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The Treasury

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**Submission on the consultation paper ‘Improving dispute resolution in the financial system’ and accompanying draft legislation and regulations.**

To whom it may concern,

As noted in our previous submissions to the Ramsay Review, the Australian Retail Credit Association (ARCA) supports a robust, efficient, and transparent complaints and dispute resolution framework in the financial system. We support internal dispute resolution (IDR) as a primary forum for dispute resolution, as well as easy access to external dispute resolution (EDR) where necessary.

ARCA is the peak industry body for organisations involved in Australia’s retail credit risk sector, and was established to promote common standards of best practice in credit risk assessment and responsible lending and to ensure an effective credit reporting system. Membership to ARCA is voluntary and includes nearly all significant banks, consumer credit providers, many key finance companies, and all major Australian credit reporting bodies (CRBs). As participants in the financial services industry and consumer credit reporting system, ARCA Members are currently all members of either the Financial Ombudsman Service (FOS) or the Credit Investments Ombudsman (CIO).

In our submissions to the Ramsay Review, ARCA noted that it did not support a single EDR scheme. We remain concerned that a single EDR scheme structure has the potential to lead to lower levels of accountability and effectiveness. However, given that government has accepted the Ramsay Review recommendations in this regard and announced its intention to proceed with a single EDR scheme structure, the focus of this submission is on those factors and issues considered to be essential for the effective and accountable operation of the intended “one stop shop”.

The key weakness of current EDR decision-making is its uncertainty and inconsistency. The impact of this cannot be understated as the cost of compliance arising from the current EDR decision-making is significant. Many credit providers are reluctant to disclose credit information to CRBs because of concerns that an adverse EDR decision, based at times on a misinterpretation of law, could force that credit provider to re-configure its credit reporting systems, or remove large amounts of credit information from the credit reporting system.

The credit reporting provisions in Part IIIA of the Privacy Act 1988 (Privacy Act), the Privacy Regulation 2013 and the Privacy (Credit Reporting) Code 2014 (CR Code) put in place a set of highly prescriptive and detailed compliance requirements for both credit providers and credit reporting bodies. ARCA, as Code Drafter of the CR Code, spent considerable time consulting with industry, consumer groups, EDR schemes and a range of impacted organisations to ensure the CR Code gave operational effect to the Privacy Act provisions.

For background, FOS determinations issued by Ombudsmen are binding on credit providers and credit reporting bodies. The bulk of decisions made by EDR schemes will be Recommendations (which are not currently available for review). Although Recommendations will not bind the credit providers and CRBs, they will often be accepted for commercial reasons (i.e. avoiding incurring the higher EDR fees associated with the issue of Determinations).

Following a review of FOS determinations database, ARCA has found examples where EDR schemes:

* **Fail to apply the current Privacy Act provisions**. For instance, two default listing determinations issued by FOS over a year after commencement of the new Part IIIA (case numbers 377369 and 362597) applied the pre-2014 Privacy Act requirements. This meant that critical changes to the default listing process, such as the requirement for two notices to be issued, was ignored in these determinations.
* **Evidence a lack of knowledge or understanding of the provisions of the CR Code.** In fact, the Determinations issued by FOS rarely reference the CR Code. Yet, a breach of the CR Code has the same effect as a breach of the Privacy Act, and the CR Code contains significant operative provisions, particularly concerning default listings (which appear to form the bulk of EDR credit listing disputes).

An example of how omitting reference to the CR Code results in incorrect decisions occurred in FOS determination (case number 440247) which relied only on the Privacy Act requirements for *giving* a second notice *before* default listing. By contrast, paragraph 9.3 of the CR Code clearly stipulates that a second notice should be *issued* at least 14 days prior to disclosure of default information. The result was that the determination effectively created a new requirement for a credit provider to allow sufficient time for an individual to receive a notice before default listing. The extra time period required by FOS was four days, which then meant the default listing (which was otherwise issued in the proper time under the CR Code) was deemed to have been made too early, and had to be removed. In considering this determination, it should be emphasised that the use of the word ‘issue’ in the CR Code was deliberate and the result of extensive consultation and an understanding as to the correct process for default listing. Yet this binding FOS determination did not even reference this requirement.

* **At times, fundamentally misunderstand comprehensive credit reporting (CCR) and its operation**. This is particularly worrying given that, if CCR becomes mandatory, there will be a significant influx of CCR data within the credit reporting system, and a resultant increase in disputes referred to EDR by consumers.

Illustrating this point, in one of the very few determinations to consider the entry of consumer credit liability information (CCLI) on a credit report, FOS awarded the applicant $1,000 for stress and embarrassment arising from the credit provider being named (on the CCLI entry) as ‘[FSP] Credit Risk’ rather than ‘[FSP] Credit Services’ (case number 381344). In awarding compensation, FOS considered that it may adversely impact on the applicant to have an entry of CCLI with the words ‘credit risk’.

For background, CCLI is information about an individual’s credit account, including the name of the credit provider, the type of account, the limit of the account, any repayment terms and conditions, the date it was opened and closed. It provides valuable information about an individual’s current credit accounts. Considered in this context, the actual name of a credit provider as part of a CCLI entry is inconsequential. It would certainly not be a reason for credit to be declined to an individual (instead, that individual’s actual credit position apparent from the other CCLI data is likely to be far more relevant to this assessment). It is of great concern that, in making this determination, FOS would not seek to understand how CCLI data operates in the context of a credit assessment, nor to test its assumption that a compensable loss could arise due to the name of a credit provider.

* **Apply judgements of fairness to require the removal of credit information, even though the credit provider has complied with its obligations under the Privacy Act and CR Code**. For instance, a number of FOS Determinations have required the removal of default listings where individuals have “substantially complied” with payment arrangements – but the credit provider has still exercised its right to default list (having issued proper notices and met its legal obligations). (See case numbers 431664, 427429, 431024, and 437163). FOS has also relied on fairness to import new obligations for credit providers seeking to default list. In one case, this required a default notice to be sent to an alternative address (rather than the ‘last known address’ which is the legal requirement) (case number 438507). In another case, FOS required that a credit provider take additional steps to obtain new contact details for an individual rather than relying on having issued a default notice to the last known address for that individual (case number 444907).
* **Apply the law inconsistently to similar factual and legal scenarios**. An example of this concerns FOS’s approach to default listings entered for a loan determined to have been advanced as a result of irresponsible lending. In one case it was determined that, although loan funds should not have been advanced, because the credit provider complied with the legal obligations for disclosing default information, that information could remain on the individual’s credit file (case number 446052). Yet in another case, in a similar fact scenario it was determined the appropriate outcome was for the default listing to be removed from the individual’s file given that if the loan had not been granted, the default listing would never have been made (case number 426165).

What is most concerning about these decision-making practices, is the impact this will then have on both industry and consumers. These practices create uncertainty. In turn, they undermine the effective operation of the credit reporting system.

Moreover, these practices are entirely unnecessary. EDR schemes should be required to adhere to standards of high quality and consistency in their decision-making, be expected to know and apply the correct law, ensure all decision-making staff are educated in the operation of the Privacy Act and CR Code, promote consistency in decision-making and, above all, enable an affordable straight-forward appeal process for credit providers and credit reporting bodies.

While the Privacy Act is relatively clear, as highlighted above, ARCA has found that EDR schemes regularly depart from the legislation to apply more nebulous and flexible concepts of fairness and best practice in decision making on credit data. We note that the existing EDR schemes’ terms of reference allow decision makers to consider fairness and industry practice as well as legal principles. However it is fundamental to sound administrative decision making, procedural fairness and the value of EDR determinations to improved industry practice and consumer outcomes, that EDR determinations clearly articulate the legal principles, fairness and industry practice that were considered in each decision and the weight afforded to each factor in reaching an outcome. We note the Operational Guidelines to FOS’s terms of reference also state that:

*“FOS takes the approach that it should identify relevant legal principles and take these into account in its consideration of a Dispute…. This does not mean FOS must strictly apply the legal principles. However, FOS will consider these when handling a Dispute and if it is necessary to deviate from those principles to achieve fairness in the circumstances, it will identify its reasons for doing so”.*

We are concerned that in setting this approach, FOS departs from the application of legislation and legal principles on subjective grounds of fairness with no express reasons for doing so.

These deviations from the law give rise to EDR findings which create uncertainty and see the removal of legally valid data from the CRB and see compensation amounts awarded against credit providers. In some instances, systemic issues arising from these findings have seen the removal of valid data relating to many thousands of customers by a single credit provider.

This has resulted in a situation where, despite the clear deadlines regarding CCR set in Recommendation 5.5 of the Productivity Commission Inquiry and accepted by the Treasurer, Credit Providers who are otherwise technically ready to do so, are still extremely reluctant to commence public reporting of comprehensive credit reporting, as a direct result of these issues.

At a time when the government is looking to enhanced data sharing to level the playing field in financial services and promote more vigorous competition to the benefit of all Australians, ARCA is concerned that, in moving from a two-scheme model to a single scheme in the form of the intended Australian Financial Complaints Authority (AFCA), these existing problems must be addressed or they will be exacerbated. ARCA considers the following key principles must be entrenched within the new EDR framework.

Decisions should not be contrary to the law

The controls which apply to superannuation complaints within the proposed legislation should be expanded to apply to all disputes. In particular, proposed *Section 1057(3)* requiring that all decisions regarding superannuation disputes must not be contrary to the law should be extended to all disputes regardless of whether related to superannuation or not.

EDR determinations are binding upon industry. Where such determinations are made, as the examples provided show, decisions that are made without reference to the law or without accurate and appropriate interpretation of the law, have a significant impact.

In the first instance, it is impossible for industry to operate effectively and consistently in an environment where the rules are unclear or where determinations depart from the law. Furthermore, where there is scope for determinations to be contrary to law, this leaves industry in an impossible situation – should one comply with the EDR determination, as required by the terms of reference of the EDR scheme but be in breach of other legislation; or not comply with the EDR determination in order to comply with other prevailing legislation and thus be in breach of their respective EDR terms of reference. Clearly this cannot be considered an acceptable outcome.

Secondly, where determinations are binding and are not in accordance with law, this has the unintended consequence of empowering EDR schemes with policy making powers that should remain the sole province of the Parliament. Before becoming law, proposed legislation will almost certainly go through a thorough public consultation process, the scrutiny of both Houses of Parliament, and will then require Royal Assent. It should not be within the powers of an EDR scheme to bypass that rigour.

Therefore, ARCA urges the government to extend the requirement that EDR decisions are made in accordance with the law to cover all EDR complaints and not simply those relating to superannuation.

Decisions should be subject to a right of review or appeal

ARCA further notes that proposed *Section 1056* which provides for appeal to the Federal Court on questions of law regarding superannuation disputes should be extended to all disputes.

Furthermore, given the costs and time delays inherent in matters taken before Federal Court, this should not be the only avenue whereby EDR decisions may be challenged on a point of law. ARCA believes that there should be a simpler and more accessible mechanism to review EDR decisions on questions of law and that this mechanism should not rely on an internal review by the EDR scheme itself but should provide for review by an appropriate external body, regulator and/or ‘eminent person’.

Therefore, ARCA urges that recourse to the Federal Court should not be the only mechanism available to either industry or consumers where there are questions of law in dispute. By way of example, the Financial Ombudsman Service (FOS) took a view on how Repayment History Information (RHI) should be interpreted and reported when an informal payment arrangement that is not a contract variation is in effect. ARCA and industry considered that FOS had erred at law in that it misinterpreted the Privacy Act. However because there is no appeal right for individual EDR determinations that do not satisfy the Wednesbury test for unreasonableness[[1]](#footnote-1), industry’s only recourse was to request the Information Commissioner’s view on how RHI should be interpreted and reported under the Privacy Act. After a thorough review of the FOS position, the OAIC confirmed a view that aligned with that of ARCA regarding how RHI should be interpreted and reported.

In this instance, clarifying the correct interpretation of the law took nearly a year and in the meantime, the FOS view became the main impediment to progressing with the implementation of comprehensive credit reporting. Even more concerning is the fact that the Information Commissioner’s view can only clarify future interpretation of the relevant legislation; the Information Commissioner does not have oversight or power to overrule individual FOS determinations such as the initial determination on this issue. This clearly demonstrates the need for an effective and appropriate avenue to appeal individual EDR determinations - this would have the additional benefit of ensuring a higher level of accountability and quality assurance of EDR decision making.

The recommendations outlined above would significantly enhance the certainty of the EDR system and promote a more competitive financial system, which would be to the benefit of all consumers. Furthermore, it would be confusing to have different decision-making principles applicable to superannuation and non-superannuation matters within a single "one-stop-shop" EDR scheme. To the extent that different types of disputes are subject to different principles and processes there cannot really be a "one-stop-shop" at all.

In summary, there is a need to make a number of amendments to the operating framework for the new EDR scheme. Such a framework should include clearer guidelines and practices. All EDR schemes should be guided by the application of the law, in the interests of procedural fairness and consistency. We see this as the only reasonable approach available to ensure compliance and effective operation by any scheme participants.

One final point relates to the proposed name of the new EDR scheme. ARCA notes that Consumer Advocates have raised a valid concern regarding the use of the word “Authority” in the scheme title. This word carries highly authoritarian and intimidating connotations which may serve to detract from the perceived accessibility of the scheme to the detriment of consumers. We would like to suggest that the term “Ombud” is one which conveys not only an exactly appropriate and accurate meaning but also conveys a sense of trust and confidence and is therefore preferable to the term “Authority”.

Once again, thank you for the invitation to make a submission on the consultation paper. Feel free to contact me directly if I can provide further information on 03 9863 7859 or kjenkins@arca.asn.au.

Yours sincerely

Kim Jenkins

**Chief Executive Officer**

ARCA recommendations to the consultation process:

1. Extend requirements that EDR decisions should not be contrary to the law to encompass all disputes brought before the EDR scheme and not solely superannuation complaints.
2. Ensure that the provision that EDR determinations are subject to appeal on questions of law is extended to all complaints, and not solely superannuation complaints, and that an appropriate and effective appeal mechanism is implemented that does not rely solely on recourse to the Federal Court.
3. Ensure that all EDR determinations are appropriately documented in all instances and make clear the reasons for the determination, including outlining the applicable points of law.
4. Require decision-making employees of the EDR scheme to be trained in the requirements of the Privacy Act and the CR Code (in the same manner as paragraph 2.2 of the CR Code currently requires all credit provider and credit reporting body employees who handle credit-related personal information to undertake education and training in the credit reporting system).
5. Reconsider the use of the word “Authority” in the name of the scheme in favour of a less imposing word that more accurately reflects the nature of the EDR process.
1. Associated Provincial Picture Houses Ltd v Wednesbury Corporation [1948] 1 KB 223 [↑](#footnote-ref-1)