

Review of the financial system external dispute resolution and complaints framework – Interim Report

Legal Aid NSW submission to EDR Review
Secretariat

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About Legal Aid NSW

The Legal Aid Commission of New South Wales (Legal Aid NSW) is an independent statutory body established under the *Legal Aid Commission Act 1979* (NSW) to provide legal assistance, with a particular focus on the needs of people who are socially and economically disadvantaged.

Legal Aid NSW provides information, community legal education, advice, minor assistance and representation, through a large in-house legal practice and private practitioners. Legal Aid NSW also funds a number of services provided by non-government organisations, including 32 community legal centres and 28 Women's Domestic Violence Court Advocacy Services.

Legal Aid NSW welcomes the opportunity to provide a further submission to the *Review of the financial system external dispute resolution and complaints framework* that is being undertaken by the EDR Review Secretariat.

The Legal Aid NSW Civil Law Division focuses on legal problems that impact most on disadvantaged communities, such as credit, debt, housing, employment, social security and access to essential social services. Consumer issues constitute the largest category of service for our Civil Law Division.

In 2014-15 Legal Aid NSW provided 4,887 in house advice and 5,477 minor

assistance services in consumer law matters. More than one quarter of these matters dealt with credit products, including consumer leases. This submission draws on the casework experience of civil law solicitors in providing these services.

This submission addresses the Draft Recommendations and the information requests raised in the Interim Report. In responding to these requests, we also refer to our previous submission to the review in October 2016. We follow the numbering of the chapters in the Interim Report in our submission.

Should you require any further information or wish to discuss this submission, our contact officers are:

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List of recommendations

1. The proposed Ombudsman scheme should retain the structure, approach and culture of Financial Ombudsman Service (**FOS**), with the Credit and Investments Ombudsman (**CIO**) being integrated into FOS.
2. To assist with the transition to one Ombudsman scheme:
 - a timeline for integrating the schemes should be established
 - both Ombudsman schemes should be located in the same office, and
 - both Ombudsman schemes should be established with the same corporate structure and systems.
3. The national consumer protection law should be extended to small businesses.
4. In the alternative, small business lenders should be required to be a member of EDR.
5. The Ombudsman schemes should have additional powers to:
 - compel documents
 - require mandatory discovery
 - award penalties higher than the consumer's loss
 - increase the current caps on compensation
 - award compensation from a statutory compensation scheme
 - make directions enforceable by injunctions, including requiring the trader to waive a debt or agree to a life interest.
6. Additional powers should be implemented through changes to the Ombudsman schemes' terms of reference, consultation with consumer advocates and education for traders and consumers.
7. Credit representatives should be required to maintain their membership of EDR, unless it is clarified that the credit licensee remains liable for the actions of the credit representative in the case of fraudulent or illegal activity.
8. ASIC should have the power to give directions about funding, governance, monetary limits, compliance with IDR requirements and periodic independent reviews.
9. ASIC should provide guidance about what constitutes a "complaint", common types of complaints, and when a complaint is considered to be "withdrawn" or "unresolved".
10. Financial firms should, at the very least, be required to report on:
 - the number of complaints received

- the type of complaint, and
- the outcome of the complaint, including if the complaint has been withdrawn or unresolved, particularly if it has been unresolved for a significant period of time.

11. ASIC should publish details of non-compliance or poor performance IDR, including identifying financial firms.

Draft Recommendations

Legal Aid NSW welcomes the Panel's findings in the Interim Report and strongly supports the Draft Recommendations. We provide below some comments about the Panel's proposed Ombudsman scheme.

Proposed Ombudsman scheme

One-Ombudsman scheme

Legal Aid NSW recommends that the one Ombudsman-based scheme be created by integrating the Credit and Investments Ombudsman (**CIO**) and the Superannuation Complaints Tribunal (**SCT**) into the Financial Ombudsman Service (**FOS**). Further detail supporting this position is outlined at p.34 of our October 2016 submission.

Should the Panel not agree with our reasoning and recommendation, we support Draft Recommendation 1, provided that the proposed Ombudsman scheme retains the structure, approach and culture of FOS, with CIO being integrated into FOS.

We note the Panel's comments that consideration should be given to further integrating the superannuation scheme and the financial systems scheme to create a single Ombudsman scheme for all financial system disputes in the future. To assist with this transition, we recommend that:

- a timeline for integrating the schemes be established
- both Ombudsman schemes be located in the same office, and
- both Ombudsman schemes be established with the same corporate structure and systems.

Banking tribunal not required

Legal Aid NSW supports the Panel's view that an additional statutory dispute resolution body in the form of a banking tribunal is not required. Further detail outlining this position is provided at p.40 of our October 2016 submission.

Recommendations

- **The proposed Ombudsman scheme should retain the structure, approach and culture of FOS, with CIO being integrated into FOS.**
- **To assist with the transition to one Ombudsman scheme:**
 - **a timeline for integrating the schemes should be established**
 - **both Ombudsman schemes should be located in the same office, and**
 - **both Ombudsman schemes should be established with the same corporate structure and systems.**

Chapter 5: Assessment of external dispute resolution framework

Should the national consumer protection law be extended to small businesses?

Yes, the national consumer protection law should be extended to small businesses. Legal Aid NSW assists consumers who are misled or pressured into signing up to a loan for business purposes. This occurs most frequently where the consumer has vulnerabilities, such as illiteracy or financial inexperience, or where the consumer is acting for the benefit of a loved one.

In these situations, it is difficult to pursue a remedy against the trader in EDR as the trader can argue that the national consumer protection law does not apply to loans taken out for business purposes. As a result, the consumer's only option is to resort to complex and costly litigation.

Case study: Mrs Fo

Mrs Fo is elderly, illiterate, and suffers from significant health issues. Mrs Fo agreed to guarantee her daughter's business loan, securing the loan with her house. Mrs Fo wanted to help her daughter "get along in life and not struggle" like she had. Review of the loan documents revealed that Mrs Fo was listed as the director of her daughter's company despite having had no participation in the business.

The daughter defaulted on her payments to the loan and the bank started the process to take possession of Mrs Fo's house. Her house had been specially fitted for her health issues and it would have caused Mrs Fo a great deal of hardship if she were to move out.

Legal Aid NSW raised a dispute about the loan, as it related to Mrs Fo, against the bank. We were required to make complex arguments that FOS should consider the matter, despite the loan being for business purposes. FOS determined the matter in the bank's favour for the reason, amongst others, that the loan was for business purposes. Legal Aid NSW escalated the matter to a senior contact at the bank. The bank ultimately agreed to give Mrs Fo a life interest in the property.

Case study: Mr and Mrs Ing

Mr and Mrs Ing are elderly pensioners who entered into a loan as co-borrowers, secured against their house, for the benefit of their son. Mrs Ing is illiterate and suffering from cancer.

The loan was an “investment loan”, but the son used the funds to purchase a residential property. Mr and Mrs Ing had an agreement with their son that he would make the repayments to the loan. When the son defaulted on the payments, the bank started the process to take possession of the Ings’ house.

Legal Aid NSW raised a dispute about the loan in FOS. The dispute process was lengthy as we were required to make complex legal arguments regarding the characterisation of the loan. The matter could not be resolved in FOS so we commenced proceedings in the Supreme Court. The matter ultimately settled in favour of the Ings, but they incurred legal costs in excess of \$50,000.

Recommendations

- **The national consumer protection law should be extended to small businesses.**
- **In the alternative, small business lenders should be required to be a member of EDR.**

Should schemes be provided with additional powers, and if so, what additional powers should be provided?

Yes. Legal Aid NSW supports the additional powers noted by the Panel in the Interim Report. We recommend that the Ombudsman schemes’ powers should be increased to allow them to:

- compel documents
- require mandatory discovery
- award penalties that are a multiple of any losses
- increase caps on expenses and non-financial loss
- award fair compensation for loss or damage, and
- make directions that firms take steps that are just and appropriate, enforceable by an injunction.

We provide below some comments about selected proposed powers.

Additional power: Mandatory discovery

A significant barrier to resolving disputes in EDR is the trader’s failure to provide documents. The current lack of power in EDR to compel documents means that there is no mechanism to force traders to comply with EDR directions, leaving consumers without access to evidence to pursue a remedy. We refer to the case study “Delay in resolving Danika’s complaint” at p.24 of our October 2016 submission for further detail. Providing

schemes with discovery powers and the ability to compel documents would increase the efficiency of dispute resolution and equity for consumers.

Additional power: Award penalties that are a multiple of any losses

Legal Aid NSW supports an increase in powers to award penalties that are a multiple of any loss to the consumer. We specifically support the increase in this power in relation to breaches of the responsible lending provisions. Allowing Ombudsman schemes to order penalties beyond the direct loss to the consumer will act as a greater deterrent to traders that engage in unlawful conduct. Further detail is provided at p.27 of our October 2016 submission.

Additional power: Increase caps on expenses and non-financial loss

The current caps on expenses and non-financial loss should be increased to allow schemes the power to award appropriate compensation to consumers.

The increase should reflect the increased value of the cost of financial products in Australia, including the cost of home loans and a rebuild on total loss insurance claims. Currently, the jurisdictional limit for FOS to hear general insurance matters is far below the cost of the average home in NSW. This means that average homeowners are precluded from EDR in the event that there is a total loss on their policy and their entire claim is in dispute. This may occur, for example, following a natural disaster when an insurer seeks to rely on a flood exclusion clause.

Any increase in caps should also reflect societal changes about the acceptable level of compensation for non-financial loss, for example, by referring to caps within the *Civil Liability Act 2002* (NSW) or the *Motor Accidents Compensation Act 1999* (NSW). Further detail can be found in the section below, and at p.25 of our October 2016 submission.

Additionally, the schemes' powers should be extended to award compensation through a statutory compensation scheme for losses to consumers that would otherwise go uncompensated. Further detail can be found at p.46 of our October 2016 submission.

Additional power: Make directions that firms take steps that are just and appropriate, enforceable by an injunction

We recommended at p.13 of our October 2016 submission that traders adopt a uniform definition of long-term financial hardship, and practices to address such hardship. We submit that the Ombudsman schemes should have the power to determine that debt be waived by the trader where the consumer is experiencing long-term financial hardship. Further detail can be found at p.27 of our October 2016 submission.

As the case study of Mrs Fo in the section above shows, in some situations a life interest in the property is a beneficial outcome for both consumer and trader. We submit that the schemes should have the power to determine that the trader agrees to a life interest in the property where it is reasonable in the circumstances.

How should any change in powers be implemented?

Any change in powers should be implemented into the terms of reference of that scheme and be accompanied by an education program for consumers and traders. Prior to any changes being made, the schemes should conduct a consultation process with consumer advocates.

Recommendations

- **The Ombudsman schemes should have additional powers to:**
 - **compel documents**
 - **require mandatory discovery**
 - **award penalties higher than the consumer's loss**
 - **increase the current caps on compensation**
 - **award compensation from a statutory compensation scheme**
 - **make directions enforceable by injunctions, including requiring the trader to waive a debt or agree to a life interest.**
- **Additional powers should be implemented through changes to the Ombudsman schemes' terms of reference, consultation with consumer advocates and education for traders and consumers.**

Does EDR scheme membership by credit representatives provide an additional or necessary layer of consumer protection that is not already met through the credit licensee's membership?

Legal Aid NSW submits that EDR scheme membership provides a necessary layer of consumer protection that is not met through the credit licensee's membership.

In our experience, it is not uncommon for a credit licensee to deny liability for the conduct of a credit representative. In particular, this occurs in situations where the credit licensee claims that the credit representative acted fraudulently or illegally. Under the current law, it is difficult to determine from sections 76(2) and 77 of the *National Consumer Credit Protection Act 2009* (Cth) the exact circumstances where a licensee is liable for the actions of a representative.

Where the credit licensee is able to successfully deny liability, consumers are required to pursue their claim against the credit representative. However, if the credit representative is no longer required to have EDR scheme membership, consumers would not have access to this forum, and would be required to commence proceedings in court to obtain a remedy.

We submit that removing the requirement for credit representatives to be a member of EDR could significantly decrease access to justice for consumers by creating an unnecessary carve out in protections for a specific group of consumers.

If it were clarified that a licensee remained liable for the actions of a credit representative in the case of fraudulent or illegal activity, Legal Aid NSW may support the change to the

EDR membership. However, if liability remains unclear, Legal Aid NSW recommends that credit representatives should be required to maintain their membership of EDR.

Recommendation

- **Credit representatives should be required to maintain their membership of EDR, unless it is clarified that the credit licensee remains liable for the actions of the credit representative in the case of fraudulent or illegal activity.**

Chapter 6: A future framework

What should be the monetary limits and compensation caps for the new scheme? Should they be different for small business disputes?

Legal Aid NSW supports an increase in the monetary limits and compensation caps to \$2 million for both consumers and small businesses. A uniform threshold would reduce confusion, improve consistency and simplify jurisdictional disputes for the scheme.

What principles should guide the levels at which the monetary limits and compensation caps are set?

The monetary limits and compensation caps need to keep pace with economic factors such as wage growth, home lending data, property price increases and total loss claim information. This would help ensure that the limits and caps are in line with the actual experience of consumers on an ongoing basis.

What indexation arrangements should apply to ensure the monetary limits and compensation caps remain fit-for-purpose?

Legal Aid NSW submits that the limits and caps should be regularly reviewed at an interval set by ASIC. This approach would allow ASIC to examine the actual economic circumstances of consumers, and adjust the limits and caps accordingly. We are concerned that benchmarking would not adequately ensure that these matters are considered in any changes to the caps and limits.

On what matters should ASIC have the power to give directions?

Legal Aid NSW submits that ASIC should have powers to give directions in relation to governance, funding and monetary limits. We also consider that ASIC should take a more active role in investigations of traders' compliance with IDR requirements. However, we note the Panel's comments about the strength of the existing co-regulatory approach between ASIC and the EDR schemes, and we agree that this approach should continue.

Funding

If ASIC is provided with the power to give directions about funding arrangements, the directions must be expressed transparently so that consumers can see where the funds are coming from and how they have been allocated.

Governance

We refer to our comments at p.27 of our October 2016 submission.

Monetary limits

We refer to our comments in the section above, and at p.25 of our October 2016 submission.

Oversight of IDR

We refer to our comments in the section below, and at p.16 of our October 2016 submission.

Periodic independent reviews

Legal Aid NSW supports regular reviews of EDR by ASIC. We consider that the reviews should be transparent and independent with the results, recommendations and compliance with the recommendations made public.

Recommendation

- **ASIC should have the power to give directions about funding, governance, monetary limits, compliance with IDR requirements and periodic independent reviews.**

What IDR metrics should financial firms be required to report on?

Legal Aid NSW strongly supports Draft Recommendation 9 that financial firms should be required to publish information and report to ASIC about their IDR activity. For this information to be comparable across the sector, firms must use consistent definitions when collating and reporting IDR data. To assist with this process, ASIC could prepare a guideline defining “complaint”, common types of complaints, and when a complaint is considered to be “withdrawn” or “unresolved”.

Legal Aid NSW submits that financial firms should, at the very least, be required to report on:

- the number of complaints received
- the type of complaint, and
- the outcome of the complaint, including if the complaint has been withdrawn or unresolved, particularly if it has been unresolved for a significant period of time.

Further detail is provided at p.16 of our October 2016 submission.

Should ASIC publish details of non-compliance or poor performance IDR, including identifying financial firms?

Yes, ASIC should publish details of non-compliance or poor performance IDR, including identifying financial firms.

Publishing this information may have significant benefits, including:

- increasing consumer awareness of IDR and empowering sophisticated consumers to advocate for themselves
- assisting consumers to make an informed choice when purchasing a financial product
- providing consumers with greater bargaining power when raising a dispute with a firm acting improperly, and
- encouraging improvement in IDR standards across the sector.

Recommendations

- **ASIC should provide guidance about what constitutes a “complaint”, common types of complaints, and when a complaint is considered to be “withdrawn” or “unresolved”.**
- **Financial firms should, at the very least, be required to report on:**
 - **the number of complaints received**
 - **the type of complaint, and**
 - **the outcome of the complaint, including if the complaint has been withdrawn or unresolved, particularly if it has been unresolved for a significant period of time.**
- **ASIC should publish details of non-compliance or poor performance IDR, including identifying financial firms.**