

Who should pay for the new compensation scheme?

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All Australian Financial Complaints Authority (AFCA) members should pay for and be covered by the Compensation Scheme of Last Resort, except prudentially regulated entities given the higher level of regulation applied, according to The Fold Legal.

In an analysis on the scheme to be introduced by the Government by the end of the year, the law firm said voluntary members should be included in the scheme, otherwise there was less reassurance to consumers that determinations would be paid.

It said this would ensure unpaid decision made by AFCA were covered and did not penalise members unlikely to need the scheme.

The Government's proposal is that the scheme would compensate the consumer or small business if AFCA made a determination for compensation that was not paid. It was also considering if the scheme should provide compensation for unpaid court judgements or tribunal decisions.

The Government was also considering whether the scheme should have a narrow coverage and be restricted to financial advice failures.

“Alternatively, the scheme could cover distribution services (including the provision of financial advice and brokerage services), investment services (including services relating to investment in securities, managed investment schemes and derivatives) and/or credit provided to consumers and small businesses,” the analysis said.

“An argument for this is that there is evidence of unpaid compensation in all these areas, while an argument against is that it may not be clear to consumers whether the services they receive are covered.

“The broadest coverage would be to cover all AFCA members. This allows unexpected claims costs to be met by a wider range of members, while on the downside it would also cover prudentially regulated firms who are at low risk of not paying a determination.”

The analysis also questioned the Government's paper on the scheme on whether to cost the scheme at financial service class level.

“For example, the levy is determined by reference to the services a firm is authorised to provide, without reference to whether that firm actually provides the service, or how frequently it is provided, or if it has ever been provided non-compliantly,” it said.

“This would be simpler but the question is then whether to apply a levy for administrative costs evenly plus a levy based on the risk level of services provided by the firm.

For example, for the higher risk associated with providing personal advice. It notes that a risk based funding model may make it unaffordable for smaller financial firms and result in increased costs to consumers.”