3 February 2017

By email to: EDRreview@treasury.gov.au

EDR Review Secretariat
Financial System Division
Markets Group
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Sir / Madam

EDR Review – Interim Report

Thank you for the opportunity to comment on the *Review of the Financial System Dispute Resolution Framework – Interim Report* (**Interim Report**). This joint submission was coordinated by Consumer Action Law Centre with funding from ASIC.

The following organisations have contributed to and endorsed this submission:

Consumer Action Law Centre
Care Inc Financial Counselling Service and the Consumer Law Centre of the ACT
Caxton Legal Centre
Consumer Credit Law Centre SA
Consumer Credit Legal Service (WA) Inc
Consumers' Federation of Australia
Financial Counselling Australia
Financial Rights Legal Centre

Details about each contributing organisation are contained in **Appendix A**.

Executive Summary

Consumer advocates welcome the Interim Report. We commend the Panel's focus on enhancing the existing external dispute resolution (**EDR**) framework and for extending the benefits of EDR to superannuation customers. The integrated package of reforms proposed in the Interim Report will significantly improve dispute resolution in the financial system.

Contributors to this submission have supported and represented thousands of consumers in disputes with financial services providers and superannuation funds over many years. This includes extensive experience with the Financial Ombudsman Service (**FOS**), Credit and Investments Ombudsman (**CIO**) and the Superannuation Complaints Tribunal (**SCT**). The EDR Review is an important opportunity to address shortcomings in consumer protection in financial services that have been exposed in a number of inquiries and scandals in recent years.

Our primary position remains that the best framework for dispute resolution in the financial system is a single industry ombudsman scheme for all disputes, including superannuation disputes. In our view, the best way to achieve this is to integrate the SCT and CIO into FOS, rather than creating two new schemes.

Nevertheless, we strongly support Draft Recommendation 1. Consumer advocates agree with the Panel that moving to a single industry ombudsman scheme for all financial, credit and investment disputes will have substantial benefits relative to the status quo.

Similarly, we strongly support the transition of the SCT to an industry ombudsman scheme. We agree with the Panel that the long-standing problems with the SCT cannot be fully resolved within a statutory tribunal structure, even with reforms to its funding and governance. Superannuation customers should not have to wait any longer to access the free, fair, fast, and accessible dispute resolution that can be offered by an industry ombudsman scheme.

The two new industry ombudsman schemes should, as far as possible, be linked from the outset to ensure consistency of approach and a smooth eventual merger. We encourage the Panel to mandate concrete steps for an eventual merger of the two new ombudsman schemes.

We also strongly support panel's finding that competition between ombudsman schemes is not appropriate and does not lead to improved consumer outcomes. Our detailed response to arguments in favour of competition between ombudsman schemes is available at **Appendix B**.

Consumer advocates strongly endorse the Panel's view that an additional statutory tribunal is not necessary in light of the integrated package of reforms proposed in the Interim Report.

Our submission makes a number of recommendations to improve consumer outcomes in the new industry ombudsman schemes. To resolve existing gaps, EDR coverage should be extended to lending for small business and investment purposes, debt agreement administrators and debt management firms. We strongly support the draft recommendations to increase the monetary limits and compensation caps, and recommended a general claim

limit and compensation cap of $2 million. To improve efficacy, we recommend that the ombudsman schemes have additional powers to:

- require mandatory discovery and open exchange of information between the parties;
- award fair compensation for loss and damage, including non-financial loss;
- award penalties that are a multiple of losses;
- award greater penalties for breaches of responsible lending;
- waive a consumer's debt in circumstances of long-term financial hardship; and
- direct a financial firm to take reasonable steps, enforceable by injunction.

Importantly, we recommend that the new schemes undertake a review of decision-making models to ensure that the decision-making is fair and appropriate at all stages of a dispute. One of the great advantages of the industry ombudsman model over the adversarial approach of courts and tribunals is its ability to investigate a person's complaint, particularly in light of the power imbalance that exists between unrepresented consumers and financial firms, which generally have access to specialised staff and legal advice. Thus, it is important that the new ombudsman schemes are staffed by skilled staff at all stages of case management and investigate all apparent claims, rather than taking a narrow approach to the definition of a dispute.

Consumer advocates strongly support the Panel's draft recommendation that financial firms report on internal dispute resolution (**IDR**). We agree with the Panel's that inadequate data means that it is difficult to assess the effectiveness of dispute resolution is and whether it is improving over time. Casework agencies report that internal dispute resolution is highly variable between financial firms. Firms should be required to report a range of IDR metrics and use comparable data, including the definition of complaint in the international complaints-handling guideline. For IDR reporting to be useful, it is imperative that data is comparable.

A last resort compensation scheme must be established to remedy uncompensated losses and build trust and confidence in the financial sector. A series of financial scandals have left many Australians out of pocket and in some cases, resulted in the loss of the family home or a secure retirement. Scandals have not just occurred in relation to financial advice; many people have suffered loss that has gone unremedied from the mis-selling of complicated investment products, collapse of managed investment schemes and predatory credit provision.

It is critical that the establishment and design of a last resort compensation scheme builds trust and confidence in the financial sector as a whole. To do so, the compensation scheme must be broad in its scope and apply retrospectively. It should apply to all financial service providers, including credit licensees and operators of managed investment schemes, and all relevant unpaid determinations of courts and industry ombudsman schemes.

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LIST OF RECOMMENDATIONS

1. Broad approach

a. There should be a single industry ombudsman scheme for all disputes in the financial system, including superannuation disputes. The SCT and CIO should be integrated into FOS.

b. Alternatively, if a new superannuation industry ombudsman scheme is necessary as an interim step:
   - the CIO should be integrated into FOS;
   - the new superannuation industry ombudsman scheme should merge with the new industry ombudsman scheme for financial, credit and investment disputes;
   - the Panel should mandate concrete transition steps and timeframes for the merger into a single industry ombudsman scheme.

2. Ombudsman scheme for financial, credit and investment disputes

a. The new industry ombudsman scheme for financial, credit and investment disputes should generally adopt the FOS model, culture and approach.

b. The new scheme's jurisdiction should include:
   - a requirement that its members implement the findings of systemic issues investigations; and
   - the ability to consider disputes (in limited circumstances) after a court judgment has been entered.

c. In respect of life insurance disputes:
   - The new industry ombudsman scheme for financial, credit and investment disputes should have sole jurisdiction for all life insurance disputes, including life insurance through superannuation.
   - Alternatively, consumers with life insurance through superannuation should have a choice of scheme where there is overlapping jurisdiction.

3. Monetary limits and compensation caps

a. The jurisdictional limits and compensation caps should be reviewed every three years as part of the scheme's periodic independent review and increased by a fixed amount.

b. Alternatively, the limits and caps should be indexed to CPI, increased annually and reviewed for adequacy every three years as part of the scheme's periodic independent review.

Limit/Cap	Recommendation
Claim limit (general)	$2 million
Compensation cap (general)	$2 million
Consequential financial loss	Remove existing carve out. Empower scheme to award fair and reasonable compensation within the general compensation cap
Consequential non-financial loss	Remove existing carve out. Empower scheme to award fair and reasonable compensation within the general compensation cap

Uninsured third party motor vehicle claims	$15,000
Income stream life insurance	$20,000 per month
Life insurance claims	No cap (alternatively, $2 million)
General insurance broking	Remove existing carve out and include within general compensation cap

4. **Small business lending**

   All small business lenders should be required to hold a relevant licence and maintain membership of an ASIC-approved industry ombudsman scheme. One method to achieve this is by extending the *National Consumer Credit Protection Act 2009* (Cth) to small business lending.

5. **Investment lending**

   All managed investment scheme lenders should be required to hold a relevant licence and maintain membership of an ASIC-approved industry ombudsman scheme. One method to achieve this is by extending the *National Consumer Credit Protection Act 2009* (Cth) to lending for the purpose of managed investment schemes.

6. **Debt management firms**

   A seamless regulatory framework should be introduced for debt management firms. All debt management firms should be required to hold a relevant licence and maintain membership of an ASIC-approved industry ombudsman scheme.

7. **Debt agreement administrators**

   Debt agreement administrators should be a member of an ASIC-approved industry ombudsman scheme as a requirement of registration.

8. **Regulatory oversight by ASIC**

   a. ASIC should be appropriately resourced to undertake increased oversight of industry ombudsman schemes.
   b. ASIC should be able to give directions to the new ombudsman schemes to remedy any failure to comply with the Benchmarks for Industry-based Customer Dispute Resolution.

9. **Ombudsman powers**

   a. The new ombudsman schemes should be provided with the following powers in addition to the powers of the existing schemes:
      - Power to obtain information and documents
      - Power to require mandatory discovery and open exchange of information between the parties
      - Power to award fair compensation for loss and damage, including non-financial loss
      - Power to award penalties that are a multiple of losses

- Power to award greater penalties for breaches of responsible lending
- Power to waive a consumer's debt in circumstances of long-term financial hardship
- Power to direct a financial firm to take reasonable steps, enforceable by injunction

b. The additional powers should be implemented through changes to the schemes' terms of reference in consultation with consumer advocates, with education for traders and consumers.

10. Decision-making

a. The new schemes should review decision-making models to ensure that decision-making is effective and fair at all stages of a dispute.

b. The new schemes should properly investigate all apparent claims, rather than taking a narrow approach to the definition of the dispute.

c. A random selection of disputes should be periodically externally quality-assessed. The quality assessment should encompass whether the outcome was fair and legally correct, as well as the appropriateness of the conduct of the dispute resolution process.

11. Internal dispute resolution

a. The IDR reporting regime should require clear and consistent terminology across all financial firms to ensure the data is comparable.

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

12. Last resort compensation scheme

An industry-funded compensation scheme of last resort should be introduced. The compensation scheme should:

a. apply to all financial services providers, including credit licensees and operators of managed investment schemes;

b. only accept claims from retail clients (consumer claims) and operate as a last resort scheme, that is, only be available for claims after all avenues have been exhausted, including a relevant award from an EDR scheme or a court and professional indemnity insurance;

c. not require an ombudsman scheme to enforce its determination in court as a precondition to compensating an affected consumer; however, after the scheme has compensated the affected consumer, the scheme should be able to recover from the financial service provider on a subrogated basis;

d. involve people with relevant industry and consumer experience in its governance, based on the existing industry ombudsman model;

e. award compensation at levels aligned with EDR caps that are reviewed and increased over time.

f. be retrospective in application;

g. be funded by industry, through a levy imposed by the government.

13. Funding

Adequately fund legal and financial counselling services for all aspects of the proposed dispute resolution framework in the financial system.

BROAD APPROACH

Consumer advocates welcome the Panel's Interim Report and draft recommendations. We commend the Panel's focus on enhancing the existing industry ombudsman framework and for extending the benefits of the industry ombudsman model to superannuation disputes.

A single industry ombudsman scheme for all disputes

We strongly support the merger of FOS and CIO into one scheme and the SCT's transition to an industry ombudsman scheme.

However, our primary position remains that the best framework for dispute resolution in the financial system is a single industry ombudsman scheme for all disputes, including superannuation. In our view, the best way to achieve this is to integrate the SCT and CIO into FOS, rather than creating two new schemes.

We note the Panel's preliminary view that it is preferable to initially introduce an industry ombudsman scheme focussed exclusively on superannuation disputes to facilitate strong stakeholder engagement. As the Panel observes, stakeholder engagement has been important to the success of ombudsman schemes in other sectors.

In our view, such engagement can be accommodated within a single ombudsman scheme. Stakeholders could have significant input in the development and implementation of a new superannuation stream within a single industry ombudsman scheme.

If the Panel maintains its view that a separate superannuation ombudsman scheme is necessary to garner industry support, then this should be an initial step on a path to a single industry ombudsman scheme for all disputes in the financial system. The two schemes, as far as possible, should be linked from the outset to ensure consistency of approach and a smooth merger.

The Panel's final recommendation should include concrete steps for the merger of the two new ombudsman schemes. Appropriate recommendations may include:

- timeframes for the merger;
- co-locating the new schemes in the same building(s);
- sharing back-office functions, such as human resources and IT systems;
- that the new schemes have at least one joint board meeting each year;
- publishing joint reports where appropriate;
- developing consistent procedural and decision-making approaches, particularly where there is jurisdictional overlap;
- adequate resourcing to ensure a smooth transition; and
- actively developing harmonious workplace cultures.

Recommendation 1

a. There should be a single industry ombudsman scheme for all disputes in the financial system, including superannuation disputes. The SCT and CIO should be integrated into FOS.

b. Alternatively, if a new superannuation industry ombudsman scheme is necessary as an interim step:

    - the CIO should be integrated into FOS;
    - the new superannuation industry ombudsman scheme should merge with the new industry ombudsman scheme for financial, credit and investment disputes; and
    - the Panel should mandate concrete transition steps and timeframes for the merger into a single industry ombudsman scheme.

Competition between schemes

There are several competition arguments that have been made by proponents of maintaining multiple ombudsman schemes in financial services. The main arguments can be summarised as follows:

- A single merged industry ombudsman scheme will be prone to monopolistic and bureaucratic behaviour, leaving it sluggish, inflexible and unresponsive to stakeholder concerns about performance.
- Without competitive tension between industry ombudsman schemes, turnaround times, service levels, innovation and continuous improvement will all suffer. There will be less incentive to keep costs in check and run the scheme efficiently.

We have seen little evidence to support these claims. Indeed, we are concerned that the maintenance of the status quo and competition between schemes leads to worse outcomes for consumers. We respond to the main arguments below. For a more thorough response, please see **Appendix B**.

First, it doesn't follow that a single merged scheme will become a bureaucratic and monopolistic organisation. FOS has been the largest industry ombudsman scheme in financial services for many years and it has a proven track record of stakeholder engagement, including regularly surveying its members and applicants about how it can improve its dispute processes and piloting new ways of working to meet user needs. After its last independent review, FOS re-engineered its dispute processes, delivering significant benefits to users including faster turnaround times. FOS states that competition between schemes has not been the driver for change in its organisation.

Second, as consumer advocates have previously submitted, competition between ombudsman schemes is a poor and inefficient way to drive innovation and change. While one scheme may innovate and experiment with a change, it takes a significant amount of time for the other scheme to follow, if they do at all. In the meantime, many consumers lose out. Even without competitive pressure from other schemes, there are more effective drivers for change and innovation within industry ombudsman schemes including:

- consumer liaison functions;
- consumer movement advocacy, policy development and campaigning;
- periodic independent reviews;
- regulatory oversight; and

- individual actors within schemes who (for a variety of reasons) drive proactive change within their organisations.

Third, as the Panel points out in its Interim Report, competition generally benefits the person that has the choice of service. In the current framework, it is financial firms and not consumers that have the choice of industry ombudsman scheme. Consumers are one-off users of EDR, if at all. They have no experience from which to choose a financial firm based on its choice of EDR scheme. In any event, by the time the consumer has a dispute, their firm may have changed schemes. Rather, any benefit of competition flows to financial firms. In a competitive environment, schemes will be driven to take actions which attract and maintain membership and may not always be in consumers' best interests.

Finally, it is, as the Australian and New Zealand Ombudsman Association (**ANZOA**) has stated, inappropriate to apply concepts of market forces and competition to what are effectively 'natural monopolies'. Competition may lead to manipulation of dispute resolution services, differing standards, and inconsistencies in decision-making which could be adverse for consumers and participating organisations. Competition between ombudsman schemes promotes 'forum shopping' by financial service providers with adverse impacts on balanced and fair outcomes for users of the scheme.

Statutory tribunal

Consumer advocates strongly endorse the Panel's view that an additional statutory tribunal is not necessary in light of the draft recommendations in the Interim Report.

We refer to our joint submission in response to the EDR Review Issues Paper (**Initial Submission**), where we detailed our concerns about an additional forum in the form of a statutory tribunal.[1] Consumer advocates remain opposed to the establishment of a banking tribunal to replace the existing industry ombudsman model.

We note the First Report of the House of Representatives Standing Committee on Economics in its *Review of the Four Major Banks*.[2] The Committee noted our concerns and that it was 'critical that, if the Government were to proceed with the establishment of a tribunal, these concerns be adequately addressed.'[3]

Notwithstanding our opposition to a replacement statutory tribunal, the Committee recommended that:

> the Government amend or introduce legislation, *if required*, to establish a Banking and Financial Sector Tribunal by 1 July 2017. This tribunal should replace the Financial Ombudsman Service, the Credit and Investments Ombudsman and the Superannuation Complaints Tribunal.[4]

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[1] At pages 2-5 and 68-71. Submission available at http://consumeraction.org.au/edr-review/.
[2] House of Representatives, Standing Committee on Economics, *Review of the Four Major Banks: First Report* (tabled 24 November 2016) available at http://www.aph.gov.au/Parliamentary_Business/Committees/House/Economics/Four_Major_Banks_Review/Report.
[3] Ibid [2.16].
[4] Ibid [2.1], Recommendation 2.1 (emphasis added).

Although there is little detail at this stage about how the proposed tribunal would operate, in principle, consumer advocates are opposed to the Committee's recommendation. In light of the draft findings and integrated package of reforms proposed in the Interim Report, in our view a Banking and Financial Sector Tribunal is not required.

The Committee states in paragraph 2.17 of the First Report:

> To help address many of the consumer groups' concerns, the Committee proposes that the new banking and financial services tribunal have the following features. It should:
>
> - be free for consumers to access;
> - have equal numbers of consumer and industry representatives on its board;
> - require all firms holding a relevant ASIC or APRA licence (in the case of superannuation/retirement savings account's providers) to be a member;
> - operate without lawyers (to the extent possible);
> - be funded directly by the financial services industry;
> - have the power to refer potential systemic issues to ASIC for formal investigation. For example, this could occur when the tribunal receives a large number of similar complaints over a year; and
> - make decisions that are binding on member institutions.[5]

Save for the requirement that it operate without lawyers to the extent possible, we strongly endorse the features listed by the Committee in paragraph 2.17 of its Report. However, these features describe an industry ombudsman scheme, not a statutory tribunal. It is difficult to reconcile the Committee's support for these features with its recommendation to establish a tribunal to replace the existing ombudsman schemes.

On the issue of legal representation, we refer to our comments in our Initial Submission on the need for representation and the inconsistency of outcomes for represented and unrepresented consumers.[6] The reality is that, in most cases, there is a power imbalance between the consumer and the financial firm, which will have specialised staff and access to internal or external legal advice, whether or not a lawyer is on the record. Accordingly, consumers should not be restricted from relying on advocates such as financial counsellors or lawyers for support and representation. Rather than a requirement to operate without lawyers, we prefer a requirement that the dispute resolution scheme avoid operating legalistically and be as user-friendly as possible.

Internal dispute resolution

Consumer advocates strongly support the Panel's draft finding on IDR, including that inadequate data makes it difficult to assess the effectiveness of internal dispute resolution and whether it is improving over time. Casework agencies report that internal dispute resolution is highly variable between financial service providers. Firms should be required to report a range of IDR metrics and use comparable data, including the definition of 'complaint' in the international complaints-handling guideline.

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[5] Ibid [2.17].

[6] See pages 43-45.

FINANCIAL, CREDIT AND INVESTMENTS DISPUTES

One scheme for all financial, credit and investment disputes

Draft Recommendation 1: There should be a single industry ombudsman scheme for all financial, credit and investment disputes (other than superannuation disputes) to replace FOS and CIO

We refer to our comments on the broad approach and Recommendation 1, above.

Our primary position remains that the best framework for dispute resolution in the financial system is a single industry ombudsman scheme for all disputes, including superannuation. In our view, the best way to achieve this is to integrate the SCT and CIO into FOS, rather than creating two new schemes.

Nevertheless, we strongly support Draft Recommendation 1. Consumer advocates agree with the Panel that moving to a single industry ombudsman scheme for all financial, credit and investment disputes will have substantial benefits relative to the status quo. We refer to our comments on the benefits of industry ombudsman schemes in our Initial Submission at pages 2, 61-63.

Generally, the FOS model, culture and approach should be maintained in the new ombudsman scheme, subject to concerns outlined in this submission and our Initial Submission.

<u>Jurisdiction</u>

In addition to the jurisdictional features outlined at page 147 of the Interim Report, the new scheme's jurisdiction should include:

- a requirement that its members implement the findings of systemic issues investigations; and
- the ability to consider disputes (in limited circumstances) after a court judgment has been entered.

We also refer to our recommendations below on the monetary limits and compensation caps, scheme membership, and ombudsman powers.

Anna's story

Anna sought advice from CCLSWA through her legal administrator. Anna had a court judgment against her in relation to a loan which was secured against her home. Anna had taken out the loan several years previously with the intention of starting her own business, although she had no business experience, but had used the funds for living expenses. Anna did not work and was later diagnosed with a mental illness. Anna lived in her home by herself. Anna had inherited her home from her parents when they passed away.

Anna had been served with a Property (Seizure and Delivery) Order (**PSDO**) which would allow the lender to take possession of Anna's home, leaving her homeless.

CCLSWA lodged a dispute with CIO on the basis that the lender had been dealing with Anna and not her administrator, in circumstances where it knew that an administrator had been appointed. Lodging the dispute prevented the lender from being able to execute the PSDO.

This hold on enforcement gave CCLSWA enough time to provide the administrator with legal advice in relation to the loan, and to seek the opinion of a pro bono barrister in appealing the default judgment.

The complaint at CIO was closed and the parties entered into a confidential settlement.

If not for the CIO's ability to consider disputes post-judgment, CCLSWA would have been unable to prevent the PSDO from being executed unless it brought an application in the Supreme Court of WA, and Anna would have been homeless.

Source: Consumer Credit Legal Service WA

We recommend that the new ombudsman scheme for financial, credit and investment disputes have sole jurisdiction for all life insurance disputes, including life insurance through superannuation. The existing inconsistencies in the treatment of life insurance between FOS and the SCT should be reconciled during the establishment of the new ombudsman schemes. This will reduce inconsistency in outcomes for consumers in the interim and assist in the eventual merger into a single scheme for all disputes in the financial system.

Alternatively, consumers with life insurance through superannuation should have a choice of scheme where there is overlapping jurisdiction between the new ombudsman schemes for superannuation disputes and for financial, credit and investment disputes.

We note that this recommendation will likely require superannuation trustees to be a member of both schemes. Consideration should be given to ensuring trustees do not face a greater fee burden as a result.

Governance

We agree with the Panel's Draft Finding that:

> The governance model of industry ombudsman schemes, with even numbers of directors with industry and consumer expertise and an independent chair, assist in ensuring that schemes can operate independently of industry, despite being industry funded.

We support this articulation of the benefits of the governance model of the existing schemes. We note that the short-hand terms 'consumer representative' and 'industry representative' are often used to refer to board members with industry or consumer experience. Properly understood, the board members are not, nor should be, a true 'representative' of a particular group or industry segment. We do not support an approach where each industry sector considers that it is entitled to a 'seat at the board'. Rather, board members must have relevant consumer or industry experience and expertise, in addition to governance skills and other appropriate qualifications. Importantly, once they are appointed, directors act in the interests of the company, in accordance with corporations' law requirements.

Recommendation 2

a. The new industry ombudsman scheme for financial, credit and investment disputes should generally adopt the FOS model, culture and approach.

b. The new scheme's jurisdiction should include:

- a requirement that its members implement the findings of systemic issues investigations; and
- the ability to consider disputes (in limited circumstances) after a court judgment has been entered.

c. In respect of life insurance disputes:

- The new industry ombudsman scheme for financial, credit and investment disputes should have sole jurisdiction for all life insurance disputes, including life insurance through superannuation.
- Alternatively, consumers with life insurance through superannuation should have a choice of scheme where there is overlapping jurisdiction.

Monetary limits and compensation caps

Draft Recommendation 2: The new industry ombudsman scheme for financial, credit and investment disputes should provide consumers with monetary limits and compensation caps that are higher than the current arrangements and that are subject to regular indexation.

Consumer advocates strongly support Draft Recommendation 2. The existing limits and caps must be raised substantially, and should be no less than the existing jurisdiction of the three complaint bodies.

Draft Recommendation 3: The new industry ombudsman scheme for financial, credit and investment disputes should provide small business with monetary limits and compensation caps that are higher that are higher than the current arrangements and that are subject to regular indexation.

Consumer advocates strongly support Draft Recommendation 3.

Information request: What should be the monetary limits and compensation caps for the new scheme?

Contributors to this submission support the following jurisdictional limits and compensation caps for consumer disputes.

Limit/Cap	Recommendation
Claim limit (general)	$2 million
Compensation cap (general)	$2 million
Consequential financial loss	Remove existing carve out. Empower scheme to award fair and reasonable compensation within the general compensation cap

Consequential non-financial loss	Remove existing carve out. Empower scheme to award fair and reasonable compensation within the general compensation cap
Uninsured third party motor vehicle claims	$15,000
Income stream life insurance	$20,000 per month
Life insurance claims	No cap (alternatively, $2 million)
General insurance broking	Remove existing carve out and include within general compensation cap

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

It is important that the ombudsman scheme's jurisdiction is, as far as possible, uniform and consistent across claims, compensation, and types of disputes. A uniform threshold would reduce the substantial confusion faced by consumers, industry, and their respective advisors. It would improve consistency of outcomes and simplify jurisdictional disputes for the scheme.

The monetary limits and compensation caps should reflect the value and cost of financial services and products in Australia, including:

- the cost of home loans;
- property prices;
- the cost of a rebuild on total loss insurance claims;
- the average coverage on insurance policies.

The current limits and caps have clearly failed to keep up with the pace of the Australian property market, particularly in Sydney and Melbourne. As at December 2016, the median house price was $1,123,991 in Sydney and $795,447 in Melbourne.[7] As the price of housing increases, so too does the size of home loans and, consequentially, guarantees given on home loans.

In recommending a uniform claim limit and compensation cap of $2 million, we have had particular regard to the issue of guarantee disputes. Unlike disputes about home loan debts, in guarantee disputes the amount of the claim will generally be the whole amount of the guarantee, given that the remedy usually sought is that the guarantee is unenforceable due to non-compliance with the law or *Code of Banking Practice*.

If, contrary to our recommendation, the general claim limit remains less than $2 million, we consider that the claim limits for disputes involving a personal guarantee should be higher than the general claim limit, and should be set at $2 million.

At present, the jurisdictional limit on a life insurance dispute depends on whether or not the policy is held through superannuation and, consequently, whether the dispute is heard by the

[7] https://www.domain.com.au/news/sydney-house-prices-climb-more-than-10-per-cent-to-record-11-million-domain-group-20170123-gtryjd/.

SCT or FOS. There is no principled reason why the jurisdictional limit should differ based solely on whether or not a life insurance policy is held through superannuation. The new scheme should have no cap on life insurance claims, consistent with existing unlimited jurisdiction of the SCT. Alternatively, an appropriate jurisdiction limit would be $2 million.

Information request: Should they be different for small business disputes?

No. It is sensible and fair for the same limits to apply to consumer and small business disputes. This would also simplify the jurisdiction and avoid further confusion for all parties.

Information request: What indexation requirements should apply to ensure the monetary limits and compensation caps remain fit-for purpose?

Once the monetary limits and compensation caps are raised, they should continue to be reviewed regularly to ensure that the scheme's coverage is sufficient, in accordance with ASIC Regulatory Guide 139.

Our preferred approached is a fixed increase every three years. The new limits and caps should be based on a review of the adequacy of the existing limits and the principles outlined above. This review could be undertaken in conjunction with the scheme's periodic independent review.

Alternatively, we support an annual CPI increase, with a review every three years to ensure the limits and caps are fit-for-purpose.

The limits and caps should be rounded to the nearest $10,000 to ensure the jurisdiction is as simple and clear as possible. It may be appropriate to round to a smaller interval for the lower caps. For example, the uninsured third party motor vehicle compensation cap could be rounded to the nearest $1000.

On balance, we prefer a fixed increase than CPI indexation to ensure that the scheme's jurisdiction is simple to understand. Annual changes, and the odd numbers produced by CPI adjustments, lead to confusion and difficulties for all parties.

Recommendation 3

a. The jurisdictional limits and compensation caps should be reviewed every three years as part of the scheme's periodic independent review and increased by a fixed amount.

b. Alternatively, the limits and caps should be indexed to CPI, increased annually and reviewed for adequacy every three years as part of the scheme's periodic independent review.

SCHEME MEMBERSHIP

The jurisdiction and membership of the new ombudsman scheme for financial, credit and investment disputes should resolve the current gaps in coverage, including:

- small business lending;
- lending for managed investments;

- debt management firms; and
- debt agreement administrators.

Small business lending

Information request: Should the national consumer credit protection law be extended to small business?

We strongly support compulsory licensing and membership of an ASIC-approved industry ombudsman scheme for all small business lenders. In our experience, many people with small business loans:

- can be as unsophisticated in financial and legal matters as any individual consumer;
- hold very little bargaining power in negotiating products and services contracts; and
- are often asked to sign non-negotiable standard form contracts.

The gap in coverage for small business lending can often impact upon people who agree to give a guarantee to help a family member with a new business venture. If the business fails, this can put the family home in jeopardy.

The Christies' story

Mr and Mrs Christie were an elderly couple who provided a guarantee for a loan taken out by a company controlled by their son. Mr and Mrs Christie were a migrant couple who spoke limited English and did not read or write in English. A mortgage was taken out over the family home to secure the guarantee. The company became insolvent and winding up proceedings were commenced. Meanwhile, the lender commenced proceedings against Mr and Mrs Christie seeking repayment of the loan pursuant to the guarantee, and possession of the family home.

As the loan was for a business purpose, the lender was not required to be a member of an EDR scheme.

CCLSWA is currently instructing pro bono counsel to assist the client defend the proceedings in the Supreme Court of WA.

Had the lender been a member of an EDR scheme, Mr and Mrs Christie would have been able to lodge a dispute with this scheme, rather than engage in the complex, time-consuming, resource-constraining litigation, which is causing them a great deal of stress.

Source: Consumer Credit Legal Service WA

Broadly, we support the extension of the *National Consumer Credit Protection Act 2009* (Cth) (**NCCPA**) to small business lending. Beyond licensing and EDR membership, many of the protections in the Act could assist people operating small businesses, such as hardship variations and requirements on repossession. However, consideration should be given to particular issues in small business lending that may not arise in consumer lending. Careful consideration would also need to be given to the definition of 'small business' to ensure that it is clear and appropriate.

As part of any extension of the NCCPA to small business lending, consideration must be given to funding appropriate legal and financial counselling services to assist small business borrowers who cannot afford private legal advice. At present, there is minimal or no free legal advice for small business borrowers. We refer to our comments below on funding arrangements in the future dispute resolution framework.

Ken's story

Ken had a loan for a truck. His finance company was trying to repossess the truck after Ken missed only two payments. Ken was in financial hardship following his wife developing a heart condition. The finance company would not make a repayment arrangement at all even though Ken had told them he should be able to catch up within two months. He explained about his wife's illness but the finance company did not care.

Ken rang Financial Rights desperate for help. We had to explain that we were not funded to assist small business, however, we would check whether the Finance company was a member of an EDR scheme. They were not a member of any EDR scheme. We explained that there was no requirement in the law for the finance company (lending for small business) to be a member of EDR. We also explained that he had no right to hardship and no right to a default notice before repossession of his truck. We confirmed that his truck was at immediate risk of repossession and he needs to find a way to catch up the repayments or negotiate with the finance company for more time. We mentioned he could see a private solicitor but this would cost money he did not have. Ken said it was all 'bloody unfair' and hung up.

Source: Financial Rights Legal Centre

Recommendation 4

All small business lenders should be required to hold a relevant licence and maintain membership of an ASIC-approved industry ombudsman scheme.

One method to achieve this is by extending the *National Consumer Credit Protection Act 2009* (Cth) to small business lending.

Lending for investment purposes

A further gap in EDR coverage is borrowing for investment purposes, such as managed investment schemes. The NCCPA does not apply to lending for investment purposes, except for residential investment properties. As with lending for small business purposes, many problems can arise in lending for managed investment schemes.

The Senate Economics References Committee detailed the 'urgent need' for reform of credit advice and full recourse loans for retail investors in its recent report, *Agribusiness managed*

investment schemes: Bitter harvest.[8] Where a borrower defaults on a full recourse loan, the lender can target assets that were not used as loan collateral. Evidence presented to the Committee showed that, in many cases, investors did not realise that if their investment failed to generate the anticipated returns or failed completely, they would need to meet repayments from other sources and could be at risk of losing their home.[9] The Committee received numerous accounts of growers signing over a power of attorney to their adviser to arrange and refinance loans, with growers unaware not only of the risky investment venture but of the high risk loan agreement they had entered.

In the Committee's view, the responsible obligations imposed on brokers and lenders under the consumer credit laws should apply equally to the promoters, advisers and lenders involved in providing funds for investment purposes. To resolve these problematic gaps in the regulatory framework for lending for managed investment schemes, the Committee recommended that:

> the Government initiate discussions with the states and territories on taking measures that would lead to the introduction of national legislation that would bring credit provided predominantly for investment purposes, including recourse loans for agribusiness managed investment schemes, under the current responsible lending obligations. The provisions governing this new legislation would have two primary objectives in respect of retail investors:
>
> - oblige the credit provider (including finance companies, brokers and credit assistance providers) to exercise care, due diligence and prudence in providing or arranging credit for investment purposes; and
> - ensure that the investor is fully aware of the loan arrangements and understands the consequences should the investment underperform or fail.[10]

The Committee considered that a referral of legislative power from the states and territories would be necessary to extend the consumer credit laws to managed investment schemes. Consumer Action Law Centre notes that a referral of powers may not be necessary in light of the existing referrals. A memorandum of advice from Brind Zichy-Woinarksy QC on the existing referrals of powers is available at **Appendix C**.

Frank's story

In 2006, Frank was 60 years old and borrowed $100,000 from Great Southern Finance to invest in the Great Southern managed investment scheme. The loan was assigned to Adelaide Bendigo Bank. Frank did not realise that if he did not receive a return from the investment, he would still be liable to pay the loan and that his home would inevitably be at risk. Frank was granted the loan even though he would be unable to service the loan without sale of his home in the event there was no return on the investment.

Source: Consumer Credit Law Centre SA

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[8] The Senate, Economic References Committee, *Agribusiness managed investment schemes: Bitter harvest* (March 2016) available at:
http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/MIS/Report.

[9] Ibid xxxiv.

[10] Ibid [11.92], Recommendation 15.

Recommendation 5

All managed investment scheme lenders should be required to hold a relevant licence and maintain membership of an ASIC-approved industry ombudsman scheme.

One method to achieve this is by extending the *National Consumer Credit Protection Act 2009* (Cth) to lending for the purpose of managed investment schemes.

Debt management firms

Draft Recommendation 11: Debt management firms should be required to be a member of an industry ombudsman scheme. One mechanism to ensure access to EDR is a requirement for debt management firms to be licensed.

Consumer advocates strongly support Draft Recommendation 11. A seamless regulatory framework including compulsory licensing and membership of an ASIC-approved industry ombudsman scheme is needed to stem the ongoing harm caused by debt management firms.

Consumer advocates have significant concerns about the conduct of debt management firms, including the charging of high up-front fees for services of little value, poor or inappropriate services that can leave consumers worse off, and misleading and predatory behaviour affecting people in financial hardship.

In February 2016, around forty experts from consumer advocacy organisations, industry associations, ombudsman schemes, government agencies and regulators met to discuss the social and industry impacts of debt management firms. Following the roundtable, representatives released a communique calling on the Government to take urgent action to tackle the exploitation of financially stressed consumers.[11]

Improved standards of conduct by debt management firms, protection of consumer interests, the enhancement of consumer outcomes and a reduction in industry costs could be achieved with the introduction of a regulatory framework for debt management firms. This framework should include licensing as well as rules to regulate business behaviour, and would bring these businesses into line with other financial services in Australia. Similar measures have been implemented in the US and UK to successfully deal with the problems associated with debt management firms.

Recommendation 6

A seamless regulatory framework should be introduced for debt management firms. All debt management firms should be required to hold a relevant licence and maintain membership of an ASIC-approved industry ombudsman scheme.

[11] Communique available at: http://policy.consumeraction.org.au/2016/03/03/debt-management-firms-comm/.

Debt agreement administrators

Consumer advocates are increasingly concerned about the consumer harm arising from the growing use of debt agreements under Part IX of the *Bankruptcy Act 1966* (Cth). Debt agreements are a form of insolvency generally only suitable for a very narrow band of debtors, being people who:

- own or have equity in their home (because under bankruptcy, the debtor would lose the home) or earn an income in excess of threshold for repayments under the *Bankruptcy Act*; or
- would have their employment restricted by bankruptcy, for example, company directors.

Recent statistics from the Australian Financial Security Authority show that debt agreements are at an all-time high, now accounting for 40% of personal insolvencies.[12] The growing use of debt agreements is concerning given that our casework experience reveals that many consumers are entering debt agreements that are plainly unsuitable for their circumstances. Many people entering a debt agreement appear to be unaware of their other, often better, options (such as temporary hardship variation or bankruptcy) and without understanding the true consequences of the debt agreement. This is likely due to a combination of:

- the financial incentive for debt agreement brokers and administrators to place people into a debt agreement rather than a temporary hardship variation or bankruptcy;
- heavy (and occasionally misleading)[13] advertising of debt agreements, despite the *Inspector-General Practice Guideline 1: Guidelines relating to advertising and marketing of debt agreements (July 2016)*;[14]
- inappropriate entry thresholds which see people on low incomes or social security payments making repayments to creditors that they can't afford and would not have to make if properly advised of more appropriate debt solutions.

Consumer advocates are concerned about the lack of effective dispute resolution for debtors in unsuitable debt agreements. Debt agreement administrators must be registered and are regulated by the Australian Financial Security Authority. However, administrators are not required to be a member of an ASIC-approved industry ombudsman scheme. This is anomalous in that, unlike most other aspects of the financial system, the only dispute resolution forum is a superior court.

Nora's story

Nora works as a carer, earning approximately $1,400 per fortnight. She is approaching retirement, with approximately $50,000 in superannuation. She lives in a caravan which is 40 years old and worth very little, and owns a car worth $900. Nora's part IX debt agreement proposal states that she has $30,950 in unsecured debts with two creditors.

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[12] https://www.afsa.gov.au/statistics/quarterly-statistics-commentary.

[13] Consumer Action Law Centre, *Fresh start or false hope: A look at the website advertising claims of debt agreement administrators* (April 2013) available at: http://consumeraction.org.au/wp-content/uploads/2013/05/Fresh-start-or-false-hope-April-2013.pdf.

[14] https://www.afsa.gov.au/about-us/practices/inspector-general-practice-guideline-1.

Worried about her debts, Nora called a registered Debt Agreement Administrator (**DAA**) after seeing an ad on TV promising that it 'would stop all interest and make it easier to pay.'

As a result of the call, a man came to her home on the same day. He was only there for about half an hour. He said that if Nora paid $1,800, the DAA would negotiate with her creditors to stop interest, and that she would be able to make payments to pay off the debts. He did not say how much the payments would be, and he did not mention any further fees to be paid to the DAA. She showed him a payslip and a rent receipt. The DAA did not mention any of Nora's other options to manage her debts, like informal negotiations or bankruptcy.

Nora signed an agreement and a direct debit form for the DAA to take $300 per fortnight towards the set-up fees (being $1600 to the DAA and a $200 government charge). The DAA then provided her with a pre-filled debt agreement proposal. Under the proposal, Nora would repay $21,569 to her unsecured creditors and pay fees totalling $7,930 to the DAA.

The debt agreement proposal contains information that is not based on Nora's instructions. For example, in response to the question '*What have you done to manage your debt?*' the DAA has pre-ticked the box '*Contacted your major creditors to obtain relief or hardship assistance*'. Nora instructs that she has not done this.

The debt agreement proposal states that Nora's uncommitted income, before debt repayments and the DAA's fees, is $244 per fortnight. Despite this, the DAA fee for preparing the proposal was $300 per fortnight – putting her budget into deficit for 5 consecutive fortnights before she even makes a repayment to her creditors.

Nora did not sign the proposal and saw a financial counsellor. Her financial counsellor's view is that informal arrangements with creditors would have been more appropriate than a debt agreement. In Consumer Action's view, bankruptcy also would have been a better option than a debt agreement. None of Nora's assets would be lost in bankruptcy, and she would not have to make repayments to creditors from her income, or when she retired and realised her superannuation.

Nora paid $900 to the DAA before receiving assistance from her financial counsellor and Consumer Action. If Nora had proceeded with the debt agreement proposed by the DAA, she would have paid $31,720 – more than her total debt.

Source: Consumer Action Law Centre

Recommendation 7

Debt Agreement Administrators should be a member of an ASIC-approved ombudsman scheme as a requirement of registration.

Credit representatives

Information request: 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?

Consumer advocates are mindful of the costs for industry and ASIC associated with compulsory EDR membership for credit representatives. Where the lender or broker is also a member of an ombudsman scheme, there may be little additional benefit in the credit representative also maintaining EDR membership.

We would support the removal of the requirement for credit representatives to be a member of an ASIC-approved EDR scheme on the following conditions:

- credit representatives be required to cooperate with the industry ombudsman scheme, for example, by providing information and documentation;
- a searchable public list of all credit representatives and the license under which they operate is maintained so that complaints can be directed to the appropriate body;
- credit representatives be under a specific obligation to facilitate dispute resolution, for example, by putting the consumer in touch with the licensee;
- the licensee be liable for the conduct of the credit representative even where the credit representative acts outside the authority of the licensee, including in cases of fraudulent or illegal activity; and
- these changes are reviewed two years after implementation to ensure that there are no gaps or unintended consequences.

SUPERANNUATION DISPUTES

New superannuation industry ombudsman scheme

Draft Recommendation 4: The SCT should transition into an industry ombudsman scheme for superannuation disputes

Consumer advocates strongly support the SCT's transition to an industry ombudsman scheme.

We refer to our comments on the broad approach and Recommendation 1(a), above. Our primary position remains that the best framework for dispute resolution in the financial system is a single industry ombudsman scheme for all disputes, including superannuation. In our view, the best way to achieve this is to integrate the SCT and CIO into FOS, rather than creating two new schemes.

An immediate move to a single scheme for all disputes in the financial system is a sensible approach, which would necessitate only one transition (SCT to single scheme) instead of two (SCT to separate scheme to single scheme). A single scheme could work collaboratively with the superannuation industry and stakeholders to develop procedures and approaches that reflect relevant product differences. Importantly, a single ombudsman scheme would be best

placed to resolve the jurisdictional overlap and inconsistencies that currently exist between FOS and the SCT, as identified in the Interim Report.

However, if the Panel considers that a new superannuation ombudsman is necessary as an interim step on the path to an eventual merger with the financial, credit and investments ombudsman scheme, then we support this development.

We agree with the Panel's draft findings in respect of the Superannuation Complaints Tribunal. The long-standing problems with the SCT cannot be fully resolved within a statutory tribunal structure, even with reforms to its funding and governance.

Indeed, the SCT's transition to an industry ombudsman scheme was recommended over 15 years ago. In 2002, the Productivity Commission undertook a thorough review of dispute resolution in superannuation in its *Review of Certain Superannuation Legislation*. Consistent with Draft Recommendation 4, the Productivity Commission recommended that:

> The *Superannuation (Resolution of Complaints) Act 1993* should be repealed, subject to some transitional arrangements.
>
> All superannuation entities regulated by the Australian Prudential Regulation Authority should be required to join a dispute resolution scheme approved by the Australian Securities and Investments Commission. This should be mandated as part of the compliance requirements of those superannuation entities. [15]

Superannuation customers should not have to wait any longer to access the free, fair, fast, and accessible dispute resolution that can be offered by an industry ombudsman scheme model.

It is important that the new superannuation industry ombudsman scheme builds upon the success of existing industry ombudsman schemes, particularly FOS, and does not attempt to reinvent the wheel. The beneficial features of the SCT, such as its industry knowledge, expert staff and unlimited jurisdiction, should be retained in the new scheme.

We note that amendments to the *Superannuation Industry (Supervision) Act 1993* (Cth) may be necessary to permit superannuation trustees to delegate decision-making to the ombudsman scheme.

We refer to our comments and Recommendation 2(c) above on disputes about life insurance through superannuation.

Death benefit disputes

We note that there has been some concern expressed about the ability of an industry ombudsman scheme to bind non-participating third parties to its decisions.

The decisions of an industry ombudsman scheme are binding on the financial service provider, but not on the consumer. If unsatisfied with the outcome at the ombudsman, an aggrieved consumer can take their dispute to court. Similarly, the decisions of the SCT are binding on

[15] Draft Recommendation 8.2. See http://www.pc.gov.au/inquiries/completed/super/report/super.pdf.

the super trustee. If unsatisfied with the outcome at the SCT, an aggrieved third party beneficiary can take the dispute to court.

We note that there may be an issue where a third party beneficiary does *not* participate in the dispute. The SCT determination, if not appealed, will apply and the trustee is bound to comply with it and distribute the funds in accordance with the SCT's decision. The non-participating third party then has approximately 15 years to take action against the beneficiary to whom the death benefit was paid. In practice, however, it is very rare for the non-participating party to do so down the track, for the simple reason that the distributed funds are no longer there.

We note that, in terms of access to justice and the timely resolution of disputes, any death benefit dispute with a non-participating party bound by the decision of a dispute resolution scheme—be it the SCT on ombudsman scheme—is less than ideal. It is in everyone's interest for all relevant parties to participate in the dispute and achieve a final resolution of the matter.

We encourage the Panel to investigate any potential issues raised by an industry ombudsman scheme making determinations that affect the rights of a non-participating third party.

Superannuation Code of Practice

Draft Recommendation 5: The superannuation industry should develop a superannuation code of practice

We strongly support Draft Recommendation 5.

Consumer groups have a long history of working with industry to set minimum standards through the use of industry codes of practice. Codes have become common in financial services and are important in setting expectations between industry and consumers, including small business. Codes can be useful in setting minimum standards and have the potential to raise confidence in the industry as a whole. Codes also have the advantage of being more flexible than legislation and can therefore adapt to changes in consumer demand.

We are aware that the superannuation industry is working to develop a code which aims to address a number of community concerns in relation to life insurance provided within default superannuation products.[16] We understand that the code development working group have prioritised:

- the impact of premiums on account balances, including the right cover for younger people;
- addressing duplicate default insurance policies;
- improving claims handling practices; and
- improving superannuation fund member communications on insurance, especially around 'opt-in' and 'opt-out'.

While these are good first steps and areas of keen interest for consumers, the proposed code is limited in that it does not aim to cover broader aspects of superannuation service provision. The proposed does not cover other conduct by superannuation trustees, fund managers and

[16] https://investmentmagazine.com.au/2016/12/minto-to-head-working-group-for-insurance-in-super.

services providers generally, for example, in relation to death benefit claims, investments and service complaints. This likely to undermine the efficacy of the proposed code. For example, the proposed code is looking to set standards for communication around life insurance products. Without also setting standards for how superannuation product information is communicated in general, there is the potential for the creation of multiple sources of information, which are not streamlined and further contribute to the problem of 'information overload' for consumers.

Any proposed code needs to start with a holistic review of information requirements, claims and complaints handling processes in superannuation and group insurance, as well as conduct by superannuation trustees, fund managers and service providers generally. Failing to do so will lead to piecemeal policy development that does not adequately address the underlying problems consumers face in dealing with the superannuation market.

THE NEW SCHEMES: OTHER MATTERS

Accountability and Oversight

Consumer advocates strongly support Draft Recommendations 6 and 7.

We recommend that ASIC's funding be increased to ensure it is adequately resourced to undertake enhanced oversight of the two new ombudsman schemes. We note, however, that an eventual merger of the two schemes into a single industry ombudsman scheme for all financial system disputes would reduce the cost of regulatory oversight.

Information request: On what matters should ASIC have the power to give directions? For example, should ASIC be able to give directions to governance and funding arrangements and monetary limits?

Consumer advocates support an increased role for ASIC in the oversight of schemes, but not to the extent that the new scheme effectively becomes a statutory scheme.

There is a trade-off between flexibility and responsiveness of the existing industry ombudsman schemes and increased oversight by ASIC. One of the advantages of the existing industry ombudsman model, particularly by comparison to courts and tribunals, is its ability to respond quickly and flexibly to changing circumstances and needs. ASIC's oversight should not to detract from the important role of the board. The board should remain responsible for the achievement of the scheme's objectives. However, ASIC shouldn't have a hands-off position either.

We also note that ombudsman schemes in the financial system exist to deal with disputes about a wide range of matters, not just those covered by ASIC legislation.

One example of the increased role that ASIC could play is ensuring greater accountability for the response to, and implementation of, recommendations of periodic independent reviews.

ASIC should also have sufficient powers to ensure that the ombudsman schemes comply with the Benchmarks for Industry-based Customer Dispute Resolution. If a scheme is failing to

meet a benchmark, ASIC should be able to give directions to the scheme to remedy the problem.

These changes could be implemented through amendments to ASIC Regulatory Guide 139: Approval and oversight of external dispute resolution schemes.

Recommendation 8

a. ASIC should be appropriately resourced to undertake increased oversight of industry ombudsman schemes.
b. ASIC should be able to give directions to the new ombudsman schemes to remedy any failure to comply with the Benchmarks for Industry-based Customer Dispute Resolution.

Ombudsman powers

Information request: Should schemes be provided with additional powers and, if so, what additional powers should be provided? How should any change in powers be implemented?

We recommend the following additional powers for the two new ombudsman schemes:

- power to obtain information and documents;
- mandatory discovery and open exchange of information between the parties;
- fair compensation for loss and damage, including non-financial loss;
- penalties that are a multiple of any losses;
- power to award greater penalties for breaches of responsible lending;
- power to waive debt in circumstances of long-term financial hardship; and
- power to direct the financial firm to take steps that are just and appropriate, enforceable by injunction.

These additional powers should be implemented through changes to the schemes' terms of reference in consultation with consumer advocates, with education for traders and consumers.

Billie's story

Billie fled a domestic violence relationship and feared for her and her child's safety. She packed her essentials in a car that she was forced to take out a loan to purchase for her ex-partner and drove from the Eastern States to Western Australia. On arriving in WA, Billie stayed at a women's refuge, and, using the small savings she had, registered the vehicle in WA and made some small repayments on the loan. Billie was referred to CCLSWA by a financial counsellor.

As a first step, CCLSWA made a document request to the lender's IDR, which was then escalated to EDR. Subsequently a complaint that the lender had breached its responsible lending obligations was lodged. In the meantime, Billie surrendered the car to the lender, which was sold at auction, and the proceeds were used to repay part of the loan. At this stage, Billie had moved out of the refuge, but she was unable to find work and her only income was Centrelink benefits. The proceeds from the sale of the car only repaid part of the debt. Even if the responsible lending claim was successful, Billie was still liable to repay

the part of the principal that was still owing. The EDR scheme was unable to compel the lender to waive the shortfall debt, even though the responsible lending claim was strong, and even though the client was in severe financial hardship. Eventually, the lender waived the debt as a gesture of goodwill. The process from lodging the initial document request letter at IDR to having the shortfall debt waived took one year.

Had there been a power for EDR schemes to either waive debts for long term hardship, award fair compensation for loss or damage, or award greater penalties for breaches of responsible lending, this would have been far less stressful for Billie and would have saved CCLSWA's resources.

Source: Consumer Credit Legal Service WA

FOS and CIO currently have the power to request information and documents from parties and, if not provided, make an adverse inference. Some consumer advocates have raised concerns that, in practice, the schemes tend not to use these powers. Even when the schemes do request documents, financial services providers do not always provide the relevant information or documents. This is problematic where the documents held by a financial service provider are needed to prove its unlawful conduct. If the ombudsman scheme does not compel the financial service provider to provide all relevant documents, then it may not have sufficient information to make appropriate findings of fact and come to a fair and just determination. Consumer advocates support mandatory discovery powers for the new schemes to overcome these difficulties.

We recommend that new schemes require the financial firm to provide all relevant documents in a dispute. In the digital age, competent and well-managed financial service providers should be able to provide all relevant documents quickly in digital format. As such, this requirement should not unduly delay the proper resolution of a dispute nor impose a significant time or cost burden on the financial firm.

Recommendation 9

The new ombudsman schemes should be provided with the following powers in addition to the powers of the existing schemes:

- Power to obtain information and documents
- Power to require mandatory discovery and open exchange of information between the parties
- Power to award fair compensation for loss and damage, including non-financial loss
- Power to award penalties that are a multiple of losses
- Power to award greater penalties for breaches of responsible lending
- Power to waive a consumer's debt in circumstances of long-term financial hardship
- Power to direct a financial firm to take reasonable steps, enforceable by injunction

The additional powers should be implemented through changes to the schemes' terms of reference, in consultation with consumer advocates, with education for traders and consumers.

Decision-making

Use of Panels

Draft Recommendation 8: The new industry ombudsman schemes should consider the use of panels for resolving complex disputes. Users should be provided with enhanced information regarding under what circumstances the schemes will use a panel to resolve a dispute

Contributors to this submission expressed varying views on the use of panels. Some indicated that single ombudsman decisions, for example in banking and insurance decisions at FOS, have been of high quality in complex cases without the use of panels. Others stated that consumer representatives on panels can be useful in ventilating relevant issues that aren't always articulated by the consumer (particularly an unrepresented consumer) during decision-making. Others observed that the external input from industry and consumer representatives on panels is useful to ensure the ombudsman scheme does not become 'stuck in its ways'.

Consumer advocates agree that, where panels are used, the scheme should develop and publish clear guidance on when a particular dispute will be referred to a panel for determination. Even low-value claims can raise complex issues that require careful investigation. One consumer representative suggested there could have a series of triggers for referral to a panel, such as:

- complexity;
- where requested by the consumer;
- where the dispute raises a systemic issue;
- where the matter has been flagged by consumer groups as an issue of concern; and/or
- where the value of the claim is over a certain threshold.

All contributors agree that, should the schemes use expert panels, the consumer representative should be a suitably qualified person with genuine consumer experience. It is apparent that FOS has had some difficulty in recruiting suitably qualified panel members with consumer experience. There have been, on occasion, situations where the career and experience of the consumer representative would be more accurately described as industry experience.

Investigation

One area of concern is decision-making during the earlier stages of case management. We consider that determinations made by a lead ombudsman or expert panel are generally of very high quality. However, only a very small number of disputes reach an ombudsman or expert panel. It is important that early case management is staffed by experienced and skilled case managers that can identify all relevant issues, whether or not those issues were raised directly in the consumer's application. This is particularly important for unrepresented consumers. Unlike financial service providers, consumers are largely unaware of the relevant laws and, thus, the potentially unlawful conduct engaged in by the firm. We expanded on our concerns about inconsistent and inferior outcomes for unrepresented consumers in our Initial Submission at page 43.

This can occur in the overlap between financial hardship and responsible lending laws. Take the example of a person who has struggled to repay their loan from the outset, attempted to negotiate a hardship variation unsuccessfully, and then lodged a financial difficulty dispute at FOS. Under the responsible lending provisions of the *National Consumer Credit Protection Act 2009*, a lender is prohibited from entering into a loan if it is likely that the borrower could only comply with their obligations under the loan with substantial hardship.[17] Given that the consumer has struggled to pay their loan from the outset, this would suggest a breach of Act, entitling the consumer to a refund of all interest, fees and charges – much more than a simple hardship variation. Most consumers are not aware of the intricacies of the Act, and it generally requires a financial counsellor or lawyer to identify the breaches of the responsible lending laws. Where the consumer is unrepresented, it is incumbent upon a skilled case manager at the ombudsman scheme to:

1. identify the potential responsible lending breaches at an early stage; and
2. request the relevant documents such as the assessment of suitability (which the consumer is unlikely to hold) to investigate the financial firm's conduct.

Given that the vast majority of consumers are unrepresented, and thus unlikely to identify all relevant legal claims, it is important that the new schemes take the time to properly investigate all apparent claims during case management, rather than taking a narrow approach based on the consumer's application.

Indeed, one of the great advantages of the industry ombudsman model over the adversarial approach of a tribunal or court is its ability to *investigate* a person's complaint. Thus, it is essential that the new ombudsman schemes investigate all apparent claims on the information available, whether or not specifically identified in the complaint. This will ensure fair outcomes and assist in the identification of systemic issues.

Quality assessment

There can be a trade-off between the quality and timeliness of decision-making in ombudsman schemes. While timeliness is important, we don't want this to be at the expense of quality and the fair resolution of disputes.

The assessment of whether decision-making is fair and high-quality must go beyond satisfaction surveys. While surveys are useful in identifying trends, consideration must also be given to feedback from vulnerable and unrepresented consumers, and periodic external quality assessment, including file audits.

File review processes are expensive but valuable from time to time. File audits can serve to challenge internal wisdom and bring a new perspective for the benefit of decision-making in future disputes. We recommend that a random selection of disputes be periodically externally quality-assessed. The quality assessment should encompass whether the outcome was fair and legally correct, as well as the appropriateness of the conduct of the dispute resolution process. If some public transparency is given to the external assessment process, this can also build stakeholder confidence and enhance the credibility of the dispute resolution scheme.

[17] See, for example, section 133 and Chapter 3 generally.

Hilda and Gary's story

Hilda and Gary jointly owned a home. Gary made a modest income from his small business and was 6 years from retirement. Hilda received social security payments and was a full-time carer for their two children with disabilities. Despite their modest incomes, the bank advanced Gary and Hilda approximately $125,000 by way of two Viridian Lines of Credit and a home loan. The bank failed to request any information or supporting documentation to demonstrate their capacity to service the proposed loans. The only information that the bank obtained was a credit report, which showed over $27,000 of debt.

Consumer Action assisted Hilda and Gary to take their dispute to FOS. FOS's Recommendation was largely in favour of the bank. Despite having made no enquiries about Hilda and Gary's actual income and expenses, the case manager found that the bank had made all reasonable enquiries. Consumer Action, recognising that this finding was contrary to the responsible lending laws, assisted Hilda and Gary to progress their dispute to the next stage. The Determination was largely in favour of Hilda and Gary, and their home was saved from repossession by the bank.

If they had accepted the Recommendation, Hilda and Gary would have lost their home.

Source: Consumer Action Law Centre

Recommendation 10

a. The new schemes should review decision-making models to ensure that decision-making is effective and fair at all stages of a dispute.

b. The new schemes should properly investigate all apparent claims, rather than taking a narrow approach to the definition of the dispute.

c. A random selection of disputes should be periodically externally quality-assessed. The quality assessment should encompass whether the outcome was fair and legally correct, as well as the appropriateness of the conduct of the dispute resolution process.

INTERNAL DISPUTE RESOLUTION

Draft Recommendation 9: Financial firms should be required to publish information and report to ASIC on their IDR activity and the outcomes consumers receive in relation to IDR complaints. ASIC should have the power to determine the content and format of IDR reporting.

Consumer advocates strongly support Draft Recommendation 9.

Some industries are already moving towards increased data reporting. For example, the General Insurance Code of Practice Code Governance Committee published its first *General Insurance Industry Data Report 2014-15*, which included data on claims and stage two IDR collected from Code subscribers.[18] The Committee observed that:

[18] General Insurance Code Governance Committee, *The General Insurance Industry Data Report 2014-2015*, page 31.

> This exercise revealed gaps and inconsistencies in the data, and underscored for us just how important data integrity is. Over the coming year, we will be working closely with industry to build a firm foundation for better data collection. The aim is not to impose an onerous new set of obligations, but to ensure that industry has the information it needs for proactive and continual improvement.[19]

While detailed and useful report, we note that it does not include data about stage one IDR. We refer to our concerns, case studies and recommendations about multi-tiered IDR in our Initial Submission at pages 17-19.

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

At present, it is impossible to compare all financial firms on their IDR performance. This is due to different reporting among firms, and a lack of reporting by others. We recommend that IDR reporting include, at a minimum, the following metrics:

- number and type of complaints/disputes;
- length of time to finalise a dispute;
- outcome (resolved and in whose favour, withdrawn, abandoned, and unresolved);
- certain demographical information about complainants (e.g. age, region)
- number of contacts with consumer necessary to resolve complaint; and
- any other metrics deemed appropriate by ASIC.

It may be appropriate for different data to be collected in different industries or for different products. For example, insurers should report on both phases of multi-tiered IDR, including the number of complaints not pursued to stage two. It would be useful for insurers to report on the reason for claim denial and, for claims/disputes regarding insurance products with multiple components (e.g. consumer credit insurance with unemployment, life/trauma and disability coverage), a breakdown of claims/disputes by component.

Similarly, it may be appropriate to have different reporting requirements for smaller financial firms.

Essential to the success of an IDR reporting scheme will be clear and consistent terminology across all financial firms to ensure that the data is comparable and reflects, rather than obscures, IDR performance. Much can be hidden in the clever use of statistics. If, for example, 'withdrawn' disputes includes those where the consumer fails to respond to a request for further information due complaint fatigue, this will mask poor IDR. Our Initial Submission details examples of complaint fatigue caused by poor IDR.[20]

At the very least, consumer advocates strongly recommend that financial service providers should have the same definition of ‘complaint’ and collect data about all complaints. We note that ASIC Regulatory Guide 168 already requires financial service providers to adopt the definition in the international standard (AS ISO 10002-2006), which refers to an expression of

[19] General Insurance Code Governance Committee, *General Insurance Code of Practice Annual Report 2015-2016*, page 1.
[20] See, for example, the case study on Rose at page 18.

dissatisfaction made to an organisation.[21] Despite this requirement there is a lack of uniformity so a compliance framework is needed. For IDR reporting to be useful, it is imperative that data is comparable.

A suitable transition period will be necessary to ensure all financial firms have sufficient time to update their systems to enable effective reporting. We consider that 24-36 months would be appropriate.

We recommend that participation in IDR reporting be a requirement of ASIC Regulatory Guide 165: Licensing: Internal and External Dispute Resolution.

Information request: 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, and should identify the financial firm. ASIC should do so in response to:

- information collected by ASIC, including through the proposed IDR reporting requirement;
- complaints by a sufficient number of customers; and
- complaints by recognised consumer groups.

A well-functioning financial system depends on well-informed customers who are able to make choices in their own interests. For this reason, we support the naming of problematic firms to reduce information asymmetry and encourage a culture of compliance and continuous improvement.

Draft Recommendation 10: Schemes should register and track the progress of complaints referred back to IDR

We strongly support Draft Recommendation 10.

Consumers are often confused when they are referred back to IDR after lodging a complaint with an ombudsman scheme. The referral back to IDR is not well understood by consumers. It can cause complaint fatigue and otherwise result in poor outcomes for consumers. Draft Recommendation 10 has benefits for consumers, including:

- incentivising financial firms to address complaints promptly;
- reassuring consumers that their dispute will be considered;
- reducing complaint fatigue;
- assisting the scheme to measure the effectiveness of IDR and identify systemic issues; and
- that it does not require the consumer to understand the intricacies of ASIC Regulatory Guide 165 and the varying time limits for IDR.

We refer to the recommendations in our Initial Submission at pages 15-16 on reducing IDR timeframes for simple disputes.

[21] ASIC Regulatory Guide 165.78.

Recommendation 11

a. The IDR reporting regime should require clear and consistent terminology across all financial firms to ensure the data is comparable.

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

LAST RESORT COMPENSATION SCHEME

Panel observation: The Panel is of the view that there is considerable merit in introducing an industry-funded compensation scheme of last resort.

Consumer advocates agree with the Panel's observation. We refer to our detailed comments on the impact of uncompensated losses in our Initial Submission at pages 72-78 and make the following additional recommendations on design of the last resort compensation scheme.

Scope

The compensation scheme should apply to all financial service providers, including credit licensees and operators of managed investment schemes, and all relevant unpaid determinations of courts and industry ombudsman schemes. The compensation scheme should not be limited to Australian Financial Services Licensees for failures in financial advice.

Trust and confidence in the financial sector is low. A series of financial scandals have left many Australians out of pocket and in some cases, resulted in the loss of the family home or a secure retirement. Scandals have occurred not just in relation to financial advice; many people have suffered loss that remains unremedied from the mis-selling of complicated investment products, collapse of managed investment schemes and predatory credit provision. Indeed, the banking, finance and insurance sectors are perceived to be the least ethical sectors of our economy.[22]

It is critical that the establishment and design of a last resort compensation scheme builds trust and confidence in the financial sector as a whole. To do so, the compensation scheme must be broad in its scope. If it does not cover all relevant unpaid determinations of an ombudsman scheme or court, the community will continue to lack trust in the financial sector. From a consumer's perspective, it matters little whether their uncompensated loss arises out of financial advice or another financial product or service—what matters is that despite a meritorious complaint, their loss remains uncompensated. As the Panel observed, consumers should be able to expect that financial products and services will be appropriate and perform in the way they were led to believe and, where they do no, have access to effective redress. Effective redress should not depend on whether or not financial advice was involved.

[22] Governance Institute of Australia, *Ethics Index*; see also Clancy Yeates, *Ethics survey: Banking, media and big business on the nose*, Sydney Morning Herald (20 July 2016) available at: http://www.smh.com.au/business/banking-and-finance/ethics-survey-banking-media-and-big-business-on-the-nose-20160719-gq9f5h.html.

The inclusion of credit disputes in the compensation scheme is unlikely to place an undue burden on industry. Successful credit disputes generally result in a change to the terms of the contract (for example, a hardship variation) or waiver of debt. It is far less common for a determination in a credit dispute to result in an award of compensation to the consumer. However, in circumstances where it does, and in the rare case that the credit provider becomes insolvent or is otherwise unable to pay, that consumer should be entitled to claim compensation from the last resort scheme.

It will also be important for the compensation scheme to be available in relation to other 'product' failures, not just where financial advice was deficient in relation to a product. For example, a dispute may arise where a particular investment product has defective or misleading disclosure and any loss is not caused by advice alone.

Similarly, a consumer's ability to obtain compensation should not depend on which forum heard their dispute. The compensation scheme should cover people with unpaid court judgments against a financial service provider that would otherwise be covered by the compensation scheme. It is important that the design of the scheme does not distort consumer choice about dispute resolution forums. Again, it is rare for a consumer to choose to take their dispute to court instead of the relevant industry ombudsman scheme, so the additional burden on the compensation scheme would be minimal. There are reasons why consumers may want to take their matter to a court. For example, it is a much more transparent dispute forum. Moreover, consumers have a right to take their matter to a court should the EDR scheme not decide in their favour.

It might be argued that allowing court awards to be claimable on a compensation scheme of last resort would 'encourage' class actions. This is not a valid concern. First, an effective financial sector dispute resolution system should facilitate compensation for all losses. It does not matter whether this loss is remedied through an EDR scheme (including through any systemic investigation) or through courts (including through class actions). While an EDR scheme is most often preferable, because a consumer does not have to incur legal costs in gaining a remedy, there will be occasions where courts are appropriate, including, for example, where it is an untested area of law and the EDR scheme refuses to investigate. Second, so as to avoid incentives for private lawyers to advance claims in courts, the scheme could ensure that legal costs are not claimable. In Victoria, the Motor Car Traders' Guarantee Fund (a last resort compensation scheme), does not allow claims for legal costs or loss of wages as a result of pursuing the matter against a licensed motor car trader.[23]

These inclusions in the scope of the last chance compensation scheme will enhance trust and confidence in the financial sector.

Retrospectivity

Consumer advocates strongly support a retrospective scheme. The form of retrospectivity should be a wide as possible. This includes, at a minimum, people with unpaid EDR determinations. However, there is also a class of people with uncompensated losses who did not proceed with an ombudsman complaint because they were told at the outset that the

[23] See https://www.consumer.vic.gov.au/motor-cars/compensation-claims.

process was futile as their financial service provider could not satisfy any determination. The compensation scheme should also include this class of people.

Process

The scheme should only be available for claims after all avenues have been exhausted, including a relevant award from an ombudsman scheme or a court and a claim on professional indemnity insurance. It is, in this respect, 'last resort'. However, should an award be unpaid, the process should be a seamless as possible from the consumer perspective. Further, the compensation should not require, as a precondition to compensating an affected consumer, that the ombudsman scheme has taken legal action to enforce its determination. Any such requirement would simply delay compensation for the consumer and add further cost for the ombudsman scheme and, in turn, industry.

The ombudsman scheme's right to take legal action under the tripartite agreement to enforce its determination could be transferred to the last resort compensation scheme after the consumer has been compensated by the scheme. That is, the compensation scheme could recover from the financial service provider on a subrogated basis.

Recommendation 12

An industry-funded compensation scheme of last resort should be introduced. The compensation scheme should:

a. apply to all financial services providers, including credit licensees and operators of managed investment schemes;
b. only accept claims from retail clients (consumer claims) and operate as a last resort scheme, that is, only be available for claims after all avenues have been exhausted, including a relevant award from an EDR scheme or a court and professional indemnity insurance;
c. not require an ombudsman scheme to enforce its determination in court as a precondition to compensating an affected consumer; however, after the scheme has compensated the affected consumer, the scheme should be able to recover from the financial service provider on a subrogated basis;
d. involve people with relevant industry and consumer experience in its governance, based on the existing industry ombudsman model;
e. award compensation at levels aligned with EDR caps that are reviewed and increased over time.
f. be retrospective in application;
g. be funded by industry, through a levy imposed by the government.

FUNDING

An essential element of an effective and efficient dispute resolution and complaints framework in the financial system is access to free and independent legal and financial counselling advice. As discussed above, we strongly support the extension of ombudsman scheme coverage to disputes about superannuation, small business lending, lending for investment

purposes and debt management firms. As part of these changes, consideration should be given to funding appropriate services to assist people, particularly those experiencing disadvantage or vulnerability.

The existing dispute resolution framework places a heavy reliance on financial counsellors, community legal centres, and legal aid commissions to function properly. This reliance may be appropriate but increasingly problematic given the increasingly under-resourced nature of the sector.[24] For example, in South Australia there have been substantial cuts to community legal centre funding and there is no legal aid funding for civil disputes.

While ombudsman schemes are more accessible than the court system, in practice, vulnerable people often need advice and assistance to navigate the system. Many consumers are simply overwhelmed by the process, compounding the stress arising from the substantive issues in dispute.

If the inadequate funding of financial counselling, community legal centres and legal aid commissions persists, people—particularly those experiencing vulnerability or disadvantage—will continue to significant barriers to effective, affordable dispute resolution in the financial system.

Recommendation 13

Adequately fund legal and financial counselling services for all aspects of the proposed dispute resolution framework in the financial system.

[24] The Productivity Commission recommended that the federal, state and territory governments provide additional funding of $200 million per annum for civil legal assistance services to address pressing gaps in services: *Inquiry Report: Access to Justice Arrangements* (December 2014), Recommendation 21.4.

The contributors to this submission would be pleased to discuss the issues addressed in this submission in further detail.

Please contact Policy Officer Cat Newton at Consumer Action Law Centre on 03 9670 5088 or at cat@consumeraction.org.au if you have any questions about this submission.

Yours sincerely

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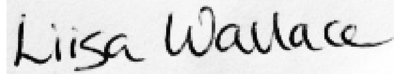

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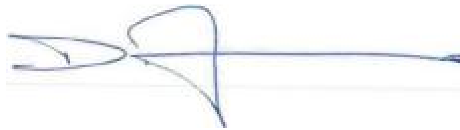

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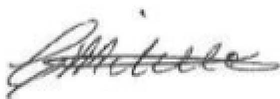

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APPENDIX A: ABOUT THE CONTRIBUTORS

Care Inc Financial Counselling Service and the Consumer Law Centre of the ACT

Care Inc. Financial Counselling Service has been the main provider of financial counselling and related services for low to moderate income and vulnerable consumers in the ACT since 1983. Care's core service activities include the provision of information, counselling and advocacy for consumers experiencing problems with credit and debt. Care also has a Community Development and Education program, provides gambling financial counselling as part of the ACT Gambling Counselling and Support Service in partnership with lead agency Relationships Australia; operates outreach services in the region and at the Alexander Maconochie Centre and makes policy comment on issues of importance to its client group. Care also operates the ACT's first No Interest Loans Scheme, which was established in 1997, and hosts the Consumer Law Centre of the ACT.

Caxton Legal Centre

Established in 1976, Caxton Legal Centre Inc. is Queensland's oldest community legal centre. Caxton is a non-profit community organisation providing free legal advice to people on low income or who face other disadvantage. Caxton has a specialist Consumer Law Service providing advice and assistance to people with legal problems arising out of consumer disputes and consumer credit contracts.

Consumer Action Law Centre

Consumer Action Law Centre is an independent, not-for-profit consumer organisation based in Melbourne. We work to advance fairness in consumer markets, particularly for disadvantaged and vulnerable consumers, through financial counselling, legal advice and representation, and policy work and campaigns. Delivering assistance services to Victorian consumers, we have a national reach through our deep expertise in consumer law and policy and direct knowledge of the consumer experience of modern markets.

Consumer Credit Law Centre South Australia

The Consumer Credit Law Centre South Australia was established in 2014 to provide free legal advice, legal representation and financial counselling to consumers in South Australia in the areas of credit, banking and finance. The Centre also provides legal education and advocacy in the areas of credit, banking and financial services. The CCLCSA is managed by Uniting Communities who also provide an extensive range of financial counselling and community legal services as well as a large number of services to low income and disadvantaged people including mental health, drug and alcohol and disability services.

Consumer Credit Legal Service (WA) Inc

Consumer Credit Legal Service (WA) Inc is a not-for-profit charitable organisation which provides legal advice and representation to consumers in WA in the areas of credit, banking and finance, and consumer law. CCLSWA also takes an active role in community legal education, law reform and policy issues affecting consumers. In the 2015 / 2016 financial year, CCLSWA provided comprehensive legal advice to 1350 clients on 1424 matters.

Consumers' Federation of Australia

The Consumers' Federation of Australia is the peak body for consumer organisations in Australia. CFA represents a diverse range of consumer organisations, including most major national consumer organisations. Our organisational members and their members represent or provide services to millions of Australian consumers.

Financial Counselling Australia

FCA is the peak body for financial counsellors. Financial counsellors provide information, support and advocacy for people in financial difficulty. They work in not-for-profit community organisations and their services are free, independent and confidential. FCA is the national voice for the financial counselling profession, providing resources and support for financial counsellors and advocating for people who are financially vulnerable.

Financial Rights Legal Centre

Financial Rights is a community legal centre that specialises in helping consumers understand and enforce their financial rights, especially low income and otherwise marginalised or vulnerable consumers. We provide free and independent financial counselling, legal advice and representation to individuals about a broad range of financial issues. Financial Rights operates the Credit & Debt Hotline, which helps NSW consumers experiencing financial difficulties. We also operate the Insurance Law Service which provides advice nationally to consumers about insurance claims and debts to insurance companies. Financial Rights took over 25,000 calls for advice or assistance during the 2014/2015 financial year.

APPENDIX B: RESPONSE TO ARGUMENTS AGAINST THE MERGER OF FOS AND CIO INTO ONE SCHEME

Argument	Response
Bureaucratic Giant Syndrome A single ombudsman scheme in financial services would be prone to be monopolistic in its behaviour – dictating terms, rather than being responsive to stakeholder concerns about performance. A single scheme acting as a monopoly will become court-like and lose its consumer-friendly flexibility.	As ANZOA states, it is 'inappropriate to apply concepts of market forces and competition to what are effectively 'natural monopolies'. Other tried and tested, robust mechanisms such as independent reviews, strong consumer liaison functions, benchmarking, peer reviews and ASIC oversight can produce the benefits in a monopoly dispute resolution scheme. It doesn't follow that a single merged scheme will become a bureaucratic and monopolistic organisation. Lots of large private organisations that have near monopolies in their fields have stayed agile and flexible, such as Google, Amazon and Microsoft. In the EDR space, FOS's track record of stakeholder engagement – regularly surveying its members and applicants about how it can improve its dispute processes and piloting new ways of working to meet user needs – is on the public record and has broad third party endorsement. The success of the dispute process reengineering carried out by FOS in 2014-15 is a compelling example. Within one year, working with stakeholders, FOS re-engineered its dispute processes including a new registration and referral process, introduced a fast track process and improved the way it handles financial difficulty disputes. At the same time, it upgraded its case management system, introduced new technologies such as the online dispute form and the electronic statement of financial position, and enhanced its secure member portal. The changes enabled FOS to resolve disputes much more quickly (see FOS Submission to EDR Review Issues Paper (**FOS Submission**), page 57).

Competition Improves Efficiency Without competitive tension, turnaround times, service levels, innovation and continuous improvement would suffer, and there would be less incentive to keep costs in check and run the scheme efficiently.	Competition is an inefficient way to drive change Competition in EDR schemes is a poor and inefficient way to drive innovation and change. While one scheme may innovate and experiment with a change, it takes a significant amount of time for the other EDR scheme to follow, if they do at all. In the meantime, thousands of consumers lose out. Competition in EDR benefits members, not consumers Competition generally benefits the person or entity that has the choice of whether to acquire the good or service. For example, competition in financial services is generally seen to benefit the consumer as companies must compete with each other to attract consumers and therefore strive to produce what benefits or attracts the consumer (see Interim Report page 99). In the current EDR framework, it is the financial firms and not consumers that have the choice of which industry ombudsman scheme to belong to. In general terms, this means that there could be the potential for a scheme to provide a service which is valued by the firms, but which does not align with what is in the consumer's best interests (see Interim Report page 100). Perverse consequences to competition in EDR Competition may lead to manipulation of dispute resolution services, differing standards, and inconsistencies in decision making which could be adverse for consumers and participating organisations. Competition in EDR doesn't create efficient economies of scale ASIC has worked with industry to reduce the number of schemes, with resulting improvement in economies of scale and efficiency, the removal of uncertainty for consumers and financial investors, and the reduction in jurisdictional boundary issues. Following the merger of five EDR schemes into FOS in 2008 and 2009, there are now two ASIC-approved EDR schemes in Australia (see ASIC Submission to Financial System Inquiry). Competition is likely to add unnecessary and inefficient costs to Ombudsman services, e.g. inefficient duplication of infrastructure/resources/services/information systems, mechanisms to establish a 'common door' approach, and the need to provide information to consumers about different offices (ANZOA). There are other ways to drive innovation besides competition A range of other factors are stronger drivers for change and innovation within EDR schemes. These factors include: • consumer movement advocacy, policy development and campaigning;

Argument	Response
	• periodic independent reviews; and • individual actors within EDR schemes who (for a variety of reasons) drive proactive change within their organisations. The FOS dispute process is significantly different to that of CIO. The improvements FOS has made have seen the average time to resolve a dispute at FOS drop from 95 days in 2014-15 to 62 days in 2015-16. This has been achieved through collaboration with our members and consumer bodies (see FOS Submission page 56)
Systemic Issue Data One scheme would mean less sources of data for systemic issue spotting	The production of data from multiple organisations does not mean more systemic issues will be spotted. In fact, if the data is not collected in the same way it will not be easily comparable. Regulators may need to set up separate reporting and communication systems for different EDR schemes, creating extra work to collect different sets of data potentially about the same issues. In fact, consumer groups argue that competing sets of data would mean the value of the Ombudsman's office as a source of information and analysis to contribute to the ongoing improvement of an industry or service area will be diluted, to the detriment of consumers, service providers and the wider community (see our Initial Submission page 54).

Argument	Response
Member Choice A consolidation of CIO and FOS would mean financial firms who are dissatisfied with service levels or costs can't vote with their feet. Providers can choose the arrangements that benefit them the most (and consumers can choose the provider based on its choice of EDR scheme if they want)	ANZOA position is that competition among ombudsman schemes runs counter to the principles of independence, accessibility, fairness, efficiency, effectiveness and accountability. ANZOA asserts that poor performing financial firms may choose to join a scheme they believe is not as rigorous in its approach to complaints. In addition, ANZOA argues that a framework consisting of multiple schemes can impact negatively on firms in that: • it may lead to manipulation of dispute resolution services, differing standards and inconsistencies in decision making which could be adverse for both consumers and members; and • the value of the ombudsman scheme as a source of information and analysis to contribute to the ongoing improvement of an industry is diluted, to the detriment of consumers, financial firms and the wider community. (see Interim Report page 101). The existence of competition for members promotes 'forum shopping' with adverse impacts on balanced and fair outcomes for users of the scheme. The report on the independent review of COSL conducted in 2012, page 17: "In COSL's case, choices such as lukewarm support for a one-stop shop consumer call centre, an overemphasis on saving COSL resources by closing complaints at the pre-investigation stage or opting in its complaints handling for a narrow approach to the law and fairness can all be seen by stakeholders as evidence of 'competing' too hard for a favourable reputation with members" (see FOS Submission page 24). Financial service and credit providers acting rationally will choose the scheme where they are likely to pay lower fees (which may reduce resources available per complaint received) and that has processes and policies in its interest – not the interest of consumers (see our Initial Submission page 54). Finally, the argument that a consumer would choose a financial service provider based on its choice of EDR scheme is ludicrous. Consumers are one-off users of EDR, if at all, they have no experience from which to choose a provider based on the EDR scheme they belong to and are lucky to even know what one is before they have need to use it.

Argument	Response
Industry Segment Specialisation CIO & FOS represent different business sectors with different needs; Big end of town vs small end of town – little guys will be marginalised in FOS	FOS also has members from each of these sectors as well as a much broader range of services than CIO and has a depth of understanding about the products and services offered by all member types. 83% of FOS's licensee members are small entities and most of these had no disputes at FOS in the past financial year. FOS makes a significant investment in providing our smaller members with details about effective IDR processes and with information about how to avoid having disputes at FOS (see FOS Submission page 57). The supposed 'benefits' of having product specific Ombudsman schemes to consolidate expertise were disproven by the merger of schemes across several financial services sectors into FOS in 2008 and 2009. Indeed, with increasing convergence of insurance, advice and traditional banking and finance products, having separate schemes is likely to cause greater complexity and duplication. CIO's jurisdiction is more narrowly confined to corporation's law matters than that of FOS. This provides an incentive for forum shopping by financial firms, and leads to poorer consumer redress. The existence of two separate schemes prevents the joining of CIO members into a dispute at FOS (or vice versa). This problem may arise, for example, where the primary dispute is with a bank (FOS member) but involves a mortgage broker, or an authorised credit representative of a financial adviser, that is a CIO member (see FOS Submission page 54).
Benchmarking Performance Having two EDR schemes allows each scheme to benchmark its performance against the other. This produces better outcomes for financial firms and consumers because the schemes are forced to adopt best practice and improve their service offering.	The driver of change at FOS has not been competition from the CIO. It has been based on feedback from members and consumer organisations, identification of process improvements through FOS's own analysis of its dispute volumes and trends, and in response to recommendations from the Independent Review of FOS. FOS has significantly evolved over the past eight years and in 2015 re-engineered its dispute processes, delivering significant benefits to users. The innovation and re-design in its processes and technology enhancements has been achieved through strong collaboration with our stakeholders and best practice in other jurisdictions, not any comparisons with the CIO (see FOS Submission page 29).
Cost Passed on to Consumers One scheme could mean higher prices which would be passed on to consumers	It is not guaranteed that competition between schemes would result in lower cost for consumers. Instead competition could result in reluctance for schemes to accept disputes that go beyond the minimum jurisdiction, an outcome not beneficial to consumers (see Interim Report page 100).

Argument	Response
Unconstitutional and Un-Australian "It would be extraordinary for any government to mandate its citizens and businesses financially contribute to, and comply with, the requirements imposed by a private sector provider operating to the exclusion of all other providers" – like a compulsory super scheme with one industry super fund "Apart from being completely unacceptable and offensive to Australian norms, one wonders what its legal and constitutional basis is."	"Patriotism is the last refuge of a scoundrel" – Samuel Johnson As discussed above, a single merged EDR scheme should be seen as a 'natural monopoly', not unlike the court system which does not have competitors. Natural monopolies arise where the largest supplier in an industry, often the first supplier in a market, has an overwhelming cost advantage over other actual or potential competitors. We would argue FOS is already in this position in Australia. We don't have competition in courts. Also FOS is a not-for-profit, so the government is not endorsing a profit-making private sector provider. Other 'natural monopolies' that have been endorsed by government: Sydney Water, Australia Post, Sydney trains.

Re: The Enactment of an Anti-avoidance Provision in the Australian Consumer Credit Regime

Memorandum of Advice

1. I am asked to advise whether the Commonwealth parliament has sufficient legislative power to enact a general anti-avoidance provision in the *National Consumer Credit Protection Act 2009* (Cth) ("the Act").
2. I am instructed that the credit industry, notably the payday lending industry and consumer lease industry, has a long history both in Australia and overseas of developing schemes to avoid consumer protection regulation. As a consequence, the Consumer Action Law Centre has for many years called for an anti-avoidance provision, similar to that to be found in Part IVA of the *Income Tax Assessment Act 1936* (Cth). Such a proposal was included in the exposure draft of the *National Consumer Credit Protection Amendment (Credit Reform Phase 2) Bill* 2012 ("the Bill"). The proposed amendment is contained in Schedule 6 to the Bill. Subsequent to the change of the Commonwealth government in the 2013 election, the Bill did not progress beyond the submission of public comments on the exposure draft.
3. I am instructed that the Consumer Action Law Centre has been informed by Treasury that such an anti-avoidance provision would require an additional referral of powers from the States. Treasury has further advised that the relevant Council of Australian Government ("COAG") agreement expired on or about 1 July 2012, and the current government is not willing to revisit the issue with the States. Accordingly, it is the view of Treasury that without a further referral of power an anti-avoidance provision would have to be based on a patchwork of constitutional powers relying upon interstate trade and commerce or corporations powers, and that this would end up with credit providers avoiding the anti-avoidance provision.
4. I am further instructed that Treasury have foreshadowed the removal of two exemptions to the application of the Act, which have been used by some lessors to avoid the application of the Act. Treasury apparently has taken the view that the application of the Act to contracts which were previously excluded from the Act is similarly not subject to a referral of power from the States. Accordingly, Treasury is looking at other Commonwealth legislative powers, such as those identified in the preceding paragraph.

Background

5. In 2009 the Commonwealth passed the Act. This was pursuant to the National Credit Law Agreement 2009 ("the Agreement"), which was signed by the Commonwealth and each of the States and Territories on 7 December 2009. By reason of clause 2.2, each of the Commonwealth, States and Territories became bound by the Agreement from that date.
6. The Agreement provides for the enactment by State parliaments of State Referral Legislation, the enactment by the Commonwealth parliament of the National Credit Law [which is the Act] in reliance on the referrals, and the amendment from time to time of the National Credit Law in accordance with this Agreement and the State referral legislation.[1]
7. Clause 5.1(1)(c) specifically provided that the legislative scheme agreed to "*involves...the amendment from time to time of the National Credit Law in accordance with this Agreement and the State Referral Legislation.*"
8. In 2010 the Victorian Parliament passed the *Credit (Commonwealth Powers) Act* 2010 ("the Victorian Act"). Subsection 1(a) of the Victorian Act identifies that its purpose is to "*adopt the National Consumer Credit Protection Act 2009 of the Commonwealth (as amended) and the National Consumer Credit Protection (Transitional and Consequential Provisions) Act 2009 of the Commonwealth, and to refer certain matters relating to the provision of credit and certain other financial transactions to the Parliament of the Commonwealth for the purposes of section 51(xxxvii) of the Constitution of the Commonwealth.*"
9. This form of referral of power by the States and territories pursuant to section 51(xxxvii) of the Constitution by reference to identified text or texts is not novel[2]. It was done, for example, in a similar manner in the case of corporations[3] and terrorism[4].
10. In the Digest to the Bill, it is stated that "*[a]s a way to avoid these problems* [of ensuring the Commonwealth has power], *section 51(xxxvii) of the Constitution allows a State or States to adopt a Commonwealth law. In that case at least one State must*

[1] The Agreement Part 5.1.

[2] Generally see: "*New Directions in Co-operative Federalism: Referrals of Legislative Power and their consequences*" by Pamela Tait S>C., Solicitor-General for Victoria (as she then was), 18 February 2005, at [28] to [30]; "*After a Referral: The Amendment and Termination of Commonwealth Laws relying on s 51(xxxvii)*", by Andrew Lynch, (2010) 32 SLR 363, at pp.364 and 369

[3] Corporations (Commonwealth Powers) Act 2001 (Vic).

[4] Terrorism (Commonwealth Powers) Act 2003 (Vic).

have referred a matter to the Commonwealth. The Commonwealth is then empowered to enact a law about that matter which will also apply in the referring State. Once that has occurred, any other State or States can adopt the new Commonwealth law by passing a State law setting out the extent of the adoption and annexing the relevant Commonwealth law."[5]

Relevant Provisions of the Victorian Act

11. The following definitions contained in section 3 of the Victorian Act are relevant for my immediate purpose:

> "***amendment reference*** *means the reference under section 6(1)*"
>
> "***Commonwealth Credit instrument*** *means any instrument (whether or not of a legislative character) that is made or issued under the National Credit legislation;*"
>
> "***Commonwealth Credit instrument*** *means any instrument (whether or not of a legislative character) that is made or issued under the National Credit legislation.*"
>
> "***express amendment*** *of the National Credit legislation means the direct amendment of the text of the National Credit legislation (whether by the insertion, omission, repeal, substitution or relocation of words or matter) by another Commonwealth Act or by an instrument under a Commonwealth Act, but does not include the enactment by a Commonwealth Act of a provision that has or will have substantive effect otherwise than as part of the text of the National Credit legislation;*
>
> "***National Credit legislation*** *means—*
>
> > *(a) the National Consumer Credit Protection Act 2009 of the Commonwealth; and*
> >
> > *(b) the National Consumer Credit Protection (Transitional and Consequential Provisions) Act 2009 of the Commonwealth—*
> >
> > *as in force from time to time;*
>
> "***referred credit matter*** *means a matter relating to either of the following—*
>
> > *(a) credit, being credit the provision of which would be covered by the expression "provision of credit to which this Code applies" in the relevant version of the National Credit Code;*

[5] At p.4.

> *(b) consumer leases, being consumer leases each of which would be covered by the expression "consumer lease to which Part 11 applies" in the relevant version of the National Credit Code;*
>
> ***"relevant version of the National Credit Code** means the text of Schedule 1 to the National Consumer Credit Protection Act 2009 of the Commonwealth as originally enacted, and as later amended by the National Consumer Credit Protection Amendment Act 2010 of the Commonwealth;*
>
> ***"relevant version of the National Credit legislation** means—*
>
> *(a) the National Consumer Credit Protection Act 2009 of the Commonwealth as originally enacted, and as later amended by the National Consumer Credit Protection Amendment Act 2010 of the Commonwealth; and*
>
> *(b) the National Consumer Credit Protection (Transitional and Consequential Provisions) Act 2009 of the Commonwealth."*

12. I should immediately note, as it becomes of importance in this matter, that the definition of "express amendment" in the Victorian Act specifically contemplates the "*insertion, omission, repeal, substitution or relocation of words or matter*". The question asked of me very much depends on what is meant by those words. As a matter of statutory interpretation that is not the problem, rather it is the context of the referral to which they relate that may cause a problem.
13. Subsection 4(1) of the Victorian Act provides that the "*relevant version of the National Credit legislation is adopted within the meaning of section 51(xxxvii) of the Constitution of the Commonwealth.*"
14. Subsection 6(1) of the Victorian Act provides that, subject to section 7 (which for my immediate purpose is irrelevant) "*any referred credit matter is referred to the Parliament of the Commonwealth but only to the extent of the making of laws with respect to such a matter by making* ***express amendments*** *of the National Credit legislation.*" [My emphasis]
15. Section 9 of the Victorian Act is also relevant, it is as follows:

> *"For the avoidance of doubt, it is the intention of the Parliament of the State that—*
>
> *(a) the National Credit legislation may be* ***expressly amended****, or have its operation* ***otherwise affected****, at any time after the commencement of this Act by provisions of Commonwealth Acts the operation of which is based on any legislative powers that the Parliament of the Commonwealth has on account of a reference of any matters, or the adoption of the relevant version of the*

> *National Credit legislation, under section 51(xxxvii) of the Constitution of the Commonwealth; and*
>
> *(b) the National Credit legislation may be* ***expressly amended****, or have its operation* ***otherwise affected****, at any time after the commencement of this Act by provisions of Commonwealth Acts the operation of which is based on legislative powers that the Parliament of the Commonwealth has apart from a reference of any matters, or the adoption of the relevant version of the National Credit legislation, under section 51(xxxvii) of the Constitution of the Commonwealth; and*
>
> *(c) the National Credit legislation may have its operation affected, otherwise than by express amendment, at any time by provisions of Commonwealth Credit instruments.*"

16. Attention should also be drawn to section 10 of the Victorian Act. It permits the "amendment reference" to be terminated without termination of the adoption of the relevant version of the National Credit legislation. The "amendment reference" means (as defined) the power under section 6(1) of the Victorian Act. I am not instructed that the "amendment reference" has been terminated, and accordingly it is a power still referred to the Commonwealth with respect to any "referred credit matter".
17. It is also necessary to have some consideration of the provisions of the Act and the National Credit Code ("the Code"). The definition of "Commonwealth Credit instrument" in the Victorian Act is "*any instrument...issued under the National Credit legislation*", which in effect is the Act as in force from time to time. The Act establishes the Code: Schedule 1 to the Act. The Act defines the Code as meaning means *Schedule 1 to this Act, and includes: (a) regulations made under section 329 for the purposes of that Schedule; and (b) instruments made under that Schedule.*" The Code itself provides that a power to make an instrument[6] includes a power to amend or repeal the instrument[7] and authorizes a wide variety of statutory instruments to be made with respect to the Code[8].
18. Further, the scheme and operation of the Act are very dependent upon the Code[9]. This is clear from the very definition of "referred credit matter" in the Victorian Act. Section. 5 of the Act defines a "credit provider" as having the "*the same meaning as in section 204 of the National Credit Code and incudes a person who is a credit provider*" because of section 10 of the Act [which is basically concerned with

[6] Defined in s.204 of the Code to include a statutory instrument.
[7] Section 214 of the Code.
[8] Section 215 of the Code.
[9] In this regard it is of interest that many of the proposed amendments in the Bill are to the Code.

assignments from an original credit provider]. It is the Code which effectively identifies a transaction as one which does or does not fall within the legislation. For example, sections 3 and 4 of the National Credit Code define the meaning of "credit" and the "amount of credit", the meaning of "credit contract" respectively for the purposes of the National Credit Code. Section 5 and section 6 of the National Credit Code set out the "provision of credit" to which the National Credit Code does or does not apply respectively.

19. Thus it can be seen the Victorian parliament in passing the Victorian Act clearly contemplated and provided for the Commonwealth to bring about amendments to the Commonwealth legislation it was, in effect, approving when it referred it to the Commonwealth under section 51(xxxvii) of the Constitution. Further, the Victorian parliament contemplated and referred power to amend to the Commonwealth, and not only by statutes but also by instruments.

The terrorism legislation precedent

20. In form this referral of power is similar to that adopted by the States and Commonwealth when the Commonwealth repealed and enacted a revised Part 5.3 of the *Criminal Code* (Cth) ("the Criminal Code"), which is concerned with terrorism. The revised legislation was supported by legislation passed by each of the States referring certain powers relating to terrorist acts to the Commonwealth. The relevant referring legislation there, similarly, provided for the referral of the matter by reference to the text of legislation (which the Commonwealth was "empowered" to enact by the reference) which was a schedule to the Act. The referring legislation also empowered the Commonwealth to make "express amendments" to that legislation.
21. Subsequently, in 2005 the Commonwealth enacted further legislation dealing with the subject of terrorism. This legislation introduced Division 104, which provides for control orders for "suspected" or "potential" terrorists, into the Criminal Code,. The constitutional validity of Division 104 of the Criminal Code was the subject of the challenge in *Thomas v Mowbray.*[10] Unfortunately, in that case only two of the seven Justices saw it necessary to consider whether Division 104 of the Code was a valid

[10] (2007) 233 CLR 307; [2007] HCA 33.

enactment of the Commonwealth pursuant to section 51(xxxvii) of the Constitution[11]. Both Kirby J and Hayne J considered this issue and came to contrary conclusions.

22. It should be noted that neither justice expressed any view suggesting that the referral of power under section 51(xxxvii) of the Constitution by this method did not achieve its purpose. The issue on which they disagreed was simply whether the referral made by Victoria (the Terrorism (Commonwealth Powers) Act 2003 (Vic)) empowered the Commonwealth to pass the amendments made in 2005.

23. Kirby J concluded that Division 104 was not supported by section 51(xxxvii) of the Constitution.[12] Hayne J concluded that the provisions met the description of laws with respect (inter alia) to the head of a referred legislative power pursuant to section 51(xxxvii) of the Constitution.[13] In part the nub of the disagreement was the reasoning of each Justice with respect to the term "express amendment" as used in the legislation relied upon to support Division 104. It is necessary therefore to consider the differences in their reasoning.

24. In *Thomas v Mowbray* the referring Act defined "terrorism legislation" as "*the provisions of Part 5.3 of the Commonwealth Criminal Code enacted in the terms, or substantially in the terms, of the text set out in Schedule 1 and as in force from time to time.*"[14] The definition of "express amendment" contained in the relevant legislation in *Thomas v Mowbray* is, (subject, naturally, to the words describing the subject matter of the referral legislation) although not absolutely identical, in effect the same as the definition contained in the Victorian Act. It is in the following terms:

> *"**express amendment**" of the terrorism legislation or the criminal responsibility legislation means the direct amendment of the text of the legislation (whether by the insertion, omission, repeal, substitution or relocation of words or matter) by Commonwealth Acts, but does not include the enactment by a Commonwealth Act of a provision that has or will have substantive effect otherwise than as part of the text of the legislation."*[15]

25. It needs also to be noted that in *Thomas v Mowbray* the relevant State legislation referring the power to the Commonwealth defined "terrorism legislation" to mean *"(a) the matters to which the referred provisions relate, but only to the extent of the*

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[11] Ibid, per Gleeson CJ at [6]; per Gummow and Crennan JJ at [154]; per Callinan J at [582] and [601], (although His Honour did doubt the validity of section 100.8 of the Code, but which has no relevance for my current purposes – see at [602] to [607]; per Heydon J at 650].
[12] Ibid at [203]: see generally [184] to [207].
[13] Ibid at [457]: see generally [446] to [457].
[14] *Terrorism (Commonwealth Powers) Act 2003* (Vic), section 3.
[15] Ibid.

making of laws with respect to those matters by including the referred provisions of Part 5.3 of [the Code] enacted in the terms, ***or substantially in the terms****, of the text set out in Schedule paragraph 1 and as enforced from time to time; and (b) the matter of terrorist acts, and actions relating to terrorist acts, but only to the extent of the making of laws with respect to that matter by making express amendments of the terrorism legislation or the criminal responsibility legislation..*"[16] (My emphasis.) I note, at this point, that the definition of National Credit legislation does not contain any words or form of words to the effect of "*substantially in the terms*". Although, that appears to have played some part in the reasoning of Kirby J, that issue does not presently arise.

26. It is also necessary to recognize that in *Thomas v Mowbray*, Kirby J opined that the Commonwealth "*relied heavily on one precedent said to be analogous, namely the reference of power from the State Parliaments*" to support the enactment by the Commonwealth of the *Corporations Act 2001* (Cth).[17]
27. Given the definitions in the referring Victorian Act of "terrorism legislation" and "express amendment", Kirby J saw the issue as whether "*the meaning of express amendment extends to the insertion of an entire new Division, in this case Div 104*".[18] Kirby J did not accept the Commonwealth's argument that it clearly did.[19]

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[16] Ibid.

[17] Ibid, per Kirby J at [190] ff. Despite Kirby J's assertion to this effect the summary of argument in the CLR does not appear to support it: see Ibid at p.318 in particular. I have reviewed the relevant part of the transcript of argument in the High Court hearing and whilst the Commonwealth did refer to the precedent of the *Corporations Act 2001*, it was in the context of explaining how the like terms of the referral contained a like power to make an"express amendment" (in the corporations matter) had permitted the introduction of significant new divisions in the *Corporations Act 2001*. But, so the argument went, it would not permit a like provision being enacted in a different new piece of stand-alone Commonwealth legislation. The transcript of argument (on 10 February 2006) reveals the following submission on behalf of the Commonwealth:

The purpose of those words, your Honour, is clear if you go to tab H in the volume and across to page 5 - this is the explanatory memorandum accompanying the corporations reference. At the top of page 5, the last sentence of the indented words: "This ensures that the matters covered by the second reference cannot be the source of power for other Commonwealth legislation." We say that is the sole purpose of the qualification on the express amendment power, but it is not designed to prevent amendment of the referred text whether that amendment take the form of simply repeal of the subsection and substitution of the new subsection, the insertion of the new sections or the insertion of new divisions, such as occurred here, provided the law can still be characterised as coming within the subject matter referred."

I take the view Kirby J has overstated the Commonwealth's reliance on the analogy.

[18] 233 CLR 307 at [189].

[19] Ibid at [189].

28. Firstly, Kirby J compared the terrorism referring legislation with that used by the Victorian Parliament in the corporations power referral to the Commonwealth and noted that terrorism referring legislation was far more specific (by reference to the specific text of the Commonwealth legislation) than in the corporations referral (by reference to the texts of proposed Bills for Commonwealth Acts tabled in the New South Wales Parliament.[20] This was an important distinction to Kirby J in that it affected "*the definition and specification of the State legislative power that was surrendered by the referral to the Federal Parliament*".[21] And although the Corporations referral permitted "express amendments" by the Commonwealth, that was very different to the terrorism referral since the term "express amendment" in the terrorism legislation "*was qualified not only by the matters referred but also by the specified form of the legislation to which only express amendments could be made*".[22]
29. Kirby J then turned to the specific terms and context of the referring Victorian Act. Again, Kirby J contrasted the difference between the specific text of the legislation being a Schedule to the referring Victorian Act whereas in the corporations' referral the Victorian legislature had defined the "Corporations Legislation" by reference to provisions tabled in the Parliament of another State[23]. It was this specificity of referral[24] that was of importance in assessing whether the legislation enacting Div 104 was an "express amendment" for the purposes of the Criminal Code provisions pursuant to the referral of terrorism to the Commonwealth and the referring Victorian Act.
30. Accordingly, Kirby J conclude Div 104 was not supported by section 51(xxxvii) of the Constitution because of two limitations inherent in the definition of "express amendment". Firstly, Div 104 "*must constitute an express amendment of*" the text of the Commonwealth Act in Schedule 1 of the Victorian Act. Secondly, the express amendment "*must be a direct amendment*" of that same text. Although an express amendment included the "*insertion of text*", that term needed to be read restrictively because it must be read ejusdem generis with the preceding words "direct amendment"[25]

[20] Ibid at [190] to [194].
[21] Ibid at [194].
[22] Ibid [197].
[23] Ibid at [195].
[24] Ibid at [199].
[25] Ibid at [204].

31. Ultimately, Kirby J concluded that Division 104 "*did not amount to a direct amendment of the terrorist legislation [but] rather it was an addition to the scope of...the Code by federal law alone.*" Kirby J saw an important distinction between the power referred by reference to the specific text of the Commonwealth legislation and which related to "*the regulation, definition and punishment of terrorist acts*" and Division 4 of the Code which related "*the prevention of terrorist acts and the control and detention of particular persons in order to protect the public from potential terrorist acts.*"[26]
32. Hayne J rejected the contention that Division 4 of the Code introduced into the Code an entirely new regime that would have effect otherwise than as part of the text referred.[27]
33. Firstly, Hayne J noted that what was referred to the Commonwealth was both the text of the legislation (section 4(1)(a) of the referring Act) and the matter of terrorist acts, and actions relating to terrorist acts by making express amendments to the specified text (subsection 4(1)(b) of the referring Act). Further His Honour identified that subsection 4(3) of the referring Act specifically "*provided that the operation of each of paras (a) and (b)... is not affected by the other paragraph.*" Accordingly, His Honour concluded that the matter of terrorist acts, and actions relating to terrorist acts (subsection 4(1)(b) of the referring Act) was not to be confined by reference to the specified text.[28]
34. Hayne J then turned to the meaning of the definition of "express amendment". His Honour accepted the Commonwealth's argument[29] that the term permitted "*amendment by the insertion of new matter so long as that new matter falls within the description of a law with respect to the matter referred (terrorist acts, and actions relating to terrorist acts)...*"[30]
35. In my opinion the reasoning of Hayne J is to be preferred. The reasoning of Kirby J, in my opinion, ignores the natural and ordinary meaning of the words used by Parliament.

[26] Ibid at [205].
[27] Ibid at [449] - [450].
[28] Ibid at [451].
[29] See the argument set out at footnote 11 above.
[30] 233 CLR 307 at [454].

36. It is to be remembered that the starting point for discerning the meaning of a statute is its words and context. As was said in *Project Blue Sky Inc v Australian Broadcasting Authority*[31]:

> "*The primary object of statutory construction is to construe the relevant provision so that it is* ***consistent with the language and purpose of all the provisions of the statute****. The meaning of the provision must be determined 'by reference to the language of the instrument viewed as a whole'. ...*
>
> *A legislative instrument must be construed on the prima facie basis that its provisions are intended to give effect to harmonious goals. Where conflict appears to arise from the language of particular provisions, the conflict must be alleviated, so far as possible, by adjusting the meaning of the competing provisions to achieve that result which will best give effect to the purpose and language of those provisions while maintaining the unity of all the statutory provisions.*" [my emphasis]

The High Court recently referred to, and relied on, this very passage in *Independent Commission Against Corruption (NSW) v Cunneen*[32].

37. I do not accept the "text specificity" distinction Kirby J relies upon in his comparison between the Corporations referral and the terrorism referral, and which is an essential part of his reasoning. In my opinion it is an illusory distinction. Whilst the documents containing the text being referred are clearly different, it is not the descriptor of the document or documents (be it a Bill or an Act) but the text contained in that document or documents that is the important thing: it being the specified text identified as being referred. Similarly, the difference between a Schedule to the State Act and an identified documents in the Parliament of another State: again it is the specified text identified that is being referred. If I am correct in that, then his basis for concluding the term "express amendment" did not permit the enactment of Div 104 does not exists.

38. I have already opined that the Victorian parliament clearly contemplated the Act would need amending and referred the power to that.[33] The term "express

[31] (1998) 194 CLR 355 at 381-382 [69]-[70] per McHugh, Gummow, Kirby and Hayne JJ; [1998] HCA 28, recently applied in *Certain Lloyd's Underwriters v Cross* (2012) 248 CLR 378 at 389 [24] per French CJ and Hayne J; [2012] HCA 56 and in *Plaintiff S4/2014 v Minister for Immigration and Border Protection* (2014) 88 ALJR 847 at 855 [42] per French CJ, Hayne, Crennan, Kiefel and Keane JJ; 312 ALR 537 at 546; [2014] HCA 34.

[32] (2015) 89 ALJR 475; [2015] HCA 14.

[33] See paragraph 19 above.

amendment" clearly contemplates that the Commonwealth may amend the terrorism referred legislation by the insertion (or by omission, repeal, substitution or relocation) of words or **matter**. The reasoning of Kirby J gives no consideration to the word "matter", which is clearly to be contrasted with the word "words". Clearly, as is identified by Hayne J, the Victorian Parliament in referring the terrorism power to the Commonwealth was including the power to amend the legislation by including an additional matter or matters providing such are within the definition of "terrorism legislation".

39. Further, Kirby J does not appear to have considered, let alone dealt with, the effect of section 4(3) of the referring Victorian Act that *"[t]he operation of each paragraph of subsection (1) is not affected by the other paragraph."* As I have noted in paragraph 33, this was a matter that Hayne J considered, and considered relevant in determining what had been referred. In my opinion, it cannot be said that the matters covered by Division 4 of the Code were not matters that fell within the description of the matters referred by subsection 4(1)(b) of the referring Victorian Act: namely, terrorist acts, and actions relating to terrorist acts.

Proposed amendment to the Act

40. I turn then to consider the matter upon which I am asked to opine having regard to the decision of Hayne J in *Thomas v Mowbray*.
41. Immediately it should be noted that the Victorian Act contains section 9, of which there was no equivalent in the referring Act on *Thomas v Mowbray*. That section must be read as part of the context of the Victorian Act and, importantly, as giving context to the definition of "express amendment".
42. The Exposure Draft of the Bill with Commentary contains the following with respect to the proposal about which I am asked:

> *"This Schedule introduces amendments intended to provide a systematic response to avoidance practices, rather than individual responses being developed that address a specific practice after it has come into use in the credit market.,*
>
> *In summary, the amendments operate as follow:*
>
> - *a person is prohibited from beginning or carrying out a scheme for the*
> *purpose of avoiding the application of a provision of the Credit Act;*

- *purpose is to be determined on the basis of objective factors, rather*
  than the subjective intentions of the person engaged in the scheme;
- *a number of factors are listed as being relevant to the assessment of purpose, including:*
  - *any representations made to consumers (paragraph (i)), which would include whether products are advertised as credit or loans; and*
  - *any change in the conduct of a person following amendments to this Act (paragraph (l)), which would include changes in practices or structures to mitigate or avoid the effect of amendments;*
- *a scheme is presumed, other than for criminal proceedings, to be for*
  the purposes of avoidance where it is a scheme of a type prescribed by
  regulations or ASIC by a legislative instrument (with this approach taken to provide greater regulatory consistency in respect of particular
  avoidance techniques, by allowing for the onus to be placed on the providers of the scheme, rather than ASIC positively having to establish
  the purpose in respect of each provider for similarly structured schemes)."

43. Thus it is fair to say that the proposal is not intended to create new or harsher restrictions on the provision of credit or the manner in which it was provided or who could provide it. Rather, it is a commonsense approach to attempt to prevent practices that are aimed at circumventing the operation of the Act. In other words, to make the current restrictions in the Act in its current form more effectual. That, in my opinion, falls squarely within the meaning of "express amendment" and clearly accords with the reasoning of Hayne J. in *Thomas v Mowbray*.

44. Once this is recognized, it follows in my opinion, not only from the reasoning of Hayne J in *Thomas v Mowbray* but also from accepted principles of statutory interpretation, that the proposal is within the scope of the powers referred to the Commonwealth by the Act.

45. Further, even if one were to consider the proposed legislation in accordance with the reasoning of Kirby J, my conclusion is not altered. Such a proposal can hardly be said, to adopt the language of Kirby J, to be the introduction of an addition to the scope of the Act by federal law alone. Rather, it is simply endeavouring to achieve the original purpose and intent.

46. Accordingly, in my opinion the proposed amendment contained in Schedule 6 to the Bill is within the power of the Commonwealth parliament.

47. I am also asked to consider a number of other matters:

> "2. Whether an anti-avoidance provision could otherwise be introduced in the Act, for example based on the Commonwealth's heads of power under the Constitution (such as the Corporations and interstate trade and commerce powers);
>
> 3. Whether the States could introduce an anti-avoidance provision;
>
> 4. If the second or third approaches were taken, whether this is likely to create loopholes and reduce the effectiveness of the provision (i.e. lead to avoiding the anti-avoidance provision); and
>
> 5. Whether a distinction may be drawn between the Commonwealth's power to enact an anti-avoidance provision directed at:
>
> a. general avoidance measures that seek to avoid the application of the Act altogether, and
>
> b. internal avoidance measures where the contract is covered by the Act, but a scheme is implemented to avoid the application of one or more of the provisions of the Act (e.g. masking a credit contract as a lease to avoid interest rate caps)."

48. As to the second question asked of me: I am of the opinion it is highly unlikely to withstand constitutional challenge or that it would deal with the problem successfully. It must be remembered that to enact the Act, the Council of Australian Governments considered it necessary to refer the matter in the way in which it occurred. That not only demonstrated a desire for the issue to be dealt with on a national basis but that to achieve that constitutionally (at least in the way most likely to be constitutionally valid) there was a need to do it in the way it was done. It must also be remembered that a "credit provider" need not be a corporation or a real person who engages in interstate trade. That being so it is difficult to see how the use of the Corporations or interstate trade and commerce powers could cover the field. Accordingly, in my opinion the use of such powers is unlikely to be constitutionally valid or effective.

49. As to the third question: Undoubtedly, each State and Territory could pass such legislation but again I am of the opinion it is unlikely to withstand constitutional challenge. Firstly, I would suspect a challenge to any such legislation under sections 92 (free trade and commerce) and 109 of the Constitution (inconsistencies between a

Commonwealth law and a State law). Additionally, it may be difficult to achieve agreement between the States and Territories.

50. As to the fourth question: In my opinion such an approach would, even if it were to be found to be constitutionally valid, almost certainly fail to cover the field. Accordingly, it would reduce the effectiveness of the provision.

51. As to the fifth question: Given my answer to the primary question this question does not require an answer. However, for the reasons I have already expressed, in my opinion the Commonwealth has the power to enact an anti-avoidance provision. Whether it is done in either of the two ways proposed in the question is not to point.

52. I would be happy to discuss this matter further with those instructing me.

W. Brind Zichy-Woinarski

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Aickin Chambers
15th July 2015

Re: The Enactment of an Anti-avoidance Provision in the Australian Consumer Credit Regime

Memorandum of Advice