



Investment & Financial Services Association Ltd

## **Response to ASIC Consultation Paper 102 Dispute Resolution – Review of RG 139 and RG 165**

Dated: 14 November 2008

## **PART I - INTRODUCTION**

IFSA members have in the past strongly supported the operations of FICS and, the merger of the Financial Industry Complaints Service (**FICS**), the Banking and Financial Ombudsman Service, and the Insurance Ombudsman Service to establish the Financial Ombudsman Service (**FOS**). FOS provides a venue for the settlement of disputes with retail clients where a matter cannot be determined through internal dispute resolution processes.

FOS, and its predecessor FICS, are each the product of earlier industry initiatives to merge external dispute resolution (**EDR**) bodies in the interests of efficiency. The development and evolution of financial services industry EDR bodies predates and has been broadly consistent with the findings and recommendations of the Productivity Commission's report into *Australia's Consumer Policy Framework* (No.45, 30 April 2008).

FOS is an industry scheme funded by its members, not a statutory scheme. It offers an alternative to the courts and provides resolution of complaints against the criteria of the relevant law, good industry practice, relevant industry codes and what is fair in all the circumstances. Clients of FOS members do not pay a fee to lodge a complaint with FOS and, if a decision is made by FOS, it is binding upon the member but not the client.

IFSA members deal primarily with the Life Insurance and Superannuation section (**ILIS**) of FOS. The rules applying to ILIS are those that have previously been developed by and in consultation with members of FICS. Those rules have set the parameters within which members have been prepared to support a free EDR as an alternative to the courts. Jurisdictional and monetary thresholds for access to FOS have been established having regard to the relative risk of client detriment for the relevant classes of financial product and the aim that the limits cover the majority of retail clients. Any proposal to change those parameters should only be following a thorough factual cost benefit analysis.

## **PART II - RESPONSE TO SPECIFIC QUESTIONS**

### **NEW AUSTRALIAN STANDARD ON COMPLAINTS HANDLING (AS ISO 10002)**

#### **Proposal C1**

ASIC propose to update RG 165 to adopt the definition of 'complaint' in AS ISO 10002.

Question C1Q1: Do you agree with this proposal? Please give reasons

While IFSA members do not disagree with the definition of complaint in AS ISO 10002 and that having a single definition of complaint promotes consistency and certainty, the adoption of the AS ISO 10002 definition in RG 165 could have a significant impact on costs and the systems and processes members currently use for capturing and resolving complaints. Currently, while the processes put in place by IFSA members may differ, many enquiries and potential complaints are resolved at the initial point of contact and, if not resolved, they are escalated and tracked until resolution.

If the AS ISO 10002 definition of complaint is adopted in RG 165, this could mean that even minor expressions of dissatisfaction that turn out to be queries regarding processes need to be

captured and records maintained. This would impose a significant administrative burden while the amount of consumer benefit would be negligible at best. Instead, it may actually reduce levels of customer service and increase costs.

In addition, the definition of complaint does not exclude template complaints made by large numbers of individuals under campaigns orchestrated by some law firms and consumer advocates. IFSA recommends that complaints made in the same or substantially similar form recommended for use by an organisation which is not itself an affected consumer, for example Choice, be excluded from the definition.

### Proposal C2

ASIC propose to update RG 165 to require IDR procedures to satisfy the following aspects of AS ISO 10002:

- (a) the Guiding Principles in Section 4;
- (b) the following sections in the main body of AS ISO 10002:
  - (i) Section 5.1 – Commitment;
  - (ii) Section 6.4 – Resources;
  - (iii) Section 8.1 – Collection of information;
  - (iv) Section 8.2 – Analysis and evaluation of complaints.

Question C2Q1: Should RG 165 require IDR procedures to satisfy the Guiding Principles in Section 4 and the sections of AS ISO 10002 in proposal C2(b)? Please give reasons.

Subject to the following comments, the proposal seems reasonable, noting that none of the requirements in C2(b) impose any extra burden than the equivalent elements in AS4269:

1. 8.1(e) (Collection of Information) of AS ISO 10002 requires an organisation to specify how and when statistical non-personally identifiable complaints data is disclosed to the public. We DO NOT AGREE with this requirement. Statistics, in respect of those 'complaints' which are unresolved by IDR are appropriately maintained by FOS and made publicly available. Requiring organisations to perform this task would also add to compliance costs.
2. Organisations may take a 'subjective' view of what may constitute a 'complaint' for public reporting purposes. We believe that an obligation to report publicly all 'complaints' is unlikely to add value to the complaint handling system.

### Proposal C3

ASIC propose to update the Schedule to RG 165 to reflect the Guiding Principles and other specific aspects of AS ISO 10002 that IDR procedures will need to comply with.

Question C3Q1: Is the Schedule to RG 165 useful? Should ASIC update it?

Yes, the schedule to RG 165 is useful and should be updated to reflect AS ISO 10002.

It is noted that ASIC refers to the Guiding Principles as something that IDR procedures will need to **comply** with. IFSA notes that Guiding Principles provide **guidance** to industry and that members should take into account the Guiding Principles when developing complaint handling procedures consistent with the size, nature and complexity of their business. ASIC's use of compliance oriented language when discussing issues of guidance is, in IFSA's view, inappropriate.

## **OTHER IDR REQUIREMENTS**

### **Proposal D1**

ASIC propose to:

- require financial services providers to provide a final response to complaints within a maximum of 45 days, but within 30 days if possible;
- clarify how the right to access EDR applies to complainants with a complaint in a multi-tiered IDR procedure;
- clarify how the requirements for IDR procedures apply to financial services providers that outsource the delivery of the IDR process.

Question D1Q1: Do you agree with this proposal? Please give reasons.

IFSA members note that ASIC recognises that it will not be possible to respond to all complaints within 45 days (paragraph 80 of CP 102). However, the wording 'final response' is somewhat of a concern in that it will not always be possible to provide a final response within this time period despite the best efforts of the member.

As noted in IFSA's submission to FOS on the development of its Terms of Reference (**Attachment A**), given the complexity of some products and services and the complaints associated with them, as well as the need for third party assessment in some cases, the proposed time limit may be insufficient in some instances. The financial services provider should notify the complainant if the IDR process will take longer than the prescribed time limit, provide them with an anticipated timeframe for resolution and the opportunity to escalate the matter to FOS if they are unhappy with this.

If the consumer takes the opportunity to escalate the matter to the EDR scheme at that time, we believe FOS should liaise with the member to determine whether the particular complaint requires a longer period for resolution through the IDR process and whether the member is genuinely actioning the complaint. We have proposed that FOS give the member 14 days to provide the reasons for the delay and an indicative time-frame for resolving the complaint. If the reasons support a longer period for investigation and consideration and the member is genuinely attending to the complaint, FOS should support the member in their efforts to resolve the complaint through the IDR process.

In some complex insurance claims/matters where fraud has been identified or claimed (by the consumer, in relation to advice or actions of financial planners), 45 days is insufficient to allow members to fully investigate issues and determine an appropriate outcome. A timeframe of 90 days would be more reasonable in these situations.

We also note that paragraph 78 of the Consultation Paper refers to requiring financial services providers to *write* to complainants. We believe that the words *contact* the complainant should be used to enable other forms of communication to be used if agreed by both parties.

We also believe that this time limit should restart where there has been a substantial change to the nature of the person's complaint. For example, where they bring new information to the member towards the end of the 30 day period.

### **Proposal D2**

ASIC propose to clarify that the timeframes for providing a final response to complaints apply to financial services providers that operate multi-tiered IDR procedures.

Question D2Q1: Do you agree with this proposal? Please give reasons.

IFSA is of the view that a uniform timeframe for all AFSL holders should be put in place.

### **Proposal D3**

ASIC propose to clarify that a financial services provider that outsources its IDR procedures to a third party service provider remains responsible for ensuring that the IDR procedure complies with RG 165.

Question D3Q1: Do you agree with this proposal? Please give reasons.

As for D2, all AFSL holders should meet the same timeframe no matter what their own procedures are.

## **COVERAGE OF EDR SCHEMES**

### **Proposal E1**

ASIC propose to clarify RG139.34(a) to make it clear that it refers to types of complaints.

Question E1Q1: Do you agree with this proposal? Please give reasons.

This may be a significant issue of redrafting from the industry's perspective. As things currently stand, the wording of RG 139.34(a) is an accurate reflection of the fact that the monetary limits applied under the EDR scheme, which currently define the jurisdiction of the scheme, results in the "coverage being sufficient to deal with the majority of consumer complaints in the relevant industry".

If these words are to be replaced to state that EDR schemes must be sufficient to cover the majority of types of complaints consumers have, then the jurisdiction of the scheme will be much broader and possibly exceed the the scope of the legislative requirements.

IFSA members continue to support the current monetary thresholds under FOS. FOS members in the Life Insurance and Superannuation section (**ILIS**) continue to support the periodic review of the monetary thresholds for disputes involving financial planning, managed investments and stockbroking claims relative to movements in the Consumer Price Index<sup>1</sup>.

As stated in that submission, indexation of monetary thresholds is not appropriate for and should not be applied to life insurance risk products. The thresholds should nevertheless be reviewed periodically (2, 3, or 5 years). Increases in the proposed monetary thresholds should be determined having regard to the level of coverage of retail clients.

IFSA members have strongly supported the operations of FOS's predecessor FICS as a venue for the settlement of disputes with retail clients where the matter cannot be determined through their internal dispute resolution processes. The continued success of the EDR scheme is underpinned by industry support for the scheme requirements. We believe that Australia has a world class EDR scheme that deals with a majority of disputes involving financial services transactions of clients. Any fundamental change to the rights and obligations of FOS members may undermine the integrity and support for FOS.

In so far as the current Rules define what FOS can and cannot hear, together with the monetary limits, forms the best basis for a simple and clear definition of the types of disputes an EDR scheme should cover.

### **Proposal E2**

ASIC propose that monetary limits should be replaced with caps on the amount of compensation each EDR scheme can award. A consumer or investor with a complaint involving an amount that is higher than an EDR scheme's compensation cap should be permitted to waive the excess to access the scheme.

Question E2Q1: Should EDR schemes and members allow complainants with a claim that exceeds an EDR scheme's compensation cap to waive their right to pursue the balance of their claim elsewhere?

Please see IFSA's submission to FOS and responses to questions 1, 20 and 21 in particular. IFSA also made submissions to FICS in response to FICS Discussion Paper on the review of monetary limits in 2007 (**Attachments B & C**). Each of IFSA's submissions argued against the introduction of an 'opt-in' or compensation cap system. The position stated in those three submissions on the issue remains IFSA's position, in short:

- We believe that the EDR process is intended to provide consumers without ready access to legal means of resolution, and at no cost, an opportunity to have their complaints addressed by an independent third party and broadening access to the EDR process to consumers with means to raise complaints through the legal system may increase the number of cases lodged with FOS and impede the quick resolution of complaints by those without other methods of recourse;

<sup>1</sup> IFSA Submission to FICS dated 18 September 2007.

- The 'opt-in' model is problematic due to its potential for abuse by consumers as a 'dry-run'. Consumers may use the scheme to assess whether a legal action would be successful and 'opt-out' of the complaint once they have used the forum to test the strength of the case, in favour of pursuing the full amount through judicial proceedings.

### Proposal E3

ASIC propose to reformulate their guidance in RG139.34(b) on setting the amount for compensation caps to ensure they are adequate. ASIC propose to require EDR schemes to operate compensation caps that reflect the value of the vast majority of consumer transactions in the relevant industry or industries. At this time, with some limited exceptions, (see paragraphs 138 and 139 of ASIC CP102) this should be a minimum of \$280,000.

Question E4Q1: ASIC are seeking views on their proposed reformulation of RG 139.34(b).

FOS is an industry funded scheme that is free to consumers. The FOS Constitution and Terms of Reference (**Rules**) bind FOS members contractually but are not binding on consumers who seek to have disputes resolved by FOS.

Current monetary thresholds have been imposed on the basis that they will cover the majority of retail consumer complaints. In relation to non-life insurance complaints, the current monetary threshold far exceeds the average consumer claim.

An arbitrary uniform limit of \$280,000 does not "reflect the value of the vast majority of consumer transactions" dealt with by the Investments, Life Insurance and Superannuation section (**ILIS**) of FOS. In fact the average non-life insurance claim dealt with by ILIS (and its predecessor FICS) is less than a third of the current threshold limit amount.

FOS, as an amalgamation of the Banking and Financial Services Ombudsman (**BFSO**), the Financial Industry Complaints Service (**FICS**), and the Insurance Ombudsman Service (**IOS**), deals with complaints ranging from basic deposit products, personal lines of general insurance, life insurance, superannuation, managed investments etc. and there is no logical reason to have a single limit given the diversity in the nature, scale and complexity of the products and of the customer's potential claim associated with each.

As noted in our submission to FOS and our submissions to FICS in 2007, we strongly believe that the technical differences and values involved with different products and services across the industry warrant specific approaches in relation to monetary limits. We note that the limits for matters dealt with by the ILIS section of FOS have been thoroughly reviewed recently by stakeholders and increases, where justified, have been implemented. Where a person has made an enquiry to FOS, information on monetary thresholds applying to different types of products is freely available. Additionally, there are licence conditions requiring members to disclose the existence of the EDR schemes and provide contact details to all retail clients in regulated documents as well as advising those details to complainants as part of the IDR process.

Question E4Q2: ASIC are also seeking views on the adequacy of \$280,000 as the minimum compensation cap.

IFSA is of the view that EDR schemes have worked well in practice with the monetary limits which have been in place in the past and the updated monetary limits from 1 July 2008 and would seek from ASIC any evidence to suggest that a majority consumers, without financial resources to have matters determined by the Courts, are disadvantaged by the current approach of different compensation limits for different products and services.

Seeking to effectively impose a \$280,000 threshold cap is arbitrary and is not supported by experience. Any such requirement would be a defacto legislative in nature and should be expressly provided for in the Corporations Regulations and subject to the same the same cost benefit analysis as any other legislative proposal. Until such a review based on objective data is undertaken, IFSA members will not support the proposal.

Question E4Q3: ASIC are also interested in feedback on other options identified in their paper, and other suggestions.

As an industry funded EDR scheme, IFSA members support the continuation of the current arrangement with monetary thresholds being reviewed periodically.

#### **Proposal E4**

ASIC propose to clarify that consumers and investors should be entitled to claim interest in addition to compensation up to an EDR scheme's compensation cap. In other words, an award of interest by a scheme can lead to the amount of compensation being over the cap.

Question E4Q4: Do you agree with ASIC's proposal on interest? Please give reasons.

IFSA members have reviewed their response to the IFSA submission to FOS monetary limits and consider that current FICS Rules 34 should continue to apply in relation to an award of interest and the total amount that may be awarded. To date we are not aware of any case or circumstance where the operation of FICS Rule 34 has led to any inequitable outcome..

#### **Proposal E5**

ASIC propose that compensation caps should be adjusted every three years using the higher of the increase in the CPI or MTAW (male total average weekly earnings) (this is the formula used for quarterly indexation of Commonwealth pensions).

Question E5Q1: Do you agree with our proposal for indexing compensation caps? Please give reasons.

FICS (and, therefore, the ILIS Division of FOS) already has indexation of limits. This was agreed by all stakeholders in 2007 to ensure retention of relevant jurisdictional monetary limits thus

reducing the need for time consuming and expensive reviews. IFSA supports the continuation of indexation and expansion to all divisions of FOS and all other EDR schemes.

For the sake of clarity, IFSA's position on the review of monetary limits is that the monetary limits should be automatically indexed by CPI every 3 years. Indexation of monetary thresholds is not appropriate for, and should not be applied to, life insurance risk products.

We do not agree with the use of the MTAW formula for adjustment of the monetary limits.

### **Proposal E6**

ASIC recognise the need for adequate transitional arrangements when they reformulate their guidance on EDR scheme coverage. *NB this question is asked after a discussion in relation to the relationship between compensation and insurance arrangements.*

Question E6Q1: What transition period would be appropriate

Two years from the later of the release of the final ASIC policy or the implementation of the single Terms of Reference for FOS.

### **Proposal E7**

ASIC are interested in feedback about whether dual access to EDR would be beneficial.

Question E7Q1: Should we require EDR schemes to accept complaints referred by financial services providers, provided the relevant time limits have expired?

Our interpretation of this question is whether third party financial service providers should be able to lodge complaints against other (member) financial service providers on behalf of clients. EDR is a mechanism which is in place for consumers who have a complaint about a financial services provider. If the consumer needs assistance, the EDR scheme is bound to assist. Furthermore the consumer should first bring the complaint to the original financial service providers IDR before referring it to EDR.

Third party financial services providers that bring complaints on behalf of an aggrieved customer of another financial services provider will, more often than not, have a conflict of interest and should not be allowed to refer the complaint but rather should have the consumer refer the complaint to the original financial services provider's IDR facility.

For these reasons IFSA members do not believe there is any benefit in this proposal.

## **HARMONISING EDR SCHEMES**

### **Proposal F1**

ASIC propose requiring all EDR schemes to have jurisdiction to deal with complaints about a financial services provider that was a scheme member when the complaint was made, but that subsequently ceases to carry on business.

Question F1Q1: Do you agree with this proposal? Please give reasons.

The proposal reflects the current provisions of FICS and the ILIS Division of FOS and is supported. However, if the member ceases to be a member prior to the complaint being lodged with the EDR scheme the scheme must not be allowed to deal with it.

While the current situation is an impost on members (i.e. current members paying for complaint handling of a previous member that was financial at the time the complaint was lodged) members should not bear the additional cost of a complaint lodged against an ex-member. Generally, if a complaint is lodged against an existing member who subsequently ceases to be a member there is some residual of fees paid by that member that can be applied to the processing of the complaint. This is likely not to be the case where the member had ceased prior to the complaint being lodged. Issues, of course, may arise in the enforcement of a determination where a member has ceased to be a FOS member.

### **Proposal F2**

ASIC propose requiring all EDR schemes to prohibit scheme members from commencing legal proceedings that are related to a complaint that has been lodged with the EDR scheme, except:

- (a) where the limitations period for legal proceedings will shortly expire; and
- (b) in test case situations.

Question F2Q1: Do you agree with this proposal? Please give reasons.

Members should be free to protect their proprietary rights by injunctions and other orders against disputants and their property where delay would jeopardise those rights or where it can be established that there is a reasonable basis to believe serious misconduct by the complainant such as fraud. Also, members should be entitled to recover loans and other assets used by the disputant.

ASIC propose that the member pay the legal costs of the complainant in the event that the member commences legal action. It needs to be made clear that this will only arise in the event of what ASIC calls “ test cases” and not all instances where a member commences legal action to preserve its rights (such as for recovery of an overpayment or where the statute of limitations may be exceeded while the case is dealt with by EDR).

A definition around what is considered a ‘test case’ would also be useful.

### **Proposal F3**

ASIC propose:

- (a) to require all EDR schemes to introduce a six year time limit for bringing complaints; and
- (b) that the time limit should run from the date that the consumer or investor first became aware, or should reasonably have become aware, that they suffered the loss the complaint is about.

Question F3Q1: Do you agree with this proposal? Please give reasons.

Given the introduction of FSR and annual reporting it would be more appropriate for (b) above to read as follows:

*“that the time limit should run from the date that the consumer suffered the loss the complaint is about”*

Given the regular and comprehensive disclosure requirements that apply to the financial services sector, there is no reason a consumer should not be aware of an event, or all the facts concerning an event, that gives rise to a complaint well before 6 years has elapsed. We strongly believe that a consumer should lodge complaints as soon as possible.

#### **Proposal F4**

RG 165.87 states that EDR schemes can exclude complaints that have already been, or should be dealt with in another forum. We propose to clarify that this applies to complaints that have been dealt with in a court or tribunal or another EDR scheme approved by ASIC.

Question F4Q1: Do you agree with this proposal? Please give reasons.

Where a complainant has initiated court proceedings, access to EDR should be conditional on the withdrawal/cessation of those proceedings. The term “dealt with” implies that the matter has been adjudicated and determined by the Court. It appears to contemplate parallel proceedings – the Court and the EDR.

The proposal does not exclude a subsequent complaint to the FOS which had already been dealt with by the Office of Fair Trading. This seems an unnecessary concession to disputants and encourages forum shopping. The proposal should also clarify that complaints that have been through an annexed or court directed ADR process should also be excluded.

In addition, a complainant should not be able to take a complaint through an ADR process and then withdraw the complaint just before the end of the process so that it can instead be taken through an EDR scheme.

#### **Proposal F5**

ASIC propose to prohibit EDR schemes from conferring a power on scheme members to veto proposed amendments to their Rules or Terms of Reference.

Question F5Q1: Do you agree with this proposal? Please give reasons.

On 21 April 2008 IFSA provided a submission to ASIC in relation to the proposed draft FOS Constitution. In that submission we expressed our concern that accountability to members in relation to the making of the FOS Terms of Reference had been significantly reduced. Under the draft Constitution, a Director could amend or revoke any Terms of Reference after consultation with ASIC and the relevant Advisory Committee and without consultation to FOS members.

As a result of negotiation between IFSA, ASIC and FOS, clauses 14.2(e) and (f) were inserted into the FOS Constitution in relation to the FOS Terms of Reference. This clause provides for an appropriately qualified independent person appointed by the Directors to consider submissions and make a recommendation to the Directors as to whether the proposed Terms of Reference should be amended.

It is IFSA's view that should scheme members be prohibited to vote on proposed amendments to their Rules or Terms of Reference, a similar provision for an independent arbitrator to that now contained in the FOS Constitution should be put in place. It should be noted that EDR schemes are industry funded and scheme members, therefore, have a fundamental interest in the Governance and Rules of any EDR scheme funded by them.

### **Proposal F6**

ASIC are interested in feedback about whether communication by EDR schemes should be addressed as part of ASIC's policy.

Question F6Q1: Should we require EDR schemes to communicate clearly with complainants and members about their role, process and decisions? If so, how should this be done?

IFSA members are of the view that there should be no need for this obvious requirement to be part of ASIC policy.

## **OUTCOMES, REVIEW & REPORTING**

### **Proposal G1**

ASIC propose to clarify that a decision by an EDR scheme must not bind the consumer or investor who made the complaint, except where the consumer waives the amount in excess of an EDR scheme's compensation cap in order to have their complaint heard by the EDR scheme and the consumer accepts the EDR scheme's decision.

Question G1Q1: Do you agree with this proposal? Please give reasons.

For the reasons expressed above, IFSA members do not support the cap option. IFSA members support a continuance of the policy underpinning FICS Rules 37 and 38..

FICS Rules 37 provides that there is an expectation that Complainant's will comply with decisions of the Panel and that a Complainant must elect whether or not to accept a Panel decision within one month of the date of the decision. Where the decision is accepted by a Complainant the decision is considered binding on the Complainant.

FICS Rule 38 provides that Members are bound by Panel decisions and that Members are entitled to ask a Complainant to execute a Deed of Release covering the issues the subject of the complaint before the Panel.

These Rules work well together and encourage finality of the complaint which is in the interests of all parties. The proposed amendment has the potential to interfere with these Rules which would not be in the interests of an efficient EDR Scheme.

### **Proposal G2**

ASIC propose to require an EDR scheme to commission an independent review of its operations and procedures:

- (a) three years after the scheme is initially approved by ASIC, and
- (b) thereafter, every five years from the date that the EDR scheme's last independent review comments, or sooner if required by ASIC.

Question G2Q1: Do you agree with this proposal? Please give reasons.

We agree that EDR schemes should be subject to regular independent review.

### **Proposal G3**

ASIC propose to update RG 139 to:

- (a) reflect the fact that EDR scheme reports to ASIC about systemic issues and serious misconduct generally do not identify the scheme member or members involved; and
- (b) state that, where necessary, ASIC can compel EDR schemes to provide information identifying the scheme member that is the subject of a systemic issue or serious misconduct report.

Question G3Q1: Do you agree with this proposal? Please give reasons.

FOS is currently required to report providers they consider have systemic issues. Given this proposal and the broad meaning of 'systemic issue', we believe the EDR should give the member notice and, an opportunity to discuss the issue with the EDR prior to their contact with ASIC. This will enable the member to clarify the situation and any measures they have taken to address the issue. We also support the development of example of the types of recurrent issues that would be considered as giving rise to a systemic issue.

### **Proposal G4**

ASIC propose to require EDR schemes to publish an annual report of statistical information about the number of complaints receive and upheld for each scheme members,

Question G4Q1: Do you agree with this proposal? Please give reasons.

ASIC proposes that EDR schemes publish an annual report containing statistical information about the number of complaints received and the number of complaints upheld for each scheme member. This proposal would unfairly identify the larger retail financial services operators and give a misleading impression of its complaint history.

Licensees are already subject to a number of reporting requirements. Making these details public represents no additional benefits and has the risk of providing a misleading impression to consumers.

# ATTACHMENT A



Investment & Financial Services Association Ltd

**IFSA Submission on  
Developing New Terms of Reference for the  
Financial Ombudsman Services**

Dated: 20 October 2008

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## PART I – INTRODUCTION

The FOS Investments, Life Insurance and Superannuation section (**ILIS**) currently operates under the Rules previously applying to the former Financial Industry Complaints Service (**FICS**). FICS and its predecessor Schemes, commencing in the 1990s, were designed on the basis of covering most but not all complaints. The scheme has operated successfully on the basis of monetary threshold limits.

The FICS Rules had been subject to extensive consultation and review prior to the merger of the Banking and Financial Services Ombudsman, FICS, and the Insurance Ombudsman Service. While IFSA members accept that certain changes to the Rules that will be reflected in the proposed Terms of Reference applying to ILIS may be necessary for greater FOS efficiency, members expect that efficiency to be translated into greater levels of service to FOS members and their clients who choose to avail themselves of the FOS processes to settle a dispute with a FOS member.

The comments and recommendations made in this submission are limited to the proposed Terms of Reference as they apply to ILIS. It is important to acknowledge that ILIS is an industry funded arrangement that is designed to provide a quick and relatively inexpensive determination of client disputes. It is not intended to be a substitute for the courts although FOS ILIS members have, to date, agreed contractually through their participation in the scheme to forego any rights of appeal to the courts other than in the case of a failure of procedural fairness.

As an industry funded scheme it is appropriate that its members determine the scope and purpose of the scheme. It is not, nor should it be the intention that FOS covers all disputes. The fundamental requirement under section 912A(1)(g) of the *Corporations Act 2001 (Act)* that an Australian Financial Services Licensee must be a member of an external disputes resolution scheme in respect of financial services provided to persons as 'retail clients'. The meaning of 'retail client' is defined at section 761G of the Act.

Members recognise that the 'retail client' definition may introduce a level of complexity that would make the operation of ILIS and the determination of access to the scheme by clients difficult. The compromise to date has been that the industry funded scheme should be available to clients of ILIS members where disputed claims fall below specified monetary thresholds for specific types of financial product or service. FICS was designed, on this basis, to cover the majority of claims made, although not all claims. It continues to be the position of IFSA members that any significant change to the scope of the Rules and monetary limits must be based on solid research data, proper assessment of the impact of the changes and cost/benefit analysis<sup>2</sup>.

It should be noted that a number of IFSA members favour limiting the ILIS Terms of Reference to 'retail clients' as defined in the Corporations Act. This would be consistent with the requirements of the Corporations Act, but will limit current access to FOS. A retail investor condition for access will also require additional administration to determine access to FOS.

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<sup>2</sup> IFSA Submission to FICS dated 18 September 2007.

## PART II - RESPONSES TO ISSUES

Issue A: How can FOS simply and clearly define in the new Terms of Reference who is entitled to access the scheme, bearing in mind the need to maintain access for anyone who currently has access to the scheme?

Access to the scheme must be defined by reference to section 912A of the Act. While it is open to FOS members to widen the scope of the scheme, it is the position of members that the scheme supported by ILIS members be available only to investors with claims within specified monetary thresholds. Where claims are in excess of the specified thresholds they are more appropriately dealt with by the courts.

We note that many claims are satisfactorily dealt with at the Internal Dispute Resolution (**IDR**) stage. To avoid the complexity of establishing whether a client is a retail client, no barrier operates under the Rules to exclude any client where the claim is below the monetary threshold. IFSA members would support a continuation of this approach. However, if monetary threshold are increased without solid data, a proper assessment of the impact of the changes and cost/benefit analysis, IFSA members would seek to limit claims to retail investors. This would be consistent with the requirements and obligations of IFSA members under the Corporations Act.

Issue B: How can FOS simply and clearly define small business access to the scheme?

The concept of 'small business' is clearly defined in section 761G(12) of the Corporations Act.

Issue C: How can FOS best promote speedy, ready access to the scheme, whilst preserving the important role of IDR?

The issue implies that IDR acts as a barrier to the operation of FOS. The fact is that many disputes and concerns are settled at IDR. Additionally, IDR is an opportunity for the financial product/service provider to gather all necessary information for the purpose of reviewing the concerns/claim of the client. This documentation forms the basis of the response where a claim is lodged with FOS.

Some IFSA members have expressed a concern that the initial review process favours the complainant rather than the member. In other words, a "no" from the member when dealing with the complaint in accordance with its internal dispute resolution procedure rarely translates into a "no" from the "tribunal" at the initial review stage.

There needs to be an increased discretion and power for those making the initial assessment to, on the papers, make a determination that the claim has no merit. At present, and again this is a general observation which does not apply in all circumstances, if a no is given it is on the basis of jurisdiction not necessarily merit.

This is a process issue which does need to be addressed.

Issue D: How can FOS simply and clearly define in the new Terms of Reference the types of disputes FOS can consider, bearing in mind the need to maintain at least its current scope of jurisdiction?

The current FICS Rules, in so far as they define what FOS can and cannot hear, together with the Monetary limits, forms the best basis for simple and clear definition of the types of disputes that FOS can hear.

Issue E: What exclusions from jurisdiction – including exclusions on the basis of timeframe – should be specified in the new Terms of Reference, bearing in mind the need to maintain FOS's current scope of jurisdiction?

IFSA members continue to support the requirements under the Rules as a jurisdictional basis for the operation of ILIS.

Issue F: When should FOS decline to consider a dispute on the basis of alternative proceedings in another forum? How can FOS best achieve consistency of approach to this across all disputes?

The initiation of proceedings in another forum should disqualify an application to FOS unless both parties agree to submit to FOS and to the determination of the matter by FOS ie. the complainant agrees that in consideration of submitting to FOS it will be bound by the FOS determination.

Anyone who has been charged with a criminal offence relevant to the complaint, or in the event of a conviction – including where fraud issues are involved – FOS should not have jurisdiction to deal with the complaint until the court matters are complete. These are legal issues that are better dealt with in a court (rules of evidence etc).

Issue G: What should be the monetary limits to FOS jurisdiction? How can FOS best achieve consistency of approach to this matter across the divisions?

IFSA members continue to support the current monetary thresholds. As previously advised to FICS, members support the periodic review of the monetary thresholds for disputes involving financial planning, managed investments and stockbroking claims relative to movements in the Consumer Price Index<sup>3</sup>.

As stated in the IFSA submission to FICS dated 20 July 2007, indexation of monetary thresholds is not appropriate for and should not be applied to life insurance risk products. The thresholds should nevertheless be reviewed periodically (2, 3, or 5 years). Increases in the proposed monetary thresholds should be determined having regard to the level of coverage of retail clients.

#### Issues H

We believe that FOS should develop and publish (on website) a Guidelines document (per BFSO Guidelines) which provides more definition to process and approach, and which provides

<sup>3</sup> IFSA Submission to FICS dated 18 September 2007.

members with the context within which FOS can take action and make decisions. Such a document will prevent misinterpretation of terms of reference and ensures accountability.

Issues I to M.

No IFSA member comments received.

### **PART III - RESPONSES TO QUESTIONS**

Question 1: Are there any impacts of the proposed description of consumers that have access to FOS that have not been adequately considered?

We believe the EDR process is to enable consumers without ready access to legal means of resolution an opportunity to have their complaints addressed by an independent third party. Broadening access to the EDR process to consumers with the means to raise complaints through the legal system may increase the number of cases lodged with FOS and impede quick resolution of complaints by those without other methods of recourse.

In relation to the use of the term “individual” in the proposed description of consumers who can use FOS, we note that under the current FICS Rule 7.1 to have access to the scheme the individual must have a legal or beneficial interest in a dealing or transaction.

We also note that under FICS Rule 14.2 discretion existed to the effect that FICS could decide not to deal with a complaint by a **person who was not a “retail client”** as defined under the Corporations Act. IFSA would support the inclusion of a similar provision in the FOS Terms of Reference.

Question 2: Are you aware of any circumstances in which discretions to exclude consumers because of their economic or business status would be essential to FOS operations?

We are of the view that certain individuals/entities should be excluded on the basis that their personal or corporate resources allow them readily to seek remedy via other means (e.g. the courts or professional mediation). For instance (and as suggested above) those who are of high net worth or professional or wholesale investors or those who are running investment companies with sizable assets are well situated to solve their own issues. EDR schemes were established as ‘access to justice’ mechanisms – to assist ‘normal consumers’ who otherwise suffer a negotiation or resource imbalance of power.

Question 3: Do you have a view on excluding access to FOS by otherwise eligible small businesses – if they are part of a group of companies that does not meet the eligibility criteria?

We do not support the extension of FOS ILIS jurisdiction to deal with small businesses that are not retail clients or that otherwise have access to resources. Where an otherwise eligible small business is part of a group of companies that does not meet the eligibility criteria the small business could access other legal forums to address their complaint. We, therefore, believe they should not have access to ILIS.

FOS is not designed for, nor intended to service, entities that otherwise are well situated to address their own concerns (and/or afford representation).

Question 4: Do you have examples of small business that would be excluded by this provision?

No comment.

Question 5: Are there any compelling reasons to consider different definitions for small business access for different sectors of the financial services industry?

We do not consider there are reasons for different definitions provided the aim of restricting access to the majority of consumers who cannot readily access other legal forums is achieved by a common definition. For the purpose of ILIS, access should be limited to consumers within the monetary thresholds who are defined as retail clients.

Question 6: For general insurers, what would be the implications if FOS could consider disputes (claims and non-claims) brought by any small business (as defined in terms of Group employees rather than turnover) in relation to one of the listed business insurance products?

No comment

Question 7: Are there business products not currently listed in the General Insurance TOR that should be included in the new Proposed Terms of Reference as well as within FOS' jurisdiction?

No comment

Question 8: Should FOS itself refer disputes to the IDR area if the complaint has been raised with any area of the financial services provider and remains unresolved (rather than requiring the consumer to do this themselves)?

FOS should not lodge a complaint unless it has first been through the financial services provider's IDR process. Consumers should not be able to go directly to the Ombudsman. It is part of AFSL conditions that the licensee directs consumers to the IDR process and a failure to do so would result in a breach. Such a requirement did not previously exist when the existing scheme terms of reference were developed.

Lodgement by the Ombudsman of a complaint prior to it being through the company's IDR process results in high administration costs. It is also important for the financial services provider to have the opportunity to resolve the complaint and enhance its relationship with the customer. ASIC Guidance Note 165 currently allows a period of 45 days and a shorter period is not justified.

The BFSO charges significant fees to the financial services provider for lodging complaints which are then resolved entirely by the financial services provider. The IOS and FICS do not charge the financial services provider where customers are referred to them for resolution of a complaint. The IOS and FICS arrangements are, in this respect, preferable.

On page 20 of the Issues Paper there is a comment that "ILIS has no requirement that a dispute must be considered by a designated IDR process before it is lodged". We are of the view that FICS Rule 8.1 indicates an IDR is required before a complaint can be accepted as an EDR at FOS. IDR and EDR represent sequential stages in reviewing and resolving a complaint.

We are also of the view that it is not unreasonable for the customer to be the one to lodge a complaint with the IDR department, rather than FOS. There is scope for confusion, double-handling and loss of consumer confidence in the financial institution.

Question 9: What steps should FOS take when using its discretion to commence investigation of disputes that have been with IDR for longer than the ASIC-prescribed time limit?

Given the complexity of some products and services and therefore the complaints associated with them, and the need for third party assessment in some cases, the ASIC-prescribed IDR time limit may be insufficient in some cases. The member should notify the complainant if the IDR process will take longer than the prescribed time limit, provide them with an anticipated timeframe for resolution and the opportunity to escalate the matter to FOS if they are unhappy with this.

If the consumer takes the opportunity to escalate the matter to the EDR scheme at that time, we believe FOS should liaise with the member to determine whether the particular complaint requires a longer period for resolution through the IDR process and whether the member is genuinely actioning the complaint. We propose that FOS give the member 14 days to provide the reasons for the delay and an indicative time-frame for resolving the complaint. If the reasons support a longer period for investigation and consideration and the member is genuinely attending to the complaint, FOS should support the member in their efforts to resolve the complaint through the IDR process.

Where fraud has been identified or claimed (by the consumer, in relation to advice or actions of financial planners), 45 days is insufficient to allow members to fully investigate issues and determine an appropriate outcome. A timeframe of 90 days would be more reasonable in these situations.

Question 10: Are you aware of any disputes that should be within the scheme's jurisdiction in relation to contracts or obligations created outside Australia?

No

Question 11: Are there any other circumstances in relation to the provision of a banking, investment or insurance products where the dispute should be considered by FOS even though the consumer is not a customer or client of the financial services provider?

If there is no contract/agreement that exists between the member and the complainant FOS should not consider the matter unless the complainant is deceased or incapable of initiating a review by FOS and the person can show a beneficial interest in a policy or financial product. For

example (and as reflected by Section 48A of the *Insurance Contracts Act (Cwlth) 1984*) in circumstances where any money that becomes payable under a life policy to a third party, that third party should have access to FOS even though they are not a party to the contract of life insurance.

Question 12: Are there any difficulties that arise from FOSs jurisdiction to consider disputes about privacy or confidentiality in relation to investments or insurance disputes?

The Privacy Commissioner is the subject matter expert on privacy matters and should retain jurisdiction of disputes on such matters to ensure they are handled appropriately. The Privacy Commissioner has recently been provided with additional resources that should enable them to handle privacy complaints more effectively. If complaints are entirely based on a breach of privacy, they should be heard by the Privacy Commissioner.

Additionally, privacy disputes involve awards for non-financial loss and we do not support FOS increasing their jurisdiction to make awards for this, as discussed below. To allow privacy matters to be heard and provided with such awards would be inconsistent. It would also require specialised skills or referral to specialists in Privacy Law and would give rise to increased numbers of complaints, both of which would slow the processing of other cases and impede efficiency.

We note that confidentiality requirements are different to privacy and a breach of confidentiality may involve financial loss. However, these matters would be difficult to investigate and decide and therefore may compromise efficiency.

Question 13: Do the proposed exclusions from FOS' jurisdiction in paragraphs (a) to (d) above adequately address those matters that should be excluded?

We do not have any concerns with the proposed exclusions. However, we believe that FOS should consider the addition of a further exclusion for 'vexatious or frivolous' disputes. This would be consistent with other EDR schemes and allow FOS to focus on genuine disputes rather than devoting resources to disputes which clearly do not have merit. Guidance for FOS officers on what disputes should be excluded on this basis should be provided in operating guidelines. FOS may also wish to consider contacting the provider involved for their views on whether the dispute should be excluded on this basis where the circumstances warrant this.

Many other EDRs include the following:

- (a) the complaint is frivolous or vexatious or was not made in good faith;
- (b) the complainant does not have a sufficient interest in the subject matter of the complaint; or
- (c) an investigation, or further investigation, is not warranted.

*(From the Telecommunication Ombudsman Constitution)*

We would also recommend the exclusion of :

- underwriting or actuarial factors leading to offer of insurance on non standard terms;
- frivolous or vexatious complaints;
- complaints lacking in substance;

- claims related or subject to criminal conduct or charges;
- complaints that are out of time; and

consider that the Terms of Reference need to include the exclusions current FICS Rules 14.1 (i), (l), (m), (n), and (o).

Question 14: Are there any reasons why a single time frame of six years from the date of the cause of action or from when the consumer should have reasonably known of all the facts, should not apply to FOS?

Given the regular and comprehensive disclosure requirements that apply to the financial services sector there is no reason a consumer should not be aware of an event, or all the facts concerning an event, that gives rise to a cause of action well before 6 years has elapsed. We strongly believe that a consumer should lodge complaints as soon as possible, both to the applicable IDR and EDR schemes, as delays in doing so give rise to prejudice and circumstances that hamper investigation and resolution of disputes. This is particularly the case in relation to complaints regarding insurance products as assessors, experts and witnesses to the event, damage or injury may no longer be contactable and damage and injuries/illness may have been exacerbated by the passing of time. We understand that FOS will not reduce the time limits currently available for lodgement and therefore do not support any changes to the current time limits for lodging complaints with FOS.

We believe that after closure of a complaint at FOS, consumers should not be able to reopen the matter after a reasonable (and specifically designated) period of time has elapsed - we suggest 12 months.

It has been noted that the Banking Terms of Reference has a clearer statement of how this applies than the ILIS Terms of Reference. The Banking Terms of Reference (clauses 5.5 and 5.7) say the complainant must notify FOS within 6 years of the event to which the dispute relates (In advice claims, this would be the date of the advice). However, the Ombudsman may consider it if the claimant was not aware of the event and could not have discovered it using reasonable diligence. The ILIS Terms of Reference say a complaint won't be heard if the complainant knew or should reasonably have known of all the relevant facts 6 years before notifying the service." "Relevant facts" isn't defined, and could be interpreted more broadly than the events that gave rise to the dispute. We recommend for clarity, adopting Banking Terms of Reference clauses 5.5 and 5.7.

Question 15: Are there any circumstances in which FOS should be prepared to re-open a dispute where the parties have agreed to settle?

We believe that due care and consideration should have been given to the terms of settlement prior to agreement being reached and actioned. We, therefore, do not consider that FOS should have the power to re-open disputes that have been settled.

Question 16: Should the ToR provide jurisdiction if there is agreement from the parties to consider the dispute?

There may be instances where a member elects to have a matter referred to and/or investigated by FOS where no jurisdiction otherwise exists. This should be entirely at the direction/agreement of the member concerned.

Question 17: Are there any reasons why the Ombudsman should not have the power to decline to consider a dispute if in his/her view there is a more appropriate forum?

No. It is general practice that Ombudsmen have the right to decline to consider a dispute. This faculty exists in all ombudsman charters/constitutions etc.

Question 18: Do you support a common monetary limit for lump sum disputes across the FOS jurisdiction?

We strongly believe that the technical differences and values involved with different products and services across the industry warrant specific approaches in relation to monetary limits. We note that the limits have been thoroughly reviewed in 2007 and increases, where justified, have been implemented. A copy of the IFSA submission setting out the position of IFSA members is attached (Attachment A). The current limits allow access to the majority of consumers based on an analysis of those consumers and the products and services concerned.

Consistency is valuable where it reduces confusion for consumers and enhances the efficiency of the scheme. In this instance, confusion can be limited by providing clear information on the lump sum monetary limits for each product and service in information on the FOS website and in other published material. Additionally, efficiency is not enhanced by consistency in this area as increasing the limit, by almost double in some cases, will result in a larger number of disputes being lodged, slowing processing for the majority of consumers. We therefore do not support any changes to the current monetary limits.

Question 19: If a common monetary limit is not applied for FOS disputes jurisdiction, what policy basis should be used to establish and maintain differential limits for sectors or products?

As set out in IFSA's submission in response to FICS Discussion Paper on the review of monetary limits in 2007 we would support:

1. The periodic review of monetary thresholds for disputes involving financial planning, managed investment and stockbroking claims relative to movements in the Consumer Price Index; and
2. An increase reflecting CPI increases every three years.

As stated in the IFSA submission dated 20 July 2007, indexation of monetary thresholds is not appropriate for and should not be applied to life insurance risk products. The thresholds should nevertheless be reviewed periodically (2, 3, or 5 years). Increases in the proposed monetary thresholds should be determined having regard to the level of coverage of retail clients.

Question 20: Should there be a fixed ratio between the lump sum monetary limit and the monthly income stream limit? If not, what should be the basis for fixing the monthly income stream limit?

We believe extensive input into this specific issue has already occurred during 2007 and we reject that this now be a subject for consideration under the new Terms of Reference. It was rejected by the Industry and the rejection was accepted by FICS (see IFSA submission dated 20 July 2007 – Attachment B).

The current limit for monthly income stream claims should be fixed. This should be the case as fraud is often a factor in such claims and is difficult to prove without the benefit of cross examination and rules of evidence applied to cases in the judicial system. The proposal to increase the limit to almost double the current limit will significantly impact providers and is inappropriate, given the majority of such cases involve technicalities that are best addressed through the judicial system where consumers seeking more than the limit should be able to pursue these claims.

Question 21: What are the reasons why consumers should or should not be allowed to 'opt-in' to the FOS monetary jurisdiction?

Consumers should not be able to opt-in and effectively 'shop around'. FOS should seek the quantum of the dispute up front. If the quantum is beyond the jurisdictional limits, the dispute should not be heard by FOS. This is a longstanding principle used in civil law.

The other problem with the 'opt-in' model is the potential that some consumers may elect to use FOS as a 'dry run' for court proceedings (e.g. a customer with a \$500,000 complaint may reduce it to \$279,000 and have the matter investigated by FOS. If FOS issues a Finding in favour of the consumer, he or she could then reject the Finding and go to the courts – with the FOS Finding in hand. This would make FOS a 'free discovery' service which, clearly, it is not intended to be.)

Again, as set out in IFSA's submission in response to FICS Discussion Paper on the review of monetary limits in 2007 if an 'opt-in' system is proposed IFSA members believe it would need to be supported by:

- solid research data;
- a proper assessment of the impact of behaviour and approach to disputes that removal of jurisdictional monetary thresholds will have; and
- a costs/benefit analysis

before it can be seriously considered.

There is, we believe, existing evidence under current arrangements to suggest that, depending on the amount of a claim, complainants may for a variety of reasons use FOS as a dry run. By way of example, an IFSA Member has advised that it is aware of at least three matters which arose in 2007 where a complainant has initiated legal proceedings requesting that the matter be held in abeyance while the matter is heard by an EDR scheme. Their assessment is that this appears to be a developing trend which is likely to be significantly fuelled by any opt-in proposal.

It needs to be noted that claims coming to FOS have already been through Internal Dispute Resolution procedures of licensees. Matters going to FOS involve a further cost to licensees and FOS does not afford the protections that are available to Members through the litigation process, particularly in claims which can be considered as significant.

Question 22: If either a 'cap' system of limiting the Ombudsman's power to award, or a discretion to the consumer to 'opt-in' were used, what would the impact be? What measures would be required to manage that impact?

IFSA is of the view that there would be significant impact and for this reason opt-in should not be allowed. Please refer to the answer provided to Question 21 above.

We believe a 'compensation cap' or 'opt-in' proposal would increase the number of applications and include numerous complaints intended to be dry runs, which would reduce the efficiency of the system..

Additionally, claims with values that exceed the monetary limits will often involve complex issues and technicalities that may best be addressed through the judicial system. It is also likely that such consumers are able to access the judicial system more readily than others. We, therefore, believe providers should be required to consent to FOS addressing complaints where consumers wish to 'opt-in'. This measure, in addition to that suggested above will ensure frivolous claims and those that are best addressed through the judicial system are excluded from the FOS scheme and do not compromise the efficiency of the scheme for other members and consumers.

Question 23: Should the monetary limit(s) be required to be reviewed by the Board every three years or automatically indexed to CPI every three years?

As set out in our response to Question 19 above, the monetary limits should be automatically indexed by CPI every 3 years. Indexation of monetary thresholds is not appropriate for and should not be applied to life insurance risk products. The thresholds should nevertheless be reviewed periodically (2, 3, or 5 years). Increases in the proposed monetary thresholds should be determined having regard to the level of coverage of retail clients.

Question 24: If an Ombudsman model is adopted rather than a Panel model, what arrangements would best give the Ombudsman access to industry/consumer expertise?

We do not support the elimination of the panel model.

Should a hybrid or Ombudsman system be adopted, the current system whereby case managers access technical advisers should be reviewed. It may be that specialists from members and consumer groups are available to provide advice to FOS.

Question 25: If you have experience of both systems, do you think that the Ombudsman model or the Panel model would best deliver fair and consistent decision making in the most time and cost efficient manner?

While FOS' comments regarding costs associated with the panel model are acknowledged, it is believed that the Ombudsman Model may involve similar amounts where complex matters require referral to industry specialists. Similarly, while it may appear more efficient, the referral to a

technical specialist may take some time, following the initial consideration and determination that a referral is required. Considerably more time would be involved should the process then involve escalation to the Ombudsman.

While FOS may seek to employ case managers that would give fair consideration to cases and refer complex matters when necessary, recruitment of such individuals is not guaranteed and training may not eliminate the risk that case managers do not refer complex matters when appropriate or give them due consideration. The Panel Model ensures that a technical/industry and consumer representative considers the dispute and brings their experience and knowledge to the assessment with mediation by a Panel Chair. This approach therefore provides more confidence of a balanced assessment and reduces the risk of a bias or lack of action by a single individual tasked with the management of the dispute and therefore should be available when required.

To ensure efficiency and consistency in decision making for the majority of cases of small value or where the issues are not complex, an Ombudsman model may be best practice. We propose a hybrid model which combines elements of the Ombudsman and the FOS (FICS) panel.

In our proposed approach the FOS Case Manager would receive submissions from the member and the consumer. If the matter is straight forward and the case officer feels able to, they should then make a recommendation to both parties. If both parties accept the recommendation then the matter is resolved, otherwise the matter should either be taken to conciliation or sent to the adjudicator or panel for a determination.

If upon receiving the submissions the Case Manager determines that a recommendation is not appropriate but that a conciliation meeting has a high chance of resolving the complaint, they should have the power to refer the case immediately to conciliation or the adjudicator or panel. In cases where it appears that the parties are diametrically opposed (i.e. the consumer wants \$100K and the member is offering \$0) then the matter should be referred immediately to a decision by the adjudicator or panel.

In relation to the references to adjudicator or panel, we suggest that a monetary limit and assessment of complexity determine which of these is appropriate in the circumstances of the dispute. We would seek to make separate recommendations on an appropriate threshold amount. Amounts over the adjudicator's threshold would go to the panel. Adjudicators should be technically qualified in the areas in which they hear cases to ensure confidence in their decisions. Regardless of monetary limits, a provider should be able to request panel consideration of a matter if the technicalities of the dispute are particularly complex.

Question 26: Should there be a different dispute resolution process for General Insurance fraud disputes?

We believe that all insurance product disputes involving fraud require particular attention and, given the nature of the issues involved should not be decided solely on the basis of documented case histories and accounts. We therefore support development of a different process.

This process should involve an oral hearing to ensure the decision maker, be that a panel, adjudicator, case manager or Ombudsman, speaks to the consumer directly regarding the particular issues in the case. We wish to point out that the current system applied to general insurance fraud cases, particularly in relation to oral hearings, is deficient in some areas. The ability of consumers to prevent providers from attending oral hearings is biased and does not allow the provider fair access to all of the information on which the dispute will be decided. Additionally, the current system does not provide confidence that consumers' honesty is assured. While we acknowledge that honesty can never be totally assured, we believe a requirement for

truthfulness (e.g. by requiring that information be provided under a statutory declaration) and adverse implications for a party if they are proven to have been dishonest should be imposed.

We note that cross examination and other processes associated with a court hearing are inappropriate in the context of an EDR scheme. However, we suggest that a system where the Ombudsman, case manager or panel can ask questions of consumers, providers and relevant experts and witnesses with a requirement for honesty should be implemented. Both parties should be given access to this hearing. Where there is a subsequent finding of dishonesty, any decision based on that should be reversed and the matter reconsidered as a matter of course. This process should be developed and applied to life and income protection insurance in addition to general insurance matters involving allegations of fraud.

Question 27: Do you have any comments about the general principle of limiting the amount of procedural detail in the proposed Terms of Reference?

IFSA supports FOS in its statement that it does not wish to set out the detail of its processes in the Terms of Reference (p. 36 of Issues Paper). Whilst we believe that some reference should be made in the Terms of Reference to FOS operating manuals and guidelines, IFSA is of the view that the model of the BFSO in providing its operating guidelines on a website would be an appropriate course of action.

Question 28: Do you have any comments about the FOS dispute resolution procedures described in (a) – (e) above?

The proposed procedures appear appropriate and to reflect best practice. In particular we support FOS' proposal to attempt initial resolution of disputes through negotiation and conciliation.

In terms of FOS not being bound by previous decisions, it would be appropriate for FOS to provide communication and/or guidelines in regard to this issue. It should be clear that FOS aims for consistency and, while each case has its own facts and issues, FOS intends that a similar approach will be adopted in respect of certain recurring issues (see Issue H above).

Question 29: If you have any experience with more than one FOS Division, are there advantages or disadvantages from your perspective to common dispute resolution procedures as described?

We believe that consistency across the divisions will improve efficiency. While we do not support consistency where this will compromise the aims of the system, such as imposing common monetary limits across the divisions, we do believe a consistent approach to processing the disputes will reduce confusion among consumers and enhance the transparency of the system. We note, however, that within the broad framework proposed there should be specific guidelines for cases that warrant particular processes, such as insurance fraud disputes, as discussed above.

Question 30: Should FOS have the ability to award compensation for non-financial loss?

Consideration of amounts required to compensate for non-financial loss would involve subjective assessments of individual circumstances. Given the process does not use the rules of evidence associated with the court system, the inclusion of such compensation would be inappropriate and give rise to inconsistent decisions. In the interests of efficiency and consistency in decision-making we believe non-financial loss should not be considered by FOS.

IFSA members support the retention of FICS Rule 33.4.

Courts hear evidence on the nature of non-financial loss and have some experience in determining appropriate amounts. This is a very complicated situation, and it is not appropriate for a forum such as FOS to make a decision in situations where which hears evidence only on the papers, doesn't have witnesses and there is no opportunity for cross-examination.

Question 31: Should FOS have the ability to award compensation for consequential loss?

Consideration of consequential loss would also be subjective and involve the impacts discussed above. A decision as to whether this flows directly from the conduct complained of is a complex one and can involve a degree of speculation. The awarding of consequential loss is not appropriate for a forum which works on papers etc, and is intended to be short and inexpensive for both parties. Therefore, we do not support FOS having the power to award compensation for consequential loss.

Question 32: Should there be any limits specified in the proposed Terms of Reference as to the amount that can be awarded by FOS in relation to these types of losses?

Monetary limits should include all amounts that may be awarded. This includes legal costs, interest and awards for the claim itself, including for non-financial or consequential loss should they be included as a result of this review. Where interest is included, members should not be liable for delays by the consumer in lodging with FOS, or through the period in which FOS considers the matter. It may be difficult to identify and exclude all such periods but, where possible, we encourage FOS to consider this as a means of encouraging efficiency in the lodgement of disputes and commitment to an efficient resolution process.

IFSA members do not support FOS having an ability to award compensation for indirect loss, non-financial loss or punitive damages.

Question 33: When calculating the amount being claimed for the purposes of the monetary limit, should claimed non-financial losses and interest be included?

Current FICS Rule 34 should continue to apply. As provided in our response to Questions 30 to 32, FOS (ILIS) should not have an ability to award compensation for non-financial or consequential loss.

Question 34: What would be the advantages and disadvantages of allowing both parties an opportunity to make submissions when a Recommendation was appealed to Determination

stage?

We believe that members and consumers should be encouraged to accept Recommendations and appeal to the Determination stage in only significant cases. Where this occurs, both parties should be given the opportunity to provide written statements in response to the Recommendation.

Advantages are:

- provides an ability to respond to a recommendation;
- should allow the admission of new evidence;
- may result in earlier finalisation of the issue.

Disadvantages are:

- may delay the final determination of issue;
- may make the first stage of negotiation and conciliation less important (a precursor to the second).

Given the ability of consumers to not accept a determination under any outcome, ILIS members would seek a right to appeal a determination. Certainly, at a minimum FICS Rule 36.3 should be replicated in the Terms of Reference.

Question 35: Does this approach to the “test case” process appropriately balance financial services providers interests in ensuring that really significant matters are determined by the Courts and fairness to consumers given that they may be deprived of access to FOS if process invoked before the decision is made?

We believe that the proposed grounds for removing a case to the judicial system as a ‘test case’ will ensure appropriate cases are treated as such. However, we believe providers should be able to give notice of a ‘test case’ at any stage of the FOS dispute resolution process and not only as an appeal process. Allowing test cases to be elevated to the judicial system as soon as possible will ensure they do not compromise the efficiency of the FOS process for other cases.

The approach adopted in Rule 18 of the FICS Rules is the preferred approach of ILIS members. That approach provides both appropriate barriers to misuse and safeguards in relation to costs.

Question 36: Would the inclusion of examples assist in the understanding of what constitutes systemic issues? The examples that ASIC gives in RG139 are: poor disclosure or communication, administrative or technical errors, product flaws and improper interpretation or application of standard terms.

FOS is currently required to report providers they consider have systemic issues. ASIC is currently reviewing the Regulatory Guides that pertain to EDR schemes and has indicated that schemes often do not disclose the names of providers they report for this. ASIC proposes to include measures in the Regulatory Guides to compel EDR schemes to disclose providers who they consider have systemic issues and to publicly report on the number of these issues and reports to ASIC. Given this proposal and the broad nature of the definition, we strongly believe that examples should be provided. These may be in detailed guidelines supporting the Terms of Reference or the Terms of Reference itself.

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Further, we believe FOS should give the provider notice and an opportunity to discuss the issue FOS may propose to report as systemic prior to their contact with ASIC. This will enable the provider to clarify the situation and any measures they have taken to address the issue.

Question 37: Is the definition of 'serious misconduct' sufficiently clear and the ambit appropriate? What can be done to minimise the "grey area" as to what is reportable and what is not?

We acknowledge the difficulties in including prescriptive measures in the Terms of Reference and support the principles-based approach, as discussed above. However, we believe the definition of 'serious misconduct' is not sufficiently clear, given the consequences of a finding of this nature. We believe examples should be provided, as above. We also believe FOS should engage with the provider regarding actions they consider to be serious misconduct prior to contacting ASIC, for the reasons discussed above.

#### **PART IV – OTHER MATTERS**

On 24 July, IFSA made a submission to the Ombudsman for the Investment, Life Insurance and Superannuation Division, Alison Maynard, in relation to FOS members' voting power under the FOS Constitution.

Under the Constitution each FOS member has one vote for each dollar paid by way of levies and case costs. This provision has the undesirable effect that those FOS members who have had more complaints made against them in any financial year will have more voting power on resolutions that are put to a poll.

As noted in IFSA's submission, our members consider the departure from votes being based on membership category to votes being based on dollars paid, to be a significant governance issue. While we note that the practical effect on voting may be insignificant, IFSA considers that the current provisions of the FOS Constitution regarding voting sends the wrong message to industry and consumers.

We note FOS' response to our submission indicated that the issue of voting rights under the Constitution would be reviewed in 2010 with such review having regard to:

- Experience of current voting arrangements from 1/7/08 to 31/12/09;
- Feedback from Stakeholders in relation to current voting arrangements received 1/7/08 to 31/12/09;
- Feedback received from the relevant Board Advisory Committees; and
- New levy and case cost structure adopted from 1/10

IFSA looks forward to working with FOS in its proposed review of voting rights under the FOS Constitution in 2010.

**Attachment A**

IFSA Submission dated 18 September 2007 on *Review of the FICS Monetary Limits – Discussion Paper*

**Attachment B**

IFSA Submission dated 20 July 2007 on *Review of the FICS Monetary Limits – Consultation Paper*

# **ATTACHMENT B**



Investment & Financial Services Association Ltd

ACN 080 744 163

20 July 2007

Mike D'Argaville  
Legal Counsel  
Financial Industry Complaints Service

mdargaville@fics.asn.au

Dear Mike

### **REVIEW OF THE FICS MONETARY LIMITS – CONSULTATION PAPER**

We refer to the FICS Consultation paper on the review of Monetary Limits and make the following submission in response to the issues raised. The following submission reflects the views of IFSA Members following wide ranging consultation.

As a preliminary comment, IFSA members strongly support the operations of FICS as a venue for the settlement of disputes with retail clients where the matter cannot be determined through internal dispute resolution processes of Members. We consider that the recent review and amendment of the FICS Rules has improved the existing framework and transparency for the resolution of retail client disputes.

Our comments are made in relation to:

1. Application of the monetary limits
2. Two tiered approach
3. Level of limits
4. Indexing the limits

#### **1. Application of the monetary limits**

Members do not favour the proposal to effectively remove the monetary limits other than for the purpose of capping the maximum amount that could potentially be awarded by FICS. The proposal would potentially expand the jurisdictional coverage of FICS while limiting the quantum of awards that could be made where an adverse finding is made against a FICS member.

Potentially this would encourage claims from both retail and non-retail clients, and any perceived administrative advantage arising from not having to address jurisdictional issues is likely to be lost through increased volumes of speculative claims made at no cost to the claimant.

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We note from the FICS 2006 Statistics appearing on the FICS website that there was a total of 7045 Telephone Enquiries and Complaints Received in 2006, with only 713 Complaints Received progressing to investigation. It is not unreasonable to anticipate that this area would become a much more attractive ground for plaintiff lawyers without necessarily benefiting consumers and that a much larger number of these matters would progress to investigation although not necessarily be finalised.

The concept of complainants being effectively required to sign a Release to give up rights to claim any amount in excess of the threshold raises issues of equity, good faith and the appropriate forum for the hearing of the dispute. It is, we believe, in the interests of both consumer and industry to have issues determined in the appropriate forum.

Specifically in relation to the point made in the Consultation Paper that at “present FICS seeks to establish whether a complaint is within the monetary limit at the time the complaint is received” and that this “process can be complex, time consuming and expensive for FICS and its members” we make the following comment. At first instance, this appears to be primarily a communication issue with potential complainants. In this regard, we note that the Banking and Financial Services Ombudsman (**BFSO**) service uses an electronic ‘Jurisdiction Checker’ as a tool to assist potential complainants and we recommend that FICS consider the introduction of a similar facility and consideration be given to making the FICS webpage more ‘user friendly’.

IFSA Members do not support the UK Financial Ombudsman Service style approach to monetary limits. We do, however, support appropriate monetary thresholds being determined for the life insurance and other categories of complaint. In each case the threshold should reflect a dollar amount that provides sufficiently broad coverage of retail clients for that type of investment product or service. We note ASIC’s statement in PS139 (now Regulatory Guide 139) at paragraph 96 that sets out the underlying principles of the guidelines. It states that:

RG 139.97 Whether a scheme has a sufficiently broad coverage will be assessed by us on a case by case basis. However, determining an appropriate level of coverage will always involve a degree of compromise as some complainants will be denied access to the scheme’s procedures.

To expand the jurisdictional approach of FICS beyond its current settings would, in our view, necessitate the consideration of charges being levied on complainants as suggested in RG 139.102. ASIC states:

RG 139.102 However we also recognise that charging may be appropriate in some limited circumstances. For example, where the scheme seeks to extend its jurisdiction beyond the consideration of “consumer” or appropriate “small business” complaints, or where a scheme seeks to provide its services for a fee where the complaint is clearly outside the scheme’s jurisdiction.

## **IFSA Position – Conclusions and Recommendations**

IFSA Members:

1. do not support an amendment to the FICS Rules that would waive the jurisdictional monetary threshold limit for the consideration of a dispute by FICS and would apply the monetary threshold limit to the maximum amount that could be awarded against a FICS Member against whom there is an adverse finding;
2. consider it preferable to amend the monetary jurisdiction limits to ensure that the threshold amounts remain appropriate. We recommend that a requirement for a periodic review of the monetary threshold be introduced. Such a review could be carried out on a 2, 3 or 5 yearly basis.

## 2. Two tiered approach

IFSA Members do not support the introduction of a two-tiered approach.

## 3. Level of limits

IFSA Members support an increase of the FICS monetary limits for lump sum insurance products. However, IFSA Members do not support a general increase to the BSFO limit for non-life insurance products, or for life insurance income stream products.

The IFSA FICS Working Group met on 21 June 2007 to consider the proposals for increases to the lump sum limits. The recommendations of the Working Group for both life insurance and non-life insurance products and services are considered separately below.

### Life Insurance

The IFSA FICS Working Group recommended that the existing lump sum life insurance limit of \$250,000 be aligned with the BSFO limit, increasing the threshold amount to \$280,000. IFSA Members are, however, supportive of an increase to \$300,000 for lump sum life insurance.

IFSA Members do not support any variation of the threshold amounts for Insurance Income Stream products.

A survey of IFSA Members with life insurance business was undertaken to gather information for the purposes of the Consultation Paper produced the following results:

### **Insurance Lump Sum**

Number of Risk Policies < \$300,000	% in force within limits
1,565,841	72.6%

### Insurance Income Stream – Monetary Limit \$6,000 per month

Number of Risk Policies < \$6,000	% in force within limits
319,000	78%

#### IFSA Position - Conclusion and Recommendations:

1. FICS statistics continue to indicate that consumers have low levels of complaints with respect to life insurance products.
2. An increase in the current *Lump Sum* limit of \$250,000 to \$300,000 will approximate the same level of coverage at its 2004 level i.e. 74% of all risk insurance lump sum policies in force.
3. In 2004, IFSA was advised that the average size of income protection policies was below \$4,000. The monetary limit of \$6,000, set in 2002, far exceeded the size of the average income protection product. The current threshold will continue to provide an appropriate level of coverage at 78% of all income protection policies in force.

IFSA will not support raising current limits unless it can be shown that retail clients are actually being disadvantaged. Indexation is not an appropriate factor to be taken into account for life insurance products as premiums paid relate to a fixed sum insured – an insured who has paid for premium coverage of \$250,000 can only ever recover a maximum of \$250,000.

#### Non-Life Insurance

Non life insurance claims cover financial planning, managed investments and stockbroking. Such claims will always relate to the value of money invested at a future point in time. As such, the Consumer Price Index (**CPI**) is a relevant factor in assessing the monetary threshold for activities in these areas.

IFSA Members support the increase in the FICS monetary threshold in respect of financial planning, managed investments and stockbroking claims from the current limit of \$100,000 to \$130,000.

#### IFSA Position - Conclusion and Recommendations:

1. IFSA Members support the periodic review of the monetary threshold for disputes involving financial planning, managed investments and stockbroking claims relative to movements in CPI.
2. The current monetary threshold of \$100,000 should be increased to \$130,000 to reflect increases in CPI.

#### 4. Indexing the limits

As discussed in section 3 above, IFSA Members consider indexation is an appropriate measure for reviewing and determining movements in the value of the monetary threshold for disputes in relation to financial planning, managed investments and stockbroking claims. It is not relevant to life insurance risk claims where the sum insured is fixed.

**IFSA Position - Conclusion and Recommendations:**

1. IFSA Members support the indexation of the monetary threshold for disputes involving financial planning, managed investments and stockbroking claims on the basis of movements in CPI.
2. The monetary threshold for financial planning, managed investments and stockbroking claims should be reviewed periodically (2, 3 or 5 years) on the basis of movements in CPI.
3. Indexation of monetary thresholds is not appropriate for, and should not be applied to, life insurance risk products. The thresholds should nevertheless be reviewed periodically (2, 3, or 5 years). Increases in the proposed monetary threshold should be determined having regard to the level of coverage of retail clients.

IFSA would be pleased to provide further explanation or assistance to FICS in relation to the current review. Should you require further clarification please contact me or David Micó on 02 9299 3022.

Yours sincerely



**David O'Reilly**  
Policy Director - Regulation  
**Investment & Financial Services Association**

# **ATTACHMENT C**



Investment & Financial Services Association Ltd

ACN 080 744 163

18 September 2007

Mike D'Argaville  
Legal Counsel  
Financial Industry Complaints Service  
PO Box 579  
Collins Street West  
Melbourne Vic 8007

Dear Mike

### **REVIEW OF THE FICS MONETARY LIMITS – DISCUSSION PAPER**

We refer to the further FICS Discussion Paper on the review of Monetary Limits and make the following comments in response to the issues raised.

Members have broadly expressed their concern that FICS appears to have summarily dismissed the earlier IFSA submission in relation to:

- 1 Jurisdictional Limits – monetary limit applies to Panel awards only;
- 2 Monetary threshold for life insurance income stream claims; and
- 3 Increases in the monetary threshold for non-life insurance claims.

A number of IFSA Members have advised that if these proposed changes to the FICS Rules are approved by the FICS Board, they will move to disallow them within the 60 day period following notification.

#### **1. APPLICATION OF THE MONETARY LIMITS**

IFSA Members do not support an amendment to the FICS Rules that would waive the jurisdictional monetary threshold limit for the consideration of a dispute by FICS and, applying the jurisdictional monetary threshold limit to the maximum amount that could be awarded against a FICS member against whom there is an adverse finding.

We do not agree with the analysis or reasons provided in the Discussion Paper for rejecting IFSA Member concerns.

##### **1.1 Efficiency**

A primary reason advanced by FICS for this change is that it will save FICS time and resources in making an initial assessment of the amount of the claim for jurisdictional purposes. Any such savings is likely to be minimal as the number of matters to be considered by FICS is likely to increase significantly. This will result in both additional administrative costs for FICS and FICS members.

We note that:

- FICS will still have to make an initial assessment of the quantum of a claim.
- Early assessment of a claimed amount helps the complainant to understand what they could realistically expect if they were successful and allows FICS members to further assess the commercial benefits of settling the matter, increasing the prospects of settlement and reducing the prospects of adjudication or panel hearing being necessary.

- Where a claim exceeds the relevant threshold it should not be entertained and the client should be directed to an appropriate forum for the determination of their claim.

## 1.2 “Dry Run”

We note that FICS is dismissive of the likelihood that the removal of jurisdictional limits will encourage the lodgement of claims in excess of the claim thresholds to enable complainants to have a “dry run”. The basis for the assertion is that FICS is aware of only 5 occasions in the past several years in which unsuccessful complainants have pursued a claim in the courts.

Before such a fundamental change to FICS jurisdiction will be seriously considered by IFSA Members it needs to be supported by:

- solid research data;
- a proper assessment of the impact on behaviour and approach to disputes that removal of jurisdictional monetary thresholds will have; and,
- a cost/benefit analysis.

FICS would not necessarily be informed when an unsuccessful complainant has chosen to pursue legal action in the courts. We believe it has occurred more frequently than the cases of which FICS is aware. We are advised that one IFSA member is currently defending 2 separate litigated proceedings where the claimant obtained a FICS determination, was dissatisfied, and then issued court proceedings. Another IFSA Member has advised that it currently has 2 cases that have proceeded from FICS to Court and a further 2 complainants have put their court cases on hold until the matters go through FICS. A third IFSA Member has advised that over the last 12 months they have had 1 claim where the complainant has gone to Court after initially having the matter determined by FICS and that over the same period they have between 35 – 40 litigated claim files for amounts above the current limits but below the increased limits. It would seem that the FICS assumption is likely to be grossly understated if a proper review of the FICS membership was undertaken.

In relation to behavioural assessment, the proposed rule amendments will change the incentives for a claimant to take a “dry run”. At present, the risk for FICS members is that if a complainant is dissatisfied with a FICS determination or ruling on damages that complainant will have a second go in court in the hope that the outcome will be different. The proposed change introduces a rather different risk that a complainant with a claim substantially exceeding the jurisdiction will get a favourable determination from FICS, and forgo that to litigate the same case in the hope of getting the same outcome but higher damages. This is not conducive to efficient and speedy resolution of complaints.

There is, we believe, existing evidence under current arrangements to suggest that, depending on the amount of a claim, complainants may for a variety of reasons use FICS as a dry run. By way of example, a fourth IFSA Member has advised that it is currently aware of at least three matters which have arisen in recent months where a complainant has initiated legal proceedings requesting that the matter be held in abeyance while the matter is heard by an EDR scheme. Their assessment is that this appears to be a developing trend which is likely to be significantly fuelled by the FICS proposal. Additionally, by its own admission, FICS states that “it remains open for complainants to reject the decision” and that they could then “pursue the claim afresh in another forum”.

It needs to be noted that claims coming to FICS have already been through Internal Dispute Resolution procedures of licensees. Matters going to FICS involve a further cost to licensees and FICS does not afford the protections that are available to Members through the litigation process, particularly in claims which can be considered as significant. Members are bound by decisions of FICS (unlike complainants) and the normal protections of the Court do not apply.

IFSA Members are unwilling to support the proposal without solid research, behavioural assessment, and cost benefit analysis being first undertaken. We do note, however, the concerns raised by FICS and ASIC over loss calculations close to the threshold limit that may fluctuate over time and IFSA Members would support FICS being able to consider non-life claims and hear cases above the monetary limits but only within a closer range (for instance up to 10% above the monetary limits).

## 1.3 Appropriateness of FICS as a forum

IFSA supports FICS as a cost-effective, informal and quick alternative to court proceedings. IFSA notes that PS 139.34 refers to “a majority of consumer complaints”. FICS and ASIC acknowledge that the forum will not cover all complaints.

IFSA believes that relevant factors for FICS to take into account when determining where setting the boundaries should include the following points:

- because the procedure involves no cost to claimants, there is no disincentive to claimants bringing speculative or completely unmeritorious claims. Members invest time and resources in providing a substantive response to such claims, and are then required to expend significantly greater time and resources to participate in the FICS procedure.
- the procedure deprives members of safeguards including strict rules of evidence, ability to join other parties and the right of appeal.

FICS has acknowledged these issues but does not seem to have given any weight to them in its preferred outcome.

Life insurance contracts provide a further illustration of the difficulties with the jurisdictional approach. Life Insurance contracts involve ‘all or nothing’ liability. Regardless of the type of contract, an insured either meets the definition and is entitled to the full benefit, or they do not meet the definition and no entitlement arises.

The FICS position is that they will effectively only be able to rule on part of the contract where the amount exceeds the monetary limit. This will force insurers to make part payments, effectively altering the terms of the policy. The proposal means that FICS will have the power to vary the contractual terms as agreed between the parties. This is not, and was never intended to be, the role of FICS.

## 2. INCOME STREAM LIMITS

IFSA Members will not support raising current limits unless it can be shown that retail consumers are actually being disadvantaged. The current Income Stream limit will continue to provide an appropriate level of coverage at 78% of all income protection policies in force.

### 2.1 Understanding Income Stream

No consideration appears to have been given to the potential impact of the proposed increase in the threshold limits on Insurers where there is an adverse FICS decision. Income stream products generally have benefits payable to age 65 and in some cases beyond 65. With the income tax changes announced in May 2007, the two year benefit limit on members of superannuation funds has been removed with cover now available to age 65.

Using the current Income Stream limit of \$6,000 per month, the table below demonstrates the potential liability an Insurer would incur.

<i>Age at Claim</i>	<i>Calculation</i>	<i>Maximum Liability</i>
30	\$6,000pm 12 months 35 years	\$2,520,000
40	\$6,000pm 12 months 25 years	\$1,800,000
50	\$6,000pm 12 months 15 years	\$1,080,000

### 2.2 Limits & Liability

The life insurance industry made a very generous concession in supporting a change to the current limit of \$6,000 and now FICS is attempting to impose a substantial increase and make

provisions for automatic increases without due regard to either the liability exposure it places on an insurer or the relativity to lump sum limits.

The Income Stream liability of \$2,520,000 (assumed 35 year benefit payment) represents a multiple of 10 times the current Lump Sum Limit and 9 times the proposed new limit of \$280,000.

By increasing the Income Stream limit to \$7,000pm, then the liability increases to \$2,940,000 which is nearly 12 times the current Lump Sum Limit and 10.5 times the proposed new limit.

### **3. LUMP SUM LIMITS**

#### **3.1 Life Insurance**

IFSA Members support an increase of the FICS monetary limits to \$280,000 for lump sum insurance products. However, IFSA Members do not support automatic indexation as proposed for life insurance products. Indexation is not an appropriate factor to be taken into account for life insurance products as premiums paid relate to a fixed sum insured – an insured who has paid for premium coverage of \$280,000 can only ever recover a maximum of \$280,000.

As stated in our submission of 20 July 2007, indexation of monetary thresholds is not appropriate for, and should not be applied to, life insurance risk products. Increases in the proposed monetary threshold should be determined having regard to the level of coverage of retail clients.

#### **3.2 Non-life insurance**

The data justifying the significant increases seems largely to be derived from aggregated figures (total Funds under management, total increase in superannuation contributions). As these may reflect larger numbers of consumers holding investments at all, or increases at the lower end of the scale, they do not really tell us whether the average investment superannuation balance has significantly increased beyond the present FICS limits.

In any event, average balance is not a reliable guide to the average size of a non-life claim. Insurance claims are often all or nothing - the policy responds or it does not. In these situations the size of the policy does reflect the potential size of claim. Investment claims are most likely to involve partial loss. In the case of catastrophic claims such as Westpoint, where the total investment may have been lost, these are situations where the consumer is most likely to have access to a low cost or no cost avenue such as class action / litigation funder - this should be taken into account when balancing the benefits and disadvantages of extending FICS coverage to potentially very large claims.

Statistics on claim size that have been collated by one IFSA Member with significant distribution has found that, in the period from 1 October 2005 to present, the vast majority -- 86% -- of advice-related complaints dealt with for its dealerships, fell within the existing FICS limit of \$100,000. IFSA Members believe that the case for raising the monetary threshold as is proposed has not been established.

IFSA Members restate the recommendation made in the IFSA submission dated 20 July 2007 and their support for:

3. the periodic review of the monetary threshold for disputes involving financial planning, managed investments and stockbroking claims relative to movements in the Consumer Price Index; and
4. an increase, reflecting CPI increases in CPI, of the current monetary threshold of \$100,000 to \$130,000 .

### **4. TIMING**

Some IFSA Members believe that the Discussion Paper should be withdrawn or deferred given both the recent announcement regarding the merger of FICS with the Banking and Financial Services Ombudsman and the Insurance Ombudsman and, until there is greater certainty from ASIC in relation to compensation and insurance arrangements for Australian Financial Services Licence (AFSL) holders..

As you are aware, ASIC released a Consultation Paper on Compensation and Insurance arrangements for AFSL holders on 23 July 2007. This paper proposes a link between the professional indemnity insurance arrangements required for AFSL holders and the EDR scheme limits. It is, therefore, important that the outcome of this paper is taken into consideration in any amendment to the FICS monetary limits.

In addition, given the proposal to merge the three EDR schemes, it would seem more appropriate to wait until the merger occurs and consider the monetary limits (as well as other practical consequences) with respect to the merged entity.

## 5. CONCLUSION

IFSA Members strongly support the operations of FICS as a venue for the settlement of disputes with retail clients where the matter cannot be determined through internal dispute resolution processes of Members. However, IFSA's Members will not support significant changes to the FICS rules that are not based on solid research data, a proper assessment of the impact of the changes and cost/benefit analysis.

IFSA would be pleased to provide further explanation or assistance to FICS in relation to the current review. Should you require further clarification please contact me, David O'Reilly or David Micó on 02 9299 3022.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Richard Gilbert', is written over a vertical red line.

Richard Gilbert

**Chief Executive Officer**