

1 August 2014

Submitted by email

Dear Mr D'Argaville

Financial Ombudsman Service Proposed Terms of Reference Changes

Financial Rights Legal Centre (**Financial Rights**) and the Consumer Action Law Centre (**Consumer Action**) welcome the opportunity to comment on FOS' proposed Terms of Reference changes.

Our broad response to each of the proposals is below:

- Proposal 1: support;
- Proposal 2: support, subject to clarification on some points;
- Proposal 3: support, subject to the introduction of some safeguards;
- Proposal 4: support
- Proposal 5: no response;
- Proposal 6: support;
- Proposal 7: broadly support, though a \$5,000 cap is still inadequate, and the increase to \$5,000 should occur before the scheduled indexation in 2015;
- Proposal 8: do not support;
- Proposal 9: support, subject to some safeguards;
- Proposal 10: of the options discussed in the Proposed Changes document, we prefer option one (retaining the existing limit). However, this matter is complex and deserves more detailed consultation before a final decision is made;
- Proposal 11: support in principle. More detailed operational guidelines are required;
- Proposal 12: we have no view on jurisdiction relating to accountants. However we propose an additional change which is similar to that in proposal 12 to close a loophole in the TOR in relation to non-AFSL businesses participating in credit activities;
- Proposal 13: we believe the compensation caps are set too low and should be increased;
- Proposal 14: we do not believe there is a need to change the jurisdictional limit at this point.

About the contributors

Financial Rights Legal Centre

The Financial Rights Legal Centre (*formerly known as the Consumer Credit Legal Centre (NSW)*) is a community legal centre that specialises in helping consumer's understand and enforce their financial rights, especially low income and otherwise marginalised or vulnerable consumers. We provide free and independent financial counselling, legal advice and representation to individuals about a broad range of financial issues. Financial Rights operates the Credit & Debt Hotline, which is the first port of call for NSW consumers experiencing financial difficulties. We also operate the Insurance Law Service which provides advice nationally to consumers about insurance claims and debts to insurance companies. Financial Rights took over 22,000 calls for advice or assistance during the 2013/2014 financial year.

Financial Rights also conducts research and collect data from our extensive contact with consumers and the legal consumer protection framework to lobby for changes to law and industry practice for the benefit of consumers. We also provide extensive web-based resources, other education resources, workshops, presentations and media comment.

Consumer Action Law Centre

Consumer Action is an independent, not-for-profit, campaign-focused casework and policy organisation. Consumer Action offers free legal advice, pursues consumer litigation and provides financial counselling to vulnerable and disadvantaged consumers across Victoria. Consumer Action is also a nationally-recognised and influential policy and research body, pursuing a law reform agenda across a range of important consumer issues at a governmental level, in the media, and in the community directly.

General remarks regarding Operational Guidelines

The consultation paper notes that operational guidelines will be drawn up for many of the proposals. These operational guidelines will have significant impact on how these proposals work in practice. The views expressed in this submission are based on the consultation materials provided, including the proposed operational guidelines, and changes to those guidelines may lead us to change our views. We ask that FOS conduct a further round of consultation if it makes any substantive changes to the draft operational guidelines.

1. Streamlined process for simpler, low value disputes

Overall we support this proposal. Consumer advocates have been very concerned with dispute resolution delays in the last few years, and hopefully this new process will help FOS produce quicker and more streamlined decisions.

However, we note that the new role of the Adjudicator seems to signal the creation of a new and separate version of dispute resolution and it will need to be closely monitored and thoroughly reviewed before the use of the Adjudicator is expanded to too many disputes. This new process should be limited and restricted to appropriate categories of disputes until the following can be assured:

- decisions made by the Adjudicators are consistent with decisions made and outcomes achieved through FOS ombudsman and panel processes;
- the Adjudicators have sufficient expertise, comparable with other FOS decision-makers (panel and ombudsman);
- an appeal process to the Ombudsman or panel is available in limited circumstances; and
- procedural fairness standards are adhered to.

There also must be clear guidance to consumers about how this new streamlined process is going to work, what consumers need to address in their arguments, and what documents they will need to produce for the Adjudicator. We expect that this proposal will be informed by FOS's recent experience with a streamlined process for low value credit reporting disputes, and we would also want to see a plan for how the Adjudicators' decision-making is going to be reviewed in the short and long-term.

2. One-step lodgement and referral process

Consumer advocates have long been concerned with access to EDR being as easy as possible. Currently FOS has two streams for entry:

1. Those disputants who do not state they have been to IDR; and
2. Those disputants who state they have been to IDR and have got a response they are dissatisfied with or no response within 45 days (with financial hardship as an exception)

Those consumers who do not indicate they have been to IDR are at risk of falling out of the FOS process when redirected to IDR because they must take action to return to FOS otherwise their case is closed. We have long been concerned that this process makes access hard for consumers (particularly disadvantaged consumers). We were also concerned that many consumers indicated that they had not been to IDR simply because they did not know the exact date they went.

We are encouraged to see a proposed TOR change that will produce a more streamlined and fair lodgement process. In particular, if consumers must go through the IDR process again, it is essential that the dispute has been registered and jurisdiction checked so it can be streamlined into a decision making process after an IDR response is received from the FSP.

Consumer advocates support this proposal as long as, in practice, all applicants are treated as officially lodged with FOS at the point of application, whether they have been through IDR or not. Applicants who have already been through the IDR process will have the opportunity to communicate with IDR once more (usually at a more senior IDR level). Applicants that have not been through IDR will get the chance to resolve their dispute with the FSP while still lodged in FOS, reducing the risk of them dropping out of the FOS process.

Our most important issue (which we hope will be confirmed through this consultation process) is that consumers become officially lodged, and stay lodged in FOS from the beginning, protecting them from any subsequent enforcement action by the FSP.

3. Outside Terms of Reference (OTOR) objection timeframes

We have no concerns with this proposal, however FOS should put the following in place to ensure the reforms operate fairly.

Longer timeframes for complex disputes

Operational guidelines should explicitly state that applicants have 30 days to object to OTOR assessments where the assessment is complex or arguable. This provides balance to the instruction in the proposed guidelines that shorter timeframes will apply to less complex cases.

Monitoring for fairness

Whatever changes are made to the OTOR timelines, FOS must continue to ensure that changes do not prevent applicants from objecting to OTOR assessments in practice. FOS should monitor and report on:

- how many OTOR assessments are made;
- on which grounds they are made;

- how many OTOR assessments receive objections; and
- how many objections are successful.

This will help FOS and its stakeholders ensure that reduced timelines for objections are not compromising fairness.

4. Small Business Credit Disputes

Consumer advocates support this proposal. We support effective limitations on high value small business credit disputes, or disputes that raise complex issues that would be more appropriately dealt with in the courts.

We agree with FOS that the \$2 million cap will provide greater consistency and transparency compared with a discretionary exclusion. However, we believe the \$2 million cap should be indexed to ensure it remains adequate.

5. Traditional Trustee Company Service disputes

No response.

6. Small Business Insurance Disputes

Consumer advocates support the proposal to return the scope of its small business general insurance broking jurisdiction to pre-2010 levels, to expand its jurisdiction in this area to include loss of profits and business interruption insurance, and to allow FOS to consider disputes about an excluded category of small business insurance in exceptional circumstances.

7. Uninsured third party motor vehicle disputes

Consumer advocates support this proposal and we note that it is long overdue. Although we are pleased to see the TOR expanded to allow FOS to consider a dispute even if the insured driver who caused the damage has failed to pay the excess and to increase the maximum award FOS can make in these disputes to \$5,000. We submit that \$5000 is still too low and the 2015 indexation should apply to the increased amount.

In our joint submission to the 2013 FOS Review consumer advocates recommended increasing the threshold to \$15,000. We recognise that this would be a much larger increase than the proposed compensation cap but we continue to submit that even a \$5,000 compensation limit is too low at a time when the cost of car repair is steadily increasing. Additionally, waiting until 2018 for the next increase will mean the indexation is even further out of step with the reality of car repair costs.

8. Disputes involving rating factors

Consumer advocates find the recommendation of the reviewer to expand the exclusion in 5.1(e) is not reasoned and strongly disagree with the proposal whose only effect is in our view designed to exclude more disputes. This recommendation was not discussed with consumer representatives as part of the independent review, nor were our views canvassed. Without reasons, examples, or some context consumer advocates reject the proposed limitation.

Currently FOS offers the only redress for consumers with premium or excess pricing issues, but under the current TOR it is very narrowly defined as set out in 5.1(b), (d), (e) and (f).

FOS jurisdiction about premium pricing is limited to where premiums are incorrectly applied (5.1(b)) or insurance is refused and the decision was “indiscriminate”, “malicious” or based on incorrect information (5.1(f)). Under section 75 of the Insurance Contract Act insurers are obligated to provide a statement of written reasons where they do not accept an offer to enter into a contract of insurance, cancel a contract of insurance, refuses to renew or due to a special risk over insurance on less advantageous terms. The Act provides some redress for an insurer to be obligated to provide reasons for decisions. In our view, consumers are unaware of this right, rarely use it, and due to its lack of specificity it has little utility in disputes over pricing and coverage. Consumers need access to FOS and its jurisdiction for help with premium pricing and insurance coverage rejections.

Through the Insurance Law Service, the Financial Rights Legal Centre regularly receives complaints from consumers about the level of their premium. This includes consumers believing that the premium is incorrectly calculated given their claims history, or on incorrect information used. From our experience, consumers who dispute their premium pricing or excess pricing with the insurer are generally left feeling unsatisfied. We are told:

- a) the sales team cannot explain why the premium is priced as it is;
- b) they are provided generic answers; or
- c) they do not feel the insurer has taken any steps to look at their particular issue.

This in our view is detrimental to the insurance industry, and it does not foster transparency or accountability.

The general insurance industry is increasingly using more granular data and factors to price products. Home and contents insurance is priced on specific localised data, and equally in motor vehicle insurance more and more “big data” findings are informing insurers about risk and price. In our view the more granular the insurer becomes in the assessment of its risk, the higher the chances of error or misapplication.

Introducing further exclusions to shield the insurance industry from providing relevant information on the grounds that there are using ‘commercially sensitive’ rating factors and weightings would remove consumers’ only means of access to justice when they have a legitimate dispute about the reasons behind a premium or excess price or the policy conditions as applied to their insurance. For example, under the expanded TOR there would be no dispute resolution for a consumer notwithstanding the consumer’s insurance policy may:

- be offered with a premium the consumer believes to be unreasonable due to inappropriate assessment of risk; or

- have complex terms and conditions the consumer cannot understand and, as a consequence, the consumer finds they have an inappropriate policy.

Case study

Sandy lives in a cyclone prone area and was affected by a cyclone in 2008. Her local council has undertaken extensive mapping about the flood risks in her local area. She was zoned in a low risk area, but other parts of her suburb were high risk. Sandy also made renovations to her home after the last cyclone, increasing and strengthening the footings. Her builder told her she was now “cyclone rated”.

Her insurance was due for renewal, and she got a shock when she was informed that the insurer was declining to reinsure her due to her high risk. She rang the insurer and told them about the renovations in 2008 and that she was classified in a low risk zone. They said they were not going to change their mind. Sandy rang around and could not find insurance.

Sandy was able to escalate her dispute and she raised a dispute in internal dispute resolution about her insurance, she mentioned the renovations and her local councils mapping data. The Insurer agreed to change their decision and offered her a renewal of her policy.

Had Sandy’s insurance refused to reconsider their decision to renew her policy she would have no other recourse to challenge the rating factors and weightings used by the Insurer to determine her insurability.

In its recent publication entitled “Enhancing the consumer experience of home insurance: Shining a light into the black box”¹ the Fire Services Levy Monitor (**FSLM**) reasoned that by improving the efficiency of insurance markets, through removing information asymmetry and making competition more effective, policyholders will be better informed and premiums will fall, thereby making insurance more accessible. In order to achieve this goal and to improve consumer awareness the FSLM specifically recommended that FOS:

Provide easier access to information and dispute resolution – by removing hurdles to information provision by insurers and dispute resolution by the Financial Ombudsman Service, consumers are less likely to be disadvantaged by opaque risk rating practices of insurers.²

The FSLM report argues there is a need for greater contestability of premium pricing and cost pricing. FOS should be assisting consumers by providing access to more transparency in these areas, not less.

9. Disputes lodged by agents charging a fee for service

We support the proposal at paragraph 9.1 of the discussion paper to enable FOS to refuse to accept disputes which are brought on behalf of an applicant by fee-for-service agents, subject to the following safeguards:

Clear exclusions for financial counsellors and CLCs

¹ Fire Services Levy Monitor, “Enhancing the consumer experience of home insurance - Shining a light into the black box” (July 2014) Available at:

<http://www.firelevymonitor.vic.gov.au/home/news+and+information/publications/publication+shining+a+light>

² Id. At page xiii

The Terms of Reference should be explicit that financial counsellors and solicitors from community legal centres are not intended to be captured by this provision. The proposed drafting of 6.1(d) is already relatively clear that it does not apply to financial counsellors and CLC's (because it specifies that the power to decline applications only extends to where an agent 'may receive any remuneration') however, it should be put beyond any doubt.

Assistance to applicants affected

The Terms of Reference should provide that, where FOS declines to accept an application on these grounds, FOS will invite the applicant to re-apply on their own behalf, or refer them to a free service that can assist. We refer to COSL's proposed response to fee-for-service agents which includes this safeguard.

Monitoring and reporting

FOS should collect and report data on the number of applications it receives where applicants have received assistance from fee-for-service providers, the numbers of applications declined on these grounds and the common reasons for declining. This will assist FOS and its stakeholders to understand and monitor the volume of these applications, and whether this proposed response is helping to limit problematic use of FOS by fee-for-service agents.

Further action

We note that COSL is currently consulting on a change to its guidelines to restrict access to paid representatives, such as credit repair businesses. In our view, COSL's approach is preferable to FOS's proposed approach as it targets a business model which has demonstrated consumer harm. While in some cases credit repair and other paid representatives may lodge claims with merit, in general, these businesses charge exorbitant fees and impose onerous terms and conditions (and, in fact, many complaints appear not to be meritorious). The benefit of lodging a complaint is outweighed by the cost imposed by these businesses.

We note that some similar businesses do not actually represent consumers in disputes lodged with EDR schemes, but instead provide consumers with information to lodge their own complaint. In our experience, this approach involves similar consumer harm as there is very limited (if any) assessment of the merit of the complaint, and consumers are charged significant fees without being informed of their right to make a complaint to EDR free of charge. It appears to us that neither the approach proposed by FOS or COSL will deal with this scenario and, in fact, the proposed changes may provide incentives for businesses to act in this manner. That is, these businesses will "do less" for their services and only instruct consumers to make complaints. Consumers, unaware of their broader rights and often driven by financial desperation, will continue to enter into such arrangements.

For this reason, we submit that there needs to be further regulation of such businesses, and encourage EDR schemes to advocate for such regulatory reform (this should also ensure such businesses are within EDR jurisdiction, an issue which is referred to at item 12 below). One model for regulatory reform is that proposed by law academics at University of Melbourne who have closely reviewed the credit repair business model³

³ See summary of report by Associate Professor Paul Ali, Lucinda O'Brien and Professor Ian Ramsay, *A quick fix? Credit repair in Australia*, available at: <http://consumeraction.org.au/report-a-quick-fix-credit-repair-in-australia-summary-of-findings/>. Full report, forthcoming.

10. Jurisdiction over income stream insurance claims disputes

Of the options discussed in the Proposed Changes document, we prefer option one (retaining the existing limit). However, this matter is complex and deserves more detailed consultation before a final decision is made.

We support option one at this stage because this option:

- is the most logical approach: it caps FOS's jurisdiction based on the amount actually in dispute, that is the 'amount of disputed arrears or past benefits potentially refundable'. In our view, the maximum monthly benefit payable under the policy is an arbitrary approach to determining jurisdiction, as it may have little bearing on the size or nature of the dispute;
- appears least likely to exclude consumers from FOS' jurisdiction. FOS, along with other industry EDR schemes, exist to provide access to justice in circumstances where consumers would otherwise struggle to access dispute resolution. We should be very wary of amending the Terms of Reference in a way that restricts access by consumers to FOS. We do note, however, that option one may exclude consumers who delay bringing their dispute if delay pushes the amount in dispute above jurisdictional limit;
- is the simplest of the three options proposed.

We do not support option two. This option would also exclude consumers that would be expected to be retail clients and should have access to FOS (anyone earning over \$120,000 per annum, according to the Proposed Changes document). This option also introduces complexity and a level of arbitrariness to FOS' jurisdiction. For similar reasons, we do not support option three, though it is preferable to option two.

We would not support any option which deemed projected future benefits as part of the amount in dispute, as this would exclude large numbers of consumers based on speculative projections of what a policy may pay in future.

11. Discretion to allow sale of an asset

This proposal (to provide FOS the discretion to allow FSPs to sell an asset) is supported in principle. However, we are unable to provide full support until we see final guidelines determining how the discretion will operate in practice, and until those guidelines provide more detail concerning exercise of the discretion to allow the sale of key assets.

Page 14 of the consultation paper says that it is 'highly unlikely that FOS will allow the sale of a primary place of residence while a dispute is open with us'. We do not believe that it will ever be appropriate for FOS to allow the sale of a primary place of residence while a dispute is open, except where both parties consent. We recommend that the Terms of Reference (or at a minimum, the Operational Guidelines) should state that FOS does not have the discretion to allow sale of a primary place of residence while the dispute remains open.

FOS should also give detailed guidelines for the discretion to allow the sale of a car where:

- it is the only car owned by the debtor or their family, and the car is essential for the debtor / family to meet work or family commitments; and
- it is arguable that the car has been illegally repossessed. If repossession has been made illegally, the appropriate remedy is immediate return of the car, and any storage costs are irrelevant as they are not enforceable against the applicant.

12. Accountants Joining FOS

Consumer advocates do not have a view on how FOS might best define the scope of its jurisdiction over disputes relating to accountants. However, we would like to submit a proposal for a change of TOR that is very closely related to the changes FOS is intending to make in relation to accountants joining FOS.

Consumer advocates believe there is a loophole in FOS TOR in relation to non-AFSL businesses participating in credit activities (such as personal budgeting services, credit negotiators, etc.) FOS sets out its jurisdiction based on the FSP definition which is worded same as Corporations Act and AFSL legislation.

Consumer advocates submit that it is just a matter of time before a consumer dispute motivates one of these credit activity providers which does not have an AFSL to drop out of FOS (because there is no legislative requirement that they be a member) or claim that in fact FOS has no jurisdiction over its activities.

Consumer advocates strongly submit that if the TOR can be modified to include accountants, than it can be modified to fix this impending problem.

Under the FOS terms of Reference:

4.1 Eligibility to lodge a Dispute with FOS

FOS may only consider a Dispute if the Dispute is between a Financial Services Provider and an individual or individuals (including those acting as a trustee, legal personal representative or otherwise).

A “Financial Services Provider” is defined in the TOR as relevantly a provider of a Financial Service that is a Member. Whilst some personal budgeting services are currently members of FOS, they are not a Financial Service Provider within the meaning of the TOR as:

“Financial Service” means a product or service that:

- a) *is financial in nature including a product or service which is or is in connection with:*
 - (i) *a loan or any other kind of credit transaction (including a credit card used overseas) and guarantees or charges to secure any moneys owing;*
 - (ii) *a deposit including a term deposit, a fund management deposit or a retirement savings account;*
 - (iii) *an insurance policy;*

- (iv) a financial investment (such as life insurance, a security or an interest in a registered managed investment scheme or a superannuation fund);
- (v) a facility under which a person seeks to manage financial risk or to avoid or limit the financial consequences of fluctuations in, or in the value of, an asset, receipts or costs (such as a derivatives contract or a foreign currency contract);
- (vi) a facility under which a person may make, or cause to be made, a non-cash payment (such as a direct debit arrangement or a facility relating to cheques, bills of exchange, travellers cheques or a stored value card);
- (vii) leasing and hire purchase arrangements; or
- (viii) financial or investment advice; or
- (ix) Traditional Trustee Company Services; or

b) is a custodial service.

The definition of “Financial Service” is analogous to the definition of an Australian Financial Services licensee not a Credit License for “credit activities”.

What this means is whilst some credit activity businesses have a credit license their activities are not covered in the FOS TOR as a financial service provider. Accordingly, FOS’s jurisdiction may be challenged by these businesses as soon as they are faced with an inconvenient consumer dispute or FOS itself may find it does not have jurisdiction.

We recommend including a sub point (x) to make it abundantly clear that members who provide services include activities to repair the credit report of an individual, credit activities including debt negotiation and budgeting services.

13. Indexation of compensation caps

We do not agree with the assessment in the consultation paper that there is no need to increase the compensation caps. We agree with the Senate Economics References Committee that the compensation caps are set at too low⁴ and should be increased. The \$280,000 cap, for example, means that many applicants challenging an insurer's decision following total loss of their home in a natural disaster will not be able to be completely compensated for their loss.

As the discussion paper notes, the compensation caps will be indexed on 1 January 2015 in line with Term of Reference 9.8. However, this will only index the caps from one inadequate amount to another inadequate amount. The compensation caps must be increased to an adequate amount and then indexed in line with ToR 9.8 to ensure they remain adequate.

14. Indexation of jurisdictional limit

We do not believe there is any requirement to change the jurisdictional limit at this stage.

⁴ Senate Economics Committee, *Performance of the Australian Securities and Investments Commission*, June 2014, Final Report paragraphs 7.80, 7.83.

Concluding Remarks

Thank you again for the opportunity to comment on the Proposed Terms of Reference changes. If you have any questions or concerns regarding this submission please do not hesitate to contact the Financial Rights Legal Centre on (02) 9212 4216.

Kind Regards,



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