences including that a defect was not discoverable given the state of scientific and technical knowledge at the time of supply (Corones and Clarke 2002).

Prior to the introduction of the civil liability reforms (see below), the statute of limitations applying to legal actions under Part VA involved a general limit of ten years from the date of supply and three years from the date a person became aware of the defect and the identity of the manufacturer. No time limits applied to other TPA provisions that (at least technically) provided alternative avenues for compensation for defective products (see later). In addition, all suppliers of the product could be held jointly and severally liable (meaning the entire damages awarded could be retrieved from any individual supplier) if the manufacturer could not be identified.

While there were concerns that a substantial rise in product liability litigation would follow the introduction of Part VA, there have been just 27 judgements under those provisions (though a number of these have involved representative actions). Most outcomes have favoured the defendant (Kellam and Nottage 2007). The paucity of judicial activity has been attributed to the availability of other avenues for consumers to seek redress (via common law in particular), and the settlement of many cases out-of-court. The ACCC highlighted the preponderance of negotiated settlements (in cases involving multiple plaintiffs) in its submission to this review:

It is important to note that many private class actions, as well as representative actions, commenced by regulators are resolved either before or after the commencement of litigation if a negotiated settlement is agreed to by the parties. The ACCC through its enforcement processes is often able to resolve issues through the use of enforceable undertakings under s. 87B of the Trade Practices Act. (sub. 80, p. 102).

Available evidence suggests that many of these settlements involve smaller levels of damages (McGarvie 2005).

Other statutory mechanisms

Access to Part VA of the TPA does not limit an individual's right to take action under other sections of the act. Other statutory avenues that are at least technically available to consumers include:

- misleading or deceptive conduct (Part V Div 1 sections 52 and 53 of the TPA) where the marketing of unsafe products is associated with such conduct;
- unconscionable conduct (Part IVA sections 51AA, 51AB, 51AC of the TPA); and
- enforcement and remedies provisions (Part VI of the TPA) where a supplier fails to meet the requirements of a product ban, standard or recall, and where such contravention leads to loss or damage.

However, according to Ipp et. al (2002), the unconscionable and misleading or deceptive conduct provisions of the TPA have rarely been used to bring claims for compensation, primarily because common law has been viewed as an adequate source of redress.

Common law

Under common law (specifically the tort of negligence), a duty of care has been imposed on manufacturers to take reasonable steps to avoid foreseeable risk of injury. Previously, where that duty was breached and loss or injury resulted, manufacturers were liable for civil damages. In determining whether a breach had occurred, courts were required to consider what a reasonable person in the position of the manufacturer or supplier would have done in the circumstances (Kellam and Nottage 2007). This basis of liability has now effectively been reversed as a result of the civil liability reforms (see below).

Although this was considered an objective test of liability, judgements relating to breach of duty in cases mainly involving negligence issues have been subject to common trends over time. As the Chief Justice of New South Wales remarked prior to the introduction of the civil liability reforms:

From the 1960s to the 1990s, a long-term trend of judicial decision making can be discerned by which liability and damages expanded. However, that trend has, in recent years, been decisively stopped and reversed. There is now a significant body of recent High Court decisions, and an even larger body of intermediate court of appeal decisions, which find in favour of defendants, when the opposite decision would have been made if the long-term trend had continued. (Spigelman 2002)

This change to judicial practice has roughly coincided with the introduction of statutory restrictions on the scope of liability at common law in specific areas such as motor vehicle and industrial accidents and medical negligence that began in the 1980s. The aim of these restrictions is to reduce the cost of insurance for providers and to maintain the viability of the private insurance sector.

However, while there has been an explicit desire to promote uniformity in the application of these laws across jurisdictions, there are significant inconsistencies in the sixteen different statutory compensation schemes that now operate across Australia. As a result, Australia's personal injury compensation arrangements have been characterised by one observer (who also provided a submission to this inquiry) as fragmented, costly and inequitable (Smith 2003). As a corollary, the financial penalties facing prospective defendants (and hence one of the incentives to exercise reasonable care) vary depending on the context of the conduct in question. In the words of Smith:

Compensation for personal injury in Australia is a historical accident. It reflects the fact that the compulsory state schemes, first brokered by a strong labour movement in the early part of the 20th century, mainly sought to ensure compensation for people injured in the workplace, and by the then new fangled automobile. To the extent that there is now a national system it is very much still underwritten by those compulsory schemes and they have not kept pace with changes in society. In 2003 the fees, benefits and eligibility criteria vary depending on what state or territory you are in when injury occurs. (Smith 2003, p. 184)

In a more specific context, the NSW Court of Appeal noted in its judgement on *Landon v Ferguson* 2005:

The statutes in this State relating to workers compensation and common law damages claims by workers against their employers and others can be described as a hodge-podge. No consistent thread of principle can be detected. For example, the caps on damages under the Workers Compensation Act are lower than the caps under the Motor Accidents Compensation Act. Some workers' injuries occur in circumstances where the workers are required to bring their claims under the Workers Compensation Act. In other circumstances workers are required to bring their claims for damages under the Motor Accidents Compensation Act. In yet other circumstances neither Act applies, but other legislation governs the claims. No detectable rational reason explains the difference in categories. In some cases it is difficult to discern under which particular statute the case falls, and difficult and sometimes illogical distinctions have to be drawn. (NSWCA 2005)

These disparities in personal injury compensation arrangements have been amplified by the recent amendments to negligence law.

Civil liability reforms

In response to the rising cost and reduced availability of civil liability insurance (that focused on public liability and medical indemnity issues rather than product liability matters), an expert panel was convened to examine and review the law of negligence with the object of '... limiting liability and quantum of damages arising from personal injury or death' (Coonan 2002b).

The changes recommended in the subsequent report (see box 8.1), the *Review of the Law of Negligence* fell into three categories dealing with:

- establishing liability — changes to the law governing decisions on liability, including contributory negligence and proportionate liability;
- damages — changes to the amount of damages paid to an injured person for personal injury or for a claim of economic loss against a professional; and
- procedural reforms — time limits and methods for making and resolving claims, including court procedures, legal conduct and legal costs (Treasury 2006a).

Box 8.1 Selected recommendations from the Ipp review

The Ipp panel recommended the introduction of caps and thresholds to limit compensation awarded in negligence cases (primarily to reduce the number of small claims and the associated legal costs) and that equivalent provisions be applied to relevant parts of the TPA and Fair Trading Acts to prevent these avenues being used to circumvent the proposed changes to negligence law. Other key recommendations designed to restrict litigation and liability included:

- limits on recovery of legal costs from defendants (with no order for damages below \$30 000 and no more than \$2500 for damages up to \$50 000);
- abolition of exemplary and aggravated damages (as punishment for particularly severe breaches of the law);
- replacing joint and several liability with proportionate liability (so that defendants are only liable for that portion of loss or damage for which they are responsible);
- introducing the notion of contributory negligence (where negligent actions of a plaintiff that contributed to the loss or damage are taken into account and reduce the level of damages awarded);
- reducing the statute of limitations for actions under common law to three years from discoverability and introducing this time limitation to TPA provisions previously exempt from such limits (specifically Part IVA — unconscionable conduct, Part V Div 1A — product safety and product information, and Part V Div 2A — liability of manufacturers and importers of goods); and
- preventing the ACCC from bringing representative actions under the misleading or deceptive conduct provisions of the TPA (Part V Division 1) for damages for personal injury or death.

Between 2002 and 2004, all Australian jurisdictions enacted changes to negligence law that were both independent of, and in response to, the recommendations of the review panel. Relevant provisions of the TPA were also amended to prevent changes to negligence law being circumvented (as recommended by the review panel). This included the *Trade Practices Amendment (Personal Injuries or Death) Bill 2003*, which gave effect to the review panel's recommendation to remove scope for representative actions for damages for personal injury or death under the misleading or deceptive conduct provisions of the TPA.

Sources: Ipp et. al 2002, Treasury 2006a.

Commenting on the impact of the proposals on the consumer protection provisions of the TPA, the panel said that while they ‘... may reduce the level of consumer protection currently provided by the TPA (and equivalent or mirror legislation in the State and Territories) they do so consistently with the objectives underlying our Terms of Reference’ (Ipp et. al 2002, pp. 80-81). In any event, the panel judged that actions and remedies available under Part VI (injunctions, punitive and non-punitive orders, pecuniary penalties and criminal proceedings etc) of the TPA afforded

sufficient protection to consumers and, overall, the proposals would not unacceptably reduce consumer protection.⁵ However, a number of participants to that review disagreed, including the ACCC (see below).

While the panel recommended adopting a uniform national approach to negligence law embodied in a single statute, each jurisdiction individually and selectively applied (or rejected) specific proposals (table 8.1). The timing of the amendments has also varied (further complicating attempts to assess their impact). In describing the approach taken in different jurisdictions, one legal academic recently wrote:

Many of the reforms introduced by the states and territories depart in their detail from the Ipp recommendations, and most if not all of the jurisdictions elected, in varying respects, not to adopt some of the recommendations; indeed, in at least one respect most jurisdictions acted contrary to the recommendations of the Ipp review. (Wright 2006)

As a result, the scope of liability and the scale of damages available in different jurisdictions varies considerably, increasing the complexity of personal injury law in Australia. In commenting on the suite of changes that were implemented, the chairman of the review panel recently raised several concerns about the implications for plaintiffs (generally):

Certain of the statutory barriers that plaintiffs now face are inordinately high. ... Small claims for personal injuries are a thing of the past. Establishing liability in connection with recreational activities has become difficult. Stringent caps on damages and costs penalties make most plaintiffs think twice before suing. Public authorities are given a host of novel and powerful defences that are in conflict with the notion that the Crown and government authorities should be treated before the law in the same way as ordinary citizens. It is difficult to accept that public sentiment will allow these changes to remain long-term features of the law. (Ipp 2007b)

Impact of the civil liability changes

Given the highly targeted nature of the reforms to civil liability arrangements, it would be surprising if their *stated objectives* were not being achieved. Indeed, early evidence from a database established to monitor their impact indicates a significant decline in the average annual number of personal injury claims in most jurisdictions and a 16 per cent fall in the average cost of public liability claims (the category that includes product-related injuries) from the 2004 to the 2005 underwriting year (Treasury 2006a).⁶

⁵ The panel did acknowledge a significant body of opinion supporting the introduction of a no-fault system for dealing with personal injury claims (as in the New Zealand Accident Compensation Scheme), but noted the issue was not within the scope of its terms of reference (Ipp et. al 2002).

⁶ South Australia was the only jurisdiction to show a higher incidence of claims after tort reform, although the numbers involved were comparatively small and did not include all relevant data.

Table 8.1 Comparison of jurisdictional application of civil liability reforms

Establishing Liability	<i>Cth</i>	<i>NSW</i>	<i>Vic</i>	<i>Qld</i>	<i>WA</i>	<i>SA</i>	<i>Tas</i>	<i>ACT</i>	<i>NT</i>
<i>Foreseeability</i>									
No liability for simply failing to take precautions against foreseeable risk of harm; unless risk 'not insignificant' and unless reasonable person would have taken such precautions	na	√	√	√	√	√	√	√	u/c
<i>Causation and remoteness of damage</i>									
Plaintiff bears the onus of proof in relation to issues associated with causation	na	√	√	√	√	√	√	√	u/c
<i>Fair trading laws</i>									
Action prohibited for personal injury and death under Division 1 of Part V of the <i>Trade Practices Act 1974</i> and similar provisions under state and territory fair trading law	√	√	-	√	-	u/c	√	-	u/c
<i>Contributory negligence and assumption of risk</i>									
Negligence calculus for contributory negligence	na	√	√	√	√	√	√	√	u/c
100 per cent reduction of available damages for contributory negligence	na	√	√	√	-	-	√	√	u/c
<i>Proportionate liability for economic loss</i>	na	√	√	√	√	√	√	√	√
Damages									
<i>General damages</i>									
Set threshold before general damages apply	√	√	√	-	√	√	√	√	√
Assessment procedure for general damages	na	-	-	√	-	√	-	-	√
Cap on general damages	√	√	√	√	-	√	-	-	√
<i>Limits for loss of future earnings or capacity</i>	√	√	√	√	√	√	√	√	√
<i>Discount rate used in civil liability matters 5 %</i>	√	√	√	√	na	√	√	-	na
<i>No punitive damages in personal injury cases</i>	na	√	-	√	-	-	-	√	√
Procedural Reforms									
<i>Limitation periods</i>									
Commencement period is date of discovery	√	√	√	-	-	-	√	√	u/c
Limitation period 3 years	√	√	√	√	√	√	√	√	u/c
<i>Restrictions on advertising of personal injury legal services and touting</i>	-	√	-	√	√	-	-	-	√
<i>Limits on legal costs awarded for small claims</i>	-	√	-	√	√	-	-	√	√

[√] legislated. [u/c] under consideration. [na] no jurisdictional responsibilities. [-] not agreed

Source: Treasury 2006a.

But looking beyond their stated objectives, at least in principle, the recent amendments to civil liability arrangements are likely to have changed the incentives for *some* businesses to invest in safer products (even though the changes were primarily aimed at restricting suits against public authorities and medical

practitioners). This view was supported by the ACCC in a submission to the Commission's recent Review of Australia's Consumer Product Safety System:

In risk management terms, the consequences for suppliers (of having to pay out for damages) have been reduced by the 2004 amendments because the amount of claim has been limited. More importantly however is that the likelihood of having to pay out at all is further diminished. The likelihood has always been affected by whether a defective good will lead to injury and whether the injured party will sue. Now further diminishing factors are whether the injury reaches the required threshold and whether the claim can be made in the shortened time limit.

The ACCC is concerned that the 2004 amendments may have diminished the incentives for suppliers to make safe goods and this needs to be taken into account in reviewing the consumer product safety system as a whole. (PC 2006)

Of course, the impacts of the changes on the actual levels of safety built into products will also depend on the interplay of a range of other factors including:

- the potential reputational (and associated financial) damage from adverse publicity for firms which supply unsafe products;
- the specific characteristics of the product market (for example, the incentives to meet appropriate safety standards are likely to be weaker for a firm looking to exploit a short-term opportunity, by selling a one-off consignment, than for a firm with a long-term commitment to the same product and market);
- the nature of the product or service — this is especially relevant in relation to safety hazards that are complex in nature or not immediately obvious, and those where adverse health effects only become apparent long after the product has been used — asbestos providing a contemporary example); and
- the costs of defending particular claims.

Accordingly, the Commission commented in the Draft Report that coming to a definitive judgement about the overall impact of the civil liability reforms is difficult at this point in time. And even over time, this may continue to be the case given the paucity of reliable information regarding the incidence of product-related injuries and their cost (both before and subsequent to the introduction of the civil liability reforms).

That said, it noted that implementation of the recommendations made in its recent report on consumer product safety (see box 8.2) would help to address this information gap to some extent. Among other things, that report proposed:

Box 8.2 Key recommendations from Review of Australia's Consumer Product Safety Arrangements

In 2006, the Commission conducted a review of Australia's consumer product safety system and found that the combination of market forces, product liability laws, media scrutiny and organised consumer advocacy provide reasonable incentives to encourage most businesses to supply safe products. However, it noted that significant regulatory inconsistencies between governments reduce the overall efficiency and effectiveness of the system. The Commission also found that while it was too early to judge the impact of the recently introduced civil liability reforms, the changes are likely to have weakened the incentives for some businesses to supply safe products.

The Commission made a number of recommendations to improve the operation of the current consumer product safety system, including:

- introducing a single national product safety law administered by the ACCC or, if this is not achievable, harmonisation of core legislative provisions across jurisdictions.
- introducing nationally applied threshold tests for product bans and mandatory recalls that include notions of 'reasonably foreseeable conditions of use'; and 'reasonably necessary to prevent or reduce risk' for mandatory safety standards.
- developing a broadly-based hazard identification system based on information and analysis of consumer product incidents that is disseminated to all jurisdictions.
- establishing a national system for the exchange of complaints information.
- requiring suppliers to report products associated with serious injury or death.
- provision of better regulatory information to consumers and businesses through a 'one-stop-shop' Internet portal.
- adoption of a hazard-based approach to mandatory safety standards and streamlining the standards-making process to improve timeliness.
- undertaking a review of existing product recall guidelines to improve their effectiveness.
- establishing a national clearinghouse for relevant information and analysis, complemented by a comprehensive study of consumer product-related injuries.

In responding to the report, CoAG (2006a) requested the Ministerial Council on Consumer Affairs (MCCA) to develop options for a national system for product safety regulations and a recommended approach. Subsequently, CoAG (2008) agreed that the Australian Government should assume greater responsibility for regulating product safety — with MCCA, through CoAG's Business Regulation and Competition Working Group (BRCWG), to develop a detailed implementation plan for a national system by July 2008. CoAG has further indicated that, under this national system, States and Territories could retain the power to impose interim product safety bans (an 'intermediate' model that was not examined by the Commission in its consumer product safety study).

Sources: PC 2006, CoAG 2006a, 2008.

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- commissioning of a base-line study to identify the historical incidence and costs of product-related injuries;
 - the development of a hazard identification system to gather information and analysis of consumer product incidents;
 - the introduction of mandatory reporting requirements for voluntary product recalls; and
 - a requirement that suppliers report products that have been associated with serious injury or death to the appropriate regulator or, if that should not be adopted, report products which have been the subject of a successful product liability claim or multiple out-of-court settlements.

A base-line research study examining product-related accidents was commissioned by MCCA in 2006 and is now complete. The results are due for public release around May 2008.

In addition to commenting on enforcement of the product safety provisions in the new national generic consumer law (see chapter 4), respondents to the Draft Report also provided input on a range of other product safety matters. Apart from suggestions that the Commission should revisit the need for a General Safety Provision (see below), participants variously argued that:

- product safety regulation should be based on identified hazards rather than the current practice of being either product or industry specific;
- there is a need for more stringent reporting requirements than those suggested by the Commission; and
- that notification of product recalls should be to the ACCC alone rather than the current requirement for multi-jurisdictional reporting.

There were also suggestions made on how to ensure that data collection requirements to meet the Draft Report proposals are cost-effective.

A selection of comments from participants on these issues is presented in box 8.3.

In responding to these suggestions, the Commission notes that this current inquiry is not a supplementary review of Australia's product safety arrangements. Having said that, it does see merit, *prima facie*, in some of the suggestions that have been put by participants, and in particular:

- using hazard data to inform new, and review current, regulatory interventions in this area;
- rationalising product recall notification requirements; and

-
- implementing cost-effective data collection processes.

Such matters should be considered as part of the development of the product safety component of the new national generic consumer law. Indeed, certain issues (such as the ACCC becoming the notification point for product safety recalls) would be automatically addressed were, as the Commission has proposed, the Australian Government to become solely responsible for regulating consumer product safety.

Box 8.3 Participant's comments on the product safety recommendations

The Australian Toy Association (ATA) argued that product safety regulation should be hazard based and that hazard data should be used to vet the efficacy of regulation:

... regulation should be hazard based rather than product or industry specific In the recent case of Bindeez beads regulation was introduced banning Bindeez which prevented the product being sold even after the hazardous material had been replaced and also did nothing to stop the hazardous material being used in any other product.

The ATA is also aware of many regulations that exist in one jurisdiction and not others. It is clear that there is not a universal acceptance of the need for these regulations. Regulation should be properly justified by hazard data and any existing regulation that does not meet this criterion should be removed. (sub. DR161, p. 2)

Coles Group supported the suggestion that the Australian Government alone be responsible for the consumer product safety regime in the specific context of product recall requirements.

... it should be mandatory for product recall notifications to be made to the national consumer protection regulator (the ACCC) only, rather than the multiple bodies that must be advised presently. (sub. DR146, p. 2)

Dr Luke Nottage generally supported the draft recommendations but urged more far-reaching reform. Specifically,

Since ever fewer product liability claims are being filed ... related to the effects of tort reform since 2002, [the proposal] requiring suppliers to report serious product-related injuries only if multiple settlements or a successful claim ... will have little effect on suppliers.

Since "further reforms to civil liability laws" ... seem very unlikely for several years ... a separate General Safety Provision (as in the EU) should be added as well.

The "precautionary principle" ... should guide risk assessment in triggering remedial action in this ... and indeed related fields under generic consumer legislation. (sub. DR114, p. 12)

Vero, the commercial insurance arm of Suncorp, was concerned about the costs of obtaining the information necessary to give effect to the draft proposals. It said:

... it is seen as likely that, insurers, specifically claims departments, will be a major source of the data required in relation to product-related injuries and consumer product incidents. ...

This potentially involves capital expense in modification of computer systems to capture the data required and administrative time in training and providing regular reporting. Government needs to work with the insurance industry to ensure that increased [reporting] requirements ... are implemented in a cost effective manner. (sub. DR171, pp. 6-7)

The Commission also considers that Australian Governments should monitor trends in product-related accidents, including any impact on product safety levels from the civil liability reforms. Such monitoring should draw on the MCCA base-line research study and the other relevant initiatives proposed in the Commission's consumer product safety inquiry to improve the available information base. If evidence of any significant diminution in product safety is revealed, there could be a case to re-examine product liability arrangements. In these circumstances, the relationship between those arrangements and other personal injury compensation regimes could also be reviewed.

RECOMMENDATION 8.2

Consistent with the recommendations in the Productivity Commission's Review of the Australian Consumer Product Safety System, Australian Governments should:

- *develop a hazard identification system for consumer product incidents;*
- *introduce mandatory reporting requirements for voluntary product recalls; and*
- *require suppliers to report products associated with serious injury or death or products which have been the subject of a successful product liability claim or multiple out-of-court settlements.*

Ideally, these measures should be implemented as part of the development of the new national generic consumer law (see recommendation 4.1).

RECOMMENDATION 8.3

Drawing on the mechanisms proposed in recommendation 8.2 and on the baseline study examining product related accidents prepared for the Ministerial Council on Consumer Affairs, Australian Governments should monitor trends in product safety, including any impacts of the civil liability reforms, with a view to assessing whether the incentives to supply safe products continue to be adequate.

General Safety Provision

One potential option to improve the incentives to supply safe products (should this be required) would be to introduce a General Safety Provision that would create an explicit *ex ante* obligation for suppliers to market only 'safe' (or not 'unsafe') products. Under such a provision, action could be taken against a producer or supplier if a product is deemed unsafe, irrespective of any injury or loss having been caused by the product.

Advocates of this mechanism argue that it would provide for a more pro-active product safety regime compared to the current system focussing on redress after the event, as it affords the regulator broader power to act before injury occurs and highlights for producers their obligations to supply safe goods. (See, for example, Victorian Government, sub. DR226, pp. 68-69.) And one participant to this inquiry, Kildonan Uniting Care, considered that it could actually ease the burden on regulators.

The onus on suppliers to ensure their products meet the regulated Australian standards can reduce overall policing and regulation and lift confidence in the market. (sub. DR206, p. 8)

Similar mechanisms have been introduced in other countries, including by most members of the European Union (since 1992) and by New Zealand.

The Commission was specifically asked by MCCA to consider the desirability of introducing a General Safety Provision in its recent review of Australia's consumer product safety system (PC 2006). At that time, it noted there could be a number of potential benefits from introducing a provision of this kind, including that it could strengthen incentives to supply safe products, lessen the need for mandatory safety standards and reduce administrative costs. But it went on to argue that those benefits were likely to be limited for a variety of reasons including that:

- the current system appears to be generating reasonable safety outcomes;
- action can already be taken to recall or ban unsafe products irrespective of whether an injury has occurred;
- without better enforcement and warning systems, a General Safety Provision alone would make little or no difference to early detection of hazards;
- based on experience in other sectors and countries, most if not all of the existing regulatory framework would remain;
- mandatory standards would still be required for higher risk products;
- while the intention of a General Safety Provision is to make suppliers more proactive on safety issues, the previously stricter product liability rules should already have had this effect; and
- a General Safety Provision is likely to have little impact on recalcitrant and fly-by-night suppliers.

Transitional costs associated with implementation of a General Safety Provision, significant uncertainty about how a benchmark level of safety should be defined and measured, and lack of evidence regarding significant benefits in countries with similar mechanisms, reinforced the Commission's perception that introduction of a General Safety Provision would not provide a net benefit to the community.

Overall, it judged:

The benefits of a General Safety Provision (GSP) applied to consumer products under reference are unlikely to justify the costs involved. A particular concern is that the GSP may fail to target the areas of biggest risk and may deliver little benefit beyond what might be achieved with appropriate modifications to the existing consumer product safety regime ... (PC 2006, p. 131)

However, the Commission did note that it was too early to judge the impact of the civil liability reforms on product safety outcomes and that any future consideration of a General Safety Provision should be undertaken in the context of examining the overall regulatory framework rather than the one aspect of it under reference at that time.

The nature of the evidence presented to the Commission during this current inquiry has not been sufficient for it to conclude that the case for introducing a GSP has increased in the two years since its earlier report into consumer product safety. But this is obviously a matter that needs ongoing examination, and not just because of the reforms to civil liability law. If a reliable evidence base emerges indicating that the incidence of product-related harm has increased, whether attributable to changes in those laws or other factors, the need for a GSP should be revisited. And consistent with good regulatory practice, the efficacy of alternative mechanisms should also be considered. Those alternatives might draw on some other recent developments regarding better methods of identifying and testing consumer product safety hazards and assisting suppliers to assess and manage consumer product risks across the supply chain (see Standards Australia, subs. 44 and DR136).

9 Access to remedies

Key points

- Consumer access to redress is an important feature of existing consumer policy regimes. Avenues of redress include regulatory agencies, industry-specific alternative dispute resolution (ADR) schemes, and lower courts and tribunals.
- The low value of many consumer transactions requires that any redress system is efficient, timely and accessible if consumers are to use it. Once consumers have attempted to resolve problems privately, they need to be able to access a layered range of avenues of redress involving:
 - efficient systems for providing information and receiving and referring complaints;
 - alternative dispute resolution; and
 - judicial redress, including adequate scope for representative actions.
- The main factors impeding the effectiveness of the existing system are gaps and overlaps in ADR schemes; the costs, intimidating nature and jurisdictional inconsistencies of judicial action for smaller claims; difficulties in undertaking representative action; and problems in referring consumer complaints to the appropriate body.
- There are several strategies to overcome these weaknesses, including:
 - improved systems to help consumers find out about how and where to make complaints;
 - a more consistent framework for energy ADR across jurisdictions and in financial services across the different segments of the industry, and an expanded role for the telecommunication ombudsman;
 - an adequately resourced capacity for consumer ADR in areas not covered by existing ADR schemes and for legal aid and financial counselling for disadvantaged consumers generally;
 - some procedural changes and greater standardisation of jurisdictional requirements for small claims courts and tribunals; and
 - a capacity in the generic consumer law for regulators to take representative action on behalf of affected consumers who are not parties to the proceedings.

9.1 Introduction

Compensation or some form of amends for loss sustained by a consumer when markets fail to function properly — the concept of ‘redress’ — is an important element of consumer policy regimes.

There are three broad observations that should be noted upfront about what this chapter covers. First, a full consideration of redress mechanisms would invoke a large number of design questions about specific processes and institutions of the kind spelt out by Cashman (2007) — for example, pre-litigation disclosure. However, such detail is outside the scope of this inquiry, which is focused on the broader consumer framework. Accordingly, this chapter places redress in an economic framework, considers some of the bigger systemic problems and the broader institutional design changes that might be beneficial over the longer run.

Second, for the sake of convenience, this chapter deals with redress and the next with enforcement. The distinction between redress and enforcement is, to a significant extent, artificial, since restitution often requires effective enforcement — they are two sides of the same coin. Even non-compensatory penalties imposed on a trader that has broken the law can act as a form of redress since they meet consumers’ needs for justice to be seen to be done. And compensation paid by a supplier to consumers for a contravention of consumer law — an instance of redress — is often an essential part of an effective enforcement regime since it provides deterrence generally. However, in looking at the policy issues, this chapter focuses on what consumers need when purchases go wrong.

Third, questions about the capacities of State and Territory lower courts and tribunals to provide redress for consumers under various broad institutional options for applying the new national generic law are addressed in chapter 4, rather than in this chapter.

9.2 Criteria for assessment and some principles

Redress arrangements should be effective and efficient in the broadest sense (box 9.1). They should be accessible, procedurally fair, proportionate, timely, and accountable, have no major gaps in coverage and be run efficiently.

Based on the Commission’s analysis and the views of participants about various deficiencies, this chapter focuses on four issues about the design of the system.

Box 9.1 **A framework for assessing redress mechanisms**

Redress processes (and enforcement) aim to secure just outcomes for consumers and businesses and to provide financial compensation in some instances. But they have other features that need to be taken into account in deciding how to design an efficient and effective regime.

The costs of redress can be high. These involve the resources of the various agencies and courts that provide them, their support staff, the policymakers, the consumer advocacy agencies and all the various lawyers and other intermediaries that are involved. They involve unpriced costs too — such as time spent in seeking and securing redress, emotional distress for consumers and businesses and a litany of other obstacles that represent costs to users (spelt out by Cashman 2007 and in IPSOS 2007). In higher courts, the monetary costs can be large. The average recurrent cost per finalised civil case in magistrates' courts in Australia — often the first judicial recourse for a consumer — was a relatively modest \$280 in 2005-06 (derived from SCRGSP 2007), but is much greater in higher courts. The average costs of civil matters finalised in a District Court and a Supreme Court are about 10 and 21 times this respectively. Costs recovered from businesses or consumers are only a share of these.

Redress processes have positive and adverse incentive effects:

- They serve an enforcement role in their own right, pushing up the cost of, and thereby deterring, 'bad' behaviour by business.
- Since consumers have the option of seeking more formal redress later, they increase the leverage that complainants have in private negotiations with businesses and reduce the transaction costs of such negotiations. Where complaints are valid, this enhances consumer welfare and efficiency.
- Expensive redress systems that carry the risk of awarded costs, favour parties with deep pockets (usually businesses). This provides a case for cheaper, less risky redress, at least in initial stages of disputes.
 - But strategic behaviour is not just exercised by businesses, and nor are they always in the wrong. No-fault misunderstandings may occur and consumers can also contrive detriment. Systems in which consumers bear no charges for redress are more prone to such misuse.
- They provide incentives for public disclosure of complaints, which helps regulators to identify rogue traders and systemic problems that might require legislative or other responses.
- They provide efficient insurance by reducing consumer risk when engaging with suppliers whose reputation is inherently uncertain (such as for experience goods or for new, smaller firms). Confident consumers are more likely to be willing to shift their demand to new suppliers, aiding innovation and competition in its own right.
- Accessible and cheaper redress mechanisms can divert complaints from more costly ones.

First, the need for an efficient and quick way of directing consumers to the best redress option — sometimes just the knowledge of their rights — is particularly important when the system of redress is complex and the individual detriments are modest. Low value transactions dominate consumer complaints (IPSOS 2006). Just the costs of looking for help will deter complaint if referral (and information provision) processes are inefficient. Section 9.3 explores some of the potential problems in the current system and mechanisms to remedy these.

Second, the principle of proportionality applies as much to redress as it does to enforcement — it is hard to justify a resource-intensive redress mechanism unless there are commensurate benefits. Only highly economical redress methods can cost-effectively reach consumers suffering detriment from small value purchases. Alternative dispute resolution schemes, such as ombudsmen, offer such a method, as do small claims procedures. The key issues surrounding them are discussed in sections 9.4 and 9.5 respectively.

Third, Australia uses a variety of judicial institutions and procedures across States and Territories. Some of this variety is not appropriate (section 9.5).

Fourth, some consumers may need other parties to assist them seek effective redress (section 9.6):

- Representative action by a regulator may be able to deal with modest individual consumer detriments where private incentives to act are small, but whose collective significance nevertheless warrants redress.
- It is sometimes argued that consumer groups should have a larger role in activating investigations by a regulator.
- Disadvantaged people need help to access effective redress.

9.3 Making a complaint

Redress is mostly instigated by complaints from consumers. Overwhelmingly they initially complain to the business concerned and most complaints are resolved successfully through this informal route (IPSOS 2006, 2007). But in those instances when consumers take complaints beyond this, they have many choices about who to contact. These contacts vary depending on their jurisdiction, the type of good or service purchased and the nature of the complaint. They include State and Territory and Australian Government regulators, over 20 consumer ombudsman's offices, multiple private dispute resolution and complaint bodies, and a variety of legal aid offices, tribunals, and small claims courts across jurisdictions.

Ideally, consumers would directly approach the right redress body. If not, they should be rapidly referred to the right body by any of the various contact points in the redress system. However, there is some concern that consumers are confused by the diversity of choices about where to obtain help and that referral processes are of mixed quality.

Several online sites provide advice to consumers about which option to choose. *Complaintline*, a private initiative developed as a non-profit community service (with no government funding), appears to be the most useful in this regard. It provides a comprehensive, guided listing of complaint and dispute resolution options for consumers, as well as information on other consumer policy matters. The ACCC also provides an online one-stop website, *Consumers online*, but it is structured in a way that would make it difficult for some consumers to choose the right complaint body. For instance, a search of the category, Telecommunications and Internet, of the 'Consumer Handbook Online' lists 20 contact points alphabetically without indicating the best likely first contact point for a consumer complaint.

In addition, there is no single national system that provides telephone guidance about where to make complaints among the multiplicity of state and national bodies — which may be particularly important for consumers without access to the Internet.

If confusion arises, consumers may choose the wrong complaint option with the risk that, as they are passed to other bodies, they will no longer seek to make a complaint — 'referral loss'. Some consumers will be deterred in the first place by the many complaint and information options.

The evidence about the extent and nature of these problems is mainly qualitative or suggestive. In its inquiry consultations, the Commission was frequently told that consumers did not know where to make a complaint and that referral processes could be poor. Written submissions and other evidence also identified such problems. For example, some participants claimed that basic complaint resolution options, like an ombudsman, have low recognition among young people (National Children's and Youth Law Centre, sub. 40, p. 9 and the Banking and Financial Services Ombudsman (BFSO) sub. DR170, p. 3). In fact, only 15 per cent of consumers of all ages have unaided awareness of the Australia-wide Telecommunications Industry Ombudsman (TIO), though problems in telecommunications are the most frequently encountered by consumers (Sweeney Research 2006). About 65 per cent of consumers with a banking complaint did not know to approach the BFSO and 99 per cent were unaware of the Financial Industry Complaints Service (FICS) as a possible entry point for such complaints (ANZ and ACNeilson 2005b, p. 249). Recent Victorian survey data revealed that there is relatively low awareness of the Energy and Water Ombudsman

(IPSOS 2007). Other Victorian data suggest that three times as many consumers with a complaint about essential services (initially) go to Consumer Affairs Victoria than to the specialised ombudsman services that were set up to deal with most of these concerns (IPSOS 2006).

External referral data from consumer agencies provide additional evidence about the extent to which consumers are confused about where initially to lodge a complaint. In some cases, there are few external referrals. For instance, Consumer Affairs Victoria refers less than 2 per cent of its initial inquiries and the Energy and Water Ombudsman (Victoria) fewer than 5 per cent (Department of Justice 2007, p. 15ff). But referral is much higher in other contexts:

- The ACCC diverts around 25 per cent of its consumer inquiries to other bodies, mainly State and Territory Offices of Fair Trading (ACCC, sub. 80, pp. 40-41).
- In 2005-06, about one in five consumer inquiries to the TIO were deemed ‘out of jurisdiction’ — indicating that consumers did not know about the boundaries of its functions (Consumers Telecommunications Network, sub. 78, p. 51).

Overall, it is hard to know the severity or consequences of confusion faced by consumers because many who mistakenly go to one agency will still be promptly and correctly re-directed to another. Cross-referral appears generally to function well,¹ and the extent of referral loss appears to be modest (Department of Justice, 2007, p. 15ff).

Nevertheless, given the qualitative evidence cited above, the system could be improved. One strategy for reducing consumer confusion is to re-structure ADR bodies to reduce unnecessary proliferation and overlaps. This would also have other benefits. It is considered in section 9.4.

Another approach is to develop an integrated national system that provides information to consumers about their rights and directs all consumer complaints to the correct body. Such an approach would build on arrangements mooted by the Commission in consumer product safety, which involved a national web-based portal for providing information about product safety and a central location for complaints (PC 2006, p. 214, p. 258). Whether such an integrated approach should be pursued will depend on the particular model adopted, its likely efficiency and whether any incremental further reduction in confusion and referral loss is worth the investment required.

¹ Though in some cases, different consumer complaint bodies are also confused about where a matter should be handled, with different referral patterns for identical problems. According to the Consumers’ Telecommunications Network (sub. 78, p. 50), Offices of Fair Trading sometimes direct consumers to agencies that do not have jurisdiction over the referred matter.

There are several broad mechanisms that could be used to develop such an integrated national system, each with advantages and limitations:

- (a) retention of existing contact points, but with more efficient networking and cross-referrals between bodies, so that a complaint made in any one part of the system is rapidly transferred to the right place.
- (b) the creation of a virtual single telephone referral centre that takes advantage of the current network of contact and referral services spread across all jurisdictions. It could involve the existing decentralised telephone call centres, re-badged from a consumer perspective as a single entity and using a common referral and training system; or
- (c) creation of a centrally-run national contact point for consumers akin to *UK Consumer Direct* and the New Zealand complaints system (PC 2004a). These use single call centres, buttressed by online and other options, to direct consumers to the right resolution bodies. Such an integrated approach was supported by various participants (for example, Kildonan Child and Family Services, sub. 65, p. 23; Choice, sub. 88, p. 63). The model is already applied in some specific consumer areas in Australia, for example, financial ombudsmen through the Financial Ombudsman Service.

The ACCC (sub. 80, p. 129) was sceptical about a new centrally-run telephone call centre — inherent in option (c) — because it would entail ‘considerable costs’ and would not reduce the need for call centres used by the various state and Australian Government regulators. It remains a long run possibility if Australia ultimately shifts to single national regulator responsible for generic consumer policy (chapter 4).

Option (b) would also involve significant establishment costs, including extensive training, promotion of the entity as a ‘brand’ for consumers, and negotiation to get agreement by the various jurisdictions about the level of funding each would have to commit to it. It may also be the case that the existing cross-referrals that take place between jurisdictions would merely be replicated as cross-referrals *within* the new virtual system (Victorian Government, sub. DR226, p. 11).

Accordingly, while there are generic consumer regulators in each jurisdiction, (a) is likely to represent the only practical policy option.

Regardless, the ACCC’s web-based information tool for consumers, *Consumers online*, should be enhanced to emulate the best features of *Complaintline*. This tool should guide consumers to the right dispute resolution bodies and provide other information to them. To ensure that it is easy to use and has the appropriate content, any such tool should be subject to consumer testing among diverse groups and take

account of comments from advocacy groups (National Children's and Youth Law Centre, sub. DR196, p. 8 and Redfern Legal Centre, sub. DR151, p. 5). The costs of enhancement are likely to be low since they would mostly take the form of one-off costs of changing (and testing) an already developed website. The Commission's recommendation of such a tool was supported by many participants in this inquiry.² The ACCC is now progressing its development (sub. DR176, p. 11).

Of course, it should not be the only tool for increasing accessibility to redress, as noted by the National Ethnic Disability Alliance (sub. DR135, p. 2) and the Victorian Aboriginal Legal Service Co-operative Ltd (sub. DR238, p. 8). Other measures, such as consumer-based education on consumer rights (chapter 11) and adequate translation services, are also important.

An associated, but separate, issue is agencies' use of data on complaints to uncover serious systemic issues and coordinate investigations across jurisdictions. There is an existing system for doing this — AUZSHARE — a shared database of (serious) complaints and cases developed by the Fair Trading Officers Advisory Committee. However, only three jurisdictions upload complaints to AUZSHARE, with the ACCC calling for participation by all Australian governments (sub. 80, p. 130). There are sound arguments for a genuinely coordinated approach to complaints intelligence, and the incremental costs of participation by the currently missing jurisdictions are unlikely to be large. This was generally supported by participants, although the Office of the Privacy Commissioner noted the need for appropriate preservation of privacy and open disclosure to consumers of how the data are used and protected (sub. DR190, p. 3).

RECOMMENDATION 9.1

To facilitate more effective referral of complaints to the right body and sharing of information on complaints:

- ***all consumer regulators should participate in the shared national database of serious complaints and cases, AUZSHARE; and***
- ***the Australian Competition and Consumer Commission should provide an enhanced national web-based information tool for guiding consumers to the appropriate dispute resolution body, as well as providing other consumer information. It should be subject to consumer testing to ensure that it is easy to use and has the appropriate content.***

² For example, the BFSO, sub. DR170, p. 3; Optus, sub. DR173, p. 6; Telstra, sub. DR156, p. 12; and AMTA, sub. DR175, p. 4.

9.4 Alternative dispute resolution

Alternative dispute resolution (ADR) schemes generally offer relatively economical, accessible, fast arrangements for dealing with individual complaints that could not be cost effectively tackled using any other method (ASIC, sub. 103, p. 52). For example, on a full cost-recovery basis, the marginal cost of stage one complaints — the most common for the Telecommunications Industry Ombudsman — is \$33 (levied on the business). This is less than the resource cost of court action — perhaps reflecting the number and routine nature of complaints addressed in this area.

ADR schemes often do not require evidence to be given in-person, which helps lower their costs and allows them to be located, if needed, in just one place. The informal nature of ADR may be more likely to encourage use by disadvantaged consumers. Industry-based ombudsman offices have dependable funding, and often a capacity to make binding decisions on their business members if a complaint proceeds that far. ADR can also readily adapt to the needs of particular groups of consumers, such as Indigenous Australians (Victorian Aboriginal Legal Service Co-operative Ltd, sub. DR238, p. 3).

As well, access to cheap redress can help to address inappropriate systemic practices. For instance, the Consumer Action Law Centre observed that in the past:

... insurers routinely denied 10 per cent or so of the quantum of car accident claims on the basis that the claimant was 10 per cent at fault. These amounts were generally too small for a consumer to fight through the courts or tribunals. However, caseworkers saw this practice virtually stop overnight when the Insurance Ombudsman Scheme was established. This is an example of a change in practices that can occur simply by improving access to dispute resolution. (sub. 94, p. 91)

ADR can also be used for highly complex cases or where the alleged consumer detriment is large, as in many disputes concerning financial services (though various ceilings apply to claims). In these instances, it provides an accessible mechanism for consumers who may lack the resources for court action, while also avoiding the costs borne by society generally from using expensive judicial processes.

But despite their value, ADR schemes have some well explored limitations, including the challenge of ensuring that decision makers are accountable for their performance (ASIC, sub. 103, p. 53). They cannot supplant the judicial system. Indeed, there are a host of policy questions about ADRs that the Commission has left untouched because they have been addressed well by others (for example, Field 2007). For this chapter, the main strategic focus is the *scope* of ADR provision, which affects specialised and generalised ADR services differently.

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- Some specialised ombudsman schemes have ‘gaps’ — incomplete coverage of the issues that concern consumers. And consumer complaints outside the specialised ombudsman areas are not covered by a consistent ADR process.
 - Conversely, other schemes may have potentially inefficient overlaps, or there may be too many disparate bodies with too small a scale and excessive costs.

Defining the roles of ombudsman offices

Whatever substantive changes may be required to existing ombudsman offices, an important ongoing requirement is for processes in government that periodically re-assess (say every five years) the nature and structure of ADR arrangements to address redundancies or new needs. This is probably best overseen by the key regulators — the State and Territory Offices of Fair Trading, ACCC and ASIC — in consultation with consumer groups, business, the peak ombudsman body (the Australian and New Zealand Ombudsman Association), individual ombudsman offices and other regulators. And as emphasised by Energywatch UK (sub. DR197, p. 6), the key aspiration of ADR services is a quality service and adherence to best practice. Certain strategies, such as consolidation of disparate services, may help achieve this end, but they are not appropriate goals by themselves.

There are some gaps

The most glaring gap in consumer dispute resolution processes relate to consumer credit. The latter gap was perceived as a ‘gaping hole’ by the Credit Ombudsman Service Limited (COSL, sub. 53, p. 3). Specifically, there is no obligation for businesses supplying credit or financial advice associated with credit to belong to an ADR scheme, though many voluntarily agree to do so. This gap would be closed by the Commission’s recommendation (5.2) that such financial services should belong to an ASIC-approved dispute resolution scheme.

A more general gap concerns all the goods and services that are not covered by specific ADR arrangements. Some participants have argued that ADR — especially that provided through ombudsmen — should be more broadly adopted (BFSO, FICS & IOS, sub. 89, p. 14 and CCAAC, sub. 38, p. 10). This invites the question of whether a ‘super’ ombudsman office should cover the consumer transactions not adequately covered elsewhere. This would have several advantages. Consumers would be able to access dispute resolution services for all goods and services and it would avoid the future proliferation of new industry-specific arrangements.

Yet such a general body may be unable to replicate the features that make existing industry-based ombudsman services successful. Industry ownership (and funding) of a general ombudsman would probably be hard to achieve given the huge number of Australian businesses and their diversity — with the prospect of charges for consumers. (There are around one million business enterprises with employees and more when non-employing businesses are considered.) Its cost structures could be higher given a lesser capacity for specialisation when complaints arise from such diverse segments of the economy. And in the absence of industry ownership, it may be a violation of natural justice to give the ombudsman determinative powers over any significant claims unless these were subject to subsequent court appeal. Allowing such appeals begins to mimic the judicial system, which is what ADR is intended to avoid.

In that context, one model for ADR for consumer transactions not covered by the existing ombudsman arrangements could centre on mediation and conciliation. There is already some provision for this kind of general dispute resolution. There is limited provision of mediation services by courts (Field 2007, p. 97), often through pre-hearing processes. More often, such services are provided by State and Territory Fair Trading Offices and other government departments. For instance, the Queensland Department of Justice and Attorney-General provides free Dispute Resolution Centres based on mediation throughout that State, while Consumer Affairs Victoria provides dispute resolution services for more than 12 000 complaints a year.

However, there are limitations in these services. Consumers may still be deterred from making a complaint if their initial point of contact is a court. ADR processes run by the regulators and government departments vary in their power and scope — a comment that applies more generally across the whole field of ADR (Department of Justice 2007). For example, Consumer Affairs Victoria cannot compel a party to a dispute to attend mediation or conciliation and its conciliators play a strictly facilitative role (Victorian Government, sub. 92, p. 84).

Accordingly, there may be value in developing a more coherent set of generally applicable consumer ADR arrangements — a view supported by the Victorian Government (sub. DR226, p. 12). Such arrangements would require appropriate resourcing (probably by government); the avoidance of sub-scale specialised ADR schemes; similar powers across jurisdictions; links with the existing ombudsmen to aid learning; and the capacity to refer relevant matters to judicial processes. Whether these features would be incorporated into a single ombudsman, part of re-invigorated ADR within a government regulator, or an adjunct to tribunals/magistrates courts is a subsidiary question, best resolved through specific cost-benefit analysis of detailed alternative proposals.

Redrawing the boundaries of existing ombudsman offices

Ombudsman offices are products of history. The number and variety reflect the gradual corporatisation and de-regulation of utilities across various jurisdictions, and the development and wider use of new, complex services in financial and telecommunications services. There are now six energy, and sometimes associated water, ombudsman in separate Australian States (but just one telecommunications ombudsman since that reform process was national). In financial and communications services, the proliferation has taken the form of industry, rather than jurisdictional, specialisation. For example, there are eight financial service ADR bodies, six specifically taking an ombudsman form. However, the structure of ADR services that emerges from these historical influences is not necessarily well-suited to the future. Their continuing formation was seen as ‘ad hoc’ (Victorian Government, sub. 92) and growing like ‘topsy’ (Simon Smith, sub. 10, attachment).

Whether this proliferation matters depends on whether:

- it confuses consumers about where to go;
- variations between the individual schemes mean consumers buying similar services are treated in a materially different way either procedurally or substantively; or
- there are efficiency gains in specialisation or alternatively in consolidation or sharing common assets.

Using these as the criteria, the evidence suggests that there are grounds for re-considering the boundaries of ADR arrangements in telecommunications, energy and water, and financial services.

Telecommunications

In communications, the scope and nature of services is rapidly evolving with technological change and with the convergence of telecommunications and broadcasting. With this expansion, new needs for dispute resolution have arisen, for example, in 190 premium service numbers and Pay TV, which have been met through the formation of different complaint handling methods and institutions. The TIO deals with disputes concerning mobile, ISP and fixed-line telecommunications services, with handsets purchased as part of a mobile contract, and with mobile premium services. Complaints concerning other premium services, other handsets, Pay TV, privacy issues and content-related issues (such as obscenity) are dealt with by other agencies, despite some overlap in the underlying difficulties that prompt complaints.

Some participants claimed that the existing arrangements are becoming overly complex, with the potential for incomplete redress, insufficient intelligence about systemic problems, consumer confusion, and the loss of economies of scope (Pinnock 2007; Choice, sub. 88, p. 30; the Consumers' Telecommunications Network [CTN], sub. 78, p. 62). The Victorian Government observed:

The carve up of telecommunications regulation may make legislative sense. However, it does not make sense to consumers and is a significant source of consumer confusion. (sub. DR226, p. 11)

This prompted calls for a single communications ombudsman embracing most services (Choice, sub. 88, p. 83), or for a review of complaint handling in this area that takes account of the desire by consumers for a one-stop shop (CTN, sub. 78, p. 62 and sub. DR211, p. 3). The TIO itself indicated that it supports the concept of a one-stop shop, while also acknowledging some practical realities in achieving this end (trans. pp. 869ff).

However, many participants saw benefits in the existing range of specialised ADR arrangements. For example, the CTN (sub. DR211, p. 4) noted the effectiveness of the Telephone Information Services Standards Council (TISSC), which covers complaints relating to 190 premium service numbers. The TISSC not only provides an ADR function, but also pre-empts problems by monitoring 190 premium services. Similarly, the present division of responsibility for mobile handsets between the TIO and various Offices of Fair Trading apparently works well. The demarcation avoids the practical problem that full coverage by the TIO would vastly expand the number of business members of the TIO scheme, and potentially weaken the capacity of the TIO to undertake its core tasks in telecommunications (Legal Aid Queensland, sub. DR202, p. 3; Telstra, sub. DR156, pp. 12-13). Many service providers were generally opposed to any significant widening of the functions of the TIO, arguing that existing arrangements were working well enough. Telstra (sub. 35, p. 20) argued that there is a risk that a mega complaint body might dilute the specialised expertise currently present in separate bodies, such as privacy matters covered by the Office of the Privacy Commissioner.

Whatever the merits of retaining some separate ADR processes under the broad umbrella of communications, ADR provision could become increasingly fragmented and confusing if new ADR agencies are formed following further technological and market changes. The Commission's recommendations about better referral systems will partly help. But there should be immediate consolidation of pay TV services because they share so many features with standard communications services and are often bundled with them. A longer-run transition to more integrated complaint arrangements for communications services is also warranted. Options include a one-stop shop for consumers or, as discussed below

for financial services, an umbrella arrangement encompassing all individual dispute resolution services in this area.

Energy and water

In the case of the energy and water ombudsmen, consumer confusion is not relevant since consumers would be unlikely to contact an out-of-state ombudsman. But there are grounds for re-considering the provision of ADR services in these services on other grounds:

- Relative cost efficiencies vary significantly, with the highest cost scheme being around eight times more expensive per consumer contact than the least. An important reason is that the smaller schemes have a limited capacity to spread their fixed costs over many complaints. For example, the smallest, the Tasmanian Energy Ombudsman, had only around one contact per day with consumers in 2005-06, about 2 per cent of the contacts made in Victoria. This is an example of when the apparent low cost advantage of an ombudsman scheme does not compare well even with courts.
- There are concerns about the inconsistencies in the treatment of consumers and businesses across different jurisdictions (AGL Energy, sub. DR149, p. 3; Origin Energy, sub. DR158, p. 3). For example, processes for handling complaints and reporting vary (though some aspects have been harmonised ANZEWON, sub. DR254, p. 2).
- Rationalisation would allow the development of greater expertise within a larger body on complex issues, enable better benchmarking of the consumer performance of suppliers across jurisdictions, and provide greater capacity to feed regulators advice about systemic issues.

However, some parties regarded their local ombudsman as effective (Synergy, sub. DR155, p. 5) and argued that national consolidation might undermine effective local representation and liaison.³ That said, other national ADR schemes (such as the TISSC and the TIO) appear to be effective, despite the absence of local offices, perhaps reflecting their other advantages. Any ADR process has to deal effectively with a wide variety of complaints and to be sensitive to the characteristics of complainants (such as disadvantaged consumers, migrants, the young, those in remote areas and so on). A consumer's jurisdictional location is just one of these characteristics. It is not clear that it should be so decisive in determining the institutional form of ADR services.

³ For example, the Energy Industry Ombudsman South Australia (sub. DR133, p. 2); Financial Counsellor's Association of Queensland (sub. DR134, pp. 1-2); Kildonan Uniting Care (sub. DR206, p. 7); and the South Australian Minister for Consumer Affairs (sub. DR219, p. 14).

Overall, the Commission considers that a national ADR scheme for energy will be beneficial in the long-run. The most important obstacle to an immediate shift to a national energy ombudsman (as advocated in the Commission's draft report) is that Australia has not yet moved to a nationally consistent consumer policy framework for energy (chapter 5 and appendix F). Nor are energy markets all equally contestable (National Consumers' Roundtable, sub. DR199, p. 4 and WACOSS, sub. DR243, p. 10). Two jurisdictions, Western Australia and the Northern Territory, are not members of the national energy market.

Consumer issues concerning water supply share some similarities with energy (such as billing complaints), and in some instances ADR bodies deal with complaints relating to both industries. However, there is a much more State and Territory variation in the extent of regulatory and market reforms in water supply, and significant differences in the characteristics of demand and supply across jurisdictions (ANZEWON, sub. DR187, p. 5). The ownership arrangements for water are also much more complex. For instance, in Victoria there are 22 responsible statutory authorities and in each of NSW and Queensland there are more than 100 local government bodies (National Consumers' Roundtable, sub. DR199, p. 10). These features of the water market suggest that the creation of a national water ombudsman — whether as part of a combined energy and water ombudsman or as a separate entity — is realistically further off than energy.

These practicalities suggest that dispute resolution in energy and water will have to remain local for some time, though national consolidation is likely to be beneficial when markets are better integrated and regulations more closely aligned. The immediate prospects for a national ombudsman are greater for energy than for water, though one consideration in creating such a body is its impact on the viability of stand-alone water ombudsman schemes in each State and Territory (Essential Services Consumer Council, sub. DR204, p. 4). In the period before national consolidation, State and Territory Governments should review the processes of their utility ombudsman's offices to ensure they are nationally consistent, and some jurisdictions could seek to combine their energy ADR arrangements on a bilateral basis.

Financial services ombudsmen

There is already significant cooperation between, and some impending consolidation of, the existing financial service ombudsmen. For example, several of the financial services ombudsmen participate in jointly sponsored seminar and educational programs (Credit Ombudsman Service Limited [COSL], sub. 53, p. 6). All of the ombudsmen use the Financial Ombudsman Service as a central toll free telephone contact point for consumers. The three largest schemes currently share IT

systems and corporate services, and will merge into a single entity by 1 July 2008 (FICS 2007).

The question is whether there is the scope for further convergence (as raised by Pearce 2007) by simplifying processes, creating a single body, or by exploiting synergies between the various schemes. Some of the heads of the existing schemes have apparently ‘stated quite candidly that we now have too many schemes’ (Pearce 2007). The three biggest schemes floated the option of:

... having a single name and point of entry for consumers but at the same time retaining expertise in the various and distinct areas within the wider financial services industry. (BFSO et al. sub. 89, p. 17).

This was the approach taken in the UK, which merged several predecessor schemes into the Financial Services Ombudsman, but with the intention to ‘retain the expertise from the prior sectoral schemes’ (Rickett and Telfer 2003). Such convergence has several possible advantages. It could:

- bring greater sophistication in infrastructure, complaint management, better learning, and the capacity to identify systemic issues — which are more difficult to achieve in some schemes. For example, concerns about these matters permeated the review of COSL (Khoury and Russell 2006);
- allow specialisation in dispute resolution by product rather than by the financial provider. For example, complaints about mortgages issued by credit unions, building societies and banks could be dealt with using a single process and with the advantage of specialised expertise in this area;
- lead to greater coherence in processes among the schemes, including adoption of best practice, for example, in setting ceilings on the value of transactions subject to ADR;
- make it easier to inform members about the pathways that consumers should use to access ADR. Reviews of the Credit Union Dispute Resolution Centre and COSL identified considerable concern over such referral processes (Khoury and Russell 2005, p. 15 and 2006, p. 13);
- further address concerns about ongoing consumer confusion, notwithstanding the important role of the Financial Services Ombudsman as a gateway service. While evidence is hard to gather, there was a concern by several parties about the potential for consumer confusion associated with multiple schemes (BFSO et al. sub. 89, p. 17; ASIC, sub. 103, p. 53; and the Finance Sector Union, sub. DR157, p. 1). An independent review of COSL found evidence of confusion for its consumers (Khoury and Russell 2006, p. 10). However, COSL (sub. DR148, pp. 7-8) and the Financial Cooperative Dispute Resolution Scheme

(sub. DR154, p. 3) questioned the extent of any confusion relating to the fragmented nature of the schemes; and

- produce some efficiency benefits from sharing overheads or from economies of scale and scope. The size of these gains is conjectural, as exploratory analysis found that cost differences per new contact do not appear to be scale-related. Nevertheless, three schemes have clearly perceived gains from integration and can provide lessons for other schemes about these gains.

The extent of these benefits should not be overstated. For example, the biggest risk of consumer confusion and poor service is associated with coverage of the schemes, not from their fragmentation. In this context, it is notable that consumers make twice as many complaints to COSL about non-members than members (COSL 2006, p. 13). (In chapter 5, the Commission has recommended that all credit providers be required to belong to an approved ADR scheme, which should address this issue.)

There can also be offsetting disadvantages associated with some forms of convergence (as explored particularly by COSL, sub. DR148 and by the Association of Superannuation Funds of Australia, sub. DR188). Full consolidation into a scheme like the UK model is one option, but may lack the flexibility of present arrangements. There are marked differences in the types of complaints dealt with — for example, insurance or superannuation claims compared with credit issues. As well, the different nature of member businesses covered by the different ADRs (some dominated by small businesses and others by big business) may raise difficulties for fee-setting arrangements for members (Khoury and Russell 2006, p. 42). And any model of convergence should not undermine the need for expertise in the very different areas covered by the financial services ADR schemes (COSL, sub. 53, p. 7), or for the capacity for unique innovative approaches.

In light of these competing considerations, the Commission, on balance, considers that the mandated introduction of a single scheme, like the UK Financial Services Ombudsman, is not warranted at this stage.

However, ahead of any formal consolidation, a more loose-knit ‘umbrella’ arrangement is likely to be beneficial — as mooted in the draft report. This could be achieved by affiliating the existing separate entities into a federation — with common telephone, website, mail and email consumer contact details — allowing a single referral and complaint pathway for consumers and suppliers. This would extend the role of the existing gateway service, the Financial Ombudsman Service, and would not represent a radical organisational step entailing complex internal bureaucracies. This model could also facilitate greater organisational rationalisation in the future if this provided a better dispute resolution service to consumers or

realised economies of scale or scope. (And, as noted by the Australian Bankers' Association (sub. DR245, p. 20), the merger between the BFSO, FICS and the IOS may well provide valuable experience relevant to any future formal consolidation.)

Such an organisational structure would not require a 'one fits all' service (contrary to the perceptions of the Finance Brokers' Association, sub. DR177; the Mortgage and Finance Association of Australia, sub. DR119; and COSL, sub. DR148). Schemes could still maintain their independence as arms within the umbrella organisation so as to maintain some of the flexible features of the current arrangements. For example, the Superannuation Complaints Tribunal could maintain its existing unbounded financial limits to compensation. Such a scheme could also readily incorporate any new financial ombudsman — it would be undesirable to see an even greater proliferation of ADR services in this area. And an umbrella scheme would provide an opportunity for its members to set up a formal process to consider ways in which they could reap any further synergies between each other on a consensual basis.

The Commission further considers that regardless of the organisational changes to financial ADR schemes, the processes used for setting limits on monetary compensation should be reformed. There are three elements to such reform.

First, ombudsmen should update the ceilings on the value of transactions subject to ADR in a timely and coordinated way, rather than in the staggered way experienced in the past. For example, the BFSO increased its limit from \$150 000 to \$280 000 in December 2004, while FICS will be putting in place a similar increase for insurance products in mid 2008. Excessively staggered and untimely changes may undermine the adequacy of dispute resolution (ASIC, sub. 103, p. 53 and COSL, sub. 53, p. 5), particularly for consumers experiencing greater risks.

Second, the ceilings set for any particular scheme should reflect the underlying distribution of risks of detriment facing consumers for the relevant financial services (which means that ceilings do not necessarily have to be equal across schemes). A practical issue in setting thresholds based on this principle is that some scheme members may find difficulties in arranging sufficient personal liability insurance to cover their full risks. Reasonable notice of threshold changes should help in most cases. But just as safety standards are not waived for those facing a high cost in meeting them, ongoing difficulties in securing insurance should not be a basis for setting a lower standard of consumer protection. Rather, the appropriate responses are better supply-side risk management and rationalisation of any excessively risky suppliers.

Finally, a further practical initiative would be to allow a consumer with a claim exceeding any given threshold to waive the excess and have their claim met up to the limit (ASIC, sub. DR174, p. 15). This already applies in COSL.

Australian Governments should improve the effectiveness of alternative dispute resolution (ADR) arrangements for consumers by:

- *extending the functions of the Telecommunications Industry Ombudsman to pay TV and reviewing options for further consolidation, including through a single consumer entry point for communication services complaints, or an umbrella arrangement (similar to that proposed below for financial services) encompassing all individual dispute resolution services in this area;*
- *reducing the inconsistencies in the complaint-handling and reporting processes used by energy ombudsman and assessing the scope for some jurisdictions to immediately combine their energy ombudsman offices on a bilateral basis, prior to the ultimate formation of a national energy ombudsman;*
- *further enhancing financial ADR services through:*
 - *integration of the existing bodies into a single umbrella scheme to provide one referral and complaint pathway, while allowing independent governance of its subsidiary schemes;*
 - *the requirement that any new industry ADR services, including for credit, be accessed through the gateway service, the Financial Ombudsman Service;*
 - *timely and coordinated revision of ceilings on the value of transactions subject to ADR, with ceilings differentiated according to the relative risks of consumer detriment for the relevant classes of products; and*
 - *allowing a consumer with a claim exceeding any given ceiling to waive the excess and have their claim met up to the limit;*
- *ensuring there are effective, properly resourced, government-funded ADR mechanisms to deal consistently with all consumer complaints not covered by industry-based ombudsmen; and*
- *establishing a formal cooperative mechanism between the various regulators, ADR schemes and other stakeholders to re-assess every five years the nature and structure of ADR arrangements to achieve best practice and address redundancies or new needs.*

9.5 Court action

Effective judicial redress is both a complement and substitute for ADR schemes. It is complementary because the threat of it provides businesses with incentives to participate positively in ADR and it provides consumers with an avenue for redress if ADR fails. It is a substitute because consumers always have the capacity to take up a matter directly in a court without taking it to ADR at all and because regulators may want to establish a clear legal precedent⁴ or publicly punish a business that has broken consumer laws.

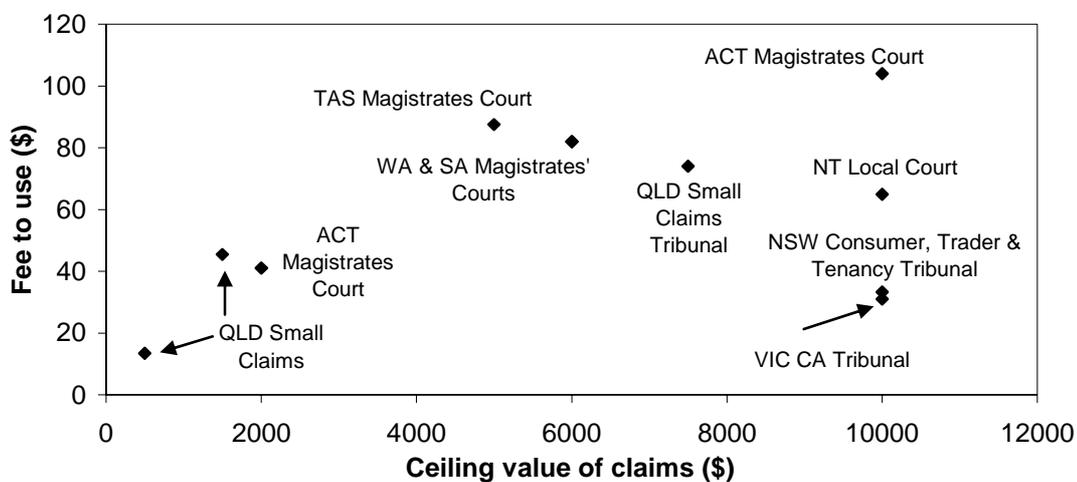
Accessible and cost-effective resolution of smaller claims

As in ADR schemes, the judicial system must deal with the full continuum of case complexity and consumer detriment. This means that it has to be appropriately layered, with access to its lowest levels facilitated by arbitration, high efficiency to maintain low access charges for parties, and less legal formality. Each Australian jurisdiction has a group of bodies that give effect to these goals, with tribunals or small claims divisions of magistrates' courts offering low cost, more informal options compared with higher courts (figure 9.1). These courts and tribunals do not generally utilise legal representation by parties, avoid jury trials, are not bound by the rules of evidence and usually do not award costs (vexatious claims aside).

Nevertheless, despite these similarities, there are variations in the processes and requirements for resolving small claims across jurisdictions. One important difference is that the ceilings for minor claims vary significantly across jurisdictions. This means that a consumer problem that might be heard with informal proceedings and low application fees in a small claims setting in one jurisdiction has to be heard with proceedings that are more formal and costly in another jurisdiction. For example, small claim limits are \$10 000 in Victoria and the Northern Territory, \$7500 in Queensland, \$6000 in Western Australia and South Australia, and \$5000 in Tasmania. These differences appear to be accidents of history, rather than decisions of considered design. Further, the values of some commonly purchased consumer goods now exceed even the higher ceilings. Court access fees also vary.

⁴ Some claim that a weakness of ADR generally is that resolved cases do not establish precedent. However, even in courts, only about 5 per cent of cases reach a judicial verdict with the rest settled (Cannon 2002). Also ASIC (sub. 103, p. 40) cited the influential value of quasi-jurisprudence from the cases decided by the BFSO.

Figure 9.1 **How much does it cost to seek judicial redress for a consumer claim under \$10 000**



Note. Queensland tribunals have tiered fees for different sized claims, which is why they appear three times in the chart.

Data sources: Compiled from the fees and ceilings described in the various Australian courts and tribunals (from <http://www.aija.org.au/links.htm>).

However, there are fewer grounds for such fees to be harmonised given that the costs of different courts may vary across jurisdictions. That said, there is no sound rationale for the inconsistent application of court fee waivers such as for disadvantaged consumers.⁵

Another variation between States and Territories is the use of tribunals for resolving consumer disputes. Tribunals have the advantage that they are more informal and tend to set lower fees for applicants than courts. Some participants considered that tribunals are superior on these grounds, and suggested their creation in jurisdictions where they are absent. However, the variations are not great for most disputes and, in the Commission's view, do not warrant changes in court arrangements in the States and Territories. (In Western Australia's case, re-creating tribunals would represent a reversal of a process of consolidating courts and tribunals that was only completed in 2005.)

Another across-the-board procedural reform would be to provide consumers with an option to make written submissions to tribunals and small claims courts (as in ADR schemes), instead of requiring oral testimony from the disputing parties at hearings

⁵ Telstra (sub. DR156, p. 14) was concerned to clarify the circumstances where waivers would be available. The Commission suggests criteria that already exist in some courts. For example, regulation 8 of the Federal Magistrates Court Regulations 2000 specifies clearly the criteria for a fee waiver (http://www.fmc.gov.au/html/fees_general.html).

(Australian Retailers Association, sub. 71, p. 12 and the Real Estate Institute of Australia, sub. DR172, p. 11).

This (and the wider use of oral testimony by telephone or video-conference) could lower the transaction and other less direct costs for disputing parties, especially when they are some distance from the court (as in remote cases or Internet-based disputes), are running a small business, or have many national outlets. Coles, for example, supported the capacity for written submissions (sub. DR146, p. 2). Allowing written submissions may be less intimidating for consumers and facilitate speedier resolution of disputes. And it would lower the costs for legal aid agencies of effectively representing some disadvantaged consumers, since the only requirement would be preparation of written material on behalf of their clients. Such agencies would, however, need the resources to prepare such submissions (Legal Aid Queensland, sub. DR202), an issue considered later.

Written submissions are already employed in the United Kingdom. The small claims track of UK county courts allows applicants to seek to have the matter heard without their presence (Her Majesty's Court Service 2007). Moreover, in these courts judges can, on their own reading of the submissions, make a decision without having a hearing. The European Commission has implemented a small claims procedure for cross-border consumer disputes that only uses written submissions (EC 2006a). And some Australian jurisdictions already accept written submissions, though usually this requires prior approval from the Court and is at the discretion of the magistrate.

A potential disadvantage of written submissions is that they may preclude examination of parties by the presiding tribunal member or judge, which may be seen as reducing the rights of parties. The disadvantage could be overcome by:

- giving disputing parties the continued right to have an oral hearing (in person or remotely) if either wishes to exercise it; or
- allowing a Tribunal or Court to decide whether they wished to hear oral testimony, based on the case before them and any request by a party (The Foundation for Effective Markets and Governance, sub. DR122, p. 4).

The second approach would constitute a more radical step, since it would probably make written submissions the default, rather than, as the Commission intended, an option that parties may wish to exercise. Several participants emphasised the need for an ongoing capacity for parties to make oral submissions, for example, as a response to a written submission or because, in some cases, it may be cheaper or quicker (Telstra, sub. DR156, pp. 14-15; Redfern Legal Centre, sub. DR151, p. 8; and NSW Government, sub. DR251, pp. 17-19).

Accordingly, the Commission prefers a system that gives parties a choice about their form of representation. Buttressing written submissions with the wider use of oral testimony by video-conferencing or telephone (Australian Finance Conference, sub. DR216, p. 10) would further expand effective choice in this area.⁶ The capacity for more flexible forms of testimony may be progressed by the Standing Committee of Attorneys-General (South Australian Minister for Consumer Affairs, sub. DR219, p. 14).

RECOMMENDATION 9.3

Australian Governments should improve small claims court and tribunal processes by:

- *introducing greater consistency in key aspects of those processes across jurisdictions, including:*
 - *common higher ceilings for claims;*
 - *common criteria for fee waivers for disadvantaged consumers; and*
- *allowing small claims courts and tribunals to make judgments about civil disputes based on more flexible forms of testimony, including written submissions and video-conferencing, unless either of the disputing parties requests otherwise.*

9.6 Consumer representation

Collective court actions by consumers

By their nature, some contraventions of consumer law, especially misleading or deceptive claims, have detrimental effects on many consumers. The losses faced by each consumer would not generally be sufficient to justify the costs of an individual civil action. In any case, such actions would often be inefficient given that court resources would be spent on repetition of the same issue.

Private collective action is an insufficient remedy

A key question then is whether there are sufficient means for consumers to take collective civil actions through class and representative proceedings without the assistance of a regulator. Private collective actions may be pursued through:

⁶ Some Australian tribunals already encourage oral testimony by video-conference and telephone (Barker 2005).

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- the various rules of court in all of the Supreme Courts of Australia, which allow a person to take a representative action on behalf of a group who share the ‘same interest’ in the proceedings;
 - the Consumer Credit Code for matters covered by that code; and
 - the statutory provisions in the *Federal Court Act of Australia 1976 (FCAA)* generally and using the nearly identical provisions recently available in the *Supreme Court Act 1986 Victoria (SCAV)* for actions in Victoria alone.

However, while there are multiple methods for collective private action, the existing provisions cannot be applied in many circumstances. The ‘same interest’ test has proved a forbidding one for a range of reasons (Charles 2004). And the Consumer Credit Code can only be applied to consumer problems involving credit.

Moreover, while, the FCAA and parallel Victorian arrangements are regarded as being more wide-ranging and favourable to plaintiffs (Charles 2004), the empirical evidence suggests relatively modest use of these statutory provisions (Black 2005). Most collective actions have focused on product liability and, more recently, shareholder interests, rather than the full range of conduct covered by the TPA.

A litany of procedural, cost and other barriers explain why the statutory provisions have not been widely used (Murphy and Cameron 2006, Morabito 2007 and Choice, sub. 88, p. 64). This has not only affected private parties, but as discussed later, also the ACCC. The most recent emerging issue is obstacles to third-party financing of private class actions. Such financing is an important way in which consumers can afford to take class actions. There is controversy over whether a class action can or should be restricted to a group of consumers who sign up to a financing agreement. A recent appeal to the full bench of the Federal Court suggests that the jurisprudence is tilting towards a more permissive attitude to such financing.⁷ The Victorian Law Reform Commission (VLRC) has considered this matter as part of a broad inquiry into civil justice and has mooted a range of measures, including a Justice Fund (financed from damages from privately funded cases) to help finance meritorious class actions.

The VLRC inquiry and the emerging jurisprudence in this area raise complex issues about the right approaches to ensure efficient and equitable access to civil class

⁷ Federal Court judgments have reached different conclusions about the capacity for effective third-party financing under the existing FCAA. The first, *Dorajay (2005) 147 FCR 394*, reduced the scope for successful third-party financing of private class actions under the statutory provisions (Davidson et al. 2006 and Morabito 2007). However, the second, *P Dawson Nominees Pty Ltd v Multiplex Limited [2007] FCA 1061* opens the door to such financing and has subsequently been endorsed at an appeal hearing by the full bench of the Federal Court (*Multiplex Funds Management Limited v P Dawson Nominees Pty Limited [2007] FCAFC 200*).

actions. Any approach will have to deliver an appropriate balance between an effective capacity for private class actions (Law Council of Australia, sub. DR227, p. 4) and the problems that might ensue from excessive litigation (Telstra, sub. DR156, p. 15) or high legal costs (Suncorp, sub. DR171, p. 7). These are highly technical legal questions, which lie outside the Commission's expertise. They may be better considered by the Standing Committee of Attorneys-General (South Australian Minister for Consumer Affairs, sub. DR219, p. 14) or some other legal authority.

RECOMMENDATION 9.4

In the light of the Victorian Law Reform Commission's Civil Justice inquiry and recent decisions by the Federal Court of Australia regarding third-party financing of private class actions, Australian Governments should assess the desirability of clarification (or amendment) of the relevant legislation and the use of other policy approaches to facilitate appropriate private class action, taking into account any risks of excessive litigation or other unintended effects.

Representative action by the regulator is desirable, but has been stymied

Even with arrangements in place that enable appropriate private litigation, there are strong grounds for regulators also to be able to act on behalf of consumers. This recognises that:

- the motivation for individuals to join a civil class action can be low if the individual stakes are small, even if the aggregate costs are large;
- collective private actions are based on the private benefits to those involved, yet public policy is also interested in broader benefits that may not always be equivalent to those private benefits. Such divergence in public and private interests can arise in several contexts, such as when a group of consumers suffering detriment is outside the class action. This can particularly affect disadvantaged consumers who are less likely to contribute to 'fighting funds' or become aware of private class actions;
- such a representative action may be a more efficient way of proceeding to the extent that it reduces the potentially excessive transaction costs of organising a private class action and any third-party financed arrangements; and
- representative actions that are restricted to the regulator alone under generic consumer law could be less constrained than actions available to all parties under the FCAA and SCAV. This is because the risks of vexatious claims — a persistent concern with widening the scope of private actions under the FCAA/SCAV — are likely to be lower.

Moreover, if civil pecuniary penalties (chapter 10) are not implemented for all aspects of the generic consumer law, such actions will also have a desirable enforcement role by providing an additional disincentive to business misconduct that causes significant collective consumer losses.

However, the capacity for representative actions by consumer regulators is currently circumscribed (box 9.2). One option has been recently closed after a court decision. The other two mechanisms suffer significant limitations.

The drawbacks of present arrangements have meant that:

- the ACCC has generally been deterred from taking representative actions (sub. 80, pp. 100ff);
- in just one case of alleged business misconduct, the inability to mount a case may have deprived 100 000 to 300 000 consumers of redress totalling millions of dollars (ACCC, sub. 80, p. 101); and
- where the provision has been used, only consumers giving consent have received any restitution in representative actions, despite a likelihood that un-named consumers were also affected (Samuel 2006).

As recommended by the ACCC and many other participants in this inquiry,⁸ a remedy for these problems would be to remove the current stipulation in the TPA/FTAs that consumers must give consent to be part of a representative action. This would allow consumer regulators to take representative actions using the generic consumer law on behalf of affected consumers who are not parties to the proceedings.

Some telecommunications businesses were opposed to change in this area, arguing that existing approaches are adequate (Telstra, sub. DR156, p. 15; Communications Alliance, sub. DR185 pp. 4-5; AMTA, sub. DR175 p. 4; and Optus, sub. DR173, p. 7), but did not indicate the particular risks that would realistically be entailed by a new provision. It is notable that consumer regulators in several other countries (the United States, New Zealand and Canada) already have this power, without evident problems. Such a capacity would still be subject to judicial oversight and could therefore not be readily abused by the regulator.

⁸ For example, ACCC (sub. 80, pp. 100–102); ASIC (sub. 103, p. 63 and sub. DR174, p. 18); Choice (sub. 88, p. 71 and sub. DR194, p. 3); Dr Nottage (sub. 61, p. 6 and sub. DR114); Ms Nagarajan (sub. 48, p. 9) and Financial Counsellors Association of Queensland (sub. DR134, p. 2).

Box 9.2 **Obstacles to representative action by consumer regulators**

Following *Medibank Private Ltd v Cassidy* [2002] FCAFC 290, the capacity of the ACCC to undertake representative actions exclusively using s. 80 of the TPA has been removed. In the wake of this decision, the ACCC must now choose between the flawed remaining provision in the TPA (s. 87(1B)) and Part IVA of the *Federal Court Act of Australia 1976* (FCAA) (the same act used for private actions).

Under s. 87(1B), the ACCC must obtain the written consent of each consumer and the claims of each consumer must be pleaded and proved separately. These conditions make actions under the TPA protracted and costly, even for a modest number of consumers. (While the statutes are different, similar problems beset the use of representative actions by ASIC and most state and territory consumer regulators. For example, see ASIC (sub. 103, p. 64). CAV has scope to bring representative actions under s. 105 (3b) of the Victorian FTA without the consent of all parties, but this involves other pragmatic difficulties.)

The conditions for action under the FCAA appear less onerous than under the TPA. There only needs to be at least seven people, including the ACCC, who have a claim against the same person in 'similar circumstances' and the action can be pursued without the consent of each represented person. However, there are several elements of the FCAA that have frustrated its practical application, and so far the ACCC has only ever used the provision three times, failing twice (ACCC, sub. 80, pp. 100ff and personal communication from the ACCC, 18 July 2007):

- First, action is costly and time-consuming with complex and lengthy pleadings and the need for close judicial consideration of all of the group and individual issues raised by the representative action. Justice Finkelstein observed the capacity for deliberately delaying tactics by respondents in such actions in the FCAA generally (Murphy and Cameron 2006).
- Second, there can be potential conflicts of interest between parties, as was the case in the Giraffe World pyramid selling case, since some pyramid participants had made money and others expected to.
- Third, the ACCC loses control over the settlement process. Any settlement must be approved by the court and all members of the action must be given notice of the settlement, with the court deciding whether any settlement is then fair in all the circumstances.

Sources: Bhojani (2001); *Medibank Private Ltd v Cassidy* (2002); High Court (High Court: M176/2002, 20 June 2003); *ACCC v Giraffe World Australia Pty Ltd (No 2)* [1999] FCA 1161.

Given its benefits and low risks, the Commission agrees that an enhanced provision for representative action is warranted in the generic consumer law. Redress need not necessarily be in the form of damages, but could involve a refund or an enforceable promise to honour the representations that were made (ACCC, sub. 80, p. 104).

Australian Governments should ensure a provision is incorporated in the new national generic consumer law that allows consumer regulators to take representative actions on behalf of consumers, whether or not they are parties to the proceedings.

One remaining issue is whether there should be any provision for consumers to ‘opt-out’ of a regulator’s representative action so as not to prejudice their scope to mount private actions. While an opt-out provision would have some value, it could also involve delay in mounting any representative action as the regulator would need to advertise or otherwise make clear to the relevant consumer group that a representative action was pending. Its merits should be considered when determining the details of the new representative action legislation.

Should there be a super-complaints mechanism?

Some participants raised the option of requiring regulators to give privileged attention to complaints made by designated consumer advocacy bodies — a ‘super complaint’ mechanism, as used in the UK from 2002.⁹

Under the UK provision, a designated consumer body notifies the UK Office of Fair Trading and other relevant regulators about a consumer problem. The super-complainant is required to set out its reasons why the problem is significantly harming consumers’ interests. The regulator must then publish a reasoned response within 90 days. There are eight designated consumer groups at present (including the Consumers Association and the National Consumer Council).

There were several claims about the benefits of introducing a similar super-complaints mechanism in Australia, such as alerting regulatory agencies to systemic issues. For instance, Ms Nagarajan observed that the UK arrangement led to various initiatives for dealing with systemic consumer problems concerning dentists (sub. 48, p. 13), while Mr Asher (chief executive of Energywatch UK) considered that such a mechanism put the ‘content’ into empowerment by giving the community the capacity to:

... identify priorities and problems and make sure that they’re followed through. (2006, p. 2)

⁹ For example, Choice (sub. 88, p. 7); Ms Nagarajan (sub. 48, p. 13); MCCA Working Party on Consumer Policy (sub. 75, pp. 109–110); Spier (sub. 19, p. 10).

The key question on which the desirability of a super-complaint mechanism turns is the adequacy of existing intelligence about, and prioritisation of, consumer problems. It is not clear that there are material shortcomings in these aspects of complaint handling in the current Australian system:

- It is not evident that regulators are ignorant of the important systemic issues. Regulators receive advice about systemic issues in many ‘hotspot’ areas from a multitude of ADR schemes. The thousands of complaints made to the various Australian regulators also serve as a basis for identifying key issues, though the databases could be improved (hence recommendation 9.1) to provide greater guidance about emerging systemic problems.
- There are formal institutional arrangements already in place to give consumers a voice in policy and regulatory processes, such as through ASIC’s Consumer Advisory Group and the ACCC’s Consumer Consultative Committee. In addition, the Commonwealth Consumer Affairs Advisory Council (CCAAC) provides independent advice on current and emerging consumer issues to the responsible Minister, who may then act on them. The Commission has recommended additional resourcing and other measures to increase CCAAC’s effectiveness (recommendation 6.2).
- Consumer advocacy groups, like other parties, obviously already have an independent capacity to point to particular problems and to influence the priorities of the regulators. The Victorian Government (sub. DR226, p. 77) noted that a ‘very important input into prioritisation is from key stakeholders’. There is no compelling evidence that their representations are downplayed. As observed by the NSW Office of Fair Trading:

The concept of the ‘super complaint’ institutionalises what is, in fact, a common practice in Australian fair trading/consumer protection agencies. (sub. 73, p. 39)
- The complementary role played by consumer groups in prioritisation and intelligence gathering would be strengthened by appropriate funding of research and advocacy, as recommended by the Commission (chapter 11).

Sometimes regulators will fail to formally investigate an issue raised by consumers (as cited in an example given by Choice, sub. DR194, p. 11), but that could reflect regulators’ prioritisation of issues, rather than institutional failure. Regulators must choose carefully where to spend their investigation resources among the large range of competing issues. If that process is working well, then mandating priority to investigation of complaints from a designated consumer group could use investigative resources that would otherwise have been better deployed elsewhere.

Choice (sub. DR194, p. 11) and the Victorian Government (sub. DR226, p. 77) contested this, arguing that super-complaints would be complementary to the

existing processes used by regulators to set priorities for their investigations. But there is a significant difference between responsiveness to stakeholders' views on important issues and a *requirement* to investigate them. If there were any divergence between the priorities identified by the regulator and those from a super-complainant then, given resource constraints, the regulator would be obliged to alter what it considered to be the most appropriate focus for its activities.

In sum, given the existence of a myriad of alternative mechanisms for empowering consumers and identifying systemic consumer problems, the benefits of a super-complaints mechanism are probably insufficient to outweigh its likely downsides. It is notable too that the New Zealand Ministry of Consumer Affairs (2006) has recently rejected the mechanism for that country.

Catering for disadvantaged consumers

Disadvantaged consumers have less capacity to seek redress independently. For example, people holding a concession card have a significantly lower propensity to get help from a dispute resolution body than those without such cards (IPSOS 2007, p. 18 and Treasury 1999, p. 12). They are also only half as likely as other consumers to use the Internet when searching for help, indicating the current limitations of this technology for providing information to this group (IPSOS 2007). More broadly, disadvantaged consumers often have lower incomes, poorer English proficiency, do not know their rights, and can be discouraged by overly formal redress mechanisms. This is despite the fact that the ethical basis for more accessible redress is strongest for such consumers. This raises the issue of the adequacy of current mechanisms to assist disadvantaged consumers to access redress.

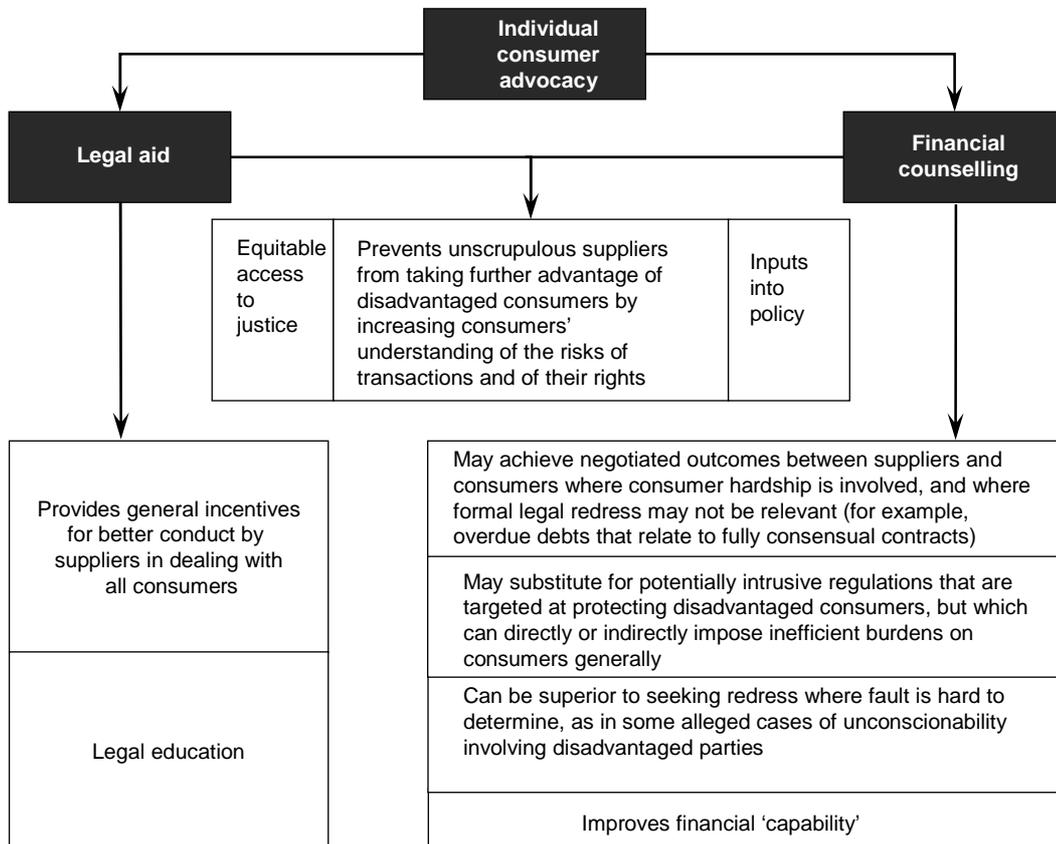
Some of the Commission's earlier proposals would help, such as consistent access to fee waivers where small claims are involved and more flexible forms of testimony for consumers seeking redress for such matters. Another key strategy is individual consumer advocacy through legal aid and financial counselling services.

Legal aid

Legal aid services provide legal representation/advice and help for self-advocacy for lower income and disadvantaged consumers, as well as general legal education. In addition to their prime role in improving access to redress by disadvantaged consumers (Martin 2006), such targeted services have other potential advantages, including for consumers generally (figure 9.2). For example, casework agencies that

deal with disadvantaged consumers have drawn ASIC's attention to unfair debt collection practices and regulatory gaps that affect all consumers (sub. 103, p. 71).

Figure 9.2 The roles of individual consumer advocacy



While ombudsman and ADR schemes provide significant support for non-judicial redress, there is relatively little assistance for legal aid in consumer disputes. Most jurisdictions provide some funding for help with consumer civil disputes as part of broader support for legal aid services. However, this is primarily through community legal centres, rather than state legal aid commissions, which, with funding changes a decade ago, now have little involvement in civil cases.¹⁰ Even community legal centres devote relatively few resources to consumer issues. For example, the National Association of Community Legal Centres indicated that consumer problems, including credit and debt, accounted for about 20 per cent of their total activities (NACLC 2005 p. 9). Total Australia-wide funding from all governments for the Community Legal Services Program is about \$40 million,

¹⁰ For example, Victoria Legal Aid (2006, p. 5) observed that there is little funding for civil matters generally, with spending dropping by around 95 per cent from 1996 to 2006 due to reduced Commonwealth funding. Legal Aid Tasmania (2006) has decided to accept no further state civil matters, and took on only 13 Commonwealth civil matters of any kind in 2005-06.

implying that funding across Australia for consumer matters through that program is likely to be modest.

There is a growing view that national resourcing of legal aid and financial counselling is inadequate. A recent broad review of legal aid and other individual advocacy services by the Legal and Constitutional References (Senate) Committee (2004) identified many deficiencies, including evidence of low resourcing for consumer civil matters. The review of NSW community legal centres found similar resourcing problems (Legal Aid Commission of NSW 2006a). The Chief Justice of Western Australia, the Hon. Wayne Martin (2006), recently claimed that the 'main problem with legal aid is, of course, the inadequacy of funding.' These concerns were reflected in submissions to this inquiry (such as the Victorian Aboriginal Legal Service, sub. 79 p. 2; and Kildonan Child and Family Services, sub. 65, p. 23).

Other inquiry participants pointed to interstate anomalies in government funding for individual consumer advocacy, with Queensland identified as having relatively limited resourcing in comparison with Victoria, NSW, Western Australia and the ACT (Centre for Credit and Consumer Law, sub. 93 p. 36; Legal Aid Queensland, sub. 51 p. 4). For example:

The consumer protection unit of Legal Aid Queensland consists of one effective full-time position, based in Brisbane, but servicing the whole state. And in our current research with financial counsellors in Queensland, they have told us that all services are over-stretched, that most who are working part-time are doing so because of a lack of funding, not a lack of demand, and that there are clear gaps in geographical coverage of financial counselling services. (Centre for Credit and Consumer Law, sub. 93, p. 36)

The Australian Government increased funding for legal aid in the 2007-08 Federal Budget, but this was directed at family law matters in non-urban areas and for criminal cases. The Queensland Government considered a national approach to funding of such services is needed (sub. 87, p. 60).

Financial counselling

The functions of financial counselling overlap with legal aid. Such counselling services aim to help consumers who are in financial stress to: manage their finances; communicate with their financial institution or other supplier; direct them to legal representation if required; provide them with support during the period of distress; and through education, to reduce the future risks of problems. There is only sparse and qualitative evidence about its effectiveness in Australia, but the available results

are positive.¹¹ For example, a survey of the experiences of consumers using counsellors found that:

For people who saw a financial counsellor, it was unanimously a positive empowering experience for them, albeit at a negative point in their life. In addition, the majority stated it had changed the way they viewed their finances and changed their financial behaviour. (ANZ and ACNeilson 2005a p. 17)

Kildonan Child and Family Services (sub. 65, p. 12) observed that it is difficult for people experiencing hardship to either self advocate or seek redress and therefore they turn to services such as financial counselling as the first step.

Yet despite the benefits they provide, financial counselling agencies, like legal aid services, are generally run on a small budget and appear increasingly under pressure from growing demands. In some jurisdictions there is no government funding at all. Even where funding is provided, there are strains on the system. For instance, in Victoria, around \$5 million was provided in 2006-07 for such counselling (Victorian Government, sub. DR226, p. 78). But one agency providing services in that State estimated that consumers must usually wait 8 weeks before receiving assistance, affecting the ability of counsellors to provide emergency relief (Eastern Access Community Health, sub. 56, p. 2). The Australian Financial Counselling and Credit Reform Association (sub. 62, p. 16) commented that government funding is 'patchy, insufficient and diminishing in real terms', while the number and complexity of cases is rising. This view was echoed by other providers of counselling services.¹²

The pressures have recently been exacerbated by growing indebtedness and financial distress in the community, which is associated with higher interest rates and lower credit availability (Australian Financial Counselling and Credit Reform Association, sub. DR205, pp. 4-5).

The Lismore and District Financial Counselling Service pointed out that these pressures not only affect clients and counsellors, but also other third party providers that rely on the availability of financial counselling:

A growing number of organizations rely on the availability of financial counselling as a key element in their client casework i.e. Probation and Parole, DOCS, the court and the lending institutions. (sub. 139, p. 2)

¹¹ There is some quantitative evidence for the United States. This shows that, outside bankruptcy proceedings, credit counselling tends to reduce default risk (Hirad and Zorn 2001; Ellihhausen et al. 2003).

¹² Such as the Financial Counsellor's Association of Queensland (sub. DR 134); Financial Counsellors of NSW (sub. DR138); and the Lismore and District Financial Counselling Service (sub. DR139).

In that regard, ASIC (sub. 103, p. 72) observed that frontline individual consumer advocacy agencies do not have sufficient resources to provide policy input and data on caseloads — a key requirement for effective policy development and for general consumer advocacy.

There are grounds for more funding

Adequate resourcing of individual consumer advocacy for disadvantaged consumers is needed to provide equitable access to judicial redress, reinforce incentives for suppliers to behave appropriately, and deal with hardship arising from some consumer transactions (figure 9.2). The available evidence suggests that existing funding does not adequately meet the needs of disadvantaged consumers.

There are, accordingly, sound reasons for greater government support of individual consumer advocacy. The details of that support — its quantum, the methods used to distribute funding, the nature of the services being funded, the respective funding roles of Australian governments and the potential role of co-funding from private sources — require further consideration. Several submissions provided specific suggestions (the Financial Counsellors Association of Queensland, sub. DR134, pp. 2-3; the Victorian Aboriginal Legal Service Co-operative Ltd, sub. DR238, p. 3; and the Australian Finance Conference, sub. DR216, p. 10). But the need for further work on these details does not in any way diminish the priority for more support.

RECOMMENDATION 9.6

Australian Governments should provide enhanced support for individual consumer advocacy through increased resourcing of legal aid and financial counselling services, especially for vulnerable and disadvantaged consumers.

10 Enforcement

Key Points

- While Australia's current enforcement framework is performing reasonably well in balancing the interests of consumers and businesses and containing the cost of enforcement activity to the community, there is scope to improve the effectiveness of the current arrangements. In particular:
 - regulators are limited in their capacity to employ a layered approach to enforcement that involves tailoring regulatory action to the severity of specific compliance breaches; and
 - regulatory performance reporting systems can be improved to deliver a higher level of regulatory accountability.
- Expanding the suite of tools available to enforce the generic consumer law would be a cost-effective means to achieve greater deterrence of inappropriate supplier conduct and better redress for consumers suffering detriment from breaches of the law. Specifically, the Commission supports the introduction of civil pecuniary penalties (including disgorgement of profits), banning orders and substantiation and infringement notices within the proposed new national generic consumer law. Inclusion of naming and shaming powers in that law should be a matter for further examination and consideration by the Australian and State and Territory Governments.
- Better collection, analysis and reporting of information about the nature of current enforcement problems, their consequences, and the impact of steps taken to address them, would improve the accountability of consumer regulators. Such information collection and analysis should be informed by input from stakeholder groups.

10.1 Introduction

Effective enforcement is a key element of a well-functioning consumer policy framework as compliance with laws designed to protect consumers will depend on the vigour (both actual and perceived) with which breaches are monitored and policed by regulators. Indeed, inadequate enforcement may create a perception that an otherwise appropriate regulatory tool is not working properly.

Importantly, the role of regulators in monitoring and enforcing compliance with consumer laws is supplemented by the scope (including under common law) for

consumers to pursue legal action on their own behalf and for businesses to protect their legitimate competitive interests (and thereby indirectly promote the interests of consumers). In fact, in certain areas such as misleading or deceptive conduct, private actions dominate court-based application of the generic consumer law.

As well as formal compliance mechanisms, informal channels such as education and awareness campaigns by regulators and the pressure brought to bear by media and consumer organisations can have a powerful impact on business behaviour. These formal and informal avenues are not entirely separate. On occasion, regulators use the media to encourage compliance with regulatory requirements. And a media spotlight on consumer law breaches can sometimes precipitate regulatory action.

In commenting on the operation of the current system, most inquiry participants considered the rights and obligations of consumers and suppliers are reasonably well balanced. However, there were various concerns about the adequacy of enforcement and the need for a proactive approach. For example, the Australian Finance Conference highlighted the consequences of regulatory inaction:

Too often in our experience, a new regulatory measure is enacted with expectation that whatever the mischief was, [it] has now been addressed. There is a lack of accountability on regulators to enforce, or at least engage in meaningful compliance programs. Lack of enforcement results in an anti-competitive outcome, with most businesses complying, but many do not in the knowledge that the risk of being found in breach is low. (sub. DR216, p. 11)

And Anglicare Tasmania focussed on the importance of a more proactive approach to enforcement to protect the particular interests of disadvantaged consumers:

No piece of legislation, set of guidelines or code of practice can be truly effective unless it is proactively enforced. Reactive enforcement depends on complaints being made, but, for a range of reasons, many disadvantaged people do not complain when their rights are disregarded. (sub. DR191, p. 8)

Moreover, a number of specific issues were raised that were perceived as limiting the effectiveness of the current enforcement regime. They included the scope and suitability of penalties, sanctions and other compliance mechanisms; the cost of applying those mechanisms; adequacy of resources devoted to monitoring and improving compliance; inconsistencies in the application of consumer protection law across jurisdictions; and the adequacy of coordination arrangements between regulators. More broadly, the extent to which better enforcement of generic regulation would obviate the need for some industry-specific regulation was also mentioned.

Against this background, this chapter examines options to improve the efficiency and cost-effectiveness of enforcement. These are canvassed in terms of the Commission’s proposals for developing a nationally coherent consumer policy framework.

10.2 Outline of the current enforcement landscape

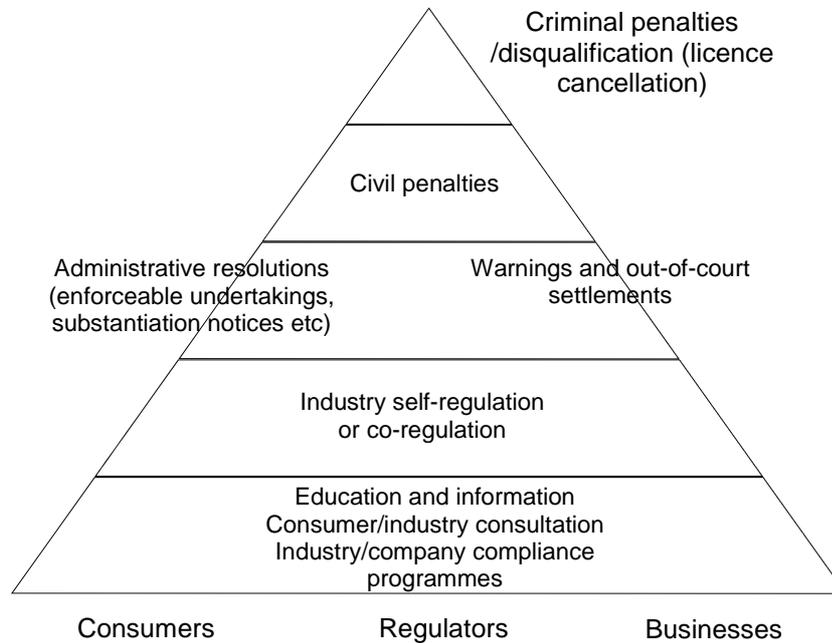
The diversity of Australia’s consumer policy laws (see chapter 2) is matched by more than 100 regulators charged with their enforcement. At the national level, the Australian Competition and Consumer Commission (ACCC) and the Australian Securities and Investments Commission (ASIC) are responsible for generic law enforcement, while sector-specific regimes in energy, therapeutic goods, telecommunications and food safety are policed by separate regulators. Fair Trading Authorities enforce equivalent generic laws at the State and Territory level, as well as some jurisdictional industry-specific regimes. Also, an array of independent regulators at the State and Territory level are responsible for licensing, registration, safety regulations and compliance with other standards. Formal and informal coordination arrangements attempt to minimise inconsistency and duplication across jurisdictions and activities.

Those regulators use a mix of criminal, civil, administrative and educative tools to deliver a set of enforcement outcomes to the community. As a group, these tools have been characterised as an ‘enforcement pyramid’, where compliance measures of increasing intensity and sanctions of escalating severity (and cost) are imposed on a hierarchy of potential or actual regulatory breaches (figure 10.1). Importantly, the balance between the different tools employed can vary significantly according to the particular focus of (and, as discussed later, resources available to) individual regulators (see table 10.1). For example, the Victorian Government highlighted the need for State and Territory regulators (in contrast to the ACCC) to concentrate on broader compliance measures given the large number of typically smaller firms that they deal with.

Generally, State and Territory consumer affairs agencies focus on encouraging business compliance rather than enforcement per se — although effective enforcement is necessary to ensure credibility as a regulator — and State and Territory consumer affairs agencies tend to undertake more consumer education, information and advice than does the Australian Competition and Consumer Commission. A wide range of tools are used by regulators, working with businesses and consumers, to achieve compliance with the law. (sub. DR226, pp. 79-80)

As well as cost considerations (see below), the choice of specific tools will depend in part on whether the specific regulatory objective is to:

Figure 10.1 **An enforcement pyramid for business compliance**



Data source: adapted from Robin Brown, sub. 63, p. 14.

- raise awareness among consumers and businesses of their rights and legal obligations;
- deter future contraventions of the law by potential offenders;
- punish parties engaging in serious or habitual contraventions;
- provide redress for loss or damage from prohibited conduct (see chapter 9); or
- stop prohibited conduct quickly to limit ongoing consumer detriment (MCCA 2005a).

Criminal sanctions aim to punish and deter the most culpable conduct by imposing fines or custodial sentences on offenders (although the latter are available for consumer law breaches in only one Australian jurisdiction). Importantly, injunctions and judgements for damages are not typical features of Australian criminal processes. In addition, safeguards such as rules that govern the gathering and admissibility of evidence, privilege against self-incrimination and a higher relative burden of proof required in criminal proceedings, add complexity and extend the duration of these processes. Accordingly, criminal remedies do not always

constitute an effective means of either stopping illegal conduct quickly or providing consumer redress.¹

Civil remedies (including injunctions, pecuniary penalties, confiscation orders, corrective advertising, restitution and other compensation orders) fill this gap to some extent as they offer a more flexible and responsive means of dealing with inappropriate conduct and the scope to compensate consumers for the financial and non-economic loss that results. However, as discussed in chapter 9, there are restrictions on the use of civil remedies in Australia (such as limits on representative actions) and the Commission has therefore recommended some changes to improve the opportunities for their application. Moreover, limits on the range of civil penalties currently available to regulators detract from their capacity to employ a layered enforcement approach and, correspondingly, to deter certain conduct (see below).

Administrative powers such as enforceable undertakings and substantiation notices give regulators the discretion to act without the need to seek court approval. As such, they provide more timely, flexible and less costly means of stopping conduct that may be in breach of the law. There has been an increasing reliance on these types of mechanisms in recent years (although the range of administrative powers currently available to regulators varies across jurisdictions). But for reasons discussed below, they will not be appropriate in many circumstances.

Information and education programs that can include publications specific to either consumers or businesses, outreach services, call centres and website portals are among the range of non-regulatory mechanisms used to encourage compliance with the law. In some respects, they can be considered a more proactive approach to achieving compliance than court-based enforcement.

The choice of instrument

In considering what mix of litigation, administrative tools and education programs will deliver the greatest net benefits for the community, regulators need to take account of the costs imposed by the enforcement system. As the ACCC noted:

In determining which compliance mechanisms should be used in each matter, the ACCC considers a range of issues including how to achieve compliance in the most cost effective way and achieving fast and effective results for consumers. For example, only a small percentage of investigations result in litigation. In many cases, the ACCC will accept a court enforceable undertaking ... because this can produce a quicker outcome that better meets the needs of consumers. (sub. 80, p. 26)

¹ Successful criminal actions require establishing guilt beyond reasonable doubt. In civil cases, on the other hand, a variable standard of proof at or above the balance of probabilities is employed (ALRC 2001).

To the extent that enforcement activity focuses on the small number of suppliers who break the law and does not affect the large number of legitimate traders, those costs may not be large in overall terms. But from the point of view of choosing the most cost-effective tool, it is important to consider both the immediate costs faced by the regulator and those that will arise if the safeguards against regulatory errors (such as appeal processes) are invoked. Such safeguards are particularly important adjuncts to administrative powers (especially if those powers provide scope for significant financial penalties to be imposed on suppliers). The implication is that caution is required in considering the range of breaches to which administrative powers should be applied.

In that context, the rights of defendants will best be served in many cases by independent judicial oversight and an escalating burden of proof placed on the prosecution regarding the seriousness of the offence. The desirability of providing such ‘insurance’ was acknowledged by the Real Estate Institute of Australia (REIA) as part of its support for a range of new administrative penalty provisions:

In order to ensure that the standard of proof remains high however, the REIA suggests that those prosecuted should retain an ability to appeal penalties to the courts, at the risk of greater penalties being applied. There should also be penalties for consumers found to be making frivolous complaints which result in unnecessary costs for affected businesses. (sub. DR172, p. 14)

Lynden Griggs (a legal academic) also highlighted the role of the courts in minimising the risks associated with introducing new enforcement tools such as civil pecuniary penalties:

[civil penalties] could only serve to increase the remedial smorgasboard, and given the confidence and integrity within the Australian judicial system, additional options available to the decision makers arguably serve no harm. (sub. 8, p. 11)

And while judicial processes are more costly than administrative options, they offer a much greater potential deterrent effect.

A further important consideration is the level of resources that should be devoted to education and information programs designed to prevent the emergence of future compliance breaches that would otherwise potentially require more costly court-based intervention. As noted above, such measures are likely to be more suited to educating and modifying the behaviour of smaller regionally-based enterprises (including unincorporated firms and sole traders) compared to nationally-focused businesses with the resources to be more cognisant of their legal responsibilities.

However, in keeping with the thrust of most submissions to this inquiry, the focus of the remainder of this chapter is on enforcement mechanisms rather than broader compliance measures, and in particular whether the current range of enforcement tools

should be augmented. Indeed, as alluded to above, without the backup of an effective enforcement toolkit, education and information programs are likely to be less effective.

10.3 Suitability of current enforcement powers

As noted above and elaborated on in box 10.1, the TPA and the Fair Trading Acts provide a range of specific enforcement tools for regulators to deter, punish and provide recompense to consumers for illegal conduct. However, some tools are not currently available to all regulators. This can restrict their ability to adopt a layered approach to enforcement whereby regulatory responses are tailored to the severity of particular legal breaches.

In turn, such differences mean that suppliers can face different incentives to comply with the law depending on where they reside and the activities or conduct they engage in. Accordingly, some undesirable practices may not be sufficiently dealt with in a cost-effective manner and consumers will not be afforded sufficient or consistent protection from those practices.

A number of participants considered that this is a key deficiency in Australia's enforcement framework. In calling for an urgent expansion of the broader consumer policy toolkit, Choice, for example, said:

... a package of reforms to key consumer legislation is needed to give regulatory agencies greater flexibility and more cost-effective enforcement and consumer redress powers. (sub. 88, p. 56)

Others focused specifically on the need for uniformity of enforcement powers across jurisdictions. Hank Spier said in this regard:

It is essential that all agencies have the same powers. The Commonwealth has lagged in recent times due to a perceived reluctance for the Commonwealth Parliament to give agencies such as ACCC or ASIC too much power and powers that effectively involve a reversal of onus. (sub. 19, p. 6)

In illustrating these comments, a number of inconsistencies in the enforcement powers available to regulators in different jurisdictions were specifically brought to the Commission's attention. Particular concerns related to the absence generally, or in some jurisdictions, of provision for:

- civil pecuniary penalties including disgorgement orders;
- banning orders that prevent individuals from engaging in certain conduct either permanently or for a set period;
- substantiation notices requiring evidence or proof about the basis of a claim or representation;

Box 10.1 Remedies currently available under the TPA and FTAs

Criminal sanctions

Under the TPA and the equivalent provisions of the State and Territory fair trading laws, criminal sanctions only apply to specific conduct involving false or misleading representations; bait advertising; harassment or coercion; referral selling; and falsely offering prizes. While convictions can be recorded, individuals cannot be imprisoned (except in NSW). Financial penalties are capped at \$0.22 million for individuals and \$1.1 million for corporations under the TPA, though these are high by international standards. In addition, orders for adverse publicity, probation, community service and corrective advertising can be sought (following a court imposed penalty).

Criminal sanctions do not apply to breaches of the general misleading or deceptive conduct provisions (Section 52), except in Tasmania; unconscionable conduct; prescribed codes of practice; implied conditions and warranties; or certain actions against manufacturers or importers.

Civil remedies

Remedies available through civil court processes include:

- injunctions (interlocutory and final) preventing the continuation or repetition of prohibited conduct;
- recovery for loss or damage (compensation) from contraventions of the provisions;
- non-punitive orders preventing individuals from engaging in contrary conduct during a probation period, requiring the performance of community service, or issuance of advertising dispelling misleading representations;
- punitive orders requiring a person to publish an advertisement acknowledging illegal conduct (once a criminal offence has been proven); and
- other orders to compensate or prevent/reduce loss or damage suffered by a party including refunds, variation of contracts or provision of repairs.

Administrative resolutions

Actions available to the regulator that do not require the imprimatur of a civil or criminal court include enforceable undertakings that are given by an individual to resolve an alleged breach of the unfair practice provisions (false or misleading representations; bait advertising; harassment or coercion; referral selling; and falsely offering prizes). Undertakings can include refunds and other corrective action and a commitment by the offender to adhere to a compliance program to avoid future breaches. Where undertakings are breached, a court can make orders either directing compliance; requiring payment of any financial benefit from the conduct; compensating parties suffering loss or damage; or any other appropriate order.

Other administrative options currently available in some jurisdictions include cease trading orders and infringement, substantiation and public warning notices (see text).

Sources: MCCA 2005a, Miller 2005, ACCC, sub. 80.

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- cease and desist orders that temporarily halt certain conduct while a matter is investigated;
 - infringement notices; and
 - public warning ‘naming and shaming’ notices.

As a general observation, the Commission notes that there was little in the way of hard evidence provided by participants on the magnitude of the problems caused by gaps in the availability of enforcement mechanisms (either individually or in combination). Rather, proposals to widen the range of tools were more of an in-principle appeal for powers that would facilitate a more layered approach to enforcement. These included the submissions from the ACCC (subs. 80, DR176), ASIC (subs. 103, DR174), Choice (subs. 88, DR194), the Small Enterprise Telecommunications Centre (sub. DR168), Kildonan Uniting Care (sub. DR206), the joint response from nine consumer advocacy groups (sub. DR228) and the REIA, with the latter commenting in relation to the introduction of certain administrative powers that:

Currently, it is generally only possible to pursue meaningful enforcement of consumer protection laws via court based prosecution. ... it would be of benefit to both consumers and businesses to have a range of civil penalties available for alleged minor breaches of consumer law. These penalties could include fines, substantiation notices, cease and desist notices or other types of remedies. (sub. DR172, p. 14)

Also, the ACCC’s regulatory counterpart in New Zealand noted that it is seeking similar additions to its enforcement powers.

In the New Zealand context the [Commerce] Commission has also advocated some ... possible improvements ..., in particular, substantiation notices, banning orders and the rules governing class actions. We agree that the consumer policy toolkit needs to be expanded and shaped by amendments to the generic law which enable that law to be enforced more readily and effectively. (sub. DR193, p. 2)

But while the Commission considers that a layered enforcement response is a critical element of good consumer policy (see chapter 3), as it emphasised in the Draft Report in proposing an expanded set of enforcement tools, such augmentation to the regulatory toolkit is not without some risks and costs. Specifically, it is likely to involve some additional compliance costs for firms (especially where those tools reverse the onus of proof) and increase the risk of regulatory error (even in the presence of appropriate safeguards).

In querying the need for additional tools, certain participants focused on these potential costs and risks given the lack of evidence about adverse consequences for consumers ensuing from current enforcement deficiencies. Optus, for example, in responding to the Commission’s draft proposals said that it:

... believes that consumer regulators already possess a range of enforcement tools for dealing with breaches of the law that are completely sufficient to carry out their responsibilities.

... there is little evidence to indicate that lack of access to particular enforcement tools is imposing significant costs on consumers and ... adding to the current range of tools may result in additional compliance costs on firms and the risk of regulatory error. (sub. DR173, p. 7)

Similarly, Telstra argued:

... there is insufficient evidence disclosed in the Draft Report to endorse an increase in the powers of the ACCC or the introduction of additional remedial provisions. In any event, the array of enforcement tools and remedial outcomes currently available to regulators is more than adequate to effectively enforce consumer protection laws. (sub. DR156, p. 19)

Beyond the telecommunications sector, the Australian Finance Conference (sub. DR216, p. 11) was also ‘... cautious about any increase to current enforcement powers’ while banking and insurance group Suncorp commented that it:

... does not support any increase to current enforcement powers – rather, Suncorp prefers to rely on existing comprehensive powers the regulators currently have available, or adoption of existing State powers such as those within the UCCC’s to the federal sphere, but without increase. (sub. DR171, p. 14)

However, the evident need for caution in augmenting the set of tools available to regulators — especially given the interactions and overlaps between them — is not a sufficient reason to maintain a regime which, prima facie, has some significant gaps which restrict the adoption of a layered enforcement approach. With appropriate safeguards in place (such as appeal rights) to limit the potential for regulatory over-reach and the imposition of unnecessary costs on firms and consumers, such additional tools can still deliver net benefits to the community.

Furthermore, the Commission notes that the State and Territory Offices of Fair Trading (as a group) currently have access to most if not all of the powers of concern to the businesses referred to above. There was little evidence presented to this inquiry suggesting either the misuse of these powers or any unwarranted costs associated with their application. That said, the Commission has still stopped short of supporting all the additions suggested by Australia’s consumer regulators and other participants.

Civil penalties

Limits of current arrangements

Presently, criminal proceedings are the only avenue through which offenders can be explicitly penalised for breaching consumer protection laws. Those penalties are capped to reflect the associated criminal conviction and, unlike in other countries, do not apply to breaches involving general misleading or deceptive conduct (except in Tasmania) even though these prohibitions are considered to be the ‘cornerstone’ of Australian consumer law (see below). Moreover, for a range of reasons, regulators are constrained in their ability to pursue criminal actions in some consumer cases where a financial penalty might be warranted. These include circumstances where:

- there is a need for timely action to provide redress such as corrective advertising or compensation and to stop further detriment occurring;
- the nature of the evidence may not support a criminal conviction;
- the cost of criminal investigations limits the number of cases that can be pursued given resource constraints faced by regulators and prosecutors; or
- there are disparities in the enforcement priorities of regulators and the jurisdictional Directors of Public Prosecutions (in those jurisdictions where regulators cannot bring criminal cases to the court directly).

Although regulators can employ both criminal and civil proceedings to achieve punishment and redress in respect of the same matter, this will necessarily involve additional (and potentially unnecessary) costs for defendants, regulators and the judiciary. For all of these reasons, civil proceedings will be preferred in some situations where criminal actions may be an intrinsically stronger but less cost-effective form of deterrent. This is reflected in the paucity of criminal cases either referred to the DPP or prosecuted directly by Australian consumer regulators.² Indeed, if there is a reluctance to pursue criminal actions, then the practical deterrent effect of criminal penalties may actually be weaker than from civil penalties were these to be available. In the words of the ACCC:

The relative infrequency with which the ACCC can pursue criminal proceedings under the current system lessens the overall risk to businesses of penalties being imposed for breaches, and therefore lessens the deterrent effect. (ACCC 2005b)

² For example, there were 2 criminal matters involving the Trade Practices Act dealt with by the Commonwealth Director of Public Prosecutions in 2004-05 and none in 2005-06. (Commonwealth DPP 2005, 2006)

Of course, consumer regulators already have various civil remedies available to them focused on undoing the harm caused by breaches of consumer law, including injunctions, compensation and corrective advertising. As noted by Telstra, such remedies and the associated adverse publicity may also have some more general deterrent effects.

However, they are not *explicitly* aimed at deterring conduct (regardless of the associated detriment), and in some cases, evidently do not provide for a strong deterrent effect. For example, given that representative actions can presently only be made on behalf of consumers consenting to those actions in writing (see chapter 9), the financial consequences of an award for damages against a defendant (in a civil case alone) may fall well short of the benefit they derive from their conduct.³ Similarly, as the US Federal Trade Commission argued in seeking a civil penalty authority in certain information technology areas, compensation may be impractical in cases where the injury suffered by consumers is non-economic or difficult to quantify and where disgorgement of profits (see below) from unlawful conduct is unavailable because the defendant has not profited from the action.

Specific new powers

In the Commission's view, the introduction of a civil penalty regime, including fines, disgorgement of profits and banning orders (see below) has the potential to allow for a more layered enforcement approach to deter breaches of the generic consumer law that may not justify criminal sanctions. It would also facilitate more cost-effective enforcement as redress and punishment could be achieved in a single proceeding. As the Ministerial Council on Consumer Affairs observed:

Civil penalties are a middle ground between criminal penalties and civil remedies and may assist in ensuring a proportionate regulatory response to breaches of the law, as well as allowing enforcement agencies to achieve consumer redress in the same proceeding. The level of civil penalties is often higher than criminal fines. Since a consumer law breach will often result in an economic benefit to the trader, a civil penalty of some significance will act as an economic sanction. Like criminal penalties, civil penalties are designed to deter conduct in breach of the law. (MCCA 2005a, p. 4)

Similarly, the ACCC remarked:

³ As an example of the extent of potential detriment, in *ACCC v Danoz Direct* [2003] FCA 881, the Federal Court declared a range of advertising claims made by the defendant regarding a fitness system to be misleading or deceptive. Approximately 100 000 units were sold with a total value of around \$16 million before the product was withdrawn from the market. While the ACCC sought refunds for consumers, the Federal Court held that it did not have the power to provide refunds for non-named parties.

The introduction of civil pecuniary penalties would bridge the existing gap between the civil compensatory measures currently available for breaches of fair trading and consumer protection provisions and the criminal penalty provisions. In particular, it would enable a more proportionate response to breaches of the consumer protection provisions increasing the deterrent effect of existing laws. (ACCC, sub. 80, p. 96)

ASIC went further in suggesting that the level of financial penalty should be tied to the benefit attributable to the conduct (provided a number of legal and policy considerations were addressed).⁴ It argued that such disgorgement powers:

... can act as a powerful deterrent against undesirable conduct by stripping away the profits that would otherwise be earned by an offender, in excess of any compensation payable to affected consumers. We would welcome the inclusion of a disgorgement remedy in the remedies available to ASIC under the ASIC Act and Corporations Act. (sub. 103, p. 65)

Indeed, based on its experience with seeking civil penalties under Corporations Law, it questioned whether access to civil penalties for breaches of consumer law would be particularly effective in deterring inappropriate conduct in the absence of such a capacity.

In the Commission's view, enforcement mechanisms should aim to ensure that the ultimate cost of engaging in illegal conduct significantly outweighs its perceived benefits and the costs to other parties of taking enforcement action. In considering the consequences of a particular breach, the small number of traders willing to break the law will weigh a range of factors that include the likelihood of discovery and prosecution and the potential damages, fines and other costs incidental to the court finding guilt (such as adverse publicity). As the judgement in *Vogel and Son Pty Limited v Anderson (1967)* 120 CLR 57,164 noted:

[F]or some people little seems to matter but fear of the consequences of discovery. The *Customs Act* makes those consequences potentially drastic. It is for courts to make them, in suitable cases, drastic in fact, for otherwise traders who are not saved by qualms of conscience from willingness to defraud their fellow citizens may weight the profits they hope for against the penalties they have cause to fear and find the gamble worthwhile.

Where a regulator has difficulty in using available enforcement tools and/or cannot

⁴ Similar powers were introduced for breaches of the anti-competitive conduct provisions following a review of the TPA in 2003 (Dawson 2003). Under those provisions, penalties of up to three times the value of the benefit reasonably attributable to the conduct (or, if greater, \$10 million) are now available. Where the benefit from illegal conduct cannot be determined, a penalty of 10 per cent of the annual turnover of the offender can be imposed. These powers can be contrasted to other civil penalties that are fixed by statute and linked to the level of penalty for a parallel criminal offence. Given the effect of a criminal conviction, civil penalties are typically larger than criminal financial penalties.

obtain appropriate restitution, incentives to engage in conduct detrimental to both consumers and competition more generally will rise. While the deterrent effect of adverse publicity and remedial costs may be a sufficient check on bad behaviour for many firms, in the absence of scope for the regulator to seek civil penalties, some may still judge the benefits of acting inappropriately to outweigh the costs.

With this in mind, in the Draft Report, the Commission proposed the introduction of a civil pecuniary penalty regime for breaches of the generic consumer law including its application to breaches of the general misleading and deceptive conduct provisions (see box 10.2). It argued that this would facilitate an appropriately layered approach to consumer protection, with little additional cost and without adding to either the compliance burden or regulatory uncertainty for business (given their general understanding of existing legal obligations under the law).

This proposal was widely supported by participants (see, for example, ACCC, sub. DR176, Choice, sub. DR194, Law Council of Australia sub. DR225 and the Victorian Government, sub. DR226). Opposition, primarily from those arguing against the introduction of any new powers, mainly revisited arguments that the Commission had taken into account in concluding that provision for civil pecuniary penalties should be introduced. And though ASIC (sub. DR174, p. 18) questioned the frequency with which it would use such an instrument, especially if it did not provide for disgorgement powers, that observation should help to allay the concerns expressed by those participants highlighting the risk of regulatory over-reach.

However, some additional issues relating to the operation of a civil penalty regime were raised by participants. In particular, the Foundation for Effective Markets and Governance argued that the deterrent effect of civil pecuniary penalties will be lessened where there is scope for firms or individuals to pass on part or all of the penalty to consumers.

Who eventually pays civil (or criminal) financial penalties? Although competitive theory suggests these are borne by shareholders, surely some of these come back to the consumer in some form, It takes a great deal of faith in the conventional economic model to overlook the possibility that fines are ultimately passed through to consumers. (sub. DR122, pp. 13-14)

Tortoise Technologies similarly suggested (sub. DR126, p. 10) that such penalties are simply treated as a cost of doing business and went on to argue that the process of redress needs to include the views of those who have been adversely affected.

... action is often taken against a corporation, rather than the individuals who may have directed the unlawful actions and fines are paid from the resources of the corporation.

Financial penalties are only a part of the process of redress; what is needed is a wider range of options open to the judiciary, than are presently available, so that those who have been damaged by the actions have a say in the penalties levied.

Box 10.2 Application of civil penalties to section 52 of the TPA

In the Draft Report, in supporting the introduction of civil penalties, the Commission argued that they should apply more widely than envisaged by the ACCC and extend to certain breaches associated with general misleading or deceptive conduct (section 52 of the TPA). Complaints in that area dominate alleged contraventions of Australian consumer law and feature prominently in civil litigation brought by both consumer regulators and private parties.

Neither criminal nor civil penalties are currently available for section 52 breaches in any Australian jurisdiction other than Tasmania. The ACCC argued (sub. 80 and personal communication) that this provision should be excluded from a civil penalty regime because [in line with the judgement in *Brown v Jam Factory Pty Ltd (1981) 53 FLR 340*], it establishes a norm of conduct rather than creating liability. In addition, it said that as section 52 breaches generally do not involve serious moral culpability, and include many situations involving unintentional or inadvertent breaches of the law (that go to the issue of fault), it would be inappropriate to penalise such conduct.

The ACCC also cited the decision in *Briginshaw v Briginshaw (1938) 60 CLR 336* where the court determined the evidentiary burden in a civil prosecution may vary according to the severity of the alleged offence and the consequences of it being proven. Therefore, the ACCC said:

... a court is likely to require additional evidence, beyond that which might otherwise be sufficient to make out a breach of the Act on a balance of probabilities, in relation to an ACCC civil prosecution seeking a pecuniary penalty for breach of the TPA fair trading provisions. It would be logically consistent, therefore, if section 52 was excluded from a civil pecuniary penalty regime. (personal communication)

However, guidance provided by the Australian Law Reform Commission regarding the range of factors to be considered in imposing a civil penalty highlights the discretion that should be available to the court to take account of the nature and seriousness of the offence, the circumstances in which it was committed and the deterrent effect of any penalty. In the Commission's view, the court is the appropriate forum for adjudicating the severity of section 52 breaches and the standard of evidence required. Indeed, in an earlier submission to a MCCA discussion paper, the ACCC supported the application of civil penalties to certain section 52 breaches on just these grounds.

In regard to the issue of fault, the Commission understands that in a range of civil legal contexts (such as statutory product liability and common law negligence cases), notions of strict liability are imposed by the courts specifically because this acts to strengthen the incentives to exercise reasonable care. And in other areas, courts have the discretion to consider notions of fault depending on the severity of the breach. The desirability of such discretion is also explicitly acknowledged by the advice provided in the *Guide to Framing Commonwealth Offences, Civil Penalties and Enforcement Powers* (Ellison 2004).

Significantly, the ACCC did not take issue with the case put by the Commission for extending the application of civil penalties to section 52 breaches in its response to the Draft Report.

Also, some sought the inclusion of so called ‘cy pres’ provisions that would distribute the gains from illegal conduct (where it is difficult to identify most or all of the consumers affected) to a cause acting in the interests of consumers generally. In this regard, the Consumer Action Law Centre (sub. DR241, p. 4) provided an example from the late 1980s of a finance company that engaged in dishonest and unfair selling practices being directed to fund the establishment of an advocacy centre for Victorian consumers.

The Commission agrees that where competition is constrained there is likely to be some pass-through of civil pecuniary penalties to consumers. But this is not an argument against the introduction of such penalties. Rather, it points to the importance of effective competition policies in limiting market power and the adverse effects this has on consumers. And to the extent that financial penalties are insufficient to deal with illegal conduct, the Commission simply notes that there are a range of other remedies currently available (such as compensation orders) to provide redress to affected parties.

As to the possible inclusion of ‘cy pres’ orders, while the Commission sees some merit in them, it is concerned that they would be administratively cumbersome and may also be a source of dissonance among competing advocacy interests. On balance, it does not consider that such orders should be part of the proposed new civil penalty regime.

In summary, while civil pecuniary penalties are not a panacea for dealing with the gaps in the current enforcement toolkit, they are a potentially useful addition to that toolkit which could sometimes provide for more effective enforcement action than at present. They would also strengthen somewhat the deterrence against inappropriate conduct and thereby potentially reduce the number of significant breaches of the generic consumer law.

Banning orders

Criminal convictions have a range of direct and indirect financial and personal consequences including ineligibility to hold positions of public office or company directorships, denial of permission to travel to certain countries and deprivation of certain civil rights (if the sentence includes incarceration). They are, therefore, a punitive means of punishing and deterring certain conduct and protecting the public. Equally, as noted above, even where conduct warrants such a response, a range of factors may constrain regulators from pursuing criminal actions.

Banning orders, by comparison, are a form of court injunction that disqualify or restrict *individuals* from participating in specific activities (either permanently or

for set periods) to reduce the risk of habitual offending. While they do not carry the additional weight of a criminal conviction, they are still considered both punitive and protective in nature and are used in many Australian legal contexts. These include breaches of the *Corporations Act 2001*, financial services regulation and the restrictive trade practices provisions (Part IV) of the *Trade Practices Act 1974*. Most States and Territories allow courts to make orders (to cease trading) that share some similarities with banning orders, though there are important distinctions.⁵

These instruments embody features potentially more effective in deterring certain conduct than existing civil enforcement mechanisms because they specifically target individuals. For example, these orders can readily prevent offenders from routinely establishing new corporate entities ('phoenix' companies) to repeat what is substantially the same or similar conduct.

For other reasons, banning orders can be more effective than civil pecuniary penalties (were these to be available) because, as discussed above, financial penalties may sometimes be absorbed by the corporate entity rather than the individual (and treated as a cost of doing business). In addition, isolating the penalty for illegal conduct to the responsible individual rather than the corporate entity may prevent (or limit) harm to associated parties (for example, shareholders, employees, creditors and consumers seeking compensation) who may be indirectly affected by a financial penalty. Therefore, banning orders can be a potentially important and useful complement to civil penalties and other remedies.

However, there are serious personal and financial consequences associated with making such orders, including through the adverse publicity they entail. While judicial processes reduce the risks of regulatory error, those processes are not error-free. And the stigma associated with a court ruling may persist even if an initial finding is reversed on appeal. Hence, although the Commission believes that access to banning orders (as a complement to civil pecuniary penalties) would increase the effectiveness of the current enforcement regime, its support for their introduction is conditional on their being appropriate safeguards in place to protect the rights of legitimate traders.

In this context, the Commission notes the approach adopted in aspects of restrictive trade practices law (Part IV of the *Trade Practices Act 1974*) where certain orders can only be made after a court has imposed a financial penalty or proclaimed a criminal offence. In the Commission's view, triggers of this kind would be an

⁵ For example, the scope of cease trading orders is limited to the carrying on of a business of supplying goods and services. Banning orders, on the other hand, have a broader prohibitive effect on individuals.

appropriate threshold for similar provisions in the new national generic consumer law.

Aside from those participants opposed to consumer regulators being given any new powers (see earlier), there was strong support for the Commission's draft recommendation calling for the introduction of banning orders. This included the Victorian Government (sub. DR226), New South Wales Government (sub. DR251), Choice (sub. DR194), the Law Council of Australia (sub. DR225) and ASIC (sub. DR174), with the latter noting that it expected banning orders would be required in the specific context of a new registration/licensing system for credit providers (see chapter 5).

Administrative powers

A number of participants called for an extension of the discretionary powers currently available to regulators to give them the ability to issue substantiation notices, cease and desist orders, infringement and public warning (naming and shaming) notices.

Substantiation notices

Claims or representations made in promoting the supply of goods and services are often made on an inferential, as opposed to a factual, basis. Accordingly, the scope for consumer regulators to verify that such promotion is based on reasonable grounds is seen by many as an important safeguard against misleading or deceptive conduct.

The substantive provisions of the generic consumer law specifically prohibit making representations that are false or likely to mislead on grounds including quality, price, availability and place of origin (section 53 of the TPA and the equivalent provisions of the FTAs).⁶ The standard applied is whether the claim was capable of misleading the ordinary reader, not whether they were actually misled.

However, some participants (and other commentators) argued that certain conduct does not fall within the scope of these specific prohibitions. One example put forward was so-called puffery or exaggeration which the ACCC (sub. 80, p. 113) claimed was not covered '... because they are not considered likely to mislead.' Another involved implied, as opposed to express or actual, claims that a trader may

⁶ The common law tort of deceit provides another avenue through which such conduct can be tested.

not even be aware they were making but would be motivated to consider if they were potentially subject to sanction (Fels 2007).

As an aid to policing breaches of the misleading or deceptive prohibitions in the generic consumer law, powers are available to regulators (under section 155 of the TPA and its equivalents) to investigate possible contraventions of that law by requiring information and documents, or appearance before the ACCC from a person capable of providing such material. These powers include the right to enter premises and inspect documents, in appropriate circumstances, that are similar to the search warrant provisions in the *Crimes Act 1914*. They also explicitly abrogate the individual's rights against self-incrimination (Miller 2005).

But the submission from the ACCC argued that the usefulness of these powers is limited by the evidentiary threshold required for their activation:

In many cases involving false or misleading representations, it will not be apparent on the face of the claim whether a breach is likely to have occurred or not. In such cases, use of s. 155 powers may not be available as the threshold requirement — that the ACCC must be satisfied that there is a matter that may constitute a contravention — may not have been met. (sub. 80, p. 108)

It went on to list a range of matters (such as two part advertising, product safety, food and environmental claims) where misleading conduct can be difficult to detect at the outset, arguing that substantiation powers are needed to facilitate earlier detection:

Due to lack of information, the ACCC may find itself devoting resources to investigating claims which may prove to be legitimate, or worse, dismissing complaints for lack of evidence where there may be misleading conduct occurring. Further, matters where the misleading elements are not apparent and there is least initial evidence to warrant an investigation are the matters most likely to actually deceive consumers. (sub. 80, p. 112)

However, according to Miller (2005, p. 1346), the powers conferred under section 155 are 'extremely wide' and only require 'a relatively low threshold' that the regulator has reason to believe that the person to whom the notice is directed is capable of providing information concerning a possible breach. It is not necessary for the regulator to have reason to believe that a breach has actually occurred.

But the ACCC argued in a subsequent communication that:

... the information sought in a section 155(1) notice must relate to the matters the subject of investigation by the ACCC, and there must be some factual basis for the suspicion that the matters identified in a notice may constitute a contravention of the TPA (*Seven Network v ACCC* [2004] FCAFC 267). (personal communication)

In turn, Telstra responded to this contention by claiming that section 155 powers already serve the function of substantiation notices and that:

... the use of coercive powers and a reversal of the onus of proof in the absence of any factual basis for a suspicion on the part of the regulator would amount to a denial of natural justice and to imposing no threshold at all on the activation of these powers. (sub. DR156, p. 16)

The preceding interplay indicates that the scope of section 155 powers is open to debate. And these are not the only considerations bearing upon the desirability of substantiation provisions.

- The Commission notes that in regard to the specific issue of puffery raised by the ACCC, while the general provision for misleading or deceptive conduct (section 52) does not prohibit such exaggeration in contractual negotiations or advertising, there is a considerable body of case law that has dealt with the distinction between such promotion and illegal conduct. In this context, while the courts have been reluctant to elevate behaviour designed to attract the interest of potential purchasers to the status of potentially misleading conduct, they have not been so reticent where the conduct has induced, or was capable of inducing, error. (*General Newspapers Pty Ltd v Telstra Corp* (1993) 40 FCR 98, *Eveready Australia Pty Ltd v Gillette Australia Pty Ltd* (2000) ATPR 41-751).
- Because they effectively reverse the onus of proof from the regulator to traders, substantiation powers will necessarily involve additional compliance costs for some firms. This will be particularly problematic in situations where a trader may not have a high degree of knowledge about specific products, for example, where a retailer relies on information supplied by a manufacturer.
- Also, while substantiation powers are currently available under the fair trading laws in five States and Territories, they are rarely used (Fels 2007) — a point acknowledged by the ACCC (sub. 80, p. 109).^{7,8} Although this could be due to a number of factors (including the availability of effective alternatives such as injunctions), it does raise a valid question about the need for, and practical effect of, the introduction of substantiation powers more broadly.

In the Draft Report, after carefully weighing up the competing considerations, the Commission concluded that there is a case for including substantiation notices in the new national generic consumer law. Amongst other things, the Commission noted that such powers would provide an additional regulatory tool to deal with

⁷ Regulators in those jurisdictions also have information disclosure powers equivalent to section 155.

⁸ The ACCC noted that just 6 substantiation notices were served by Consumer Affairs Victoria in 2005-06. The figure for 2004-05 was slightly higher at 9 (CAV 2006c, p. 59).

increasingly complex representations made through traditional mediums and via the Internet provided that the associated compliance costs are contained.

Also, the Commission noted the scope to contain compliance costs by tailoring the power to the nature of a specific claim (as suggested by Fels (2007)). In this context, ASIC pointed to the current requirement in financial services regulation (section 945A of the *Corporations Act 2001*) that advisers ‘...have a reasonable basis for their advice ...’ (sub. 103, p. 12). Similarly, the Federal Trade Commission in the United States requires a higher level of proof for express claims (eg, ‘five times stronger’ or ‘studies have shown’) compared to other (including implied) claims where only a reasonable basis is needed.

Apart from that group of participants opposed to the introduction of any new regulatory powers, others generally supported the Commission’s conclusion with ASIC (sub. DR174, p. 18) again commenting that such provisions would be required in the specific context of a new registration/licensing system for credit providers.

Coles Group also supported the proposal, but sought clarification of certain operational features to make manufacturers the first point of contact and to provide enough scope to ensure:

... that the requirement does not become overly burdensome for retailers, and suppliers, in line with the Productivity Commission’s objectives to reduce cost and burdens on business. (sub. DR 146, p. 2)

The commentary on the Draft Report has served to reinforce in the Commission’s mind the case for incorporating substantiation provisions in the new national generic consumer law. Particularly given the increasing complexity of consumer markets, applied prudently, these powers could deliver more cost-effective and timely remedies than pursuing court action on the grounds of misleading or deceptive conduct. And while the Commission agrees with Coles Group that in most cases the burden of substantiation should reside with manufacturers (or importers) if they are the source of the advertised claims, it would be concerned if this served to lessen the incentives retailers have to independently scrutinise the claims made by their suppliers. The Commission considers the approach used under the Corporations Law — that retailers should have a reasonable basis for accepting the claims made by their suppliers — would serve to provide the right balance in this regard. Similarly, retailers would evidently need to have a reasonable basis for direct claims that they themselves make.

A further consideration is that with such powers already available in most State and Territory Fair Trading Acts, support for a single national generic consumer law could be weakened if substantiation provisions were not available under that new

law. Though not of itself a sufficient reason for their introduction, it does serve to strengthen the intrinsic arguments for doing so.

Cease and desist orders

Cease and desist orders require traders to temporarily cease conduct potentially in breach of the law while a matter is investigated. They are, in effect, administratively imposed interlocutory injunctions which their proponents argue offer a faster, more flexible means of stopping prohibited conduct compared to court-based orders (essentially because they reverse the onus of proof).

While not available to the ACCC and some jurisdictional Fair Trading Authorities, cease and desist orders are available to consumer regulators in Victoria and NSW and are also used in a number of other countries. The product safety provisions of the TPA also grant equivalent power to the Minister (rather than the regulator) through compulsory recalls or product bans — although it could be argued that the trigger for that action, the occurrence of damage or injury, usually provides strong *prima facie* evidence of a breach.

But while some participants called for all regulators involved in applying generic consumer law to have these powers, those enforcement agencies without current access to them did not. In fact, the ACCC argued that injunctive relief was sufficient to achieve similar outcomes. This position is supported by the findings of a recent review of the TPA which considered cease and desist powers in the specific context of competition law. That review concluded that there was little evidence (either locally or internationally) that these orders are ‘... speedier or more efficient than the existing process of obtaining an interlocutory injunction.’ (Dawson 2003, p. 108). Telstra similarly argued:

... the law which has been developed around the grant of interlocutory injunctions appropriately balances the interests of the parties in attempting to arrive at a just outcome, and is well understood by all stakeholders. The creation of an administrative power to impose cease and desist orders in the absence of a hearing or judicial supervision is inappropriate. (sub. DR 156, p. 17)

Given this evidence, the Commission does not see a strong case for making cease and desist orders part of the new national generic consumer law.

However, though not advocating cease and desist orders, the ACCC did highlight a procedural issue that it claims limits its ability to investigate potential breaches of fair trading laws once an application for an interlocutory injunction is made. Specifically, it said that after such an application is made, the scope to further investigate a matter and gather evidence (under section 155) to be used in substantive proceedings is restricted. This is due to a legal requirement that courts

supervise information disclosure and exchange between parties to proceedings to protect the legitimate rights of the accused.

In elaborating on this restriction at the public hearings, the ACCC commented that there have been several occasions where the current provisions have precluded it from using its investigative powers (in both a competition policy and consumer protection context) with the result being that:

... [we] then have to choose between seeking an injunction to stop the conduct ... which we think might be particularly injurious to consumers ... [and] losing a significant part of our investigative tools [to gather further evidence]. (trans., p. 719)

But the Law Council of Australia considered the information gathering powers under section 155 are extensive and adequate and accordingly, it is unnecessary to broaden ‘... the already very wide powers of the regulator in relation to evidence gathering ...’ (sub. DR225, p. 13).

Moreover, extending these powers would not be without some risks — a point emphasised by both Telstra and the Redfern Legal Centre. Telstra said:

... [the provision of] any further powers to gather evidence after an application for injunctive relief has been granted is likely to pose a substantial risk to due process, and be likely to lead to a defendant being unfairly prejudiced in the conduct of its defence of the proceeding. (sub. DR156, p. 19)

Similarly, the Redfern Legal Centre commented:

It could be argued that on the one hand, such evidentiary powers could be used in the manner of secret police, but on the other, that once injunctive relief has been granted, the regulator has embarked down the normal interrogatory/discovery-type procedure. The difference is that where a regulatory authority is operating in such a way, it is not necessarily bound by common law, or other rules by which Courts are bound. (sub. DR151, p. 10)

It was primarily for this reason that the Commission recommended in the Draft Report that a review of the extent to which procedural fairness might be compromised by an extension to regulators’ powers in this area be conducted by an expert legal authority. The subsequent interplay on this issue (see above) has reinforced its view that a cautious approach is warranted. Such caution was supported by several participants including ASIC (sub. DR174, p. 18) and the Motor Trades Association of Australia (sub. DR169, p. 2).

Infringement notices

Infringement notice schemes empower regulators to serve notices on suspected offenders alleging an offence and requiring payment of a penalty to avoid

prosecution in a court-based setting. As noted by the Law Council of Australia (sub. DR225, p. 13), these provisions involve a departure from the traditional separation of powers allowing courts alone to impose penalties. Hence, their use is considered most appropriate for relatively minor offences, where a high volume of contraventions is expected, where a penalty must be imposed immediately to be effective, and where it would not be a good use of enforcement resources to take action through the courts. While the provision of such administrative discretion increases the risk of regulatory error, this can be reduced when these powers are based on objective assessment criteria (Ellison 2004).

Infringement notice powers for breaches of consumer protection law in areas such as product bans, recalls and lay-by sales requirements are already available in some Australian jurisdictions, but generally not for fair trading provisions such as misleading or deceptive conduct. Given the current remit of the ACCC and those regulators administering Commonwealth laws to focus on issues of national and widespread consumer detriment, these powers are of little relevance to their current activities.

However, the inclusion of such powers in the new national generic law would be desirable to continue to provide scope for consumer regulators to deal with minor offences in a cost-effective manner.

There was considerable support for this proposition among participants including from the New South Wales Government (sub. DR251, p. 21) and the Victorian Government (sub. DR226, p. 87). And though some were concerned about the risk of regulatory over-reach (see, for example, Telstra, sub. DR156, p. 17), the ACCC (sub. DR176, pp. 11-12) pointed to advice provided in the *Guide to Framing Commonwealth Offences, Civil Penalties and Enforcement Powers* (Ellison 2004) as a means of minimising the risk of regulatory errors.

Infringement notice provisions should state that a person to whom an infringement notice is issued has the right to opt to have the matter dealt with by a court. Direct 'enforcement' of the notice by any other means should not be permitted. (Ellison 2004)

Given these guidelines, and in particular the right to have a matter dealt with by a court, the Commission considers the risk of regulatory over-reach to be small. However, in implementing such a provision in the new national generic consumer law, there will need to be consideration given to certain constitutional issues raised by the ACCC:

... the Constitution restricts Commonwealth agencies that belong to the executive from exercising judicial power. Therefore, a power to issue infringement notices needs to be carefully drafted. (sub. DR176, p. 11)

The Commission understands that a review of the operation of the infringement notice provisions currently available to ASIC under the Corporations Act 2001 is presently being conducted by the Australian Treasury. That review should clarify how infringement notice provisions would best be incorporated in the new national consumer law.

Naming and shaming powers

Public warning notices (or ‘name and shame’ powers) enable enforcement agencies to inform consumers about suppliers engaged in unfair business practices to reduce or stop the associated detriment. A number of Australian jurisdictions provide ministerial or administrative discretion to issue such notices. At the national level, provision to issue warning notices is currently limited to the product safety provisions (section 65B) of the TPA (and where used, these have generally related to specific products or classes of goods rather than brand or supplier names).

Given the potentially significant personal and financial consequences for suppliers from adverse public exposure, the objectives these notices seek to achieve need to be balanced against the rights of legitimate traders. Even if further investigation or an appeal reveals that the conduct was not in breach of the law, the stigma associated with the original decision is unlikely to be entirely extinguished. This in turn highlights the need for procedural fairness in exercising such powers — a point recognised by the Queensland Government in commenting on the impact of *Kioa v West (1985)*:

There is debate about the reliance that should be placed on direct reputational action through consumer policy. Jurisdictions across Australia vary in the application of naming of businesses with some more willing to take action than others. In part this may be due to the varying degrees of perceived risk across jurisdictions in relation to the potential negative outcomes for agencies and businesses where there is a small chance of a false positive (i.e. when naming occurred but was unjustified) or backlash from business even when the naming is a correct call. (sub. 87, p. 63)

The Commission also notes that a range of existing mechanisms appear to deliver similar informational outcomes to public warning notices, but with the added safeguard of court-based oversight. For example, under section 86C of the TPA (and the mirror provisions in the FTAs), regulators can ask the court, in appropriate circumstances, to order the publication of corrective advertising aimed at dispelling incorrect impressions gained from misleading advertisements, raising public awareness of the type of conduct that may contravene the law and the outcome of litigation (Miller 2005, p. 883).

Similarly, regulators commonly issue media releases in print and on their Internet sites detailing injunctions awarded and prosecutions pending against those alleged

to have breached consumer law and, where proven, the remedies imposed by the court. Details of enforceable undertakings are also routinely published through these mediums. Further, other mechanisms such as SCAMwatch (which issues email alerts and maintains a database about certain types of conduct), are available to deal with activities that may lie beyond the reach of a domestic court (for example, the fraudulent acquisition of confidential information via email and overseas-based entities). Moreover, as noted above, court-ordered injunctions can provide for a stronger response for dealing with potentially illegal conduct.

However, some participants expressed concern that a failure to replicate naming and shaming powers available to some state regulators in the new national generic consumer law would diminish the protections afforded to consumers. For example, the New South Wales Government commented that public warning notices and statements are an important part of the regulators' enforcement options in that state and are issued in accordance with specified procedures and guidelines:

... to ensure that decisions about issuing warnings are made with consistency and fairness, in accordance with the public interest and the principles of natural justice. (sub. DR251, p. 21)

And the Victorian Government noted that these powers provide an early warning system to consumers of unfair practices and traders. Highlighting the difficulty of using legal processes to identify traders operating under assumed names (as well as the additional time involved), it contended that court-based injunctions are not a substitute for such powers. It also commented on the safeguards in place to protect businesses from inappropriate naming:

Businesses are protected from the misuse of this provision. First, there is a public interest test — the power can only be used when it is in the public interest to do so. Second, there is no immunity for the crown, and thus the business or individual in question has all the normal legal rights they would have regarding public statements made about them. (sub. DR226, p. 88)

Importantly, however, the Commission understands that certain safeguards (such as the crown's potential exposure to prosecution) are not available in all States and Territories where naming and shaming powers are available to consumer regulators.

In summary, the Commission remains sceptical about the intrinsic merit of including public warning notices in the new national generic consumer law. Certainly, the case for these powers is nowhere near as strong as that for civil pecuniary penalties or substantiation or infringement notices. In that context, their 'early warning' role would not appear to be particularly significant given that just five public warning notices were issued in Victoria in 2005-06. Nonetheless, the Commission acknowledges that failure to replicate existing jurisdictional powers of this kind could undermine the consensus for a new national generic consumer law

and even be a source of regulatory break-out in the future. Accordingly, it considers that their possible inclusion in the new law should be a matter for further examination and consideration by the Australian and State and Territory Governments through the auspices of MCCA. However, should that process result in their inclusion, to help ensure that these powers were not misused, there should be no immunity from prosecution provided to the Crown.

RECOMMENDATION 10.1

The new national generic consumer law should give consumer regulators the capacity to:

- *seek the imposition of civil pecuniary penalties, including the recovery of profits from illegal conduct, for all relevant provisions;*
- *apply to a court to ban an individual from engaging in specific activities after the court has found that a breach of consumer law has occurred;*
- *issue notices to suppliers requiring them to reasonably substantiate the basis on which claims or representations are made; and*
- *subject to guidelines informed by the current Treasury review of infringement notice powers under corporations law, issue infringement notices for minor contraventions of consumer law.*

The possible inclusion of naming and shaming powers in the new law should be the subject of further examination and consideration by the Australian and State and Territory Governments under the auspices of the Ministerial Council on Consumer Affairs.

RECOMMENDATION 10.2

The Australian Government should commission a review by an appropriate legal authority of the merits of giving consumer regulators the power to gather evidence after an initial application for injunctive relief has been granted, but prior to substantive proceedings commencing.

10.4 Regulatory consistency

Implementation of a nationally coherent consumer policy framework would help to address many of the weaknesses and inconsistencies that currently exist in respect of the protections provided to consumers across different activities and jurisdictions. In particular, a single national generic consumer law — that included civil pecuniary penalties (with scope for disgorgement of profits), banning orders, substantiation and infringement notices and an enhanced capacity for representative

actions — would provide stronger, and more consistent and cost-effective deterrence and redress compared to the current arrangements.

However, as discussed in chapter 4, while the Commission sees some advantages in making the ACCC solely responsible for enforcing the new national generic law, it is proposing that except for the product safety provisions, enforcement responsibility should continue to be shared between the Australian and State and Territory Governments. And though the Commission has recommended the transfer of credit regulation to the national level as well as a process for assessing whether other areas should be similarly transferred, much specific regulation will continue to be enforced at the jurisdictional level for the foreseeable future.

Hence, there is a risk that differences in enforcement priorities, the intensity of enforcement effort and/or coordination failures between jurisdictions that lead to enforcement gaps will continue to be a source of divergent outcomes for consumers. Such divergences were a significant concern for many participants under the current multi-jurisdictional arrangements (see box 10.3).

As discussed in chapter 4, evidence of any significant inconsistency in the enforcement of the new national generic consumer law would be one important reason to revisit the single-regulator model as part of the proposed review of the enforcement arrangements for that new law. In the meantime, however, the Commission sees scope to reduce the risk of variable enforcement in a multi-jurisdictional enforcement environment.

Improving regulatory accountability

The provision of adequate resources to regulators is an obvious requirement for the delivery of consistent enforcement across jurisdictions and activities. But making those regulators more visibly accountable for their performance is also important.

In many jurisdictions, the nature of current performance reporting requirements is an impediment to gaining a better understanding of how significant coordination and resourcing problems are at present. Specifically, the current focus of regulatory performance reporting often appears to be on the collection and presentation of activity-based statistics on indicators such as complaint handling, litigation, judgements, undertakings and levels of consumer redress. In many cases, there is much less effort devoted to gathering, analysing and publicly reporting on areas where current enforcement problems (including coordination issues) arise, what steps are being taken to address them and how successful previous initiatives of this kind have been.

Box 10.3 Participants' views on the nature of enforcement problems

A number of participants were concerned about inadequate resources devoted to enforcement of generic and industry-specific regulation by some jurisdictions. These included the ACCC (sub. 80), Anglicare Tasmania (sub. DR191), ASIC (sub. 103), Choice (sub. 88), Consumers' Federation of Australia (sub. 83), Motor Trades Association of Australia (sub. 43), Telstra (sub. 35) and the Tasmanian Council of Social Services (sub. 32), with the latter noting a number of specific consequences:

TasCOSS has repeatedly called for increased funding for the Office of Consumer Affairs and Fair Trading in our annual submissions to the State government budget process. We believe the under-resourcing of the Office of Consumer Affairs and Fair Trading seriously hinders the implementation of adequate consumer protections for Tasmanians in some key areas (including residential tenancy and unfair contract terms, ...). It also limits the ability of the agency to adequately investigate consumer complaints and to provide access to redress, as well as limiting the agency's ability to enforce compliance. (p. 3)

Choice commented on the need to address inadequate coordination and inconsistent enforcement approaches (among other issues) across jurisdictions:

Australia's consumer policy framework would benefit from improved coordination and accountability across agencies. It would also benefit in many cases through developing consistent approaches to enforcement agencies' legislative base, their operational approach, accountabilities including monitoring compliance, enforcement and reporting thereon and the tools and powers available to them to respond effectively to conduct that harms consumers. (sub. 88, p. 71)

The Consumers' Telecommunications Network used the results of a jurisdictional complaint handling survey to highlight divergences in the ability and/or willingness of regulators to deal with complaints in the telecommunications sector. It concluded:

The result of that research was overwhelming, with widespread confusion and uncertainty about jurisdiction and willingness of various agencies to deal with the complaint at hand. There is a pressing need for [a] better understanding of where complaints belong in a telecommunications context. (sub. 78, p. 50)

Telstra raised the resourcing issue in respect of both generic and industry-specific regulation and argued that it results in the company being unfairly used as an example for other telecommunications providers:

Telstra is often the target of regulators seeking to prevent conduct that is widespread across the telecommunications industry. Yet when other industry operators fail to modify their behaviour following regulatory action against Telstra, too often no equivalent action is taken against them. ...

Telstra understands that the limited resources of regulators means that enforcement by example is sometimes necessary, but feels strongly that it is not appropriate or effective if the same operator is always targeted. (sub. 35, p. 19)

And ASIC noted its '... concerns about the level of resources available to state and territory agencies to undertake the range of tasks associated with administration of the industry-specific regulation of credit', going on to say that '... the resources available for both policy development/law reform and compliance and enforcement activities appear unevenly spread and inadequate.' (sub. 103, p. 44)

Examples of the information that could be analysed and reported on include tracking of referral loss, identification of disparities in enforcement action by jurisdiction or offence, and the incidence of complaints being pursued by multiple regulators.

Some such information should already be available to individual regulators through their complaint handling processes. That data could be usefully supplemented by regular targeted feedback from specific stakeholder groups, including firms operating on a national basis, industry associations and consumer advocacy bodies, with the resulting outputs also used to build on the strengthened AUZSHARE database (see chapter 9). This would, in turn, provide a useful vehicle for benchmarking jurisdictional performance. In that regard, the Director of Consumer Affairs Victoria recently noted:

An area for agencies to develop further is benchmarking their compliance and enforcement activities and reporting more fully on these activities and the outcomes obtained. (Cousins 2007)

And Choice (2008) have similarly argued that:

A crucial aspect of transparency is the comprehensive and comparable publication of information on enforcement outcomes. The collection and reporting of enforcement outcomes by regulators should help in assessing agency performance and in the setting of standards. (p. 29)

As well, there may be other ‘spin-off’ benefits from greater attention to reporting on current enforcement problems and issues, such as aiding the measurement of trends in consumer detriment or deterrence over time and analysing the factors driving those trends. As ASIC commented:

Developing tools to identify and quantify consumer detriment and benefit for specific proposals to introduce new regulation or remove existing regulation requires rigorous research and analysis of consumer experience. In Australia there is no overarching body with responsibility for this, and the frontline agencies that hold evidence of consumer detriment in their case work files are often not adequately resourced to collaborate on policy research. (sub. 103, p. 77)

In the Draft Report, the Commission proposed that all consumer regulators be required to report on the nature and consequences of specific enforcement problems and the impact of steps taken to address them. A number of participants endorsed the Commission’s recommendation including Choice (sub. DR194, p. 3), the Law Council of Australia (sub. DR225, p. 13) and the REIA which viewed such requirements as being a key element of the proposed consumer policy framework. In addition, the REIA suggested that:

... this process should also allow external stakeholders (such as industry associations) to comment on the performance of the generic consumer law, the national regulator, MCCA and the CoAG reform process on a regular basis. (sub. DR172, p. 14)

Anglicare Tasmania similarly highlighted stakeholder input as a means of enabling independent scrutiny and stimulating better regulatory performance:

Draft Recommendation 10.3 would place more onus on regulators and enforcement agencies such as [Consumer Affairs and Fair Trading Tasmania's] residential tenancies division to justify their actions in relation to enforcement decisions, and requiring the inclusion of stakeholder groups would ensure the process was rigorous and objective. (sub. DR191, p. 10)

And though endorsing the proposed requirements, the Consumers' Telecommunications Network considered that they should go further.

We are very pleased to see a recommendation that addresses many of the issues we identified in enforcement undertaken by regulators. This is a critical way of addressing the gaps in accountability of the industry and regulators which we discussed in detail in our initial submission to the Commission.

However, we think the Commission needs to clarify that its not only enforcement problems that should be reported on, but the agency's entire enforcement strategy and priorities for the year ahead that need to be more transparent. This will allow better tracking of progress on improvements on systemic issues. (sub. DR211, p. 11)

The Victorian Government (sub. DR226, p. 90), on the other hand, claimed that it '... already undertakes much of the Productivity Commission's recommended activity [in this area]'. However, it also indicated that it could not speak on behalf of other jurisdictions in this respect. Evidently, the concerns expressed in the initial submissions to this inquiry and the broad support for the Commission's draft proposal suggests that, in many cases, current reporting practices fall well short of what is required.

The Commission agrees that the publication of enforcement strategies and priorities by regulators would be an additional way of increasing regulatory transparency and accountability and be a useful supplement to the other requirements detailed in the draft proposal. In principle, it also agrees that broadening stakeholder input beyond that elicited through targeted surveys has merit. However, the benefits of garnering feedback must be balanced against the cost and timeliness of expanding the scope of stakeholder consultation.

RECOMMENDATION 10.3

Australian Governments should ensure that all of their consumer regulators are required to report annually on the nature of specific enforcement problems, their consequences, steps taken to address them (including enforcement strategies and priorities) and the impact of such initiatives. Such reporting should be informed by input from stakeholder groups.

11 Empowering consumers

Key points

- Though having various rights, consumers also bear considerable responsibility for making prudent and informed choices.
 - But consumers' confidence and empowerment in markets can be weakened by poor information; behavioural or individual traits that limit good decision-making; and a limited individual capacity to affect consumer policy.
 - Accordingly, there are sound reasons for governments to promote consumer empowerment.
- In some markets, mandatory disclosure can improve the decisions of consumers.
 - However, disclosed information must be comprehensible and tested and designed properly to ensure that it actually assists consumers.
 - There should be greater 'layering' of information, allowing detailed information to be made available on request or via the Internet.
- Consumer education campaigns can augment information and advice available in the marketplace, but it can be difficult to reach consumers at risk at the time of purchase, and to prompt appropriate responses by them.
 - Greater evaluation and testing of such education initiatives would enhance their effectiveness.
- There is a case for additional government support to promote better consumer advocacy and to facilitate more research on consumer policy issues. Specifically, additional funding should be provided to:
 - support the basic operating costs of a representative national peak consumer body and the networking activities and policy functions of consumer advocacy groups;
 - establish a dedicated National Consumer Policy Research Centre to undertake policy-related research into consumer issues and to build expertise and research capacity in consumer policy matters; and
 - for contestable grants for research on specified consumer policy issues.
- Such support should be subject to governance arrangements that help ensure that taxpayer funding is used appropriately and effectively and that the national interest is appropriately represented.

11.1 Introduction

Confident and empowered consumers secure better outcomes for themselves and society as a whole:

- In an increasingly complex marketplace, empowered consumers should be better able to choose those products that match their preferences.
- Demand from empowered consumers can encourage firms to develop new and better products, boosting innovation and productivity.
- Educated and informed consumers are the first line of defence against poor behaviour by suppliers. This is important as it would not be feasible or sensible to use regulation to deal with all of the problems that consumers may face.
- When problems arise, empowered consumers, are more able to seek redress and avoid further detriment.
- Enabling effective consumer input to policy making should lead to better policies, and generate greater support for those policies.

While consumers have a range of rights, to a significant extent, it is their responsibility to take steps to become more confident and informed. To this end, consumers have access to a wide range of information and private help on products and services from a multitude of sources. Indeed, the development of the Internet has seen an explosion in the array of available information.

However, particular behavioural and individual traits of consumers (appendix B), inadequate or ineffective disclosure by businesses and the lack of voice consumers may have in consumer policy, can sometimes be barriers to empowerment. These barriers provide a basis for government policies explicitly targeted at facilitating more confident and able consumers.

This chapter looks at two key measures to enhance the information available to consumers — disclosure laws and consumer education initiatives. It then examines what is required to provide for effective consumer input into policy making and to ensure that policy development is underpinned by soundly-based research on consumers and consumer issues.

11.2 Disclosure issues

While more information is not always better, information provided by businesses nevertheless underpins consumers' judgments about the quality, risks and usefulness of competing goods and services. Businesses often have a commercial incentive to disclose such information, as consumers will tend to favour, and be

willing to pay more for, products they know more about. As Consumers Affairs Victoria commented to a recent review of food regulation:

More [mandated] standards, and more labelling, are not always the answer ... If consumers really want an attribute, and are prepared to pay more than it costs to supply, the market will generally supply it without government intervention. (quoted in VCEC 2007a, p. 153)

However, businesses will not always provide clear, sufficient or appropriate information to consumers. They may:

- sometimes seek to conceal their product's defects;
- provide information as part of a broader marketing package that aims to persuade rather than to facilitate consideration of competing products;
- provide too much or excessively confusing information to consumers. For example, electricity or telecommunications businesses often present complex information about multiple pricing options. At an extreme, the resulting confusion might work to benefit a large incumbent firm, thus weakening competition — so-called 'confusopoly' (Gans 2005); and
- face 'free rider' problems, which can dull incentives to provide some forms of information. For example, individual firms may have limited incentives to distribute generic information about an industry's product (such as the health benefits of fresh fruit) because other firms in the industry are likely to benefit without incurring any of the costs.

Markets are able to circumvent some of the limitations of individual firm's disclosure practices. For example, industry associations can share the costs of providing generic information, and third parties can sell independent and impartial comparative information or advice (as with Choice and many other private sector intermediaries).

However, governments may sometimes be able to resolve the limitations of disclosure by firms more efficiently through mandated disclosure requirements. Specific disclosure requirements have been mandated in relation to:

- *financial services* — those providing a financial product or giving financial advice must provide information about the product and any relationships or conflicts of interests they have with other providers;
- *consumer credit* — summary information about matters such as interest rates and penalty fees must be included at the front of all credit contracts;
- *food* — most foods must have nutritional information labels and warnings on the presence of allergens;

-
- *therapeutic goods* — most medicines must be labelled with advice or warnings (such as ‘keep out of reach of children’ and indications of side-effects);
 - *motor vehicles* — in New South Wales, for example, second hand car dealers must usually provide a list of defects excluded from statutory warranties; and
 - *real estate* — in most states and territories, real estate agents must disclose to clients the commissions and benefits they receive from a sale.

Disclosure requirements can be helpful to consumers

Disclosure requirements have two key advantages compared with more intrusive government intervention:

- Because they simply provide information to consumers, the final decision about whether to purchase a product remains with the consumer. This is in contrast to other regulatory options (such as product bans) that directly prevent consumers from making particular trade-offs or choices.
- Disclosure requirements do not prevent firms from providing new products or otherwise innovating. Nor do they prevent new firms from entering an industry, providing those firms meet disclosure requirements. And they do not preclude provision of additional information where this may be helpful and valued by consumers.

However, to be effective, consumers must be able to readily interpret and use the information disclosed. Accordingly, disclosure requirements work best when they are provided in a clear, comparable and comprehensible manner and highlight the salient features of a product. They must also be primarily designed to aid decision making by consumers rather than to merely provide legal protection for the supplier.

Disclosure requirements are not a panacea

Mandated information provision will not remove all consumer errors. Indeed, the costs of such errors provide incentives for consumers to carefully assess risks and to learn about products and markets. Accordingly, consumer errors should not necessarily be seen as problems warranting further government responses.

Even so, in situations where poor decisions can cause widespread, significant and/or irreversible damage (such as scams, health decisions or superannuation investments), the use of more directive policies, such as bans, licensing and mandatory standards, is often appropriate. In addition, text-based information will not generally be useful for consumers who lack literacy and numeracy skills. And disclosure may not adequately protect some disadvantaged and vulnerable

consumers who face limited choices among riskier products, such as ‘high cost’ lending (ASIC, sub. 103, p. 49).

Also, gathering and disseminating information can be costly. Designing it in a fashion that is most effective in improving consumer decisions often requires significant resources for testing, refining and monitoring its impact. And there are costs of the physical processes of printing and applying labels to consider. For instance, ACCORD Australasia (sub. 77, p. 7) indicated that labelling products to comply with unique Australian information requirements can involve multiple handling/repacking operations, with the total costs for some products amounting to millions of dollars.

The imposition of poorly crafted mandatory information requirements can also lead businesses to concentrate on strictly meeting their legal requirements rather than providing a better service or more effective information to customers. For example, some participants said that the disclosure requirements for financial products and services have led businesses to focus unduly on protecting themselves from liability, rather than helping consumers to protect themselves from poor financial decisions:

... a PDS [Product Disclosure Statement] for a typical managed investment or superannuation product is very likely to exceed 100 pages. This reflects the response of financial services providers to the regulator’s efforts to ensure that consumers have “complete disclosure”, essentially as a way of mitigating the financial service provider’s own risks. (Commonwealth Consumer Affairs Advisory Council, sub. 38, p. 16)

Indeed, when tied with licensing arrangements, some information disclosure requirements can actually prevent information from flowing to consumers. For example, a recent review of financial services regulation recognised that:

A front counter representative of a financial institution, who is permitted to provide only general advice, would be unable to offer basic useful advice to a client on the suitability of a product based on that client’s personal circumstances. Even though they may be well-placed to offer such guidance about suitability, that advice would constitute personal advice which they are not authorised to provide. (Treasury 2006a, p. 13)

Just as detailed requirements can skew business decision-making, poorly designed information requirements will not improve consumer decisions and, in some cases, can cause consumers to make worse decisions (ASIC, sub. 103, p. 13; Fung et. al. 2005, p. 2 and MCCA, sub. 75). For example, the latter observed that:

... sometimes consumers ignore or misinterpret the information provided. ... In addition, providing too much information can be counter productive. When faced with large amounts of complex and confusing information consumers often walk away from the market or stay with their current product or supplier, in effect choosing not to make a choice. (p. 11)

More specifically, according to ASIC (sub. 103, p. 17), the highly prescribed disclosure requirements of the Uniform Consumer Credit Code may not have improved consumers' understanding of financial products. (As discussed in chapter 5, there may be opportunities to beneficially streamline the disclosure and other requirements of the Code subsequent to the transfer of responsibility for regulating consumer credit to the national level.)

It may also be that the sort of decision making cues used by consumers to simplify choices in complex markets can be distorted if too much 'noise' or information makes identifying these cues difficult, or directs consumers to the wrong cues (Todd and Gigerenzer 2000 and appendix B). For instance, requirements for finance brokers to disclose their commissions and relationships with lenders can lead some consumers to focus unduly on the costs of these commissions, rather than on the interest rate, which is much more important for the total costs of a financial product (Lacko and Pappalardo 2007).

How can disclosure requirements be improved?

The preceding discussion serves to illustrate that disclosure must be carefully designed to benefit consumers. Its role and usefulness will depend on the context and nature of the transaction.

Numerous participants commented that many current mandatory disclosure requirements have not in fact been implemented in a sophisticated or helpful way (box 11.1). Principally, these participants argued that such regulation is predicated on a philosophy that 'more is better'. The sort of examples drawn to the Commission's attention — such as phone contracts running to hundreds of pages — leave little doubt that this is sometimes the case.

In the Commission's view, the design of information disclosure requirements could be significantly improved through:

- increased consumer testing to ensure information is comprehensible; and
- a more layered approach to information delivery, permitting firms to tailor the level of detail in the information provided to consumers' needs.

This is consistent with the principles-based approach suggested by ASIC (box 11.1).

Greater use of consumer testing

Most research indicates that decision-making is sensitive to how information is presented and the environment in which it is delivered (Sless and Tyers 2004).

Accordingly, implementing information disclosure requirements without first testing their impact on consumer behaviour may not produce the desired result or, even worse, be counter-productive.

Box 11.1 Participants' views on disclosure requirements

Many participants argued that there is currently an over-reliance on disclosure requirements:

There is a tendency for over reliance on disclosure as a 'fix it all' tool for empowering consumers. It is not just a question of providing consumers with information; information must be understood and able to be utilised. It is often a problem of receiving too much inaccessible information, as well as not enough appropriate information. (Joint Submission from WA Community Organisations, sub. 76, p. 11)

Some focused particularly on deficiencies in information disclosure in the financial services sector:

Failing to consider behavioural principles can be seen in the use of disclosure regimes in the financial services market. Not only are consumers highly unlikely to actually read complex and detailed disclosure documentation, other forms of disclosure, such as disclosure of conflict of interest, can have the opposite effect to that intended by raising trust rather than promoting caution. (Consumer Action Law Centre, sub. 94, p. 4)

Others recommended improvements in the implementation and design of disclosure requirements:

... greater efforts must be made to ensure that disclosure is accessible, relevant, timely, and comparable. In addition, policy makers should be conscious of the limitations of disclosure as a policy tool, and should not use disclosure as a replacement for more specific conduct and transaction regulation where that is needed to protect consumers. (Centre for Credit and Consumer Law, sub. 93, p. 1)

Indeed, some of these deficiencies have already been recognised by policymakers. As the Commonwealth Treasury recently commented in regard to financial services regulation:

The content requirements for the various disclosure documents are resulting in excessively lengthy and complex documents ... which are difficult to reconcile with the legislation's requirement that information be presented to consumers in a clear, concise and effective manner. (2005, pp. 1-2)

ASIC considered that principles-based disclosure requirements may be superior to prescriptive ones:

An alternative approach might be to move away from the current detailed but limited provisions to a broader, more principles-based disclosure regime, with more of the detail (where deemed necessary) being elaborated via regulations and/or administrative instruments such as policy statements and guidance notes. This approach has the potential to deliver much timelier responses to marketplace issues than one requiring legislative amendment. (sub. 103, p. 38)

Further, a previous review of the credit code disclosure requirements recommended lessening and clarifying the amount of summary information presented to consumers on the front of a credit contract (MCCA 1999 and KPMG 2000).

For example, since 2003, credit providers have been required to display a ‘comparison’ rate for fixed term loans, which is calculated using interest charges as well as most fees and other charges. This information was intended to improve consumers’ ability to differentiate between loans of different costs, especially as a part of the costs are often hidden in the fees and charges levied. However, a recent study found that, of people who had recently obtained a loan, only 28 per cent knew that the comparison rate enabled comparison among providers and only 16 per cent could identify that the rate included interest, fees, and charges (Ewing 2006, p. 57).

Even more starkly, a recent Federal Trade Commission study in the USA showed that the inclusion of information about mortgage broker costs actually reduced the number of consumers who could identify the lowest loan cost. Such disclosures were proposed in response to concerns that brokers were profiting by recommending higher cost loans to clients. However, while over 95 per cent of the consumers tested in a study of the proposed regulations correctly identified the lowest cost loan when the broker’s commission was not disclosed, only 49 to 71 per cent (depending on the type of disclosure used) were able to do so when the commissions were disclosed (Lacko and Pappalardo 2004).

It may of course be that such perverse outcomes can be addressed through associated education campaigns. For example, ASIC suggested that the ineffectual nature of some Australian information requirements reflects inadequate education and promotion initiatives by responsible authorities rather than a defect with the requirements themselves:

... neither the State and Territory governments responsible for administering these requirements, nor industry, have invested significant resources in promoting these requirements to consumers or educating the community about how to make the most of them. Promotional and educational activities are crucial to the success of such requirements. In other jurisdictions, where there has been more attention given to implementation and promotion, consumers appear to have benefited. (sub. DR174, p. 20)

Even so, there is substantial evidence that testing and related refinement processes can significantly improve consumers’ ability to find information and use it properly (box 11.2). As the Association of Superannuation Funds of Australia Ltd (ASFA) said:

One element that should be considered when developing consumer protection policy is to actually test the proposed policy prescription with real consumers. ASFA has found that consumer comprehension testing of sample disclosure documents is an invaluable tool in this regard. (sub. 70, p. 5)

Box 11.2 The results of consumer testing

Some recent studies of information requirements have used survey results to redesign labels or disclosure documents and, in doing so, have achieved much higher levels of consumer understanding.

ASFA funded a study of consumers' comprehension of a product disclosure statement for superannuation products. The study found that many consumers have difficulties dealing with information about superannuation.

Initially, only 10 per cent of consumers were able to correctly answer 90 per cent of the questions. Interview processes were used to reveal why consumers were making mistakes and this information was used to re-design the document. Some of the changes included clearly explaining superannuation terms; using worked examples when relying on percentages; including useful 'signposts' (such as a table of contents and logical headings); and including a checklist (effectively requiring consumers to answer guided 'homework' questions to increase their understanding). Following another round of testing and refinement, 40 per cent of consumers were able to correctly answer 90 per cent of the questions.

GlaxoSmithKline, a pharmaceuticals company, funded a study into the comprehension of its labels on a 24-pack of Panadol and used the results to improve the label. Using the old labelling, consumers were able to correctly comprehend and use the information 72 per cent of the time. Errors reflected the poor sequencing of information; long and cramped line lengths; lack of differentiation between different types of information; and unnecessary information. The label was subsequently redesigned and, with the new labels, consumers achieved a 'success rate' of 92 per cent.

A FTC study in the USA showed similar positive impacts from redesigning the presentation of information on mortgage costs. A group of 36 consumers were asked about their purchase of a recent mortgage, including the information they had gleaned from the disclosure documents. The insights from these interviews were used to create a different 'prototype' disclosure document. It focussed on the key mortgage costs that consumers need to understand when obtaining a loan — less important or confusing information was excluded. The costs were conveyed in simple, easy-to-understand language, and the form was organised and formatted so that the various costs could be easily recognised and identified. (Lacko and Pappalardo 2007, p. ES-4)

The revised form increased the percentage of consumers choosing the cheapest loan from 61 per cent to 80 per cent, with a greater improvement for more complex loans.

Sources: Ageing Agendas (2003), Sless and Tyers (2004) and Lacko and Pappalardo (2007).

Formal testing has in fact been adopted for some forms of labelling. In 2004, the TGA ruled that compliance with an industry-developed 'Labelling code of practice' would satisfy the performance-based requirements for labelling on non-prescription medicines (Bryan 2004). This code requires that all labels be tested on consumers. Only labels that enable 90 per cent of consumers to find information *and* correctly use what they find pass the test. If a label fails this test, it must be redesigned. In addition, ASIC has advised financial service providers that similar standards should be adopted for the 'product disclosure statement' (PDS).

Introducing a layered disclosure approach

Another approach for helping to improve consumer comprehension is to reduce the amount of information that is sometimes disclosed to consumers at the point of sale. Especially when purchasing financial services, consumers are often overloaded by disclosure documents. The length of these documents can run to hundreds of pages and, understandably, they often are unread or can hide important information from consumers. Highlighting the salient information at the point of sale (or in documents considered by consumers when deciding on a particular offering) would arguably allow consumers to make more informed choices. Such information could be provided in a summary document.

Detailed information may still be useful for intermediaries advising individual consumers and for firms that specialise in comparing different products from a consumer perspective. And although much of this information is unlikely to be useful for most consumers at the time of purchase, some may wish to use the information in the future. For example, many consumers will consult such documentation if they have a dispute or a query and wish to review their rights (Centre for Credit and Consumer Law, sub. 93, p. 23).

However, there will often be better ways of delivering this information to consumers than in long documents provided at the time of purchase. There is greater potential for providing much of what is currently included in some contract documents only on request, with the primary disclosure documents simply indicating how this other information can be accessed, both via online or through requested hardcopies. Importantly, recent amendments to the Corporations Law provide for some information currently required in product disclosure statements to be ‘incorporated by reference’ to a website. Chris Pearce, the then Parliamentary Secretary to the Treasurer, recently explained that these proposals:

... will allow financial service providers to include a brief description of the product in their product disclosure statements, together with references or links to other documents if the consumer wants more detailed information. This will not only save the service provider from having to supply sheaves of documentation — but the consumer from having to wade through it if they don’t need that level of detail. (2007, p. 4)

ASFA considered that these amendments provide a useful example of how layering can work in practice and that they have:

... the potential to reduce unnecessary complexity in the basic disclosure document while still providing consumers with the information necessary to make an informed decision. (sub. DR188, p. 4)

More broadly, the ability to provide and tailor information through electronic means, including interactive web pages and other web based tools, arguably offers more effective disclosure to individuals with access to a computer than present arrangements. By way of example, Suncorp highlighted current restrictions on electronic disclosure in insurance and banking services:

The principle issue regarding disclosure for insurers is that under the *Insurance Contracts Act* we are required to send the full insurance policy and schedule to the insured in writing. This has been interpreted (over 100s of years of common law) as meaning that we have to post the contract and schedule. Therefore we are *unable* to send the contract electronically - at present. Additionally we have to send full terms & conditions, which makes it rather difficult to produce a four page PDS ...

In terms of banking, we cannot provide electronic offer and acceptance for a State UCCC regulated mortgage or personal term loan. They still have to be paper-based. There are other issues for mortgages eg, some State titles office registries don't yet allow electronic lodgement, but the e-conveyancing project CoAG are supporting may progress this issue. (sub. DR256, p. 1)

What should be done?

The Commission strongly endorses the notion that the design of mandatory information requirements (particularly prescriptive obligations such as for certain financial services and credit products) should be based on prior consumer testing to improve consumers' understanding of disclosed information. The costs of such testing should be seen as an integral part of regulation development. Requirements should also be periodically evaluated after introduction to ensure that they are contributing to better consumer decision-making. That said, some exemptions from testing requirements may be warranted. This might be the case, for example, for relatively simple forms of disclosure (such as 'use by' or 'best before' requirements), and those for which sufficiently similar testing has already been undertaken, and lessons learned.

There should also be wider adoption of layering of complex information (also subject to market testing), particularly in the financial services area. That is, firms should initially only be required to provide agreed key information for consumers to plan or make a purchase, with more detailed information available by right either on request or by reference.

There was widespread support for these two requirements (as reflected in the draft report proposal) across a range of participants including the ANZ Banking Group (sub. DR178), ASFA (sub. DR188), ASIC (sub. DR174), the Council of the Aging over 50s (sub. DR120), the Law Council of Australia (sub. DR225), National Legal Aid (sub. DR220) and the Victorian Government (sub. DR226).

However, some stressed the importance of proper prior examination of whether mandatory information requirements are needed before considering how they should be designed. Optus (sub. DR173), for example, argued that criteria such as establishing market failure, benefits outweighing costs, regulation being the best course of action and the likelihood of mandated requirements being met, should inform the case for regulation in the first instance. In elaborating, Telstra (sub. DR156) suggested that better consumer education might sometimes obviate the need for mandated information and that a review of the effectiveness of a sample of such measures (see section 11.3) should precede the introduction of new disclosure requirements.

These and other participants also raised implementation issues such as which entity should be responsible for conducting the consumer testing and for the content (and amendment) of the information disclosed as a consequence. For example, ASIC (sub. DR174) said that the recent ‘incorporated by reference’ [to a website] amendments referred to above did not resolve whether the product issuer was actually responsible for the incorporated material. And the Australian Bankers Association (ABA) focused on the compliance costs associated with amending existing disclosure requirements.

... the ABA wishes to make the point that in going ahead with [the Commission’s proposed] reforms particular account should be taken of the compliance costs incurred by financial services institutions to date and any additional compliance costs that may be incurred in order to meet any reformed mandatory disclosure requirements. (sub. DR245, p. 25)

For its part, the Commission is encouraged by the broad consensus that: where a need for mandatory disclosure has been established (see chapter 3), it should be underpinned by the principles of proper consumer testing and the layering of information to improve consumer understanding of product features and risk. Indeed, it considers that these principles are also generally relevant to effective information provision, even when it is not mandated.

In the Commission’s view, the entity that should be responsible for consumer testing of proposed mandatory disclosure requirements will depend on the circumstances in which they are imposed. In some cases, for practical or other reasons (such as where the target audience is the broader community), it may be more appropriate for the regulator to undertake (and for taxpayers to fund) this task. In others, it may well be that firms should be made responsible for such testing — especially where the costs can and will be passed on to a distinct consumer cohort that benefits from the disclosed information. But in either case, it will be important that the regulatory development process clearly articulates the respective roles and responsibilities of regulators and businesses in this area and in determining issues

such as the precise content of disclosed information and the process for making necessary amendments.

RECOMMENDATION 11.1

Where a need for mandatory information disclosure requirements has been established, the regulator concerned should require that:

- *information is comprehensible, with the broad content, clarity and form of disclosure consumer tested prior to and/or after implementation, and amended as required, so that it facilitates good consumer decision-making; and*
- *complex information is layered, with businesses required to initially provide only agreed key information necessary for consumers to plan or make a purchase, with other more detailed information available (including by electronic means) by right on request or otherwise referenced.*

Also, the respective roles and responsibilities of regulators and businesses in regard to such matters as consumer testing, content and amendment should be understood and agreed at the outset.

Consistent with these principles, prospective reform of mandatory disclosure requirements for financial services should be progressed as a matter of urgency.

11.3 Consumer information and education initiatives

Government programs to disseminate consumer information, like disclosure requirements, seek to equip consumers with information to make better purchasing decisions. Such initiatives focus on matters such as improving financial literacy, providing information on consumer rights, access to remedies, avoiding scams (box 11.3) and how to buy certain broad types of products (such as superannuation).

Governments disseminate general consumer information through several channels. These include websites, publications, the media, direct mail, exhibitions, and via intermediaries such as financial lenders, retailers, schools and libraries. In addition, governments sometimes seek to improve consumers' capabilities through more formal education channels, such as through the provision of teaching resources on consumer rights to schools.

Challenges for campaign design

One challenge posed for the effectiveness of information/education campaigns is reaching those consumers who are most at risk. Information that is heavily reliant

on text or provided via the Internet may not be readily accessible for many disadvantaged people. Advertisements in the electronic media may overcome these problems, but are costly and cannot provide the same depth of advice. Another approach is to provide courses for disadvantaged groups — such as those on tenancy rights provided by Consumer Affairs Victoria. However, while courses can be tailored to meet different audience characteristics, they generally do not have as much reach as other information measures.

A second challenge is to reach consumers at the time they need the information. Unlike businesses, government agencies generally do not have a direct relationship with consumers, so they cannot use client databases or personal contact to furnish information to (all) relevant consumers.

Box 11.3 **Scams**

Scams designed to dupe consumers into handing over money for little or no return are continuously appearing, and have many different forms, including: international 'matchmaking', chain letters and pyramid schemes; 'get-rich-quick' investment scams; money transfer requests ('Nigerian' scams); and banking and online account scams. With the uptake of new technologies, scams are increasingly internationally-based and computer-related — the Internet offers a low cost means for scammers to reach large numbers of potential victims.

Many scams go unreported and consequently it is difficult to provide an accurate estimate of the consumer detriment associated with consumer fraud in Australia. However, it is likely to be significant: a survey carried out for Consumer Affairs Victoria indicated that there were 370 000 cases of scamming in Victoria in the 12 months to March 2006, involving almost \$130 million (CAV 2006a). And in 2007, the Queensland Police Service estimated that almost \$500 000 a month is sent by people in Queensland to 'Nigerian' email scammers (Queensland Police Service 2007).

Consumer fraud is proscribed under the Trade Practices Act and in each of the State and Territory Fair Trading Acts. Fraud relating to financial services is proscribed under the ASIC Act 2001. Since 2005, enforcement of the Federal, State and New Zealand unfair practices provisions has been coordinated through the Australasian Consumer Fraud Taskforce, which is a group of 18 government regulatory agencies and departments with responsibility for consumer protection regarding fraud and scams.

But legislation is only part of the answer. Most consumer fraud is perpetrated by fly-by-nighters and is increasingly internationally based, making it difficult for enforcement authorities to keep up with scams. And enforcement action can only be taken once scams have come to the authorities' attention, by which time consumers have suffered detriment. As such, the main weapon against scams is greater public awareness of their existence and forms, government education initiatives and media exposure.

Accordingly, indirect avenues often must be used. For example, Consumer Affairs Victoria indicated that it sometimes distributes information via intermediaries such as

finance lenders, estate agents and hardware stores to reach consumers at key points in their purchasing lifecycle and help them make better-informed purchasing decisions.

A third challenge is promoting consumer awareness and the effective use of the information provided:

- The combination of numerous competing messages and consumers' cognitive limitations and other behavioural tendencies (appendix B) means there is a risk that some information initiatives will be ignored by consumers, or misunderstood.
- Information provided by an education program may displace information from other sources, with little net impact on consumer understanding.

Finally, challenges arise in the design and use of so-called 'social marketing' in consumer policy (CAV 2006a). According to an information paper prepared for MCCA (sub. 75, p. 65):

Social marketing is a type of government policy response that responds to and capitalises on so called 'irrational' tendencies to lead to better societal outcomes. There are various examples of social marketing that appeal to people's sense of upholding social norms or 'doing the right thing' even if it is not in their short term best interest.

According to the Victorian Government, social marketing tools are used extensively in areas such as health promotion and have been recognised as an important means by which behavioural change can be achieved. It said:

A social marketing approach has the potential to deliver much better outcomes for consumers, since it is based on rigorous research and ongoing evaluation. It can also reduce consumer detriment as a result of voluntary changes among consumers or traders, reducing the need for more explicit regulation. (sub. DR226, p. 94)

However, the Victorian Government also acknowledged that social marketing can be costly (a point similarly raised by the Western Australian Department of Consumer and Employment Protection, sub. 99, p. 52), restricting the range of applications to which it is suited. And in the Commission's view, social marketing has other drawbacks as a tool for consumer empowerment, including that programs may not work as intended (see appendix B).

Evaluating campaigns

There is evidence that consumers access the sort of education material described above. For example:

- A recent Queensland Household Survey estimated that 81 per cent of Queensland's adult population had heard or read advice in the previous 6 months

from the Office of Fair Trading over ten key message areas delivered through awareness and education activities (Queensland Government, sub. 87, p. 59).

- The Victorian Government (sub. 72, p. 39) noted that, during the 2006 calendar year, the Consumer Affairs Victoria website received more than one million visits, making it one of the Government's most highly frequented websites.

But such data does not indicate whether the information was effective in improving consumer decisions.

There have been reasonably sophisticated evaluations of consumer information and education campaigns in some areas (Victorian Government, sub. 72, p. 42). High profile and expensive media-based education campaigns addressing issues such as smoking and drink driving, are particularly likely to be subject to sophisticated periodic evaluations.

Nonetheless, in overall terms, it is not clear that there has been sufficient evaluation of the existing suite of consumer information and education programs across Australia to be reasonably sure about what works best in particular circumstances.

What should be done?

Up until now, assessments of existing initiatives, and decisions about whether to introduce further initiatives, have largely been the prerogative of individual government departments and consumer regulators including those responsible for campaigns relating to particular areas of consumer activity (for example, food safety and financial services). As the ACCC (sub. 80, p. 145) argued, there are grounds for a more coordinated approach to consumer information and education initiatives.

An important element of such a coordinated approach should be an assessment of the effectiveness and prospects for improvement of a sample of consumer information campaigns and education programs across Australia, especially in areas where the benefits from changing consumer (or supplier) behaviour are likely to be the greatest. Such an evaluation should consider the same sort of issues that arise in relation to disclosure requirements, including their cost-effectiveness, best form, the advantages of layering, their usefulness to different types of consumers, and the feasibility of pilot studies and testing. An enhanced research program on consumer policy issues (section 11.5) would also contribute to the future development of more effective and relevant education initiatives.

There was a deal of support for these propositions as reflected in a recommendation in the Draft Report. As noted in section 11.2, Telstra (sub. DR156) considered such

evaluations as being particularly important in helping to minimise the need for mandatory disclosure requirements. Other supporters of better evaluation in this area included ASIC (sub. DR174), the Australian Bankers Association (sub. DR245), Law Council of Australia (sub. DR225) and Victorian Government (sub. DR226), with the latter suggesting that the proposed cross-jurisdictional evaluation could be undertaken by the recently formed National Education and Information Advisory Taskforce (NEIAT). Among other activities, the NEIAT will:

... establish and maintain an accessible bank of research, evaluations, strategies, campaign creative concepts, publications and other information that can assist other States in the development and implementation of their own education and information activities. (sub. DR226, p. 95)

The Commission considers that NEIAT would be an appropriate vehicle to progress the improvements to information and education campaigns it is proposing (see below).

Other participants called for such evaluations to give particular attention to the needs of certain groups including children and young people and vulnerable and disadvantaged consumers more generally. The National Children's and Youth Law Centre, for example, highlighted the issue of youth debt and the need to evaluate initiatives such as the proposed school-based financial literacy program (which is similar to programs operating in a number of other OECD countries). The Centre said that it:

... supports the development of the National Consumer and Financial Literacy Framework. This framework, endorsed by the Australian Education Systems Officials Committee on 4 November 2005, is due to be adopted by the school curriculum of all states and territories this year [2008]. The framework must be evaluated to ensure it is incorporated into [the] school curriculum and is effective in building skills and knowledge. (sub. DR196, p. 6)

And emphasising the importance of resourcing and presentation issues in the conduct of education campaigns, Anglicare Tasmania said that:

To be effective, consumer education campaigns must be adequately resourced and ongoing. Many consumer education campaigns run only for a short period, or in short bursts. Unfortunately, Anglicare financial counsellors advise that many people do not notice information unless they actually need it, and then, it may not be immediately available. The solution to this is to ensure that information is provided in as many different formats and locations as possible so that when people do need the information, it is easy for them to locate. (sub. DR191, p. 11)

The Commission considers that the appropriate focus for particular evaluations will depend on the goal of the education campaign concerned. However, the needs of specific groups and the relevance of mechanisms employed to target audiences will often be an integral part of such evaluations. It further notes that there will often be

scope to draw on the results of evaluation work by other stakeholders involved in these areas. One example was provided by the Redfern Legal Centre which said:

We should note that for many years now, our Credit and Debt Service has been running educational programmes on credit and debt-related matters, and has obtained evaluations from course participants. (sub. DR151, p. 6)

More generally, consultation with key stakeholders is a critical requirement for good evaluation outcomes.

RECOMMENDATION 11.2

Through the National Education and Information Advisory Taskforce, Australian Governments should commission a cross-jurisdictional evaluation of the effectiveness of a sample of consumer information and education measures, and the prospects for improving them. The evaluation should focus on campaigns in areas where the benefits from changing consumer (or supplier) behaviour are likely to be most significant. It should also include an evaluation of the proposed school-based financial literacy program, drawing on evidence from similar programs overseas.

11.4 Consumer input into policy making

Another element of consumer empowerment is the ability of consumers to influence government policies that affect them. Advocacy is one means of providing consumers with such influence. Most obviously, it can help to identify problems faced by consumers that may warrant government action (ASIC sub. 103, p. 70-72), and to ensure that policy makers properly consider the effects of policy proposals on consumers.

Several participants argued that robust consumer advocacy is also particularly important to counter what they perceived as the better-resourced and more powerful voice of business. For example, according to the Queensland Government (sub. 87, p. 43):

...without adequate consumer input, consumer affairs agencies risk being captured by the supply side on issues of regulatory burden, competitiveness and efficiency. This perspective is only one side of the story.

On the other hand, the recent Regulation Taskforce (2006) report pointed to several factors that can cause policy makers and regulators to give insufficient attention to business interests. Among other things, the Taskforce found that regulators face strong incentives to minimise the risk of criticism by politicians and the media for failing to protect consumers, and that while ‘pro-consumer’ outcomes commonly

feature in regulators' performance indicators, there are typically no equivalent performance indicators for the effects on business.

But whatever the balance of these competing incentives and disciplines, it is uncontroversial that the interests of consumers *should* be identified and accounted for in the development and administration of policies that materially affect them; and that the input of consumers or their representatives can aid efforts to achieve this.

Many consumer representatives and some State Governments argued that consumer input into consumer policy development should in fact be seen as a right, and pointed to statements to this effect by governments in Europe and by bodies such as the OECD and the United Nations. The Consumer Action Law Centre (sub. 94, pp. 64-5) stated:

Strong and effective consumer representation and advocacy is a very important element of the overall functioning of the consumer policy framework (and indeed of a functioning democracy).

However, several participants argued that consumer advocacy has been weak in recent years and that therefore consumers lack a sufficient voice in policy debates. Box 11.4 contains a selection of the concerns.

Do policy development and implementation procedures allow consumers to be heard?

A pre-requisite for consumers to have effective input into policy is that there are avenues via which consumer representatives can deliver such input.

Existing routes

Like people representing any set of interests, consumers or consumer groups can draw issues of concern to the attention of government in several ways. As well as dealing directly with their parliamentary representatives, they can make pre-budget submissions on government spending priorities, and participate in regulators' advisory groups and the boards of alternative dispute resolution schemes. And consumers and consumer organisations can raise issues in the media in order to increase the policy profile of the matters concerned.

Where a proposed policy change entails new or amended regulation, most jurisdictions have formal guidelines and procedures for assessing the merits of the proposal. Subject to certain triggers, these require a Regulation Impact Statement (RIS) to be prepared that, among other things, documents the impacts on consumers and the consultation undertaken with affected groups in developing the proposal.

Box 11.4 Some consumer and community organisations' concerns about current arrangements for consumer input into policy

The Consumers' Federation of Australia said:

In our view, while some governments, agencies and reviews do take a progressive approach to consumer participation in the policy process, many do not. There is not a consistent approach taken across all levels of government that adequately acknowledges the value of consumer participation, and demonstrates support for that participation. (sub. 83, p. 9)

The Consumer Action Law Centre commented:

A key missing link in Australian consumer policy is the inability for governments and other decision-makers to meaningfully consult consumer representatives. (sub. 94, p. 65)

The Joint Submission from WA Community Organisations noted:

There is currently a general lack of investment in consumer capacity in Australia. Consumers participate in research, policy development and monitoring from a significantly unequal position of power and resourcing compared to industry and government. (sub. 76, p. 4)

The Victorian Council of Social Services (VCOSS) argued:

While business interests are strongly represented in regulatory and policy debates, there is often a distinct lack of effective and coherent consumer voices. Where a strong consumer voice does exist (such as in energy policy, especially in Victoria), it is generally attributable to the presence of an industry-specific, fully funded consumer advocacy body. (sub. 91, p. 17)

Choice observed:

A large range of consumer organisations are regularly called upon by government agencies to provide evidence and advocacy to assist government policy development through submissions, informal consultations and formal representative arrangements. But most consumer organisations are funded to provide casework or advisory services rather than advocacy, or do not receive government funding at all ... (sub. 88, p. 51)

The Consumers' Telecommunications Network considered that:

At times, CTN has been extremely frustrated that our input to various policy decisions, via the public comment mechanisms, does not seem to be incorporated into the end policy. There is little transparency about why a certain decision is made and why, and what priorities guide certain decisions. (sub. 78, p. 35)

The Consumer Law Centre of ACT stated that:

The lack of an appropriately resourced and independent national consumer policy research and advocacy body has led to a lack of detailed qualitative and quantitative analysis in all areas of economic reform that have impacted consumers over the past 11 years. This has resulted in significant consumer detriment in the area of consumer credit and telecommunications in particular... (sub. 74, p. 8)

And TasCOSS mentioned that:

In the absence of a non-government generalist consumer advocacy body in Tasmania, and with an under-resourced State Office of Consumer Affairs and Fair Trading, TasCOSS introduced a dedicated part-time consumer policy officer position within our organisation in 2003. Through this position TasCOSS has taken an active role in consumer policy and has sought to establish, with several submissions to the State government for funding, an independent non-government consumer advocacy organisation in Tasmania. These have been unsuccessful. (sub. 32, p. 2)

In relation to the administration of regulation, a number of consumer consultative panels have been established to provide input to particular regulators and utilities. Examples at the Australian Government level include the Consumer Consultative Forum established under the *Australian Communications Authority Act 1997*, the ACCC's Consumer Consultative Committee and ASIC's Consumer Advisory Panel. And, at the State and Territory level, the Victorian Government has, for example, established a government-funded but independent organisation, Consumer Utilities Advocacy Centre, to 'ensure the interests of Victorian consumers are effectively represented in the policy and regulatory debate on electricity, gas and water.'

Further, several consumer organisations indicated that they are often pro-actively approached by governments (and sometimes industry bodies) to provide input into policy processes. For example, consumer representatives frequently serve on the boards of ombudsman offices.

Concerns

Despite these avenues, consumers have not always had opportunities to make meaningful policy input. For instance, the Australian Public Service Commission (2005) found that only one quarter of regulatory agencies surveyed actually consulted the public when developing regulations. And even then, concerns can arise about the nature of consultations. As the Consumers' Federation of Australia (sub. 83, pp. 9-10) said:

It is not uncommon for government departments and agencies to provide periods of less than a month to respond to often complex and detailed material. This does not provide sufficient time for even a well-resourced organisation to review material, collect evidence and formulate and finalise a response.

Interestingly, some of the concerns raised by consumer groups during this inquiry mirror concerns that business groups conveyed to the Regulation Taskforce. The Taskforce agreed that consultation practices were patchy, and recommended a number of improvements. Importantly, while the Taskforce's brief was to reduce unnecessary regulatory burdens on business, it indicated that there is a need for stakeholders generally to be properly consulted; not just business.

Recent and prospective reforms to regulatory consultation processes

In its response to the Regulation Taskforce's report, the Australian Government agreed to all its recommendations for enhanced consultation processes, indicating among other things, that it would:

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- develop a whole-of-government policy on consultation requirements;
 - require that all regulators establish standing consultative committees;
 - require policy ‘green papers’ and exposure drafts for matters of major significance; and
 - release Annual Regulatory Plans.

Such changes should improve opportunities for consumer input into Australian Government policy. Similar arrangements would also be appropriate at the state and territory level where they do not already exist.

Is there a case for greater government support for consumer policy advocacy?

As well as having *opportunities* to contribute to policy making, consumers or their representatives also need to have the *means* — time, money and know-how — if they are to make input that is effective.

It is difficult for individual consumers to represent themselves. While some do engage in policy forums — for example, a number of individuals made submissions to this inquiry — people normally leave it to others to represent their views as consumers, and/or may simply trust or hope that their interests as consumers are given due weight by those responsible for government policies.

There are numerous consumer advocacy groups in Australia. Many have been formed around specific industries or concerns. Examples are the Consumers’ Telecommunications Network, the Public Transport Users Association, the Consumers’ Health Forum, the Queensland Food Alliance, the Tenants’ Union of Victoria and the Australian Financial Counselling and Credit Reform Association. The Consumers’ Federation of Australia (CFA) is a national peak body for consumer groups in Australia, with membership of around one hundred organisations including legal centres, health rights groups, local consumer organisations and public interest bodies. The most well-known consumer group in Australia, however, is ‘Choice’ (formerly the Australian Consumers Association), which engages in advocacy across a range of consumer issues. Some organisations that provide front-line consumer assistance and counselling services — such as the Credit Legal Centre (NSW) Inc — also engage in some general policy advocacy.

Many consumer groups obtain resources for policy advocacy purposes predominantly from voluntary contributions (time or money) by individuals. In the case of Choice, it also obtains revenue from subscriptions and sales of its magazine,

which contains product tests and comparisons, and other advice for consumers. Government funding explicitly for the purposes of policy advocacy is limited.

Some consumer advocacy groups are able to attract sufficient resources to make cogent submissions and have an influence on public debate. For example, Choice receives no government funding and yet is able to make high quality and influential contributions on a range of policy matters.

However, a number of consumer advocacy groups argued that they, or the consumer movement generally, lack sufficient resources to adequately represent consumer interests in policy forums. Indeed, as evidenced by their difficulties in participating in this inquiry, it is clear that many consumer groups are stretched. For example, the CFA indicated that it was unable to address all the issues raised in the Commission's issues paper; some consumer representatives said that they had put together their submissions in spare time 'around a kitchen table'; and some struggled to get the time to attend the public hearings.

These challenges for consumer organisations are not made easier by the growing complexity of consumer policy issues, which in turn demand greater sophistication from those engaged in policy processes. Where consumer advocacy groups lack resources, the result is likely to be overworked staff and weakened capacity for research and detailed policy analysis. As noted by ASIC (sub. 103, p. 72):

We increasingly find that in the current environment, consumer and/or welfare legal centres and financial counselling agencies do not have sufficient resources to provide policy input or even provide us with data about their case work. Quality consumer research about consumers' experiences that identifies issues and policy options and provides data about the consumer benefit and detriment of proposals can't be fully effective unless researchers can access this information. We think there is a real need to resource frontline agencies with policy capability ...

The Commission's proposal to increase funding for legal aid and other frontline individual consumer advocacy services (chapter 9) would help in this regard, but the resourcing issue is also relevant to consumer advocacy groups more generally.

Why can't some consumer groups attract sufficient resources?

Even though consumers in aggregate might place a high value on consumer advocacy, each individual consumer has an incentive to 'free ride' on the contributions of others, meaning that consumer organisations may find it difficult to attract commensurate resources — whether in the form of volunteered time or donated money — from them. As the former Australian Federation of Consumer Organisations President, Robin Brown, pointed out:

The benefits of participation in advocacy are often seen to fall well below the costs. This is largely due to the “collective action problem” So, where public policy and regulation should reflect a diffuse public interest, members of the community at large will, not unreasonably, question why they should devote a lot of time and energy with everyone else “free riding” on their efforts. (sub. 63, p. 19)

Free rider problems are not as pervasive for business representative organisations, where interests tend to be more focussed and organisation easier.

The difficulties that consumer organisations experience in attracting greater funding for policy advocacy from its intended beneficiaries might also partly reflect that consumers do not see such representation as a high priority, and/or that they consider that their views and interests are already represented to a reasonable degree.

Another possible contributing factor mentioned in some submissions is that consumer organisations may be perceived as not always representing all consumer interests well. For example, the Brotherhood of St Lawrence (sub. 47, p. 5) argued that consumer organisations tend to be exposed to the problems of some groups of consumers more than others, which can bias their perception of consumer needs and, in turn, skew their advocacy activities. Similarly, Laurie Malone (a former president of AFCO) contended that, in the past, some consumer organisations had pursued agendas that did not necessarily align with the views of most consumers and that this had contributed to a withdrawal of government support (sub. 4, p. 2).

Also, the Western Australian Department of Consumer and Employment Protection, (sub. 99, p. 32), said that the formula used by governments to resource front-line consumer organisations ties funding to service delivery, rather than policy advocacy.

Should governments provide more funding?

Whatever the precise cause of the resourcing difficulties faced by many consumer policy advocates, the Commission accepts that there is a general case for governments to help ensure that consumer representatives have the financial wherewithal to make an effective input into policy. The free rider problem alone provides a prima facie rationale for government to consider assistance for such bodies. Further, many consumer groups and representatives are clearly overloaded at present, hampering their input into policy processes.

This might not matter were there sufficient consumer input on relevant issues. However, this is not always the case. For example, the Western Australian Department of Consumer and Employment Protection stated:

Certainly there have been examples in the recent past within Australia where the lack of an independent, resourced and co-ordinated consumer voice has hampered public

policy development (for example retail trading hours debates in Western Australia and home warranty insurance debates throughout Australia subsequent to the collapse of HIH Insurance in 2001). (sub. 99, p. 35).

Further, at least one major consumer organisation — Choice — indicated that it had been unable to meet some requests from government agencies for input on specific policy matters due to a lack of resources. It stated:

This demand for our input demonstrates a real need expressed by government and parliamentary inquiries for consumer advocacy. It is time that appropriate advocacy was funded at a level sufficient to meet this need. (sub. 88, p. 51)

The Commission understands that, at times, other consumer advocates have similarly had to decline such requests.

It is of course very difficult to judge the precise degree to which policy development has been hampered by insufficient consumer input. Some reforms of major benefit to consumers have been undertaken in recent years without significant specific input from most consumer groups. Indeed, consumers are the ultimate intended beneficiaries of most economic reforms.

Nonetheless, the Commission considers that there would potentially be net benefits from the provision of additional taxpayer resources for consumer advocacy provided there are means of ensuring that it generates advocacy that is appropriately representative and that benefits significant numbers of consumers.

Defining the scope of publicly-funded consumer advocacy

Which consumers' views should be represented?

Consumers are diverse, and the interests of different sub-groups of consumers will at times conflict. For example, some regulatory measures intended to assist disadvantaged consumers may inadvertently harm other consumers. This makes it difficult to present a single consumer perspective on such issues.

Most consumer groups in Australia focus particularly on the interests of disadvantaged consumers. For example, the CFA's objective is 'to promote the interests of consumers, in particular low income and disadvantaged consumers', and the Consumer Utilities Advocacy Centre (CUAC) sees itself as representing 'the interests of Victorian electricity, gas and water consumers — especially low income, disadvantaged, rural and regional, and Indigenous consumers'. Moreover, although the readers of Choice tend not to be low income or vulnerable consumers, Choice has 'recognised the responsibility it carries for taking on rights related

advocacy, by maintaining limited numbers of highly effective specialist policy staff' (Tennant 2005).

Clearly, representing the interests of low income and disadvantaged consumers is important. Disadvantaged consumers will often be the ones most in need of effective representation in the policymaking process, yet are also less likely to have the financial capacity to contribute.

However, it is no less important that the much larger number of other consumers are represented in policy processes, and that proper account is taken of any conflicts between the interests of different sub-groups of consumers. The 'free rider' problem that gives rise to a case for some public funding of consumer advocacy affects consumers at all levels. In this sense, the model adopted for disbursing public funding for consumer advocacy should seek to ensure that the advocacy supported is reasonably representative of the diversity of consumers' interests.

What perspectives are relevant?

One matter mentioned above that may bear on governments' support for consumer advocacy is a perception that they are 'partisan'. But as Choice pointed out, there is a distinction between putting forward the perspective of consumers and taking a politically partisan perspective. In its submission, Choice stated:

... the purpose of consumer advocacy is to transparently work in the interests of consumers generally or a defined class of them (for example low income communication users in the case of the Consumers Telecommunications Network). Effective consumer advocacy is focused on the broader public interest and often clashes with the immediate interest of producer groups, and where they are trying to satisfy producer groups, the interests of political parties. In short there will often be times when consumer advocacy is at odds with government policy but should never be politically partisan. (Choice, sub. 88, p. 51)

Equally, it is important that (publicly funded) consumer advocacy groups focus on the interests of consumers *as consumers*. People have views on numerous matters, including jobs, material living standards, equity, welfare, the environment, and national security, and what balance to strike between these areas where they conflict. Many interest groups seek to represent people's perspectives on these issues. But generally these issues are not consumer issues per se, even though, at the margin, some bear on people as consumers.

The Victorian Government (sub. DR226, p. 98) took issue with this observation noting that different organisations will have different views of what defines consumer policy and that this diversity of views is one of the benefits from having a broad range of stakeholders. While the Commission certainly agrees that such

diversity is a valuable underpinning for good policy input, there needs to be a limit to what should usefully be considered relevant consumer issues — especially if all or some of the funding for the advocacy functions concerned is provided by the taxpayer.

Accordingly, the Commission considers that publicly funded consumer advocacy should focus on core consumer issues and should not be dispersed too widely across other public interest issues. More focussed advocacy may also make government support more sustainable and less susceptible to revisions over the longer term.

Institutional and funding models for supporting appropriate consumer advocacy are discussed in section 11.6.

11.5 Consumer policy research needs

This inquiry has highlighted that significant information gaps exist in a range of areas relevant to the nature of the consumer policy framework and its specific requirements. A better information base is therefore a key pre-requisite for good policymaking in the future. Accordingly, the Commission considers there is a strong *prima facie* case for increased government funding for consumer research.

A number of bodies within Australia currently undertake or commission some research on consumer issues. These include government departments dealing with specific consumer issues, consumer regulators and MCCA. For example:

- Consumer Affairs Victoria has been very active in this area, undertaking several major consumer surveys on key policy issues, and commissioning or undertaking research into alternative dispute resolution and disadvantaged and vulnerable consumers.
- Research is also conducted or commissioned by some government-funded consumer advocacy bodies, such as the Victorian CUAC and the Western Australian Consumer Utilities Project.
- Some academic bodies specialise in consumer research, including the Griffith University Centre for Credit and Consumer Law and the recently established Centre of Advanced Consumer Research within the University of Western Australia.
- Finally, community-based consumer groups can themselves undertake or sponsor some research on consumer issues.

Even so, the overall quantum of research undertaken is quite limited and often takes a state rather than a national perspective. Furthermore, the results are not always

disseminated as effectively as they could be. Nor does there appear to be a coherent process for gathering together and disseminating the lessons from the considerable research on consumer behaviour that is undertaken in other countries.

During this inquiry, participants (and other observers) made a number of specific research suggestions often linked to particular regulatory proposals (see box 11.5). However, at a broad level, some major gaps in the knowledge base necessary for good policymaking include:

- the extent and nature of problems of consumer detriment (chapter 14) with one example being the incidence and cost of product-related injuries (chapter 8);
- the relative merits of different approaches and tools for addressing consumer problems, including the effectiveness of consumer information and education campaigns (section 11.3) and how consumers respond to different types of disclosure; and
- the determinants and changing nature of vulnerability and disadvantage and how the needs of these consumers might be best addressed (chapter 12).

And while there has been significant research that establishes the existence of various cognitive limitations and behavioural biases within the population, there has been less research on the extent to which consumers compensate for these through rules of thumb and learning. There is also an insufficient understanding of where regulation, education or social marketing campaigns can be most effective in exploiting or overcoming behavioural biases and, in particular, what the lessons from behavioural economics imply in this regard. As the submission from Louise Sylvan (Deputy Chair of the ACCC) noted:

While not a ‘silver bullet’, the empirical and evidence-based approach of behavioural economics will assist in producing consumer empowerment strategies that actually work. (sub. DR253, p. 3)

11.6 Institutional arrangements for funding consumer advocacy and research

As discussed in appendix C, there are several public funding models around the world for promoting consumer input into policy development. Such variation suggests that there is no obvious standout model. Rather, the arrangements in each country typically depend on historical developments and are contingent on each country’s system of government and consumer policy framework. These considerations are also relevant for assessing which approach or mix of approaches would be most appropriate for Australia.

Box 11.5 Some participants' suggestions for further research

A menu of specific research topics were proposed by participants (see below). The Commission is not in a position to endorse any of these particular suggestions, or the policy interventions that some are designed to underpin. Indeed, it may be that soundly based research in these areas, including the assessment of alternatives, would indicate that intervention is unwarranted. But these suggestions nonetheless indicate that there is a broad agenda of matters where further research may be beneficial.

Impact on purchasing decisions of incentive-based remuneration structures

According to Choice, the changing nature of consumer markets has heightened the need to look at the impact of conflicts of interest between producers and consumers on the quality of advice given to consumers:

Conflicts of interest ... become more prevalent in markets characterised by intermediaries, such as health professionals, accountants, mortgage brokers, financial advisers etc. Such markets are now more prevalent at the retail level (eg mortgage brokers had very little market presence 10-15 years ago). (sub. DR194, p. 6)

Effectiveness of credit disclosures

GE Money argued that:

... its not clear there has been sufficient research into how credit disclosures in documents can be made more effective, what information drives consumer choice and whether recent reforms (such as the Australian Capital Territory's reforms on unsolicited credit limit increases) have been effective to achieve their stated goals. (sub. DR208, p. 3)

Costs and benefits of more widespread unit pricing requirements

The Queensland Consumers Association (sub. DR123, pp. 2-3) noted that Australian retailers are not currently required to provide unit pricing information for most pre-packaged supermarket items. It argued that the introduction of a mandatory national unit pricing system would simplify consumer choice, result in major financial and time savings for many consumers and promote competition between suppliers.

Equity implications of price discrimination

FEMAG (sub. DR122, p. 5) said the practice of price discrimination among different groups of consumers is now widespread and the extent to which vulnerable and disadvantaged consumers are affected by this practice needs to be assessed.

Particular policy lessons from behavioural economics

FEMAG (sub. DR122, p. 9) commented that more research effort is needed on whether the insights from behavioural economics imply that there should be a wider role for proscription of certain market practices such as bait advertising.

Benefits and costs of giving a greater emphasis to demand-side analysis

The Joint Consumer Groups (sub. DR228, pp. 10-12) and Louise Sylvan (sub. DR253, pp. 3-4) called for ongoing analysis of consumer outcomes in specific markets (a demand side perspective) and the adequacy of regulatory and other requirements in areas where structural or behavioural barriers to competition are causing consumer detriment.

A National Consumer Council or similar body

A number of consumer advocacy bodies including Choice (sub. 88), FEMAG (trans., pp. 968-9) and the Victorian Government (sub. DR226) supported the establishment in Australia of a body like the UK's National Consumer Council (NCC). Several variants on the NCC model were also suggested. For example, VCOSS (sub. 91) advocated a model based on the Victorian Government's Consumer Utilities Advocacy Council.

The NCC is an autonomous public body that is tasked with promoting the interests of consumers through research, supporting consumer representatives and working with decision-makers to campaign for change. It is also a designated consumer group under the UK super complaint mechanism (see chapter 9). The UK Government appoints the Council's board and provides around three quarters of its funding in the form of a grant. The Council's budget in 2005-06 was £3.5 million and it employed around 50 staff. The Council has no statutory powers and does not give advice to consumers. Nor does it intervene in individual cases or consumer complaints.

The creation of such a body in Australia could have several advantages including that:

- it could develop an authoritative voice that would not be easily ignored;
- it would be able to act independently to raise awareness of consumer issues and to campaign for policy change;
- it would provide opportunities to concentrate consumer expertise and build staff know-how;
- it could represent a 'one stop shop' for government agencies seeking consumer input, and would become skilled at interceding effectively with those agencies and other policy makers on behalf of consumers;
- it would have the resources and independence to proactively commission or conduct research into a broad range of consumer policy issues; and
- as a centralised body, its operations should reduce the risk of duplication of research efforts that might occur under a more diffuse model.

That said, some of the mooted benefits of this model are not exclusive to it. As evidenced by the activities of Choice, consumer groups can already operate proactively, provided they have sufficient resources. Similarly, it should not require the creation of a central bureaucracy to coordinate, and limit duplication of, research efforts.

Further, aside from the costs of establishing such a body, the approach has some potential downsides. For example, were the body to crowd out existing consumer groups in policy processes, it could reduce the range of perspectives brought to bear in decision making. There is also a risk that such a publicly supported body might become diverted from core consumer issues. In this context, in addition to its considerable research and advocacy on core consumer issues, the NCC itself has recently ventured into areas such as a ‘green bill of rights’ and industry measures to address carbon emissions. As noted earlier, the Victorian Government (sub. DR226) indicated that there is no clear cut delineation between ‘consumer’ and other issues. Clearly, however, the diversion of resources into wider matters will reduce the resources available for core consumer issues.

The likelihood of such outcomes, and the significance of the costs entailed, were downplayed by some participants (see, for example, Choice, sub. DR194 and FEMAG, trans., p. 969). And the Commission acknowledges that the potential for these kinds of problems to emerge can be mitigated through appropriately designed governance arrangements and operational guidelines.

Even so, the risks were a concern for some participants. For example, the submission from the Council of the Ageing over 50s said that:

... the establishment of a ‘super advocacy body ... would not be appropriate’ ... as there is a major risk that the needs of specialized groups of consumers (in our case, disadvantaged or vulnerable older Australians) would receive insufficient attention. (sub. DR120, p. 2)

Notably, MCCA has considered calls for establishing an NCC-like body in Australia but, at least at this stage, has not supported it.

Funding to improve existing advocacy structures

With the benefits of ‘national’ coordination and representation in mind, an alternative, less far-reaching option would be to provide more modest funding to improve the existing advocacy infrastructure in Australia. This would involve funding to assist a peak body to represent consumers and/or consumer organisations, and to facilitate networking among advocacy groups. Such an approach could be complemented by dedicated and separate funding for consumer research (see below).

In its submission, the CFA supported this sort of approach, stating that:

[T]he Commonwealth Government commit to funding a peak body for consumer organisations. Funding should be sufficient to employ a staff including at least, a CEO, a communications manager, a network manager, 2-3 policy officers and administrative

support. The body should have a strong advocacy role based on a mandate from members. (sub. 83, p. 16)

Similarly, drawing on the findings of a recent survey of around 40 consumer advocates, commissioned on behalf of the ASIC Consumer Advisory Panel, the Consumer Action Law Centre (sub. 94, p. 65) said:

...there was overwhelming and unequivocal support for funding a peak body to represent consumer organisations from around Australia. ... A peak body with appropriate funding would be in a position to work across four key areas: policy advocacy; networking and information sharing; coordinating consumer representation; and developing best practice models.

The peak body could also play a role in improving networking arrangements among individual consumer organisations to enable more informed contributions to policy processes and ensure that the national interest is appropriately represented. During this inquiry, it has been apparent to the Commission that there is currently a lack of capacity to consolidate and share the many lessons learned by the various frontline consumer groups (including community legal aid centres and financial counsellors) that provide legal or other advice to consumers. Networking could be assisted in a number of ways, such as through support for attendance at conferences and for research that synthesises and disseminates the experiences of frontline agencies.

Relative to the NCC model, this approach would involve less disruption to current advocacy mechanisms and thereby a lesser likelihood of crowding out the views of existing consumer groups. That said, it would potentially forgo the benefits of consolidation of expertise within a single body and economies of scope across the range of advocacy activities. And without effective governance arrangements, it may be no more effective in guarding against inappropriate diffusion of consumer advocacy effort across a broader suite of public interest issues.

Funding for consumer research and policy input

Similarly, as an alternative to the in-house provision of consumer research functions (or contracting-out) by a multifunctional NCC-style body, a designated pool of funding could be made generally available in the form of contestable grants tied to specified outputs. Grants could be provided for:

- the preparation of complex policy input on specific issues; and
- general research undertaken to enhance understanding of consumer behaviour and/or to meet particular policy information needs.

The main advantage of contestable funding is that it would promote competition and diversity in the market for research ideas. That is, it would be open to any group

— whether a peak consumer body, a specialised consumer advocacy organisation, a frontline consumer service delivery body, an academic institution, a government department or private consultancy — to apply for funding based on credentials and activity, rather than restricting funding to a pre-selected organisation. It might also be easier to establish governance arrangements to prevent funds being expended on research on non-core issues.

The main disadvantage of the contestable funding approach is that it could result in support being spread too thinly and thereby inhibit the development of a critical mass of expertise and the ability to capture other associated economies of scale and scope in undertaking consumer research. The administrative costs involved in establishing a body to assess the merits of applications and disburse funding, and for consumer organisations to prepare those applications, could also be significant relative to the amount of funding provided.

Yet another option (explored further below) would be to fund a dedicated consumer research centre. In effect, this would be akin to an NCC body but without the advocacy functions. And to facilitate some contestability in the allocation of research funding, it would be possible to provide such a centre with a base level of funding, but require it to compete with other consumer research providers for an additional funding pool.

The Draft Report proposal

In the Draft Report, the Commission concluded that there was a case for modest additional government funding for consumer advocacy and research and that this should be provided through existing structures. Specifically, it proposed that the basic operating costs of a peak national consumer body and the networking and policy functions of consumer groups be supported, as well as specified research on consumer policy issues with that funding component distributed on a contestable basis. The Commission argued that such an approach could deliver many of the benefits potentially available from the creation of an NCC-type body, but without some of the attendant costs and risks.

There was considerable support for the proposal among business interests, complaint handling bodies and advocacy groups with Legal Aid Queensland, for example, endorsing it:

... as an appropriate role for government in strengthening the consumer policy framework by funding evaluation, research and assisting to ensure strong consumer advocacy (sub. DR202, p. 4)

But there were some concerns about the Commission's emphasis on modest additional funding support. The Financial Counsellors Association of Queensland (sub. DR134, p. 4), for example, held that modest funding would only maintain consumer groups in a 'survival mode', while Dr Luke Nottage (sub. DR114, p. 13) referred to the significant support received by agencies such as Standards Australia.

And in suggesting the Commission reconsider the NCC approach, others voiced concerns about the dispersion of research funding under a contestable arrangement. For example, Legal Aid New South Wales (sub. DR215, p. 3), said that contestable funding '... will not provide the infrastructure to close the current gaps in consumer input into policy development.' Choice, similarly argued:

While in general a contestable research funding program offers transparency and may support innovation, on its own it will not provide a source of coherent, engaged and independent policy advice that is most required. (sub. DR194, p. 9)

Also, as noted above, several participants contended that the Commission had overstated the risks that a NCC-type body would crowd-out specialist perspectives or inappropriately venture into peripheral consumer areas.

An intermediate approach seems most appropriate

In considering the most appropriate institutional arrangements for funding consumer advocacy and research, there are clearly trade-offs between the proposal put forward in the Draft Report and an NCC-style arrangement. As noted earlier, the NCC model has some attractions.

However, in seeking better advocacy outcomes, the Commission remains of the view that there would be advantages of working within existing structures. In particular, it is not convinced that making a single new publicly funded body primarily responsible for consumer advocacy would ensure that the full range of consumer perspectives continued to be adequately represented.

But in the case of research, the commentary on the Draft Report and the extent and nature of current gaps in this area, have caused the Commission to reconsider whether a purely contestable funding arrangement is the most appropriate way forward. It accepts that the capacity to build expertise and capture other related economies of scale and scope under a consolidated funding model would be a significant advantage. Hence, it is recommending the establishment and funding of a dedicated National Consumer Policy Research Centre (NCPRC) to conduct policy-related research into consumer issues. The Centre's broad research agenda should be informed by advice from the Australian Government regarding its priorities in the consumer sphere. However, that agenda should also draw on input

from MCCA, the revamped Commonwealth Consumer Affairs Advisory Council (see chapter 6) and other relevant stakeholders.

At the same time, the Commission continues to see valuable benefits (and disciplines) in retaining an element of contestability in taxpayer support for research in the consumer policy area. Accordingly, it is recommending that funding should be provided in two pools — a larger base funding component to support the establishment and operation of the NCPRC and a second contestable funding pool to support research on specified consumer policy issues. This same funding model is adopted for a range of other publicly funded research agencies in Australia and internationally. The effectiveness of the NCPRC in delivering beneficial consumer research policy outcomes should be reviewed after 5 years.

As to funding levels, the Commission is not in a position to specify a precise quantum of support for either the advocacy or research proposals:

- With regard to the advocacy component, the Commission acknowledges that the funding allocation needs to be sufficient to support improved outcomes in this area. However, it remains of the view that significant improvements can be achieved through relatively modest funding increments.
- In the case of the research component, a range of operational features of the research centre including staffing, infrastructure, governance arrangements and location will require further development.

The relative contributions by the Australian and State and Territory Governments will also need to be determined.

The Commission considers that within the broad implementation arrangements agreed to by CoAG for changes to the consumer policy framework (see chapter 6), the Australian Government should take the lead role in developing an agreed position on these matters.

Finally, in both the research and advocacy areas, the new funding arrangements should be subject to appropriate guidelines and governance requirements to help ensure that taxpayer support is used properly and effectively and directed at priority areas so that the national interest is best served and appropriately represented.

RECOMMENDATION 11.3

Within the broader consumer policy implementation framework agreed to by CoAG, the Australian Government, in consultation with MCCA, should take the lead role in developing arrangements to provide additional public funding to:

- ***help support the basic operating costs of a representative national peak consumer body;***

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- *assist the networking and policy functions of general consumer advocacy groups; and*
 - *enable an expansion in policy-related consumer research.*

Part of the latter funding component should be used to establish and support the operation of a dedicated National Consumer Policy Research Centre (NCPRC), with the remainder provided as contestable grants for research on specified consumer policy issues. An independent review of the effectiveness of the NCPRC in delivering beneficial research outcomes should be conducted after 5 years.

The new funding arrangements should be subject to appropriate guidelines and governance requirements to help ensure that taxpayer support contributes to high quality advocacy and policy research in priority areas, and that the national interest is appropriately represented.

12 Vulnerable and disadvantaged consumers

Key points

- A *disadvantaged* consumer is a person whose ongoing attributes or circumstances, such as poor education and low income, cause a continuing susceptibility to detriment. Disadvantage is persistent and hard to change (through consumer policy).
- *Vulnerability* is a broader term relating to the susceptibility of consumers to detriment because of their personal characteristics (such as disadvantage) or the specific context in which they find themselves (such as, purchasing goods or services at times of emotional stress, or for which the quality is difficult to ascertain).
- The Commission's recommendations in this report are aimed at improving outcomes for consumers, generally. However, some recommendations should be of particular benefit to vulnerable and disadvantaged consumers (such as those relating to credit market reform, unfair contract terms, improved access to redress, more user-friendly disclosure statements and enhanced resources for legal aid, financial counselling and advocacy).
- Looking to the future, consumer policy makers will need to monitor developments affecting the extent and sources of vulnerability and disadvantage (such as ageing of the population, the increasing importance of young consumers, and the growth of electronic commerce), and what this means for policy settings. Also:
 - more research on the behavioural responses of vulnerable and disadvantaged consumers is warranted; and
 - there could be a greater role for specific strategies to deal with the circumstances of some vulnerable and disadvantaged groups (as are already employed in the Indigenous consumer area).

In setting out objectives for the future consumer policy framework, the Commission has emphasised the importance of considering the needs of those consumers who are likely to be most vulnerable, or at the greatest disadvantage (see chapter 3). How the current consumer policy framework addresses these needs, and the scope for improvement, are discussed below. Some participants comments are provided in box 12.1.

Box 12.1 Participants' comments about vulnerable and disadvantaged consumers**Eastern Access Community Health (sub. 56, p. 2)**

Well-informed consumers are largely absent from the markets in which low income, disadvantaged and vulnerable consumers participate.

Choice (sub. 88, p. 72)

A policy approach which focuses on actual consumer behaviour, choice-making and preferences will better identify situations of potential consumer risk and detriment, in particular for vulnerable and disadvantaged consumers.

Legal Aid Queensland (sub. 51, p. 3)

... disadvantaged consumers are most likely to be assisted by legislative regimes which tip the balance in their favour to overcome inequality of bargaining power (for example reasonable cooling off periods) and by external dispute resolution schemes which provide real redress without the need for litigation.

Consumers' Federation of Australia (sub. 83, p. 5)

It may not be possible to design consumer policy that meets the needs of all consumers, including the marginalised and the vulnerable. If this is the case, there are difficult issues to grapple with in a policy sense, including whose interests should prevail if a proposed policy response benefits one group of consumers, but does not benefit, or even harms, another.

Origin Energy (sub. 31, p. 21)

... the terms 'vulnerable' and 'disadvantaged'... are close to impossible to define, which then renders certain targeted policy mechanisms unworkable. This is how we have ended up with over-coverage of policy approaches such as price controls.

Foresters ANA Mutual Society (sub. 36, p. 2)

... financial exclusion of low income consumers as it relates to an inability to access small, short-term credit at reasonable rates and on reasonable repayment terms, is a failure of competition.

Australian Securities and Investments Commission (sub. 103, p. 56)

... the use of promissory notes and other bills facilities to evade the UCCC is widespread in Western Australia where credit providers target indigenous consumers with low levels of financial literacy who do not have access to mainstream credit because of their disadvantaged economic situation.

The National Legal Aid Secretariat (sub. DR220, p. 2)

The consumer experiences of people living in poverty are characterised by: limited consumer choices; an urgent requirement to enter into transactions to provide for their basic needs; participation in markets which other consumers avoid; and a lack of market based solutions to address their needs.

Wesley Community Legal Service (sub. 37, p. 6)

The examples of predatory lending practices outlined [in our submission] would be abhorrent to the vast majority of the population... Very few people are aware of the current situation where the poor are being charged over 100 per cent per annum on loans.

12.1 What is consumer vulnerability and disadvantage?

As noted in chapter 1 (box 1.1) *disadvantage* can be seen as reflecting a set of individual traits — such as poverty, low education, disability, or poor English proficiency — that increase the risk of a consumer experiencing detriment or/and intensify the adverse consequences of that detriment. Disadvantage is typically persistent and hard to change, particularly through consumer policy.

Vulnerability is a broader term relating to a particular susceptibility of consumers to detriment based on both their personal characteristics (including, but not limited to disadvantage) and the specific context in which they find themselves (market features, product qualities, the nature of the transaction, the regulatory environment).

Disadvantage and vulnerability often overlap, but they can be distinct. For instance, in markets where the quality of services is hard to discern and convey to consumers, many will be vulnerable, despite not being disadvantaged. Conversely, for straightforward purchases, it is possible that someone who might be categorised as disadvantaged would not be particularly vulnerable, much of the time — many people on low incomes are very careful and astute consumers and have learned strategies that reduce future susceptibility in a repeat situation.

More broadly, all transactions carry some risk. But, it is generally understood in consumer policy discussions that the term ‘vulnerable and disadvantaged’ consumers delineates a narrower group encompassing those at significant risk of being misled or making poor purchasing decisions, either generally or in specific situations.

It is also important to recognise that vulnerability and disadvantage are not static concepts. Their nature and overall incidence (and associated detriment) are always changing. For example, while the potential vulnerability of the young and old has long been recognised, the concerns in these areas are increasing:

- Minors (and young adults) have acquired greater spending power and become mainstream consumers (especially for telecommunications products and motor vehicles). According to the National Children’s and Youth Law Centre, a 2003 study found that 20 per cent of mobile phone owners aged below 18 admitted phone debt caused them major problems and fewer than 10 per cent knew where to go for help with debt (NCYLC, sub. 40, p. 3).
- Increased longevity means that in coming years there will be many more aged consumers making major decisions relating to health care, accommodation (such as retirement villages and reverse mortgages), and sustainable financial investment of superannuation balances. The need to make decisions in these

areas is not new. But the potential for detriment may increase as the number of aged people rises, especially given the development of new, innovative, complex offerings marketed to this group, and the possibly greater prevalence of unscrupulous operators attracted by the larger market.

The dynamic nature of vulnerability and disadvantage requires policy makers to closely monitor developments and the consumer policy framework to be flexible and responsive to emerging needs.

12.2 Current approaches to the needs of vulnerable and disadvantaged consumers

The current consumer policy framework addresses the needs of vulnerable and disadvantaged consumers using a combination of generic and specific regulation and non-regulatory measures.

Generic laws cater for some situations

The generic fair trading and consumer protection provisions of the Trade Practices Act and State and Territory Fair Trading Acts — unconscionable conduct laws, prohibitions on harassment and undue pressure, and prohibitions on misleading or deceptive conduct — are particularly important for protecting vulnerable and disadvantaged consumers who are more likely to be the target of such conduct (ACCC, sub. 80, p. 19). The unconscionable conduct provisions have been successfully used with regard to door-to-door sales (*ACCC v Lux*), marketing educational materials to Indigenous people in the Northern Territory (*ACCC v Ramon Keshow*) and signing up the elderly, visually and/or hearing impaired people to telephone companies (Benchmark Sales Pty Ltd and Axxess Australia Pty Ltd). Box 12.2 provides a further example of the role of door-to-door selling provisions that have been embodied in State and Territory Fair Trading Acts or other generally applicable regulations.

Many specific laws seek to assist vulnerable and disadvantaged consumers

Nonetheless, the use of generic legislation to deal with problems confronting vulnerable and disadvantaged consumers has its limits. As Legal Aid Queensland (sub. 51, p. 2) commented:

Such general provisions require recourse to litigation where the facts about the description of the product or service will invariably be in dispute, there is a written

document which supports the trader rather than the consumer, and our clients, because of their vulnerabilities (eg: psychological problems) face difficulty if the case is determined solely on the basis of their credibility as a witness.

Box 12.2 Door-to-door selling

A particular example of the role played by the generic consumer law in protecting vulnerable and disadvantaged consumers is in the area of door-to-door selling (and cooling off periods). Direct selling practices are sophisticated and widespread across a range of industries and products, including new growth markets such as pay television, telecommunications and retail energy supply. Some of the most vulnerable groups in the community (especially older women living alone, Indigenous people and consumers with poor understanding of English) continue to be subjected to undesirable direct selling practices. Indeed, according to the NSW Office of Fair Trading (sub. 73, p. 25), some direct selling firms target particular suburbs or areas, including those with a high percentage of public housing.

All States and Territories have introduced specific regulations concerning door-to-door selling practices either within Fair Trading Acts, or as separate generic legislation. The provisions cover matters such as cooling off periods, rights of rescission, prohibition on certain actions (for example harassment and coercion) and restitution.

Similarly, the New South Wales Office of Fair Trading contended that there are several areas that are not well catered for by the generic consumer law — for example, residential tenancies, residential parks, strata schemes and retirement villages:

Transactions in these areas tend to be more complex than in most other trader/consumer interactions, may not allow as much leeway for the consumer in contracting with the trader of their choice and may involve circumstances in which the parties are relatively inexperienced in their roles as consumer or trader. In addition, because the transaction relates to a basic human need for shelter, [specific] regulation provides a level of protection, for reasons of social justice, beyond that given in a more standard contractual relationship between a trader and consumer. (sub. 73, p. 26)

Consumer regulation in the credit and utilities area (chapter 5 and appendices E and F) is also heavily focussed on dealing with vulnerable and disadvantaged consumers:

- The vulnerability of some consumers in credit markets is multi-faceted, reflecting:
 - the financial and legal complexity of some products;
 - these consumers’ exclusion from the mainstream credit market and therefore exposure to more unscrupulous operators;
 - the difficulty that those on low incomes often face in affording the basic necessities of life; and

-
- lack of awareness about rights and redress.
 - Disconnection of utility services has obvious harmful effects — it isolates, can make people sick or very uncomfortable, and makes it difficult for people to undertake everyday tasks, such as cooking and heating.
 - One survey showed that 53 per cent of respondents who experienced disconnection from an essential service had been on Centrelink benefits at the time of disconnection (WACOSS, sub. 68, p. 8). And the ABS (2006a) found that about 17 per cent of households in the bottom quintile of household income were unable to pay electricity, gas or telephone bills on time (figure F.2).
 - Moreover, the risk that consumers may be disconnected from essential services can increase when they are bundled with non-essential services — as non-payment can result in disconnection of all services (National Consumers' Roundtable on Energy, sub. DR199, p. 6).

However, a particular challenge when considering specific industry regulation to assist vulnerable and disadvantaged consumers, is how to weigh up the benefits for them against the costs that may be imposed on other consumers through restrictions on choice, price, and/or the entry of new suppliers. As stated by the Consumer Action Law Centre (sub. 94, p. 82):

Consumer policy has traditionally been one of the principal tools used to provide protections and to address problems affecting low-income, disadvantaged or otherwise vulnerable consumers who have been the victims of misleading and deceptive sales practices or exploitative products. The risk in this approach is that universal consumer policy regulation may be imposed to protect the interests of a small group of disadvantaged consumers. These policies may increase costs in the market overall and stifle business innovation without necessarily protecting consumers.

As with consumer policy formulation generally, good processes (see figure 3.1) — especially analytical rigour and transparency prior to the introduction of new measures (chapter 5) — will be very important to weighing up the benefits and costs of proposed regulations to protect vulnerable and disadvantaged consumers.

Redress for vulnerable and disadvantaged consumers

Various redress arrangements directly cater for the needs of vulnerable and disadvantaged consumers. For example:

- the ACCC claims to fast-track complaints involving disadvantaged and vulnerable consumers;

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- the ACCC and its Consumer Consultative Committee developed a strategy in 2003 to enable consumer and community organisations to refer appropriate complaints to the ACCC, recognising that vulnerable and disadvantaged consumers are more likely to complain to a community-based agency than to the ACCC;
 - the NSW Office of Fair Trading employs Aboriginal Customer Service Officers to provide culturally appropriate services with an emphasis on face-to-face program delivery; and
 - as noted in chapter 9, legal aid and financial counselling services are highly oriented towards vulnerable and disadvantaged consumers. Each state and territory government provides funding for a general legal aid and information service which consumers can access. And, the public network of financial counsellors is particularly important given that credit products are a source of significant detriment for some vulnerable and disadvantaged consumers. There are between 450 and 500 such counsellors practising in Australia, in a variety of full-time, part-time and volunteer roles.

12.3 Improving outcomes for vulnerable and disadvantaged consumers

The Commission's recommendations

The Commission's recommendations in this report are aimed at improving outcomes for all consumers, including those who are vulnerable and disadvantaged. As well as enhancing effective competition and thereby providing price, choice and quality benefits to consumers, the recommendations are intended to reduce the likelihood that consumers will experience problems and suffer detriment, and provide better redress when problems do arise.

Some recommendations should be especially beneficial for vulnerable and disadvantaged consumers.

- Strengthening credit market regulation, including through requiring all finance brokers and credit providers to be members of an approved alternative dispute resolution scheme, is likely to be particularly beneficial to those most at risk in this area (recommendation 5.2).
- The inclusion of a provision in the generic consumer law addressing unfair contract terms (recommendation 7.1) would similarly be comparatively favourable to vulnerable and disadvantaged consumers who may be less able

than other consumers to bear the costs of inappropriate use of such terms by suppliers.

- As discussed in chapter 9, the current multiple redress and complaints avenues are likely to be a particular disincentive for vulnerable and disadvantaged consumers to seek redress. Therefore, a well-known, national, single point of contact for referral and information should be particularly helpful for them (recommendation 9.1).
- The Commission has proposed that Australian Governments increase funding support for consumer legal aid and financial counselling services (recommendation 9.6) that are used principally by vulnerable and disadvantaged consumers.
- Like other consumers, those who are vulnerable and disadvantaged can be assisted by well targeted information on products and services. To this end, the Commission has recommended greater consumer testing and layering of disclosure requirements (recommendation 11.1). It has also recognised that this is not a complete answer to the challenge of providing effective and accessible information to vulnerable and disadvantaged consumers. For example, given the poor literacy and numeracy skills of some of these consumers, the information may need to be presented in different ways. Partly with the requirements of vulnerable and disadvantaged consumers in mind, the Commission has proposed a cross-jurisdiction review of the effectiveness of a sample of consumer information and education measures (recommendation 11.2).
- Vulnerable and disadvantaged consumers are particularly reliant on advocacy groups to ensure their views and needs are properly considered in the formulation of consumer policies. Partly for this reason, the Commission has proposed (recommendation 11.3) that additional public funding be provided to: cover the basic operating costs of a representative national peak consumer body; facilitate networking between various consumer groups, including those representing the vulnerable and disadvantaged; and establish a dedicated National Consumer Policy Research Centre, with some of its research work likely to pertain directly to vulnerable and disadvantaged consumers.

More broadly, one of the objectives of the proposals directed at facilitating a more nationally coherent policy framework (chapter 4 to 6) is to enhance the responsiveness of the framework to emerging challenges, including those faced by vulnerable and disadvantaged consumers. As the National Legal Aid Secretariat noted:

... the policy response by government must be sophisticated, multi-faceted and flexible enough to address emerging issues swiftly. (sub. DR220, p. 2)

Amongst other things, the recommendations provide for the creation of a new generic consumer law that would add to the protections available to consumers in the current TPA. As well as the new unfair contract terms provision and an expanded range of enforcement tools, the Commission is proposing that the new generic law should embody provisions from State and Territory Fair Trading laws where the current TPA provisions are inadequate to deal with a particular issue. Such augmentations would address concerns raised by the Victorian Government (sub. DR226, p. 99) that basing the new national generic law on the current TPA could leave vulnerable and disadvantaged consumers worse off.

Looking to the future

Awareness of emerging vulnerabilities

As noted above, those responsible for the future consumer policy framework will need to closely monitor developments affecting the extent and sources of vulnerability and disadvantage, and what this means for policy settings. As well as the issues surrounding the young and the old, electronic commerce has changed the nature and extent of vulnerability in some consumer markets (see chapter 13). An enhanced research capacity to generate the necessary supporting information will in turn be critical to successful policy adaptation to such developments — a capacity that would be facilitated by the Commission’s recommendation to create a National Consumer Policy Research Centre.

Better understanding the behaviour of vulnerable and disadvantaged consumers

It will also be important to give appropriate attention to the behavioural responses of vulnerable and disadvantaged consumers to different situations and policy options. Understanding why some consumers borrow from ‘predatory’ lenders and the success of scams despite warning campaigns and the otherwise sophisticated nature of many affected consumers, are cases in point. While the understanding of such matters is improving (box 12.3), the Australian Financial Counselling and Credit Reform Association (sub. 62) among others, suggested that more detailed analysis of the behaviours of low income and disadvantaged consumers is warranted.

Further advances in behavioural economics should be helpful in these contexts. To date, this field of research has focussed more on the responses of mainstream consumers. However, there is recognition that an extension to the examination of the behaviour of the most susceptible individuals is now required (see, for example, Mulholland 2007).

Box 12.3 Why do consumers borrow from 'predatory' lenders?

Wesley Community Legal Service (sub. 37) offered the following generalisation, based on its 12 years of experience:

Most poor people are aware of their poverty and this affects their self-confidence. Many have experienced rejection from mainstream lenders such as banks and have found that rejection to be a humiliating experience. By contrast, they may feel more comfortable in the environment of the local cash lender which can be first approached by telephone and then in a personal face-to-face shopfront office. Poor people have been conditioned to sign forms they don't really understand, particularly if they have been on Centrelink benefits. Hence very few ever read what they sign.

Whether or not the documentation complies with the Consumer Credit Code is not going to have any influence on their decision to borrow. It is more a question of whether they are good enough to be accepted by the lender. Having been lent money, they feel they have been done a favour, and may go to great lengths to repay the debt. Most borrowers know that they are being charged a lot for the loan. However, they simply accept being ripped off as their lot in life. They value the personal contact that comes with the collection process. Although many predatory lenders charge fees for reminder calls, the borrowers will not realise this, as the fees simply get added to the total debt.

Once the debt has been repaid, the borrower considers their relationship with the lender as an asset. If they need cash they can borrow from the same lender again. So the cycle of debt may continue for the rest of the person's life.

Australian Financial Counselling and Credit Reform Association (sub. 62, p. 3) said:

... our clients *expect* to be treated badly, if they are not it is a pleasant surprise. Perhaps that in part explains the success of otherwise overtly unfair and expensive market offerings like pay day loans, where clients make comments like – *I knew it was expensive but at least they were pleasant to me and made me feel like they wanted my business.*

Possible use of specific strategies and action plans

The role of specific strategies to deal with the circumstances of some particular disadvantaged groups should also be part of the policy calculus. The National Indigenous Consumer Strategy is the contemporary example of this approach (box 12.4). In helping to give effect to this strategy, the Victorian Aboriginal Legal Service (sub. DR238, pp. 2-4) spelt out some specific requirements relating to the Commission's recommendations regarding the funding of legal aid and financial counselling, alternative dispute resolution, written submissions to small claims courts and tribunals, consumer education and advocacy.

Box 12.4 The National Indigenous Consumer Strategy

The objectives of the National Indigenous Consumer Strategy are to:

- improve Indigenous consumers' knowledge of their rights and obligations under consumer protection laws and achieve greater Indigenous access to consumer protection programs;
- improve the behaviour of traders, through education and compliance activity, to reduce detriment experienced by Indigenous consumers; and
- promote effective engagement and partnership between consumer protection agencies, Indigenous organisations, business and other government agencies to improve consumer outcomes for Indigenous people.

The strategy identifies actions under the following eight key priority areas:

1. Employment of Indigenous staff in consumer agencies
2. Advocacy of Indigenous consumers' interests
3. Housing
4. Financial management and banking
5. Motor vehicles
6. Trading practices
7. Arts industry
8. Managing indigenous community organisations.

Progress against the actions identified in the plan will be monitored, evaluated and reported on an annual basis.

Source: MCCA 2004c.

The need for such strategies should, of course, be carefully considered, given the associated risks of fragmentation and compartmentalisation of the overall policy framework. A key prerequisite would be to establish that the issues facing a sub-group of consumers were sufficiently specific to warrant a dedicated approach — for example, as with the regional and cultural dimensions of Indigenous consumer issues. Nonetheless, in light of emerging/currently unforeseen vulnerabilities and better understanding about behavioural responses, such an approach may be appropriate for some other groups of consumers in the future. In this regard, the NCYLC called for a much more explicit policy focus on the needs of children and young people (box 12.5).

Box 12.5 The consumer policy needs of young people

In suggesting that the needs of children and young people receive much greater attention in consumer policy making, the NCYLC (sub. DR196, p. 3) said that:

... most young consumers do not know their consumer rights, nor are they aware of or equipped to access the complaints mechanisms that are available. Even if they do understand their rights, they are not likely to seek to enforce those rights or to pursue remedial action if those rights are violated, often due to a lack of confidence either in themselves or the mechanisms available.

NCYLC supports the objective of the Commission to create a nationally coherent consumer policy framework. However it is our submission that this policy framework should contain specific policy initiatives that are aimed at improving the inclusion, education and empowerment of Australia's children and young people as consumers.

The Centre proposed the following strategies tailored to the needs of young people:

- Information and education — a nationally coordinated education framework to inform children and young people of their rights as consumers, and how to assert and defend those rights.
- Hardship programs — such as flexible payment plans, additional time to pay, fee waivers and financial counselling for young people.
- Complaints mechanisms — the provision of complaint avenues that young people will trust and use.
- Funding for consumer advocacy — increased funding for legal aid and financial counselling services designed for young people.

Finally, in implementing the Commission's proposed nationally coherent consumer policy framework, it will be important to recognise jurisdictional differences in the degree of consumer vulnerability and disadvantage, especially in the Indigenous area. As noted in chapter 4, such differences may provide a reason for retaining responsibility for some particular industry-specific consumer regulation at the State and Territory level. And in policy areas where transfer of policy responsibility to the national level is found to be appropriate, any significant divergence in the degree of regional vulnerability and disadvantage should be recognised in the resourcing priorities of the national regulators concerned.

13 Other considerations for the future framework

Key points

- The generic Australian and New Zealand consumer laws are not sufficiently different to create significant impediments to closer trans-Tasman integration.
 - Nonetheless, the creation of a single national generic consumer law and the transfer of responsibility for some key industry-specific areas of consumer policy to the national level in Australia would aid closer integration by making it easier for New Zealand firms to trade in Australian markets.
- E-commerce has given rise to a number of concerns in addition to those experienced in the ‘offline’ environment, including:
 - the security of the online payment process;
 - new practices specific to the Internet which have led to impaired performance of the Internet platform, theft of personal information and invasion of privacy; and
 - difficulties for consumers in seeking redress and for regulatory enforcement.
- However, a cautious regulatory response to these problems is appropriate.
 - Given the significant cross-border dimension to electronic commerce, there are likely to be substantial constraints on what can be achieved through unilateral domestic policy intervention.
 - Given the rapid development of e-commerce, targeted regulation could become quickly out-dated and stifle innovation.
 - There appear to be strong incentives for reputable Internet businesses to develop their own responses to consumer concerns.
- That said, as consumer issues related to e- and m-commerce continue to emerge, it will be important to monitor the adequacy of existing general consumer laws. As well, privacy and identity security matters may require further attention.
- Small businesses have a dual role in Australia’s consumer policy framework as both consumers and suppliers of goods and services.
 - The current protections for businesses under the generic law seem largely appropriate.
 - The Commission’s proposals in this report to improve the framework should both enhance protection for small businesses as consumers, and reduce the costs for them as suppliers in complying with regulatory requirements.

The future consumer policy framework will have to address a number of other matters, including:

- the scope to facilitate further economic integration with New Zealand;
- issues relating to e-commerce and cross-border redress; and
- protections for small businesses as consumers.

13.1 Consumer policy and trans-Tasman economic integration

The Australian and New Zealand economies are becoming increasingly integrated. Apart from a shared legal and political heritage and geographical proximity, contributing factors to increasing trans-Tasman integration include:

- the Australian New Zealand Closer Economic Relations Trade Agreement (CER);
- the Trans-Tasman Mutual Recognition Agreement (TTMRA) — of particular importance in the consumer policy area (see box 13.1);
- a Memorandum of Understanding on Business Law Coordination; and
- the announcement by the Australian and New Zealand Governments in 2004 of their intention to build on the CER Agreement and move toward a single economic market based on common regulatory frameworks (Costello and Cullen 2004).

In this latter regard, and as reflected in the terms of reference, any significant divergence in consumer policy settings — which are an important part of the commercial policy framework in each country — would clearly be a cause for concern.

Differences between the Australian and New Zealand consumer policy regimes

Legislative

The generic consumer protection legislation in New Zealand comprises:

- the *Fair Trading Act 1986* (NZ) (FTA); and
- the *Consumer Guarantees Act 1993* (NZ) (CGA).

Box 13.1 Trans-Tasman Mutual Recognition Agreement

Many of the restrictions on the sale of goods and registration of occupations in Australia and New Zealand have consumer protection as their objective, and as such are an element of the consumer policy framework. Hence, the TTMRA is of particular relevance to further policy integration in this area. Subject to various exemptions and exclusions, the TTMRA provides that all goods legally available for sale in one country may be sold in the other, and that any person registered to practise an occupation in one country may do so in the other.

The TTMRA has been effective in achieving its objective of assisting the integration of the Australian and New Zealand economies and enhancing competitiveness (PC 2003a). While there is still progress to be made on such matters as the special exemptions and exclusions, these are to be examined in a recently announced Productivity Commission review (COAG 2008).

Broadly, the New Zealand legislation is similar to that in Australia. Its FTA was initially modelled on the Australian Trade Practices Act (TPA), and so contains substantially similar consumer protection provisions for misleading, deceptive or unfair conduct. Moreover, the CGA contains similar provisions relating to implied conditions and warranties to those in part V of the TPA, even though it was based on Canadian legislation at the time.

The main differences (box 13.2) between the TPA and New Zealand's generic laws are that:

- the CGA contains a clause that states that goods sold must be safe (s. 7(1)(d) CGA). Australia does not have a similar general safety provision;
- New Zealand has a 'no-fault, no-blame' system for compensation for injuries caused by unsafe products. In contrast, Australian consumers pursuing compensation for injury suffered as a result of faulty or unsafe products must sue the manufacturer (see chapter 8);
- unlike Australia, New Zealand has no statutory prohibition on unconscionable conduct — consumers must rely on the common law doctrine of unconscionable dealings; and
- the CGA gives protection to anyone who ends up owning the goods, not just the original purchaser.

Box 13.2 The TPA and New Zealand's generic consumer protection laws compared*Misleading or deceptive conduct and false representations*

There are few substantive differences in the legislative standards for this behaviour, or the interpretation or enforcement of these standards. The sanctions for breaches under the general prohibitions are higher in Australia: up to A\$1.1 million for businesses and A\$220 000 for individuals, compared with NZ\$200 000/ NZ\$60 000 in New Zealand.

Product safety

There are 28 compulsory product safety and information standards under the TPA, and many more at the state and territory level, compared with 6 in the NZ FTA. However, the CGA has a general requirement that goods must be safe, which the TPA does not. There are also differences in compensation arrangements: New Zealand has a 'no-fault, no-blame' compensation regime for injury or death caused by defective goods. In Australia, consumers pursuing compensation for injury suffered as a result of faulty or unsafe products must sue the manufacturer of a faulty product, either under the TPA or at common law.

Conditions and warranties

There is little substantive difference in the interpretation of the implied conditions and warranties provisions between the two countries. The protections under the TPA apply more broadly — to goods or services with a value of up to \$40 000, or of a type normally bought for personal use, or any commercial road vehicle. The New Zealand provisions in the CGA apply to a consumer, defined as one who purchases goods or services of a kind ordinarily acquired for personal, domestic or household use.

Unconscionable conduct

There is no statutory equivalent to part IVA of the TPA in the NZ FTA. Instead, unconscionable conduct is dealt with by the common law doctrine of unconscionable dealings. However, since 'unconscionable' is not defined in the TPA, the courts determine what constitutes unconscionable conduct/dealing in both countries, with their interpretations being similar.

Because New Zealand does not have a statutory provision for unconscionable conduct, the remedies available are those prescribed by common law — such as rescission and damages. For breaches of Australia's statutory provisions, sanctions are civil only, with the remedies including injunctions, rescission or variation of a contract, refund, and non-punitive orders on application by the ACCC.

The ACCC or individuals can apply to the Federal Court for relief from a breach of the unconscionable conduct provisions of the TPA. This contrasts to common law action in both New Zealand and Australia, which limits applications for relief to individuals who have suffered as a result of the unconscionable conduct or dealing. Under the NZ Credit Contracts and Consumer Finance Act 2003, however, the New Zealand Commerce Commission is able to apply to the court to reopen a credit contract that is oppressive, or is exercised oppressively.

The Australian State Fair Trading Acts are broadly equivalent to the TPA. However, one difference in a trans-Tasman integration context is Victoria's unfair contracts provision.

In terms of specific legislation, New Zealand has a smaller body of law mainly confined to occupational licensing in high-risk areas, and credit regulation under the *Credit Contracts and Consumer Finance Act 2003* (CCFCA).

Administration and enforcement

There is a high degree of cooperation between the Australian and New Zealand Governments on consumer policy matters. At the policy development level, New Zealand is a member of the Ministerial Council on Consumer Affairs and the Standing Committee of Consumer Affairs Officials.

There is also strong cooperation on the administration and enforcement of consumer policy between the ACCC and its New Zealand counterpart, the Commerce Commission (NZCC).

- The ACCC and NZCC have had an agreement since 1994 to promote cooperation and coordination between the agencies and reduce the possibility of differences in their application of competition and consumer protection laws. Key aspects of the agreement relate to information sharing and staff exchange.
- The AUZSHARE system allows authorised agencies across Australia and New Zealand to send out alerts on scams and consumer complaints via email and for users to access complaints data.

However, the Commission's recent review of Australian and New Zealand competition and consumer protection regimes (PC 2004a) noted some impediments to effective enforcement in trans-Tasman cases, such as statutory restrictions preventing the ACCC and NZCC exercising their information requisitioning powers in each other's jurisdiction. Legislation has since been prepared in New Zealand and passed in Australia to overcome these problems.

Impact of the Commission's recommendations on trans-Tasman integration

The Commission's 2004 review found that in an overall sense, the generic Australian and New Zealand consumer protection regimes are sufficiently similar as not to be a significant impediment to an integrated trans-Tasman business environment. Even so, participants in this review pointed to benefits for New Zealand firms — and regulators — from harmonisation of regulatory requirements

both within Australia and between Australia and New Zealand. For example, providing a regulator's perspective, the New Zealand Commerce Commission (sub. DR193, p. 2) said that:

This would foster greater consistency in approaches across jurisdictions and make it easier for businesses to transact. It would also be a significant boost to enforcement. In an increasing number of situations the Commission is dealing with the same issues and/or traders as Australian consumer enforcement agencies. This gives rise to opportunities for the Commission to work collectively with those agencies.

And the Australia–New Zealand Leadership Forum's Working Group on Trans-Tasman Competition and Consumer Issues (sub. DR179, p. 1) supported:

... the concept of a national consumer policy framework for Australia. Implementation of such a framework would result in significant benefits which would be shared equally by consumers, businesses and regulators. It will also contribute to the goals of the Governments of Australia and New Zealand to move towards a single economic market.

These observations give greater weight to the Commission's recommendations designed to deliver a coherent national consumer policy framework, including as an immediate priority the creation of a single national generic consumer law (see chapter 4).

13.2 E-commerce

New benefits and new concerns

The Internet has provided consumers with significant benefits, such as an improved ability to undertake research before purchasing, wider availability of goods and services from all over the world, scope for greater consumer-to-consumer trading, and the convenience of virtual shopping. On the supply side, it has enabled efficiencies in retailing and distribution, putting downward pressure on prices. For example, Brown and Goolsbee (2002) estimated that growth in Internet purchases had reduced term life premiums in the USA in the 1990s by 8 to 15 per cent.

But it has also given rise to problems for consumers. These can be divided into four broad categories:

- problems relating directly to the goods and services, that are also experienced in the offline environment, such as delayed, undelivered and defective orders, mistakes in billing, warranty disagreements, misleading advertising, and deceptive and unconscionable conduct;
- the security of the online payment process;

-
- new practices specific to the Internet such as spam, spoofing, phishing, spyware and cookies, which can be manifested as annoyance, impaired performance of computers and the web, theft of personal information (identity, financial and medical) and invasion of privacy (such as tracking of Internet search habits and purchasing profiles); and
 - difficulties for consumers in seeking redress and for effective regulatory enforcement, particularly for cross-border disputes.

Given the potential for these types of issues to undermine trust in online transacting and hinder its future development, there have been various policy and industry initiatives in Australia and other countries to address specific problems.

Profile of Internet e-merchandising

The percentage of adult Australians who ordered or purchased goods and services over the Internet rose from 5 per cent in 1999 to 31 per cent in 2004-05 (ABS 2005), and the NSW Office of Fair Trading estimates that this figure is now over 50 per cent (Burnley 2007). However, reflecting concerns about security of online payments, privacy of personal details and receiving or returning goods, there is still a considerable proportion of Australians connected to the Internet who do not use it as a purchasing medium.

Many of those who purchase via the Internet have adopted protective strategies to reduce the perceived risks. There is evidence that Internet consumers show a preference for websites of well-known offline retailers, well-known e-commerce brands and domestic suppliers. Also, purchases over the Internet are concentrated on relatively low value items — for example, books and music (Industry Canada 2004). While consumers do a lot of research via the Internet on large expenditure items such as houses and cars, they generally do not purchase them in this way. Thus, the average amount ‘lost’ when something goes wrong with Internet purchases may be lower than in the offline world.

It is not clear whether the percentage of online transactions that do not meet expectations is much different from offline transactions. Of the proportion that are unsatisfactory, most surveys suggest that undelivered orders are the biggest problem, accounting for 20 to 25 per cent of the total number of e-commerce complaints (EC 2006b; FTC 2007a). The NSW Office of Fair Trading reported that non- or partial-delivery of goods, faults or damage, and products not meeting descriptions accounted for almost half of complaints to the agency (Burnley 2007).

More broadly, only a small proportion of complaints are related to e-commerce transactions — between 2001-02 and 2005-06, complaints to the ACCC about an

online trader or e-commerce represented just 6 per cent of total complaints. However, relative to disputes involving offline purchases, e-commerce disputes may be under-reported given that their value is often lower, there is uncertainty about rights and what avenues of redress to explore, and that such disputes may be more likely to be accepted as a cost of doing business online.

Regulatory and non-regulatory arrangements for e-merchandising

The TPA and Fair Trading Acts are technology neutral in that they apply equally to online and offline consumer transactions (though differences may emerge at the enforcement stage, in part because of cross-border jurisdiction constraints).

This is in contrast to the USA and EU, which have specific regulation governing the purchase of goods over the Internet. The EU Distance Selling Directive gives consumers the right to cancel an online contract for whatever reason within seven days and receive a full refund. In the USA, the FTC's Cooling Off Rule gives consumers three days to cancel a purchase made online. In both the EU and the USA, purchases made online are to be delivered within 30 days, unless the parties have agreed to a different period.

However, it is not clear that implementation of such measures in Australia would add greatly to the protections available under the generic consumer law. This is especially the case given that there are various supplier-driven mechanisms to enhance consumer confidence and to facilitate redress if things go wrong. For example, eBay has a consumer feedback rating system, where individual suppliers are given scores according to the amount of positive or negative feedback they receive from customers. This system is widely known and trusted by e-consumers.

Consumers are also protected by 'charge-backs' on credit cards. Charge-backs allow a credit card holder who has paid for goods or services using the credit card to dispute certain or all aspects of the transaction through the card issuer. In some countries, including Canada and the USA, these protections are required as a matter of law, but in others (such as Australia) they are provided voluntarily through industry codes or other programmes by card issuers. As charge-backs can be time-consuming and potentially costly for suppliers, they will have strong incentives to take measures to minimise recourse to them.

That said, it would be prudent to monitor the extent of any problems in e-merchandising, and the extent to which current laws are adequate in this regard. If it becomes apparent that the generally applicable consumer law is deficient, then specific e-commerce measures should be considered.

Security of Internet payments

Concerns about the perceived risks associated with online payment compared with offline payment processes are little different to those that were evident during the change from cash to credit card imprint vouchers, and from imprint vouchers to electronic swipe cards (requiring PIN activation or signature). About 11 per cent of all credit and charge card transactions are now undertaken using the Internet, a figure that has increased strongly in recent years (ASIC 2007). It can reasonably be expected that some of the concerns about online payment security will abate as consumer experience grows.

Even so, there have been various non-regulatory responses which partially address online payment concerns. For example:

- some consumers self protect by using a separate low limit credit card;
- innovation in technical security of payment sites is ongoing;
- the Electronic Funds Transfer Code limits the consumer loss from unauthorised transactions, complemented by additional initiatives by individual financial institutions and credit card networks; and
- when shopping on eBay, PayPal Buyer Protection provides free protection of up to \$1500 on eligible purchases. When the transaction is not covered by PayPal Buyer Protection, a consumer may still be covered by eBay's Buyer Complaint Policy.

New and heightened concerns

Our language now includes terms such as spam, modem-jacking, spoofing, phishing, spyware, cookies, pop-ups and website hijacking. The mechanics of these practices are unique to computers, with no direct parallel in the offline world. Spam and malicious and fraudulent Internet practices are considered by most policy makers worldwide to be consumer policy issues, because they strike at the heart of consumer confidence and the longer term potential for e-commerce to foster global competition, especially in the provision of services.

Spam

Spam is vastly different to offline direct marketing: the marginal cost of sending spam is extremely low, and the speed 'instantaneous', so the magnitude of unsolicited electronic messages dwarfs traditional cold calling. Spam is estimated to account for between 60 and 80 per cent of all global email (DCITA 2006). In practical terms, spam threatens the efficiency and speed of the Internet for all users and impedes household and workplace productivity.

A number of more or less successful technical approaches to limiting spam have emerged such as filtering software, cooperation among ISPs in blacklisting sites known to harbour spammers, and configuration of e-mail servers to notice differences between the true origin of an email and a fake 'reply-to' address.

In addition, like many other developed countries, Australia has enacted specific anti-spam legislation. However, while several known global spammers, formerly based in Australia, have ceased operating here since the introduction of the *Spam Act 2003*, it is unclear what causal effect the Act has played in this regard.

Indeed, the spam case illustrates the difficulties in designing specific legislation to keep pace with developments in rapidly-changing markets. In the four years since the Spam Act was instigated, the nature of spam has evolved from being principally an annoyance for consumers and a burden on network resources, to being a major vehicle for malicious and fraudulent activity, using spyware. This suggests that the greater flexibility offered by well-designed generic legislation may be more appropriate to deal with these sort of issues. In this regard, the most serious and malicious spyware activities may be covered by the computer offences set out in the Commonwealth Criminal Code (DCITA 2005a).

Electronic privacy

Electronic privacy concerns fall into two categories:

- the potential for information about consumers that is legitimately held in databases by businesses (such as doctors, insurance companies and financial organisations) to be inappropriately provided to third parties or 'cracked'; and
- the possibility of unauthorised or unknown interception of information by 'cookies'¹ during online transactions and searches.

The first is primarily a matter for privacy policy and not dictated by consumer policy. In Australia, the *Privacy Amendment (Private Sector) Act 2000* protects the privacy of consumers' personal information when dealing with private sector organisations, and applies equally to electronic and paper information.

The privacy concerns over cookies were at their height when cookies were novel, not well understood and were impossible or difficult to self manage. However, the detriment caused was relatively minor and market responses to consumer concerns emerged. Web browser software began including tools for individuals to self

¹ Computer 'cookies' can keep detailed records on how often and where a person goes within a web site and can be aggregated across multiple web sites to provide a detailed profile of an individual's online activity.

manage cookies, knowledge and awareness spread, and large database marketing companies promised not to exploit cookies' potential. As a result, concern about unauthorised or unknown interception of personal marketing information has diminished somewhat.

Online identity and investment fraud

In contrast, the fraudulent interception of identity and financial information is currently a key concern for both consumers and financial service providers. While the level of Internet banking fraud remains lower than cheque and credit card fraud, it has grown considerably in recent years (ASIC 2007). Industry estimates of net losses in Australia are about \$25 million per year (excluding ancillary costs such as investigating fraud claims). The techniques used to perpetrate online fraud are sophisticated, rapidly evolving and not generally the domain of 'amateurs'.

Consequently, financial institutions have put in place a range of strategies to enhance security, including better user authentication, encryption of information, warning consumers of risks, monitoring activity, and imposing daily transaction limits.

Cross-border redress and enforcement

The development of online purchasing has led to strong growth in the number of cross-border transactions, both within Australia and with other countries. However, in the event of disputes between consumers and suppliers, or when consumers suffer detriment from misleading or deceptive conduct, obtaining redress can be more difficult than in the traditional purchasing environment. The difficulties can be especially pronounced for transactions with parties in other countries, which in turn focuses attention on the effectiveness of cross-border enforcement by regulatory authorities (box 13.3).

On the importance of international cooperation, the ACCC noted (sub. 80, p. 66):

International cooperation assists in the provision of information from foreign jurisdictions to determine whether unlawful conduct took place, to gain experience on dealing with new consumer issues and to improve on the effectiveness of enforcement mechanisms.

Countries such as Canada, the United States of America and the United Kingdom are increasingly looking at consumer complaints on a global basis and enforcing through co-ordination with foreign jurisdictions. Through this trend, co-operation agreements and efforts within international forums to co-ordinate enforcement activities have become increasingly important and effective.

Reflecting such considerations, the OECD recently adopted a Recommendation on Consumer Dispute Resolution and Redress, which included a statement encouraging member countries to develop multilateral and bilateral arrangements to improve international judicial cooperation on the enforcement of judgements in cross-border cases (OECD 2007a). Independent of that process, the Australia-United States Free Trade Agreement contains an article facilitating the enforcement of monetary judgements obtained by the ACCC or ASIC, and by a number of US agencies. And the Office of the Privacy Commissioner (sub. DR190, p. 4) noted that Ministers of APEC economies have agreed on an APEC Privacy Framework, which will enable the exchange of information between data protection authorities and therefore increase and promote cross-border cooperation in investigation and enforcement.

Box 13.3 Difficulties in obtaining and enforcing cross-border judgements

Difficulties obtaining judgements

Unless consumers are willing to institute legal proceedings in the overseas countries where the suppliers are located — which can be prohibitively costly for individuals — they will have to demonstrate that the courts in their own country have the jurisdiction to hear such cases. This is not straightforward, and will require some form of connection between the defendant and the country in which the action originates.

There are also disparate national rules with respect to the applicable law in cross-border cases. This serves to further hinder the chances of a consumer obtaining a judgement against an overseas supplier; indeed the lack of uniformity in the way that this issue is decided between countries can potentially be exploited by rogue suppliers.

Difficulties enforcing judgements

There are no global arrangements in place to enable mutual recognition and enforcement of judgements. So without a treaty or other arrangement, even if the difficulties associated with obtaining a judgement can be overcome, enforcing the judgement in the country where the defendant (or his/her assets) are located can be very difficult.

Sources: OECD 2006c; Gawith 2007.

Mobile commerce

Mobile commerce (m-commerce) is the purchase of goods or services using a wireless terminal, such as a mobile telephone or personal digital assistant, with access to a network. As a type of e-commerce, it offers consumers an alternative to other online and offline methods of purchasing goods and services. It also provides

merchants with a new mechanism to deliver advertising and information products to consumers, as well as enabling instant transactions to be conducted.

Presently, the majority of m-commerce transactions are for the purchase of relatively low value non-physical goods, such as ring tones for phones and information services that are delivered to the telephone handset. However, more complex m-commerce transactions are slowly emerging. For example, there have been a number of trials that enable a consumer to pay via a mobile phone for parking, rather than using the traditional coin payment. It is also expected that as more diverse and secure payment mechanisms emerge, the capacity to conduct credit facility transactions by mobile devices will become possible.

As it is still in the early days of development, there is little practical experience in testing how well existing fair trading, financial and e-commerce laws will extend to m-commerce matters. However, there are (at least) two differences between m-commerce and e-commerce that may give rise to additional consumer protection concerns. First, the use of mobile phones to make purchases has some technology-specific privacy implications:

- key information about an individual is stored on a SIM card that links their identity to a handset; and
- the location of the phone can be identified and tracked.

A second difference is the limited memory and text handling capacities of mobile devices, which has implications for displaying lengthy contracts and information about the seller and/or the goods.

That said, if past experience in the e-commerce area is any guide, these issues may well be partly or largely addressed by the market and related technological developments.

Future policy responses to developments in electronic and mobile commerce

Notwithstanding the range of consumer issues precipitated by the rapid growth of these new forms of transacting, a cautious regulatory response is likely to be important for the following reasons:

- Especially given the significant cross-border dimension to electronic commerce, the constraints on what can be achieved through domestic policy intervention are likely to be greater than in the traditional purchasing environment.
- In such a rapidly developing market landscape, targeted regulation is more likely to become quickly out-dated and potentially stifle innovation.

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- As illustrated by such instruments as eBay supplier ratings, reputable online businesses have strong incentives to develop their own responses to consumer concerns so that they can encourage repeat business.

However, achieving good outcomes for consumers in electronic and mobile commerce will put a premium on effective cooperation between regulatory agencies, both within Australia and with their counterparts overseas. To this end, some new measures may be required — especially to facilitate information sharing and cooperative enforcement activity with other countries.

More broadly, as noted earlier, it will be important to monitor the adequacy of general consumer laws to meet emerging e- and m-commerce issues. As well as the possibility that some specific consumer laws in this area could be warranted, privacy matters and identity security issues may also require further specific attention.

13.3 Small business considerations

Small businesses have a dual role in consumer policy: as well as being suppliers of goods and services, they are consumers in their own right (MTAA, sub. 43, p. 4). Indeed, in their dealings with larger businesses, small businesses can face many of the same issues as individual consumers, particularly relating to unequal bargaining power and the lack of resources to effectively negotiate contracts.

Some consumer legislation currently extends to all businesses, large or small, in specific circumstances. For example:

- In all jurisdictions, the purchase of goods and services by businesses of any size can be subject to the requirements of the TPA and the State and Territory FTAs. As outlined earlier in the report, these protections include prohibitions on misleading or deceptive conduct, implied warranties in consumer contracts and specific product liability provisions. Importantly however, the specific circumstances in which these protections are available to businesses vary between jurisdictions (box 13.4).
- At the state and territory level, the various Sales of Goods Acts provide certain excludable protections (that is, they can be contracted out) to participants in all transactions, regardless of whether they involve businesses or consumers.

There has also been a trend to provide explicit protection to small businesses.

- In 1998, the TPA was revised to protect small business from unconscionable conduct for business transactions of up to \$3 million (section 51AC). A recent amendment to the TPA raised this limit to \$10 million and, among other things,

also provided greater direction to the courts in assessing the misuse of market power through predatory pricing.

- Many industry-specific consumer protection measures encompass small businesses. For example, the consumer protection provisions in the financial services regulatory regime extend to those products or services purchased by small businesses. Also, in Queensland, the definition of small end-users in the utilities sector is those who use under 100 megawatt hours per annum, and includes both residential users and small business users (sub. 93, p. 20). In addition, the Code of Banking Practice, a self-regulatory code that sets out standards of practice towards consumers in the banking sector, applies to both personal and small business banking (ANZ, sub. 82, p. 9).

Box 13.4 Business purchases covered by generic consumer law

Australian Government (TPA)

1. goods or services less than \$40 000; or
2. if over \$40 000, must be for personal, domestic or household use, or a commercial road vehicle.

In both cases, the goods must not be for resupply, or for the purpose of using them up or transforming them in the process of manufacture, production, or repair.

New South Wales

Goods or services must not be for resupply, or (for other than farming businesses) must not be consumed or transformed for manufacture or production, or used for repair.

Victoria

Uses the two-part TPA model for sections on implied terms. For other provisions, goods acquired for business use are not covered.

Queensland

Goods or services must cost less than \$40 000 and not be for resupply.

Western Australia, South Australia and Tasmania

As for the TPA.

Australian Capital Territory and Northern Territory

Goods or services must not be for resupply, or for the purpose of using them up or transforming them in the process of manufacture, production, or repair.

The qualifier that goods or services must not be used up or transformed in a process of manufacture, production or repair does not appear to have been a deciding factor in court cases relating to the application of the generic consumer law. As such, this law would appear to cover a broad range of business purchases — subject to the other criteria listed above.

Source: Corones and Christensen 2007.

Should small businesses be protected as consumers?

In the Draft Report, the Commission indicated that its proposal for a new national generic consumer law based largely on the TPA would preserve the current consumer protections for certain business purchases. However, it did not propose adding to the protections for small business, as had been suggested in some submissions. For example, several participants, including the Australian Retailers Association (sub. 71, p. 8), argued that the TPA provisions addressing unconscionability in business transactions are inadequate.

A number of respondents to the Draft Report — including the Motor Trades Association of Australia (sub. DR169, p. 1) and the Real Estate Institute of Australia (sub. DR172, p. 11) — supported maintaining the status quo in regard to the generic law, noting the many commonalities between small businesses and consumers. And some expressed concern that the Commission had not recommended greater protection for small business (Australian Newsagents' Federation, sub. DR203, p. 5)

Conversely, some argued that the current generic consumer protections for business are too generous. Luke Nottage (sub. DR114, pp. 13-14) claimed that, given that the coverage of the TPA protections is based largely on the size of the purchase, not on the size of the purchaser, 'very large and sophisticated corporations take advantage of these provisions, to a degree probably not intended by the legislator'. And others emphasised the costs that these protections for small business impose on larger suppliers. Telstra (sub. DR156, p. 6) submitted that:

... the inclusion of business customers in the areas of consumer protection law primarily intended to protect "consumers" [is] unnecessary and potentially harmful to the Australian economy because extending protection to small business will lead to higher regulatory and transaction costs.

In the Commission's view, there are no clear principles that can be brought to bear in deciding the extent to which small business should be covered by generic consumer protections. They share some common characteristics with household consumers, but in other respects they differ. And the provision of protection is likely to come at a cost to business (and, ultimately, consumers).

In any event, the protections offered to small business are to a certain extent an outcome of the way in which consumers are defined within the relevant legislation. Hence, a by-product of the Commission's proposal to create a new national generic consumer law based largely around the provisions of the TPA would be to increase protection for small businesses in those jurisdictions where the definition of a consumer is currently more restrictive than in the TPA.

While the definition of which purchases are covered by the new generic law could be adjusted to extend, or scale back, protections for small business, the Commission is not convinced that there would be significant benefits from doing so. Indeed, any significant scaling back of consumer protection for small business would change a longstanding tenet of the generic consumer policy framework in Australia, and would run counter to the trend towards increasing small business protections in other areas of consumer policy.

The benefits of other Commission proposals for small businesses

Maintaining the thrust of the current approach to protecting small businesses in the new national generic consumer law would in turn mean that small (and other) businesses, like other consumers, would be afforded some additional protections by the Commission's proposals to improve the effectiveness of that generic law. These proposals include:

- the introduction of specific provisions covering the use of unfair contract terms (chapter 7);
- measures to improve access to redress, including allowing written submissions to tribunals and small claims courts (chapter 9);
- giving consumer regulators a wider range of enforcement tools (chapter 10);
- changes to improve disclosure requirements (chapter 11); and
- more public funding for consumer advocacy and research (chapter 11).

Also, a number of the Commission's proposals should reduce regulatory compliance costs for small businesses in their capacity as suppliers rather than consumers. In particular, the creation of a single national generic consumer law would reduce somewhat the regulatory compliance costs for those businesses that operate in multiple jurisdictions. Also, the Australian Newsagents' Federation (sub. DR203, p. 11) noted that a single national consumer policy framework would simplify the task for industry associations of informing and advising small businesses of their rights and obligations under consumer legislation.

Moreover, the Commission has highlighted the questionable nature of parts of the current occupational licensing apparatus (chapter 5). As occupational licensing mainly applies to small business operators, the removal of unnecessary requirements and the national consolidation of others could provide substantial savings to them.

14 How big would the net benefits be?

Key points

- There is a strong qualitative case for the Commission's consumer policy reforms and this is the most important basis for policy change.
 - The supporting quantitative assessment is experimental and highly assumption-dependent.
- Most recommendations would directly assist consumers by either improving the effectiveness of *existing* measures and their enforcement, or lowering compliance costs for businesses. This has better prospects of delivering sizeable gains than devising new regulations constraining business misconduct.
- The Commission's proposals would lower consumers' risks of detriment, giving them greater capacity to make informed decisions, and reducing the extent of detriment experienced when problems actually occur.
- Such lowered risks would encourage consumers to trust new firms and products more. This would stimulate innovation and productivity growth and reduce the transactions costs consumers incur to avoid risk. These indirect effects are some of the most important sources of gains from reform for consumers, but are largely invisible to them.
- There would be other benefits, including the intangible gains for consumers from fairer outcomes and less emotional distress when purchases do not work out as expected.
- There are also likely to be additional long-run benefits, most importantly, the prospect of more responsive policy making in the future.
- It is not possible to undertake a precisely quantified benefit-cost analysis of the proposed policy package, or even of the individual components within it.
 - Apart from the lack of robust data on key problems that the policy framework is intended to address, the difficulties of separating out the impacts of consumer policy from the many other influences on consumer well-being and the intangible nature of some key benefits and costs, make any quantification exercise difficult.
- Though only very broad quantification is possible, the Commission estimates that its package of reform measures could provide a net gain to the community of between \$1.5 billion and \$4.5 billion a year in today's dollars.
 - The main contributors to this estimated gain are reduced direct detriment for consumers and increased productivity and innovation.
 - There are few downside risks from the Commission's proposed policy reforms. Even if the assumptions underlying the quantification are wrong, the worst-case scenarios still produce significant positive benefits for Australians.

The Commission has put together a package of reforms covering most aspects of the consumer policy framework. The individual components of the package and their

prospective qualitative benefits are summarised in table 2 of the summary. The objective of this chapter is to assess the nature and extent of the (net) benefits in more detail and, where possible, to provide indicative quantitative estimates of the Commission's reform package.

14.1 Placing the costs and benefits into a framework

As emphasised throughout this report, consumer policy is aimed primarily at encouraging appropriate business conduct and giving consumers a greater capacity to exercise sovereignty in their decisions. Measures that do this have far-reaching effects on the welfare of consumers and on the effective functioning of the supply-side of the economy. However, regulatory reform can also entail costs, such as compliance burdens and administrative costs for governments and businesses. As well, it can sometimes have adverse effects on consumers' incentives and other unintended impacts.

The scope for reaping more benefits, without occasioning significant incremental costs, depends on the extent to which policy changes take the form of:

- (a) new laws constraining (inappropriate) business conduct;
- (b) complementary policies and regulations that improve the effectiveness of the existing laws that businesses must comply with;
- (c) measures to reduce the costs of existing policy arrangements; or
- (d) initiatives that harness market responses, through competition and innovation, and which deliver good consumer and societal outcomes without a continued need for detailed regulatory oversight.

The first approach, which is often a strong focus of policymakers and consumer advocates, has relatively modest further prospects of producing significant gains for Australian consumers. Additional layers of regulation aimed at changing business conduct will typically entail smaller marginal benefits than existing regulations, simply because the most important regulations are usually the first to be implemented.

Moreover, at some point, the additional complexity of regulation increases the incremental costs of regulatory compliance for business as economies of scope in dealing with new consumer laws are exhausted. Similarly, the cost of government administrative and enforcement arrangements rise as the number and scope of consumer provisions rise.

In these circumstances, both the diminishing marginal benefits (shown as MB_E in box 14.1) and the rising incremental costs of regulations (MC_E) increasingly curtail the possible magnitude of the benefits of additional regulation (shown as the area E in the figure).

However, the bulk of the Commission's recommendations do not involve new bars or rules governing the conduct of business. Instead, they are aimed at lowering the costs of consumer protection provisions, or increasing the impact of the existing set of consumer laws (table 14.1). This then raises the benefits associated with all existing consumer laws, while lowering their costs, shown as areas A, B, C and D in box 14.1. Such a broad-based approach has much better prospects of producing significant net benefits for Australian consumers than just devising regulations to curb apparently new forms of business misconduct.

So, on qualitative grounds, there are reasonable prospects of non-trivial benefits for Australian consumers from the Commission's suite of proposals.

14.2 Looking at the impacts in more detail

While it is useful to conceptualise the benefits and costs using the framework above, it is also helpful to understand the initial and long-run impacts of the proposals on the various actors in the system: consumers, businesses and governments. This can guide quantification, while at the same time building up a richer qualitative picture of the scope (and likely cumulative impacts) of the Commission's proposed reforms.

From a consumer perspective, there would be many initial positive effects of the new framework:

- a lower incidence of detriment (economic and emotional) from unsafe or otherwise defective goods and services and therefore, also less need to complain/seek redress;
- lower transactions costs in making purchases (products would be easier to compare, cutting the time spent on making comparisons; there would be less worry for consumers about whether a choice is correct; and better purchase outcomes);

Box 14.1 Qualitative analysis suggests that a suite of policies can yield substantial benefits

The figure below characterises the benefits and costs as the scope of consumer regulations affecting business conduct are widened. It is assumed that as regulations are widened, they initially complement each other, which is why there are temporary increasing returns. However, ultimately, the scope for significantly beneficial additions to regulatory arrangements diminishes — hence the steeply downward slope of the MB_E curve.

On the cost side, the incremental costs of consumer regulation rise only slightly at first, as most initial regulations are aimed at transparently bad conduct (for example, the prohibition of misleading conduct) and do not much affect businesses who work by the rule of trading fairly anyway. However, as regulations widen in scope, they tend to require changes in business practices of even good firms, record keeping and other compliance burdens, which push up the incremental costs of regulation more substantially.

The net gains from new measures therefore become increasingly smaller due to both diminishing marginal returns from those measures and increasing marginal costs. Ideally, regulation would cease at R_O . (The impact of the Commission’s proposals are shown as a move from the current level of regulations, R_E to R_C , but this is illustrative.)

More importantly than the shift from R_E to R_C , the Commission’s proposals shift up the marginal benefits of consumer regulation (from MB_E to MB_C), while lowering the marginal costs of regulation (from MC_E to MC_C). In the latter case, the Commission’s judgment is that the initiatives placing downward pressure on costs are greater than the few instances where policy initiatives increase those costs.

Analysis of policy changes

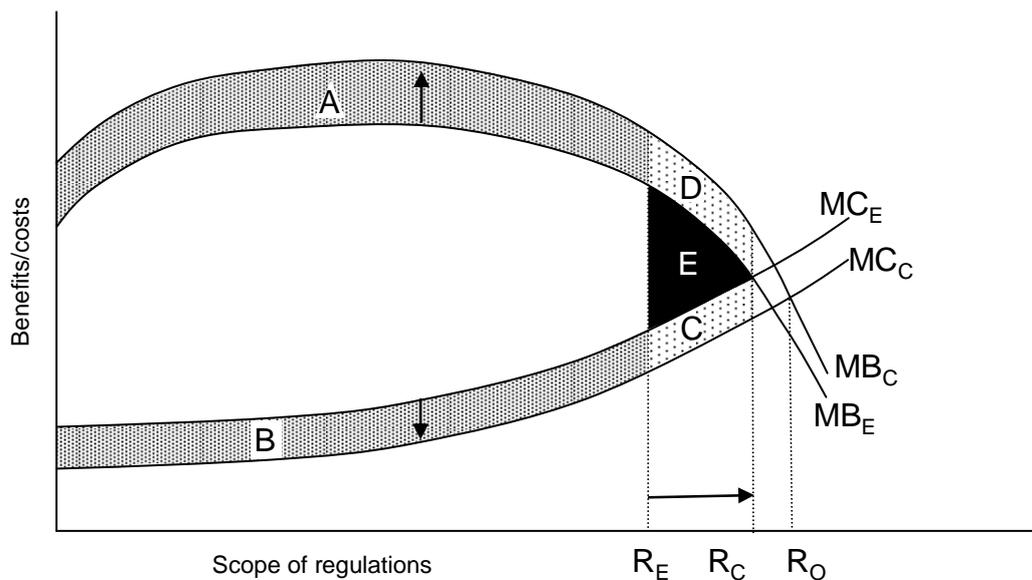


Table 14.1 The bulk of the Commission's recommendations are aimed at increasing the efficiency of existing consumer laws^a

Orientation of the Commission's policy recommendations

(a) New measures aimed at deterring inappropriate business conduct

Unfair contract provisions.

Licensing of finance brokers and licensing/registration of consumer credit providers to better address inappropriate lending and advisory practices.

Better protection for those having a home built or renovated.

(b) Increasing the impact of existing laws

One generic consumer law, operating nationally.

Better redress (better and more comprehensive ADR; better coordination of complaints; easier & cheaper access to redress for small claims; improved scope for representative actions; more funding for legal aid and financial counselling).

Better enforcement measures (eg additional enforcement tools; no carve outs from the generic law; shared data between regulators).

More comprehensible and accessible disclosure.

Better evidence base for the design of existing laws and an improved capacity for consumer feedback about appropriate policy design.

(c) Lowering costs

Elimination of needless variations in the generic law and some specific consumer laws (such as state variations in licensing and utility regulations).

Ongoing formal process for repealing unnecessary industry-specific consumer laws or dealing with costly variations in specific laws.

More cost-effective disclosure requirements.

Diversion of consumer complaints from more costly courts through improved ADR, and reducing the costs of actions in small claims courts and tribunals through provision for written submissions.

(d) Encouraging market responses

Improved enforcement and redress mean that poor business practices are punished and deterred, with the result that firms compete on fair grounds and consumers are more willing to trust unknown firms, lowering search costs and increasing competition and innovation.

A nationally coherent policy framework will reduce entry barriers for smaller firms.

More informed consumers make better choices (disclosure arrangements) and are more demanding, which, in turn, puts pressure on firms to improve their performance.

Move away from prescriptive regulatory approaches (such as some occupational licensing).

Better scope for co-and self-regulatory approaches (ADR provision).

^a Some of the Commission's recommendations have multiple benefits, and are therefore cited more than once.

- less costly and more effective redress. This would stem from improving ombudsman services, making small claims easier and providing greater access to class actions. Improved enforcement would also provide a lever for consumers seeking privately negotiated redress; and

-
- the gains from seeing fairer outcomes for others (such as, by punishing and deterring unfair practices and from better access to legal aid for the disadvantaged), and from enhanced consumer empowerment (by giving consumers a greater voice in public policy and a greater sense of control over their dealings with businesses).

In the longer run, there would be other benefits, including:

- price, choice and income benefits from better functioning markets generally. These benefits would arise because competition is stronger if consumers are willing and able to switch suppliers, can make well-informed judgments about competing products, and can punish dishonest suppliers through effective redress mechanisms. Good consumer policy then activates the benefits of competition, contributing to greater product variety, higher firm efficiency and most importantly an impetus for innovation and productivity. Effective consumer policy can also facilitate competition reforms. Governments can more easily make such reforms if the public is confident that consumer protection will be preserved. Hence, appropriate consumer policies (such as those developed for utilities) can speed up decisions to introduce contestability into previously sheltered industries;
- realisation of social externalities, which have flow throughs to both prices and tax rates or levels of government service provision (reduced demands on the health care system, and the social safety net); and
- the likelihood of more responsive policy — a key goal of the Commission’s proposals — which brings forward the benefits of policy change.

The aggregate downside risks of the Commission’s reform proposals for consumers appear to be low. For example, the Commission has chosen a prudent approach to deregulation of licensing arrangements that aim to ensure that only unnecessary arrangements are removed. Similarly, to ensure continued adequate enforcement of generic consumer law, the Commission has proposed that, at least for the time being, State and Territory consumer regulators remain jointly responsible with the ACCC for enforcing all bar the product safety provisions of the new national law (chapter 4).

Indirect costs and benefits for consumers

Costs for governments

The Commission’s reforms would require investments by governments in policy processes, regulation-making, and institutional change — all of which would involve transitional costs. For example, developing and implementing the proposed

national generic law would require new legal drafting, and negotiation by policymakers and ministers to achieve consensus. In a few cases, there would also be increased uncertainty until courts establish precedents. And in some instances, the measures proposed by the Commission involve, as their explicit intention, additional public expenditure (such as the extra funding for consumer advocacy and research, and additional resourcing for legal aid).

Costs for business

Some of the measures proposed would entail new transitory business compliance costs, requiring new information disclosure practices and re-formulated contracts.

Measures that alter the contractual balance in a way that shifts more risk onto suppliers could also be expected to raise upfront prices for consumers as businesses sought to cover, at least partly, their now higher costs (chapter 7 and appendix D).

Moreover, whenever consumers are given a greater capacity to seek redress, some will inappropriately take advantage of that provision, and others may not take as much care as warranted in their transactions ('moral hazard'). For example, while hardship provisions for essential services play a critical role in ensuring ongoing access to these important services for the disadvantaged, they may also increase the risk that some consumers are less careful in planning and containing their expenditure levels. This is also a risk with laws against unfair contract terms. Such effects push up costs for businesses, and eventually prices for consumers (and can be unfair to business proprietors).

There are analogous regulatory risks associated with the proposed new enforcement powers. The Commission presumes that regulators would generally use these powers proportionately and appropriately. Nevertheless, at the margin, regulatory errors might arise, reducing business efficiency and possibly even threatening some individual proprietors' reputations or livelihoods.

There are, however, several reasons why the business costs associated with such new powers are unlikely to be substantial:

- The abuse of these new powers and responsibilities would be tempered by their restricted scope, court oversight and other safeguards. Class actions, civil pecuniary penalties and banning orders require court decisions. There would be significant pre-conditions that regulators would have to satisfy before they could act on 'unfair' contracts under the Commission's proposal in this area. For example, the proposed regulation would not cover cases where a contract term was necessary to protect the legitimate interests of the business. Thus, contracts could legitimately include cost-based terminating charges.

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- In the case of the proposed new disclosure requirements, policy changes that are aimed at comprehensibility and brevity could ultimately reduce the *long-run* costs of compliance for businesses (noting that it has been businesses, as much as consumers, that have called for reform in this area).
 - Appropriate phasing of new measures and targeting at areas of greatest need would significantly reduce any accompanying burdens. Businesses are constantly altering their contracts, and sensible policy would seek to fit in with firms' natural cycles of contract and disclosure document changes.

Given the Commission's other policy initiatives that place downward pressure on costs, the Commission expects that its reforms would actually *lower* the overall costs of implementing current policies (the shift downwards in the MC curve in box 14.1). In particular, the Commission has proposed policies that would reduce unnecessary jurisdictional variation in regulations (for example, in the generic consumer law) and enforcement practices (for example, in product safety), that would remove regulations that have no sound basis, and that would curtail excessive regulatory prescription. As well as directly benefiting consumers, remedying these problems should reduce business compliance burdens. New enforcement tools may increase the effectiveness of the generic law, also reducing the need for future industry-specific laws, further cutting the costly variety of laws. And, ultimately, empowering consumers to act collectively in better functioning markets would be cheaper and more effective than detailed regulatory oversight of business.

14.3 Some implications of the qualitative analysis

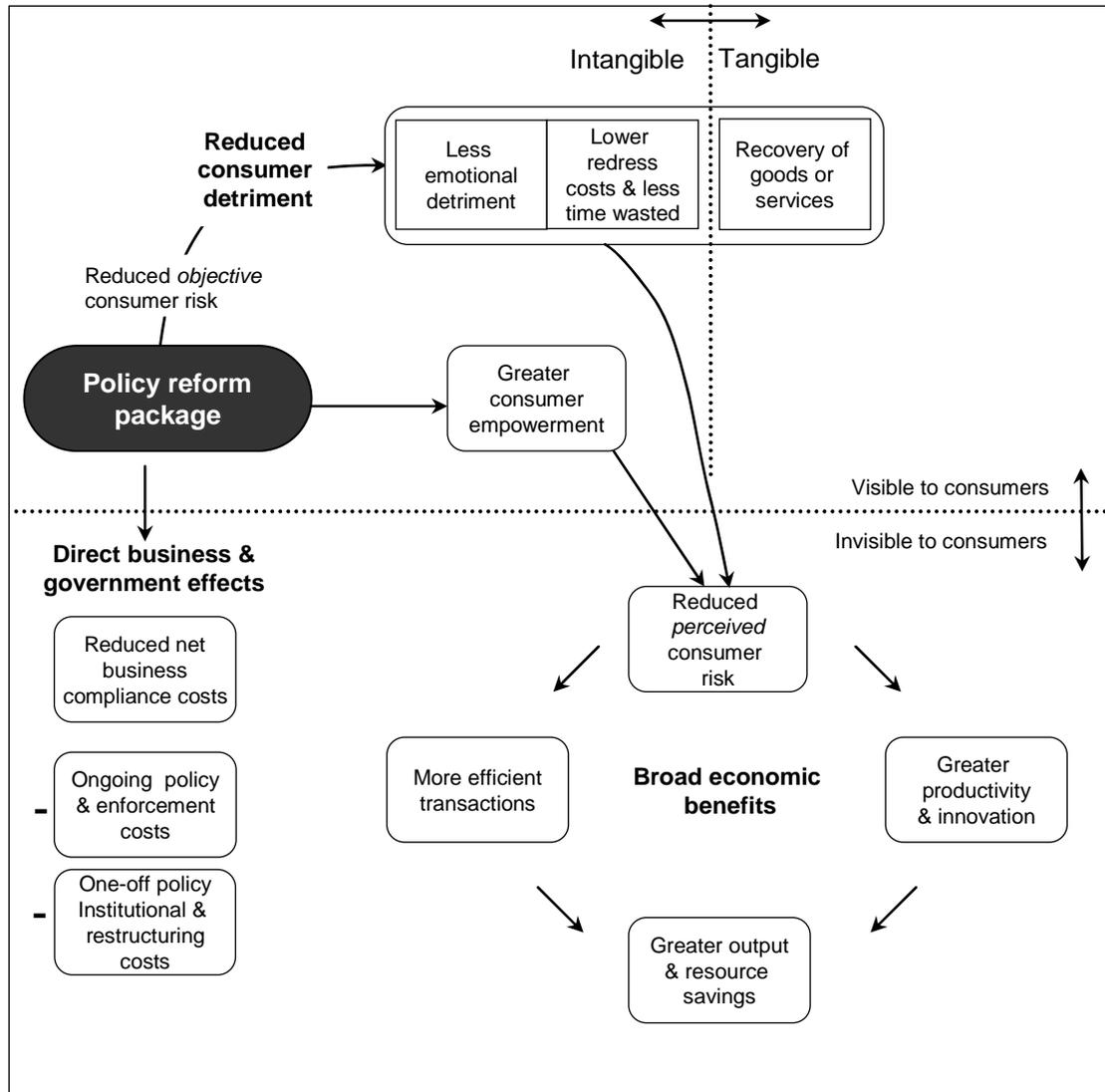
The preceding qualitative assessment provides several insights for a quantitative assessment.

First, from a consumer perspective, the Commission's proposals can be seen as lowering consumers' risks of detriment, giving them greater capacity to make informed decisions, and reducing the extent of detriment experienced when problems actually occur.

Second, such lowered risks would activate wider economic effects that are some of the most important sources of gains from reform for consumers, but which are largely invisible to them (figure 14.1). In particular, most consumers would be unaware of the importance of the cumulative effects on productivity, choice and innovation of just slight changes in the character of the billions of consumer transactions made each year in Australia. Consumers would probably also not foresee the gains realised from a more flexible future policy framework. This means that while it is important to understand the consumer perception of gains, any

quantitative assessment also needs to consider the less easily grasped diffuse benefits.

Figure 14.1 The impacts of policy reform



Finally, even among the gains perceived by consumers, many are intangible, rather than easily converted into dollar values — a fairer system, a greater sense of power, less time spent resolving problems and reduced distress. So even situations that might be seen as a zero sum game — the transfer of a profit from a supplier as compensation to a consumer for some business misconduct — can produce significant gains because of their intangible benefits. Despite the difficulties in valuing these (see below), they matter as much to a quantitative assessment as benefits that are priced in market transactions.

14.4 Quantifying these costs and benefits

It is impossible to undertake a precise cost-benefit analysis (CBA) of either the individual elements of the Commission's proposals or the proposed framework as a whole. As far as the Commission is aware, there have been no previous attempts to undertake such analysis of consumer policy as a whole. Indeed, this method has been only infrequently applied outside the much narrower field of product safety, reflecting the profound measurement difficulties in this area. Even in this field, the difficulties are often significant (box 14.2).

The nature of the Commission's proposals means that, in contrast to specific product safety measures, the Commission cannot draw on an established body of scientific information about the quantitative strength of the links shown in figure 14.1. That, and the fact that the Commission is assessing a package of reforms, rather than just one initiative, means that the potential for CBA lies generally at the more problematic end of the continuum of difficulty.

Against this background, there are several broad approaches to quantifying the prospective gains from the Commission's proposed reform to the consumer policy framework. The gains could be assessed by:

- attempting to quantify each element of the package and adding them up;
- examining how the package of reforms generates benefits and costs and, in particular, assessing its effect on consumer risks, and through these, the impacts on the wider economy. This approach would be informed by any evidence about impacts from individual reforms, but would not add them up; and
- considering different consumer regimes around the world and their characteristics, and seeing if it is possible through empirical means to isolate the effects of consumer policy settings on detriments and growth from other factors shaping these. This would entail a method similar to the research that has been undertaken on the broad links between regulation and productivity and other supply-side aspects of OECD countries (Broersma and Van Ark 2004; Alesina et al. 2003; Nicoletti and Scarpetta 2003).

The first approach has limitations, given the complementarities between individual reform measures, and in any case, would not be feasible given the scale of the task in measuring or judging impacts for each of the Commission's recommendations.

The third approach is conceptually sound and, on the surface, empirically tractable. However, the databases characterising the country variations in the type and nature of consumer policy are not developed. In any case, it seems unlikely that, given the imprecision in any such characterisations, econometric methods would be able to

robustly distinguish the likely small macroeconomic impacts from errors in the data and model misspecification.

In contrast, the second approach has fewer limitations. In particular, it can deal with complementarities and is more tractable since it relies on fewer judgments. Accordingly, the Commission has employed this approach to provide some indicative quantification of the benefits its proposed policy package might deliver for consumers and the community.

Box 14.2 Cost-benefit analysis in product safety

The nature of the difficulties in CBA for consumer policy can be illustrated by considering a concrete example where CBA is feasible, and understanding why these conditions are generally absent for the Commission's proposals.

In consumer product safety, particularly those involving well-known toxic chemicals:

- it is often the case that a regulation is able to specify and enforce a certain measurable level of some hazardous chemical — for example, the concentration of arsenic in a food;
- the costs of achieving these levels are measurable;
- there is also scientific evidence connecting different concentrations of such hazardous chemicals with various adverse health outcomes (dose-response data);
- while the costs of those outcomes are usually more difficult to measure, there are at least some empirical methods for doing so (treatment costs, the costs of death and so on). Consequently, while not necessarily straightforward, it is possible to measure costs and benefits; and
- confidence bounds based on clinical and industrial statistical evidence can be provided.

Therefore, at all stages of this CBA, there is scope to provide cardinal measures of the effects of varying regulatory options on toxicity, the dose-response effects, the associated costs and benefits associated with these impacts and some assessment of the confidence that can be placed on the results. Above all, for most aspects of the analysis (the cost of death aside) the approach is inherently scientific, in that it is possible for disagreements to be resolved through empirical testing. For example, as new evidence emerges about the health impacts of toxic chemicals, the CBA can be revised upwards or downwards, and reasonably evidence-based regulation is possible.

Yet even in a CBA of this nature, there are often unresolved empirical issues and uncertainty. For instance, in a recent Food and Drug Administration (2005) analysis of one new standard for bottled water, the range of net benefits was between -\$17 million and \$47 million (ignoring some unquantified benefits and costs), highlighting the imprecision of CBA even in cases where the data are relatively good.

14.5 Experimental estimates of the costs and benefits of the suite of reforms

At the outset, the Commission emphasises that the estimates of the costs and benefits are *experimental* because, reflecting data inadequacies, it has had to assume many of the key parameters and modelling choices. The Commission has selected parameters that appear sensible, checked the results as much as possible against any evidence, ensured internal consistency, and rigorously assessed the uncertainty of the results. In addition, it has attempted to limit the extent of discretion in the cost-benefit analysis by specifying conceptually sound, functional relationships between the key variables and using experience about the nature of these relationships to discipline the choice of parameters. (An example is the approach taken to productivity effects described later — the Commission has not conjectured a given impact, but derived it from a relationship between consumer risk and productivity growth.)

If nothing else, the value of such a quantification exercise is that it requires the complete specification of all the major factors that determine the value of policy outcomes, and requires explicit articulation of assumptions that may be implicit in a qualitative analysis.

The detailed assumptions underlying the Commission's quantitative estimates are in CMOD, an Excel-based simulation model, available on the Commission's website. The final version is easier to use and has several additional options than the version provided with the draft report. The model includes the provision for users to nominate different assumptions and see the outcomes.

Existing evidence on consumer detriment

The starting point for the Commission's analysis is evidence about the existing extent of consumer detriment since this determines the current level of consumer risk, which is a key initial target of policy reform. The only comprehensive assessment in Australia has used a survey, undertaken for Victoria by Consumer Affairs Victoria in 2006 (CAV 2006a — box 14.3) and partially updated in the 2007 Perceptions of Justice Survey (CAV 2007a). The 2006 Victorian survey largely replicated a UK survey undertaken in 1999 (UK OFT 2000).¹ When population

¹ The survey, based on responses from 2200 UK consumers, estimated consumer detriment of around £8.3 billion per annum (1.1 per cent of GDP), equivalent to £180 per adult. The comparable cost per Australian adult (aged 16 and over) in the calendar year 2006 would be around \$675 were the detriment to comprise 1.1 per cent of GDP. The UK OFT (2008) has

differences are taken into account, the two surveys found approximately similar levels of aggregate consumer detriment. This supports the credibility of the Victorian results as a benchmark for the Commission's model.

Box 14.3 Victorian studies of consumer detriment

Consumer Affairs Victoria undertook a survey of around 1000 consumers in 2006 to measure the extent of consumer detriment. Although the survey was comparable to the UK survey in its focus, it also included questions about emotional costs, impulse spending and several other issues. However, these broader aspects were not included in the aggregate estimate of detriment.

Some key findings of the survey were that:

- consumer detriment was estimated at \$3.15 billion per annum or around 1.45 per cent of gross state product;
- consumer detriment was distributed equally between three types of cost: repairing and replacing faults encountered in goods and services; following up and resolving problems (mainly out of pocket costs associated with travel, postage and telephone calls); and personal time (that could have been used more productively elsewhere);
- there were nearly 8 million different incidents of consumer detriment, with just over 60 per cent of consumers reporting at least one incident;
- the average cost of a problem with a good or service was around \$400, but there was great variation in average cost across different categories of goods and services — from less than \$40 per incident for food and drink to \$1600 per incident for building and renovations. Consumers faced an average of around 2 problems a year, which is why the average cost per consumer was around \$800; and
- the main causes of consumer detriment reported were defects (mainly manufactured items) and getting faults corrected.

Another empirical study, the Perceptions of Justice Survey, was undertaken by the Victorian Department of Justice in June 2007. Though less broad ranging than the detriment survey, it re-assessed the areas where consumers had experienced detriment. It found similar results to the 2006 detriment survey, suggesting nearly six million problems encountered by consumers in the state, with a gross cost to the Victorian economy of about \$2.8 billion (that is, about 10 per cent less than that reported in the detriment survey).

Sources: CAV (2006a, 2007a) and IPSOS (2006).

Consumer detriment in Victoria was estimated at \$3.15 billion per annum, equivalent to \$800 per Victorian adult or around 1.5 per cent of gross state product (box 14.3). This detriment includes repair and replacement costs met by consumers, and follow-up and time costs, but it contains no monetary measure of the emotional

recently repeated the UK national survey, finding consumer detriment of £6.62 billion in 2007, or about £135 per adult.

and various other intangible effects of consumer problems. Grossing up the Victorian data would imply consumer detriment across Australia of nearly \$13 billion in 2006.

Interpreting this value for the purposes of quantifying the impacts of the Commission's policy package is complicated, since it may over or understate the level of detriment that is the target of these policy changes. While the focus of policy reforms in this report are consumer detriments arising from 'unfair' or illegal behaviour by businesses and sub-optimal behaviour by consumers, detriments can also arise from:

- the outcomes of decisions by suppliers about quality control or managing supply that actually assist consumers in general. For example, the cost of implementing a zero defect rate in consumer electronics would be prohibitive, pushing up prices of these goods beyond what consumers would be prepared to pay; and
- innocent errors and misunderstandings by business staff.

Were these sources of 'innocent detriment' to be fully included in the CAV survey then it suggests that the detriment associated with problematic business behaviour and sub-optimal consumer behaviour might be significantly smaller than \$13 billion. However, the nature of the responses from the CAV survey implies that consumers often did not count innocent detriment as relevant, concentrating on cases where there was perceived misconduct by a supplier (box 14.4).

The CAV results also omit some sources of detriment relevant to the Commission's analysis. Putting aside the issue of emotional impacts, whose significance are sufficiently high to be considered separately, these omitted sources include detriments not perceived by consumers, some major consumer safety issues and the other factors described in box 14.4. These omitted sources alone, and the potential for consumer detriment to be lower in Victoria than other Australian jurisdictions, suggests that \$13 billion annually may still be a reasonable estimate of the gross direct costs (before emotional costs) to Australian consumers germane to this quantification exercise. Nevertheless, the Commission has marked down the estimate by 10 per cent to reduce the risk of overstating the relevant base level of detriment.

When emotional costs are added, these gross costs are likely to be significantly higher. Such emotional costs include annoyance, anxiety, frustration, stress and disappointment, among other negative feelings — and their existence as part of a failed consumer transaction represents as much an economic loss as pecuniary losses, though harder to measure. The Commission has assumed that such emotional costs contribute an additional 25 per cent to the standard measure of gross consumer detriment.

Box 14.4 Coverage of detriment by the CAV survey

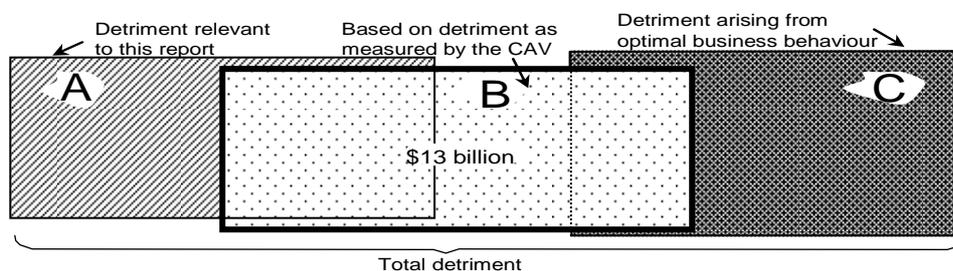
By the nature of any such surveys, the CAV and UK surveys do not cover all sources of consumer detriment. The surveys are unlikely to fully cover 'innocent' sources of detriment (C in the figure below). For example, while product defects are a commonly cited source of consumer detriment in the CAV and UK surveys, the nature of the answers suggest that consumers are more often citing cases where business conduct has been more problematic.² This omission reduces the extent to which the surveys might exaggerate the detriment relevant to the Commission's proposed policy reforms.

Moreover, quite apart from the emotional impacts of consumer problems, which the Commission analyses separately, the CAV survey omits other sources of detriment relevant to the Commission's analysis (A below), such as:

- unrevealed detriment. It is notable that in arguing for the greater power to take class actions under the TPA and for substantiation powers, the ACCC drew attention to business misconduct where consumers may be unaware that they are suffering detriment. By its very nature, any form of successful misleading or deceptive conduct will produce detriment that is not (at least immediately) perceived by consumers;
- the costs faced by consumers who, by the nature of the detriment experienced, are not represented in the survey (those, for example, who have died or been severely injured as a result of product safety problems);
- detriment to consumers that stems from some forms of costly or inappropriate regulation (as in some occupational licensing). This detriment will often take the form of higher prices for services, rather than something a consumer will categorise as business misconduct; and
- individually small, but collectively significant consumer problems. The focus of the CAV survey was on the 'most important problem'. The fact that people tend to forget small problems is likely to lead to an underestimate in this area. One illustration of this is the costs to consumers of unsolicited telemarketing calls. While the CAV rated this as a trivial consumer concern, other evidence suggests that, in aggregate, consumers see it as a more significant issue.³

Finally, participants often cited Victoria as having a tougher set of consumer policies, implying that there could be a lower level of detriment in that State relative to other jurisdictions. This is borne out, for example, by lower electricity disconnection rates — appendix F.

Judgmentally, it is possible that A and B are much the same magnitude.



² The inferential evidence for this is that in the CAV survey, consumers were generally dissatisfied with how suppliers responded to their detriment, often ceased trading with the supplier and told friends not to buy from them (IPSOS 2006). This is not usually true of routine problems with product failure or innocent mistakes by staff, in which trustworthy suppliers often replace or repair faulty goods under warranty with no fuss.

Several strands of evidence suggest such costs may be of this order (or higher):

- First, while the CAV survey did not enumerate emotional costs, it nevertheless found that 70 per cent of detriments experienced by consumers had high or very high emotional impacts, suggesting that the value of this intangible effect is considerable, and indeed could be higher than the monetary losses in many instances. CAV (2007b) also found large intangible impacts for consumers experiencing detriment related to unfair contract terms.
- Second, court outcomes likewise suggest that the emotional component of loss may be considerable. While courts in Australia and most other countries often have no legal capacity to provide damages for the emotional costs of detriment, they can do so when accompanied by product-related injuries and in certain cases for breach of contract (Holmes 2004, Thomas 2004, Chandler and Devenney 2007). When those circumstances arise, the compensation for distress and disappointment reveals these are a significant share of overall damages (box 14.5).
- Third, consumers are often willing to invest in time and follow-up costs an amount whose monetary equivalent exceeds the direct value of the loss that they have sustained, revealing the high value they place on fairness and justice.
- Finally, the emotional costs can be very high for some specific consumers and their relatives. A UK empirical study undertaken by the Office of Fair Trading of the impact of ‘scams’ (which included misleading or deceptive conduct, pyramid schemes and generally the more egregious aspects of business misconduct) found that many victims felt humiliated and embarrassed, with some groups affected severely:

Victims are often vulnerable people who may be in financial distress or are elderly or socially-isolated. The personal impact on them and on their families is often devastating in terms of future peace of mind and health. Victims can be left with damaged self-esteem and a reduced sense of self-worth. Victims suffer stress, anxiety and depression. Lives can be ruined. (UK OFT 2006b, p. 25)

In this context, while it is a judgment, a 25 per cent premium seems reasonable for the many kinds of distress arising from consumer problems — from annoyance and

³ The CAV survey (IPSOS 2006, p. 11, 20) estimated that there were under 60 000 cases of problem calls in Victoria in 2005-06, with most respondents citing just one call in the past year. CAV estimated this to have collectively cost Victorians around \$0.6 million. This implies roughly 240 000 problem calls for Australians generally, which is around 2 per cent of the more than one billion unsolicited telemarketing calls annually (p. 3, Explanatory Memorandum for the *Do Not Call Register Bill 2006*). Yet the evidence is that consumers dislike unsolicited telemarketing calls generally, and this has been strongly revealed by the registration of nearly 2 million household numbers with the Do Not Call Register in the short period since its establishment in May 2007.

embarrassment at the lower end of the spectrum of problems, to depression and extreme stress at the other.

Box 14.5 Court cases involving damages for distress and disappointment

Court damages for distress, disappointment and other emotional costs have often exceeded the monetary costs of detriment:

- A court awarded damages of \$5000 for disappointment after a cruise ship sank. This compared with a monetary loss from the uncompleted part of the journey of around \$1400 — so the damages for the non-pecuniary detriment were about 80 per cent of the total restitution (*Baltic Shipping Company v. Dillon* (1993) 176 CLR 344).
- A man who booked a Swiss holiday on the promise of a house party, yodelling, afternoon cakes and other attractions got effectively no party, a paltry show of yodelling and potato crisps as the cakes. The court awarded damages for disappointment equal to twice what he paid out for the holiday (*Jarvis v Swan Tours* in Atherton & Atherton 1999).
- A German couple who booked a four-day, supposedly relaxing and peaceful, cruise were awarded damages equal to half the cost of the trip because 500 of the 600 passengers were practising members of the Swiss Yodelling Association (Atherton & Atherton 1999).
- So-called ‘holiday cases’ of the kind described above routinely result in damages that exceed any restitution for the monetary losses involved (Atherton & Atherton 1999).
- A court awarded damages of £2500 for loss of ‘pleasurable amenity’ when a pool was built to a shallower (but fully functional) depth than stipulated in a contract — 100 per cent of the damages (Chandler and Devenney 2007).
- Damages of £10 000 for ‘discomfort’ were awarded due to aircraft noise at a newly purchased home, with the damages arising because a surveyor requested to investigate the potential for noise indicated no such noise was present (*Farley v. Skinner*, House of Lords [2001] UKHL 49).
- An Australian tribunal awarded more than \$26 000 for mental distress as a result of faulty renovation that led to complete collapse of a house (4 per cent of a total damages bill of \$630 000) (*Michellis v Carlos Steenland Pty Ltd and Meier Corporation Pty Ltd* [2006] CCT B213-05).

Often courts have applied the notion that such losses represent reductions in ‘consumer surplus’, bringing an explicitly economic approach to assessment of detriment. However, while a useful indicator of the importance of non-pecuniary detriment, these examples miss other situations where ‘emotional’ damages may arise. As a matter of jurisprudence, court-based damages do not extend to many instances when non-pecuniary detriment may arise, nor to cases of irritation or nuisance (such as those that consumers can experience with unwanted unsolicited telemarketing), despite the fact that such nuisance has as much validity in an economic sense as other sources of detriment.

Given such a premium, the relevant gross consumer detriment — before the Commission’s policy reforms — amounts to about \$14.3 billion or 2.6 per cent of household consumption in 2006.⁴ The latter figure could be characterised as an *objective* risk measure for consumers. When they engage in transactions, they face a small risk that they will suffer detriment. The main aim of an improved consumer policy framework is to lower that risk.

Consumer risk has another dimension too. While *objective* risk determines the amount of actual direct detriment suffered, *perceived* risk determines how consumers behave in markets (appendix B). This perceived risk influences the ‘invisible’ indirect consequences of policy reform that are elicited through productivity gains and transaction efficiencies (figure 14.1 and later). Given the behavioural evidence that consumers, on average, tend to overestimate the real likelihood of unpleasant events that are outside their own control, the Commission has assumed that perceived risk is 10 per cent higher (not percentage points) than the objective risk.⁵ Quantitatively, this implies a perceived risk before policy reform of about 2.86 per cent of household consumption in 2006.

The main direct impacts of the Commission’s reforms on consumers

The principal impact of the Commission’s reforms will be lower consumer detriment. The extent of that reduction depends on two opposing factors.

- On the one hand, the Commission’s proposals are both comprehensive and significant, suggesting good prospects for reduced detriment. As shown in table 14.1, the proposals encompass additional tools, better redress mechanisms, consumer empowerment measures, greater coherence of the new framework and a capacity to address national problems more quickly. (The broad nature of these proposals contradicts the claim by the Victorian Government (sub. DR226, pp. 103-4) that the thrust of the Commission’s reform suite is merely eliminating undesirable variations in consumer policy between jurisdictions.)
- On the other hand, some detriments are hard to avoid, especially in a system that is already reasonably satisfactory. Policy intervention will never fully address deficiencies in market outcomes and will sometimes simply supplant market responses to them, rather than providing an additional benefit.

⁴ That is, \$12.7 billion $\times 0.9 \times 1.25 \cong$ \$14.3 billion.

⁵ There are offsetting factors influencing this estimate. On the one hand, where consumers are aware of detriments, they probably exaggerate risk by a greater amount than that implied by the 10 per cent adjustment assumed. On the other hand, consumers are not aware of some of the detriments they experience. In that instance, perceived risks must be lower than the actual risks.

There is insufficient rigorous evidence to precisely estimate the balance of these two factors in quantitative terms. That lack of evidence was noted by the Victorian Government in critically commenting on the Commission's draft report (sub. DR226, p. 103), but this deficiency applies equally to any others' reform proposals, including the alternative package put forward by the Victorian Government.

In the absence of suitable evidence, the Commission has had to make a judgment about the impacts of its proposals. As in the draft report, the Commission has assumed a 5 per cent reduction in detriment stemming from its policy reform package.⁶ This judgment is based on a weighted average of different levels of gains for the various sources of detriment categorised by CAV. The Commission envisages smaller gains in some areas of detriment identified by CAV (for example, in relation to defective goods), but bigger gains in other areas (such as inappropriate selling practices where the policy reforms are likely to be of greater significance). The Commission's assumption is in line with the speculative assumption used by the Department of Trade and Industry in the UK in their regulatory impact statement on the adoption of the European Union Unfair Commercial Practices Directive (DTI 2007, p. 13). And, that directive encompassed a narrower set of reforms than those proposed by the Commission.

A 5 per cent reduction in detriment produces substantial gains. The gross gains — including the reduced emotional costs — would be around \$850 million in 2008-09 for Australian consumers.⁷

Of course, some of the apparent benefits to consumers are gross, not net, benefits, because they involve transfers from suppliers to consumers. That is, there is a cost of forgone income for suppliers associated with the new regulatory regime. However, the need to adjust detriment for transfers applies only to such pecuniary, market-valued, transactions, and not to non-pecuniary detriments such as time used or emotional costs. The Commission has assumed that half of the *pecuniary* benefits gained by consumers are actually transfers from business owners. The difference this adjustment makes to the total impact of the proposed reforms is quite modest because around 70 per cent of the gains from reduced detriment are non-pecuniary in nature. After taking account of the transfer components of the gross gains, the Commission estimates that the net gains to consumers might be around \$700 million in 2008-09.

⁶The Victorian Government (sub. DR226, p. 103) considered the Commission's 5 per cent assumption was too high, but this appears to reflect a narrow view about the scope of the Commission's reforms. In any case, the Commission has publicly provided its model so that others can make their own assessments based on what they believe to be justified assumptions

⁷ That is, the objective risk (0.026) × the effect of policy reform (0.05) × (household consumption in 2008-09 (about \$650 000 million) = the gross benefit from reduced detriment (\$845 million).

The gains would grow over time

These benefits are sustained, and in fact, are likely to increase with economic growth. This is because they are connected to the value of consumer transactions, and these transactions increase at about the same rate as the growth in the economy.

In this context, it is useful to be able to compare benefits (and costs) after taking account of the fact that they can occur at different times. One approach is to derive a value today that reflects the discounted stream of future costs and benefits.⁸ Another is to estimate the fixed annual amount that such a discounted value could finance forever — its ‘annuity’ value — in effect, the permanent dividend each year that Australians obtain from reform. In this exercise, the Commission has used both present value and annuity measures, but focuses on the latter since it better reflects the average gain realised by consumers each year.

The Commission estimated future household consumption as a fixed share of future GDP (with the GDP estimates derived from the Commission’s MoDEM model — Cuxon et al. 2007). The reduced consumer detriment from a new consumer policy framework can then be applied to the forward estimates of household consumption. Using a discount rate of 6 per cent, the net present value of these gains in 2008-09 (in constant 2006-07 prices) is around \$20 billion, or an annuity value of \$1200 million — testimony to the large benefits of reforms that have a sustained impact.

In fact, in welfare terms, the gains of such reduced detriment could be larger, since a monetary loss to a poor consumer has a bigger welfare cost than the same loss to a richer one. However, for the reasons set out in box 14.6, the Commission does not take account of this in its summary measure of the impacts of its proposed policy package.

Nevertheless, the point remains that the benefits are likely to be higher were the Commission’s measure of the impact of its proposed reforms to include the welfare effects associated with reducing detriment among people with different income levels.

On the other side of the ledger, the Victorian Government (sub. DR226, p. 105) argued that disruption associated with the introduction of a new national generic consumer law might temporarily increase some consumer detriments due to the diverted focus of the agencies involved in the transition. However, the

⁸ The net present value is the value to Australians now of all the future stream of benefits and costs from reform, taking account of the fact that people prefer gains now to gains later. Hence later net gains are discounted using a discount rate, often set at between 5 and 7 per cent.

modifications the Commission has made in this area to its draft report proposals in response to representations from the Victorian Government and others (see chapter 4) should help mitigate such effects. Second, the Commission's proposed model for a national generic consumer law would incorporate valuable features in the Fair Trading Acts that are not currently in the Trade Practices Act — implying less disruption. There is, in any case, little evidence that past consolidations of state-based laws have eroded regulatory standards over any transition.

Box 14.6 The welfare impacts of reduced detriment

Using analysis from the London School of Economics on the UK survey data on detriment, the Office of Fair Trading (UK OFT 2000, p. 21) estimated that the monetary loss from consumer detriment should be marked up by about 16 per cent to take account of the higher weight given to detriment affecting lower income consumers. The OFT applied this correction to the total measure of consumer detriment estimated for the UK. Were the same ratio to apply in Australia, this would imply that the welfare gain from reduced net detriment is around \$840 million in 2008-09 (with the stream of future benefits having a present value of about \$24 billion).

While noting this estimate, the summary of the results at the end of this chapter does not include this adjustment because:

- the UK estimate may not be appropriate for Australian data since income distributions associated with detriment may vary between the two countries;
- the gains from the Commission's proposed reforms may not be uniformly spread among different income groups;
- the appropriate marginal elasticity of welfare with respect to income, which is used to calculate the mark-up, is subject to many measurement and other problems;
- it is not clear whether some costs, such as emotional costs (which are included in the Commission's estimates above), should also be weighted this way; and
- it is not usual to make this adjustment, so that comparisons with quantitative measures of the impacts of other policy reforms will not be comparing like with like.

The indirect effects on consumers are also likely to be significant

The above gains can be perceived by consumers. But as noted earlier, some important gains occur because the general functioning of the economy has improved without consumers readily able to see these gains as emanating from a better consumer policy framework. The Commission has modelled two dimensions of this:

- the links between consumer policy and productivity/innovation; and
- the efficiency of transactions in the economy.

Productivity and innovation effects

There is little empirical evidence about the link between consumer policy and productivity growth, but the theoretical basis for a link is sound. There are two main routes by which innovation (and in turn) productivity can be stimulated by an improved consumer policy framework.

- First, most consumers are risk averse with important effects on their market behaviour. As the risk of detriment rises, consumers rely on more established firms. (Indeed, were the risks to be extreme, consumers would ultimately produce goods themselves, rather than rely on markets.) Undue reliance on established and known firms will reduce specialisation, competition and the potential to sell novel products, undermining productivity growth. The constrained use of the Internet provides an illustration of the impact of risk on consumer behaviour that has been relatively well researched (chapter 13 and box 14.7) and demonstrates that distrust and perceptions of risk can frustrate the growth of innovative new areas of the economy. The same forces that operate so conspicuously online have their less obvious counterparts in everyday transactions in the physical world. The key message is that higher consumer risks can affect consumer behaviour significantly, with collateral damage for innovation.
- Second, knowledgeable and demanding consumers provide feedback and advice about products, putting greater competitive pressure on suppliers and stimulating innovation (Porter 1990). The Commission's proposed reforms would give rise to benefits of this sort by increasing consumer empowerment (chapter 11). Such empowerment can also be conceptualised as reducing the perceived risks of transactions.

That said, the extent to which risk abatement from more effective consumer policy stimulates innovation might be tempered under some circumstances. Sometimes prescriptive regulations inhibit innovation directly (for example, regulators may prohibit some new types of financial instruments that are regarded as too risky) or work against new entrants, providing implicitly anti-competitive protection of incumbents and reducing incentives for innovation through that route.

However, since the recommendations in this report are mainly oriented at improving the functioning of existing laws, rather than creating new ones, perverse effects of this kind are not likely to be relevant. In fact, many of the recommendations are aimed at promoting less prescriptive arrangements and greater regulatory accountability. This should, if anything, reduce the adverse impacts of the present consumer policy regime on innovation and provide an additional fillip to productivity.

Box 14.7 Use of the Internet is affected by distrust

The Internet has a clear role in increasing competition, reducing prices and stimulating innovations. It has led to new services, like email, IP-telephony, YouTube, Google, eBay and a multitude of intermediation services in financial, airline ticketing, real estate and second-hand car purchases, often at lower prices than their physical counterparts. For example, in life insurance, the growth of the Internet reduced term life prices by 8 to 15 per cent in the 1990s (Brown and Goolsbee 2002).

Yet many people limit their use of the Internet for consumer transactions because of perceived risks of identity theft, payment security, misleading product descriptions, and non-delivery. Even of those who do undertake financial transactions, a significant minority reduce their risk by only dealing with well-known organisations online and limiting the value of transactions (DCITA 2005b). Such distrust limits the potential impact of the Internet on competition and innovation. Surveys of consumers suggest that greater trust would result in significantly greater Internet sales (Empirica and German Institute for Economic Research 2007).

Consequently, the Internet provides a case study where perceptions (and actual) risks lead to some consumers making no purchases at all and others to mitigate their risks by significantly reducing their transactions.

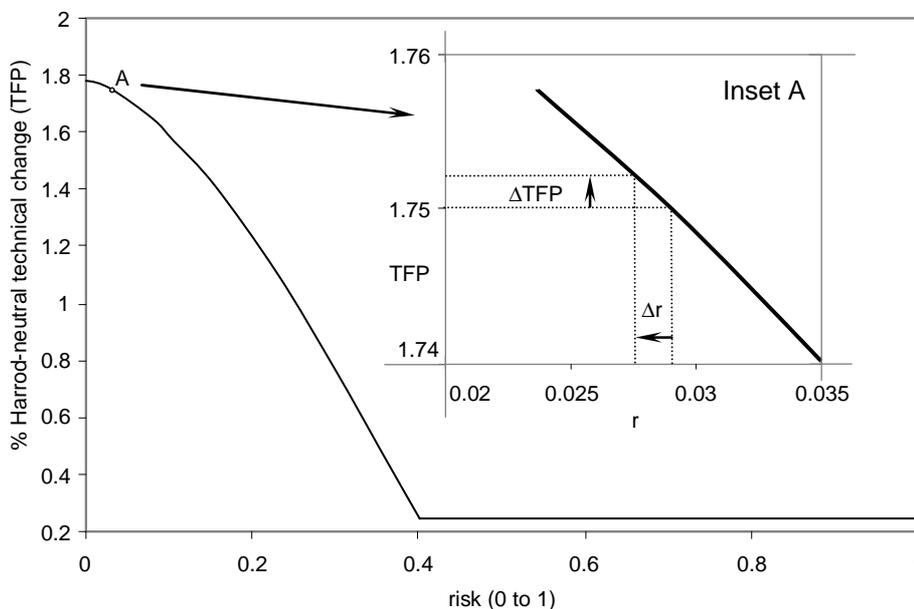
While obviously conjectural, the Commission has characterised a relationship between perceived consumer risk and productivity change, incorporating a number of features (such as diminishing marginal returns to productivity gains as risk is reduced) to ensure that the relationship is well-behaved and theoretically sound over the full spectrum of consumer risks (see CMOD). A big gain in productivity growth rates could be expected if consumer risks were high and policy were to reduce these significantly. However, since the current consumer risk is already low, the likely gain in productivity from what is a small reduction in risk would also be very small (figure 14.2). This result is robust to variations in the key parameters of the particular functional form adopted by the Commission, or of alternative forms that preserve the sensible properties that any such relationship must have.

Using the conjectural relationship shown in figure 14.2, the reduction in consumer risk increases productivity growth rates from a steady state 1.75 per cent per annum⁹ to 1.7522 per cent. While this is an extremely small increase in percentage point terms, it represents a non-trivial 0.13 per cent increase in the productivity rate

⁹ As used in the Treasury's two Intergenerational Reports and the Productivity Commission's 2005 report on the implications of ageing.

(that is, $100 \times 0.0022 / 1.75$). This would lead to higher output in the economy (GDP) and to greater consumption.¹⁰

Figure 14.2 The gain in productivity is small, but cumulatively important^a



^a A 'power' function is used because it ensures diminishing marginal gains from reductions in risk (concavity) and is relatively simple. The function is appropriately constrained at the highest and lowest risk levels. On the one hand, the maximum productivity gain is reached at zero risk. On the other, the lowest productivity growth rates are fixed at some sufficiently high rate of consumer risk (where consumers no longer trade in markets because risks are above a threshold). The effects of lower (or higher) risk levels have a sustained effect on productivity growth, since the nature of markets is permanently affected by consumer behaviour.

This postulated gain is nevertheless much smaller than the benefits achieved from policy reforms targeted at the supply side of the economy. For instance, the Commission's modelling of the wide-reaching reforms associated with the National Reform Agenda suggested an increase in the productivity rate of 0.07 points (Lattimore 2007, p. 283).¹¹ This is about 30 times the effect of the reforms discussed in this report (that is, $0.07 / 0.0022 = 31.8$). In the Commission's view, this relative magnitude is in line with the different scales of the reforms and provides one check on the plausibility of the estimate.

While the productivity changes induced by the Commission's proposed policy reform package would have only small immediate benefits for Australians, the effects nevertheless accumulate over time, and become important in absolute terms

¹⁰ The benefits for Australians from GDP growth arise from the accompanying increase in consumption levels. These consumption benefits are measured by multiplying the forward estimates of GDP by the long-run ratio of *total* (government and household) consumption to GDP.

¹¹ A difference, however, is that this gain in productivity growth is a transitory one, since it reflects the gradual impact of human capital and other reforms on the *level* of productivity.

because the economy is so large. The discounted present value in 2008 of this small change in productivity growth is about \$14 billion in 2006-07 prices (with an annuity value of \$800 million), *if the gains are perpetual*. However, over the long run, the nature of the consumer environment will change significantly, and the benefits of the Commission's reforms are much more uncertain. If only the gains realised over the next 40 years are counted, the present value of the benefits would be about \$6 billion (with an annuity value of around \$400 million).

Reductions in transaction costs

A second intangible gain to consumers emerges from the likely incremental improvement in the efficiencies of transactions. A better consumer policy framework should act, at the margin, to improve consumer trust, and to reduce the private investments that consumers make to reduce the risks of detriment (such as search costs, resources used in intermediary services and so on).

Such transaction costs are not measured by existing consumer detriment studies, which relate only to cases where consumer transactions go wrong. In contrast, the cost of 'due diligence' affects all consumers all of the time. House break-ins provide an analogy. On the one hand, there are highly visible costs of actual break-ins and the damage that this causes. On the other, there is a less visible cost component of alarms, locks and behaviours (like anxiety about leaving the house untended), that is at least as significant.

There are few estimates of the amount of economic activity taken up to reduce the relevant consumer risks. It is well established that transaction costs in general are highly significant parts of modern economies, accounting for around 50 to 60 per cent of GDP (Wallis and North, 1986; Dollery and Leong 1998; Wang 2003). These costs include, for example, insurance, information services, and financial intermediation. Moreover, whereas these studies examine market-valued transaction costs, a significant portion of consumer transaction costs is unpriced search time. That said, most of the economy's transaction costs are not relevant to the risks of detriment that consumers face in markets. In that context, the Commission has assumed that the costs of actions taken by consumers to avoid detriment are one per cent of household consumption in the base case.

The Commission has further assumed that a one per cent increase in consumer risks increases these transaction costs by one per cent, though CMOD allows other elasticities to be used. Given the initial conjecture that the relevant transaction costs are around one per cent of household consumption, then the reduction in risk

resulting from the Commission's proposals¹² generate a gain of around \$300 million in 2008-09 and would grow at the same rate as household consumption in subsequent years. If the gains were sustained forever, their annuity equivalent would be around \$500 million.

Compliance burdens

Another set of transaction costs are experienced by business. When these are in response to regulation, they are referred to as compliance burdens. The Commission's recommendations have positive (cost-increasing) and negative (cost-decreasing) effects on such burdens, but with the net result likely to be a cost saving from reduced burdens.

On the one hand, legal advice,¹³ diversion of management and staff time, and printing and distribution costs associated with dealing with any unfair contract terms will increase business compliance costs (appendix D). In addition, enhanced enforcement and redress mechanisms may cause some firms to devote greater resources to monitor employees more carefully to ensure they act appropriately (so-called 'agency' costs). Credit providers and those providing advice on credit products that are not currently subject to licensing or registration requirements would also face additional compliance burdens under the Commission's proposed policy measures in this area. And there may be transitional costs for businesses as they deal with the convergence of multiple state laws (as raised by the Victorian Government, sub. DR226, p. 105). However, it is notable that energy businesses have not pointed to any sizeable transitional costs arising from the consolidation of divergent retail energy laws — and, in fact, have argued for more speedy and widespread reform in this area.

On the other hand, for the reasons discussed before, overall compliance burdens are likely to fall, reflecting simpler disclosure requirements, the elimination of a possibly significant number of occupational licenses, and the removal of variations in generic law and some specific laws.¹⁴ On the latter point, it should be noted that while the majority of businesses (by number) operate in only one jurisdiction, some 50 per cent of the national turnover of businesses operating in consumer markets is accounted for by multi-jurisdictional businesses (chapter 4). Consequently, state variations in laws still have impacts on compliance costs.

¹² This includes risk reductions that emanate from improved disclosure arrangements, which should facilitate easier product comparisons and lower transaction costs.

¹³ The costs of litigation are dealt with later.

¹⁴ Reductions in licence fees are **not** included as reductions in compliance burdens because they are transfers, not resource costs.

The gains from lower compliance costs are likely to be smaller than the benefits from reducing detriment and from productivity improvement and transaction cost efficiencies. On the available (slim) evidence, business compliance burdens associated with consumer policy altogether are relatively modest, so incremental changes of the kind proposed by the Commission must be smaller again.

For instance, a small-scale survey of NSW business chamber members in 2007 found that administration of the Trade Practices Act (which covers both competition and consumer policy) was the least of nine regulatory concerns (NSW Business Chamber 2007). Canadian research also identified consumer protection requirements as the smallest concern among nine regulatory sources of compliance burdens (Jones and Gartner 2004). And a more detailed survey of businesses in the UK, which has similar consumer laws as Australia, suggests that costs of complying with consumer regulation in that country were negligible compared with other regulatory requirements (Allinson et al. 2006). According to that survey:

- Of an exhaustive set of regulatory concerns, consumer policy was ranked only 29th most important by business.
- Most businesses used the simple heuristic of ‘trading fairly’, rather than spending much time learning about consumer regulation in detail.
- Nearly half of the businesses surveyed were unable to indicate total hours spent on consumer legislation and those who provided estimates gave low figures.

That said, businesses might not always perceive some regulations, such as occupational licensing, as consumer policy, so compliance costs may be more significant than the preceding evidence suggests. In addition, the UK results reflect a non-federal system, whereas a significant concern in Australia is the small, but nuisance, variation in generic law and its enforcement, and more particularly the differences in statutes and subordinate regulation of specific consumer regulations (such as in utilities — appendix F). In any case, the fact that compliance burdens associated with consumer policy appear to be generally smaller than many other regulatory burdens does not mean they are trivial, and they can be significant for some firms and industries.

In order to develop a better picture of the compliance cost savings that might arise from introducing a single national generic consumer law and a generally more national approach to consumer policy, the Commission undertook a small but detailed telephone survey of the impacts of interstate regulatory differences in consumer policy. This encompassed business associations and a small number of very large Australian businesses that operate in multiple jurisdictions. Although the firms concerned were generally unable to provide a quantitative assessment of the

cost of interstate variations in regulatory requirements, they observed that the costs can be considerable because:

- training costs associated with variations can be high and are amplified because many staff are part-time;
- the variations are confusing for staff and lead to errors, which in turn have to be monitored (agency costs);
- IT costs are a critical part of service sector businesses and variations in state laws can sometimes require state-specific solutions;
- firms require ongoing expert legal advice; and
- management time is deflected to ensure compliance with each jurisdiction's specific variations.

One company pointed out that just a single change by a jurisdiction to one apparently 'minor' regulation for just one product cost \$1 million to implement.

Moreover, the compliance cost gains from a new, more nationally-oriented framework are not just those associated with eliminating the current variations. There will be gains from preventing those that would otherwise inevitably arise in the future — the Commission's proposed national generic consumer law should provide an on-going antidote to the threat of future variation in State and Territory generic requirements.

The Commission modelled compliance costs by combining:

- data on business size distribution in consumer industries and the extent to which such businesses trade interstate;
- assumptions about the relationship between compliance cost savings and firm size; and
- assumptions about the link between compliance cost savings and exposure to multiple consumer regimes (which would be addressed by the Commission's recommendation for a single national generic consumer law and by various other initiatives that would remove industry-specific arrangements or consolidate them at the national level).

The assumptions are based on judgment (with the details specified in CMOD).

The net impacts, while smaller than from other sources of gains from the proposed reform package, are non-trivial, with a net annuity value of about \$100 million in 2006-07 prices (table 14.2).

Table 14.2 **Impacts of reforms on compliance burdens^a**
2008-09

		<i>Annual saving in 2008-09</i>	<i>Present value</i>	<i>Annuity value</i>
		\$m	\$m	\$m
A	Gross ongoing compliance cost savings	64	1 813	109
B	Gross new ongoing compliance costs	6	164	10
A-B	Net savings in ongoing compliance costs	58	1 649	99
C	One-off compliance costs associated with the new policy framework ^b	20	20	1
A-B-C	Net impact (savings)	38	1 628	98

^a Present value calculations are based on discounting all future streams back to December 2008, while annuity values are for 2008-09 and all subsequent years. All values are in 2006-07 constant prices. A discount rate of 6 per cent was used. ^b As well as ongoing costs included in row B, there would be one-off costs associated with the introduction of a national unfair contracts provision (with the values based on judgment and UK evidence about the compliance costs of the introduction of the unfair commercial practices directive, as discussed in appendix D).

Source: Commission calculations based on CMOD.

Administrative, court and other costs

The proposed new framework would provide for more stringent but more layered enforcement (chapter 10), with some additional court and administrative costs and a stronger on-going policy function. The court-related expenses of contesting businesses and the proposed additional funding of some consumer empowerment measures are also resource costs that need to be considered. In addition to these on-going costs, there would be one-off costs associated with the re-organisation of the existing framework, such as those involved in re-drafting legislation and in shifting the enforcement of all credit regulation from the Fair Trading Authorities to ASIC. Overall, under the assumptions detailed in CMOD, the Commission estimates that the net costs of these have an annuity value of about \$25 million.

The Commission has not included the costs associated with the proposed additional injection of funding into legal aid and financial counselling in this amount because the appropriate level of funding depends on a complex range of factors. However, the exclusion of these costs will not materially affect the assessed total impact of the policy reform package (and in any case, some of the intangible benefits from such measures are not included in the benefits either).

What has *not* been quantitatively assessed?

The Commission's recommendations for a new framework have some important elements whose effects are captured incompletely by the quantitative assessments above. The excluded or only partially covered elements include:

- the effects of removing retail price regulations;
- the allocative efficiency gains, as opposed to the productivity effects, from price reductions flowing from reduced business entry barriers (reflecting greater consumer trust of less known firms, the reduction in business compliance costs as jurisdictional regulatory differences are minimised, and changes to occupational licensing);
- more policy responsiveness, once some of the cumbersome features of the current institutional arrangements are overcome or reduced;
- some of the future, more uncertain benefits that could emerge for firms and consumers from a complete re-consideration of industry-specific consumer laws;
- any benefits associated with a conditional long-run shift to a single national enforcement agency for the proposed new generic law, contrary to the claim by the Victorian Government (sub. DR226, p. 103) that these benefits are included in the Commission's analysis; and
- some of the intangible benefits that might arise (for example from the public health benefits of better food labelling).

Such exclusions suggest that the overall gains from the proposed reform package would be greater than the preceding quantitative exercise suggests.

A summary picture of the gains and their sensitivity

The most important gains from the Commission's proposed reform package arise from three sources: the reduction in consumer detriment, dynamic gains through enhanced productivity and innovation; and reduced transaction costs in the economy (table 14.3). The gains appear very large when given in present value terms — but this is because they represent all present and future gains. As noted above, the numbers to emphasise are the annuity values — the magnitude of the gain that Australians can typically expect to realise on an annual basis. The Commission estimates these to be around \$2.7 billion a year.

The values shown in table 14.3 are rounded to the nearest million — the usual way of representing estimates of this kind. However, such estimates exaggerate the real

degree of precision in the estimates, which rely on extensive judgment and assumptions.

To explore the sensitivity of the results, the Commission undertook various simulations using Monte Carlo analysis (with the method and its details described in CMOD). Arguably, this method is more appropriate than the ‘high, medium low’ method often used in cost-benefit analysis, which fails to recognise that the probability of deviation from a base case measure should significantly fall the further a parameter moves away from that value.

Importantly, the results (table 14.4 and figure 14.3) show that the conclusion that there are likely to be significant benefits from the proposed reform package is not altered by the uncertainty about the parameters. Reform of the framework will probably produce net annuity gains for Australians somewhere between \$1.5 billion and \$4.5 billion — still a sizeable figure at any point in this range.

Table 14.3 Summary of impacts of a new consumer policy framework^a
2008-09

	<i>Present value</i>	<i>Annuity value</i>
	\$m	\$m
Net avoided direct detriment for consumers	20 514	1 231
Reduction in risk-based transaction efficiencies	9 166	550
Gains from increased innovation/productivity	14 033	842
Net gains from reduced business compliance costs	1 628	98
All legal and administrative costs	-399	-24
Net gain	44 943	2 697

^a Present value calculations are based on discounting all future streams back to December 2008, while annuity values are for 2008-09 and all subsequent years. A discount rate of 6 per cent was used. All values are in 2006-07 constant prices.

Source: Commission estimates from CMOD.

Finally, while the Commission’s experimental estimates strongly suggest worthwhile returns from the proposed policy package, they highlight inadequacies in some of the data that could be used to assess the impacts of consumer policy generally. Aside from the recent Victorian survey of direct consumer detriment, national data on key problems that the policy framework is intended to address is lacking. This includes data on deaths and injuries from unsafe products and the extent of detriment suffered by consumers from problems with unfair contract terms and because of inadequate enforcement tools. The areas of uncertainty highlighted in CMOD provide some guidance to data and information needs for evidence-based policy development. These should be priorities for support from the additional research funding that the Commission has recommended (chapter 11).

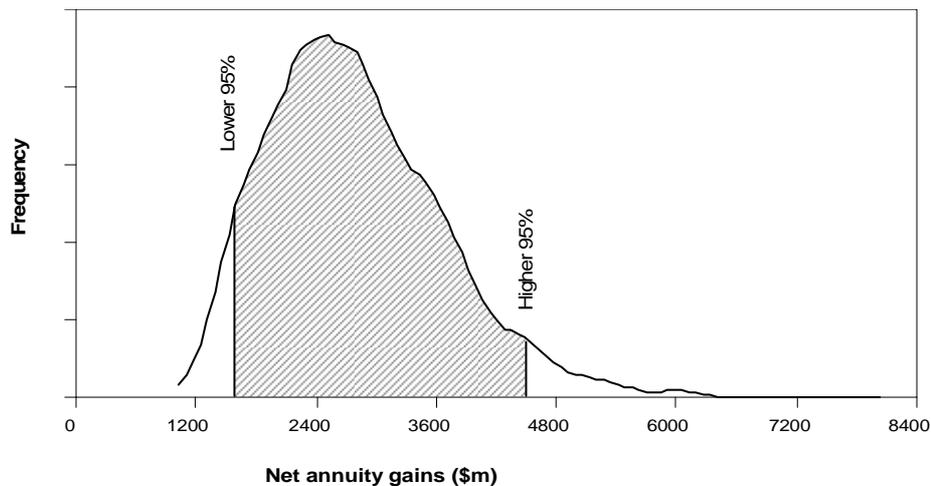
Table 14.4 Simulation analysis of the annuity gains from reform^a
2008-09

	<i>average</i>	<i>sd</i>	<i>max</i>	<i>min</i>	<i>5% percentile</i>	<i>95% percentile</i>
	\$m	\$m	\$m	\$m	\$m	\$m
Net avoided direct detriment for consumers	1 255	428	3 216	364	651	2 047
Reduction in risk-based transaction efficiencies	562	239	1 888	112	247	1 021
Gains from increased innovation	902	426	3 924	157	380	1 723
Net gains from reduced business compliance costs	105	33	233	45	60	166
All legal and administrative costs	-24	-3	-35	-18	-21	-29
Net gain	2 799	951	9 220	832	1 494	4 598

^a Annuity values relate to 2008-09 and subsequent years, and are in 2006-07 constant prices. Data are rounded to the nearest million. Results are based on 10 000 simulations. The details are in CMOD. The 5 per cent and 95 per cent percentiles represent the range of values in which a measure drawn from an underlying distribution can be expected to lie 90 per cent of the time. The averages of even large numbers of simulated outcomes are sometimes around 10 per cent higher than the outcomes under certainty. This is because symmetric errors around the default parameter settings have asymmetric effects for some variables. For example, the average of results when discount rates are 5% and 7% is not equal to that when the rate is 6%. Given that there is genuine uncertainty about discount rates and other variables, the averages shown above are a better measure of the likely gains from the proposed policy package than the ones given under the assumption of certainty (in table 14.3), though mostly the results are similar.

Source: Commission calculations using CMOD.

Figure 14.3 The distribution of total annuity gains from a new consumer policy framework



Source: Commission calculations based on CMOD.

14.6 The judgment in perspective

There is a strong qualitative case for reform of consumer policy and this is the most important basis for policy change. The supporting quantitative assessment is experimental, incomplete and clearly highly assumption-dependent. It is, for example, necessarily less precise and conceptually rigorous than quantification that has informed competition policy reform. Nevertheless, the assessment usefully pinpoints the fact that the gains from factors not generally visible to consumers — such as reduced transactions costs and improved productivity — are as important as the more recognisable gains from reductions in consumer detriment. It also shows that even large variations in the assumptions underlying the quantitative analysis do not alter the judgment that significant net gains are likely.

APPENDIXES

A Public consultations

A.1 Conduct of the inquiry

The Commission received the Terms of Reference for this inquiry on 11 December 2006, with the final reporting date subsequently extended from 11 December 2007 to 30 April 2008.

As required by the Terms of Reference, and in line with its normal inquiry procedures, the Commission has encouraged maximum public participation in the inquiry.

- Soon after receipt of the terms of reference, it placed advertisements in the national press and sent a circular to a range of individuals and organisations thought likely to have an interest in the inquiry.
- In January 2007 it released an issues paper inviting submissions (see below) from interested parties and indicating some particular matters on which it was seeking information.
- During March and April 2007, it held an initial round of public hearings in all of the State and Territory capitals (Darwin by videoconference) to receive early advice on key inquiry issues.
- In December 2007, it released a Draft Report (PC 2007b), setting out its views and draft recommendations on the matters under reference and seeking responses from interested parties via further submissions and hearings.
- In February 2008, it held a second round of public hearings in Canberra, Melbourne and Sydney to elicit feedback on the Draft Report.
- Over the course of the inquiry it held informal discussions in Australia with a broad cross-section of interested parties, including Australian, State and Territory government agencies involved in the development and/or application of consumer policy, and consumer and industry organisations. And it also met with various government, consumer and industry organisations in Canada, Europe, New Zealand, the United Kingdom and the United States.

The information gathered through these channels was complemented and augmented by more than 250 written submissions from a wide range of interested

parties. More than half were received in response to the Draft Report. (The public parts of these submissions are available on the Commission's website (www.pc.gov.au), at the Commission's Canberra and Melbourne libraries, State libraries and from Photobition Digital Imaging Centre.)

In addition:

- In September and October 2007, the Commission undertook a qualitative survey of ten firms and associations to help it better understand the nature and extent of the impacts on interstate businesses of jurisdictional differences in consumer policies. During the course of this survey, it also sought views on the impact of the Victorian legislation prohibiting unfair contract terms.
- Commissioners and senior staff attended the Commission's workshop and conference on behavioural economics in Melbourne in August 2007. And a representative from the Commission attended a conference on behavioural economics in Washington DC in April 2007.
- The Commission engaged Professors Corones and Christensen from the Queensland University of Technology to assist it with some specific consumer policy matters.

Further details on these matters are provided below.

A.2 Submissions

<i>Participants</i>	<i>Submission no.</i>
ACCC	80, DR176
ACCORD Australasia	77
ACT Government	DR250
AEEMA	84
AGL Energy Ltd	57, DR149
Anglicare Tasmania	DR191
ANZ Banking Group	82, DR178, DR246
Armstrong, Barry	DR186
Association of Independent Financial Advisers	DR221
Association of Superannuation Funds of Australia	70, DR188
Australasian Retail Credit Association	DR230
Australian and New Zealand Energy and Water Ombudsman Network	64, DR187, DR254
Australian Bankers' Association	104, DR245
Australian Consumer Law Group	DR227
Australian Direct Marketing Association	DR231
Australian Finance Conference	DR216
Australian Financial Counselling and Credit Reform Association	62, DR205, DR207
Australian Food and Grocery Council	DR150

<i>Participants</i>	<i>Submission no.</i>
Australian Mobile Telecommunications Association	33, DR175
Australian National Retailers Association	60
Australian Network of Environmental Defender's Office	41
Australian Newsagents' Federation Ltd	DR203
Australian Retailers Association	71
Australian Securities and Investments Commission	103, DR174
Australian Subscription Television & Radio Association	DR189
Australian Toy Association	67, DR161
Banking and Financial Services Ombudsman Ltd	89, DR170
Best Hooper Solicitors	DR232
Black, Bob	DR229
Blums, Andris	12, DR201, DR209, DR239, DR240, DR249
Booth MP, Kim	DR210, DR237
Bransden, Janine	16, DR192
Brohier, Peter	3, 15, DR125, DR195, DR252, DR255
Brotherhood of St Laurence	47
Brown, Robin	63
Buchanan Law Pty Ltd	DR163
Buckley, John	DR116
Builders' Collective of Australia Inc	7, 9, 58, 59, DR213, DR233
Care Inc	DR207
Cash Converters	DR144
Centre for Credit and Consumer Law	93
CHOICE	88, 108, DR194, DR236
Choong, Dien	2
Clubs Australia	45
Coffey, Andrew	107
Coles	DR146
Commerce Commission New Zealand	DR193
Commonwealth Consumer Affairs Advisory Council	38
Communications Alliance Ltd	50, DR185
Communications Law Centre	DR153
Consumer Action Law Centre	94, 100, DR241
Consumer Affairs South Australia	DR219
Consumer Credit Legal Centre – NSW	95
Consumer Law Centre of the ACT	74, DR205, DR207
Consumers' Federation of Australia	83, DR234
Consumer's Telecommunications Network	78, DR211
Coombridge, Dawn and Shaw, Roderick	30, DR141
Cosgriff, Brendan and Noreen	DR224
COTA Over 50s Ltd	DR120
Council of Small Business Organisations of Australia	69
CPR (joint submission)	DR235
Credit Ombudsman Service	53, DR148
Dalton, Rae	DR140
David Wilson and Associates	DR127
Department of Consumer and Employment Protection WA	99, DR248

<i>Participants</i>	<i>Submission no.</i>
Department of Justice – Darwin	29
Earl, Peter	24
Eastern Access Community Health	56
Electrical Regulatory Authorities Council	DR143
Energy Industry Ombudsman South Australia	DR133
Energy Retailers Association of Australia	46, DR184
Energywatch UK	DR197
Essential Services Commission	DR183
Essential Services Consumer Council ACT	DR204
Field, Chris	102, DR218
Finance Brokers Association of Australia	DR177
Finance Sector Union National Office	DR157
Financial Co-operative Dispute Resolution Scheme – Ombudsman’s Office Queensland	DR154
Financial Counsellors Association of New South Wales	DR138
Financial Counsellors Association of Queensland	66, DR134
Financial Industry Complaints Service	89
Financial Planning Association of Australia Ltd	DR212
Ford Motor Company of Australia	27
Foresters ANA Mutual Society	36
Foundation for Effective Markets and Governance	6, DR122
Fulton, John	14, DR223
Furbank, John	13
GE Money	DR208
Glasson, Beryl	DR198
Glen Crest Homes (Vic)	DR118
Grenfell, Colin and Stevens, Ray	DR129
Grenvill Pty Ltd	DR152
Griggs, Lynden	18
Harden Jones Architects	DR214
Harrison, Dr Paul	85
Hazeldene Management Pty Ltd	DR165
Holloway, Murray	22, 23, DR113
Housing Industry Association	DR160
Insolvency and Trustee Service Australia	98
Institute of Body Corporate Managers (Vic)	26
Insurance Council of Australia	21
Insurance Ombudsman Service	89
Joint Consumer Groups	DR228
Joseph, Russell	DR130
Kalida Pty Ltd	DR137
Kildonan Child and Family Services	65
Kildonan Uniting Care	DR206
Kingston, Madeleine	101, DR242
Law Council of Australia	DR225
Legal Aid New South Wales	DR215
Legal Aid Queensland	51, DR202
Lismore & District Financial Counselling Service Inc	DR139

<i>Participants</i>	<i>Submission no.</i>
M R Construction	8
Mair, Peter	DR112
Malone, Laurie	4
Master Builders Australia	DR111
Michael Lee – Mates Rates Mortgages	96
Ministerial Council on Consumer Affairs	75
Mortgage and Finance Association of Australia	DR119
Motor Trades Association of Australia	43, DR169
Motor Trades Association of Queensland	17
Nagarajan, Vinjaya	48
National Children’s & Youth Law Centre	40, DR196
National Consumers’ Roundtable on Energy Joint Submission	DR199
National Ethnic Disability Alliance	DR135
National Legal Aid Secretariat	DR220
New South Wales Government	DR251
New South Wales Office of Fair Trading	73
Nottage, Dr Luke	61, DR114
O’Donnell, Carol	1, 20, 86, DR115
Office of the Privacy Commissioner	DR190
Office of the Public Advocate	54
Optus	55, DR173
Origin Energy	31, DR158
Park Road Timber and Hardware Pty Ltd	DR132
Parker, Dr Christine	25
Patterson, Kristine	11
Peach Home Loans	109
PIRAC Economics	106
Private Health Insurance Ombudsman	DR147
Queensland Consumers Association	DR123
Queensland Government	87
Reach Out for Kids Foundation	DR124
Real Estate Institute of Australia	39, DR172
Redfern Legal Centre	DR151, DR159
Reproductive Choice Australia	6, DR121
SA Council of Social Services	42
Sharpe, Michelle	5
Siebert, Robert	DR117, DR181, DR182
Small Enterprise Telecommunications Centre Limited	DR168
Smith, Simon	10
Spier, Hank	19
Standards Australia	44, DR136
Steinwell, Ray	90
Stokes, Michael	DR145
Stone, Lori	28
Suncorp	DR171, DR256
Sylvan, Louise	DR253
Synergy WA	DR155

<i>Participants</i>	<i>Submission no.</i>
Tasmanian Council of Social Services	32
TEDICORE	81
Telecommunications Industry Ombudsman	97, DR162
Telephone Services Standards Council	DR167
Telstra Corporation Ltd	35, DR156
The Australasian Compliance Institute	DR128
The Australian New Zealand Working Group on trans-Tasman Competition and Consumer Issues	105, DR179
Tortoise Technologies Pty Ltd	DR126
TRUenergy	34, DR164
Turnbull, Dr I F	DR142
Tyrrells Property Inspections	DR131
UnitingCare Wesley	DR200
Veda Advantage Information Services and Solutions Ltd	DR244
Victorian Aboriginal Legal Service Co-op	79, DR238
Victorian Council of Social Service	91
Victorian Government	72, 92, 110, DR226
WA Community Organisations (joint submission)	76
WA Council of Social Services	68, DR243
Wallace, Harry	52, DR166
Wesley Community Legal Service	37
Westpac Banking Corporation	DR247
Woolworths Limited	DR180
Zumbo, Professor Frank	49, DR217

A.3 Australian visits and meetings

Australian Capital Territory

ACT Government

AEEMA

Australian Chamber of Commerce and Industry

Australian Council of Social Services

Australian Financial Counsellors and Credit Reform Association

CARE Financial Counselling and Consumer Law Centre ACT

Consumer Action Law Centre

Consumer Advocacy Network

Council of the Australian Consumers Association

Department of the Treasury

Energy Watch

Food Standards Australia and New Zealand
Foundation for Effective Markets and Governance
Internet Industry Association
Law Council of Australia
Master Builders Australia

New South Wales

Australian Bankers' Association
Australian Consumers' Association
CHOICE
Energy Retailers Association of Australia
New South Wales Energy and Water Ombudsman
New South Wales Government
New South Wales Law Reform Commission
Optus
Real Estate Institute of Australia
TRUenergy

Northern Territory

Chamber of Commerce
Northern Territory Government

Queensland

Centre for Credit and Consumer Law
Queensland Government

South Australia

Consumers' Association of South Australia
South Australian Government

Tasmania

Anglicare Tasmania
Australian Institute of Home Economics/Consumers Federation of Australia
Council of Small Business Organisations of Australia

Energy Ombudsman Unit
Hairdressing Federation of Tasmania
Hobart Community Legal Service/Consumers Federation of Australia
National Independent Retailers Association
No-Interest Loans Scheme
Tasmanian Consumer Groups – TASCOS
Tasmanian Government

Victoria

Consumer Action Law Centre
Consumer Utilities Advocacy Centre
Cope, Deborah
Fels, Professor Allan
Field, Chris
Ministerial Council on Consumer Affairs
Telecommunications Industry Ombudsman
Telstra Corporation Ltd
Victorian Government

Western Australia

Chamber of Commerce and Industry
Small Business Development Corporation
Western Australian Government

A.4 International visits and meetings

Brussels

DG SANCO (Health and Consumer Protection Directorate)
EuroCommerce
European Consumers' Organisation (BEUC)

Canada

Canadian Chamber of Commerce

Canadian Government – Finance, Health Canada & Office of Consumer Affairs
Consumers’ Council of Canada
Ontario Ministry of Government Services
Option consommateurs (*via teleconference*)
Public Interest Advocacy Centre
Retail Council of Canada
Union des consommateurs (*via teleconference*)

New Zealand

Auckland Law Society
Banking Ombudsman
Commerce Commission
Consumers’ Institute
Federation of Family Budgeting Services
Fisher & Paykel
Ministry of Consumer Affairs
New Zealand Retailers Association
Telecom New Zealand
Warehouse Group

OECD (Paris)

OECD – Directorate for Financial and Enterprise Affairs
OECD – Directorate for Science, Technology and Information

United Kingdom

Confederation of Business Industry
Financial Ombudsman Service
Financial Services Authority
National Consumer Council
OFCOM
UK Government – Cabinet Office, Trade and Industry, Fair Trading & Treasury
Which?

United States

Consumers' Federation of America

Direct Marketing Association

Electronic Retailers Association

National Association of Attorneys General

National Consumers League

US Government – Bureau of Consumer Protection, Department of Justice, Federal Trade Commission, Office of Consumer Litigation & Office of International Affairs

A.5 First round of public hearings

<i>Participants</i>	<i>Transcript page no.</i>
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Melbourne Hearings – 20-21 March 2007

Consumer Action Law Centre	2 – 17
Telstra Corporation Ltd	18 – 34
Reproductive Choice Australia	35 – 47
Communications Law Centre	48 – 61
Builders' Collective of Australia Inc	63 – 84
TRUenergy	85 – 105
Balkin, Mark Andrew	106 – 119
Korfiatis, George	120 – 132
Dalton, Ray	133 – 139

Adelaide Hearing – 22 March 2007

Furbank, John	141 – 155
Consumers' Association of South Australia	156 – 164

Perth Hearing – 23 March 2007

Field, Chris	167 – 186
Financial Counsellors Association	187 – 193
Synergy Energy	194 – 203

Brisbane – 26 March 2007

Griffith University, Centre for Credit and Consumer Law	205 – 222
Earl, Peter	223 – 236
Motor Trades Association of Queensland	237 – 252

Canberra – 29 March 2007

National Seniors Association	254 – 267
Foundation for Effective Markets and Governance	268 – 280
Real Estate Institute of Australia	281 – 294
Australian Financial Counselling and Credit Reform Association	295 – 310
Australian Electrical and Electronic Manufacturers Association	311 – 318

Hobart – 2 April 2007

Council of Small Business Organisations of Australia	320 – 331
Brohier, Peter	332 – 342
Hobart Community Legal Service	343 – 358
Tasmanian Council of Social Service	359 – 374
Brandsen, Janine	375 – 389
Fulton, John	390 – 405

Darwin – 4 April 2007 (video link)

Department of the Northern Territory Chief Minister and Northern Territory Government	407 - 424
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Sydney – 16 April 2007

Choice	426 – 451
Consumer Credit Legal Centre	452 – 470
NSW Energy and Water Ombudsman	471 – 488
Australian Toy Association	489 – 497
Consumers' Telecommunications Network	498 – 520
National Financial Services Federation Inc	521 – 536
Malone, Laurie	537 – 544
Consumers' Federation of Australia	545 – 555

Sydney – 17 April 2007

Buchan, Jennifer	557 – 565
Insurance Council of Australia	566 – 580
Public Interest Advocacy Centre and Public Interest Law	581 – 594
Association of Superannuation Funds of Australia	595 – 609
Zumbo, Professor Frank	610 – 626
Standards Australia	627 – 639

A.6 Second round of public hearings

Participants

Transcript page no.

Melbourne – 11 February 2008

Builders' Collective of Australia Inc	641 - 654
Kingston, Madeleine	655 - 661
TRUenergy	662 - 671
Brohier, Peter	672 - 680
Penhalluriack, Frank William	681
Forge, Cheryl	682
Consumer Action Law Centre	683 - 706

Sydney – 18 February 2008

Australian Competition and Consumer Commission	708 - 725
Association of Superannuation Funds of Australia	725 - 739
Energy Retailers' Association of Australia	740 - 752
Australian Toy Association	753 - 762
Coombridge, Dawn	763 - 773
Consumer Credit Legal Centre	774 - 802
Credit Ombudsman Service	803 - 814

Sydney – 19 February 2008

National Children's and Youth Law Centre	816 - 826
Tortoise Technologies	827 - 834
Keith Atkins Bathrooms	835 - 847
Zumbo, Professor Frank	848 - 866

Canberra – 21 February 2008

Telecommunications Industry Ombudsman	868 - 881
Master Builders' Association of Australia	882 - 898
CHOICE	901 - 918
Australian Financial Counselling and Credit Reform Association	919 - 929
ACT Essential Services Consumer Council	930 - 944
Housing Industry Association	945 - 965
Foundation for Effective Markets and Governance	966 - 983

A.7 Consultants

The Commission engaged Professor Stephen Corones from the Faculty of Law, Queensland University of Technology, to conduct an early workshop for the Commission on the operation of Australia's consumer policy framework (Professor Ian MacAuley from the University of Canberra also contributed to that workshop).

The Commission subsequently engaged Professors Corones and Sharon Christensen, also from the Faculty of Law, Queensland University of Technology, to identify and comment on the effects of differences in the generic consumer laws in the Trade Practices Act and Fair Trading Acts. The resulting paper, titled *Comparison of Generic Consumer Protection Legislation*, is available for viewing and download on the Commission's website, www.pc.gov.au.

B Behavioural economics and consumer policy

Key points

- Behavioural economics draws insights from behavioural studies to better reflect people's decision-making processes. Much of behavioural economics shows how these processes and the outcomes they generate may sometimes depart from the rational, self-interested behaviour of traditional economic models.
- The main results of behavioural economics are that people:
 - often make decisions relying on simple heuristics or rules of thumb rather than considered calculation;
 - care more about losses than equivalent gains;
 - care more about immediate benefits and costs than those in the future (leading people to sometimes misjudge how disciplined they will be in the future); and
 - care about others, rewarding or punishing behaviour sometimes to their own 'cost'.
- However, some argue that behavioural economics fails to capture the dynamic workings of a market. That is, people learn and construct self-control strategies, and firms may have an interest in helping consumers to make better decisions.
- Whilst the findings of behavioural economics generally do not require radical changes to the current regulatory framework or regulatory processes, they are relevant to more specific areas:
 - Much current policy is already based on, or implicitly accounts for, behavioural economic tenets. The greatest benefit of recent behavioural economics work will be to improve policy in specific areas (such as by improving information disclosure).
 - In large part, responding to the findings of behavioural economics is similar to addressing other 'market failures', such as externalities. There is still a need to consider the significance of the problem and the costs and benefits of intervention, taking into account the way in which markets can adjust over time.

Behavioural economics draws insights from real world behaviour to better understand decision making and the operation of markets. It consists of a related series of results indicating that people's choices are influenced by, among other things, procrastination, altruism and a reliance on 'rules of thumb' rather than

explicit consideration and calculation. The results of behavioural economics are at times not surprising (procrastination is a long recognised human flaw), but they have some important implications for formal economic models and for aspects of policy that is based on the results of such models.

Conventional (or neoclassical) economics is based on a simpler set of tractable behavioural patterns. Specifically, the conventional approach models human behaviour ‘as if’ people make decisions in a rational, self-interested and consistent manner. It is not that economists have been ignorant of some of the phenomena highlighted by behavioural economics, but that analysis based on the assumption of rational decision making has produced worthwhile results for many situations, and that modelling ‘real world’ behaviour can be rather complicated.

Nonetheless, various laboratory experiments and surveys, analysing human behaviour in more detail, have indicated that existing economic models may overlook many interesting aspects of how people make decisions. These relatively recent developments in economic theory raise questions on, in general, whether they are significant enough to be integrated into policy analysis and, in particular, whether there is a need for substantial changes in consumer policy.

The Commission concludes that there is a need for policy to take account of the results of behavioural economics. Hence, the Commission is not, as the Foundation for Effective Markets and Governance (sub. DR122, p. 10) contended, ‘dismissive of any policy prescriptions based on behavioural findings’. Indeed, many policies are already based on ‘commonsense’ views that have been validated by behavioural results. Moreover, behavioural evidence may point to some innovative policy techniques and new directions in certain areas.

That said, new ways of thinking about economic behaviour do not remove the need to consider the benefits and costs of regulation, whether based on conventional or behavioural economics. It is also important to recognise that those responsible for policy formulation are also likely to be subject to behavioural biases, that may affect the choices they make.

The following discussion draws on a recent conference the Commission held on how behavioural economics should influence public policy in the broad and a roundtable on similar issues conducted by the OECD (2006a).¹

¹ Papers presented at this conference are available on the Commission’s website at www.pc.gov.au/research/confproc/behaviouraleconomics.

What is behavioural economics?

Context matters

Traditionally, economists have modelled human behaviour, as if people maximise their (self-interested) welfare subject to their available resources. Although economists have long commented on how behaviour might depart from this model of rationality,² there has been little attempt to formally model ‘irrational’ behaviour. A prominent behavioural economist summed up the new efforts of modelling human behaviour as:

... not only built on the premise that mainstream economic *methods* are great, but so too are most mainstream economic *assumptions*. It does not abandon the correct insights of neoclassical economics, but supplements these insights with the insights to be had from realistic new assumptions. (Rabin 2002, p. 4)

This is a now familiar development in economic theory, with previous extensions relaxing assumptions of perfect competition in the 1930s (leading to more detailed models of monopolistic and oligopolistic behaviour) and perfect information in the 1970s (leading to models of asymmetric information). In some senses, then, behavioural economics is simply a relaxation of the assumption of perfect rationality (Camerer et al 2003).

However, because behavioural economics has been defined against a purely rational, self-interested model of human behaviour, it has hitherto largely been concerned with pointing out where this model fails. This has led to a ‘laundry list’ of departures from otherwise rational behaviour without a widely accepted unifying theme that could be used to easily inform policy decisions.

That said, one common thread of most behavioural economics is that human behaviour is dependent on the environment in which choices are made. For example, experiments have repeatedly shown that people are influenced by the way an option is framed (including the quantity of information they are asked to process) and how far into the future any benefits or costs are incurred.

A separate theme is that people do not objectively interpret events. People often struggle to correctly judge certain risks. As Shafir stated at the Commission’s recent behavioural economics conference:

² For example, in the 18th century Adam Smith alluded to what would later be called loss aversion, “Pain . . . is, in almost all cases, a more pungent sensation than the opposite and correspondent pleasure. The one almost always depresses us much more below the ordinary, or what may be called the natural state of our happiness, than the other ever raises us above it” (quoted in Ashraf et al 2005, pp. 2-3).

People do not produce direct responses to objective experience; rather, stimuli are mentally construed, interpreted, and understood (or misunderstood). Behaviour is directed not towards actual states of the world, but towards mental representations of those states. (2007, p. 4)

Importantly, various studies indicate that people are not susceptible to these influences in a random manner; many will behave in observable, predictable patterns.

Most would accept that recognition of these factors brings more realism to economic models: people's choices obviously evolve and change within a market setting. However, from a theoretical viewpoint, greater realism is not always better. An economic model provides a 'map' of the real world to facilitate understanding of the complexity of human behaviour. More detail (or complexity) does not necessarily make the model more practically useful.³

However, the appropriate degree of simplification will depend on the context. Newton's laws of physics work very well in low gravity settings, but badly in high gravity contexts. The same applies in economics. The emerging behavioural evidence suggests that, in some but not all cases, building more detail into models of decision making will produce a degree of realism that justifies the increased complexity.

Examples of behavioural patterns

The large list of behaviours identified in the behavioural economics literature can make it difficult to isolate and identify the behaviours that are most important for policymaking purposes. As PIRAC economics commented:

... this diversity in behaviour creates a challenge for applying behavioural theory to public policy questions. It makes it difficult to analyse and provide guidance on how to identify the economic and social concerns that can arise from various types of behaviours, and the government policies and interventions that would be most effective in dealing with those categories of behaviours. (sub. 106, p. 6)

Accordingly, categorising the types of behaviour identified by the research in this area, can help policymakers focus efforts on particular issues or problems.⁴

³ A street directory would be more realistic by including contour lines, but it would be much less useful.

⁴ There is no widely agreed format to categorise behavioural patterns. Other attempts at categorising them can be found in Rabin 2002, Camerer et al 2003, Pesendorfer 2006, DellaVigna 2007 and PIRAC economics, sub. 106.

First, some of the results of behavioural economics indicate that people do not make decisions in a considered or calculated fashion; they often use ‘*rules of thumb*’ or *heuristics* in making complicated decisions.

Some of these simple decision rules work well in certain situations. For example, Todd and Gigerenzer (2000) show that many personal investors use the recognition heuristic (pick the most recognisable) when choosing stocks (leading them to often invest in large retail stores or major banks). Although simplistic, this strategy often provides greater returns than those of professional investment managers using much more sophisticated models.

Nonetheless, when decisions become very complicated, these simple rules can become difficult to apply and lead to poor decisions. Since many of these rules rely on using simple cues, at the cost of ignoring other information, forcing greater information on consumers can make it more difficult to identify these cues, or direct them to the wrong cues. As Shafir states:

To the extent that consumers find themselves in situations that are unfamiliar, distracting, tense, or even stigmatizing (say, applying for a loan), all of which tend to consume cognitive resources, less resources will remain available to process the information that is relevant to the decision at hand. As a result, decisions may become even more dependent on situational cues and irrelevant considerations ... (2007, p. 12)

Or, as the economist Herbert Simon (1971) succinctly expressed the problem of information overload, a ‘wealth of information creates a poverty of attention.’

Further, even in the absence of such information ‘noise’, these simple rules can lead to poor decisions. For example, people tend to judge the probability of an event in relation to how recognisable or available the event seems. So, when renting a car, consumers may overestimate the possibility of having a crash (given that they may more easily conceptualise it occurring) and pay many times above the actuarial value of the increased car insurance that is typically available at the time of hire.⁵

In addition, where products have attributes that are shrouded or not clear, consumers may ignore their effects. For instance, Hossain and Morgan (2006) offered consumers identical CDs on eBay with reserve prices of \$4 (with no

⁵ Rabin (2000) presents theoretical evidence that the insurance premiums paid by consumers are often inconsistent with reasonable levels of risk aversion. Supporting this theory, Sydnor (2006) more specifically finds that the average amount paid for a type of home insurance in the United States is many times greater than its actuarial value. The precise reason why consumers pay these premiums is less clear. It could be that consumers are misperceiving risk, decisions are influenced by pressure from insurance salesmen, or that consumers simply have an aversion to choosing the outlying options presented in a menu of choices (such as a high excess).

shipping costs) and \$0.01 (with shipping costs of \$3.99). On average, the latter CDs sold for \$1.79 extra.

Second, *people care about losses*. Conventional economics usually models people choosing between uncertain outcomes as exhibiting risk aversion; that is, they dislike variations (both gains and losses) from an expected amount. However, many experiments show that people tend to evaluate choices from a ‘reference point’ (say current income, wealth or market prices) rather than the expected value of a choice. More importantly, people suffer more from a loss than they benefit from an equivalent gain (evaluated from this reference point). This can lead consumers to make different choices depending on how options are framed (options presented as gains are preferred to an equivalent option presented as a loss). Further, loss aversion implies that elasticities will be asymmetric — people will respond more to price increases than they will to price decreases. Putler (1992) found such an asymmetry in consumer purchases of eggs.

Third, *people care about now*. For example, people may think that they will stop smoking tomorrow, but when tomorrow comes, they overweight the present benefits of smoking relative to the larger costs of lifetime addiction. Such ‘short-termism’ (more technically present-biased preferences or hyperbolic discounting) can explain a wide range of human behaviour such as succumbing to addiction, procrastination and impulse buying. Often these behaviours result from myopia, leading some consumers to discount those aspects of products that result in future costs. Hence, in purchasing a printer, some consumers may not adequately account for the future costs of replacing ink cartridges (Gabaix and Laibson 2005).

Indeed, even sophisticated consumers, who realise that their preferences are time inconsistent, can make suboptimal decisions (especially where the knowledge that they will succumb to temptation may simply cause them to succumb earlier than otherwise, O’Donoghue and Rabin 1999). Nonetheless, when consumers are sophisticated, they will try to implement self-commitment strategies that ‘lock-in’ behaviour, such as savings clubs, routines and strict spending budgets.

Fourth, *people care about others*. In different situations they behave altruistically or cruelly to their own ‘cost’ (especially in rewarding/disciplining the behaviour of others). In experiments, this has been demonstrated by the ultimatum or dictator games. In these games, ‘proposers’ split an amount of money between themselves and another participant (in some variants the ‘responders’ can choose to either accept or reject this offer). Participants consistently offer significant positive amounts or reject ‘unfair’ small positive offers, both of which are inconsistent with a purely self-interested strategy (Camerer and Thaler 1995).

In the real world, it has been demonstrated that people often engage in costly activities that benefit others but provide no financial gain to themselves. Indeed, in

some contexts, the addition of a financial payment (such as paying people to donate blood) can ‘crowd out’ these intrinsic motivations and reduce the supply of altruistic acts (Frey 2007).

Table B.1 explains in more detail some of these patterns of behaviour.

Criticisms of behavioural economics

There are two main criticisms of behavioural economics.

- Some have questioned its methodology and results.
- Others accept that the conclusions of behavioural economics are true for individuals, but argue that they are not significant when examining outcomes from aggregated markets.

In regard to the first criticism, several economists have expressed concern about the strength of conclusions being generated from experimental data.

- Like all experiments, there are risks that participants are not representative of the wider population. For example, Lazear et al (2005) present evidence that the most influential decision makers in real markets are often not represented in experimental studies.
- Ergas (2007, p. 3) notes that experiments test both for behavioural defects and the influence of the laboratory setting, such as the measurement techniques used. He claims it is difficult to disentangle whether the results are independently testing behavioural theses.
- Rubinstein (2005, pp. 6, 11) has commented that while experiments can cast doubt on the standard economic assumptions, they often fail, on their own, to generate testable predictions.
- Girgenzer (1996, p. 593) argued that experimental results are too vague to count as explanations:

They are labels with the virtue of Rorschach inkblots: A researcher can read into them what he or she wishes. The reluctance to specify precise and falsifiable process models, to clarify the antecedent conditions that elicit vague heuristics, and to work out the relationship between heuristics have been repeatedly pointed out. The two major surrogates for modelling cognitive processes have been (a) one-word labels such as *representativeness* that seem to be traded as explanations and (b) explanation by redescription.

Table B.1 Behavioural patterns

<i>Pattern</i>	<i>Description</i>	<i>Experimental evidence</i>	<i>Real-world evidence</i>
Availability	People overestimate the likelihood of events that are more 'available' or noteworthy.	Volunteers who were asked to imagine Gerald Ford winning the 1976 election (before the election took place) put a higher probability on him winning the election than those who weren't asked to imagine this (Caroll 1978).	People tend to overestimate the likelihood of gruesome death, such as from plane crashes or terrorist or shark attacks.
Estimating low probabilities	People have difficulty estimating low probabilities.	A study of horseracing showed that punters generally over-bet on longshots. For example, horses with 2 per cent of the total money bet on them, win only about 1 per cent of the time (Thaler and Ziemba 1988 and Hausch and Ziemba 1995).	Some overestimate the chances of winning when gambling on a lotto ticket.
Overconfidence	People overestimate their own abilities.	Svenson (1981) found that 80 per cent of respondents rated themselves in the top 30 per cent of drivers.	Ausubel (1999) found that individuals over-respond to low pre-teaser interest rate offers on credit cards. Those who accept offers naively think they will not borrow much on the credit card after the teaser rate is removed.
Endowment effect or status quo bias	People's value of a good increases once they own it. In economic jargon, people's willingness to pay for a good is often less than their willingness to accept to sell the same good. It is related to loss aversion and a preference for the status quo.	Volunteers were asked how much they would pay to buy a coffee mug. They were then given the mug and asked how much they would sell it for. The average selling price was much higher than the average buying price (Kahneman, Knetsch and Thaler 1991).	Rates of volunteering for organ donation are around 98 per cent in those European countries where people are automatically signed up but can opt-out. This compares to rates of around 15 per cent when people have to opt-in to organ donation (Johnson and Goldstein 2003).

Table B.1 (continued)

<i>Pattern</i>	<i>Description</i>	<i>Experimental evidence</i>	<i>Real-world evidence</i>
Choice overload	People opt out of deciding when there are too many choices as the avoidance of regret outweighs the gains from choosing.	People were asked to choose between varieties of jams. They more often chose to buy when there were only 6 jams presented compared to when there were 24 (Lynegar and Lepper 2000).	People may purchase prepayment schemes to avoid having to make choices (eg package holidays).
Framing	Behaviour can change depending on how a choice is framed. Generally people are more attracted to offers that are framed in terms of the possible gains rather than costs or losses.	People were asked to choose between two hypothetical government medical programs. Both saved the same <i>average</i> number of lives but one produced more variable outcomes. People were less likely to choose the less variable program when it was expressed in terms of how many people would die rather than how many lives it saved.	Can help to explain the attraction of cash back offers rather than a simple discount, since the cash back offer is framed in terms of a gain.
Present bias (hyperbolic discounting)	People prefer a smaller reward <i>now</i> to a larger reward later but will generally prefer to wait for the delayed, larger reward if both rewards are far in the future.	Thaler found that the median subject was indifferent between \$15 now and \$20 in one month and also indifferent between \$15 now and \$100 in ten years. The implied discount rates are more consistent with a hyperbolic discount function.	Can help to explain consumption of addictive substances or excessive debt. Also can provide a rationale for a number of self-control techniques such as routines, gym memberships, savings plans and the demand for the criminalisation of addictive drugs.
Legitimacy	People seek fairness in transactions even if it comes at cost to themselves.	The ultimatum game is an experiment in which volunteers are told that someone has offered them say, \$8 from a \$100 pot even though they could have offered them a 50-50 split. Most refuse the offer and get nothing (Camerer and Thaler 1995).	People donate blood for no financial compensation and give freely to charities.

As indicated above, the second group of critics accept the basic results of behavioural economics, but argue that they are moderated by learning and the workings of a real market (see Epstein 2006, Glaeser 2003 and Smith 1991). In essence, these economists claim that laboratory experiments and surveys do not accurately illustrate how decisions are made in a market context where consumers generally have opportunities to self-reflect, learn, seek supervision or oversight and construct artificial punishments and rewards (Epstein 2006, p. 111). Chris Field expanded on these points at the public hearings:

I'm a little concerned that some of behavioural economics is trying to make us mistake-free or correct mistakes that we otherwise may make. We learn from our mistakes and by those mistakes we make our subsequent decision-making stronger ... a mistake today may, in hindsight, not look like a mistake at all, in fact it's made us much stronger in our long-term decision-making. (trans. p. 171)

Behavioural patterns also tend to be more difficult to identify when analysing aggregate market behaviour rather than individual choices. In theory, a group of consumers may be subject to offsetting biases that, by cancelling each other out, yield optimal outcomes (Epstein 2006, p. 121). For example, some results predict that consumers will be overconfident and over-price goods, yet it is also plausible that others may suffer pessimism and doubt and thus under-price goods.⁶ This creates difficulties for policymakers:

Instead of the relative simplicity of the neoclassical model, behavioural economics confronts the regulator with a host of alternative behaviour patterns that make it all the more difficult to predict how consumers will react to a particular remedy ... The state of the literature is such that there appears to be many ways in which consumers stray from the rational actor model, often in ways that conflict with each other. (Mulholland 2007, p. 14)

Ultimately, the importance in market contexts of the behavioural patterns identified earlier, is an empirical question.

Some experiments that imitate market conditions suggest that, over time, markets could deliver close to optimal results. For example, stock market bubbles have been recreated in laboratory experiments, with the results indicating that the more experienced 'traders' become, the less likely a bubble will emerge (Smith et al 1988 and Schwarz and Aug 1989). In separate experiments, Chu and Chu (1990) found that deficient decision-making disappears when arbitrage is introduced to impose losses on those making inconsistent choices (as would presumably occur in a well-functioning market). A more recent study (Plott and Zeiler (2002) found that the

⁶ In an extreme example of this phenomena, Becker (1962) demonstrates that even if people randomly made decisions, market demand curves would still slope downwards.

endowment effect (the value of something is often larger for those that possess it) disappears after repeated trading of coffee mugs. This suggests that the more comfortable people become with the notion of trading, the less likely they will be to anchor their reference point to what, at times, could be an arbitrary distribution of property.

However, even in these sorts of experiments, participants generally report that they are not following rational and self-interested strategies. For example, Smith (1991, p. 880) reports that hundreds of experiments re-creating market environments demonstrate that prices converge quickly to predicted rational expectations equilibria. Yet, post-experiment discussion with participants indicates that they are not aware that they are maximising returns and often, before they see the results, describe the experiment as confused and disorderly:

What is imperfectly understood is the precise manner in which institutions serve as social tools that reinforce, even induce, individual rationality ... [E]conomic concepts ... are inexorably static and do not come to grips with the interactive process between agents and institutions. One misses all this in research limited to the individual expressing an opinion about described situations or alternatives. (Smith 1991, p. 881)

In essence, what these results are capturing is that conventional economic models explain outcomes ‘as if’ people behave optimally. The inability to pinpoint the dynamic, actual process that makes most markets efficient, is simply reflective of why Adam Smith called it the *invisible* hand.

One reason why market outcomes may not mimic the results of laboratory experiments is that consumers may ‘rationally’ correct biases when the benefits are high enough (Glaeser 2003). For example, people may not unreasonably persist with incorrect reasoning when the right decision does not yield large benefits, or when mistakes make people happier (such as a belief they you have a relatively high chance of winning the lotto). In addition, in a market environment, it may only take a relatively few motivated arbitrageurs (or marginal consumers) to drive efficient outcomes (chapter 3).⁷

Indeed, while in some situations firms may seek to exploit behavioural deficiencies, in other cases they will have incentives to help consumers make better decisions. When consumers make poor decisions they forgo certain benefits. This creates opportunities for some firms to profit by helping consumers correct these decisions. For instance, Ergas (2007, p. 6) points to a number of examples of businesses

⁷ The same logic applied to public choices, may indicate that behavioural results have more import for government decisions than the decisions of individual consumers. Voters probably have less incentive to overcome or correct their mistakes in the political arena (compared to a market situation). The cost of voting for the wrong person is minimal — one vote is unlikely to change the result of an election (Glaeser 2003 and Caplan 2007).

successfully increasing their market share by introducing simpler pricing plans; including AAPT's SmartChat (capping STD calls), Woolworths' 'Everyday Low Prices' and ANZ's 'all you can eat' transaction account (simplifying bank charges).

Still, the extent to which firms will find it profitable to help consumers overcome decision-making deficiencies, depends on whether consumers are aware of their shortcomings as market actors. In surveying the relevant literature, DellaVigna (2007, p. 43) found that if agents rationally expect themselves to suffer from certain biases, then firms will meet a demand for products that help consumers maximise their welfare. However, if consumers are naive about the extent to which they suffer from self-control and other problems, firms are instead likely to offer products that magnify the detrimental effects of the bias.

To help resolve these competing viewpoints, there is an emerging view that future research will need to focus on identifying exactly how behavioural traits manifest themselves in real markets (Levitt and List 2006 and Mulholland 2007). Some such work is already occurring through greater field research (see DellaVigna 2007). In helping to clarify the true characteristics of consumer markets, this research should help to alleviate concerns that too rash an application of behavioural economics could lead to unnecessary or potentially costly regulatory interventions.

Implications for policy

More sophisticated policy making rather than a policy overhaul

The types of behaviour identified by behavioural economists have been known to philosophers, writers and marketers for centuries and, moreover, policymakers have not been blind to behavioural issues. Indeed, there are a range of existing consumer policies that are, or could be, justified on behavioural economics grounds.

Of the behaviours identified in table B.1, four are of particular policy interest.

- *Overconfidence*. Since people may overestimate the 'deal' they are getting from purchases, cooling-off periods may be justified for large transactions such as houses, cars, etc.
- *Endowment effect*. An aversion to change increases the importance of choosing the correct default option for policies designed to engender change. For example, people's reluctance to switch suppliers may have implications for the sort of consumer policies that are established in parallel with the introduction of competition to a previously monopolistic market (such as has recently occurred in most utility markets, appendix F).

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- *Choice or information overload.* Too much choice may be detrimental for some consumers. As Peter Earl stated:

Consumers who are suffering from information processing fatigue may be liable to take impulsive choices based on a fraction of the information at hand, particularly if under pressure from a sales person ... Consumers may even face firms deliberately creating overload for strategic reasons, a possibility that has led to the term 'confusopoly' ... Market deregulation can exacerbate information overload by resulting in more suppliers between which to choose. (sub. 24, pp. 8-9)

In response, governments may require firms to publish easily interpretable comparative information (such as standardised interest rates, phone costs, etc), or to offer relatively simple default products. However, requiring firms to provide large amounts of detailed information is unlikely to help (chapter 11).

- *Present bias.* The concern that people will often underweight future costs and benefits may lead governments to force people to save (superannuation requirements) or ban particularly harmful behaviour (such as taking addictive and harmful substances or acquiring credit at usurious interest rates). And in the United States, more stringent motor vehicle fuel efficiency standards were recently introduced partly on the basis that consumers fail to fully consider the future savings from a more efficient motor vehicle (Graham 2007).

Of course, many such policies can have other rationales as well. For example, while speed limits can be justified on the basis that drivers do not properly account for the future costs of having an accident, such limits can also be justified in terms of the external costs of accidents that are imposed on others.

Accordingly, the findings from behavioural economics, even if accepted without demur, are unlikely to require an overhaul or major redirection in consumer policy. Thus, the Consumer Action Law Centre (trans. p. 14) stated that behavioural economics may have more import for the specific 'tools' of consumer policy and responses to particular policy issues, than for the overall framework.

That said, there have been some significant and original shifts in policy direction suggested by some behavioural economists, such as measures that attempt to protect those who make harmful mistakes, but which do not restrict the choice of those who make few errors (box B.1).

Yet, the espousal of this 'soft' form of regulation crystallises one of the key issues that must be addressed when intervening to protect some, but not all, consumers. Almost all approaches will restrict the choice of, or impose costs on, consumers who are sophisticated and do not require protection. As in most economic policy

debates, nothing in the theory indicates whether the gains to some are more highly valued than the losses to others.

For example, the fact that most people lock themselves into long memberships at gyms may indicate that gym owners are taking advantage of consumers' myopia about how often they will attend the gym in the future. But, gym memberships may alternatively represent a commitment strategy that lowers the cost of future gym visits because consumers realise that procrastination might otherwise cause them to opt out (Gans 2005). Both effects are probably relevant, yet it is difficult to separate and compare their relative importance. Essentially, the answers to these questions are empirical and must be judged on a case-by-case basis.

Box B.1 The use of default options

Some economists have suggested that, although the current state of behavioural economic research does not give rise to a case for new heavy-handed regulation, it may suggest ways of improving policy without overly harming others (Thaler and Sunstein 2003 and Camerer et al 2003). The basic approach of libertarian (or asymmetric) paternalism is to propose policies that protect people from making harmful decisions, without overly restricting choices of those less likely to make mistakes.

For instance, many studies have highlighted the power of default options. Madrian and Shea (2001) showed that, in the United States, making enrolment in an employer-sponsored superannuation plan the default had a large effect on participation rates: 86 per cent of those that were enrolled as a default remained in the plan after one year, compared to 49 per cent who were not. Other studies have replicated this result across different industries (Choi et al. (2001)) and in other countries (Cronqvist and Thaler (2004)). As DellaVigna sums up:

Overall, the finding of large default effects is one of the most robust results in the applied economics literature of the last ten years. (2007, p. 8)

The strength of these results has convinced some governments to change default options for retirement savings plans. One example is a recently implemented initiative of the New Zealand Government to lift savings rates. Under the KiwiSaver policy, employees will have a choice of putting either 4 or 8 per cent of their salary into superannuation. The default is 8 per cent.

However, the inertia effect that makes default policies powerful also transfers the responsibility for making the correct choice from the consumer to the government or firms. For example, while the practice of some US employers in signing up employees to superannuation plans as the default option has led to the aforementioned greater rate of take-up, those employers have generally chosen conservative investment strategies. One study found that, on average, people did not save more since the increased enrolment rates were offset by lower contribution rates and more conservative asset allocations (Choi et al 2001).

Indeed, this example highlights that the findings of behavioural economics are not necessarily biased in favour of more regulation. As spelt out earlier, some behavioural research has shown that the use of imprecise decision rules, in conjunction with learning over time, often leads to close-to optimal results. To the extent that some existing regulation is based on naïve and static models of decision making, this research may suggest the removal of that regulation (Craswell 2006). For example, financial services providers are currently required to provide consumers with copious amounts of information. Behavioural results cast doubt on the usefulness of such requirements, at least in their current form.

A further important benefit of behavioural economics research is that it may better reveal the proportion of consumers that are susceptible to particular patterns of potentially harmful decision making. For example, most laboratory experiments shed light on the proportion of consumers who make certain mistakes. More field research exploring the consequence of these mistakes in ‘real world’ settings will have even greater policy relevance. Ultimately, the better predictions generated by these results may improve regulatory design.

Some fundamental policy questions remain the same

The emerging behavioural evidence supporting the systemic relevance of certain behavioural traits indicates that the design of consumer policies should consider and, as appropriate, reflect these results.

However, any regulation underpinned by these new behavioural findings should take into account factors that affect their validity when applied to particular contexts. Specifically, policymakers should consider:

- How significant is the consumer detriment caused by the errors in judgement? Are consumers largely aware of the issues and could they easily respond to them if they desired?
- Can private responses moderate the detriment caused? Over what time frame would such responses develop and what would be the significance of the detriment in the interim? Would any regulatory intervention greatly restrict opportunities for consumers to learn and develop their own responses to the issues?
- What proportion of consumers are susceptible in a particular circumstance? Would the proposed intervention impose significant costs on those who are not at risk? Can the behaviour of the sophisticated protect those who unaware of the problem?

Many of these considerations evidently apply to all regulation making, indicating that designing policy responses to the issues raised by behavioural economics is not overly different from responding to more traditional problems such as externalities and the abuse of market power.⁸

Crucially, most policy proposals (regardless of their supporting premises) require a case-by-case, empirical evaluation of their costs and benefits. Ultimately, the policy decision remains a choice between imperfect markets and imperfect (however well-intentioned) government interventions.

⁸ Indeed, Whitman (2006) has found more direct parallels between externalities and present biases, using the term ‘internalities’ to explain people’s propensity to overvalue present benefits. According to this line of thinking, our ‘present self’ makes decisions (staying up late, getting drunk, etc) which have spillover costs for our ‘future-selves’. There are similarities then between responses that target externalities (Pigouvian taxes, establishing property rights, etc) and policies which could target internalities (sin taxes and ‘trades’ between our multiple selves).

C International approaches

Key points

- Internationally, consumer policy frameworks vary, reflecting each country's economic and political history, culture and legal traditions. The upshot is that consumers in different countries have somewhat different rights and pathways to exercise them.
- However, there is recent convergence in frameworks in some particular respects.
 - it is now widely accepted that there is a close nexus between consumer policy and competition policy — promoting competitive markets is an important means of improving consumer welfare and consumer policy can play a key role in promoting well functioning markets;
 - consumer empowerment is a strong 'mantra' worldwide; and
 - there are increasing efforts to remove obstacles to cross-border enforcement.
- Australia, the USA and NZ are the only OECD countries that have a generic 'consumer act', with EU countries relying mostly on a collection of more specific, though generally applicable, regulations.
- To varying degrees, all developed countries employ industry-specific consumer regulation, particularly for the financial and utilities sectors.
- The balance between public and private enforcement of consumer laws varies markedly across countries, as do arrangements for dispute resolution.
- There is no predominant model for consumer advocacy. In the USA there are several well established private advocacy groups, whereas the UK funds the National Consumer Council to represent consumers. Canada is concentrating on funding networking between the consumer groups.

This appendix compares and contrasts international consumer policy frameworks. It is not a comprehensive, country by country, description of the many elements that make up a consumer policy framework. Such detailed comparisons have recently been made by others (OECD 2006a, OECD 2006b, DTI 2003). Rather, it provides examples that demonstrate similarities and differences in approaches, and the thinking behind recent significant policy changes. It also incorporates insights from the Commission's discussions with government, consumer and business interests in North America, NZ, UK and Europe.

C.1 General

Internationally, the objectives for consumer policy are broadly comparable — the promotion of competitive and fair markets and protection of consumer interests where markets fail. The explicit objectives statements of several countries are documented in chapter 3 (box 3.5).

However, the means of achieving these objectives, such as through the legal and institutional framework, the nature and extent of enforcement, and the strength of consumer advocacy differ across countries. Historically, some countries have had a stronger emphasis on risk prevention, direct regulatory controls and state-led enforcement, while others have focussed more on consumers enforcing their own rights through an established legislative framework. The upshot is that no two countries have the same consumer policy framework.

Historical perspectives

Individual country's settings reflect a long, complex, mix of political and economic history, culture and legal traditions. Consumer rights in basic law have evolved over centuries — for example, weights and measures laws have their genesis in guild rules and markings (hallmarks) in medieval times in Europe. In the UK, common law principles relating to the sale of goods were first codified in the Sale of Goods Act 1893, and re-enactments of that Act still form a mainstay of consumer protection today.

However, most of the key modern consumer laws only date back around 30 to 40 years. President Kennedy's 1962 speech outlining a Consumer Bill of Rights led to an unprecedented flurry of consumer legislation in the USA. At the same time, there was also a growth in consumer activism, led by Ralph Nader which spread to Australia, the UK, Canada, the Netherlands and to a lesser extent to Japan. This trend in consumer activism was much less apparent in Germany and Italy.

The recent development of consumer policy in former socialist countries offers examples of 'starting with a clean sheet' and the challenges of addressing consumer vulnerability against a back drop of black markets and new competition laws.

Recent convergence

Despite the historical diversity, it is possible to observe some recent convergence in particular aspects of consumer policy. First, it is now widely accepted by governments in developed countries that well functioning, competitive markets are

beneficial for consumers. For example, the development and smooth functioning of the internal market is the key driver of recent EU consumer legislation (rather than consumer protection *per se*).

Second, ‘consumer empowerment’ has become a strong mantra worldwide (notwithstanding differences in how best to achieve this). A key and common principle is that confident and informed consumers make better choices and can invigorate market competition and reinforce and complement competition policy reforms. (This is reflected in the Commission’s recommended objectives for Australia’s consumer policy framework in chapter 3.)

A third area of consumer policy that is showing signs of convergence is cross-border dispute resolution. Formal international networks of enforcement agencies and bilateral arrangements have developed and there has been some progress in removing legal jurisdictional obstacles. More broadly, globalisation of trade and commerce, partly as a result of the increase in e-commerce, has driven harmonisation of policy settings in the EU in particular.

Consumer policy development

While it is widely accepted that competition policy is one of the major contributors to consumer well-being, only Australia and the USA have a single Act covering both market structure and consumer protection. Historically, much consumer policy developed separately from and prior to competition policy, which partly explains why most OECD countries have separate competition and consumer legislation. For example, in the UK, the Office of Fair Trading has responsibility for the Fair Trading Act 1973, which predated the Restrictive Trade Practices Act 1977 administered by the Competition Commission.

Even so, reflecting the nexus between consumer policy and other aspects of the commercial policy framework, the core of consumer policy at government level is, in many countries, mainly under the remit of the business or economic ministry — for example, Treasury in Australia and the Department for Business Enterprise and Regulatory Reform in the UK. That said, Ministerial responsibility for consumer affairs typically resides at a junior level. One exception is Denmark, which has recently established a Ministry of Consumer and Family Affairs. Also, as discussed in chapter 6, ministerial responsibility for consumer affairs at the Commonwealth level in Australia has recently been combined with responsibility for competition matters.

C.2 Legislation

Generic consumer protection clauses

Australia, the USA and NZ are the only OECD countries that have designated consumer protection legislation built around broad duties and general conduct prohibitions.

The US Federal Trade Commission Act declares unfair and deceptive acts to be unlawful. While the application of the deceptive conduct component has been relatively uncontroversial, the definition and use of the unfairness clause has had a chequered history from its beginning in 1938. Over the years it has been used in different ways, partly as a result of court rulings and changing Congressional attitudes. Recently it has been used to address practices (especially Internet-based) that cause substantial injury but that would be difficult to handle on the grounds they are deceptive.

New Zealand's Fair Trading Act 1986 is substantially based on Part V of the Australian Trade Practices Act (unfair practices), but unlike Australia, New Zealand does not have unconscionability provisions. (Consumers instead need to rely on the common law doctrine of unconscionable dealings). Further differences between Australia and New Zealand consumer laws (and enforcement) are detailed in chapter 13.

Canada does not have separate national consumer legislation, but its Competition Act covers misleading advertising and unfair practices. Provincial fair trading acts also have general prohibitions on misleading and unconscionable conduct.

In the EU, consumer protection laws fall into three broad groups.

- One group (such as Austria, Belgium, Denmark, Finland and Germany) have a single business or marketing act which includes one or more general clauses protecting consumers indirectly from unfair commercial practices (box C.1).
- France, Italy and the Netherlands codify consumer protection provisions in private law or the civil code — for example, the French *Code de la Consommation*.
- The UK and Ireland rely on a collection of individual pieces of consumer protection legislation, such as those necessary to give effect to the various EU consumer protection Directives.

Box C.1 General consumer protection via business or marketing acts

- The Danish Marketing Practices Act has an overarching clause stating that all marketing must be carried out in accordance with good marketing practices, though it is enforced by the Consumer Ombudsman (not the courts). It is said that the clause is very broad, used quite extensively and that Danish business does not have a problem with it (DTI 2003).
- The original aim of the German 1909 Act against Unfair Competition was to protect traders, with the vast majority of enforcement actions taken by business. In effect, the consumer interest is deemed to coincide with those of disadvantaged businesses. Since 1996 the Act has provided for a right of action by designated consumer bodies, but not individuals.
- Since competition law was revived in Hungary in the late 1980s, various consumer protection rules have been successively included in the new Hungarian Competition Acts. In the period of market transition, about 40 per cent of cases under the law were consumer related (Cseres 2004).

Also, in 2005 the European Parliament signed the Unfair Commercial Practices Directive (UCPD) — essentially a ‘general duty to trade fairly’. Introduction of the UCPD has enabled the UK to scrap around 20 specific regulations.

Amongst other things, the new directive prohibits pressure selling, misleading marketing and unfair advertising. A practice is deemed to be unfair if it is contrary to the principles of professional diligence and it materially distorts, or is likely to materially distort, the economic behavior of the ‘average’ consumer.

Historically, the meanings of unfair and average have been different in national laws and court decisions. The UCPD provides guidance on the meaning of unfair by proscribing 31 practices. However, the meaning of the ‘average consumer’ appears less clear. While key decisions of the European Court of Justice have been underpinned by the notion of an average consumer ‘who is reasonably well informed and reasonably observant and circumspect’ the EU was unable to agree that this be the definition in the Directives Articles (Stuyck 2007).¹

Specific legislation

To varying degrees all developed countries employ specific consumer regulation. Some areas are common to most such as financial and utility services.

¹ Other notions of the benchmark consumer used by national courts include, ‘the least attentive consumer who accepts without criticism the representations made to him and who is not in a position to see through the traps, exaggeration or manipulative silences’.

The arrangements in the USA provide a useful comparison for Australia in considering the configuration of its specific requirements and also of recent initiatives in the consumer credit area.

- The FTC, in addition to the generic FTC Act, has enforcement responsibilities under more than 50 other statutes and more than 30 rules governing specific industries and practices, for example: the Consumer Leasing Act (covering consumer information on lease costs and terms); the Credit Practices Rule (preventing among other things certain collection remedies); the CAN-SPAM Act; the Truth in Lending Act (which requires creditors to disclose cost information such as the annual percentage interest rate); and the Do Not Call registry.
- There are some carve outs from the FTC's jurisdiction, including telecommunications, energy, banking, product safety, food and drugs — though in most of these areas, the FTC can become involved if the circumstances warrant.
- The FTC is unique among consumer protection regulators in having delegated power to make specific regulations. If a new area of specific regulation is approved/proposed by Congress, the FTC may be required to formulate the details. It can also initiate regulation, subject to a RIS type process.

As in most countries, the financial services sector is a key focus of consumer protection in the USA. The FTC (2007b) said that, in 2008, it intends to concentrate on the following three aspects: alternate mortgages, bad debt collection, and credit-related deception.² For example, in light of the rise in consumer debt levels, as well as consumer complaints about debt collection, the FTC has indicated that it will be revisiting regulatory arrangements in this area, which are now more than 30 years old.

Differences within countries

Significant intra-country variation in generic and industry-specific consumer legislation is evident in both the USA and Canada. For example, all US states have their own versions of the FTC Act and product safety in the USA has been described as a patchwork quilt (DTI 2003). Licensing and registration of professionals and traders also varies widely among US states, in part because some

² The FTC receives more complaints about debt collectors than any other single industry, and has taken enforcement actions against those offering debt reduction services that charge hidden fees, make false promises to lower consumers' debts, or misrepresent that they will eliminate accurate negative information from consumers' credit reports.

cities and counties have their own requirements. There is little, if any, readily available evidence of the benefits and costs of these differences in laws.

Greater consistency across the USA has been pursued via a Uniform Commercial Code (UCC), Article 2 of which contains general provisions on the sale of goods, including implied warranties. Most states have adopted the UCC for their own state commercial law codes, although some have made changes often to provide consumers with additional rights.

There has also been national pre-emption of impending variable state laws in areas like telecommunications and banking. Also relevant are the activities of the National Association of Attorneys General (NAAG) which in regard to consumer protection:

- seeks to improve the enforcement of state and federal consumer protection laws by State Attorneys General;
- supports multi-state consumer protection enforcement initiatives; and
- promotes information exchange among jurisdictions.

Harmonisation of consumer laws is a key focus of the EU, and the European Commission is currently reviewing the EU's consumer protection legislation (the Consumer Acquis)³. The review was prompted by concerns that the requirements in this legislation are based on minimum harmonisation, leaving countries free to introduce or maintain stricter controls. Not surprisingly, this has led to differences in the degree of protection afforded EU consumers and the modalities for exercising rights granted by the various Directives. The divergence in arrangements sits uncomfortably with the current drive to develop the internal EU market. The UCPD (see above) is a departure from the past harmonisation approach because it sets a maximum standard to be adopted by member countries. Members are prohibited from introducing more stringent provisions than those in the UCPD until 2013.

C.3 Dispute resolution and enforcement

A mix of public and private enforcement of consumer laws is generally the norm in other countries. More specifically, the OECD (2006a) compared the enforcement regimes of eighteen countries and identified five broad models:

- reliance on the criminal justice system for penalties (for example, the United Kingdom, Japan and Switzerland);

³ The Consumer Acquis comprises eight Directives: doorstep selling (1985); package travel (1990); unfair contract terms (1993); time share (1994); distance selling (1997); price indications (1998); injunctions (1998); and sale of consumer goods and guarantees (1999).

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- reliance by administrative agencies primarily on the civil justice system to obtain sanctions and remedies (for example, Australia and Canada);
 - reliance on administrative agencies with power to impose financial penalties (for example, New Zealand, Sweden and the United States);
 - reliance primarily on consumer complaints to an Ombudsman (for example, Denmark and Finland); and
 - reliance primarily on self-regulatory arrangements and on the individual's enforcement of private rights (for example, the Netherlands).

However, care should be exercised in drawing conclusions from such high level categorisations. For example, though Australia and New Zealand fall to different enforcement groups in the OECD assessment, as set out in chapter 13, there are strong commonalities between the overall consumer policy regimes in the two countries.

Out-of-court dispute resolution

Most developed countries have some form of publicly supported out-of-court dispute resolution pathway — be it, ombudsmen, complaints boards, or alternative dispute resolution (ADR). The nature of government involvement varies between establishment of statutory dispute arrangements, funding for dispute resolution bodies and direct operation of such bodies.

Most countries have dedicated arrangements for specific sectors such as utilities, telecommunications, finance and insurance. For example:

- Canada has a two tiered ombudsman arrangement for financial services. The first tier is an industry-funded independent arbiter. The second tier is a fully independent ombudsman for the 20 per cent of cases that are not resolved at the first level.
- NZ has industry-based schemes for banking, insurance and savings, and energy. The Banking Ombudsman is a self-regulatory scheme, with the Ombudsman referring any substantial systemic issues to the Commerce Commission.
- The UK and Ireland have a single financial services ombudsman. The Financial Ombudsman Service (FOS) was created in 2000 from the amalgamation of five ombudsman schemes — banking, insurance, pensions, building societies and investment. Some of these were industry run, some statutory. Consumer credit has since been added to FOS's areas of responsibility. The amalgamation of schemes is estimated to have reduced average case handling costs by about 30 per cent (Nelthorpe and Renouf 2004). FOS receives about half a million

inquiries a year and resolves about 100 000 disputes. Three-quarters of FOS's income comes from case fees and the remainder from an industry levy.

- The UK telecommunications sector has two private companies handling dispute resolution (in line with EU policy on contestability in the service sector) — the Office of the Telecommunications Ombudsman and Communications and Internet Services Adjudication Scheme. Consumers direct their complaints to the ADR company their provider is a member of. Typically, settlements under both schemes are non-pecuniary (and relatively small when pecuniary). Around 80 per cent of the decisions made are accepted by the complainant.
- Denmark has a hybrid scheme: there are 11 authorised private consumer complaints boards covering sectors such as insurance, banking, investments, travel and construction (funded by the industry), and a state-run National Consumer Complaints Board covers complaints outside these sectors (free of charge).

The majority of OECD countries have also attempted to increase the availability of effective, timely and cheap alternatives to formal court-based dispute resolution outside the key sectors. For example, as well as to Denmark's complaints board, Japan has a new accreditation system aimed at promoting the development and use of private ADR. The UK has recently established a scheme whereby Consumer Direct refers consumers to accredited third party ADR providers. And, in the USA, out-of-court mediation, conciliation and arbitration services are supplied by both public and private sector entities, such as State government departments, law firms and the Better Business Bureaus.

However, despite the availability of such mechanisms, and the efforts in some countries to augment them, the OECD (2006b) noted that there has been no comprehensive assessment of the availability, usage and suitability of ADR schemes in member countries. In this context, it pointed to survey evidence suggesting ADR has not yet fulfilled its potential as a low cost and efficient mechanism for the resolution of business to consumer disputes. For example, one European survey on access to justice found that nearly 40 per cent of respondents had never heard of the arbitrators, ombudsmen, arbitration or conciliation bodies, that could offer an alternative to court action (EC 2004).

Small claims courts

As an alternative to ADR, or where ADR arrangements are absent, many OECD member countries have introduced simplified court procedures for small claims. Being independent, binding and enforceable, small claims procedures offer

consumers the main benefits of the judicial system without the high costs, delay and procedural complexities associated with the regular courts.

The main differences across countries in small claim court procedures relate to:

- whether they involve a modified procedure in an ordinary court or in a specialist consumer tribunal;
- the type of dispute and claim that may be heard;
- monetary ceilings for access to these procedures; and
- financial costs to parties.

Overall, Australia, the UK, the USA, and Canada were judged by the OECD (2006b) to have small claims mechanisms which work well in most cases (though the Commission has identified some areas where there is scope for improvement in Australia; see chapter 9). The Disputes Tribunal in New Zealand is also regarded by some as an example of a cost effective approach in this area. This tribunal allows consumers to pursue disputes involving amounts up to NZ\$12 000, quickly (usually no more than 6 weeks after an application is made) and at low cost (NZ\$30 to \$100 depending on the size of the claim). No legal representation is allowed and a government appointed referee presides over cases. Any consumer issue can be heard by the Tribunal except for those pertaining to tenancy and motor vehicles, which are dealt with by separate tribunals.

As under the NZ model, legal representation is not permitted in small claims courts/consumer tribunals in many US states. In contrast, in countries such as France, Germany, Italy, Japan and the Netherlands, claimants may choose to be represented by a lawyer or non-lawyer appointee.

In most countries, consumers that are unsuccessful in their claim are liable to pay some or all of the costs that the other party has incurred in responding to the claim. However, these costs are usually capped.

Finally, many OECD countries incorporate some form of ADR before or during small claims court proceedings. In Australia, the NSW Consumer Trader and Tenancy Tribunal is required to use its best endeavours to mediate a settlement among the parties before proceeding to adjudication. Likewise, in the UK, the court has a duty to encourage the parties to use ADR to resolve the dispute, but it is not mandatory for the parties to do so. And, in the USA, small claims courts commonly offer ADR services.

Private legal action

The incentive for consumers to take private legal action against a trader, where they have suffered detriment, varies widely across countries. At one end of the spectrum is the USA where triple damages are available and ‘no win no pay’ legal services are widely available. In contrast, the incentives for private court action in Germany are much reduced because of the risk of having to pay costs and because the award is limited to the detriment actually suffered.

A significant number of OECD countries allow collective action lawsuits to be filed by groups of private individuals who have suffered similar harm as a result of the actions of the defendant. Class actions in the USA are said to have had a major impact on product safety in the past.

Many countries also allow consumer organisations to file lawsuits on behalf of an individual consumer or, more frequently, a group of consumers. In the UK, the USA (state level), Norway, Portugal, and Sweden, monetary relief may be sought in addition to conduct remedies, under representative actions.

Public enforcement

Across developed countries, a range of tools are variously provided to regulators to enable them to enforce consumer laws, including:

- administrative fines;
- prohibition orders, enforceable undertakings and injunctions;
- award compensation direct to consumers;
- confiscation of goods;
- cessation orders; and
- naming and shaming.

Among OECD countries, the USA appears to have the widest set of tools. However, the FTC (2007b) argued before Congress that its ability to protect consumers from unfair or deceptive acts or practices would be substantially improved if it had civil penalty authority in the areas of data security, telephone pretexting and spyware. Specifically, the FTC contended that civil penalties are important in these areas because traditional remedies (such as consumer restitution and disgorgement of profits) may be impracticable or not fully effective in deterring unlawful acts, observing that:

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- restitution is often impracticable in these cases because consumers suffer injury that is either non-economic in nature or difficult to quantify; and
 - disgorgement may be unavailable because the defendant has not profited from its unlawful acts, for example, in cases where companies have failed to maintain reasonable safeguards to protect sensitive consumer data.

A recent review in NZ similarly recommended the addition of new measures to that country's enforcement toolkit (see box C.2).

Processes for taking enforcement action also vary considerably. In most Anglophone countries, the regulator cannot impose an administrative sanction itself, but must instead refer the matter to another institution (such as a court or tribunal). And, in the USA, where the FTC determines that court action is warranted, it is conducted by the Office of Consumer Litigation — a specialist consumer litigator within the Department of Justice. (The Office also prosecutes actions under the consumer protection programs of other agencies including, the Food and Drug Administration, and the US Consumer Product Safety Commission).

Cross-border redress and enforcement

Many developed countries are focussing closely on reducing cross-border jurisdictional difficulties, particularly as e-commerce grows. In addition, a number of multilateral cooperative arrangements have been established to remove legal (privacy) obstacles to jurisdictional sharing of information, including:

- the International Consumer Protection Enforcement Network (ICPEN), which has 34 member countries, and provides a vehicle for enforcement bodies to exchange information on fraud cases affecting consumers from their jurisdictions; and
- the European Consumer Centres Network (ECC-Net), which is a network of publicly funded information centres across 26 countries, that provides a single point of contact for consumers on their rights, how to formulate a complaint, and assistance in extra-judicial redress⁴.

Also, under the EU Injunctions Directive (1998), member states must recognise the legal standing of 'qualified' consumer organisations from fellow member states in bringing certain legal actions before their own domestic courts.

⁴ For example, a consumer in the UK who has a dispute with a French business, contacts the UK ECC-net, which in turn contacts the French ECC-net to pursue redress for the UK consumer.

Recently the OECD (2007a), in examining mechanisms for improving cross border disputes, suggested special attention be given by governments to the ability of consumers to obtain monetary redress (on the grounds that monetary remedies may be more easily recognised and enforced by foreign courts than other kinds of remedies), and to provide for access to collective action.

Box C.2 Proposed improvements to New Zealand's redress and enforcement tools

Priority recommendations

- Prohibit unfair terms in consumer contracts;
- Require product safety warning notices and provide powers of investigation;
- Allow for cease and desist orders;
- Allow for substantiation notices;
- Permit court enforceable undertakings;
- Provide compulsory interview powers; and
- Allow banning orders.

Warrant consideration

- Include small business in the definition of consumer;
- Make provision in the legislation for mandatory codes of conduct;
- Allow designated consumer groups to submit super complaints;
- Issue formal cautions; and
- Prohibit unconscionable conduct.

Source: MCA (2006).

C.4 Consumer advocacy

The strength and nature of consumer advocacy varies considerably across countries.

- In the USA, there are several well known private consumer groups — for example, the Consumers Union, the National Consumers League, Consumers' Federation of America, and Ralph Nader's Public Citizen — though the strength of their roles is generally agreed to be weaker than during the 1960s and 1970s, reflecting, in part, the removal of public funding and the changed economic environment.

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- Federal funding for consumer groups in Canada was heavily reduced in the late 1980s and since then these groups have struggled. The Canadian Office of Consumer Affairs is concentrating on public funding of networking between the sometimes disparate advocacy groups, rather than seeking to foster an all encompassing body. Consumer representation is said to be better at the provincial level — for example, Quebec, has a tradition of funding consumer groups which had close links with trade unions in the past.
 - The NZ Consumers' Institute is the equivalent of the Australian Consumers' Association (Choice). It is privately funded by subscriptions to its magazine (Consumer), which has around 90 000 subscribers. It also undertakes a broader policy advocacy role.
 - Besides the publicly funded, statutory, National Consumer Council (see chapter 11), the UK version of Choice is known as Which? and has approximately 400 000 subscribers to its magazines.
 - The European Consumers' Organisation (BEUC) comprises 40 members from 29 European countries. Funding for the operational budget is shared equally between members and the European Commission (EC). BEUC lobbies on behalf of consumers, provides training for consumer lobbyists and financial advice for consumer bodies, publishes magazines, and provides telephone help lines and supporting websites. Most of the national consumer bodies are represented, such as Which? (UK) and UFC Que Choisir (France). In addition, the EC funds a separate body, ANEC, to represent consumers in standards development processes.
 - The Danish Consumer Council is a member of the Committee for Consumer Affairs. The Council comprises representatives from 24 organisations, including a significant number of trade unions. About 50 percent of the revenue of the Council comes from the Government.
 - In France there is a system of 'approved' consumer representative bodies (by the Ministry of the Economy, Finance and Industry and the National Consumer Institute). Presently there are 18 approved national associations. The significance of this approval is that it entitles the associations to take legal action to defend consumers' collective interests. (Italy also has a system of approving consumer associations, and requires a minimum of 28 000 members.)

In considering how Australian governments could take steps to strengthen consumer advocacy in Australia (chapter 11), the Commission has had regard to these various approaches.

D Unfair contract terms

Key points

- Unfair consumer contract terms are those that disadvantage consumers, but that are not reasonably necessary for the protection of the legitimate interests of suppliers.
- There are sound in-principle rationales for proscribing unfair contract terms that cause consumer detriment:
 - fairness in contracts is a valued ethical principle, recognised in long standing common law and in broad statutes against unconscionability; and
 - consumers often do not read (what are often complex and long) contracts and may mistakenly ignore the risks that some suppliers will use particular terms against them. This can result in inefficient risk bearing by firms and consumers.
- However, such rationales are not, by themselves, a sufficient reason for proactive intervention.
- ‘Unfair’ terms appear to be widespread in contracts. While there is only limited evidence concerning the extent of their exploitation and the accompanying detriment for consumers, some emerging information suggests the detriment is likely to be non-trivial.
- Existing national laws for dealing with unfair contract terms are slow, costly and uncertain in their application. Various industry codes and some state laws bar unfair or unjust contract terms, and there is a risk that more fragmented and inconsistent approaches to the problem are impending. A clear, nationally consistent approach would provide some benefits.
- But there would also be some costs from a law against unfair terms.
 - There would be some (probably low) administrative and compliance costs.
 - The upfront prices of contracts could be expected to rise somewhat.
 - There would be a risk of unintended impacts for the bulk of consumers if it incidentally weakens the capacity of (non-rogue) businesses to appropriately deal with those few consumers who act in bad faith.
- There is little evidence in Victoria or in the many countries that have enacted laws against unfair contract terms, of significant business compliance costs or adverse unintended commercial consequences. Some businesses have supported such regulation, as have the bulk of participants in this inquiry.
- Proper design of any intervention, including limits to its application, clear definitions of, and guidelines about, unfair terms, and a focus on dealing with terms that cause detriment, is likely to increase the prospective net benefits from policy intervention.

D.1 The role of fairness in the Trade Practices Act

The TPA embraces the overarching objectives of fairness and efficiency (s. 2). Its consumer protection sections proscribe particular types of behaviours inimical to these ends, such as misleading or deceptive conduct, and unconscionable behaviour by businesses. A possible missing element in the suite of tools is a law dealing with unfair contract terms. Many participants alleged that unfairness is increasingly evident in contracts (Frank Zumbo, sub. 49; CCAAC, sub. 38) and that governments should incorporate an additional provision barring such terms into generic consumer law. Box 7.2 in chapter 7 summarises some of their views.

This appendix provides supporting material for the discussion of policy options in chapter 7. It describes what unfair contracts are, the existing state of regulation and why it might be inadequate. It explores the underlying problems that might justify statutes against unfair contracts and the extent of evidence in support of policy measures. It then considers the costs — direct and indirect — that intervention might impose on business and government, and therefore ultimately on consumers.

D.2 What are ‘unfair’ contracts and where are they found?

Unfair contract terms are typically defined as those conditions that disadvantage one party (usually consumers), but that are not reasonably necessary for the protection of the legitimate interests of the other (usually the supplier) (SCOCA 2004, p. 8). Examples of such ‘unfair’¹ terms include reserving the right to vary the contract at any time for any reason, or removing liability for interruptions in supply.

A broader prescribed list of apparently unfair terms has been set out by the Victorian Government in its *Fair Trading (Amendment) Act 2003* (box D.1).

A particular example of a contract term considered unfair is the following from an electricity retailer that attempts a complete exclusion from liability, even in cases of ‘negligent or wilful acts’:

16.3 Exclusion of liability for supply interruptions, distortions or fluctuation. ... as far as the law permits [Retailer A] is not liable for any loss the customer may suffer (including, without limitation, where caused by any negligent or wilful act or omission by [Retailer A]) arising from a) any fluctuation or distortion (in voltage magnitude, voltage waveform or frequency) or interruption to the supply (by the customer’s retail

¹ In general, throughout the rest of this appendix, unfair terms should be read as *potentially* unfair, rather than *objectively* so, because unfairness can be difficult to define and will often depend on the context.

supplier) of electricity to the customer's premises or from any such supply not being or remaining continuous; b) the customer's retail supplier discontinuing supply of electricity to the customer; or c) [Retailer A] interrupting the supply of electricity by the customer's retail supplier to the customer's premises. (Australia and New Zealand Energy and Water Ombudsman Network, sub. 64, p. 11)

Another is by a bank, which specified that the borrower will be in default even if someone else gives incorrect information about them:

... you give, *or another person* gives, us incorrect or misleading information in connection with this loan agreement or a security (italics added). (ACA 2002, p. 3)

Box D.1 **Unfair contract terms**

Typical examples of unfair terms argued to exist in standard-form contracts include provisions that:

- permit the supplier but not the consumer to avoid or limit the performance of the contract, terminate it, vary its terms, or renew or not to renew the contract.
- permit the supplier to:
 - change prices without the consumer's right to terminate the contract;
 - unilaterally determine when the contract has been breached;
 - unilaterally vary the characteristics of the goods or services to be supplied; and
 - assign the contract to the consumer's detriment without the consumer's consent.
- penalise the consumer, but not the supplier, for breach or termination of contract;
- limit the consumer's right to sue the supplier;
- limit the supplier's explicit liability for its agents;
- limit the evidence the consumer can lead in proceedings on the contract; and
- impose the evidentiary burden on the consumer in proceedings on the contract.

Source: Consumer Affairs Victoria (CAV 2003).

Some newer services have contract terms that make it difficult for consumers to complain. For example, the Telecommunications Industry Ombudsman (TIO 2002) has noted that some Internet service providers' contracts stipulate that the supplier can suspend a contract if the consumer complains to the TIO. Some software products require that any dispute resolution occur in a specific physical location, remote from most users.

The concern about such 'unfair' terms mainly relates to standard-form contracts (also referred to as adhesion or boilerplate contracts) issued for services or products used by large numbers of consumers, such as air travel, telecommunications, energy, consumer credit, car hire, holiday packages, home improvements, gym memberships and software sales (SCOCA 2004). Such contracts have been

predominant in consumer markets for some time, with 99 per cent of contracts signed by consumers estimated as standard-form as early as 1971 (cited in Legal Aid Commission of NSW 2006b).

By their nature, standard-form contracts are offered on a ‘take-it-or-leave-it’ basis. For instance, a consumer could not negotiate a higher phone tariff in exchange for a lower termination charge if they left the contract early. While usually the intractability of such contracts is seen as adverse, this is not necessarily so. Many other features of products — such as their physical specifications — also have a ‘take-it-or-leave-it’ nature. For example, a consumer often cannot specify internal electronic components of electrical appliances or the types of plastics used in manufacturing a toy, and these can be as ‘invisible’ as contract terms in a long contract.

Just as physical standardisation of products has allowed economies from mass production, the use of standard-form contracts has become widespread due to the advantages that uniform, pre-printed agreements provide to firms with large customer bases compared with the alternative of negotiating terms with each individual customer. They reduce the training costs of salespeople, who would otherwise need detailed guidelines when negotiating such contracts, and they save time in transactions. They allow for lengthy and detailed agreements to be executed promptly by consumers who only need to consider core terms such as price, quality and product characteristics. In other words, such contracts lower the cost of doing business, with those cost savings at least partly passed on to consumers.

D.3 Existing regulatory measures

The undesirability of unfairness in contracts between parties with different bargaining capacities has been a longstanding theme in Australian (and Anglo-Saxon) common law. This proscribes unconscionable behaviour and at times, has adopted the broader position that contracts between parties have an implied requirement for acting in good faith² (Hockley 2003, Allens Arthur Robinson 2005, McDougall 2006; Frank Zumbo, sub. DR217, pp. 7ff).

The requirement for a certain standard of fairness has also been set out in the general statutes for consumer protection under the unconscionability provisions (s. 51AA, 51AB and 51AC of the TPA and mirror provisions in the Australian Securities and Investments Commission (ASIC) Act and State and Territory Fair Trading Acts). NSW enacted the *Contracts Review Act 1980 (CRA)* before the

² In this context, this means contractual rights must not be exercised ‘capriciously or for some extraneous purpose’.

unconscionable conduct provisions of the TPA came into effect to control unjust consumer contracts in general. Unjustness is defined in s.4 to include ‘unconscionable, harsh or oppressive’, the so-called ‘tautological trinity’ observed by Justice Sheldon (Handley 2003). More recently, Victoria has implemented its own unfair contracts provision within the *Victorian Fair Trading Act 1999* (box D.2), which has wide scope in defining and dealing with unfair contracts.

Box D.2 The Victorian Fair Trading Act 1999 (2003)

Concerns over the growth of standard-form contracts, perceived limitations of the generic unconscionable conduct provisions and the introduction of specific legislation in this area by the European Union, led Victoria to amend its Fair Trading Act in 2003 to include provisions (s. 2B) that specifically address unfair contract terms. While the legislation draws heavily on the model adopted in the United Kingdom’s *Unfair Terms in Consumer Contracts Regulations 1999*, which focuses on substantive rather than procedural unfairness, the Victorian provisions have been criticised because they have considerably wider scope (see below).

In the Victorian legislation, a term is considered unfair ‘if contrary to the requirement of good faith and in all the circumstances it causes a significant imbalance in the parties’ rights and obligations under the contract, to the detriment of the consumer (s. 32W).³ If a court finds a term unfair, the term is void, though the rest of the contract stands. The statute does not apply to contracts between a supplier and a business, or to contracts covered by the *Consumer Credit (Victoria) Act 1995* (though the desirability of inclusion of the latter was subject to consultation in 2007, and a bill was tabled in December 2007 that will give the CAV powers to act for consumers using the UCCC).

Key differences between the Victorian and UK models include that the former:

- provides for a list of prohibited terms to be developed through the regulations;
- extends the reach of the provisions to non standard-form contracts; and
- covers terms relating to the price of a product. (This has been a point of concern for business groups because it potentially allows consumers to challenge contracts where suppliers charge different prices to different consumers.)

There are also several measures applying in specific industries. The *Uniform Consumer Credit Code 1996* proscribes ‘unjust’ transactions, which are defined in the same way as in the CRA. And, an industry code for the telecommunications industry, developed by the Australian Communications Industry Forum (ACIF 2005b), contains guidelines indicating that a term is unfair if it causes a significant

³ The reliance in the Victorian definition on the absence of ‘good faith’ emulates s. 5(1) of the UK legislation and Article 3 of the European Union directive 93/13/EEC 1993 on *Unfair Terms in Consumer Contracts*.

and unreasonable imbalance in the parties' rights and obligations to the detriment of the consumer.

The details of these various regulatory measures are well documented by the ACCC (sub. 80, pp. 72ff), the Victorian Government (sub. 72), the New South Wales SCLAJ inquiry (2006) and the Ministerial Council's discussion paper (SCOCA 2004).

Unconscionability provisions play an uncertain role

The capacity for unconscionability provisions to deal with particular unfair contract terms is often questioned (Zumbo 2006 and sub. DR217). In particular, it is widely argued that the courts have taken a narrow view of the existing TPA provisions on unconscionability (a situation apparently replicated for the CRA — SCOCA 2004, pp. 25-26). It is claimed that courts have not found contract terms, *by themselves*, to be unfair ('substantive' unconscionability), and rather have taken into account the surrounding circumstances ('procedural' unconscionability).⁴

For example, in *Hurley v McDonalds Australia Ltd (1999)* the Federal Court of Australia said that:

Before sections 51AA, 51AB or 51AC will be applicable, there must be some circumstance other than the mere terms of the contract itself that would render reliance on the terms of the contract 'unfair' or 'unreasonable' or 'immoral' or 'wrong'.

Among other possibilities, procedural unconscionability could entail taking advantage of a person with an illness or disability. In the most recent case law, the Federal Court in May 2007 found that a company, NuEra and its agents, who sold cures to cancer victims, had acted unconscionably by exploiting their vulnerability.⁵

That said, there is not much case law in this area and the limits of the unconscionability doctrine in the TPA have yet to be firmly determined. (The provisions themselves are outlined in box D.3.) S. 51AB(1) does not specifically define unconscionability, nor — unlike s. 51AA(1) — does it make any reference to the 'unwritten' or common law.⁶ This suggests a wider application of s. 51AB(1) (Miller 2007, p. 495).

⁴ Not all agree that this constitutes 'narrowness'. The Victorian Bar (2004) argues that the dichotomy is a false one, and that the determination of substantive unfairness must always take account of the circumstances surrounding the contract.

⁵ *ACCC vs. NuEra Health Pty Ltd 2007*, FCA 695 (9 May).

⁶ These are the common law principles of unconscionability set out in the specific equitable doctrines established by the courts at equity (Miller 2007, p. 484).

Box D.3 Unconscionability in the Trade Practices Act

Unconscionability is covered in Part IVA of the TPA under three sections. For consumers the two important sections are s. 51AA (a general provision) and s. 51AB (a consumer-focused provision). Section 51AC relates to business to business transactions and is modelled on s. 51AB.

s. 51AA: Unconscionable conduct within the meaning of the unwritten law of the States and Territories

This requires that a corporation must not, in trade or commerce, engage in conduct that is unconscionable within the meaning of the *unwritten law*, from time to time, of the States and Territories. It does not apply to conduct that is prohibited by section 51AB or 51AC.

s. 51AB: Unconscionable conduct

This relates to business to consumer transactions only. It prohibits conduct that, in all the circumstances, is unconscionable. In s. 51AB(2) the provision stipulates a non-exhaustive list of circumstances that are relevant to judging whether conduct is unconscionable. These are:

- (a) the relative strengths of the bargaining position of the parties;
- (b) whether the consumer was required to comply with conditions that were not reasonably necessary for the protection of the legitimate interests of the corporation;
- (c) whether the consumer was able to understand any documentation related to the supply of goods or services;
- (d) whether any undue influence or pressure was exerted on, or unfair tactics used against, the consumer; and
- (e) the amount for which, and the circumstances under which, the consumer could have acquired identical or equivalent goods or services from a person other than the corporation.

In applying the provision, the Court shall not have regard to any circumstances that were not reasonably foreseeable at the time of the alleged contravention (that is, it is not possible to have 'accidental' unconscionability).

The section makes no reference to the common law or any other definition of unconscionability and in doing so may imply a wider scope than s. 51AA. The Copyright Law Review Committee (2002, pp. 154-5) noted that there is some case law explicitly recognising that s. 51AC and s. 51AB embrace a wider definition of unconscionability. However, that committee considered the degree to which this was true was 'unclear' at the time.

Source: Trade Practices Act 1974.

Better guidance from government about the interpretation of unconscionability has followed the introduction of s. 51AC, which deals with this issue for small business. The Second Reading Speech and the Explanatory Memorandum for the *Trade Practices Amendment (Fair Trading) Bill 1997* makes clear that s. 51AC deals with unconscionability in a much wider sense than s. 51AA. The Explanatory Memorandum said that the new provision would:

... assist in the judicial evolution of unconscionable conduct, away from limited procedural unfairness doctrine towards a substantive fairness protection.

As Telstra (2004, pp. 13ff) notes, by inference this extends to s. 51AB, on which s. 51AC is explicitly modelled. The clarification given by the Explanatory Memorandum to any ambiguity in the application of s. 51AB is a relatively recent one, so there is not yet jurisprudence that has used it to help interpret the black letter law.

Certainly, the factors that a court may have regard to in determining unconscionability include both procedural and substantive considerations (s. 51AB(2) in box D.3) — a point emphasised by Zumbo (2006). Moreover, the provision does not require that all these conditions must be present. This may allow action on unfair terms, noting that s. 51AB(2) specifies a condition that is close to the definition of an unfair term used in this appendix and by SCOCA (2004). The single explicit constraint is s. 51AB(1), which bars conduct that ‘in all the circumstances’ is unconscionable. This suggests that the court must look at the full context of the contract, bringing a procedural element back into play. But arguably, this is not a fundamental constraint on the operation of s. 51AB, since it also exists for both the Victorian and UK unfair contracts laws, which have been widely used to change unfair terms. As Consumer Affairs Victoria (CAV 2003, p. 28) observed, while the UK regulations (on which its own law is modelled):

... obviously have regard to the substantive unfairness of the relevant term, the controlling factor is still procedural; that is, whether or not the supplier acted in good faith.

It also pointed out that under the Victorian unfair contracts legislation, a term considered fair in one context may be deemed unfair in another if it is detrimental to the consumer (CAV 2003, p. 13). Like s. 51AB(1) of the TPA, this reflects the requirement in the Victorian legislation (s. 32W) for the court or tribunal to take account of ‘all the circumstances’ when determining an unfair contract term. So the phrase ‘in all the circumstances’ should in principle no more curtail courts applying s. 51AB in cases of alleged unfair contracts than its counterpart in the Victorian legislation.

Some suggest that several recent trade practice decisions substantiate that there has been a move to a more expansive interpretation of unconscionability, including a duty of good faith and concepts of unfair contracts (Griggs 2001, Horrigan 2002, Telstra 2004). In several court cases, including *ACCC v Simply No-Knead (Franchising) Pty Ltd (2000)* and *ACCC v CG Berbatis Holdings Pty Ltd (2000)*, the Court explicitly acknowledged that s. 51AB and 51AC do not turn on the vulnerability of the plaintiff, a point observed by several commentators (ACCC, sub. 80, p. 78 and the Legal Aid Commission of NSW 2006b). One participant in this inquiry (Michelle Sharpe, sub. 5) argued that s. 51AB could deliver better outcomes for consumers with improved enforcement and case preparation by the ACCC. (The issue of enforcement generally is discussed in chapter 10.)

While the treatment of ‘unfair’ contract provisions is still uncertain, capriciously or unreasonably giving effect to a provision of a contract *is* covered by the unconscionable conduct provisions. So, while the Courts may not find that a provision in a home loan contract to ‘vary the conditions at any time’ is unconscionable, if the bank then tried to *use* the clause to make a customer pay back a loan in a month then that would be unconscionable.

For example, in *Dai v Telstra Corporation 2000* 171 ALR 348, the appellant (Dai) submitted that the action of Telstra in applying a contract clause was unconscionable conduct. Telstra charged Dai about \$70 for four calls made to a Chinese language sex service in the Seychelles. Dai denied he made the calls. Telstra responded by disconnecting his phone service (as per the conditions of his contract). The Full Court held that the matter should be allowed to proceed to trial indicating that the language of the unconscionable conduct provisions under s. 51AB was broad and could cover such actions, even when no vulnerability existed.

So s. 51AA, 51AB and 51AC may not (turn out to) be as limited in their legal capacity for dealing with unfair contract terms that are exploited by a business.⁷ Nevertheless, the uncertainty about its evolving interpretation aside, there are pragmatic difficulties in using the TPA generally for the abuse of unfair terms in consumer standard-form contracts.

- Actions under these provisions take a long time to move through the courts. This reflects the seriousness of the violation of the law, the complexity of the issues, the difficulties in defining unconscionable behaviour and the fact that, defendants, wishing to avoid a reputation for acting unconscionably, often take matters to appeal. As an illustration, the *ACCC vs Acepark Pty Ltd* (relating to the sale of horse betting software), a relatively straightforward matter, took 15 months; *ACCC vs. Brambles Australia Ltd (Cleanaway)* (which related to inappropriately procuring a contract for waste removal) took more than 20 months; and *ACCC vs Lux Pty Ltd* (the sale of a vacuum cleaner to a vulnerable consumer) initially took four years and then went on to appeal. The most recent application of s. 51AB(1) — relating to sales of bogus cures for cancer (*ACCC vs NuEra Health Pty Ltd & others*) — has been the fastest in recent history — taking 6 months.

⁷ Even unconscionability cases that have failed may sometimes produce beneficial outcomes for consumers by encouraging voluntary compliance. For example, as part of *ACCC v Oceana Commercial Pty Ltd & Ors [2003]*, the ACCC alleged unconscionable conduct by the Commonwealth Bank of Australia (CBA). The case involved sales of overpriced real estate on the Gold Coast to out-of-state buyers ignorant of reasonable valuations. The CBA did not disclose in the financing contract, or in any other way, its awareness that the properties were overpriced. While the ACCC’s case failed, it prompted the CBA to change its lending practices (Sharpe and Parker 2006, p. 40).

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- Actions are expensive to litigate, which stems from the nature of the courts and the usually protracted nature of court proceedings. Even private actions can be costly. In one case involving allegations of unfair treatment of third party guarantors, the costs for a private party were \$70 000 (Lovric & Millbank 2003). In cases pursued by the ACCC against corporate entities, both parties will customarily spend hundreds of thousands and sometimes millions of dollars in legal and other costs. For example, for a selection of unconscionable court cases, the ACCC's costs (before the awarding of costs to either party) were between \$200 000 and \$1.4 million.⁸
 - Actions under these provisions do not provide the ex ante capacity to strike out contract terms that, on the face of it, would be likely to be unfair in most circumstances.

Consequently, there have been few cases. It is these practical limitations of the TPA, the uncertain direction of judicial interpretation of s. 51A and the narrow focus of alternative industry-specific arrangements that are driving arguments for new statutory measures.

Policy developments: national approaches to unfair contract terms

The perceived limitations of the existing provisions in the TPA and FTAs have led to calls for a different kind of statute. This has been accentuated by concerns about a growing number of problems with unfair contract terms across Australia. The Ministerial Council on Consumer Affairs (MCCA) established a working party to investigate options to address the issue and the merits of adopting a nationally consistent approach. The working party concluded that the adoption of a model based principally on the Victorian legislation was the preferred national response. Submissions to this inquiry by consumer advocacy groups and some governments have broadly reiterated that view.

But while MCCA agreed to progress a national response to unfair contract terms in 2005, despite repeated attempts, the proposals have not passed the processes required for such new regulations. Why this is the case is discussed later.

Overseas

Internationally, there appears to be an increasing tendency to prohibit unfair contracts using statutes that have much broader application than those available in Australia's TPA and all State FTAs, bar Victoria's. The UK and the EU have added

⁸ ACCC, pers. comm. (27 June, 2007).

unfair contract provisions similar to the Victorian Act. Thailand has a provision and New Zealand is considering one. The notion of unfairness is embedded in US law in a very general way, with the boundaries of unfairness shaped by case law and subsequently codified as required (ACCC, sub. 80, p. 71). In the latter case, however, US law does not appear to have had much effect in controlling unfair standard-form contracts, as evidenced by the difficulties faced by US corporations trading with European consumers (Winn and Webber 2006).

The UK provision is of particular relevance to Australia, given the similarities of the Australian and British legal and commercial systems. It has been in place since 1994 (and amended in 1999) and is similar to the Victorian legislation, except that it does not cover upfront prices or negotiated contracts. However, there are apparently moves afoot to cover these features too (ACCC, sub. 80, pp. 75-76).

D.4 Is there a conceptual rationale for intervening?

As emphasised throughout this report, among other policy tests, interventions by governments have to be justified by sound rationales (this section) and evidence that the problem is significant enough to warrant action (section D.5).

In the Commission's view, there is a potential rationale for intervention against the damaging *exploitation* of contract terms. There are also arguments for prohibition of the *existence* of 'unfair' contract terms per se, though these are less strong. But, before sketching out why, it is important to emphasise at the outset that a rationale is a necessary, but not sufficient, requirement for intervention. It is a *conceptual* and *hypothetical* argument that might justify government intervention of some kind, but whose actual relevance will depend on evidence of the severity of the problem, the adequacy of existing laws and the practicality of new remedies.

The arguments surrounding the rationales for intervention are complex — a reader wishing to avoid them should turn to the end of this section for a quick summary.

Fairness is a valued ethical principle

A strong in-principle reason for government intervention is that fairness is a highly valued ethical norm. Most people abhor unfairness for both themselves and others. This appears to be the main basis for action identified by participants in this inquiry. People often think that such ethical concerns are outside the usual domain of economics. However, this is an excessively narrow view of economics, which can account for anything of value in people's preferences, including altruism and the demand that others behave fairly. In that case, an act of unfairness committed by A

on B will not only produce costs for B, but for others who are aware of the act. It is as ‘inefficient’ to have such unfair acts, as it is to allow unmitigated pollution. In any case, acts of unfairness can undermine trust and social capital generally, increasing the costs of all kinds of transactions between people (PC 2003b). So there can be a broader payoff from abating unfairness. (The difficulties in practically working out what is unfair or fair is a separate issue, discussed later.)

In personal relations, norms are usually dealt with by social means (for example, disapproval), rather than legal prohibitions. In less personal contexts, in which such social sanctions are ineffective — such as commercial transactions — laws play a bigger role.

Unfair conduct takes many forms, of which abuse of unfair contract terms is a small part. The TPA already incorporates many explicit restrictions on unfair practices, including among a long list, misleading or deceptive conduct (s. 52), false or misleading representations (s. 53), bait advertising (s. 56) and pyramid selling (s. 61). As noted above, in certain contexts, unfair contracts are already actionable using the unconscionability provisions in s. 51AA, 51AB and 51AC, which at the time of its introduction was seen as drawing on the ‘dictates of morality’ (Sharpe and Parker 2006, p. 5, pp. 9-10). Outside the TPA, well-established common law equity principles provide redress in cases of (gross) ‘unfairness’.⁹ In that context, contesting the ethical rationale for laws against unfair contracts would represent an unravelling of legal principles formed over centuries.

Nevertheless, it should be emphasised that laws do not need to address every unfair act and that enforcing one right can undermine the achievement of other rights (chapter 3). The economic efficiency costs or benefits of enforcing such ethical imperatives may help to define their limits.

Are there conventional economic arguments for intervening?

Beyond the ethical grounds for some legal remedies against unfair contract terms, there are some more conventional economic rationales for action, though these are less strong.

Any economic rationale has to explain why markets might not function adequately in the absence of government intervention. Markets generally allocate resources and risks effectively, at least over the longer term. If consumers value fair play by firms,

⁹ See for example the case of *Planet Securities Unit Trust v Dalrymple* described by the Australian Institute of Company Directors (2000) and the discussion by the Victorian Bar (2004).

the question arises as to why firms would not organise themselves to exploit the market advantages that this behaviour would bestow.

The model of perfectly informed consumers is of limited relevance

A 'naïve' model would conjecture that consumers read all contractual terms, observe the unfair ones and then either negotiate for their alteration or buy from another supplier. The market would work efficiently, and any residual 'unfairness' might be seen as optimal in the sense that the costs of addressing it would exceed the benefits.

However, as noted above, businesses commonly use standard-form contracts to avoid the significant transactions costs of negotiated contracts in sales of relatively homogeneous goods and services to large numbers of consumers. Consequently, even if there were a desire for consumers to have the capacity to negotiate, the value of this capacity is unlikely to be worth the price consequences it would elicit through raising transaction costs. As a result, competitive pressures between suppliers will, in the overall interests of consumers, tend to encourage obligatory standard-form contracts and weaken the forces that would otherwise operate to eliminate specific clauses that some consumers do not like.

It might still be supposed that consumers could read the various standard-form contracts from competing suppliers and choose the supplier that avoids unfair terms. However, in many instances, the allegedly unfair terms are in the body of a complex contract and expressed in 'legalese' (Frank Zumbo, sub. 49).

Generally, consumers neither read nor seek independent advice regarding such contracts except where large financial amounts are at stake. A survey by the Queensland Office of Fair Trading suggested that at least half of those signing contracts failed to read or understand them (OFT 2002). CAV (2007b, p. 16) found that around one quarter of consumers failed to read contracts at all (with another 21 per cent only giving them cursory consideration). An ANZ survey of financial literacy found that 50 per cent of people in the lowest financial literacy quintile were unable to calculate half of \$1400 (ANZ and ACNeilson 2005b, p. 282) — which would limit their understanding of the implications of even simple contracts. Some forms of contract are rarely read by any consumers. For example, to check whether purchasers read its end user licence agreements, a software firm inserted a clause offering a financial prize to those who had read the clause and contacted them about it. No one claimed the \$1000 prize for four months, during which time there were over 3000 downloads of the firm's software (Clapperton and Coronas 2007, p. 11).

Often it is practically difficult for consumers to read contracts, due to:

- the way in which contracts are divulged. For instance, this might involve numerous links in m-and e-commerce transactions. Software end-user licence agreements may be contained in a shrink wrapped package and only available for examination after purchase;¹⁰
- the small amount of time permitted in some contexts. For example, Ticketmaster allows three minutes (before they reallocate the tickets to other purchases) for a user to provide personal details as well as read: a summary contract, a ‘Purchase Policy’ and a ‘Privacy Policy’. These three documents have 3025 words in total. To go through these documents in their entirety in three minutes, consumers would need to read at a rate of nearly 17 words per second (Clapperton and Coronos 2007, p. 30). At that pace, a consumer could read a King James Bible in less than 14 hours;
- their small print size; and
- the length of the contracts. For example, some mobile telephone contracts have apparently reached 500 pages (Cousins 2006, p. 62).

In effect, many disclosure documents for standard goods and services meet the legal requirement for disclosure and protect suppliers’ interests, but are neither read nor intended to be read by consumers.

Even if aware of unfair terms, consumers usually and rationally proceed on the basis that they trust that these terms will not be exploited, or that they cannot avoid such terms by transferring custom to another supplier. (The latter reflects the fact that suppliers themselves economise on the costs of formulating contracts by copying the main features of others’ contracts.)

The trust exercised by consumers is usefully seen as a judgment about a certain type of default risk of transacting — the likelihood that the implicit contract, rather than the written contract, will be breached by a supplier. Consumers form such judgments based on the reputation, behaviour and their past experiences of firms. Consumers will often require a discount if dealing with a firm whose default risk is higher or uncertain. And they are more prudent in transactions where there is a big downside risk (a house or a car purchase).

Competition plays a role in underpinning that trust where repeat purchases are significant and consumers can easily switch suppliers. In this case, any attempt to

¹⁰ The enforceability of such contracts is still contentious. However, regardless, consumers would usually have the right to purchase the product, review terms, return the software and receive a refund, so that there is not complete loss of a capacity to respond to an unattractive contract (Kunkel 2002).

exploit unfair contract terms for a significant number of consumers in one period would encourage widespread subsequent defection to competitors and a damaging loss of reputation.¹¹ (The issue of non-competitive markets and whether they present a problem for trust is discussed later.)

Consumer trust in implicit contracts can still result in efficient markets. But it also opens the possibility of market failures in certain circumstances:

- if consumers make systematic errors in appraising default risks; and/or
- if ‘good’ firms find it hard to cheaply signal that they will generally act in good faith.

The next two sections examine the issues that arise from this.

Suboptimal risk appraisal and insurance

A key issue is whether consumers are good at appraising risk

While implicit contracts may work well most of the time, it should not be presumed that consumers are good at estimating the default risks of competing suppliers. The behavioural research suggests that consumers can be poor at estimating and understanding low probability risks (appendix B, ACCC, sub. 80, p. 73 and Consumer Action Law Centre, sub. 100, p. 7). They may underestimate or overestimate them depending on the context. *If* they underestimate the risks, then the tradeoffs between default risk and market prices will be distorted.¹² This point was noted by the Consumer Action Law Centre (sub. 100, p. 7) and reiterated by the Joint Consumer Groups (sub. DR228, pp. 16-17).

Suppliers would then have more leeway to default, without having immediately to lower prices, encouraging a higher than optimal default risk among suppliers. While prices may then tend to fall over time as the rents created by higher default

¹¹ Even in such markets, it is still possible that a rogue trader may systematically exploit contract terms, or that a generally reputable firm may act in bad faith (whether accidentally or deliberately) for a few customers. But rogue traders tend to have short lives, while the commercial gains for reputable firms of one-off acts of unfairness would have to be small, and the risk of adverse publicity might still be significant.

¹² Vickers (2003) has drawn a parallel between the impacts of unfair contracts and consumer ‘lock-in’, where consumers facing high future switching costs enter arrangements on the basis of attractive early conditions, underestimating the extent to which they are bound to subsequent, less attractive, terms.

opportunities were bid away through competition, economic inefficiency would still arise in several ways.¹³

Consumers give up some insurance

While consumers could get lower priced goods, unfair terms may result in the underinsurance of high cost, low probability events. An example might be if a rental car company had provided inadequate contractual insurance for an accident and the liability fell on the consumer. Underinsurance might particularly affect disadvantaged consumers, who will often have little capacity to self-insure, even for contingencies regarded as low cost by most consumers.

Efficient risk bearing by suppliers is generally undermined

Unfair terms may shift the management of risks that firms deal with better than consumers. Firms are usually well informed about, and able to control to a reasonable extent, the risks associated with the quality, timeliness and continuity of supply. This includes managing the risks associated with product safety, prudent financial management, avoidance of fraud, changes to input costs and interruptions to service delivery due to equipment malfunction. It excludes cases when consumers are careless or irresponsible.

This recognition of efficient risk bearing is already evident in current regulation. This includes product safety, where initial liability for defective goods rests with suppliers (with caveats to cover contributory negligence by consumers), and in financial services (such as the EFT code), where financiers are responsible for bearing most of the cost of fraud, subject to appropriate behaviour by the consumer who has been defrauded.

Efficient risk bearing by particular firms can be further undermined

A failure to deal effectively with the use of unfair contract terms may also lead to a less than ideal allocation of risks across firms. For example, imagine two electricity suppliers A and B. They both have low absolute risks of significant electricity supply disruptions, so that consumers cannot readily distinguish them on this basis. But suppose the probability of costly disruptions is nonetheless four times higher in A than B. A law against unfair terms would mean that supplier A could no longer shift the costs of disruption to those particular consumers affected, but would

¹³ In most cases, alleged unfair contracts arise in industries that can broadly be described as competitive, at least in the dynamic sense.

initially need to bear the risk itself, financing that risk through an increase in its upfront prices for all its consumers. Accordingly, the relative inefficiency of A would be revealed in higher prices. A then has a better incentive to manage their risk more effectively or lose market share to B. In other words, price differences are harder to conceal than low probability, high cost contingencies borne by particular customers after contract commencement.

The implications of such market failures

If correct, the deviation from optimal risk bearing described above has the implication that intervention, might, in principle, be warranted. But it has other, less obvious, implications.

Firstly, it is apparent that the foundations underpinning such analysis are subtle and uncertain. It relies on the assumption that consumers underestimate the relative default risks of suppliers when the risks are absolutely low. There is some behavioural evidence for that proposition. For example, people appear to underestimate the likelihood of car accidents. On the other hand, there are contexts where it appears to be wrong for very low probability, unpleasant events, like plane accidents. The behavioural evidence suggests it might be hard to establish a rule about risk appraisal biases.

Secondly, it implies that the likelihood that implementing unfair contracts law would raise prices is not a decisive criticism on its own (a point emphasised by Frank Zumbo, sub. DR217, pp. 11-12). If the above rationale is correct, it is *desirable* that prices rise precisely because it is through higher prices that consumers pay for their implicit desired insurance (risk pooling) and risk is allocated efficiently. The right efficiency criterion is not whether prices might rise with government intervention, but whether they might rise too much or cause other problems. This could occur if intervention excessively transferred risks, substantially raised compliance burdens, or restricted consumers' product choices.

Thirdly, it suggests that estimating the net economic costs of unfair contracts is even harder than might be supposed. It is wrong to measure the costs as the sum of the gross losses experienced by consumers who face contract default (and the more general costs people may experience when observing unfairness for others). The real cost is the gross losses, *less* the gains made by all consumers from lower prices (that is, the gain from not paying an implicit insurance premium).

Finally, by their nature, the market failures identified above do not relate to readily observed contract terms — such as upfront prices. Consequently, concerns about 'unfair' upfront prices would have to arise from other types of market failures, such

as unconscionable exploitation of a disadvantaged person or abuse of market power. These problems are already targeted by several existing statutes in the TPA and FTAs and are not usually seen as requiring additional measures in a legislative approach to unfair contracts.

In the absence of intervention, market signals of default risk may be inefficient

Firms generally try to act in good faith and they signal that in various ways. For example, they invest in brand names, guarantee satisfaction for the goods they supply, offer warranties for faults and so on. But it is hard for them to cheaply and credibly signal they will act reasonably in *all* respects of their dealings with consumers.

This is because good firms still need a conditional capacity to deal with consumers who themselves may act unfairly and unreasonably (for example, driving a rental car recklessly) and to manage the commercial risks from some catastrophic contingencies (for instance, electricity interruptions arising from widespread floods or fires). Consequently, good firms cannot eliminate all notionally unfair contracts as a signal of their intention to act in good faith. In any case, if consumers do not read contract terms, then they will not be able to distinguish firms with fair terms from those with unfair ones. Price signals (as discussed previously) will not work as reliable signals to consumers unless ‘bad’ firms bear the costs of their higher default risks. Collectively, these factors mean that good firms are not so easily distinguishable from bad firms with higher default risk. This is reinforced by the fact that bad firms have an incentive to appear like firms with lower default risk.

The weakened ability of firms to cheaply signal their trustworthiness implies that a proportion of ‘untrustworthy’ firms can survive in a market, at least temporarily, and that overall consumer trust is lower than it should be. Moreover, even if untrustworthy firms subsequently exit, markets are dynamic, so that some new ones will enter.

A law outlawing the use of unfair contract terms might be more efficient than the market dynamic that forces untrustworthy firms to exit over time. By raising the costs and prices of firms that hitherto had higher default risk, it would restore competitive advantage to those with lower risks and raise consumer trust. The proportion of untrustworthy firms would fall. Conceivably, such a move would also reduce the costs for business of signalling reputation and reduce transactions costs for those consumers who currently read the fine print to avoid manifestly unfair provisions.

It is clear that sometimes firms and consumers value ‘signalling’ regulations of this type. Doctors value regulation-based licensing and professional standards —

because they provide credible setting and policing of standards that would be more expensive to provide in a free market. (While such mechanisms can sometimes turn into anti-competitive entry barriers — chapter 5 — this is not automatically the case). A more recent example is the concern expressed by reputable universities about the need for regulation to control the mistreatment of foreign students by disreputable institutions.

Commenting on this rationale for unfair contracts regulation, the Commonwealth Consumer Affairs Advisory Council (sub. 38) noted such regulation could improve consumer confidence that contracts would not contain egregious elements, like hidden costs. It saw this as particularly important in e-commerce and m-commerce where (lack of) trust appears to be an issue impeding this form of transaction (chapter 13). As well, it noted that the policy change could allow for a reduction in the stringency of regulated disclosure requirements faced by firms.

In the Commission’s consultations in Australia, several firms argued that there is a need for regulation generally to deal with fringe operators — for example, small ISPs and telecommunications firms — that might not behave properly. In the Commission’s discussions with European and UK business groups, the value of unfair contracts statutes in dealing with the fringe of bad behaviour was identified as a valuable outcome. Some in Australia also advocated a new national generic unfair contracts law based on the growing divergence and variety of regulations across industries and jurisdictions (for example, Telstra, sub. 35, p. 22).

Is market power another economic rationale?

One argument sometimes put is that unfair contracts are used by firms with market power (Field 2003) and that regulatory controls are justified on this basis. However, the key unanswered question is why such firms would choose this indirect and uncertain way of exercising market power when they could simply raise prices. Indeed, the limited empirical evidence suggests that firms with market power choose to exercise it through prices, not by eroding the fairness of their standard-form contracts. Marotta-Wurgler (2005) examined around 650 software license agreements among firms, and found that those with market power did not offer relatively harsher terms than those without such power. More generally, many commentators have claimed that unfair terms flourish in quite competitive industries (Consumers’ Federation of Australia 2004; Field 2003). Thus, it appears that factors other than market power account for ‘unfair’ terms.¹⁴

¹⁴ One case where market power might affect contract terms would be if the firm — say an incumbent utility without many competitors — was subject to price regulation, but not rules about reasonable terms.

Rationales: a summing up

There has been relatively little rigorous setting out of rationales for action on unfair contracts. Yet such rationales are an essential prerequisite for considering policy intervention. Moreover, in the event that the benefits of intervention exceed its costs, such rationales are necessary to guide the design of policies.

A key rationale for action is ethically based. Two other, less clear-cut, arguments are:

- that consumers may underestimate certain risks, resulting in inefficient risk bearing among firms and consumers; and
- unfair contract regulations may help drive out ‘bad’ firms that act in poor faith and that would otherwise survive in greater numbers because of the difficulty for consumers of distinguishing them from ‘good’ firms.

Moreover, these rationales not only provide a sound in-principle case to stem the damaging *use* of unfair terms, but also grounds to stem the *existence* of unfair terms in some circumstances.

In particular, dormant, but unused, unfair terms may be problematic to the extent that the underlying beliefs to which they give legitimacy are manifestly unfair (as noted by the Redfern Legal Centre, sub. DR151, p. 10). For example, the community would consider a contract provision that discriminated against a race or religion as unethical, even if a consumer could get a regulator to stop a business from using it. One issue then is whether a provision is inherently unethical or whether its use in a particular context is unethical.

Secondly, there might also be pragmatic grounds for action against the existence of unfair terms:

- Consumers may not be aware of their rights to seek redress if a business uses a contract term unfairly (Victorian Government, sub. DR226, p. 60; Redfern Legal Centre, sub. DR151, p. 10). In its consumer survey relating to unfair terms, CAV found that around half of consumers believed that terms and conditions prevented them from taking further action or were unsure if they could take action. In that instance, the existence of a term can act as a deterrent to reasonable consumer behaviour, without the business ever actually using the term. For example, a consumer wishing reasonably to terminate a contract may not do so because of concern about excessively high termination charges. The fact that the unfair term has not been ‘used’, does not mean there is no detriment (Victorian Government, sub. DR226, p. 60; Redfern Legal Centre, sub. DR151, p. 10).

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- It may be efficient to outlaw some unfair terms if it were likely that businesses would detrimentally exploit them, or if there were practical difficulties and transaction costs in providing adequate redress for consumers affected by the use of such terms.

D.5 Incidence and consequences of ‘unfair’ terms

As emphasised earlier, rationales are a first step in making the case for specific measures to deal with unfair contract terms. A second important step is to assess whether there is evidence of problems large enough to warrant policy action.

‘Unfair’ terms appear to be widespread

There is considerable evidence that terms of the kind described as unfair in box D.1 are common in many contracts across many industries in Australia and that their existence is widespread globally where regulatory mechanisms do not discourage this. Systematic investigation by the Communication Law Centre of the leading Australian telecommunications suppliers in 2004 found many instances of unfair terms. ASIC (2004) cited concerns in a range of financial service areas about arguably unfair terms. Many specific examples have been provided in submissions to various inquiries/studies (for example, Australian Consumers’ Association 2006; the Energy and Water Ombudsman NSW — EWON 2006c — and the Consumer Action Law Centre 2008), and various legal aid agencies and regulators have claimed they are generally prevalent in standard-form contracts. For example:

The experience of the Commission is that unfair contract terms in consumer contracts are so widespread and have such an impact that legislative reform is demanded (Legal Aid Commission of NSW 2006b).

Our experience is many hundreds of terms have been amended as a result of the work that we have done and amended on a voluntary basis by businesses. (Cousins 2006 from Consumer Affairs Victoria)

Submissions to this inquiry have also claimed the widespread use of unfair terms (for example, Frank Zumbo, sub. 49 and the Joint Consumer Groups, sub. DR228, with examples given at pp 45ff).

Thousands of contraventions were detected in the UK after prohibition of unfair contracts terms came into force (SCOCA 2004). In Europe, prior to the introduction of measures against them, market studies revealed ‘the ubiquity of unfair terms in standard-form contracts’ (EC 2000). The share of standard-form contracts including apparently unfair terms often exceeded 50 per cent with, for example, 55 per cent of contracts for consumer goods judged to have unfair limits on liability and

49 per cent assessed as abrogating consumers' statutory rights. While the European Commission considered that the problems leading to regulatory action were particularly high in some sectors (real estate, motor vehicles, financial and insurance services), it still found their wide prevalence in many other sectors (essential services, moveables, electronic goods, leisure activities and tourism). The European Commission also noted the difficulties in even assessing contract terms for potential unfairness because contracts were often not readily available.

Evidence for their exploitation is incomplete

Despite persistent interest in the issue of unfair contracts over many years and good documentation of what appear to be unfair terms, there is only modest systematic evidence that firms frequently inappropriately *exercise* the rights that such terms bestow upon them. The bulk of concern about the exploitation of unfair contract terms has been based on particular instances (box D.4).

As an illustration of this, in 2006, the NSW Office of Fair Trading provided examples of unfair contract terms in a variety of industries and suggested businesses sometimes exploited these. But the Office could not provide any estimates of the incidence of such complaints, or comment in detail on the conduct of businesses that it said had exploited such unfair terms.

All jurisdictions have had the same issues we are facing here, in that no States have good information specifically about the conduct. However, the incidence has probably increased since 1980. (Baker in SCLAJ 2006, p. 5)

A similar national inquiry into unfair contracts (SCOCA 2004, p. 18) cited the same indeterminacy in the evidence. The ACCC also identified gaps in evidence, both about the extent of unfair contract terms (sub. 80, p. 77) and the effects of laws against them (sub. DR176, p. 8).

Moreover, the indirect evidence suggests problems may not be as significant as some suggest. Most business proprietors are people with ethical and moral beliefs — with 97 per cent of business traders reporting this as the most important constraint on adverse treatment of consumers, rather than regulatory or competitive factors (OESR 2006).

Box D.4 Instances where 'unfair' terms were exercised

Ms. A hired a car from a major national hire company, which she returned to the airport at the end of her rental period. It was not inspected at the time, but four weeks later the company claimed there was damage to the driver's door and debited Ms A's account by \$370. Ms A contested this, claiming there was no damage at the time of the return. The company indicated that the matter had been investigated and that under the terms and conditions of the contract they had the right to claim repair costs. Unable to proceed any further, Ms A paid the amount. (Consumers' Federation of Australia 2004)

Ms B enrolled in a fashion school, agreeing to pay \$23 900 in monthly instalments over 3 years for an advanced diploma course. After attending the course for the first semester, Ms B was forced to move interstate urgently to care for her parents who were unwell. The contract included a clause requiring continued payment of all instalments even if for any reason the student had to terminate the contract early. Although the school agreed to allow Ms B to defer her course temporarily and to study by correspondence, it would not allow her to cancel the contract, despite her urgent need to move interstate. The school referred the matter to debt collectors and Ms B was pursued for the outstanding sum of about \$19 500. (CFA 2004)

Ms C signed a 12-month contract with a fitness centre. After 4 months, Ms C moved house, and work pressures meant she was no longer able to attend the gym. She asked to cancel the contract, but the fitness centre refused, relying on a term in the contract that required her to pay the full amount of fees remaining for the 12-month term of the contract. (CFA 2004)

Based on attractive terms for frequent flying points, Mr D switched from one credit card supplier to another, paying an annual fee in advance. Half way through the contract period, the bank unilaterally halved the value of points earned for spending. On protest from Mr D, the bank drew attention to their unilateral capacity to change any terms and conditions of its points scheme (Polman 2004). Presumably, this change affected thousands of other customers.

E's electricity supply was interrupted for about four hours. When power was restored, his dishwasher made a buzzing noise and was later found to have malfunctioned. E made a claim to the electricity supplier for the \$1090 that it had cost to repair the dishwasher. Investigation showed that a mistake by the electricity supplier's contractors had probably caused the problem. The supplier rejected the claim because the connection contract excluded any liability. The Ombudsman was able to achieve a resolution despite the contract. (EWON 2006c, p. 21)

F's contract with an electricity provider was for 3 years. The provider wrote to F before the expiration of the term to advise that he had the choice of continuing with them, or changing to another supplier. F did not respond to this letter and the contract was extended under the unilateral contractual power of the supplier to rollover contracts without consent. The ombudsman was able to negotiate the waiving of a termination fee that would have applied to the new contract because the contract had been rolled over for 3 years, when the contract allowed only 12 months. (EWON 2006c, p. 15)

A couple hired a car for a holiday. When they picked the car up they weren't given the car they had booked, but were given a smaller and less powerful car. The hire company told them that the car they booked was unavailable and that the hire contract they had signed entitled the company to change the car if the type originally booked was unavailable. (SCLAJ 2006, p. 8)

G signed a contract with a pay television company, choosing to subscribe to several sport channels. After a few months, the company reduced the number of sport channels that G was subscribing to, and increased the number of comedy channels. When G complained about the change in his subscription, he was told that the contract he had signed allowed the company to unilaterally vary the service they provided to him. (SCLAJ 2006, p. 8)

David Cousins from CAV has observed that businesses often say that they are surprised by the unfair terms inserted into contracts by their lawyers, but would not act on them:

In many cases it has been our experience that particularly senior management are shocked when they see the sort of things that we have pointed out to them about what is in their contracts. Their contracts have often been written for them by lawyers who have written things in those contracts that businesses say to us they would never implement. We say "Why is it written down there if you would never use it?" We have pointed out the unfairness of what is written down there and it has not really been an issue at all for senior management to amend those contracts. A case in point was a meeting we had — and I will not mention the organisation — with the chief executive officer of the organisation around the table and it was exactly that experience of him saying 'That's ridiculous. We would never do that. Why is it there?' (Cousins 2006, p. 63)

Were this generally true, then getting rid of such terms may not be very costly for business. But equally, leaving rarely executed unfair terms in contracts could not then be very costly for consumers as a whole.

Moreover, as noted earlier, competition remains an important constraint in its own right. Reputation and the capacity to retain and attract customers are critical to the success of most firms.¹⁵ While the existence of unfair terms probably has little effect on business reputation, significant exploitation of unfair terms is likely to be damaging. Every instance of perceived unfairness cascades through a person's networks (and most consumers say that they are likely to tell others of their experiences).¹⁶ So, while it is often claimed that competitive processes do not eliminate the *existence* of unfair terms, there are powerful competitive forces restraining their *use*, especially for firms that rely heavily on reputation.

Even the assumption that competitive forces are impotent when dealing with the existence of terms is not altogether true, since collective action by consumers, without regulation, has led to some changes to unfair contract terms (box D.5).

Finally, it is apparent that most consumers trust businesses to act fairly or ethically, and this trust has tended to rise over time,¹⁷ notwithstanding the growing number of standard-form contracts signed by consumers that contain notionally unfair terms.

¹⁵ The threat of publicity is cited as a restraint on abuse by 79 per cent of traders while the loss of customers is cited by 86 per cent (OFT 2006).

¹⁶ A Victorian survey of consumer detriment suggested that 57 per cent of consumers would usually or always discuss unfair experiences with friends and acquaintances (CAV 2006a, p. 14).

¹⁷ For example, as shown by survey data from DCEP (2006) and the NSW Office of Fair Trading (sub. 73, p. 13).

(While standard-form contracts have been the dominant form of consumer contract for some time, the change is that consumers appear to be signing more contracts.)

Box D.5 Competitive pressures against unfair contracts

Software end-user licence agreements may sometimes contain unfair terms, such as forbidding publication of comparative tests of the performance of the software; bars on any reverse engineering even if such reverse engineering is allowed by statute; giving the software company the right to spy on the consumer; and to transfer copyright material produced by users (Newitz 2005; Clapperton and Coronos 2007).

But consumer pressure — without regulation or legal action — appears to have led to a reduction in the use of such terms. For example:

- In 1999, after purchasing Geocities (a free website-hosting company), Yahoo changed the usage agreement so that all content on Geocities would belong exclusively to Yahoo. After a boycott and publicity campaign by Geocities users, Yahoo changed the terms and restored ownership of content to these users (Newitz 2005).
- It is now often routine for major software vendors to post their end user license agreements online so that would-be purchasers can look at them before buying the software.
- STOP BEFORE YOU CLICK is a project of Americans for Fair Electronic Commerce Transactions, a national coalition of retail and manufacturing businesses, consumer organisations, financial institutions, technology professionals and librarians committed to the growth of fair and competitive US markets in software and other digital products. They are attempting through consumer pressure and advocacy to change terms (<http://www.ucita.com/fairterms/Newfairterms.htm>).

There is some evidence that unfair contract terms are used

Nevertheless, evidence of the detrimental use of such terms is emerging. Since enacting provisions against unfair contracts, CAV has collected some information on the extent of complaints, which are precipitated by at least a perception of consumer detriment. About 300 of the 18 000 complaints that CAV receives each year were identified as relating to unfair terms in consumer contracts (SCLAJ 2006, p. 22). However, this was seen as a large underestimate of the numbers affected by unfair terms because only about 4 per cent of consumers take any type of complaint to CAV (usually either doing nothing, approaching the business concerned or trying other approaches — CAV 2006a, p. 9). This would suggest an underlying number of cases of perceived detriment associated with unfair contracts of around 7500 a year for Victoria and 30 000 for Australia.

Some of these consumer complaints are probably not valid, as suggested by the fact that a sizeable minority of complaints brought before various ombudsmen are resolved in favour of the businesses concerned. That said, an inherently unfair contract may still detrimentally affect consumers without them being aware of this — they may simply comply with any conditions as they change over time, without recognising that they are bearing the consequences of unilateral decision making by the businesses concerned.

The survey of consumer detriment commissioned by CAV (CAV 2006a, IPSOS 2006) can also be used to produce an estimate of the incidence of unfair contracts that produce detriment. The survey found that the combined category of ‘unfair and misunderstood’ contracts accounted for just two and a half per cent of total instances of detriment experienced by consumers. However, the inferred incidence was still nearly 200 000 cases a year for Victoria, suggesting around 750 000 cases a year in Australia, or about five cases per 100 adults (table D.1). This is very much higher than the estimate derived above using the active complaints data. Recent survey data from CAV (2007b) suggest an even higher incidence, with 17 per cent of consumers encountering unfair contract terms (chapter 7).

The international evidence, while inconclusive and limited, also provides estimates more akin to a 5 per cent incidence rate:

- A UK survey of consumer detriment in 1999 found that consumers in that country suffered 86 million cases of detriment annually, of which 3.8 per cent related to ‘misunderstood and unfair terms’. This amounts to around seven cases per 100 adult consumers.
- Around 24 000 people complain annually in the UK to the Trading Standard Services about unfair terms (National Audit Office UK 2003, p. 32). Adjusted for the adult population differences between the UK and Victoria, this amounts to 2000 a year, about seven times more than the 300 annually noted by CAV. It does not appear likely that the difference reflects variations in the commercial practices in the two countries.
- A South African national survey (Department of Trade and Industry South Africa 2003), found four per cent of consumers claimed to have experienced problems from ‘unfair’ contract terms. However, some of these cases proved to be spurious and around one third were resolved through negotiation with the supplier. The real implied incidence rate of exploited unfair contract terms would therefore appear to have been about three per cent.

Table D.1 **Unfair and misunderstood contract terms^a**

Victoria 2006

<i>Category of consumer detriment</i>	<i>Share of complaints involving unfair or misunderstood terms</i>	<i>Implied cases involving unfair or misunderstood terms</i>
	%	No ('000)
Food and drink	1	12
Private & public transport (incl. repairs/fuel)	1	8
Other professional or personal services	3	7
Utilities	5	59
Building/ renovation/repairs	6	26
Credit, debt, banking & other financial services	7	43
Tenancy and accommodation	9	18
Buying, selling or letting a home	9	10
Total	2.4	183
People complaining about 'unfair terms' (%)	4.5	..

^a These are 'Misunderstood contract terms or conditions; or unfair terms and conditions in contracts or one-sided contracts that allow the provider of the goods or services to opt out or change the price, quality etc'. Respondents reported no perceived cases of detriment for some types of transactions — for example, electronics and electrical. These are omitted from the table, but the zero counts almost certainly reflect the small size of the sample.

Source: IPSOS 2006.

The extent of detriment is even harder to pin down

Understanding the extent of detriment is complicated by many factors, not least the same data problems that beset estimates of the incidence in the use of unfair terms.

Much of the case study evidence relates to instances where individual consumers suffer a relatively modest detriment. However, this is a poor guide to the overall effects of unfair contracts, since often the unfair contract terms concerned may affect many hundreds of thousands of consumers. In that case, the potential aggregate detriment may still be significant. For example, the National Audit Office (1999) review of UK unfair contracts laws found a combined £125-£145 million annual gain to consumers from changes to the contracts of eight mobile phone companies and one mortgage business — gains that would have been distributed to hundreds of thousands of customers.

Moreover, the nuisance and emotional costs of the exploitation of unfair contracts may well exceed the direct pecuniary costs for consumers. For example, in *Dai v Telstra Corporation 2000*, the contested value was less than \$100 but the consumer still went to court to seek redress. Other instances, ostensibly involving trivial instances of perceived unfairness have been taken to court by consumers,

suggesting that they may place a high value on achieving just outcomes. Even people not directly affected by a particular instance of unfairness may deplore an unresolved case of injustice. Recent research by CAV (2007b) suggests significant emotional detriments (box 7.3 in chapter 7).

However, the likely benefits of regulatory provisions against unfair terms are not equal to the apparent gross detriment from the use of such terms:

- As noted above, the monetary losses falling on consumers from exploitation of terms will tend to overestimate the ultimate losses to consumers as a group because upfront prices will tend to rise, or some other feature of the product changed, when unfair terms are barred.
- Regulations will never be able to eliminate all of the detriment associated with use of unfair terms. It is notable that complaint rates on unfair contracts in the UK continued to rise for several years after the law governing such contracts was introduced (National Audit Office 2003). While this may partly indicate growing awareness by consumers of their rights, it shows, if nothing else, that the problem has persisted after the application of regulation.

Implications of the evidence

Unfair terms appear to be commonplace in standard-form contracts. To the extent that the existence of unfair terms of itself breaches ethical standards (section D.4), this evidence provides a basis for government action. Pragmatic considerations might also sometimes suggest action against the existence to terms. But, unlike the example of racial discrimination given above, most cited instances of unfair contracts are less obviously egregious, especially since, as discussed later, there can sometimes be valid reasons for their one-sided nature. In that case, the moral judgment of unfairness, stripped of context, is harder to make.

The most important evidential burden relates to the use of contract terms in ways that are detrimental to consumers as a whole. Here the evidence is rather better than described in the most recent inquiry into unfair terms (SCLAJ 2006), but it is still hard, given the inadequacies of the existing information, to know with any precision how much business exploits unfair contracts and with what costs for consumers.

Information deficiencies have been a major hurdle in introducing national legislation (Baker in SCLAJ 2006, p. 3). Under the principles and guidelines set out by the Council of Australian Governments, such regulations must be justified by a Regulatory Impact Statement (RIS). This statement is assessed by the Office of Best Practice Regulation (formerly the Office of Regulation Review), a body now attached to the Department of Finance. Among other requirements, a RIS must

show there is sufficient evidence for the regulatory change envisaged. Past statements submitted for a national law against unfair contract terms based on the Victorian unfair contracts legislation have not met this requirement, which has been pivotal in rejections of the proposed policy change.

Changes to the coding of complaints received by the fair trading offices (Baker in SCLAJ 2006, p. 3) would be useful to help uncover such evidence, as would carefully designed surveys of consumers. There are strong grounds for research and data collection of this kind (chapter 11). Notably, CAV has recently completed detailed survey work to discover more about the incidence, nature and extent of problems associated with unfair contract terms (CAV 2007b). Nevertheless, even with additional information on gross detriments experienced by consumers, it is still likely that it will be difficult to reach a precise estimate of the net benefits of action.

Of course, this need not preclude action. As the Victorian Government noted, there are also significant problems in quantifying the net benefits of prohibitions against false, misleading, deceptive or unconscionable conduct, yet these prohibitions are now widely accepted as being in the public interest (sub. DR226, p. 59).

Where it is difficult to gather *ex ante* evidence in cases where there could be a legitimate problem of unfair terms — a genuine possibility — policymakers need to consider this in regulatory assessment and design. Faced with such uncertainty, a sensible approach may be to appraise the likely costs associated with the introduction of a law against unfair contracts. If these are low, then the indeterminacy of benefits associated with the introduction of a new measure is less likely to be a major concern (ACCC, sub. 80, p. 78). Using this sort of assessment criterion avoids the mechanical rejection of the possibility of intervention because of uncertainties about the magnitude of the problem.

However, as the ACCC notes, some variants of unfair contract provisions may in fact give rise to significant costs. This suggests there should be a major focus on the design of any proposed measure to ensure that it reduces such risks and is only applied in appropriate circumstances. By definition, a well targeted regulation is likely to pass a cost-benefit test — thus meeting this essential RIS requirement. The regulatory options that may achieve this are canvassed in chapter 7.

D.6 Other benefits?

The benefits of policy described above are based on reducing the incidence of unfair terms and their detrimental use. These benefits are probably relatively modest. However, some of the incidental benefits of policy change may be more significant.

These benefits stem from reducing the problems associated with existing fragmented and costly policy responses to unfair contract terms.

Unconscionability provisions in the TPA (and FTAs) are not ideal for standard-form consumer contracts

As noted in section D.3, s. 51AA and 51AB of the TPA already provide the capacity to act, in some circumstances, against the use of unfair contract terms. However, these sections are time consuming to apply, are expensive and are shrouded in uncertainties over their appropriate application.

The ambit of s. 51AA and 51AB may be changing to embrace a more liberal notion of the appropriate threshold of unreasonableness or unfairness in contracting. In one sense, that potential change is desirable, reflecting through jurisprudence, changed community expectations about the right threshold. Nevertheless, it further raises the uncertainty about the scope of s. 51AA and 51AB. Uncertainty about the application of unconscionability can be potentially costly for businesses (and therefore consumers). An illustration of this is *Commercial Bank of Australia v Amadio* (under s. 51AA). Mcconville and Bagaric (2002) argue that this single case prompted:

... a wholesale change in banking practice concerning the provision of guarantees. It is now standard practice across Australia that virtually every person who signs a guarantee where a bank is a party must first obtain independent legal advice. This is so, irrespective of the level of financial and business acumen possessed by the prospective guarantor. Thus, the upshot of *Amadio* is that ... lawyers got a new income stream ... and the community has paid tens of millions of dollars to lawyers for independent legal advice. The reason the banks insist on independent advice, and have not confined *Amadio* to its facts, is simple: they have no confidence that the notion of unconscionability will be confined to facts similar to those in the case.

One solution might be to change aspects of s. 51AA, 51AB and 51AC to promote greater certainty (as suggested by Frank Zumbo, sub. DR217, pp. 4ff). But, while there may be broader grounds for re-considering the scope of these provisions, changing the interpretation of the provision to clarify its use for unfair contract terms may affect its use in many other commercial contexts, with potential risks that it may become an excessively intrusive instrument. An alternative, more targeted, approach would be to devise a new section in the generic consumer law that deals with the detrimental use of unfair contract terms alone. This could both resolve the present uncertainty about the application of s. 51AA, 51AB and 51AC by giving more statutory guidance, and provide for a cheaper, quicker recourse appropriate to the small-scale problems typically occasioned by standard-form consumer contracts.

Achieving greater harmonisation is a worthwhile goal

The status quo is one in which regulations and codes concerning unfair contract already exist, and where there is a strong possibility of further development of new models across Australian jurisdictions and New Zealand. Some of those might have features adverse to efficiency, business compliance burdens or equity. The dangers of fragmented approaches have been a theme of several firms making submissions on unfair terms to the various inquiries into them. For example, in this inquiry, Telstra noted

... that it would be beneficial for consumers to be protected by a single national regime relating to unfair terms in consumer contracts, to avoid duplication and the inefficiencies associated with administering and complying with multiple regimes and ensure a level playing field for all participants. (sub. 35, p. 23)

A well-designed national and uniform approach to unfair contracts that avoids a breakout of potentially conflicting regulations would contribute to the broad goal of achieving a much greater degree of uniformity in Australian consumer policy laws.

International convergence

Globally, there appears to be a trend towards removing unfair terms from standard-form contracts. A national law may therefore make it easier to trade — especially through direct to consumer sales overseas. US firms, for example, are facing frictions in engaging in European markets through the Internet unless they alter their standard-form contracts in accordance with European fair contract directives (Winn and Webber 2006). A single Australian national law would make it easier to respond effectively to future international consumer law changes in this area.

D.7 The costs

Regulation imposes costs — direct ones on regulators and businesses, but also potentially indirect and unanticipated ones that arise from distorting incentives.

Administrative costs

Policing of unfair contracts requires regulatory resources, including time used in the justice system when testing cases. Based on the experience in policing the UK and Victorian unfair contracts legislation,¹⁸ the Commission estimates that an Australia-

¹⁸ CAV indicated that the additional resourcing costs for applying Victoria's unfair contract provision have been between 2 and 3½ staff (pers. communication, 15 August 2007). 32 staff

wide law would entail an ongoing incremental¹⁹ resource commitment by consumer regulators of about 8 to 14 full-time equivalent staff with an annual cost of about \$1 to \$1.5 million.

It is harder to estimate costs of any litigation since the intent of such regulation is to deter the use (and existence) of unfair contract terms through ex ante action or/and the threat of ex post action when unfair terms are used against consumers (chapter 7). Notably, only two cases have been contested in the justice system in Victoria. Indeed, it is conceivable that deflection of cases away from s. 51AA, 51AB and 51AC — an expensive form of recourse — might actually save litigation costs.

Compliance burdens

Some businesses would have to revise their contracts after the introduction of a new law against unfair terms. This would impose compliance costs on them (and through prices, ultimately on consumers). These costs would mainly reflect the one-off expenses of re-drafting and any re-printing of contracts. The Commission consulted with several firms affected by Victoria's unfair contracts laws. One finding from this was that it can take some time for businesses to negotiate changes to unfair terms acceptable to the regulator. This appears to reflect:

- staff turnover in the regulator, so that successful negotiations made by a business with one staff member may have to be re-commenced if that person leaves — leading to slow resolution of problems;
- a reluctance by the regulator's lawyers to sign-off a contract as 'fair'; and
- unclear authority within the regulator to give a final sign-off.

Overall, however, the Commission's consultations suggested that for large companies the costs of negotiating and changing contracts have been negligible relative to their turnover. For example, the one-off costs were about \$30 000 for one large business — which, with a discount rate of 6 per cent, is the equivalent of a perpetual annual cost of about \$2000. The costs relative to turnover may be more appreciable for smaller businesses since there is a fixed cost associated with any

were employed in the UK to deal with unfair contract issues (Edwards 2003). This included 23 case officers, a support team and senior staff. Substantial input from the legal department was also required given the links with other consumer protection legislation. The Australian estimates were derived from these staff numbers and the relative adult populations in Victoria, the UK and Australia.

¹⁹ Noting that regulators must currently address some complaints about unfair contract terms, even though there is no specific legislation, other than in Victoria, for dealing with them.

negotiation or change of contracts, but this would be ameliorated to the extent that they copy their contracts from larger businesses or industry associations.

Estimates of the compliance costs of the UK's adoption of the broader European unfair commercial practices directive can, when appropriately scaled, be used to provide another rough measure of the compliance costs that might be involved for Australia from implementing an unfair contracts law. These UK estimates suggest business compliance burdens for Australia of somewhere between \$12 million and \$30 million.²⁰ Most of these would be one-off costs, which suggests an equivalent perpetual cost of less than \$2 million per year at a 6 per cent discount rate.

Overall, while it is hard to enumerate the compliance costs that would result from the introduction of an unfair contracts law, they are likely to be small.

The risks of government failure

Regulations that are otherwise well conceived may still fail because of 'government failure'. Governments design and administer regulations without the constraints of markets to encourage convergence to efficient solutions.

Over-prescriptive regulation?

One obvious risk entailed by a general provision in the generic consumer law aimed at unfair contracts is that it may be over-prescriptive in trying to define the fairness of contracts. As an illustration of the difficulties of prescribing fairness, the Victorian unfair contracts law includes a requirement for clarity so that consumers can readily see and understand the contracts to which they are agreeing. However, in addition to having a general requirement for legibility, the legislation prescribes some criteria for clarity, such as a minimum 10 point font size (s. 163 (3)). As noted and illustrated by the SCOCA discussion paper (2004), this ignores the fact that the size of fonts of given points can vary significantly:

This is 10 points (Times New Roman)

This is 9 points (Arial)

This is 9 points (Wide Latin)

²⁰ The UK Department for Business, Enterprise and Regulatory Reform (2006 p. 12, p. 17) produced a regulatory impact statement for the directive. It estimated (mainly upfront) compliance costs of around £15-£35 per business for roughly one million businesses. This compared with the more significant assessed *ongoing* benefits of around £100 million each year.

Most people would regard 10 points Times New Roman as legible, yet Arial and Wide Latin, though equally legible at 9 points, would be outlawed by s. 163(3). This example of apparent prescriptive failure is trivial and easily remedied, but it does illustrate some of the design problems entailed by regulations of this kind.

Regulatory overreach?

Laws against unfair contract terms cannot define ‘unfairness’ precisely because it is such an inherently subjective concept. Depending on enforcement and jurisprudence, the unclear boundaries of unfairness may potentially lead to regulatory overreach. Hard bargaining between negotiating parties sometimes results in a lopsided distribution of benefits that is usually regarded as part of the contractual process and not inherently unfair. Simply because negotiation is absent is probably not enough to argue that a similarly lopsided outcome is unfair in standard-form contracts either. Some prospect of consumer detriment would be required. Ultimately, regulators must make fine judgments, some of which may be suspect.

For example, in France a regulator held that in 2006 an Internet service provider acted unfairly (in its nomenclature, ‘abusively and illicitly’) by, among other things, insisting that accounts must be paid online.²¹ That is not obviously unfair, since it could be reasonably supposed that customers could pay online for an online service. Moreover, an online payment option is likely to be more cost-effective than alternatives, with the benefits being passed on to customers.

In practice, the definitional issues do not appear to have given rise to major problems in the application of either the Victorian legislation or UK provisions to date. It is notable that the term ‘good faith’, which is sometimes seen as unclear, has been clarified by the Victorian Civil and Administrative Tribunal in Victoria and in NSW contracts law (chapter 7 and Frank Zumbo, sub. DR217). More generally, appeal processes and accumulating jurisprudence help to add clarity about the scope of the legislation for the justice system and regulators.

‘Unfair’ terms might sometimes be beneficial for consumers as a whole

A bigger risk of unintended effects stems from the fact that apparently unfair terms may have efficiency or equity benefits that might be lost if these terms are proscribed. To understand why these effects may occur, there are two important linked questions that should be answered:

²¹ www.discourse.net/archives/2006/02/french_isps_found_to_violate_french_consumer_protection_law.html.

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- Why do firms employ apparently unfair contracts?
 - What would happen if notionally unfair contracts were barred?

One of the most important reasons for apparently unfair terms is that it is costly for firms to pre-specify all of the contingencies in which it may be efficient for them to vary their general contractual obligations. As a result, they tend to use rather general ‘escape’ clauses that allow them to deny service or vary terms without the circumstances for this being spelled out. Such contracts can more readily be copied across many businesses in similar industries, reducing costs further.

As noted in section D.4, unfair behaviour is not isolated to businesses. Consumers too can act in bad faith or otherwise inappropriately. They may be careless in using their purchases and lie about damage they have done to a rented asset. They may delay payment for services provided. They may seek loopholes in a deal with a supplier to get services or goods below cost. They may vexatiously seek unreasonable compensation for suspensions of service that are an inevitable part of everyday supply relations and that would be excessively costly for a supplier to avoid. And crucially, unlike businesses, consumers do not have a brand name or reputation to lose. If a consumer acts in bad faith with one seller, another seller would rarely know this.

Therefore, one-sided contracts may actually better protect the bulk of customers from the problematic behaviour of the few than balanced contracts (Bebchuk and Posner 2006; Johnston 2005; and Gillette 2004). In that case, apparently one-sided contracts may not in fact be one-sided at all. The bulk of consumers can be sure that their implicit contract will mostly be honoured, and indeed, sometimes exceeded, while those who behave in bad faith know that the supplier will use it to act against them. Removing the protections that contracts have against such consumers will have consequences for other terms and conditions, including prices, with flow on effects for the bulk of consumers. As Professor Chris Field noted:

Unfair contract terms laws have the potential to interfere with the complex balance of the contractual bargain – the deletion of one term as unfair may see another term, which the consumer values, affected adversely. What may seem on its face attractive – the protection of powerless consumers from the excessive power of business – may in fact upset the complex balance of the contractual bargain in ways that are harmful to consumers. (sub. 102, p. 5)

Another point to note is that many business-to-consumer contracts are really arrangements in which consumers deal with each other through a business intermediary. For example, financial suppliers act as intermediaries between consumers who want to lend and those who want to borrow. Regulated terms and conditions that apparently favour borrowers as a class have repercussions for consumer lenders (and vice versa). In some emerging services, such as online

auctions, the links between trading consumers are even more transparent. In these arrangements, the auctioneer provides ‘auction services’ to a consumer who wants to sell something.²² Regulatory requirements that the auctioneer must act ‘fairly’ with a consumer who signs on as a seller can unfairly disadvantage another consumer who signs on as a buyer. In this context, the business (the auctioneer) is a veil that separates one group of consumers from another. Altering the balance of power through fairness provisions may shift, rather than eliminate, unfairness.

The best test of these possible effects is the difference between the impacts under the present arrangements and the possible outcomes under the counterfactual case with a particular unfair contract provision in place.

One illustration of this principle at work is an educational institution that requires an upfront, non-reimbursable fee or continued instalments regardless of whether a student completes the course or not — the apparently unfair case described in box D.4. Where the reasons for incompleteness are not in the control of the student, this seems unfair. However, there are large fixed costs in running courses. Once committed to running a course, a room is booked and a teacher hired. Were an unfair contract provision to strike out the capacity for a supplier to secure the payment, early termination could mean the supplier makes a loss on a marginal, more specialised, course. The knowledge that a student has the right to terminate early without making up the losses that this imposes, would mean that prices would rise and some courses would not even be offered, to the cost of students wanting to take them. This could be both an inefficient and, in its own right, an unfair outcome. Some similar arguments could apply to certain mobile phone contracts.

Likewise, pre-commitment contracts can serve the interests of the consumers they bind. For instance, a pre-commitment to pay for a fitness centre over a 12 month period can help a consumer to commit to an exercise regime, because the marginal cost of entry over the next 12 months will be zero. Were a person able to terminate such a contract at any time with a low penalty, then it would effectively destroy the capacity for pre-commitment, undermining the incentives for exercise that the consumer originally wanted. (Of course, a contract that serves such a pre-commitment purpose should make it clear that early termination fees are high. Failure to do so is not compatible with the uptake of such contracts as pre-commitment devices.)

²² The TPA defines ‘consumers’ of services broadly — s. 4B (1)(b) of part 1 — to include, among other things, any person who buys a service valued under \$40 000, which would include the small fees paid to online auctioneers for selling goods and services.

Can the costs of an unfair contract provision be reduced?

The above pitfalls and costs of an unfair contracts provision provide insights into the dangers of certain forms of regulation. But some of the worst risks are hypothetical. Others reflect factors that policymakers could ameliorate through better design.

First, regulatory provisions could give firms the scope to re-design their contract terms to achieve the legitimate business goals of the original contracts, while eliminating the potential for unfair application. For instance, an unfair contract provision need not remove the capacity for mobile phone companies to charge for any unrecovered costs associated with a subsidised handset, or to deal with the administrative and network costs of termination. It could similarly allow an educational business to recover the full expenses pre-committed to a student's tuition, if that student were to leave early. Rather, an unfair contracts provision would be aimed at removing the capacity for companies to charge above these levels.²³ This appears to be the way that regulators have usually applied the provisions in the UK and Victoria, and is in keeping with the guidelines issued by CAV (2003).

If regulators use this approach, any consumers acting in bad faith would have little to gain from vexatious litigation or its threat. The biggest issue would be regulatory error about what might constitute an appropriate fair term. The likelihood of such errors depends on whether regulators listen to business concerns and adopt a benefit-cost approach when suggesting contract term changes. It is these procedural aspects of regulation, more than the regulation per se, that will have the biggest bearing on the incentive risks posed by a move to a national unfair contracts statute.

Second, some regulatory models are less likely to raise business compliance burdens and other risks, and some could actually lower them:

- A law focused on unfair terms causing material consumer detriment would target the most significant problems, reducing regulatory risks.
- Guidance to industry about unfair terms could provide some certainty for business. Such guidance could include black lists of offending terms (the Victorian approach); grey lists of indicative terms (the UK approach); and/or the development of model industry codes (ACCC, sub. DR176, p. 8).
- Enforcement targeted at high-grade or commonly used unfair terms may mitigate regulatory administrative costs and compliance costs for small enterprises. For

²³ There is evidence that some firms have charged above such levels when not constrained by regulation (ANZEWON, sub. 64).

example, the UK regulator reduced compliance costs for business by focusing enforcement on only particularly problematic instances of unfair terms (Edwards 2003).

- Allowing time for suppliers to change terms would reduce costs, as would the fact that they are able to now learn from the Victorian and UK experiences about what are acceptable terms (ACCC, sub. DR176, p. 9). Indeed, some national suppliers have already changed their Australia-wide terms because of the Victorian laws, suggesting that the compliance costs of a national approach are likely to be less than if no prior Australian regulations were in place.
- For the reasons outlined earlier, a national model could lower regulatory compliance costs associated with cross-border trade within Australia and overseas.

Overall costs

Aside from uncertainty about the gains from policy action, the concerns over the potential for unintended effects, and the additional resources required to manage and police any unfair contract provisions, constitute the major basis for the conservative policy option of doing nothing. However, there is little evidence so far that these problems are anything other than modest. The Victorian experience suggests minor effects:

Our experience is, and I guess we can only go on what business feeds back to us, is that there have not been major costs on business. In fact, the reality has been that business does from time to time review and change contracts. And the process of taking account of the Victorian legislation in many cases has actually just been absorbed as part of the normal process of change and reviewing contracts. (David Cousins 2006).

There were very few submissions made by business to the past SCOCA (2004) and SCLAJ (2006) inquiries into unfair contracts legislation that raised significant concerns about such legislation, and this has applied in this inquiry too. The fact that those businesses that have changed their contracts because of Victoria's legislation have generally modified them for all Australian jurisdictions, suggests that any commercial disadvantages of the contract changes cannot have been significant. Moreover, the Commission's discussions abroad with the major representative industry groups, the Confederation of British Industry and Euro Commerce, suggest little discomfort with the provisions that have been operating for some time now in the UK and Europe. This is likely to reflect that regulators have implemented the policy in cooperation with industry, and that firms have been able to retain the capacity to deal with business risks.

D.8 Summing up

It is hard to estimate accurately the benefits and costs of introducing an unfair contracts provision. The likelihood is that less is at stake for consumers than some suggest, simply because most firms honour the implicit contracts they strike with their customers anyway. Equally, the experiences in Victoria and abroad suggest implementation of unfair contracts laws has not been a problem for business.

Some approaches will probably have bigger potential net benefits than others — with those benefits depending on the extent to which they provide safeguards against regulatory error and ensure that the regulator listens to business (chapter 7).

E Credit regulation

Key points

- Financial sector reform has put downward pressure on the cost of credit, facilitated innovations in the range and types of credit available, and contributed to growing use of intermediaries to help consumers make complex financial purchasing decisions.
- For most consumers, the greater availability and use of credit has been both beneficial and manageable. However, for a small proportion, the consequences have been detrimental.
 - Poor lending practices have contributed to a growing number of borrowers experiencing financial stress.
- The largely state-based regime for regulating the provision of consumer credit has various deficiencies, including gaps in coverage, variations in requirements across jurisdictions, and a lack of responsiveness to rapidly changing credit markets.
- Shifting responsibility for regulating consumer credit to the Australian Government, as recommended by the Commission (see chapter 5 of the report), should provide improved, nationally consistent protection to those acquiring credit products or seeking advice on them.
- However, a range of issues will arise in developing that national regime, and in making related changes to financial services regulation, including:
 - the precise nature of the requirements for licensing finance brokers, and for licensing or registering credit providers;
 - what modifications should be made to the requirements in the Uniform Consumer Credit Code in the light of work currently in train to improve it;
 - whether the new national regime should include interest rate caps;
 - whether the service coverage of the current arrangements should be widened; and
 - what, if any, initiatives are required to promote 'responsible lending'.

E.1 Introduction

The supply of consumer credit and provision of related advice in Australia is an important part of the economy. In 2006-07 Australian consumers borrowed over \$200 billion (ABS 2007b), with access to that credit providing correspondingly large benefits overall. Mostly, credit is used by consumers to finance home

mortgages, but it is also used for short-to-medium term purchases, such as cars or overseas holidays, and as a financing mechanism for more frequent credit card purchases.¹

This appendix, looking at the current regulatory regime for consumer credit and some issues bearing upon future requirements, provides a backdrop for discussions in various parts of the body of the report on credit related matters. These include: the case for transferring regulatory responsibility for consumer credit and related advice to the Australian Government and some features that this national regime should embody (chapter 5); dispute resolution processes and financial counselling (chapter 9); the disclosure of information about financial services and products (chapter 11); and some particular issues facing vulnerable and disadvantaged consumers in credit markets (chapter 12).

What has been happening in credit markets?

The use of credit has increased substantially over the last twenty years — the real value of consumer loans has grown at an annualised rate of 5 per cent since 1988. This reflects a combination of factors, including that:

- at least until very recently, credit has been cheaper and more accessible for many consumers; and
- average household incomes have been growing, hence increasing consumers' borrowing capacity.

Financial market deregulation has also played a key underlying role. It has facilitated the dramatic increase in the number of credit providers and competition amongst them in the market. In turn, this has put downward pressure on the cost of credit and encouraged innovation in loan products — including new and lower cost financing mechanisms and changes to approval criteria to cater for a wider variety of consumer needs.

While household debt levels are now at historically high levels, for most consumers, the greater availability and use of credit has been both beneficial and manageable.

However, concerns have emerged at two levels.

- Some have questioned whether aggregate debt levels are sustainable, notwithstanding that much of the recent growth in debt reflects increased house

¹ In 2006-07, home mortgages accounted for some 60 per cent of the total value of new consumer loans (ABS 2007b). However, a portion of these mortgage loans would have been used for non-housing related purchases.

prices and hence is backed by a higher asset base. Heightening such concerns have been the flow-ons from recent developments in the US sub-prime mortgage market, which have seen a tightening in access to credit and a reduction in its affordability globally (box E.1).

Box E.1 **Sub-prime lending**

Sub-prime lending commonly refers to loans made to borrowers who would not typically satisfy the criteria of mainstream lenders. In Australia, these loans are often referred to as non-conforming loans.

The consequences of the recent upheavals in the sub-prime market in the USA are still playing out in global credit markets. However, it is important to recognise that there are some significant differences between the US sub-prime market and the comparable component of the market in Australia.

- In the USA, sub-prime loans account for about 15 per cent of the mortgage market, compared to only around 1 per cent in Australia (according to the definition used by the Reserve Bank of Australia (RBA)).
- The loan-to-valuation ratio of a sub-prime loan in the USA has been around 95 per cent, compared to around 75 per cent on newly approved non-conforming loans in Australia.
- Initial 'teaser' rates, which have been a common feature of sub-prime mortgages in the USA, are less prevalent in Australia (with 'honeymoon rates' sometimes offered, but at discounts far less than those that have been offered in the USA). The RBA (2007b) reported that it was not uncommon for the repayments on some adjustable rate mortgages in the USA to rise by 50 per cent following the expiration of the introductory interest rate period.
- The proportion of all mortgages on-sold to investors (securitised) has been much higher in the USA than in Australia, and with the majority of mortgages in Australia remaining on lenders' balance sheets, Australian lenders' underwriting standards have also tended to be tighter.

According to the RBA (2007b), since sub-prime loans in Australia are a small proportion of the mortgage market, the likelihood of a similar crisis emerging in Australia is low.

Some inquiry participants contended that the RBA uses a narrowly construed definition of the sub-prime mortgage market, and that the sub-prime component may in fact represent close to 5 per cent of the overall mortgage market. (See, for example, the Joint Consumer Groups, sub. DR228, p. 40.)

That said, these participants acknowledged that uncertainty surrounds any estimate in this area. More importantly, as discussed in the text, while regulations governing the provision of credit should provide appropriate protection to consumers against poor lending practices and assist them to make good decisions, their purpose is not to address any concerns about the systemic sustainability of *overall levels* of sub-prime lending.

- More specifically, some contend that higher debt levels are partly the result of poor lending practices, leading to a greater incidence of financial stress for

consumers. Commenting on the effects on consumers of the growth in mortgage debt, David Tennant stated that:

It has forced unhealthy changes in the mainstream market, and according to the evidence of foreclosure activity around the country, is closely linked with significant increases in the incidence of people losing their houses and facing personal financial ruin. (trans., p. 296)

Implications for this inquiry

The primary role of consumer policy in the financial services area is to protect individual consumers, rather than influence aggregate lending activity. To the extent that higher debt levels pose risks to the stability of the financial system and wider economy, other policy tools, such as monetary policy and prudential requirements, will generally provide for a more effective response. To this end, the Council of Financial Regulators monitors potential threats to financial stability and coordinates responses by its members — the Australian Prudential Regulation Authority, the Australian Securities and Investments Commission (ASIC), the RBA and the Australian Treasury. For example, the RBA continues to monitor developments in the pattern of financing loans.

It is also important to recognise that increases in financial stress associated with higher debt levels are not a sufficient reason for additional regulation of lending behaviour and practices. The costs of such regulation for the majority of consumers who are not suffering financial stress must also be considered, especially given that there are other non-regulatory options for assisting those experiencing difficulty in meeting repayments (see further discussion in section E.3).

Equally, it is important that the regulations governing the provision of credit should provide appropriate protection to consumers against poor lending practices and assist them to make good decisions. Hence, though increased levels of financial stress do not of themselves signal the need for more regulation, the rapid changes in financial markets which have contributed to this outcome may well mean that modifications or augmentations to the regulatory regime are warranted.

E.2 How is consumer credit regulated?

Responsibility for regulating consumer credit lies primarily with State and Territory governments. The Uniform Consumer Credit Code (UCCC) is the overarching piece of legislation in the regulatory framework. It focuses on truth in lending through detailed disclosure requirements that aim to inform consumers about the terms of a credit contract prior to purchase (box E.2). This is principally achieved by requiring a

summary table at the front of a credit contract, including information on the amount of credit to be provided, details of the annual interest charge, and any fees and charges payable. As such, the disclosure requirements in the UCCC are much more prescriptive than those in the financial services regulatory regime administered by ASIC.

Box E.2 The Uniform Consumer Credit Code

The Code defines consumer credit to be that provided for personal, domestic or household purposes. It developed from a national initiative to standardise credit practice in Australia. Ensuring truth in lending is a cornerstone of the Code and is targeted through a detailed set of disclosure requirements outlining the costs of credit. The Code also regulates a number of other issues, including provisions covering:

- unjust terms that are unconscionable, harsh or oppressive;
- unilateral variation of contract terms;
- a mandatory 'comparison rate' for fixed term loans;
- disclosure of, and restrictions on, property that is mortgaged or given as security; and
- credit linked directly to a sale or the provision of insurance in relation to a credit contract or consumer lease.

Responsibility for enforcing the Code falls on the relevant State and Territory Fair Trading Authority or to consumers themselves through court action. Regulators do not have the power to bring actions on behalf of consumers, but can impose civil penalties. Most enforcement has concentrated on penalising providers for breaches of the disclosure requirements.

The Australian Uniform Credit Laws Agreement 1993 supports the consistent administration and enforcement of the Code across jurisdictions, with responsibility for ensuring this vested in the Uniform Consumer Credit Code Management Committee.

While national reviews have broadly endorsed the Code's approach, a number of changes have been suggested, including:

- the simplification of disclosure requirements;
- the closing of some gaps in the Code (bills of exchange, payday lending); and
- the introduction of uniform regulation of intermediaries providing advice on the relative merits of different credit products.

While there has been agreement on some changes to the Code, many amendments to it have been slow to progress (see text).

The UCCC also deals with a number of other matters, including provision to vary the terms of contract or postpone payments on hardship grounds. These hardship

provisions further differentiate the UCCC from the financial services regime which contains no such measures.

There are also various separate pieces of State and Territory credit regulation. For example, three States have introduced caps on interest rates and Western Australia has a licensing regime for credit providers and intermediaries that advise borrowers on the merits of competing credit products (finance brokers).

Responsibility for enforcing the Code and any separate credit regulation lies with State and Territory Fair Trading Authorities. As well, consumers can seek redress through tribunals and the courts for breaches of the Code.

The Australian Government also has an influence over the regulation of consumer credit through the financial services regulatory regime administered by ASIC. In particular, this requires credit providers to comply with provisions mirroring the consumer protection sections of the Trade Practices Act, and imposes licensing and disclosure requirements on financial service providers. Indeed, the bulk of consumer credit (by value) is supplied by financial entities that are subject to this broader regime². Moreover, as discussed below, CoAG has agreed in principle to the Australian Government assuming much greater regulatory responsibility in the consumer credit area.

Credit regulation is deficient in several respects

The range of credit products and services has been expanding rapidly. New products include, for example, non-conforming loans, equity release mortgages and margin loans. Further, many of these new forms of credit are provided by sectors that have traditionally been small lenders, or by non-deposit taking institutions (examples include the Bluestone Group and Liberty Financial) and solicitors or vendors (providing home financing). And more traditional lenders have also broadened their range of credit products. For example, all deposit taking institutions now offer low-doc loans, which require less stringent credit worthiness checks (Datamonitor 2007).

While these developments have been beneficial for many consumers — including for some who would not have been previously able to secure credit from mainstream providers — the Commission concurs with the widespread view of participants that credit-related consumer protection requirements have not kept pace with these market developments, or are otherwise deficient (box E.3).

² However, notwithstanding that a credit provider may belong to a corporate group which holds an Australian Financial Services License, ASIC cautioned that within the corporate structure, the provider itself may not be licensed (sub. DR174, p. 9).

Box E.3 The need to improve the current arrangements

Many inquiry participants contended that there is considerable scope for improvements to the current arrangements for regulating consumer credit:

... the current [credit] regime, while delivering some significant benefits, has arguably not performed as well as it could have. In particular, there are unresolved issues going to the scope and flexibility of the framework, including its applicability/adaptability to changing market circumstances and products. (ASIC, sub. 103, p. 46)

Several went on to emphasise that making necessary changes through existing inter-jurisdictional processes is difficult and time consuming:

Making amendments to the Code is a highly complex and lengthy process requiring a range of approvals at each stage of the policy development and implementation process. (Department of Employment and Consumer Protection (Western Australia), sub. 99, p. 26)

Moreover, a number of participants claimed that there has been insufficient enforcement of existing provisions, exacerbated by gaps in the Code:

There has been very little enforcement under the UCCC for any reason, including systemic avoidance. Whether this has been due to a lack of resources, other priorities, or a lack of clear powers is a question that would be better answered by the state regulators. The opportunity for avoidance, however, has been created by the narrow scope of the legislation and its various exceptions. (Consumer Credit Legal Centre, sub. 95, p. 69)

- There are gaps in coverage, with some products and services not adequately encompassed by either consumer credit or financial services regulation (see later).
- The level of protection afforded by the state-based regulatory arrangements partly depends on where those acquiring credit live. For instance, as mentioned above:
 - New South Wales, Victoria and the ACT impose (differing) caps on interest rates, with legislation to introduce a cap currently before the Queensland Parliament. South Australia and Western Australia have also signalled an intention to consider their introduction.
 - Western Australia has a positive licensing system for both credit providers and finance brokers; the ACT registers finance brokers; while all other jurisdictions (other than Tasmania which has no specific requirements) administer various forms of negative licensing schemes for credit providers only.

Also, the ACT has unilaterally introduced regulation under its Fair Trading Act, that requires a credit provider to assess a borrower's capacity to pay prior to increasing a credit card limit.

- Such unilateral regulatory requirements (despite the 1993 agreement to maintain a consistent, national approach), together with overlaps and inconsistencies between the regime for consumer credit and the financial services regime, impose additional compliance burdens on providers. This raises their costs and, in turn, the prices ultimately paid by consumers.

-
- As in many other consumer policy areas, the inter-jurisdictional processes (box E.4) for changing the UCCC and related regulatory arrangements have led to often long delays in implementing necessary reforms. Examples include the protracted time frames for developing national finance brokers regulation and for closing off some of the identified loopholes in the UCCC (section E.3). Such delays increase the likelihood that the effectiveness of consumer protection for those acquiring credit products and services will be compromised, especially given the rapidity of change in this market.

Box E.4 Delays in the policy making process

Changing the UCCC is a time consuming process. First, proposed policy changes must receive at least two-thirds majority support among the States and Territories and pass through the usual measures for inter-jurisdictional regulation (such as the preparation of a Regulatory Impact Statement). Then, the proposals must pass similar regulatory gate keeping mechanisms (such as Cabinet approval) in some States and Territories. Finally, legislation to make fully uniform, national change must be passed in Queensland, Western Australia and Tasmania. The Victorian Government (sub. 92, p. 136) said that the result is that 'on average, Code legislation projects tend to take around 3-5 years to come to fruition.'

There is little evidence that delays reflect disagreements amongst jurisdictions. Rather, as discussed in chapter 6, they seemingly reflect factors such as a lack of resources for policy development and frequent changes to those responsible for progressing particular reform initiatives. But whatever the cause of the delays, they are likely to be costly for consumers.

Major changes to the regulatory framework are in prospect

At its most recent meeting, CoAG (2008) agreed in principle to the Australian Government assuming responsibility for regulating the following credit and financial products and advisory services:

- mortgage credit and advice; including persons and corporations engaged in mortgage broking;
- margin lending; and
- lending by non-deposit taking institutions.

CoAG has also requested its Business Regulation and Competition Working Group (BRCWG) to identify any other financial services providers that best sit within the Australian Government's responsibility, citing as possible examples pay day lenders and 'fringe' credit providers. The BRCWG is to report back to CoAG by July and develop implementation plans by October of this year.

E.3 Issues bearing on the future regulatory regime

As discussed in chapter 5, a range of complex issues will have to be addressed by CoAG, in consultation with MCCA, in developing this new national regime, with the Commission having spelt out some key features that it should embody (see recommendation 5.2). The remainder of this appendix discusses a number of the underlying issues in more detail, as well as pointing to some other matters that may be relevant to the future configuration of the new regulatory requirements in this area.

National regulation of finance brokers

As alluded to above, the term ‘finance broker’ is used to capture intermediaries that provide advice on credit products. In effect, finance brokers act as a link between the purchase of personal finance by consumers and the provision of credit by lenders or third party investors.³ As also noted above, except in Western Australian and the ACT, finance brokers are not currently subject to licensing or registration requirements.

The Commission has recommended that the new national regime for consumer credit embody a national licensing system for finance brokers (including those providing advice by electronic or other arms length means), which would be enforced by ASIC and which would provide guaranteed access for consumers to an approved ADR scheme. It has also suggested that pending the development of this licensing system, implementing an interim licensing arrangement based on a draft proposal developed by the Ministerial Council on Consumer Affairs (MCCA) (box E.5), would give credit consumers some early additional protection.

The Commission notes, however, that there are differing views on the efficacy of aspects of MCCA’s draft scheme, including in regard to its ‘neutrality’ across different providers of broking services. Thus while the Mortgage and Finance Association of Australia (sub. DR119, p. 2) was generally supportive of the proposed approach, the Finance Brokers Association of Australia said that:

Finance/mortgage brokers will be cut out of the industry for many day to day finance products such as the refinancing of existing loans together with taking and submitting applications for Lo-doc and No-doc loans ... Brokers will be at a competitive disadvantage against banks and bank branches and their mobile lenders as unlike the broker the bank staff will have unfettered access for those products thus restricting any choice available to consumers. (sub. DR177, p. 5)

³ While the primary function of these intermediaries is to provide advice on mortgage and other credit products, they may also provide related advisory services (such as debt reduction options), or they may act as mortgage managers (arranging loan funding and overseeing the ongoing management of the loan, including monitoring of repayments and administering rate adjustments).

Box E.5 **Draft consultation bill for national finance broking regulation**

Through MCCA, the States and Territories previously agreed to develop a uniform regulatory scheme to apply to all providers of consumer credit broking services. New South Wales was made responsible for drafting of the new legislation and, in November 2007, released a consultation package for public comment. The proposed legislation includes:

- A requirement that brokers be licensed:
 - To gain a license, a broker would have to undergo probity checks and meet prescribed educational qualifications or skills (with experience in the industry not necessarily sufficient for an existing broker).
 - All license holders would be required to participate in an approved external dispute resolution scheme and hold professional indemnity insurance.
- A requirement for brokers to provide a reasonable basis for any recommendation, establish the credit needs of their customers and make sufficient enquiries about their financial status to ensure they can afford the product recommended (including documentation to this effect). Specifically, draft clause 33 specifies that:

...it is the broker who is responsible for ascertaining the consumer's credit needs and for determining whether the consumer has the capacity to repay a loan that satisfies those needs. (NSW OFT 2007, pp. 12-13)
- Various requirements to address conflict of interest issues, including that brokers disclose: the names of the credit providers through which they can access credit; all costs that the consumer will be liable for; and commissions received from lenders.
- Coverage of small business operators, so as to prevent brokers restructuring their activities to avoid regulation, (although business credit would be subject to different requirements that more closely reflected business needs).

A key goal of these requirements is to make brokers pay more attention to loan quality, and to promote more 'responsible' lending advice (see section E 3).

Source: NSW OFT 2007, National Finance Broking Scheme Consultation Package, by the Finance Broking Working Group, prepared for the Ministerial Council on Consumer Affairs. November.

And the Australian Bankers Association commented that:

There are aspects of the draft proposals that are not consistent with the agreed policy settings achieved at a stakeholder roundtable in 2003 that only now are apparent. There are other aspects that industry's united voice in opposition seems unheard. (sub. DR245, p. 4)

CoAG would need to take such concerns into account even if the MCCA proposal is only to be used as the basis for an interim licensing arrangement. There is also the issue discussed in the next section of how the licensing system for finance brokers should interface with a licensing or registration system for credit providers.

National regulation for credit providers

In chapter 5, the Commission has also recommended that under the new national credit regime, all credit providers be either licensed or registered, with the main intention being to ensure that consumers have guaranteed access to an ASIC-approved ADR scheme. It has indicated that this scheme could either be separate from, or a part of, the arrangements for finance brokers.

The Commission notes that National Competition Reviews previously concluded that negative licensing of credit providers would be sufficient to protect consumers. However, those reviews were conducted nearly a decade ago. In the light of evolution in credit markets since then, the relative merits of negative licensing versus other more proactive measures has almost certainly changed.

As spelt out in the submission from ASIC (sub. DR174), a range of considerations will be relevant in determining the stringency of the requirements for credit providers, including that:

- The level and nature of the risks attaching to credit provision are different from financial investment services. For example:
 - The relationship with the consumer is often confined to a one-off interaction, whereas financial investment advice is usually ongoing.
 - In a credit transaction, it is the consumer who holds the asset and makes the promise to repay the loan according to the terms of contract. For financial services, the investor has to rely on the advisor to make a return on, and adequately secure, their investment.
- There are overlaps in the activities of financial entities, so that the provision of credit often occurs in conjunction with the provision of financial investment services. Hence any licensing system for credit providers would need to take account of the fact that many providers would already hold a financial services licence (or, at least, belong to a corporate group that holds a license).
- There may be scope for ‘regulatory arbitrage’ if different licensing/registration standards are imposed on credit providers, finance brokers and financial services providers. Divergent requirements may also affect the relative competitiveness of different groups of service providers and may require ongoing modification to deal with service convergence.

Hence, in essence, there are trade-offs between a ‘proportionate’ regulatory response that recognises the lower risks attaching to credit provision relative to many other financial services, and the problems that can arise with divergent requirements where service activities overlap and evolve rapidly. Getting this trade-

off right in the new national credit regime will clearly be assisted by active consultation between the BRCWG, MCCA and key stakeholders.

Modifications to the UCCC

The Commission has recommended that the new national credit regime retain the UCCC as a self standing set of regulatory requirements within the broader financial services regulatory regime. It has further recommended that these credit-specific requirements incorporate changes agreed to by MCCA, but not yet implemented, to address identified deficiencies in the Code, or to otherwise improve its effectiveness (chapter 5).

In this latter regard, MCCA has already agreed that the Code be amended to:

- narrow the bills of exchange exemption (bill facilities regulation) so that only bills issued by authorised deposit taking institutions are exempt. Legislation to give effect to this change was introduced in most jurisdictions in November 2007;
- ensure better coverage of electronic credit transactions (or electronic receipt of notices), with the legislative process again underway; and
- address issues relating to vendor terms (instalment contracts), with the amending legislation enacted in Queensland in April 2008.

Also, a decision is apparently imminent on whether to continue the Mandatory Comparison Rate regime or introduce alternative measures. And, various changes to deal with ‘fringe lending’ (additional to the bills of exchange amendment) have been outlined in a Regulatory Impact Statement and proposed Code amendment legislation. These include:

- the removal of the presumption that a Business Purpose Declaration means that a loan is not subject to the Code, with credit providers to be encouraged to ascertain the purpose of the loan;
- clarification that a credit contract exists if total repayments under an instalment contract exceed the ‘cash price’; and
- prohibition of a credit provider taking security over essential household goods.

However, amended draft legislation incorporating stakeholder feedback is still to be prepared.

As well, MCCA has foreshadowed new requirements for reverse mortgage products, including a prescribed information statement and protections against negative equity, with a Regulatory Impact Statement currently being drafted. And, following the Post Implementation Review of the Code, amendments to section 80

on default notices are in the process of being drafted. Other credit matters that MCCA is currently examining include:

- pre-contractual disclosure requirements;
- responsible lending practices; and
- alternative dispute resolution requirements.

Interest rate caps

As noted earlier, separate from the UCCC, three jurisdictions impose caps on interest rates, with similar legislation in prospect or under consideration in several other jurisdictions:

- New South Wales and the ACT impose a 48 per cent a year cap on interest rates for both secured and unsecured loans. This cap includes all fees and charges known at the beginning of the loan, but not contingent fees (such as an early repayment fee), or fees on overdraft or lines of credit facilities.
- In Victoria, there is a 48 per cent a year cap on unsecured credit and a 30 per cent a year cap on secured credit. However, these caps do not include fees and charges.

In chapter 5, the Commission has recommended that the new national regime for credit incorporate relevant State and Territory regulation outside of the UCCC where this regulation passes a benefit-cost test. Key considerations in regard to interest rate caps will include:

- the effectiveness of regulated caps in preventing high risk borrowers from being charged excessive interest rates on loans. For example, a recent review (CAV 2006b) found that the Victorian regime is largely ineffective because of the exclusion of fees and charges from the caps. That review also questioned whether the more encompassing regimes in New South Wales and the ACT have a large effect, since usurious charges are most commonly imposed by lenders who are unlikely to be complying with regulation⁴; and
- the impacts of interest rate caps on access to (especially short term) credit by high risk borrowers. That is, such caps may see some higher risk borrowers denied access to credit, even when they are willing and able to meet a high interest rate charge on what is often a short term borrowing arrangement. Indeed, to the extent that more of these consumers are forced to switch from reputable

⁴ The Victorian review went on to recommend that a broader focus is required to handle usurious lending — perhaps through introducing tests of unfairness or unreasonableness in regard to interest rates, fees and charges.

providers servicing this part of the market to fringe or rogue lenders, such caps could be counterproductive.

Also relevant are recent initiatives by some mainstream lenders to improve the access of high risk consumers to short-term credit at reasonable cost. For example, ANZ, in association with the Brotherhood of St Laurence, has introduced a pilot program for low income consumers which provides:

...small affordable loans of between \$500 and \$3000 to people on low incomes for essential household items such as whitegoods, furniture, computers, cars, car repairs and hot water systems. Results from the pilot are encouraging, with 57 loans totalling \$70,387 approved by 30 September 2006, a 70 per cent approval rate and no loans in arrears. (ANZ Banking Group, sub. 82, p. 12)

So too will be the extent to which providers of credit to high risk borrowers self-regulate through responsible lending policies (see next section).

Responsible lending practices

As alluded to in section E.1, there has been considerable recent concern about the extent of lending to consumers perceived to have little prospect of paying off a loan. In pointing to perceived inadequacies of the UCCC in addressing responsible lending issues, the Consumer Credit Legal Centre stated that:

... there is no clear provision in the UCCC that specifies that a lender should consider a borrower's ability to repay a loan and no penalty for failing to do so. Further, while section 70 has been widely applied by the BFSO to assist borrowers and lenders to arrive at affordable negotiated outcomes, including loss of interest and fees and sometimes a reduction in the principle debt, the few court decisions that have been handed down have interpreted the section narrowly and/or applied a very limited remedy. The net result of this is that there is little incentive for lenders to ensure that borrowers have the capacity to pay. (sub. 95, p. 67)

As noted earlier, MCCA is currently looking at whether the Code requires modification to help promote responsible lending. And its proposed licensing system for finance brokers would explicitly require brokers to assess borrowers' capacity to repay loans (see box E.5).

However, the question of whether these or other regulatory initiatives are needed to 'promote' responsible lending, is not an easy one to answer:

- In the vast majority of cases, it is in the lender's commercial interests to ensure that a loan can be repaid. That is, reputable lenders do not make money from bad loans (unless the risks of default are passed on through securitisation). And in the case of deposit taking lenders, commercial incentives are reinforced by various prudential requirements.

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- Designing regulation that is effective in promoting responsible lending is likely to be challenging. For example, there has been considerable debate in this inquiry about whether the ACT's requirements governing offers of increased credit card limits have materially altered the level of loan defaults in the Territory.
 - Such regulation is likely to increase the cost of lending to all credit consumers, irrespective of whether they are at high risk of defaulting. And, like interest rate caps, there is some risk that it could lead to the denial of credit to those willing and able to pay for a loan.
 - In response to concerns from consumer groups and others, several mainstream lenders have introduced responsible lending charters and processes designed to reduce the incidence of defaults by borrowers having difficulty meeting their repayments. (See for example, ANZ, sub. DR246, pp. 1-3.) Arguably, such self-regulation may be more effective than black letter law.

Nonetheless, there are clearly linkages between the regulation of financial services providers and consumers' access to credit products. Hence, in the body of the report, the Commission has concluded that those tasked with the detailed development of the new national regime for consumer credit should consider how 'responsible lending' issues might impact on the regulatory arrangements. There may also be a need to examine whether aspects of Australia's privacy legislation inappropriately impede the use of credit reporting information to assess credit risk and promote more responsible credit provision. (See, for example, Veda Advantage, sub. DR244, p. 1-2).

Other matters which may require further consideration

Drawing on input from inquiry participants, the Commission has identified several other service coverage and related matters that may warrant attention by CoAG, in consultation with MCCA, in developing the new national credit regime, or in making any parallel changes to the broader financial services regulatory regime. (As noted earlier, in agreeing in principle to the transfer of responsibility to the Australian Government for regulating several key credit products and advisory services, CoAG has also asked the BRCWG to identify any other financial services where a similar transfer of responsibility may be appropriate.)

Loans for small business and investment purposes

The UCCC only applies to loans made for personal, domestic or household purposes. Hence, it does not cover loans made to consumers for investment purposes, such as margin loans. Nor does it cover loans to small business. The latter is in contrast to financial services regulation which applies to financial products or

services purchased by households, individuals or small businesses. Likewise, businesses may receive protections from various parts of the TPA and Fair Trading Acts (see chapter 13).

While CoAG has agreed in principle that the Australian Government will assume regulatory responsibility for margin lending, several participants argued that consumer credit regulation should also cover small business loans. For example, ASIC stated that:

Arguably, industry-specific legislation covering credit should extend to small business consumers. Minimally, like other borrowers, small business borrowers should have access to good disclosure and dispute resolution in relation to credit, as they do in relation to financial products regulated under the financial services laws. (sub. 103, p. 35)

The Consumer Credit Legal Centre added that:

There is no reason why the majority of the protections contained in the Code should not also be available to business and investment borrowers ... [although] There may be an argument to exclude business borrowing from the hardship variation provisions of the Code and there are perhaps other sections that could be specifically modified or made unavailable to business borrowers. (sub. 95, p. 42)

While not having examined this issue in any detail, the Commission observes that such an extension in coverage would at least have the advantage of promoting more consistency in the remit of applicable regulatory instruments in this area.

Property investment advice

For many consumers, investment in property is a significant part of their overall investment portfolio. Moreover, investment in property and investment in shares will often be substitutes. Yet while advice on shares is covered by the financial services regime administered by ASIC, property investment advice is not.

Several participants suggested that the current treatment of property investment advice should be reassessed. For example, ASIC said that:

Given the prevalence of real property in Australians' investment portfolios (and that credit is normally involved), and particularly its importance to many Australians' retirement incomes, there is a case for that form of investment being regulated in a similar way to other forms of financial investment. (sub. 103, p. 31)

The Real Estate Institute of Australia (REIA, sub. DR172, p. 10) similarly contended that property investment advisers are 'marketeters' as distinct from real estate agents who facilitate individual transactions between buyers and sellers 'and do not make recommendations regarding whether or not it is in the financial interests of a particular purchaser to invest in a particular property.' It went on to

propose that anyone providing advice on the relative merits of investment in property and other asset classes should be subject to the national financial services regime. The Western Australian Department of Consumer and Employment Protection (DOCEP, sub. DR248, p. 9) drew a similar distinction, stating that, in its experience, ‘most property investment advice is not given by licensed real estate agents and this is particularly true of the most problematic advice’.

The Commission notes that a recent report by the Victorian Parliament’s Law Reform Committee (2008) has called for improved protection for property investors, and has recommended that if there is no agreed national solution, then the Victorian Government should introduce its own regulation. The current CoAG process could therefore be an appropriate vehicle for preventing potentially costly regulatory break-out in this area.

That said, any move to bring property investment advice within the national financial services regime would need to address the regulatory interface between such advice and the activities of real estate agents. The latter are currently regulated by the States and Territories (though the REIA suggested that a transfer of responsibility to the national level would be appropriate — see section 5.2). Also, giving consumer regulators jurisdiction to take action in relation to financial services matters (after consultation with ASIC — see recommendation 4.2) would make it harder for rogue property investment advisers to design their activities to avoid all of the current regulatory apparatus.

Web aggregators

Those selling online account aggregation services — so called ‘web aggregators’ — are another group of financial services providers who are not currently covered by the financial services regime. While most web aggregators include information on their website on such things as terms and conditions, privacy, security, fees, direct marketing intentions, and customer liability, there are no regulations requiring them to do so.

ASIC examined web aggregation services in 2001 and identified several issues that might bear on the adequacy of protections for consumers of these services. These included liability for unauthorised transactions, liability for other losses associated with the quality, and use, of web aggregation services, complaint handling and dispute resolution.

Moreover, since then, many web aggregators have expanded their operations. In particular, it is now common for them to draw on their administrative platform to offer targeted financial advice and assistance in the direct purchase and sale of

investments. Moreover, there is potential for some web aggregators to have an ongoing role in the management of financial investment products.

Given this ongoing evolution of web aggregation services, as Suncorp (sub. DR171, p. 3) and some other participants argued, it might now be timely to re-examine whether providers of these services should be bought within the financial services regime.

Reverse mortgages

A reverse mortgage is an arrangement where the loan (and interest on the loan) is not repaid until the property is sold, with the loan secured against the equity in the home. In 2007, more than 30 000 households had a reverse mortgage with an estimated total value of \$1.8 billion (SEQUAL 2007).

The UCCC covers reverse mortgages where more than 50 per cent of the loan is used for consumption purposes. And some aspects of the product are covered by other regulations in certain jurisdictions.

However, there are concerns that protection for consumers is inadequate — especially in dealing with negative equity, when the amount of the loan increases to a point where it exceeds the value of home. Hence, Choice argued that enhanced reverse mortgage laws are required to:

... force the industry to standardise its contracts and clear up the problems and prevent excessive risks to borrowers in years to come. (sub. 88, p. 80)

As noted earlier, MCCA has foreshadowed changes to the UCCC that would help to address some of these concerns. But specific legislative amendments to the Code still appear to be some way off.

Debt collection

Currently, debt collection is primarily regulated through specific State and Territory legislation, enforced by the Fair Trading Authorities. In addition, there are some relevant provisions in the UCCC, including those relating to hardship and debt enforcement. The generic consumer law may also be applicable to certain debt collection practices, with ASIC and the ACCC having introduced national guidelines for debt collection.

However, some participants claimed that the current arrangements are inadequate to protect consumers from inappropriate debt collection practices. (See, for example, Reach Out for Kids Foundation, sub. DR124, pp. 2–3). More specifically, the

Western Australian Department of Consumer and Employment Protection (DOCEP) (sub. DR248, p. 8) said that it has received legal advice that its debt collection legislation will not apply where a debt demand originates in another jurisdiction and suggested that the same problem may arise in other jurisdictions. DOCEP went on to argue that while action is in train to address this problem, a national approach would be preferable — ‘especially given the intrinsic connection between debt collection and the provision of credit.’

Given such linkages, any move to regulate debt collection at the national level would of course need to clearly delineate the respective roles of ASIC and the ACCC. In the past, there has apparently been some confusion in this area. (See, for example, Consumers’ Federation of Australia, sub. 83, p. 4). However, ASIC (sub. 103, p. 71) indicated that the two agencies now have a formal agreement clarifying their respective responsibilities. This agreement is in line with the more general protocol that the Commission has recommended should apply in the financial services area following an end to the carve out of these services from the generic consumer law (see recommendation 4.2).

F Utility services

Key Points

- Consumer policy serves an important function in utility services, due to their 'essential' nature — revealed by the harmful effects of disconnection — and also because the lumpy nature of utility bills and the predominance of credit as a purchasing method gives rise to affordability issues.
 - In particular, policy is important for vulnerable and disadvantaged groups.
- There are overlaps and inconsistencies between state and territory consumer policies for utility services, resulting in unnecessary business compliance burdens and consumer protection that varies across jurisdictions.
- Particular consumer policy issues emerging for utility services include:
 - the proposed national approach for consumer policy in energy that preserves some significant jurisdictional variations in requirements (such as in regard to price regulation, separate ombudsman schemes and service standards);
 - increasingly complex services that may confuse consumers or, through contract design, lock them into their existing suppliers;
 - the design of hardship policies; and
 - the shortcomings in using retail price regulations to alleviate financial hardship and help disadvantaged consumers, (though, in less than fully contestable utility markets, such price controls can help to prevent detriment for all consumers arising from monopoly pricing).

F.1 Introduction

The provision of utility services has changed significantly in Australia over the past two decades. Competition reforms have mostly eliminated government monopolies. New technologies have emerged, which have added to service variety (as in mobile telecommunications) and changed service delivery (such as computer technologies that have permitted more sophisticated and cheaper billing services).

Consumers have benefited from these changes in various ways, including through often lower prices and access to a wider range of service providers, price/quality packages, contract periods and bundles that combine different utility services.

Nevertheless, given the nature of such services, problems associated with utilities account for about one in five of all consumer problems. In Victoria alone it has been estimated that in 2006 there were over one million individual problems, giving rise to around \$560 million of detriment, including follow up and resolution costs of \$164 million (IPSOS 2006) — though these estimates are subject to the caveats spelt out in chapter 14. Across Australia, the implied value of detriment associated with problems arising in utility services is around \$2 billion a year.

The key challenges for consumer policy in the utility services area are that:

- product complexity means that consumer choices may not always be well informed;
- more billing, contract and service quality problems have emerged with the entry of many new competitors, more complex products and new technologies; and
- disadvantaged consumers may need special protection. They are more at risk of disconnection from services and may struggle to afford prices, especially those (efficiently) structured with a high fixed charge component.

The reform process recognised these challenges, though in a way that has led to considerable regulatory complexity. A new set of industry-specific consumer policies, such as ombudsmen schemes and consumer codes, were put in place as each utility was reformed in each jurisdiction. Accordingly, many of the current arrangements are a result of the way in which competition reform was introduced, rather than necessarily being the best long-run way of dealing with consumer issues in these areas.

The central question addressed in this appendix is how well the present arrangements are working and are likely to work in the future. Specifically it:

- considers the importance of utility service industries in Australia, since this indicates how significant any problems are likely to be compared with other consumer expenditures (section F.2); and
- examines the current consumer policy framework for utilities (section F.3), assesses its performance and identifies potential problems, particularly in relation to inconsistencies in State approaches to energy related consumer regulation and the application of retail price regulations (section F.4).

F.2 Why utility services are important

Consumer policy for utility services recognises their special characteristics:

- Most households will need access to these services to achieve even a basic living standard (box F.1) — hence their ‘essential’ nature. Nearly every Australian

household is connected to basic essential services, with relative spending on them being higher among lower income households.

- Rather than being purchased in small divisible portions, as occurs with say food, utility services are frequently paid for on a monthly or quarterly basis — resulting in ‘lumpy’ expenditures that are high compared with weekly income.
- Households are either connected to utilities or they are not, and it is not always possible to ration consumption as usage requirements and capacity to pay change.

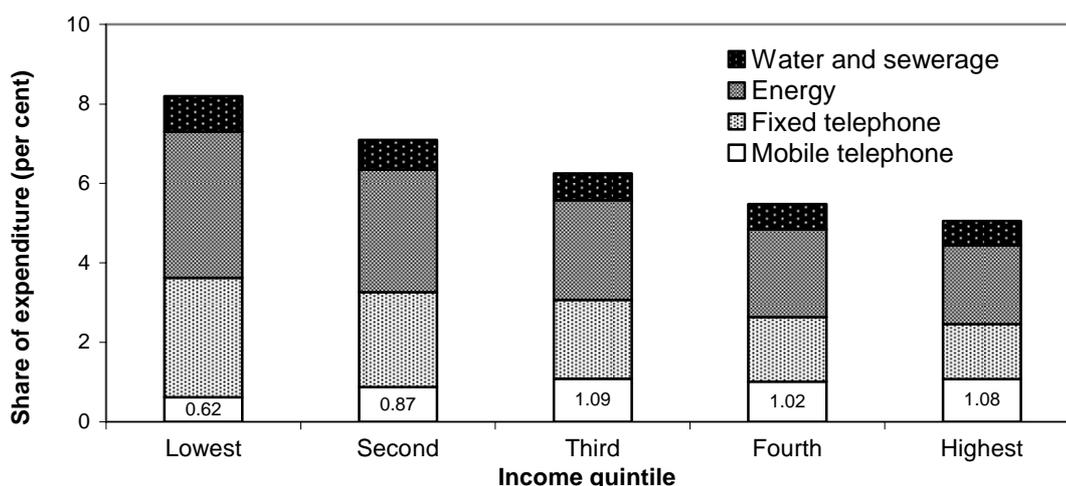
Box F.1 Household welfare and expenditure on utility services

Utility services are vital to households. They provide the basic means by which any household is able to function in a modern society (ASCARC 2004).

Household expenditure on utility services is around 6 per cent of average weekly income, but about 8 per cent for lower income households (figure).

While energy, water and basic phone services are usually characterised as essential services, some newer telecommunications services — mobile telephony and Internet services — are less clearly so. For example, mobile phone expenditure displays the reverse relationship with income as that typically observed for ‘essential’ services (figure below), with spending shares increasing as income rises. Of course, over time, expectations of what is necessary will alter, and accordingly, these services may well be regarded as essential in the future.

Share of expenditure on utilities, by household income quintiles



Sources: ABS, *Australian System of National Accounts, 2005-06*, Cat. no. 5204.0; ABS, *ICT Satellite Account 2002-03*, Cat. no. 5259.0; and ABS, *Household Expenditure Survey, 1998-99 and 2003-04*, Cat. no. 6530.0.

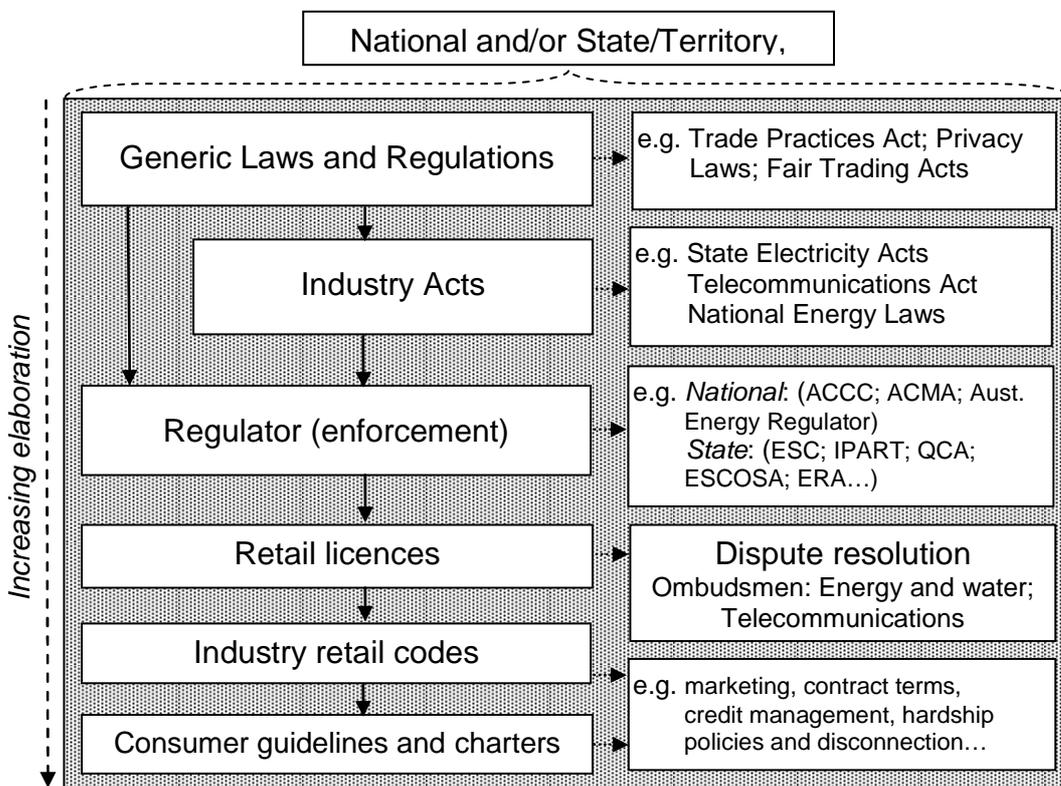
Given their essential nature, governments intervene on social justice grounds to ensure that all households have access to an adequate level of services at reasonable prices.

In particular, avoidance of disconnection remains a cornerstone of consumer protection in utility services. Disconnection of services has obvious harmful effects — it socially isolates, can make people sick or very uncomfortable, and causes difficulty in undertaking the most normal of tasks (cooking or storing food; heating).

F.3 Current regulatory framework

As well as meeting the social objectives described above, consumer policy for utility services aims to facilitate informed choice, to encourage ‘fairness’ in contracts and to minimise and deal with disputes effectively. Pursuing these objectives, the regulatory framework uses a mix of ‘black letter law’, co- and self-regulatory approaches and over-arching generic legislation (figure F.1). Specific policy tools employed include the Trade Practices Act (TPA), Fair Trading Acts (FTAs), retail price regulations, Community Service Obligations (CSOs), Universal Service Obligations, industry-sponsored ombudsmen schemes, registered (and therefore legally binding) consumer codes, and consumer guidelines and charters.

Figure F.1 The current consumer policy framework for utility services



While some aspects of consumer policy for utility services are applied at the national level, States and Territories also play a significant role. Generally, consumer policies in individual States and Territories reflect the extent of deregulation in each jurisdiction. For example, Victoria introduced Full Retail Contestability (FRC) in electricity services earlier than most and has a large number of retail suppliers competing for customers (table F.1). Not surprisingly, the reach of consumer-orientated legislation in Victoria has tended to surpass that of other jurisdictions, as illustrated by its mandated customer hardship programs for energy services.

Table F.1 Competition in retail electricity markets

<i>Jurisdiction^a</i>	<i>Introduction of retail contestability^b</i>	<i>Licensed retailers^c</i>	<i>Switching activity since FRC</i>	<i>Disconnections per 100 customers</i>	
				<i>2004-05</i>	<i>2005-06</i>
New South Wales	1 January 2002	17 [24]	30 per cent switched from regulated tariffs (2007)	1.00	0.90
Victoria	13 January 2002	18 [26]	Approx. 60 per cent switched from their local supplier (2007)	0.50	0.22
Queensland	1 July 2007	18 [20]	na	1.57	..
Western Australia	Still pending ^d	na [11]	na		1.16 ^e
South Australia	1 January 2003	15 [22]	59 per cent switched from a standing contract (2007)	1.20	1.14
Tasmania	2010 ^f	na [1]	na	0.44	0.72
Australian Capital Territory	1 July 2003	3 [8]	4 per cent switched to a retailer other than ActewAGL (2006)	0.40	0.40

^a Although not included, clause 6(4) of the Northern Territory Electricity Reform (Administration) Regulation says that all customers will be contestable from 1 April 2010. ^b All market segments contestable. ^c The first number indicates the active providers in each market (member of an industry ombudsmen scheme), figures in parentheses indicate the total number of licences issued. ^d Awaiting greater competition in existing contestable market segments. ^e Includes non-residential customers. ^f Subject to a public benefits assessment.

Sources: AER 2007, p. 195; National Comparative Performance Data Retailing Quality of Service Reporting Templates; IPART 2007; CRA International 2005; ESCOSA 2006; Economic Regulation Authority (WA) 2007; TruEnergy, sub. 34, p. 6.

There are also differences in regulatory approach across utility services:

- Gas and electricity are in different stages of development towards national regulatory regimes, with no national trading market operating for gas. And, although the Ministerial Council on Energy is pursuing a national energy consumer policy that incorporates gas, the extent to which current jurisdictional differences in consumer protection arrangements for gas will be eliminated is

uncertain. For example, customer transfers and metering requirements vary noticeably across jurisdictions (EWON 2007).

- Water supply is in the earlier stages of liberalisation, and although characterised by less prescriptive consumer provisions than those for energy and telecommunications, the arrangements are still complex and there is even greater divergence in regulatory approaches across jurisdictions.

Ombudsmen schemes

Together with suppliers' own dispute resolution processes, ombudsmen schemes provide the main way of resolving consumer disputes with utility suppliers. At the state level, independent ombudsmen have jurisdiction across electricity, gas and water markets. In the case of telecommunications, a national scheme operates, covering standard fixed line, mobile phone and Internet services. These schemes are free to consumers and require compulsory participation by service providers and network operators, who also fund the schemes — usually based on scheme usage.

Ombudsmen schemes provide an alternative to the court system for consumers who have not been able to achieve direct resolution with their service provider. The ombudsman acts to resolve disputes independently — focusing on complaint resolution, not advocacy. The activities of each ombudsman are overseen by an independently chaired council with industry and consumer representatives; or a board with funding and corporate responsibilities; and sometimes both a board and council.

There are memorandums of understanding between each ombudsman and the relevant industry regulator to address emerging issues, reduce overlap or gaps and report licence breaches. Ombudsmen are also required to identify and report on systemic issues emerging from their work. For example, the Telecommunications Industry Ombudsman has recently looked at the marketing of mobile phone service contracts (including 'capped plans') and information about unlimited Internet plans. For energy and water, systemic issues recently investigated include marketing misconduct, customer financial hardship and disputed ownership of poles and wires. Nevertheless, while ombudsmen have binding determinative powers, wider enforcement is the role of the regulating body.

The coverage of ombudsmen schemes has grown in response to developing market arrangements. For instance, state-based ombudsmen schemes for utility services were formerly specific to the retail supply of electricity, but have subsequently been extended to gas retailing, and more recently in some states to water. Similarly, the coverage of the TIO scheme continues to expand. This reflects changes in the dispute resolution needs of consumers as new products and services emerge, and continued

convergence between communications technologies and content provision. For example, a Mobile Premium Services Industry (MPSI) scheme was established in late 2006, with an associated dispute resolution function given to the TIO. This scheme applies to content services — data, news, games, video, audio, graphics and adult content — provided through mobile phones and mobile Internet connections. That said, the TIO has limited or no jurisdiction over a range of telecommunications-related areas — handsets, pay TV and some residual premium services (chapter 9).

F.4 How is the system performing?

According to both consumer advocates and utility suppliers, the current consumer protection arrangements for utility services are operating reasonably well. But some tensions and suggested areas for improvement remain (box F.2). These relate to:

Box F.2 Views on performance and scope for improvement

Submissions to this inquiry variously identified scope for improvement in the current consumer policy framework, focussing around the need for:

- better arrangements for the delivery and funding of CSOs. In particular, Telstra questioned its differential responsibilities for delivering them (Telstra, sub. 35, p. 4);
- retail price regulations, especially since hardship policies have been instituted (Origin Energy, sub. 31, p. 16; AGL Energy Limited, sub. DR149, p. 2; Telstra, sub. DR156, p. 9; ERAA, sub. DR184, p. 3);
- better regulatory enforcement (TIO, sub. 97, p. 6; Consumers' Telecommunications Network, sub. 78, p. 28);
- better resourced consumer advocacy and empowerment, to provide consumer feedback to regulators and utilities about the effectiveness of consumer policy (WACOSS, sub. 68; ANZEWON, sub. 64, p. 16); and
- greater regulatory consistency between jurisdictions and less complex regulatory responsibilities (Communications Alliance, sub. 50, p. 1; Telstra, sub. 35, p. 25).

Independent reviews of the performance of ombudsman schemes have generally been positive, suggesting only minor changes (Allen Consulting 2006; EIOSA 2006; Urbis et al. 2002). Nevertheless, some participants have been more critical, particularly of the TIO (Centre for Credit and Consumer Law, sub. 93, p. 30). Further, in discussions with the Commission, some energy retailers noted differences among ombudsmen that, in their view, raise their costs and lead to variable outcomes for consumers. Some have also flagged that the option of a national ADR scheme should not be precluded (ERAA 2006, AGL Energy, sub. DR149, p. 2; and Origin Energy, sub. DR158, pp. 2-3).

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- overlap and inconsistency between industry-specific codes and generic provisions, across States, Territories and industries;
 - product complexity, particularly information disclosure, contract terms and bundling options;
 - policies intended to help vulnerable and disadvantaged consumers, including retail price regulations and financial hardship arrangements, and the associated funding of CSOs; and
 - regulatory enforcement, including the design of dispute resolution schemes and the jurisdiction of the regulator.

A jurisdictionally-focussed regulatory regime

State variations pose problems

The supply of utility services is highly regulated, with the consumer policy component enmeshed in a prescriptive, jurisdictionally- and industry-specific framework. Regulatory measures have mostly developed in an incremental fashion to counter the progressive emergence of consumer challenges (for example, to address ‘aggressive’ marketing conduct). These features have some undesirable impacts.

In particular, variations in consumer policy for energy services across jurisdictions (box F.3) can result in different outcomes for consumers. For example, involuntary electricity disconnection rates for consumers differ by a factor of around five (table F.1). Similarly, alternative dispute resolution schemes are currently fragmented, with varying funding and ownership arrangements and, more importantly, inconsistent processes used to deal with consumer complaints.

The jurisdictional complexity of the regime may impede the efficient use of resources for regulation and redress, and is likely to be costly for providers (and in turn consumers). The ERAA (2003, pp. 12-13) has identified a multiplicity of differences in regulatory codes across jurisdictions. The provision for contestability in most parts of Australia has meant that retailers now compete in up to four state markets (AER 2007, p. 171), and increasingly face the compliance burdens associated with these multiple, inconsistent policy regimes.

It is a significant impost on energy retailers trading across states to have to manage different jurisdictional variations and consumer frameworks. (ANZEWON, sub. 64, p. 34)

...AGL is a national energy market participant operating in many jurisdictions. The complexity and differences in current regulatory requirements arising from generic and energy specific regulation across the various jurisdictions impose significant operational and compliance costs upon participants in the energy market. (AGL Energy, sub. 57, p. 2)

There are currently at least 10 national and State based schemes that regulate the sale and provision of Green Energy to consumers...The range of national and state based schemes has resulted in unnecessary and complex rules and obligations and therefore higher costs for market participants and consumers. (TruEnergy, sub. DR164, p. 2)

Green energy initiatives have progressively been introduced by various state and federal governments over the past few years ... the administrative cost burden on retailers of green schemes should not be underestimated. (Origin Energy, sub. DR158, pp. 1-2)

Participants indicated that compliance burdens might even prevent entry in some markets.

Progressing to a national framework for energy

The framework for the economic regulation of energy and the commercial focus of retailers is becoming increasingly national (box F.4). In this context, a fragmented set of consumer policy arrangements in the energy sector is increasingly out of kilter with broader market and regulatory developments that are national in orientation.

Governments have recognised this and have initiated a policy reform process to achieve more national consistency in energy consumer policy. To date, the Retail Policy Working Group (box F.4) has consulted industry, consumers and government on various approaches to a new energy consumer protection regime, with recommendations provided to the Standing Committee of Officials (attached to the Ministerial Council of Energy). Principally, these involve the development of a single set of energy-specific rules that would apply where generic consumer laws in the jurisdictions are either inconsistent or silent. For example, national energy-specific rules would be put in place for cooling off periods, which are currently treated inconsistently by various FTAs. Similarly, there would be a single set of rules applying to disconnection procedures and hardship provisions because these are not covered by generic consumer law.

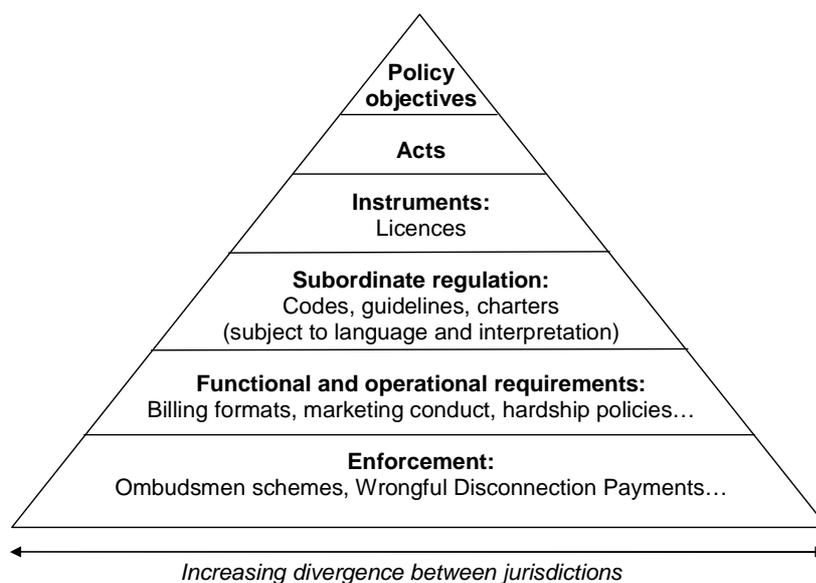
While greater national consistency would be achieved, this approach would produce a quite detailed list of energy-specific consumer protections. Moreover, it is still currently intended that for some matters (including retail price regulation, alternative dispute resolution and service performance targets), arrangements will remain jurisdictionally based. It is also likely that jurisdictions will retain scope to taper their commitment to the new national consumer regulations in specific areas. For example, hardship arrangements currently vary significantly across jurisdictions and the inclusion of less detailed provisions in the new national regime than those existing in some jurisdictions may prove to be a sticking point. Hence, the new policy framework — scheduled for introduction around 2010 — will be a hybrid, rather than a truly national regime.

Box F.3 Differences in energy consumer policy across jurisdictions

Some differences across the current state-based arrangements are:

- Design of retail price regulations, including the amount of 'headroom' provided to set prices above estimates of direct costs.
- Payment collection cycles and procedures for the notification of price changes, disconnection and reconnection:
 - Retailers adopt the systems and procedures specific to each jurisdiction, or comply with the most onerous obligations (accepting associated revenue losses).
 - Notification of a price change outside a normal billing cycle may cost a retailer around \$20 000 plus \$1.30 per customer per event.
- Mandated payment options:
 - The provision of each additional payment option can cost around \$2 million per year to support.
- Meter reading obligations and the regulation of prepayment meters.
- Marketing codes of conduct, including contact hours and information disclosure.
- Cooling off periods, and termination periods and charges.
- Customer consent for transfer and retrospective transfers.
- Ombudsman schemes:
 - some appear to adopt cases simply if the type of dispute falls within the remit of their scheme, while others are guided by a narrower, merit-based criteria.

Some retailers indicated to the Commission that the differences in consumer policy across jurisdictions become more pronounced as regulators successively develop and re-interpret detailed requirements through subordinate regulation.



Source: ERAA 2003.

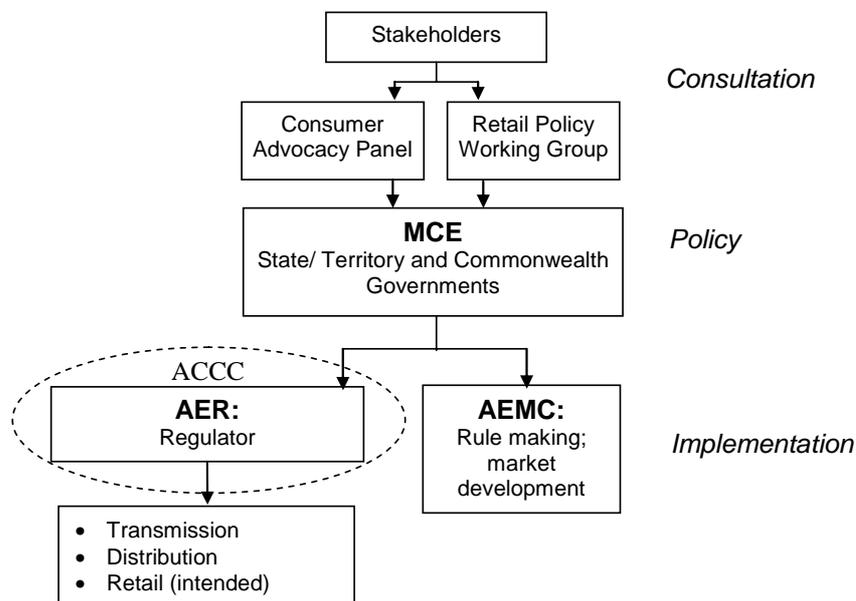
Box F.4 Institutional arrangements

The institutional arrangements overseeing a national approach to energy are complex. The Ministerial Council on Energy (MCE) has responsibility for the transfer and national consolidation of state-based economic and consumer regulations in the sector. In this setting, energy-sector policy development occurs collaboratively between the Commonwealth, States and Territories.

The retail policy working group — comprising representatives from each of the National Energy Market jurisdictions and the Commonwealth — has the major policy development function for a national approach to consumer policy in energy and on the relative roles of energy-specific and generic consumer laws.

The Australian Energy Regulator (AER) implements national regulations as decided by the MCE (though as noted above, it does not yet have coverage of Western Australia energy or Northern Territory electricity). The AER regulates transmission and distribution, and once a national framework is determined, will also cover retailing. Although located within the ACCC, the AER is a multi-governmental body that operates as a separate legal entity.

Under direction from the MCE, the Australian Energy Market Commission (AEMC) is tasked with rule making for electricity and gas. Recently, the AEMC reviewed the effectiveness of competition in electricity and gas retail markets in Victoria, and it is intended that further reviews will progressively be conducted for other markets also.



Nevertheless, while a fully national regime for consumer protection in energy is desirable for many reasons, there are practical limitations to its immediate implementation (chapter 5). Aside from the intended scope for jurisdictions to retain the ability to unilaterally set requirements for some key aspects of consumer protection in this area (see above):

-
- energy in Western Australia and electricity in the Northern Territory are currently outside the national market arrangements; and
 - jurisdictions are in different states of energy market competition (EWON 2007, p. 8). For example, full retail contestability of electricity is yet to be implemented in Tasmania¹, while the Victorian electricity market is described as one of the ‘hottest’ in the world. This limits the scope for immediate removal of retail price regulations at a national level, a factor also recognised by ANZEWON who noted the potential for significant differences in the timing of any price deregulation (sub. DR187, p. 3). Similarly, jurisdictions currently have very divergent supply arrangements, with different degrees of supply integration and government ownership (National Consumers’ Roundtable on Energy, sub. DR199, p. 4). Further privatisation of assets will also have implications for policy settings in the jurisdictions concerned.

Overtime, however, the importance of these sorts of factors is likely to subside. There is an agreement in place between jurisdictions that establishes a time path for the removal of retail price regulations (triggered by AEMC assessments of retail competition). In the near future, states will have put in place more nationally consistent arrangements for some aspects of retail supply, and will have seen some of the benefits of a national approach. This may set the foundations for the elimination of the residual regulatory inconsistencies, and provide the basis for the transition to a truly national consumer policy framework for the retail supply of energy. The desirability of this is considered further in chapter 5.

Complex products

Many utility services used to be relatively straightforward: a telephone landline, and energy and water services with simple tariffs. But technological change and competitive reforms have provided much more choice and valuable new services to consumers (box F.5). In telecommunications, for example, this has seen the technological transformation from what has been called ‘POTS’ (the plain old telephone system) to ‘PANS’ (pretty amazing new services), such as VoIP, ADSL2, 3G mobile services, SMS and videoconferencing (Laffont and Tirole 2000, pp. 1-2). Even where the basic service has stayed the same (electricity down a wire), the availability of accompanying features has widened, such as time-of-day metering, bundling options, ‘green’ energy options, and choices about contract periods.

¹ The Tasmanian Government has only committed to doing a public benefit test of Full Retail Contestability and would also have to legislate new regulations before any decision to implement it.

Box F.5 Features of product complexity

Energy

- Tariff structures and price menus. These include fixed prices for a period of time; tariff structures stepped according to usage and time-of-use; and charges that differ between network, retail, fixed and variable components.
- Rebates and discounts (connected to bundling or on-time payment).
- Flexible payment options.
- Contract terms (including a move to fixed term and termination fees).
- Non-price benefits, including product vouchers and offsets against club memberships.
- Green energy products.

Telecommunications

- An even more elaborate set of tariff structures, including 'capped' plans and charges that often vary by the terminating network; 'free' handsets; and unlimited downloads.
- Development of advanced complementary technologies in handsets (mp3 playback, cameras etc.).
- Emergence of 3G networks, providing voice calls and SMS — as with the 2G network — while additionally providing Internet, video telephony, broadband-like services, and other content services including mobile TV and data applications.

Bundling

Bundling options are now widely available that combine utility services (such as water plus electricity; landline, mobile and Internet) into a single purchase with one bill.

In addition to their direct value in expanding value and choice, these new features also have some less obvious benefits. More flexible pricing structures enable providers to tailor prices to different usage patterns: to better manage peak loads (in electricity) and target high volume users and increase network utilisation (in telecommunications). And bundling offers benefits to consumers, such as a single billing process and discounts on packages of services.

However, more service and product choice also entails complexity, which can present problems for some consumers.

First, complex pricing structures and contract terms mean that some consumers do not adequately comprehend contract provisions or the application of fees and charges, particularly in relation to Internet or phone services, which may explain the rise of more complex complaints (TIO 2006a).

Secondly, it can prolong the resolution of complaints. For example, the time needed by ombudsmen to resolve serious energy and water complaints has grown — a likely symptom of the rising complexity of products and the importance of negotiated energy supply contracts. In its monitoring activities, the Energy and Water Ombudsman of New South Wales notes ‘increasingly complex tariffs and bills’ (EWON 2006a, p. 20).

Thirdly, complexity may make it difficult to compare the offerings of competing suppliers, or even the different service bundles available from an individual supplier. In turn, this may result in some consumers making inappropriate purchasing decisions. For example, a UK study on switching activity in energy found that:

... there was a persistent bias by consumers to seek a ‘flat rate’ tariff in relation to volumetric consumption charges ... even when the consumer’s choice of a ‘flat rate tariff’ resulted in their paying in excess of 100% more for the service than they would have under available multi-tariff schemes ... Difficulties in accessing and interpreting market information give rise to significant personal costs in searching behaviour, to locate the best price. (Wilson et al. 2007, p. 5)

As discussed below, to the extent that switching is deterred, the potential benefits of greater competition in the supply of utility services could be diminished.

Finally, consumers may encounter problems from bundling essential services with non-essential services, as non-payment can result in disconnection of all services.

Some responses to greater complexity are developing

Several market responses to greater product complexity have emerged as consumers and firms have learned to transact with each other more effectively. Some regulatory changes have also been introduced. Collectively, these responses have made it easier to compare different service offerings and, in turn, assisted consumers to understand the features, rights and obligations associated with their purchases. Specific responses include:

- ‘Simpler’ payment plans, including pre-paid mobile services and pre-payment electricity meters that give consumers greater control of their expenditure by avoiding complicated tariff structures. Telecommunications providers also now offer a range of services directed at managing accounts, in particular, dollar spend limits for premium services; automatic notifications when data usage limits are being approached; and notification when a ‘pre-bill’ is detected as unusually high.
- More comprehensible and simpler standard form contracts to reduce the likelihood of consumer confusion and information overload. For example:

Telstra has undertaken a major project to re-draft its standard terms in plain and easy to understand language, in particular, its consumer contracts for mobile phone services and its BigPond Internet services. (Telstra, sub. 35, p. 9)

In addition, the Australian Communications and Media Authority (ACMA) issued the Telecommunications (Standard Form of Agreement Information) Determination 2003, requiring providers to publish a summary of their terms and conditions that is not more than four pages in length.

- Web-based price comparison tools for residential electricity and gas. These are usually provided by government regulators. For example, ACMA provides a web-based *Tool Kit* information portal, which is designed to assist consumers in matching the value of a mobile, Internet or fixed line service to their needs.
- Specialist switching firms — acting as intermediaries. These have emerged in the UK to facilitate switching and overcome the complexity of choosing service providers, and also exist for business customers in Australia.

Switching and transaction costs

Ease of switching is an important aspect of an effective competitive environment in the provision of utility services. However, transaction costs and other factors can constrain switching, locking in consumers even when another supplier could better meet their requirements. These costs and constraints include:

- Greater product and contract complexity, and search and information costs associated with finding the best offer available in the market.
- Regulatory interventions that mandate certain technologies. For example, smart electricity metering has been mandated in Victoria, but out-of-state electricity providers may not be able to read (and apply tariffs) for such meters properly, making them less likely to attract consumers.
- Arrangements that can ‘lock-in’ consumers, such as the design of fixed term contracts that feature initially attractive terms² and impose subsequent high termination penalties. When customers purchase bundled services, features of the contract that lock-in any single service act as a further barrier to switching. It is alleged, for instance, that such barriers exist in telecommunications (ACCC 2006b, p. 33 and 2005a, p. 24). More generally, there is evidence that ‘lock-in’ may not be anticipated by consumers, leading to detriment and diminishing competition (Vickers 2003, Farrell and Klemperer 2006).

² For example, retailers offer new customers discounts, loyalty rebates, and non-price rewards such as home appliances. Though designed to induce a customer to switch (or simply develop a taste for the product), there is also an expectation of capturing later sales, possibly at higher prices.

Notwithstanding these concerns, many consumers have switched between suppliers with the advent of retail competition. In energy, there has been a significant transfer of customers from non-market to market contracts (table F.1). Switching between telecommunication providers has also been significant, with the continued penetration of new technologies in the market encouraging switching between different products as well.

And for those consumers who have not switched, there is some evidence to suggest that many have stayed with their current supplier for reasons other than barriers to switching.³ Rather, lack of switching may often reflect consumer satisfaction with their current supplier, or changes made by their supplier to meet market competition and retain customers. This, in turn, illustrates that actual switching does not necessarily need to occur for all consumers to reap the benefits of competitive markets. Also, some consumers may have rationally determined that the likely cost savings from switching do not outweigh the transactions costs of actively seeking out and acquiring the most suitable product in the market (AEMC 2007, p. 5).

Nonetheless, the Victorian Government, like the United Kingdom (box F.6), has moved to reduce the risks of ‘lock-in’ by requiring that small energy customers need give no more than 28 days notice before terminating a market contract.

Box F.6 The 28 day rule in the UK

In the UK, a major goal of policy is to prevent suppliers from creating high barriers to customer transfer through lock-in contracts and high early termination charges. At one level, this goal is pursued through regulation that allows consumers to exit any contract with only 28 days notice. Depending upon the agreed term of the contract, this may require payment of a ‘reasonable’ termination charge.

More generally, provisions for dealing with unfair contract terms in the UK appear to be targeted at reducing the power that lock-in bestows on a business (Vickers 2003, pp. 16-17).

In consequence, rolling contracts — that are typically renewed if no party raises an objection — are a common feature of the UK energy market. Those UK retailers that do pursue fixed-term contracts usually offer fixed price guarantees, which can operate to share the cost savings of having a long term contractual relationship.

The consultation paper to the energy Retail Policy Working Group (box F.4) has recommended that a similar provision be implemented nationwide as part of the shift to a fully national framework for energy. In addition, in Victoria, early termination fees for energy supply contracts have recently been capped at \$25, an

³ Based on a small-scale survey of 100 households (ESCOSA 2006).

apparently ‘fair and reasonable’ estimate of damage resulting from a customer’s early termination (PIAC 2006). However, while such changes may encourage switching and greater beneficial competition for consumers, mandated lower termination charges may also increase the upfront charges faced by consumers (chapter 7, appendix D and Chris Field, sub. 102, pp. 5-6).

Policies to help vulnerable and disadvantaged consumers

Many Australian households experience greater difficulty paying for utility services (‘utilities stress’) than for other household requirements, reflecting the lumpy and uncertain nature of service bills and the predominance of credit as a purchasing method (figure F.2). These difficulties are chronic for some households, with for example, around 180 000 (or 5 per cent) of Victorian households alone in 2005-06 on ‘budget instalment plans’, which are offered to households facing problems in meeting gas or electricity payments (ESC 2006c, p. 24). In some jurisdictions, more than one in every 100 households is disconnected from electricity supply annually due to difficulty in making payments (table F.1). And around one in ten of the more than 100 000 complaints to the Telecommunications Industry Ombudsman about fixed and mobile phone services are about debt recovery and disconnection issues.

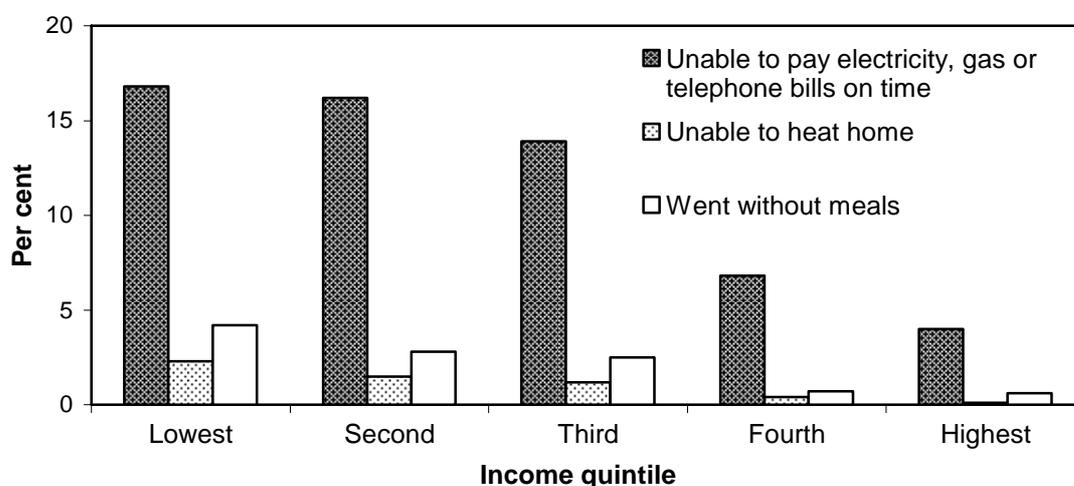
While low income is an important factor behind utilities stress, other household characteristics play a significant independent role, such as youth, private renting and disability (Debt Spiral Reference Group 2004, p. 58). For example, for a given level of income and other characteristics, a household with people aged 15-22 years has a nearly twenty-fold higher risk of utilities stress than one with people over 75 years old, suggesting that inexperience and other financial commitments play a significant role in such stress.

Utilities stress is not just important because of the risks of disconnection, but because of its wider effects on consumers. In particular:

- Debts as little as \$100 incurred as part of a utilities contract may be listed for payment default, affecting broader access to credit. The number of non-business default listings by the telecommunications industry continues to increase and is now double the number of listings by the financial services industry (ACMA 2005b).
- Obligations to pay for utility services are an important reason for difficulties in paying rent (Duggan and Sharam 2004, p. 28).

Given the adverse effects of utilities stress and the essential nature of the services concerned, several policy approaches are used to address hardship.

Figure F.2 Financial stress and household income



Data source: ABS Cat. no. 4159.0 General Social Survey: Summary Results, Australia, 2006a.

Direct financial hardship policies

There are many government-funded programs that directly target disadvantaged consumers facing difficulties paying for utility services. In Victoria alone, concessional expenditure by the government for low income and disadvantaged consumers was about \$90 million in 2005-06 (ESC 2006c).

A common policy mechanism is direct rebates paid by governments to disadvantaged consumers. For example, in the ACT, qualifying households are eligible for a rebate on their utility expenses of 10 per cent for electricity and 6.5 per cent for water, while there is a rebate of around \$30 per quarter in New South Wales and Queensland.

Various other measures offer temporary assistance, such as Utility Relief Grants (Victoria) and vouchers offered through the NSW Government's Energy Account Payment Assistance program. The latter are distributed by endorsed community welfare organisations, taking account of the specific circumstances of each consumer, illustrating the flexibility of targeted approaches.

Suppliers also have hardship programs, which vary by jurisdiction, industry and supplier (box F.7). In some jurisdictions, suppliers' obligations to provide hardship programs have been formalised by industry codes governing the delivery of retail services to low-income customers.⁴ Victoria, in particular, has more stringent requirements for energy retailers to implement hardship programs than other jurisdictions, including statutorily-mandated payments by suppliers to customers for wrongful disconnection.

⁴ See AER (2007) and ACMA (2006), describing energy and telecommunications codes respectively.

Box F.7 **Company hardship programs**

While binding codes sometimes force suppliers to provide what amount to implicit subsidies to disadvantaged consumers, the main role of suppliers is to identify consumers facing problems; provide information about solutions; refer them to counselling services and government assistance; and, above all, to provide methods that allow them to meet debts in an orderly way. The latter is achieved through late payment waivers, pre-paid options and instalment plans that provide additional time to pay outstanding debts.

As well as helping consumers facing hardship, there are incentives for suppliers to run these programs. In particular, they help suppliers to:

- recoup some payment in situations where a customer is simply unable to pay immediately rather than unwilling to pay, thus reducing costs of debt collection; and
- identify potential problem customers and apply preventative measures before substantial debts arise.

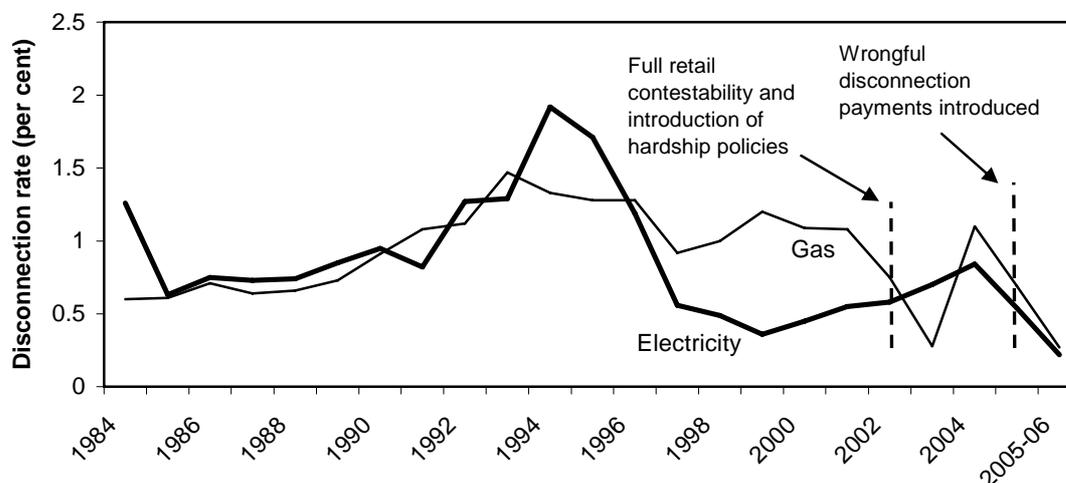
However, suppliers argue that the role of hardship programs is temporary assistance and that government-funded social programs should be used to provide longer term help (ERAA 2005).

Sources: ANZEWON sub. 64, pp. 7, 25. Financial and Consumer Rights Council Victoria, Committee of Inquiry into Financial Hardship of Energy Consumers, Submission, June 2005.

Assessing the impacts of varying hardship policies is difficult because so many other factors play a role in determining the extent and nature of hardship, including general economic conditions and the transition to full retail contestability. For instance, it took some time after the introduction of full retail contestability in Victoria for new entrants to achieve disconnection rates roughly on par with established suppliers (ESC 2006c, pp. 25, 50). Nevertheless, while it is hard to disentangle the impacts of supplier hardship programs from such influences, they are generally regarded as having been successful in helping disadvantaged consumers. In Victoria, which has the strictest hardship regime, disconnection rates are below the lowest levels achieved under government monopoly ownership and are lower than any other Australian state. They have also fallen more than in any other jurisdiction in the past few years (AER 2007, p. 195; figure F.3).

However, while such hardship policies are seen as effective and appropriate by most stakeholders, including suppliers, the more prescriptive approaches may impose compliance burdens on industry, which, in turn, are paid for by consumers. For instance, some applications of the wrongful disconnection law in Victoria have imposed high statutory penalty payments for what amount to technical violations, rather than substantive breaches of ‘good faith’. The Victorian Essential Services Commission has observed that it does not have the discretion to vary statutory payments in these cases (ESC 2007a).

Figure F.3 Energy disconnection rates in Victoria
1984 to 2005-06



Data source: ESC 2006c.

Moreover, while often regarded as the best regime from a consumer's immediate perspective, some suppliers have criticised the Victorian arrangements for the indirect costs they impose on business and ultimately consumers. For example:

Victoria is universally acknowledged as imposing the most onerous and costly regulatory framework in Australia. ... Victoria has three times the number of pages of regulation as Queensland, the most recent and efficient regulatory framework established. As an example, credit management obligations are imposed in other jurisdictions through a single regulatory instrument, such as the Retail Code. By contrast, credit management obligations in Victoria are detailed in the Retail Code, as well as in Guideline 1/4 – Credit Assessment, Wrongful Disconnection Operating Procedures, and Guideline 21 - Energy Retailers' Financial Hardship Policies. ... Assuming Queensland represents best practice, the additional cost of the Victorian regime is \$6.84 per account, based on a total cost-to-serve estimate of \$95 per customer. Across 4 million customer accounts (gas & electricity) the additional cost in Victoria is \$27 million per annum. (TruEnergy 2007, p. 5)

Future implementation of a national consumer protection regime for energy (chapter 5) would provide an opportunity to assess the most appropriate tradeoff between regulatory burdens from hardship policies and effective consumer protection.

Retail price regulations

Retail price regulations apply to some utility services to limit the possible misuse of market power in specific segments of the retail market, and to provide a 'safety net'

in the move to a fully contestable retail market.⁵ Such regulations established ‘default’ products that are supplied according to standard terms and conditions and at approved retail prices. In part, this price regulation has helped to address concerns about those consumers who, by virtue of their disadvantage or the perception that they are unprofitable to serve (for example, low-use or remote customers), may not switch services or providers to access the full benefits of retail competition (AEMC 2007, p. 10).⁶

But, rather than being a permanent feature of supply arrangements, it was planned that price regulations be retained only for a transitional period following deregulation of retail supply, subject to timetabled review and removal once effective contestability had been established. Specifically, under the Australian Energy Market Agreement, Australian Governments have agreed to phase out retail price regulation where effective retail competition is demonstrated. A process of reviews (by the AEMC) has recently commenced to establish the effectiveness of competition — the first completed in late 2007 for Victoria and another to commence shortly in South Australia.

Some regulations applying to retail gas services have already been removed — such as those previously applying in Tasmania, the Northern Territory and the ACT. However, price regulations remain widespread in telecommunications and electricity. As noted above, such regulations are imposed on a ‘default’ basic product, with customers able to opt-out by switching to alternative competing products offered by the incumbent supplier or its competitors.⁷

The preservation of the price regulated default option even in a contestable market is often strongly supported by consumer and social advocacy groups because it may help some consumers (Victorian Council of Social Service 2007). It is conceivable, for instance, that were there no control in place, consumers who have a low propensity to switch could face higher prices. Indeed, with different types of consumers and differentiated products,⁸ a fully de-regulated market will almost always lead to variations in prices across groups of consumers and this could make

⁵ Retail price regulation should be distinguished from regulated network access prices that help non-incumbent firms to compete in downstream markets. In contrast to retail price regulations, these are intended to be an ongoing feature of the market environment.

⁶ Although, separate to price controls, retaining an ‘obligation to supply’ on ‘host retailers’ also helps to address these access-related concerns.

⁷ In telecommunications, retail price controls are only applied to Telstra, but these indirectly influence prices set by other service providers (ACCC, sub. DR176, p. 7)

⁸ Products are differentiated by a variety of factors, including brand presence and reputation, payment methods (direct debit, credit, pre-payment); consumption quantity; market location (regional, urban); timing of use (peak, off-peak, point-of-time); and energy type (gas, electricity, green power etc).

some households worse off. For example, the UK experience following complete price deregulation of electricity suggests that the incumbent exploited some (residual) market power in respect of captive non-switchers, who generally had below average incomes (Salies and Price 2004).⁹

Though clearly having distributional impacts, this alone, does not justify the retention of retail price regulations, especially since they are a blunt tool for helping vulnerable and disadvantaged consumers — the main intended beneficiaries. For instance, price regulations cannot deal flexibly with the particular type, extent and duration of hardship a disadvantaged consumer may face. Also, many customers of the regulated default product are not in the disadvantaged target group. Because of their poor targeting and other inefficiencies, regulated prices are not usually employed in other consumer areas where financial hardship may result in detrimental under-consumption (such as food or housing).

In contrast, policies that directly seek to alleviate hardship (see earlier) can be more flexibly targeted and transparently paid for by governments, and can generally avoid the adverse efficiency and perverse effects of retail price regulations (see below).

Moreover, retail price regulations lose their beneficial role for consumers as a whole once effective retail contestability is in place, and with it, their economic rationale (PC 2005b, Ofgem 2003, ESAA 2007). In fully contestable markets, it is reasonably easy for retailers to enter the market and consumers are generally able to switch suppliers. Accordingly, the scope for host retailers to exercise market power and maintain prices significantly above costs would be small. Indeed, there are risks that maintaining retail price regulations in such an environment may have unintended impacts:

- Overly stringent price controls may adversely affect the longer term supply of the services concerned. (The most extreme manifestation of this sort of outcome were the interruptions to electricity supply in California in 2000 and 2001.)
- Price regulated, default contracts can have the appearance of being a signal by government that the default product is a ‘good deal’. This can penalise non-switchers, some of whom will be vulnerable and disadvantaged consumers, since default products are usually more expensive (or lower quality) than those offered under market contracts. For example, it has been estimated that South Australian consumers have the potential to reap average savings of around 9 per cent in transferring from a standing (price regulated) contract to an electricity market contract (ESCOSA 2006). Similar savings are apparent in the Victorian energy market (AEMC 2007, p. 54).

⁹ More recently, however, it has been found that price differences in the UK have reduced as competition continues to develop and the share of non-switching customers continues to shrink (Ofgem 2007).

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- It is difficult to design price regulations that can provide for the flexibility needed to facilitate interval metering or other demand-management initiatives, thereby denying access to the benefits that the use of such technology could otherwise deliver. For example, it may be possible to avoid building new generators by switching demand to non-peak periods when existing generator capacity is sufficient. This would have environmental and economic efficiency dividends. However, it requires that retail prices vary sharply with peak load demands, which retail price regulations may stymie. (There may be other regulatory issues associated with interval metering — such as the risks of very large bills for some consumers if they are inadequately informed about high peak prices — but these concerns will not usually be dealt with effectively using price regulation.)

Hence, as outlined in chapter 5, once utility markets are fully contestable, there is little reason not to give effect to the intended abolition of retail price regulations, with the needs of disadvantaged consumers then addressed through targeted CSOs and company provided hardship programs.

Dispute resolution processes and enforcement

Ombudsmen and company-based dispute procedures are the key mechanism for problem resolution in utilities. In particular, they provide a cost-effective avenue for the resolution of lower-value disputes that might otherwise go uncontested.

Company complaint handling systems

Australian governments mandate effective internal complaint handling schemes for energy and telecommunications suppliers. Such schemes can act as an initial cheap remedy for resolving consumers' difficulties (ESCOSA 2006, Standards Australia 2006), can reduce burdens on more resource-intensive external complaint handling schemes and on regulators, and sometimes act as a way of reporting suppliers' potential statutory breaches to regulators (for example, as in energy in Victoria; ESC 2007b). The telecommunications Complaint Handling Code (now existing within the consolidated Telecommunications Consumer Protection Code) is illustrative of mandated arrangements. It requires that 'reliable, easy to access' complaint processes are available to consumers regardless of language background, and stipulates various time limits on responses and a variety of other procedural requirements.

The relatively low numbers of complaint enquiries to energy and water ombudsmen and the high resolution rate of complaints to ombudsmen that are referred back to retailers, supports the view that, in most cases, the internal complaint handling

systems of energy retailers are working well. Indeed, the Energy and Water Ombudsman of NSW has attributed a decrease in complaint enquiries to an increase in the effectiveness of retailers' internal complaint handling processes (EWON 2006, p. 10). Only a few major difficulties have been evident and these have been satisfactorily resolved. For example, in 2006, IPART issued an enforceable undertaking on an energy retailer (Jackgreen) because the company did not have an effective internal complaint handling system. Jackgreen amended their system, avoiding further enforcement actions.

In contrast, the TIO (2006b) and Allen Consulting Group (2006 p. 3) noted more systemic concerns about compliance with the telecommunications Complaint Handling Code, with 40 per cent of all code breaches investigated by the TIO concerning complaint handling. There is also a concern that there are duplicated costs associated with various Australian Communications Industry Forum codes (ACIF 2005a, p. 12).

Ombudsmen schemes

To be effective, utilities ombudsmen schemes must:

- be efficient, readily accessible and well known;
- avoid any obvious gaps or ambiguities in the type of complaint they address, and adapt to technological and market changes; and
- be adequately resourced and skilled.

The view of the Commission and of most participants who commented on the matter (box F.2) is that these criteria are largely fulfilled by existing services. Nonetheless, some issues have arisen:

- Complaint resolution times have been increasing (TIO 2006b). However, this is not necessarily a problem if it reflects the additional time it takes to deal with a growing number of complex complaints.
- Disadvantaged consumers are often less likely to use and be aware of their options for dispute resolution.
- The evolution of national markets in some utility areas may provide an argument for consolidation of, or more formal networking between, State ombudsmen offices. Also, the range of utility services is growing, raising the question of how dispute mechanisms for these new services should fit into the current arrangements. In particular:
 - Jurisdictionally based energy (and water) ombudsmen do not use consistent reporting frameworks to assess their performance, nor is there a consistent

approach used to assess the merits of incoming cases.

- The caseload and resourcing requirements of state ombudsmen offices varies significantly, with bigger states generally having scale advantages.

Possible solutions to these issues are discussed in chapter 9 of the report.

Broader enforcement

The effectiveness of utilities' ombudsmen schemes and retailers' internal complaint handling systems will, among other things, hinge on the effectiveness of broader enforcement and the incentives it provides for appropriate supplier behaviour.

Effective broader enforcement requires reliable information on compliance, and following that, a suitable and effective range of remedies. Compliance monitoring in the utilities sector variously refers to the evidence from ombudsmen and complaints; compliance audits (mandated under licences); and a range of other sources such as media reports. If non-compliance is detected, a range of responses are available, including administrative actions that focus on cooperation and agreement, through to statutory enforcement orders, penalties, or revoking the service provider's licence. An enforcement response generally considers the history of the business; whether there was any intent or knowledge surrounding the instance of the contravention; and whether the provider attempted to rectify the problem and prevent any subsequent contravention.

In most cases, regulators tend to focus their enforcement efforts on non-compliance that might affect market confidence — such as the perceived risk from switching — while also giving particular attention to the needs of disadvantaged consumers.

- In telecommunications, since 1997 only two enforcement notices have been issued by ACMA for the breach of registered codes, and no subsequent action was determined necessary in either case. While the TIO (sub. 97, p. 2) and some other participants pointed to scope to improve enforcement of these codes, the key deficiency may be the codes themselves rather than their enforcement. Recently, however, a new Telecommunications Consumer Protection Code has been developed to replace six separate Codes. It is intended that this single and improved Code will clarify the rights of consumers, while allowing greater scope for providers to comply flexibly with their obligations.
- Optus (2005) has noted that enforcement activity in telecommunications tends to focus disproportionately on the major players, which may result in uneven compliance by retailers and a false sense of comfort for some consumers. Complaints to the TIO show relatively worse compliance by minor players in the

industry. In particular, some second-tier Internet service providers have experienced large numbers of complaints as a proportion of their customer share.

- In energy, the focus has been on marketing conduct and company hardship policies. Poor compliance has been identified mainly among smaller and second tier energy retailers — though it is recognised that scale effects will influence the particular approach of retailers to implementing minimum hardship provisions (ESC 2006b).

As companies continue to institute better processes and gain experience, regulators have seen it as sufficient, for the time being at least, to strengthen compliance monitoring and better educate providers, rather than to revoke licenses or introduce more prescriptive regulations.

G Occupational licensing

Key points

- State and Territory Governments collectively license nearly 100 occupations for consumer protection reasons.
- There are significant differences in the range of occupations licensed in individual jurisdictions.
 - Over one-third are licensed in only one or two jurisdictions.
 - Only 26 occupations are licensed by all jurisdictions.
- More than 30 of these licensing regimes were assessed by the National Competition Council as not complying with national competition policy principles.

In order to understand the contribution of occupational licensing to consumer policy in Australia, the Commission undertook a desktop analysis of licensing/registration regimes in the states and territories. The jurisdictions were requested to confirm the accuracy of the information; the resulting lists are reported in table G.1 below.

In reading the table, it is important to note the following:

- The table relates to ‘consumer-related’ licensing regimes — that is, where the overarching aim of the regulation is to improve consumer protection. As such, licensing regimes with different objectives, commonly relating to occupational health and safety, are omitted.
- As one of the main aims of this table is to identify inconsistencies in occupational licensing across jurisdictions, licensing regimes administered by the Australian Government have been omitted.
- There can be ambiguity in the distinction between occupational and business licensing requirements. For example, while the registration schemes for various activities such as introduction agents and motor car traders are based on proprietorships, they provide for assessment of individuals on the basis of personal character.
- There is not necessarily consistency across jurisdictions in the title given to an occupation/set of licensed activities. For example, some jurisdictions register

legal practitioners, while others register barristers or solicitors or both. The Commission has attempted to group those occupations that appear the same.

- All jurisdictions require the licensing of building practitioners who contract directly with consumers; in the following table this is captured in the ‘Builder’ row. Only two jurisdictions require licensing of building practitioners regardless of whether they contract directly with consumers or act as sub-contractors; this is captured in the rows relating to individual building-related trades.
- In February 2006, COAG requested Senior Officials to implement full and effective mutual recognition of occupational licences for six priority trades (electricians, plumbers, carpenters and joiners, bricklayers, refrigeration and air-conditioning mechanics and motor mechanics) by 30 June 2007. In March 2008, COAG announced that all other vocationally trained licensed occupations would have mutual recognition by September 2008.
- In March 2008, COAG agreed that the nine medical and allied health occupations that require registration in all jurisdictions (chiropractor, dentist, medical practitioner, nurse, optometrist, osteopath, pharmacist, physiotherapist and psychologist) will be subject to a national registration scheme by July 2010. It is intended that other health-related occupations will subsequently be incorporated into this regime.

Given these caveats, the table should be used as a broad guide only.

Table G.1 Consumer-related licensing and registration

Occupation or business activity	Jurisdictions requiring licensing/ registration								NCP non-compliant ^a
	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	
Aboriginal health worker								✓	
Acupuncturist		✓				✓			
Architect	✓	✓	✓	✓	✓	✓	✓	✓	SA
Auctioneer	✓		✓	✓		✓	✓	✓	
Boxing/kickboxing/martial arts industry	✓	✓		✓	✓		✓		
Bricklayer	✓		✓		✓				
Builder	✓	✓	✓	✓	✓	✓	✓	✓	
Building designer		✓	✓			✓			
Building surveyor		✓	✓	✓		✓		✓	
Business agent	✓			✓			✓	✓	
Carpenter	✓		✓		✓				
Child care centre	✓	✓	✓	✓	✓	✓	✓	✓	NT
Chinese medicine practitioner/dispenser		✓							
Chiropractor	✓	✓	✓	✓	✓	✓	✓	✓	WA
Collectors agent (commercial)/fundraiser		✓			✓		✓		
Commercial and private agent	✓	✓	✓	✓	✓	✓		✓	WA
Concreter	✓		✓		✓				
Conveyancer/Conveyancing agent	✓	b	c	✓	✓	✓		✓	WA
Credit provider/finance broker ^d		✓		✓			✓		WA
Dental prosthetist		✓	✓	✓	✓	✓	✓		WA, ACT
Dental technician	✓		✓				✓		NSW, ACT

(Continued next page)

Table G.1 (continued)

Occupation or business activity	Jurisdictions requiring licensing/ registration								NCP non-compliant ^a
	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	
Dental therapist/hygienist		✓	✓			✓	✓		
Dentist	✓	✓	✓	✓	✓	✓	✓	✓	WA, SA
Diagnostic radiographer/sonographer	✓	✓	✓	✓	✓	✓		✓	
Electrical worker or contractor	✓	✓	✓	✓	✓	✓	✓	✓	
Employment agent				✓	✓		✓		WA, SA, ACT
Energy Assessor							✓		
Engineer (building industry)		✓				✓			
Entertainment industry agent/manager	✓								
Fencing contractor	✓	✓	✓		✓				
Firearms instructor		✓							
Firearms repairer				✓					
Floor finisher and coverer	✓		✓						
Gasfitter	✓	✓	✓	✓	✓	✓	✓	✓	Tas
Glazer	✓	✓	✓		✓				
Hairdresser				✓					WA
Hawker							✓		
Hire car service provider	✓	✓	✓			✓	✓		NSW
Hydraulic services designer		✓	✓						
Inbound tourism operator			✓						
Introduction agent		✓	✓						
Kitchen, bathroom, laundry installer	✓	✓	✓		✓				
Kit home supplier	✓								

(Continued next page)

Table G.1 (continued)

Occupation or business activity	Jurisdictions requiring licensing/ registration								NCP non-compliant ^a
	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	
Land valuer	✓		✓	✓		✓			
Legal practitioner	✓	✓	✓	✓	✓	✓	✓	✓	NSW, Vic, Qld, WA, SA, Tas, ACT, NT
Liquor seller	✓	✓	✓	✓	✓	✓	✓	✓	QLD, WA, SA, NT
Marine designer			✓						
Marine surveyor			✓						
Medical practitioner	✓	✓	✓	✓	✓	✓	✓	✓	
Metal fabricator	✓		✓		✓				
Motor vehicle dealer	✓	✓	✓	✓	✓	✓	✓	✓	
Motor vehicle driving instructor	✓	✓	✓	✓	✓	✓	✓	✓	
Motor vehicle repairer	✓			✓					
Nuclear medicine technologist	✓	✓	✓	✓	✓	✓		✓	
Nurse	✓	✓	✓	✓	✓	✓	✓	✓	WA
Occupational therapist			✓	✓	✓			✓	QLD, WA, SA
Optical dispenser	✓				✓				WA, SA
Optometrist	✓	✓	✓	✓	✓	✓	✓	✓	WA, SA
Osteopath	✓	✓	✓	✓	✓	✓	✓	✓	WA
Painter	✓		✓	✓					
Passive fire equipment installer					✓				
Pawn broker/second hand dealer	✓	✓	✓	✓			✓	✓	WA
Pharmacist	✓	✓	✓	✓	✓	✓	✓	✓	NSW, Vic, Qld, WA, SA, Tas, ACT, NT

(Continued next page)

Table G.1 (continued)

Occupation or business activity	Jurisdictions requiring licensing/ registration								NCP non-compliant ^a
	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	
Physiotherapist	✓	✓	✓	✓	✓	✓	✓	✓	WA
Plasterer	✓	✓	✓		✓				
Plumber or drainer	✓	✓	✓	✓	✓	✓	✓	✓	Tas
Plumbing plan certifier							✓		
Podiatrist/chiropracist	✓	✓	✓	✓	✓	✓	✓		WA
Professional engineer – chartered		✓	✓						
Property developer			✓						
Property inspector (pre-purchase)	✓								
Psychologist	✓	✓	✓	✓	✓	✓	✓	✓	WA, SA
Quantity surveyor	✓								
Radiation therapist	✓	✓	✓	✓	✓	✓		✓	
Real estate agent	✓	✓	✓	✓	✓	✓	✓	✓	Qld, WA, Tas
Refrigeration, airconditioning and mechanical service provider	✓	✓	✓	✓	✓	✓	✓	✓	
Rehabilitation provider						✓			
Roof tiler	✓	✓	✓		✓				
Security industry worker	✓	✓	✓	✓	✓	✓	✓	✓	
Shopfitter			✓						
Site classifier			✓						
Specialised contractor			✓						
Speech pathologist			✓						Qld
Steel fixer	✓		✓						

(Continued next page)

Table G.1 (continued)

Occupation or business activity	Jurisdictions requiring licensing/ registration								NCP non-compliant ^a
	NSW	Vic	Qld	WA	SA	Tas	ACT	NT	
Stone mason	✓		✓		✓				
Strata manager	✓								
Structural landscaper	✓		✓						
Surveyor (land/cadastral)	✓	✓	✓	✓	✓	✓	✓	✓	
Swimming pool and spa constructor	✓	✓	✓		✓		✓		
Taxi service provider	✓	✓	✓	✓	✓	✓	✓	✓	NSW, Qld, ACT, NT
Teacher (school)	✓	✓	✓	✓	✓	✓		✓	
Towing service provider	✓	✓	✓		✓			✓	SA
Travel agent	✓	✓	✓	✓	✓	✓	✓	✓	Vic, WA, ACT
Venue consultant	✓								
Veterinary surgeon	✓	✓	✓	✓	✓	✓	✓	✓	NSW, WA, ACT
Wall and floor tiler	✓	✓	✓		✓				
Waterproofing applicator	✓	✓	✓		✓				
Wool, hide and skin dealer	✓								

^a 2005 NCP assessment (NCC 2005). ^b Legislation establishing a licensing scheme for conveyancers in Victoria was enacted in 2006, and the scheme is expected to begin operation during 2008. ^c Queensland does not allow non-lawyers to undertake conveyancing. ^d In New South Wales, Queensland, South Australia and the Northern Territory, credit providers can be banned from the industry, but there are no formal licensing or registration requirements.

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