



**Submission by CHOICE
to the Productivity Commission
Review of Consumer Policy Framework**

February 2008



CHOICE is a not-for-profit, non-government, non-party-political organisation established in 1959. CHOICE works to improve the lives of consumers by taking on the issues that matter to them. We arm consumers with the information to make confident choices and campaign for change when markets or regulation fails consumers.

CHOICE is independent: we do not receive ongoing funding or advertising revenue from any commercial, government or other organisation. With over 200,000 subscribers to our information products, we are the largest consumer organisation in Australia. We earn the money to buy all the products we test and support our campaigns through the sale of our own products and services.

Our policy voice is widely recognised. We campaign on key consumer issues based on research into consumers' experiences and opinions and the benefit or detriment they face. Our current campaigns cover food, health, financial services, product safety, communications and consumer protection law.

CHOICE conducts research, publishes policy reports and online information, gives presentations and keeps the media informed of our policy views. We provide representatives for many industry and government committees and independent bodies considering matters of concern to consumers.

To find out more about CHOICE's campaign work visit www.choice.com.au/campaigns and subscribe to CHOICE Campaigns Update at www.choice.com.au/ccu.



Introduction

The Productivity Commission's draft report is a significant milestone in the reform of Australia's Consumer Policy Framework and the laws and institutions that govern consumer policy. CHOICE particularly welcomes proposals to deliver:

Nationally coherent consumer law and policy

- Introduce a nationally consistent generic consumer law (Draft Recommendation 4.1),
- Establish objectives and principles for consumer policy (DR 3.1),
- Transfer regulation and enforcement of consumer credit and product safety to the Commonwealth and reform the regulation of credit brokers (DR 5.2) and similarly raise the responsibility for product safety regulation to the Commonwealth (DR 4.3)
- Introduce unfair contract terms legislation (DR 7.1) (See below for comments about how the proposed unfair contracts legislation could be improve).

Stronger enforcement powers and better redress mechanisms

- Provide new enforcement powers to consumer protection regulators, namely the right to seek civil pecuniary penalties, to apply to a court to ban an individual from specific activities, and to issue substantiation notices to traders (DR 10.1),
- Require regulators to report on enforcement problems and their response (DR 10.3),
- Remove impediments for regulators to take representative actions (DR 9.5) and
- Improve ways for consumers to access remedies for breaches of consumer law through better external dispute resolution (DR 9.2), and improved consumer claims procedures (DR 9.3),
- Increased funding for financial counselling and legal aid in consumer matters (DR 9.6).

Home Building

- Ensure consumers having a home built or renovated have improved and uniform protection (5.5)

Improve product safety regulation

- Implement the recommendations of the PC's Report on consumer product safety and review the impact of the recent civil liability reforms in this area (DR 8.2, 8.3)

Removal of unnecessary regulation

- Undertake a review and reform program for industry specific consumer regulation, in particular where it applies in only one or two jurisdictions (DR 5.1) (Although we note that there should not be a presumption that all such regulation is unnecessary)



Better institutions and consumer representation

- Increase consumer input into policy development and increase research into consumer markets (DR 11.3)

CHOICE welcomes the Commission's acknowledgement of the need to elevate the importance of consumer policy (DR 6.1), including through the establishment of a Ministerial portfolio combining competition policy and consumer affairs (already implemented by the Commonwealth Government), and the effective coordination of areas of government policy development that impact on consumers (including health, telecommunications, food and energy policy). CHOICE supports recommendations designed to ensure successful implementation of a more national approach (DR 4.4).

Areas for Improvement

CHOICE has also identified a series of recommendations that could be extended and/or modified to improve consumer policy and consumer market regulation. We have also identified some areas that require further work or consideration by the Productivity Commission and/or through subsequent industry or policy reviews. These are set out below.

Consumer Policy - Objectives and Principles

The Commission recommends the Government adopt objectives for consumer policy (DR 3.1) and suggests principles to flesh out those objectives. CHOICE supports the broad intent of the proposed objectives but proposes four modifications that will better focus for these objectives.

In the text of its report the Commission states that its primary benchmark is '**the well being of the community as a whole**' (Draft Report, Volume 2, p11). Like the Commission, CHOICE believes that consumer welfare should be placed at the centre of consumer policy. The proposed overarching objective does not do this but with a simple amendment could. 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

The Commission's proposed objective currently focuses on the "confident and informed participation of consumers in competitive markets". **Consumer confidence in markets** is essential to their effective operation. In light of the alternative overarching objective



proposed above, it would be appropriate to acknowledge consumer confidence in the operation objectives. The consumer policy framework should aim to:

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

The UK Government has also considered the issue of the objectives of consumer policy, and CHOICE believes that there are elements in the UK approach that would be beneficial in Australia. For example, it has acknowledged the role that consumer policy can play in delivering social justice, economic goals and environmental progress. We believe Australia’s consumer policy framework could learn from this approach. Specifically, we believe these aspects of the UK model could be adopted within the operational objectives:

Consumer rights are proportionate, balanced with responsibilities, and clear and simple enough to be well understood.

Consumers are able to understand the impacts of their own consumption decisions on our shared environmental and social wellbeing¹

Finally, despite devoting considerable discussion in the report to the field of behavioural economics and accepting that this knowledge may have a role to play in the design of consumer policy, the importance of **evidence about how consumers actually behave** is not to be found in the proposed operational objectives or supporting principles.

Barriers to effective competition

The Commission is to be commended for its identification and consideration of the way in which consumer markets actually work (Draft Report, Volume 2, Appendix B). It has considered important limitations on the effectiveness of markets in achieving the end goal of increased consumer welfare. It has described how some of those limitations arise from increased demand side barriers to competition including product complexity, conflicts of interest and behavioural biases. We would add that these issues are often more acute in markets for services – and services are taking a greater share of consumers’ ‘share of wallet’ over time.

These issues have proven to generate very significant problems for consumers in some Australian retail markets. The Commission has not fully explored the opportunities to increase consumer welfare through developing a more robust policy response to barriers to competition, in particularly demand side barriers.

Conflicts of Interest

¹ Department of Trade and Industry, *A Fair Deal for All: Extending Competitive Markets: Empowered Consumers, Successful Business*, 2005,



One area that deserves greater attention is the problems created by conflicts of interest in consumer markets. Conflicts of interest are of course not new, but they become more prevalent in markets characterised by intermediaries, such as health professionals, accounts, 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).

Conflicts of interest harm consumers. As an examples, conflicts of interest are structurally embedded into the retail financial services industry. This has had clear and demonstrable negative impacts on the quality of advice received by consumers (see, for example, the financial advisory industry “shadow shops” carried out by both CHOICE and ASIC over the last decade).

The policy response to conflicts of interest has overwhelmingly seen disclosure as the solution to market problems created by such conflicts, especially in financial services. However, disclosure has failed to have any significant impact on the extent of impact of these conflicts. Economic research is now providing some answers as to why disclosure is a poor tool for dealing with conflicts of interest. Research by Cain et al suggests that not only is disclosure ineffective, it may worsen the problems of conflicts of interest by exacerbating the tendency for both suppliers and consumers to underestimate the effect of such conflicts².

Another reason why disclosure is an inadequate solution to conflicts of interest in retail markets (especially more complex service markets) is that the information cannot be “actioned” by consumers. Disclosure of conflicts of interest essentially provides consumers with an opportunity to *discount* the value of the advice they are receiving. But how is a consumer to do this?

- Is the advice tainted by conflicts at all? If so, by how much should it be devalued?
- If the advice is about several financial products or several different types of medicine, should the value of that advice be discounted more if the upfront commission is high, or if there is an ongoing commission, or if the adviser is provided with office equipment by the supplier?
- Should the advice be discounted more if the adviser gets a bonus holiday for meeting a volume target? Or is a “buyer of last resort arrangement” likely to lead to lower quality advice?

These questions barely scratch the surface of the decision-making issues confronting a consumer dealing with conflicts or interest. On this point it is instructive to observe that in the financial services sector, while many websites have calculators that will allow a consumer to compute an exact figure for the impact of fees and charges on investments, there is no calculator on any website, including ASIC’s site, that allows a consumer to compute the discount factor for conflicts of interest.

² ‘Coming Clean but Playing Dirtier: The Shortcomings of Disclosure as a Solution to Conflicts of Interest,’ Daylian M Cain, George Loewenstein and Don A Moore in *Conflicts of Interest: Challenges and Solutions in Business, Law, Medicine and Public Policy*, edited by Moore, Cain, Loewenstein and Bazerman (Cambridge, 2005)



The result is ineffective regulation that imposes costs on industry while failing to address consumer problems. Hence the recommendation about yet another review of disclosure (DR11.1), while sensible if it improves basic product information, will not improve consumer outcomes in those markets that are characterised by significant conflicts of interest.

In the financial services industry, a significant step forward would be to start with a simple question – what market problems can disclosure fix? Until this question is honestly addressed we will continue to see reviews and reform processes for disclosure in financial services – all of them well intentioned and aiming for simpler disclosure documents – that have no meaningful impact on the quality of advice, the quality of products available to consumers, or the ultimate complexity of disclosure.

CHOICE believes that that Productivity Commission should recommend a review of the regulatory tools and approaches for dealing with conflicts of interest in complex service markets, particularly financial services. There appears at times, at the Commonwealth level, to be a policy preference for disclosure that is impervious to evidence of its limitations. The recognition of such limitations would represent an important opportunity to ‘refresh’ policy thinking.

Market Inquiries

One way of addressing such issues would be to allow regulators to formally undertake **market inquiries** in response to identified market problems, such as conflicts of interest, that do not respond to market forces or where competition is clearly not working. There should be powers that regulators can recommend or use in such inquiries so address these structural obstacles to competition on the demand and supply side (including outlawing specific practices that have anti-competitive effects in the studied market).

Unfair Contracts

CHOICE supports the Productivity Commission’s identification of the need for legislation to address unfair contract terms and we support elements of the proposed model (eg overall public benefit requirement, and see comments below about a safe harbour). However, we believe that there are some areas where the current proposal could be improved.

CHOICE, as stated in our original submission, favours an unfair contracts model based on the current Victorian legislation. In particular, we believe there is value in having the capacity to identify a term as ‘unfair’ prior to the identification of material detriment to consumers. This is good regulatory practice, as it allows risk-based, targeted, clearly communicated action, rather than always having “after the event” approaches. It facilitates an approach that allows cooperative and negotiated outcomes with suppliers, potentially before they have incurred significant costs. It would also be inefficient from a



regulatory perspective to require a regulator to wait before taking action in cases where contracts have been issued with terms that have clearly caused consumer detriment in the past by other suppliers.

The PC's proposal suggests that an unfair term 'would only be voided for the contracts of consumers subject to detriment'. In cases where losses have arisen, we are unclear whether this would require a regulatory agency to individually obtain the agreement of each consumer and individually assess the amount of detriment suffered by each consumer. This would be fundamentally impractical in most cases. Indeed the Commission has effectively recognised the limitations of similar current restrictions in the ability of regulators to take collective actions, and has hence recommended that regulators be allowed to take representative actions on behalf of consumers whether or not they are parties to the proceedings (DR 9.5). Of course such restrictions have a greater impact on consumers with lower education and literacy levels, who are less likely to be able to prepare well documented cases for loss or damage. We therefore suggest that the Productivity Commission clarify that such limitations not apply in the case of unfair contracts.

We could support some version of a "safe harbour" provision if it operated in similar ways to current applications from businesses or industry sectors for "relief" from aspects of the law in special circumstances and where a public benefit test was met. Industry organisations and/or individual firms can currently apply for relief from various provisions of the TPA or Corporations Law as long as this is not inconsistent with policy objectives and the broader public interest. Key regulators such as ASIC and the ACCC have extensive experience in dealing with these types of requests, and consulting with stakeholders where necessary. It is important the regulatory agencies are able to exercise such flexibility and discretion (as long as processes for making such decisions are consistent and fair), as no law can foresee all market circumstances.

Consumer policy development

CHOICE believes that the Commission could do more to guide government by proposing a consumer strategy over a period of perhaps 5 years. Such a strategy – based on the objectives and principles articulated by the Commission amended in the way we have suggested – would provide clear direction and milestones to those charged with implementing the Commission's recommendations.

Independent research and advice

A focus on evidence-based policy requires a realistic strategy to ensure that the relevant evidence is obtained and taken into account. The Commission's recognition of the value of consumer advocacy and the role of government funding to support it is appropriate. But the Commission's proposal for a program of contestable research funding will not be adequate to obtain the evidence nor ensure that it is given due weight in policy formation.



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. We believe part of the total of funds available for research should be allocated to a standing consumer policy research and advisory body which would have some similarities to the UK National Consumer Council which has worked very effectively under the Labour government in the UK.

In addition to efficiency considerations, the primary advantage of an independent standing body is that it can play an important accountability role through monitoring the effectiveness of consumer policy over time, including by commenting on Departmental proposals. It will also develop necessary expertise and corporate knowledge which would be dissipated in a purely contestable model. Funds above and beyond that necessary for the suggested research and advisory body could be allocated on a contestable basis (possibly by that advisory body.)

Our preference would be for a statutory body to undertake that role. However, we also recognise that, with additional resourcing and significantly improved secretariat support, the Commonwealth Consumer Affairs Advisory Committee (CCAAC) could be an alternative location for advising on major consumers issues, including a consumer policy research agenda. CCAAC could also directly commission and provide oversight for some consumer policy research projects. A review of the process through which members are appointed to CCAAC would need to be undertaken if it was to play this role.

Coordination across government

The importance of ensuring that all relevant government policy development processes give due weight to good consumer policy is in effect recognised by the Commission: “consistency in approaches within a government is just as important as between levels of government” (section 6.1, p 105). The Commission proposes in Draft Recommendation 6.1 that the Commonwealth ‘put in place arrangements to promote effective coordination of across other areas of government with responsibilities in the consumer policy area.’

In our view the Commission could do more to spell out the areas that need such coordination and the ways in which it could be ensured. While the detail will ultimately need to be left to government, the current recommendation is imprecise. It will be difficult to assess whether it has been successfully implemented – there may be a tendency to do the minimum possible. As we noted in our original submission to the Review:

There is no consistent approach to consumer policy between industries. Consumers face the same kinds of issues across service based industries as diverse as health, food, financial services, communications, and energy. But because the regulatory structures are in silos, different approaches are taken for no good reason.

One additional reason for recommending a formal policy advisory body would be to monitor the extent to policy development in any particular consumer market is failing to



have regard to good practice and draw attention to those failings. It would act as a counterweight to the inevitable tendency of industry specific regulators and policy departments to place greater weight on the interests of the regulated industry than the affected consumers.

An implementation plan

CHOICE believes that the Commission could do more to guide government by proposing a consumer strategy over a period of perhaps 5 years. Such a strategy – based on the objectives and principles articulated by the Commission amended in the way we have suggested – would provide clear direction and milestones to those charged with implementing the Commissions recommendations.

Whether or not the Commission does so, it will be necessary for government to adopt a clear implementation plan. Given the complex proposed changes to the balance of Commonwealth and State responsibilities this plan will need to be approved by COAG. A taskforce to oversee the transition should be established which should report to COAG on a regular basis.

An ongoing work program

The Commission has chosen to comment on a small number of specific industries and areas of consumer policy. In some cases it has recommended particular changes, for example a re-vamping of compulsory home building warranty insurance (DR 5.5). On others it has proposed that further reviews are undertaken, for example in relation to streamlining current industry specific arrangements (DR 5.1). It would of course be unrealistic to expect that the Commission could within the time and resources available for the current inquiry address all outstanding policy issues. It would however be useful for the Commission to propose a program of work to be undertaken during the transition phase and under the new arrangements. In this submission we identify what we believe are the issues to place on such a work program.

CHOICE believes that consumer policy around the food industry requires substantial review. There are a mix of sometimes conflicting objectives, unclear federal and state based regulation and regulators, and serious consumer issues (eg food labelling, obesity) that require consideration. We believe that the Productivity Commission should recommend that the consumer policy framework within the food industry be reviewed as a matter of urgency.

Super-Complaints

In its initial submission to this Review, CHOICE had argued that it was appropriate to adopt the UK model of super-complaints in Australia. Super-complaints are made by designated consumer bodies to the consumer regulator, who must make a considered response within 90 days to properly investigated complaints.



The Commission has raised the following objections to a super-complaints model in Australia;

1. Consumers already have sufficient avenues of complaint.
2. There is sufficient information available about consumer problems.
3. Consumer problems are appropriately prioritized.
4. The relatively small size of the Australian economy is a practical limitation.

The super-complaint mechanism is not intended for complaints about matters that can be handled directly by existing enforcement powers, particularly single-firm conduct. In that regard super-complaints neither replace nor crowd-out standard complaint processes.

In the UK, super-complaints have been made on matters such as doorstep selling, dentistry services, aged care homes, payment protection insurance and most recently the Scottish legal profession. The super-complaint mechanism enables consumer groups to bring to the attention of the regulator market features harming the interests of consumers. Super-complaints are useful in circumstances where regulatory failure means the complaints process is insufficient to resolve the problem. Such complaints are not made lightly, and the system requires consumer organizations to put together evidence and material to support their concerns.

For example, over 30,000 consumer have downloaded a standard complaint letter (from CHOICE's website www.fairfees.com.au) to complain about unfair bank penalty fees. Many of those consumers have gone on to make complaints to the ombudsman, who refuses to resolve individual complaints. Despite the scale of the problem, no consumer regulator has been willing to investigate the matter. To date, public information and complaints about the problem have not resulted in action.

Super-complaints should not be seen skewing the prioritisation of the regulator's workload. It is another means of ensuring that analysis of demand side or consumer problems takes place as part of an effective competition regime

With regard to the relative size of the Australian economy, we do not believe that this would limit the effectiveness of the mechanism. Rather, the practical implication would mean that fewer organisations would be designated under the scheme.