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Dear Professor Ramsay

Consultation on the establishment, merits and potential design of a compensation scheme of last resort and the merits and issues associated with providing access to redress for past disputes

The Association of Superannuation Funds of Australia (ASFA) is pleased to provide this submission in response to the Supplementary Issues Paper from the Review of the External Dispute Resolution Framework, titled *Consultation on the establishment, merits and potential design of a compensation scheme of last resort and the merits and issues associated with providing access to redress for past disputes*.

If you have any queries or comments in relation to the content of our submission, please contact me on (02) 8079 0808 or by email gmccrea@superannuation.asn.au, or Julia Stannard, Senior Policy Adviser, on (03) 9225 4027 or by email jstannard@superannuation.asn.au.

Yours sincerely

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Response to Supplementary Issues Paper: *Consultation on the establishment, merits and potential design of a compensation scheme of last resort and the merits and issues associated with providing access to redress for past disputes*

A. ABOUT ASFA

ASFA is a non-profit, non-political national organisation whose mission is to continuously improve the superannuation system so people can live in retirement with increasing prosperity. We focus on the issues that affect the entire superannuation system. Our membership, which includes corporate, public sector, industry and retail superannuation funds, plus self-managed superannuation funds and small APRA funds through its service provider membership, represent over 90 per cent of the 14.8 million Australians with superannuation.

B. EXECUTIVE SUMMARY

In relation to a proposed compensation scheme of last resort, ASFA:

- considers the current regime in Part 23 of the Superannuation Industry (Supervision) Act 1993 to be an appropriate and effective means of providing compensation for losses due to fraud or theft within the APRA-regulated superannuation sector
- sees no benefit in displacing Part 23 in favour of a generic compensation scheme of last resort
- does not support any proposed industry-wide compensation scheme that has the potential to involve cross-subsidisation by the APRA-regulated superannuation sector of losses incurred within other sectors.

Whilst sympathetic to the plight of consumers who have been unable to obtain redress for past disputes, ASFA has significant reservations about the proposal to introduce a scheme for redress. ASFA's concerns relate to:

- the difficulties of adequately addressing issues of moral hazard
- the inappropriateness of subjecting providers, particularly trustees of APRA-regulated superannuation funds, to unquantifiable and potentially open-ended liability in respect of past disputes
- the need for all stakeholders to have certainty, with clear timeframes and criteria applying to the resolution of financial system disputes, which mitigates against special rules for past disputes.

C. A COMPENSATION SCHEME OF LAST RESORT

C.1 General Comments

ASFA agrees that consumer confidence in financial services is adversely impacted when a consumer does not receive the compensation due to them in relation to a dispute with their provider. However, we note that cases of non-payment of determinations and other failures to compensate have not been experienced uniformly across the financial services industry, but have been primarily confined to particular sectors.

The Panel's Supplementary Issues Paper, *Consultation on the establishment, merits and potential design of a compensation scheme of last resort and the merits and issues associated with providing access to redress for past disputes* (Paper), notes that there was outstanding, as at 2 May 2017:

- $13,909,635.50 in determinations made in favour of complainants by the Financial Ombudsman Service (FOS), excluding interest
- $399,862 in determinations by the Credit and Investments Ombudsman (CIO), excluding interest[1].

[1] Review of the financial system external dispute resolution framework: *Consultation on the establishment, merits and potential design of a compensation scheme of last resort and the merits and issues associated with*

The Paper further reveals that the largest categories represented amongst those unpaid FOS determinations relate to:

- disputes relating to the provision of financial product advice
- disputes with operators of managed investment schemes
- disputes with credit providers[2].

The experience of the APRA-regulated superannuation sector, in respect of payment of determinations by the Superannuation Complaints Tribunal (SCT), is quite different. The Paper acknowledges (our emphasis):

> In the case of superannuation disputes, as at 2 May 2017, **the SCT had no outstanding unpaid determinations**. This is due to the nature of prudential regulation in the superannuation system, which means it would be **rare for a superannuation fund to be unable to pay its obligations**.[3]

ASFA concurs with the Review Panel's assessment. Trustees of APRA-regulated superannuation funds are subject to extensive legislative and prudential requirements as well as overarching fiduciary duties designed to ensure that funds are operated in the best interests of members.

Past instances of unpaid SCT determinations have been infrequent and quickly addressed. On those rare occasions where fraud or theft has occurred to such an extent that a fund's ability to benefits to members was jeopardised, these have been effectively addressed through the operation of the existing compensation scheme for APRA-regulated superannuation, Part 23 of the *Superannuation Industry (Supervision) Act 1993* (SIS Act) (see further our comments in part C.2 below). 'Phoenix' behaviour, which has been observed within the broader financial advice sector, has not been a concern in the APRA-regulated superannuation sector and is less likely, given the substantial regulatory barriers to securing registrable superannuation entity licensee status.

More specifically, the proposed compensation scheme raises the prospect of an adverse impact on the APRA-regulated superannuation sector. Depending on the design of the scheme, there would appear to be the potential that other sectors of the industry may incur costs in relation to a compensation scheme of last resort – whether through direct contribution toward a grant of compensation, or an indirect contribution toward funding the administration of the scheme (see further our comments in part C.3 below).

Further, we note that the occurrence of a failure or misconduct within a sector that is significant enough to trigger the proposed compensation scheme is likely to itself impact consumers' confidence not only in the particular sector impacted, but also potentially in the broader financial system.

ASFA does not support the introduction of any compensation scheme of last resort that involves the potential for APRA-regulated superannuation monies to be used, directly or indirectly, to cross-subsidise losses incurred in other sectors of the financial services industry.

providing access to redress for past disputes - Supplementary Issues Paper, May 2017 (Supplementary Issues Paper), paragraph 43

[2] Ibid., paragraph 94

[3] Ibid., paragraph 122

Rather than imposing a generic compensation scheme of last resort on the entire financial services industry, ASFA considers that consumer confidence might be more effectively supported by implementing measures directly targeted to those sectors where most issues are experienced.

In this respect, ASFA notes that Mr Richard St John, who during 2010-12 conducted an extensive inquiry of compensation arrangements in financial services, concluded that greater efforts were required to secure compliance by individual providers, before it would be appropriate to consider any compensation scheme of last resort. ASFA considers the following comments by Mr St John to be particularly apposite (our emphasis):

> I have concluded that it would be inappropriate, and possibly counter-productive, to introduce a more comprehensive last resort compensation scheme to underpin the current relatively light compensation regime for financial advisers and other providers of financial services. **Given the limited regulatory measures to protect retail clients from the risk of licensee insolvency, it would be inappropriate to require more responsible and financially secure licensees to underwrite the ability of other licensees to meet claims against them for compensation**. There would also be an element of regulatory moral hazard should a last resort scheme be introduced without a greater effort first to put licensees in a position where they can meet compensation claims from retail clients. It would reduce the incentive for stringent regulation or rigorous administration of the compensation arrangements.
>
> **Priority should be given**, in any move to bolster the protection of retail clients, **to a more rigorous approach to compliance by licensees to provide greater assurance that they will be in a position to compensate their own clients through their insurance arrangements and the capital resources they have at risk**.
>
> To put it another way, **the regulatory platform for financial advisers and other licensees needs to be made more robust and stable before a safety net, funded by all licensees, is suspended beneath it**. I see this as a necessary step **before further consideration is given to a scheme under which the cost of uncompensated claims against one firm would be passed on to other firms who are not so remiss**. This would be consistent too with the more robust regulatory approach to the providers of services elsewhere in the financial system, including prudential regulation, where last resort protection is offered to consumers.[4]

ASFA endorses the comments made by Mr St John and is of the view that efforts should be focussed on implementing the types of regulatory reforms he recommended. ASFA considers it premature to consider implementing, at this time, an industry-wide compensation scheme of last resort.

Rather than imposing a generic compensation scheme of last resort on the entire financial services industry, ASFA considers that consumer confidence might be more effectively supported by implementing measures directly targeted to those sectors where most issues are experienced.

[4] Richard St John, *Compensation arrangements for consumers of financial services*, April 2012, piii-iv

C.2 A compensation scheme already exists for APRA-regulated superannuation

As acknowledged in the Paper[5], the APRA-regulated superannuation sector already has in place arrangements which effectively provide a compensation scheme of last resort.

Part 23 of the SIS Act provides protection for members of a regulated superannuation fund (other than a self-managed superannuation fund or SMSF) or an approved deposit fund, where there has been a loss as a result of fraudulent conduct or theft, causing substantial diminution of the fund leading to difficulties in the payment of benefits.

Where an 'eligible loss' has been established, the Minister may approve a grant of financial assistance to the trustee of the impacted fund. The level of compensation provided is subject to the Minister's discretion, but has typically ranged between 90 and 100 per cent.

To date, Part 23 has been utilised only a handful of times since it was established in 1993, with levies raised in respect of the 2001-02, 2002-03, 2003-04, 2004-05, 2010-11 and 2012-13 years. These grants primarily relate to two main incidents of fraud or theft, affecting the members of superannuation funds formerly under the trusteeship of Commercial Nominees of Australia Limited and Trio Capital Limited. In each case, a levy has been raised on all APRA-regulated funds to recoup the amount of the grant initially provided by the Government – that is, the compensation provided has been entirely funded from within the APRA-regulated superannuation sector.

The operation of Part 23 has also been the subject of review[6] and refinement[7] to ensure that it operates effectively and appropriately.

The Part 23 regime does not provide full coverage for all losses resulting through fraud or theft through superannuation, and nor was it intended to. We refer the Panel to our comments in response to its Interim Report[8], explaining the rationale for exclusion of SMSFs and pooled superannuation trusts (PSTs) from Part 23, and why this remains appropriate today. In summary, however, we note that:

- Consumers are not able to invest *directly* in a PST. However, to the extent that a consumer has *indirect* exposure through an investment in a PST by the trustee of an APRA-regulated fund of which the consumer is a member, and the trustee incurs a loss due to fraud or theft involving that PST, the trustee's loss may be eligible for financial assistance under Part 23.
- The members of an SMSF are also its trustees, have direct control over their superannuation savings and are better placed than members of an APRA-regulated fund to protect their own interests.
    - SMSFs are not subject to the extensive and onerous prudential regulation, and many of the stringent requirements under the SIS Act 1993 and the SIS Regulations 1994, faced by APRA-regulated funds.
    - SMSFs pay a modest supervisory levy to the ATO, reflecting their reduced level of regulation, but are exempt from the levies raised from the APRA-regulated superannuation sector to recoup the financial assistance awarded under Part 23.

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[5] Ibid., paragraphs 71-72

[6] Superannuation Working Group: *Options for Improving the Safety of Superannuation - Background Issues*, December 2001

[7] Including by the *Superannuation (Financial Assistance Funding) Levy Amendment Act 2003*,*Financial Framework Legislation Amendment Act 2005*, and the *Financial Sector Legislation Amendment (Simplifying Regulation and Review) Act 2007*

[8] ASFA, *Response to Interim Report: Review of the Financial System External Dispute Resolution and Complaints Framework*, 27 January 2017 - see section 2.8.1

- As noted by Richard St John, the "degree of protection afforded … reflects the perceived intensity of the financial promises in question"[9].

ASFA is of the view that the Part 23 regime is an appropriate and effective means of providing compensation for losses due to fraud or theft within the APRA-regulated superannuation sector. We see no benefit in displacing Part 23 in favour of a generic compensation scheme of last resort.

C.3 APRA-regulated superannuation should be excluded from any industry-wide scheme

ASFA does not support any proposed industry-wide compensation scheme that has the potential to involve cross-subsidisation by the APRA-regulated superannuation sector of losses incurred within any other sector.

In the event that the Government were to proceed to introduce a broader compensation scheme, ASFA considers it imperative that APRA-regulated superannuation monies are entirely excluded from the scheme, with any eligible losses continuing to be redressed via Part 23 of the SIS Act 1993.

In particular, ASFA takes the view it would be inappropriate for APRA-regulated superannuation monies to be levied as part of any compensation scheme, other than where misconduct has caused a superannuation fund to fail. This is on the basis that APRA-regulated funds:

- are prudentially supervised and regulated
- already pay a significant levy for that supervision, as well as other levies
- have had a relatively low incidence of failure and a negligible incidence of non-payment of SCT determinations.

Similarly, it would be inappropriate for superannuation funds to have to pay any up-front, annual management levy to the scheme.

As noted in part C.2, there are fundamental differences in the structure and regulation of APRA-regulated superannuation funds and SMSFs, with SMSF members better able to manage the risk associated with their investment. These differences are of such magnitude that it would be inappropriate to treat SMSFs and APRA-regulated funds as part of the same 'sector' for the purposes of any compensation scheme of last resort.

APRA-regulated superannuation monies should be entirely excluded from any compensation scheme of last resort. Any eligible losses arising in relation to APRA-regulated superannuation monies should continue to be redressed solely via Part 23 of the SIS Act 1993.

C.4 Any compensation scheme must be risk-based and must address moral hazard

We have noted at C.3 above our view that APRA-regulated superannuation monies should be excluded from any compensation scheme of last resort.

More broadly, in considering any such scheme it is in ASFA's view critical that the issue of moral hazard is effectively dealt with, by continuing to mandate, as part of the conditions for holding an AFSL, the holding of adequate professional indemnity insurance.

[9] St John, 2012, p56

The Review Panel has acknowledged[10] the moral hazard concerns associated with the potential introduction of a compensation scheme, noting that moral hazard can arise where there is knowledge that protection exists against possible financial loss, and this encourages individuals – and entities – to assume risks they might not otherwise assume.

In particular, the existence of a compensation scheme may:

- encourage consumers to become complacent about the risks of dealing in the market
- induce riskier behaviour by some providers
- reduce the incentive for stringent regulation or rigorous administration of the existing compensation arrangements.

ASFA considers these to be genuine and significant concerns, which must be fully addressed. The introduction of any compensation scheme should not supplant the underlying obligations on consumers to exercise reasonable caution when acquiring financial products and services, or on financial services providers to exercise diligence in complying with the responsibilities imposed on them by the financial services regulatory regime. Critically, the existence of a compensation scheme should also not displace the obligation on Government, and on all relevant regulators, to continually monitor and assess the adequacy of the regulatory framework to protect consumers and hold providers appropriately to account.

ASFA is also of the view that in determining the contribution that financial providers may be required to make toward compensation, there must be full consideration of the risk profile of the relevant sector, and not simply the size (funds under management or advice), of the providers subject to the levy.

The scheme must reflect the fact that some sectors are subject to more stringent regulatory requirements and that their risk of contributing toward a failure requiring compensation is, therefore, less than that applicable to other sectors. In this respect, we note that – according to the Review Panel's own assessment - the APRA-regulated superannuation sector should be considered relatively low-risk.

C.5 Additional comments in response to points raised in the Paper

C.5.1 Prospective operation of any compensation scheme

ASFA notes, and agrees with, the comment in the Paper that any compensation scheme of last resort should operate in a *prospective* way[11], open only to claimants who *in the future* receive a decision in their favour, which is not ultimately paid. This is, in ASFA's view, important to allow the design of any compensation scheme model and, critically, its funding, to be determined with some measure of certainty for all stakeholders.

The Paper indicates that "separate arrangements may need to be put in place to address legacy uncompensated losses, such as existing unpaid EDR determinations"[12]. ASFA notes that it would be important to ensure that any such proposals are the subject of a full consultation process with industry.

[10] Supplementary Issues Paper, op. cit., paragraphs 90-91
[11] Ibid., paragraph 31
[12] Ibid., paragraph 32

C.5.2 Funding

In ASFA's view, establishing an equitable funding basis for any compensation scheme is both critical and problematic.

The identification of appropriate 'sectors' for compensation purposes is, ASFA considers, an important threshold issue. It will be imperative to ensure that cross-subsidisation between sectors is avoided to the extent possible – providers in those sectors which have not contributed toward claims for compensation should not be required to fund that compensation.

As noted earlier in this submission, ASFA would not support any scheme that involved the potential that APRA-regulated superannuation monies might be exposed to cross-subsidisation of losses arising in other sectors.

The Paper refers to the funding model adopted for the Financial Services Compensation Scheme (FSCS) in the United Kingdom (UK), and notes (our emphasis):

> A participant firm's permissions to conduct activities determine which class, or classes, it belongs to. If a firm is a member of more than one funding class, they are required to contribute to both classes. Each of the relevant funding class has a threshold to try to ensure that firms' contributions to the FSCS are affordable and sustainable. **If compensation and specific costs in a funding class are so high that the threshold is breached, firms in other classes are called upon to contribute**.[13]

The adoption of such a funding model in Australia would not be acceptable, in ASFA's view, as it could lead to APRA-regulated superannuation monies being used to cross-subsidise losses incurred in other sectors of the financial services industry.

The Paper acknowledges that the UK's Financial Conduct Authority (FCA) is "currently consulting on options for changing the funding of the FSCS and the coverage it provides to consumers, and specific proposals to change rules around the scope and operation of FSCS funding"[14].

ASFA is of the view that considerable learnings can be derived from the UK's experience with the FSCS, with a view to informing the development of any compensation scheme for Australia. In particular, we note that the FCA has highlighted a number of difficulties experienced with regard to the stability and equity of the levies imposed on providers and the primary role that the FSCS has assumed in providing compensation, over and above existing professional indemnity requirements:

- the scale and impact of FSCS levies has risen sharply for some firms over recent years, causing concern about the unpredictability of the levies
- in some sectors, a relatively small number of firms have been responsible for a large proportion of FSCS compensation claims
- there are concerns about the way that some firms are grouped for levy purposes
- in recent years, FSCS levies have been largely driven by the failure of firms which have given unsuitable investment advice to consumers

[13] Ibid., paragraph 103
[14] Ibid., paragraph 106

- although professional indemnity insurance was intended to be one of the main ways for providers to protect their clients, it has been found that it is "not necessarily reliable", and the FSCS "has increasingly taken on the role of 'first line of defence' when a firm fails".[15]

Each of these issues is likely to arise in the context of any compensation scheme introduced for the Australian financial services industry.

We urge the Review Panel, and the Government, to monitor the outcomes of the FCA's review process and to consider its recommendations as part of the development of any compensation scheme for Australia.

C.5.3 Compensation caps

Having regard to the risk of moral hazard and the affordability of the scheme, ASFA submits that the amount of compensation should be determined in accordance with a sliding scale up to a maximum compensable loss.

We note that while the Paper refers to the 'compensation caps' that apply to EDR as potential limits on the compensation that may be available under the proposed scheme[16], it does not specifically acknowledge that the EDR arrangements for superannuation currently provide for unlimited monetary jurisdiction, with no cap. The Review Panel's own Final Report recommended that this be maintained, and the Government appears to have accepted that recommendation[17].

As noted earlier in this submission, ASFA strongly considers that claims in relation to APRA-regulated superannuation should be excluded from any compensation scheme of last resort and should continue to be redressed via Part 23 of the SIS Act. While Part 23 involves a process of ascertaining the eligible loss, there is no threshold limit imposed on applications for financial assistance.

C.5.4 Scheme administration

ASFA considers it appropriate that, if any financial services compensation scheme of last resort is established in Australia, it should be independent of government and industry, established under statute, have a board of directors (appointed by the relevant minister) and report to ASIC.

Clear mechanisms for accountability and transparency should be provided, including detailed reporting of all contributions collected from industry and the amounts of compensation paid.

There should also be a clear and direct obligation for the scheme operator to consider, and report to government on, any deficiencies in the regulatory framework that caused, facilitated or contributed to, the events which resulted in the payment of compensation under the scheme.

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[15] Financial conduct Authority: Consultation Paper CP16/42: Reviewing the funding of the Financial Services Compensation Scheme (FSCS), December 2016, paragraphs 1.6 – 1.7, 1.9

[16] Supplementary Issues Paper, op. cit., paragraph 107

[17] Treasury, Consultation Paper: *Improving dispute resolution in the financial system*, May 2017, Paragraph 38

In ASFA's view such a model would be preferable to an industry-administered scheme. In particular ASFA would not support a compensation scheme of last resort forming part of the proposed new EDR arrangements, although we accept that this may appear attractive from an administration and efficiency perspective. ASFA is of the view that clear independence between the two schemes is critical, as the triggering of the compensation scheme may highlight deficiencies in the EDR framework which need to be comprehensively and independently reviewed.

In this respect, ASFA does not support the proposal of the Australian Banking Association (outlined in the Paper at page 27) "that there should be further investigation of the EDR scheme providing the administrative services for the scheme and collecting funding levies" and prefers the administration model proposed by the Financial Ombudsman Service (as outlined in the Paper at page 30).

C.5.5 Scheme's ability to recover compensation

The Paper notes, at paragraph 111, that "where a compensation scheme of last resort makes a payment to a claimant, the scheme **may** seek to recover this compensation from the firm that failed to satisfy the EDR determination" (our emphasis). In ASFA's view, it should be a requirement of any compensation scheme that the operator **must** make reasonable attempts to recover compensation from the firm that failed to satisfy the EDR determination.

While we accept that recovery may not be possible in all cases, it should nonetheless be a pre-requisite to any award of compensation under the scheme.

It must be borne in mind, at all times, that the provision of the compensation under the scheme will involve a direct impost on financial services providers that were not involved in any failure in relation to the claim, and that the compensation scheme should only be utilised as a matter of genuine "last resort".

D. ACCESS TO REDRESS FOR PAST DISPUTES

D.1 General Comments

Whilst sympathetic to the plight of consumers who have been unable to obtain redress, ASFA has significant reservations about the proposal to allow access to redress for past disputes.

D.1.1 Liability for past disputes is unquantifiable

Firstly, we note the deeply concerning potential that financial services providers may become subject to an unquantifiable and open-ended liability in relation to past disputes. The Review Panel has itself noted this concern, in the Paper (our emphasis):

> The Panel notes that in many of the classes of cases identified **the value of losses is unquantifiable**. This creates challenges in determining how such a scheme could be funded.[18]

[18] Supplementary Issues Paper, op. cit., paragraph 156

The imposition of responsibility on the financial services industry to provide compensation in respect of an unquantifiable liability associated with past disputes is not an outcome that can, in ASFA's view, be accepted. It is clearly inappropriate that such a liability be imposed in relation to the APRA-regulated superannuation sector, where monies are held on trust and the funding of such compensation would impact adversely on the outcomes provided to all superannuants.

D.1.2 Time limits provide certainty

Where time limits apply to the bringing of claims, their purpose is to provide certainty for all stakeholders.

The Paper notes that under the existing EDR framework, FOS and the CIO may waive time limits "in exceptional circumstances or where member firms consent to a waiver"[19]. In ASFA's view, this discretion is an appropriate means of allowing access to redress where a consumer has compelling reasons for not having pursued their dispute within any applicable timeframe.

The Paper further notes that no limits apply to superannuation disputes, other than in relation to death and total permanent disability (TPD) claims[20]. These time limits are important, as they ensure that payment of death benefits to a member's beneficiaries is not unduly delayed, and that complaints regarding a member's TPD status – which is often an evolving matter - can be properly assessed in light of contemporaneous medical evidence.

ASFA notes that a third example applies in relation to superannuation, with respect to complaints about statements provided by a trustee to the Commissioner of Taxation[21] (these relate to mandatory reporting by trustees that may be taken into account by the Commissioner in determining, for example, a member's potential liability to excess contributions tax). Again, this timeframe is appropriate given the limited period afforded to individuals to lodge an objection in respect of their tax liability.

With the exception of these three cases, members and former members of an APRA-regulated superannuation fund are currently able to make a complaint and seek redress via the SCT.

The position with effect from 1 July 2018, when responsibility for EDR and complaints handling for financial services is transferred from FOS, the CIO and the SCT to the new Australian Financial Complaints Authority, is not yet entirely clear. We would anticipate that the new EDR regime will involve time limits similar to those that apply currently.

The need for certainty, for consumers and providers alike, in ASFA's view mitigates special rules allowing access in cases where time limits were not observed.

[19] Ibid., paragraph 141
[20] Ibid., paragraph 141
[21] *Superannuation (Resolution of Complaints) Act 1993*, subsection 15CA(2); *Superannuation (Resolution of Complaints) Regulations 1994*, regulation 5A

D.1.3 Administrative burden and evidentiary issues

Allowing past disputes to be pursued will involve an administration burden and cost for financial sector providers that should not be underestimated.

Of potentially greater concern, however, is the prospect that crucial evidence may no longer be available, either because prescribed record-keeping periods have expired or because, in the absence of an 'active' dispute, it was not considered necessary to obtain particular types of evidence (for example, regarding the health of a member/product holder).

The unavailability of contemporaneous evidence will have a significant impact on the resolution of past disputes, as it will require assumptions to be made and will inevitably lead to suggestions of bias in favour of either the consumer or the provider.

D.1.4 Managing moral hazard

The Paper contemplates a number of circumstances in which redress might be available for past disputes.

A number of these circumstances involve a consumer who has sought EDR being denied an outcome due to no fault of their own.

However, others contemplate situations where the consumer failed to seek EDR at the time of their dispute (see further comments at D.2.1 below), for reasons including 'dispute fatigue'. While the reasons for such behaviour may be readily understood, particularly where the consumer is not financially sophisticated, they raise important issues of moral hazard.

ASFA has **significant reservations** regarding the proposal to allow access to redress for past disputes.

D.2 Additional comments in response to points raised in the Paper

D.2.1 Reasons why EDR was not pursued

The Paper outlines a number of scenarios which the Review Panel has indicated could "lead to circumstances where consumers are unable to access redress through EDR"[22]. ASFA considers that these scenarios raise a number of different issues.

(i) the financial firm was insolvent or otherwise unable to pay

In this instance, affected consumers are entirely blameless for the failure to obtain redress. Going forward, it is likely that this scenario would be covered under any proposed compensation scheme of last resort.

To the extent that any scheme for redress of past disputes was established (see D.1 above regarding ASFA's concerns in this respect), it would appear reasonable that such cases are considered for potential eligibility.

[22] Supplementary Issues Paper, op. cit., paragraph 133

(ii) the monetary value of the dispute exceeded the EDR scheme's monetary limits

Unlimited monetary jurisdiction applies to superannuation complaints currently, and ASFA has submitted that it is critical that this continues under the proposed new EDR arrangements.

Where EDR of a (non-superannuation) dispute has not occurred because it exceeds any relevant monetary limits, ASFA has concerns about allowing redress simply because the dispute is now within any revised limits. We note that the monetary limits for the current industry ombudsman schemes are revised periodically and this is expected to continue, for non-superannuation complaints, once AFCA commences operation[23].

That is, the use of monetary caps is a distinct feature of the current EDR arrangements as well as the proposed new arrangements. Allowing past disputes to be progressed simply because they have now come within increased monetary limits involves elements of 'moving the goalposts' and runs counter to providing the certainty that all stakeholders should be entitled to expect from EDR arrangements.

(iii) the dispute was outside the EDR scheme's time limits

Where a financial services provider makes a decision that is eligible for EDR, it is required to notify the consumer of the outcome and of any time limits which apply for EDR purposes. ASFA considers the time limits that apply to EDR important, to provide certainty for all stakeholders – see our comments at D.1.2 above. In ASFA's view, access to redress for a dispute that was not taken to EDR within the applicable timeframe should not apply in the absence of exceptional circumstances.

(iv) the consumer or small business did not pursue their dispute with the EDR scheme for other unspecified reasons, for example, because of personal circumstances or cost involved, dispute fatigue or emotional distress.

ASFA considers this category of past disputes to be the most problematic raised in the Paper. We acknowledge that some consumers may feel overwhelmed and distressed by the process of raising a dispute with their provider and navigating the internal dispute resolution process, and that consumers may find the cost of engaging legal assistance to prepare their claim and represent them before an EDR scheme to be prohibitive.

However, we note that each of the existing EDR and complaints arrangements allow disputes to be lodged at no cost to the consumer, that legal representation is not a requirement, and that there are many free sources of information (particularly online) from which consumers can draw assistance when preparing to take a dispute to EDR. As such, ASFA would be concerned if 'cost' were taken to be a blanket criterion for access to redress.

[23] Treasury, Consultation Paper: *Improving dispute resolution in the financial system*, May 2017, paragraphs 43-46

ASFA is also concerned that accepting 'dispute fatigue' as grounds allowing subsequent access to redress raises clear issues of moral hazard. Where a consumer is aware of their rights to EDR in relation to a dispute, but fails to exercise those rights within any relevant timeframes, it is not clear, in ASFA's view, that the consumer should later be able to 'opt back' into the dispute resolution process and claim that they should receive redress for that dispute.

D.2.2 Who is the decision maker

The Paper notes that in any scheme for redress, there are a number of potential options to consider in selecting an appropriate decision-maker.

ASFA is of the view that any scheme to provide redress for past disputes should be administered entirely separate to the EDR framework for reasons of independence.

In particular, we would not consider it appropriate for any scheme for redress to be integrated with the new EDR scheme, AFCA. We can, however, see synergies for integration with any compensation scheme of last resort, should one be implemented, as similar considerations around independence, transparency and accountability will apply to each scheme.

D.2.3 Decision making criteria

The Paper refers to whether the test to be applied for redress should be "the same as those applied by the EDR bodies (that is, the FOS or CIO test), or something different"[24].

ASFA notes that a different test is currently applied by the SCT in hearing superannuation complaints and that – on the basis of the Panel's final report of the Review of the EDR framework - the Government appears to have accepted that this should continue. The recent consultation on the draft Bill to implement the new EDR framework has, however, raised some concerns about the test to be applied to EDR of superannuation complaints under the new arrangements. As indicated in our response to that consultation, ASFA is of the view that the current test applied for superannuation purposes is appropriate and should continue[25]. We further consider that it would be the appropriate test to the extent that any past superannuation related complaints should fall for consideration under a scheme for redress.

[24] Supplementary Issues Paper, op. cit., paragraph 167

[25] ASFA, Response to consultation package: External Dispute Resolution and Complaints Framework, 20 June 2017 – see part D.1.2

D.2.4 Compensation and funding

ASFA has noted our concerns regarding the prospect of exposing financial services providers to a potentially unquantifiable liability in respect of past disputes in part D.1.1 above.

The Paper notes, at paragraph 180:

> Depending on how any compensation arising from past disputes is funded, it may not be possible to fully compensate all claimants. This may require a 'rationing' mechanism to determine the amounts of compensation which are awarded. A rationing mechanism could be based on hardship. For example, claims which have resulted in financial hardship may be given priority in cases where a defined pool of money is available to fund past dispute determinations

In ASFA's view, recognition of a potential need for 'rationing' of compensation provides a compelling argument that any scheme for redress should be subject to a clear and limited 'window' within which potential claimants must come forward to register.