

28 June 2017

EDR Review Secretariat
The Treasury
Langton Crescent
PARKES ACT 2600

Email: EDRreview@treasury.gov.au

Dear Secretariat,

RE: COMPENSATION SCHEME OF LAST RESORT

We refer to the proposed Compensation Scheme of Last Resort ('CSOLR') and the Issues Paper ('Paper') dated March 2017.

Ballast Financial Management Pty Ltd ('Ballast') is a boutique Australian Financial Services Licensee ('AFSL') which provides holistic financial planning advice to a wide variety of consumers. Ballast is not aligned with a major bank, and has operated in the industry for over 20 years. Over this time, Ballast has become familiar with the operation and terms of the External Dispute Resolution ('EDR') schemes.

Please find below Ballast's response to the issues raised by the Paper.

Scope and Primary Considerations

1. It is without doubt that the current consumer compensation regime has flaws. The statistics provided by the Panel in the Paper reveal that despite the number of unpaid claims being low compared to the total amount paid, there are still considerable amounts that consumers are yet to receive.
2. Currently, it is difficult for consumers to receive compensation for inappropriate advice even once a determination has been made by an External Dispute Resolution ('EDR') body. This is due to several factors including the fact that the EDR schemes are underfunded and often don't have the resources to enforce these decisions. Whilst the Government guarantees losses in relation to fraud and theft these same protections don't apply to Self Managed Superannuation Funds or other situations of misconduct.
3. However, in deciding whether or not to establish the CSOLR, it is important to consider not only how to remedy the current rate of unpaid determinations, but critically analyse the current EDR regime. An analysis of the root cause of the problem may serve to reduce the need for the CSOLR or even make its functions redundant.

4. Should the CSOLR be established, it must be cognisant of the effect it will have on not just consumers, but the industry itself. The current proposals made by the Panel in the Paper, if accepted in full, would put a significant amount of pressure on small Financial Services Providers ('FSP') both financially and administratively.
5. A key driving factor behind these reforms is the fact that consumer confidence in the financial sector is low. Whilst improving the EDR system is an important step into improving these statistics, trust and confidence should be earned in an organic way. Simply widening avenues for consumer compensation and increasing compensation is a short term solution which is unhealthy for the industry. This is particularly true in relation to allowing past disputes to be reheard.

Evaluating the CSOLR

6. Unequivocally, the CSOLR will benefit consumers who have unpaid determinations. The level of this benefit will depend on the types of disputes able to be heard, and the level of compensation able to be awarded.
7. The current proposed CSOLR would perform the following functions:
 - i. Compensate consumers for future unpaid determinations which have remained unsatisfied due to the company being insolvent or otherwise unable to make payment;
 - ii. Potentially compensate consumers in situations where a court of tribunal has made an order which has not been fulfilled; and
 - iii. Potentially compensate consumers for decisions previously made by the EDR scheme which were uncompensated due to insolvency or not meeting the monetary or time limits; or not lodging a complaint due to emotional or circumstantial barriers.
8. The premise of the CSOLR is sound; however the functions that have been proposed do not have clear direction. Is the CSOLR intended to be a review board, a compensation scheme or both?
9. Ballast argues that the CSOLR should remain core to its premise and simply provide redress to consumers who have completed the EDR process and are the recipient of unpaid determinations.
10. The CSOLR should not enforce court or tribunal decisions as there are already multiple avenues for consumers to have this redressed.
11. Similarly, the CSOLR should not review EDR decisions. Providing a full review is inefficient and undermines the decision made by the scheme. Within the EDR scheme should be a mechanism for consumers and FSPs to receive an independent review upon appeal. This will allow the CSOLR to enforce a decision will full confidence in its legitimacy.

12. The Paper uses the Financial Services Compensation Scheme ('FSCS') as an example of how the proposed CSOLR might operate. Ballast believes that the FSCS creates large amounts of double handling, as a case will have been heard in full twice and had two determinations by the time the process is finalised. This is not a model which would be beneficial for our industry.
13. As mentioned in paragraph 2, the current issue in compensating consumers is enforcement and funding. The current EDR regimes don't have the capability or capital to chase FSPs who have not paid their determinations. Similarly, clients who have claims against companies who have wound up due to insolvency do not have an avenue of relief.
14. If the CSOLR was able to provide assistance to those who have not been able to claim due to this insolvency, it would inevitably be beneficial for consumers. Ballast agrees that the CSOLR should have the power to assist consumers in this situation.
15. In line with the above, the EDR scheme should have its Terms of Reference expanded to be able to determine whether or not an insolvent company has breached its duties to a consumer and caused loss. This will then flow through to the CSOLR to enforce the determination, depending on whether the company has fully wound up and if any duties have been breached.
16. In performing this function the CSOLR should be funded by all FSPs who engage in the EDR process, not just advice firms. Whilst the majority of unpaid determinations may arrive from advice firms, funding by advice firms only puts unreasonable pressure on smaller FSPs and is anti competitive in an already expensive and heavily regulated system. The burden should be spread out to avoid this.

Retroactive Decision Making

17. The largest area of concern for Ballast is the potential for the CSOLR to make retroactive decisions. The Paper has outlined four scenarios in which retroactive decisions may be made. They are:
 - i. Financial firm is insolvent or otherwise unable to pay;
 - ii. Monetary value too large;
 - iii. Outside time limits; and
 - iv. Other reasons including emotional distress and personal circumstances.
18. When deciding whether to implement retroactive decision making, it is fundamentally important to understand the relationship between FSPs and the EDR scheme, as well as giving mind to the inherent issues with retroactivity.
19. The Terms of Reference ('TOR') of any EDR scheme is a contract between the FSP and the scheme. It governs the terms of engagement and sets the rules of debate. An important part of this process, and any legal decision making process, is consistency and certainty. A consistent and certain process is a key indicator of a fair process. Though this is not always

the case, at least participants know that when proceeding they can fall back on the terms of the agreement for support in case anything goes wrong.

20. Altering previous decisions, or allowing for rehearing of decisions already made, is inherently unfair if it is against the TOR governing the original decision making process. The monetary compensation caps and time limits were put in place specifically to exclude decisions which breached their thresholds. More particularly, the compensation caps were designed to limit claims which could have been heard in a court; and the time limits there to meet each State's limiting statute.
21. Allowing consumers redress in situations where they have not made a claim within the time limit set by the TOR, or which are too large should remain excluded. This should also include claims which have not been made due to emotional distress or personal circumstances. The EDR process, whilst daunting for those involved, is far less onerous than legal proceedings. It is designed to readily assist clients in articulating their claims and is conducted in an informal setting. Clients who suffer from anxiety or other mental illnesses preventing them from participating can engage in the process remotely, and may appoint a third party to act on their behalf. Ballast does not believe that emotional distress or personal circumstances are a reasonable cause for withholding a complaint, particularly given the client has 6 years in order to make lodgement or 2 years post Internal Dispute Resolution.
22. The only circumstances which Ballast feels are reasonable for review are when compensation has not been received due to insolvency, or delinquency. However, enforcing a legacy decision of this nature is difficult if the company no longer holds any assets. In this situation, the dispute should be heard through the EDR scheme, and as mentioned in paragraph 16, enforcement made depending on the Directors' culpability.
23. In the event that the CSOLR is created with the full suite of decision making powers listed in the Paper, the impact on the industry will be immense. The largest concern for firms like Ballast is Professional Indemnity Insurance ('PII'). The terms of the every PII policy within the industry will need to be amended to include past disputes which have previously been excluded due to the Terms of Reference. This creates colossal liability and uncertainty for insurers which will result in either: no insurance; dramatically increased premiums; or exclusions for any past disputes. The flow on effect is that consumers who manage a successful claim may not be compensated due to FSP not being covered by PII.
24. Making the full suite of proposed changes will also negatively impact the opinions of FSPs who engage in the EDR process and further fuel the conception of inequality between FSP and consumer. It diminishes the value of the Terms of Reference, as the terms become uncertain in the face of future change.

Levies, Reporting and FSP Penalties

25. Any levy to raise funds for the scheme should be done in a tiered fashion, based upon the type of advice provided and volume. Personal advice firms, being the most likely to be

claimed, should be tier 1 and have their fees modified by volume. This should then be followed by general advice; deposit products, insurance advice or otherwise should not be segregated.

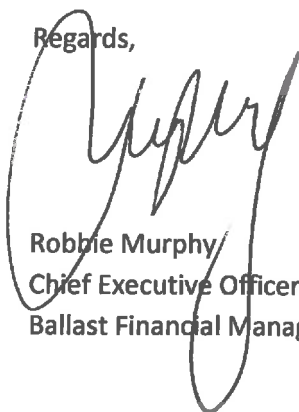
26. Details of non-payment should be reported by the CSOLR to ASIC. Repeat offenders should be at risk of losing their AFSL or having administrative penalties placed upon them by ASIC. The EDR scheme and CSOLR should not have the ability to revoke FSP membership from the EDR scheme. This would invalidate the FSPs Australian Financial Services Licence and be an overreach of the scheme's powers.

Summary

27. Ballast believes that consumers should be compensated for wrongs committed by FSPs. Currently, the system of ensuring that this takes place within the EDR environment is not adequate and has led to a number of consumers being left in an unacceptable position.
28. However, Ballast does not believe the answer to this solution is simply increasing avenues for consumer compensation, or changing the outcomes of previous determinations. This is short sighted and will cause significant damage to the industry.
29. This is particularly true given that there are only 38 offending parties over 151 determinations. Have avenues of direct enforcement been explored against these individuals, instead of imposing a further levy on the whole industry?
30. In the event that the CSOLR is established, it should remain simple and keep to its core values. It should provide compensation to consumers who have been through the EDR process and have not been paid their determinations. It should not extend to court of tribunal decisions, and should only assist clients retroactively with claims denied due to insolvency. The adverse effect on industry when granting powers greater than this outweighs the potential benefit for consumers.

Should you have any questions please do not hesitate to contact calc@ballast.com.au.

Regards,



Robbie Murphy
Chief Executive Officer
Ballast Financial Management Pty Ltd