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[FBAA Submission to the Review of the financial system external dispute resolution framework Supplementary Paper](#)

The FBAA as the leading national professional association to finance and mortgage brokers welcomes the opportunity to provide a submission in response to this paper.

Broadly speaking, the paper seeks submissions that relate to two primary issues:

- a) Whether to establish a fund of last resort and the details that would go around this proposal; and
- b) Whether to allow redress for past disputes where claimants have not been able to achieve a resolution for a range of reasons.

This submission is confined to issues around the *National Consumer Credit Protection Act* and consumer credit and does not attempt to make specific comment against financial services except where it is necessary to provide context to our response.

The dynamics between financial services and consumer credit are significantly different. The Corporations Act and NCCP Act recognise these differences through imposing different obligations and standards on participants in either regime. The nature of potential risks and areas for loss are fundamentally different between financial services and consumer credit, as are the compositions of licensees in both regimes. We are concerned to ensure that each regime is given separate treatment and that there is a valid business case for proposals made out against each on their own merits. Our view at this time is that consumer credit licensees are being drawn into a proposal which might more appropriately be considered solely against financial services.

Our general position is that we do not support the establishment of a scheme of last resort. The costs of such a scheme would be primarily borne by those in the industry who are least likely to be the cause for claims made against it (long-term, hard-working, viable businesses that have adequate resources/insurance and maintain current EDR membership) and the cost and complexity of administering such a scheme is likely to be as large as the scheme itself.

We also believe care needs to be taken to identify a genuine deficiency between the intention of a compensation regime and the current operation. A consumer receiving a successful determination but being unable to collect payment is one such deficiency. We agree that consumers and investors must have the confidence to participate in the system and avail themselves of the services offered through consumer credit and financial services and that to give them confidence they must be protected from fraud and negligence. Consumers and investors take risk and receive reward for this risk and care must be taken not to absolve consumers from the consequences of taking this risk or for consequences of their own conduct. Striking this balance is both very difficult but critical.

If further consideration is given to changes in consumer credit, then we believe that modifications to mandatory PI insurance run-off cover should be explored.

Any further discussions must involve a detailed analysis of the licensees and industry groups who would be part of any proposed scheme. The types of issues which must be considered are not dissimilar to those addressed during consultation on the ASIC industry funding model whereby the pricing of such a model must take into account the heaviest users and weight costs accordingly.

Scope and Principles

We agree with the broad principles of the Panel's approach to the scope of the scheme of last resort.

We do not agree with the scope of the redress for past disputes criteria. Consideration about redress for past disputes should be more confined than the proposed scope. We recognise the complexity of this issue however we believe that it is not appropriate to give consideration to situations where an entity never brought a claim against their services provider. This includes reasons where claims could not have been brought because they were out of time or exceeded the monetary thresholds or were not brought for other reasons.

Compensation scheme of last resort

Existing compensation arrangements

3. What are the strengths and weaknesses of the existing compensation arrangements contained in the *Corporations Act 2001* and *National Consumer Credit Protection Act 2009*?
4. What are the strengths and weaknesses of the National Guarantee Fund, the Financial Claims Scheme and Part 23 of the *Superannuation Industry (Supervision) Act 1993*?
5. Are there other examples of compensation schemes of last resort that the Panel should be considering?

FBAA Response

The existing compensation arrangements under the NCCP Act strike a fair balance between the impost on licensees and giving consumers free access to redress.

Its strengths are that:

- consumers have multiple points for resolution of disputes through IDR and EDR;
- licensees are required to provide consumers with a significant amount of information and assistance through the IDR process;
- consumers have a robust assistance framework to bring disputes through EDR;
- PI insurance is affordable for licensees, many of whom are individual operators or small businesses.

The greatest weakness, as has been observed in the Paper, is that some determinations are never paid. Whilst this is not a situation we want to occur, we have little information available to us to understand the extent to which this has occurred in consumer credit.

The Consultation Paper identifies that “Disputes relating to the provision of financial product advice currently make up the largest proportion of unpaid FOS determinations. These are followed by disputes with operators of managed investment schemes and credit providers”¹.

The age of the data behind some of the reports referenced in the Consultation Paper support the notion that a significant proportion of the unpaid determinations is within financial services.

Relevant to this consideration is the difference in custodial arrangements between financial services and consumer credit. In financial services, investors generally entrust their money to financial services licensees. In consumer credit, licensees generally entrust their money to consumers. The potential for losses can still be significant in both regimes however for most participants in consumer credit, the size of potential claims against them by a consumer is often proportionate to the size of the business. Small credit businesses face small claims by consumers. Large credit businesses are more likely to face larger claims. Licensees providing large scale credit are generally APRA regulated, hold insurance and are unlikely to ever be unable to pay a claim.

Evaluation of a compensation scheme of last resort

6. What are the benefits and costs of establishing a compensation scheme of last resort?
7. Are there any impediments in the existing regulatory framework to the introduction of a compensation scheme of last resort?
8. What potential impact would a compensation scheme of last resort have on consumer behaviour in selecting a financial firm or making decisions about financial products?
9. What potential impact would a compensation scheme of last resort have on the operations of financial firms?
10. Would the introduction of a compensation scheme of last resort impact on competition in the financial services industry? Would it favour one part of the industry over another?
11. What flow-on implications might be associated with the introduction of a compensation scheme of last resort? How could these be addressed to ensure effective outcomes for users?
12. What other mechanisms are available to deal with uncompensated consumer losses?
13. What relevant changes have occurred since the release of Richard St. John's report, *Compensation arrangements for consumers of financial services*?

FBAA Response

We only see costs, and not benefits of establishing a compensation scheme of last resort for consumer credit licensees. We do not believe a scheme of last resort is necessary for consumer credit. The NCCP Act and Regulations recognise that credit providers are essentially self-insured². Credit assistance providers are required to hold PI insurance that meets the requirements prescribed by ASIC. We do not have any information to suggest the current limits of \$2m per claim and an aggregate total proportionate to the activities (capped at \$20m) is inadequate.

The FBAA requires members to hold PI insurance that includes run-off cover for a period of seven years. We understand some PI Insurance policies offer run-off cover of much shorter periods than seven years.

Introducing a compensation scheme of last resort would expose consumer credit licensees to an obligation to financially support a scheme that has a diminished chance of being claimed against when compared to financial services. This would impose a disproportionate burden on credit licensees to co-fund a scheme established predominantly for financial services related matters.

² Paragraph 94

² Regulation 12(3) of the NCCP Regulations

Potential design of a compensation scheme of last resort

14. What are the strengths and weaknesses of the ABA and FOS proposals?
15. What are the arguments for and against extending any compensation scheme of last resort beyond financial advice?
16. Who should be able to access any compensation scheme of last resort? Should this include small business?
17. What types of claims should be covered by any compensation scheme of last resort?
18. Should any compensation scheme of last resort only cover claims relating to unpaid EDR determinations or should it include court judgments and tribunal decisions?
19. What steps should consumers and small businesses be required to take before accessing any compensation scheme of last resort?
20. Where an individual has received an EDR determination in their favour, should any compensation scheme of last resort be able to independently review the EDR determination or should it simply accept the EDR scheme's determination of the merits of the dispute?
21. If a compensation scheme of last resort was established and it allowed individuals with a court judgment to access the scheme, what types of losses or costs (for example, legal costs) should they be able to recover?
22. Should litigation funders be able to recover from any compensation scheme of last resort, either directly or indirectly through their contracts with the class of claimants?
23. What compensation caps should apply to claims under any compensation scheme of last resort?
24. Who should fund any compensation scheme of last resort?
25. Where any compensation scheme of last resort is industry funded, how should the levies be designed?
26. Following the payment of compensation to an individual, what rights should a compensation scheme of last resort have against the firm who failed to pay the EDR determination?
27. What actions should ASIC take against a firm that fails to pay an EDR determination or its directors or officers?
28. Should any compensation scheme of last resort be administered by government or industry? What other administrative arrangements should apply?
29. Should time limits apply to any compensation scheme of last resort?
30. How should any compensation scheme of last resort interact with other compensation schemes?
31. Are there any aspects of compensation schemes of last resort in other sectors and jurisdictions that should be considered in the design of any compensation scheme of last resort?

FBAA Response

Many of the points in the Consultation Paper summarising the ABA proposal identify features which already have traction in both the AFS and Credit regimes including move to greater professionalism of those involved in the industry, ensuring the scheme [consumer's right] is well understood and regular certification from licensees they are in compliance with their obligations.

We acknowledge and agree with the potential downside consequences of the establishment of a fund of last resort including the potential for increasing consumer complacency where unnecessarily high protection measures are introduced and the likely cost increase associated with providing services to consumers which in turn has potential to further price out consumers from accessing such services.

We support further investigation of increasing run-off cover.

Where we maintain financial services and consumer credit require different treatment, we certainly agree that any consideration of the establishment of a funds be confined to prospective claims.

Overall we believe a compensation scheme of last resort is fraught with risks which increase in magnitude the more broadly its terms are drafted. Our strong preference is to look to address any real problems through the existing services and requirements – most notably the operation of PI cover, the EDR schemes' ability to accept matters where licensees are not current members and the enforceability of EDR determinations.

Legacy unpaid EDR determinations

32. What existing mechanisms are available for individuals who have legacy unpaid EDR determinations to receive compensation?

33. Is there a need for an additional mechanism for those with legacy unpaid EDR determinations to receive compensation? If so, who should fund the payment of the legacy unpaid EDR determinations?

FBAA Response

Consumers with legacy unpaid EDR determinations essentially become a creditor of the entity. They can pursue their entitlements through court. This leaves them in the same position as any other person who has received a judgment. If the entity has no money to satisfy the judgment and there is no insurer or other party against which to bring a cross-claim then the creditors can seek to wind up a company or bankrupt an individual. We acknowledge this is not a realistic option for most people in this situation nor it is a realistic option for any other individual with an unsatisfied judgment.

Professional indemnity insurance policies should cover instances such as this. We note the Panel's observations about the shortcomings of PI Insurance and the difficulty of influencing individual insurers to change their products however this aspect should be further explored. PI Insurers would be required to change their product (or else not be able to offer PI) if it were a licensee condition of holding PI that the policy meets specific criteria.

Further work needs to be done to understand the potential impact on the PI insurance market however we see considerable benefits in this approach. Most significantly, the structures to manage claims are already in place via the insurers and would not require the creation of a Panel or a body to administer claims.

Providing access to redress for past disputes

Circumstances which have prevented access to redress

34. Other than circumstances that may be covered by a compensation scheme of last resort (such as outstanding unpaid determinations), what kinds of circumstances have given rise to past disputes for which there has not been redress? Are there any other classes besides those identified by the Panel?

35. What evidence is there about the extent to which lack of access to redress for past disputes is a major problem?

FBAA Response

We do not agree with the Panel's views on appropriate categories of persons who may be identified under a proposal for redress for past disputes. It is an everyday occurrence that individuals encounter situations where they are unable to pursue certain options because of expired timeframes or ignorance of remedies or causes of action available to them. It is unfortunate, but timeframes and thresholds exist for good reason. They strike a balance between fairness for all parties whilst providing certainty. In some cases, certain timeframes and thresholds can be waived such as an individual's right to commence out of time legal action if new material facts become known. Such waivers usually place the burden of proof on the claimant. It is not a matter of right.

The statutory limitations on timeframes for bringing a claim are not unreasonable. The monetary thresholds on EDR are not unreasonable, bearing in mind that EDR is not intended to be a proxy to bring risk, and cost-free action against licensees in all circumstances.

The area where we believe EDR Scheme rules may have unfairly impacted consumers and investors is where the conduct that caused the issue occurred at the time the licensee was an EDR member but the claim would have been/was brought after the membership had ceased. We would support changes to the rules of EDR schemes accepting claims against licensees for conduct that occurred at the time the membership was current rather than

making it a requirement that licensees be current members at the time the claim is brought.

We support further exploration of finding mechanisms to assist consumers with determinations to recover payment on those determinations but do not support re-opening past or lapsed claims for categories identified in the Consultation Paper under the heading of redress for past matters.

Approaches to providing access to redress for past matters

36. Which features of other approaches established to resolve past disputes outside of the courts (whether initiated by industry or government) might provide useful models when considering options for providing access to redress for past disputes in the financial system?

FBAA Response

We have no further response under this item.

Evaluation of providing access to redress for past disputes

37. What are the benefits and costs associated with providing access to redress for past disputes?

38. Are there any legal impediments to providing access to redress for past disputes?

39. What impact would providing access to redress for past disputes have on the operations of financial firms?

FBAA Response

We refer to our response under questions 34 and 35.

Evaluation of providing access to redress for past disputes (continued)

40. What impact would providing access to redress for past disputes have on the professional indemnity insurance of financial firms?

41. Would there be any flow-on implications associated with providing access to redress for past disputes? How could these be addressed in order to ensure effective outcomes for users?

FBAA Response

We refer to our response under questions 34 and 35.

Design issues for providing access to redress for past disputes

42. What are the strengths and weaknesses of the Westpac proposal?
43. What range of parties should be provided with access to redress for past disputes? Should all of the circumstances described in paragraphs 133-144 be included?
44. What mechanism should be used to resolve the dispute and what criteria should be used to determine which disputes can be brought forward?
45. What time limits should apply?
46. Should any mechanism for dealing with past disputes be integrated into the new Australian Financial Complaints Authority (once established) or should it be independent of that body?
47. Who should be responsible for funding redress for past disputes? Is there a role for an ex gratia payment scheme (that is, payment by the Government)?
48. Should there be any monetary limits? If so, should the monetary limits that apply be the EDR scheme monetary limits?
49. Should consumers and small businesses whose dispute falls within the new (higher) monetary limits of the proposed Australian Financial Complaints Authority but was outside the previous limits be able to apply to have their dispute considered? Should access to redress for past disputes be provided through a transition period whereby the higher monetary limits are applied for a defined period retrospectively? If so, what would be an appropriate transition period?
50. If it is not possible to fully compensate all claimants, should a 'rationing' mechanism be used to determine the amounts of compensation which are awarded? Should such mechanism be based on hardship or on some other measure?
51. Are there any other issues that would need to be considered in providing access to redress for past disputes?

FBAA Response

We reiterate our position that we generally do not support redress for past matters. Any further exploration of this issue must acknowledge that the credit industry has only been regulated by ASIC and under the NCCP since 2010. This is perhaps matter more relevant to financial services however it will need to be clear how such matters are quarantined from any consideration of a joint industry funded scheme, if in fact, that is an option which is further pursued.

End.

Yours faithfully



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