

Head of Secretariat
AFCA Transition Team
Financial Services Unit
The Treasury
Langton Crescent
PARKES ACT 2600

20th November 2017

Via email: afca@treasury.gov.au

Dear Sir/Madam,

The FBAA as the leading national professional association to finance and mortgage brokers, welcomes the opportunity to make a submission in response to the November 2017 Consultation Paper on the Establishment of the Australian Financial Complaints Authority.

PART 1 - TERMS OF REFERENCE

QUESTION FOR DISCUSSION

1. Are there any other principles that should be included in the guiding principles for AFCA's establishment?

FBAA Response

The guiding principles that are currently expressed are:

Compliance – with statutory requirements, Ramsay Review recommendations, any guidance the Minister gives on the requirements for a scheme to be authorised and ASIC regulatory requirements.

Incorporation of better practice principles for dispute resolution – including reflecting ASIC requirements on EDR, ensuring accessibility of the AFCA scheme and ensuring that the coverage and consumer rights under the AFCA scheme are not less than those currently applying under the various EDR schemes.

Adoption of what's working – effective and well-established dispute resolution processes and practices should be incorporated in arrangements for the new body – there should be no 'change for change's sake'.

Efficient and effective transitional arrangements – no dispute existing on AFCA's commencement should be left behind.

We support these principles.

Care must be taken when referencing “compliance with ASIC regulatory requirements”. It is reasonable such a phrase relates to specific obligations that are prescribed in legislation, but it is not reasonable where such a phrase also extends to guidance issued by ASIC. ASIC regulatory guides are not law.

Fair treatment of members and service providers must also be a guiding principle for the new body. This is consistent with the second principle expressed above. “Better principles for dispute resolution” must involve fair treatment of all parties involved in EDR. It is important not to excessively restrict the Government’s stated purpose “to have a new ‘one stop shop’ dispute resolution body to ensure that consumers and small businesses have access to free, fast and binding dispute resolution”. Equitable treatment of all parties should remain a priority.

QUESTIONS FOR DISCUSSION**Specific monetary limits**

2. As AFCA will be a new EDR scheme, is it appropriate to maintain specific limits for:

- income stream risk disputes;
- general insurance broking disputes; and
- third-party motor vehicle insurance?

3. If these specific limits are to be retained, should there be an increase in the limits?

Impact on Professional Indemnity Insurance

4. Are there any anticipated effects on firms that will be disproportionate to any increase in specific increased monetary limits?

We make no submission in relation to the above group of questions.

QUESTIONS FOR DISCUSSION

5. What measures may assist in ensuring AFCA's decision-making processes promote consistency, while:

- deciding each case on its merits based on the facts and circumstances of the complaint; and
- maintaining the objective of achieving fairness and flexibility to adapt to changed circumstances?

6. Are there any other principles that may assist in ensuring AFCA provides fair, efficient, timely and independent decisions?

7. To what extent should these principles be reflected in the Terms of Reference, while allowing for operational flexibility?

FBAA Response

We support the measures already expressed in the CP.

Members have been critical of the speed of EDR schemes to assess the basic merits of claims, stating that schemes are slow to conclude that claims have no merit or have been brought against parties who should not be party to a dispute. Members are charged even where it is found there is no basis for the claim.

Examples include:

- Where a representative moves licensee and the complaint is made against the representative for conduct that occurred whilst at their former licensee. Schemes take considerable time to reach a decision to release a licensee from a claim – often well after a licensee has committed resources to investigating the complaint and defending their position;
- Vexatious claims where there is no merit or prospect of success;
- Claims brought for tactical reasons such as to frustrate valid enforcement action;
- Claims where the complainant has provided no evidence – leaving the licensee to mount a defence to a claim that is not even substantiated;
- Claims where EDR scheme staff have “redefined” the complaint to more neatly fit within existing parameters. An example of this is where a consumer complains about the quality of a financed product and the EDR scheme deems the complaint to be about the licensee's responsible lending processes.

AFCA must ensure the staff empowered to hear matters and make decisions are qualified, trained and have sufficient real-world experience on which to base their

decisions. We agree that publishing decisions and holding decisions to high standards of internal consistency will assist with this however it has been our experience that not all EDR staff appear adequately experienced to be adjudicating matters.

QUESTIONS FOR DISCUSSION

8. How should AFCA balance the advantages of using panels in certain circumstances against efficiency and service implications including cost and timeliness of its decision making?
9. Are there other factors that should be taken into account when considering whether a panel should be used?
10. How best can AFCA provide clear guidance about to users about when a panel should be used?

FBAA Response

We support the use of expert panels for complex and novel matters. The costs of using such panels should form part of the operating costs of the scheme having regard to the fact that any staff hearing and adjudicating matters should already be adequately qualified and experienced such that they are making decisions based on their deep subject matter knowledge and experience.

The Scheme should publish information about when a matter might be referred to an expert panel. We support those factors already identified including:

- the complexity of the dispute;
- the amount of loss as well as other potential consequences of the dispute;
- whether the dispute raises a systemic issue; and
- whether the dispute is likely to result in a 'new' decision that raises novel issues and may set an industry standard in a particular context.

We support the adoption of a materiality threshold for disputes which may be referred to a panel – such amount to be the subject of further discussion. For the sake of speed and efficiency it is not practical to refer disputes over minor sums to an expert panel, nor should such disputes be the basis for setting industry standards. Claims must be material before such a step is considered.

Members report a worrying approach taken by EDR schemes to potential “systemic issues”. In particular, CIO has been identified as an EDR scheme that aggressively wields the notion of “systemic” issues, essentially putting members to a reverse onus of proof where the scheme has suggested an issue will be treated as systemic unless they can satisfy the scheme that it is not. Where an entity has not committed multiple breaches, the evidence of there being no systemic issue is the fact that there is no evidence of further breaches. Requiring members to provide negative proof of non-compliance (or exhaustive proof of compliance in order to demonstrate no non-compliance) is extremely costly and time consuming. Below are several real-life examples:

Example 1

A licensee listed a consumer for a default before the 60-day period allowable under the privacy legislation. The listing was defective and the licensee agreed to remove it from the consumer’s credit file. The EDR scheme subsequently insisted the licensee prove that this was not a systemic issue – despite having no information before it that the listing error was anything more than a one-off mistake. The only evidence to support the fact that it was not a systemic error was the absence of any evidence that it had ever happened before or since. The licensee spent days compiling information about all listings and pairing them up with default notices to show the EDR scheme that it ordinarily complied with the relevant time periods before listing a consumer. The EDR scheme concluded its “systemic investigation” but charged the licensee more than \$6,000 before doing so. There was never any information to support a concern that the licensee’s error was systemic.

Example 2

A consumer advocate, on behalf of a consumer, lodged a complaint against a license alleging breaches of specific obligations under the legislation. The licensee in question was exempt from complying with the particular obligations identified in the complaint. The EDR scheme commenced a systemic breach investigation concurrently with the individual complaint. The EDR scheme was informed of the exemption at the outset yet chose to progress the systemic investigation, making a series of requests of the licensee for information over the subsequent months. The EDR scheme concluded after almost six months that the licensee was exempt and that there was no systemic contravention of the legislation. The scheme invoiced the member around \$3,500 which it

subsequently withdrew when it was directed back to the initial correspondence. The licensee incurred thousands of dollars seeking external advice and assistance to defend the allegations.

Greater controls need to be placed around when the Scheme can commence a systemic investigation and costs should follow the event. Where there is no systemic issue or fault found against the licensee / member then they should not be charged. Failure to curtail this practice may result in the Scheme using systemic investigations as a revenue raising mechanism.

QUESTION FOR DISCUSSION

11. Apart from the review of the impact of the higher compensation cap, are there other aspects of AFCA's operations that should be subject to independent review within the first three years of its commencement?

FBAA Response

Yes.

- Consistency of decision making;
- Costs levied against members for individual matters – consideration of the ratio of cost to amount in dispute;
- Outcomes of systemic investigations and a review of the basis on which they are commenced.

QUESTIONS FOR DISCUSSION

12. How and where should the charter of the independent assessor be defined? Who should be able to make a complaint to the independent assessor?
13. What safeguards should be put in place to ensure the assessor remains 'independent' (for example, should there be restrictions on early termination of the independent assessor)?
14. Should the independent assessor have guaranteed direct access to the AFCA Board?
15. What other reporting arrangements should be in place (for example, if there is serious misconduct or a systemic issue)?
16. Should the independent assessor publish their findings in each case on an anonymised basis?
17. What should happen if AFCA disagrees with the independent assessor's decision?
18. When should a review of the functions and operation of the independent assessor be undertaken?

FBAA Response

We support the role of requiring the Scheme to have an independent assessor. The charter should be a public document.

We absolutely support publication of the independent assessor's findings. If AFCA disagrees with the independent assessor's decision, then the independent assessor's decision should prevail. Licensees are bound by AFCA's decisions. AFCA should be bound by the decision of the independent assessor.

It would seem appropriate to have the functions and operation of the independent assessor reviewed after the first reporting period which is within the first three years.

QUESTIONS FOR DISCUSSION

19. Do existing exclusions from FOS and CIO jurisdictions present any unreasonable barriers to accessing the schemes?
20. Is there more that could be done so that complaints lacking substance are excluded from being dealt with by AFCA?
21. What, if any, further practices should be adopted to ensure the correct balance between accessibility to the scheme and ensuring that complaints not appropriate for consideration by an EDR scheme are excluded?

FBAA Response

We do not believe there are any material gaps in the accessibility of the schemes cause by current exclusions.

The real issue about complaints lacking substance is twofold:

1. They consume a large amount of member's time even compiling a response that is detailed enough to assist the scheme to reach a determination; and
2. The member is still charged a fee by the scheme regardless

This second point gives consumers and consumer advocates a significant lever to extort money out of members for low dollar amounts since it costs less time and money to settle minor disputes than have them heard.

We would like to see AFCA put consumers to some measure of proof before initiating a complaint against a member. Our current view is that EDR schemes are too quick to accept a complaint and commence a matter against a member and often rely on a member to produce records to assist the Scheme to formulate the consumer's complaint – or dismiss it as the case may be.

Correct apportionment of costs would be a significant step towards a more equitable scheme. We do not oppose claims that have some merit being heard by the Scheme. Costs however should more closely follow the event. Members should bear no cost for vexatious and frivolous claims. Our preference would be to see consumers (or advocates) bringing such claims bearing the costs. We understand a major imperative of EDR is for it to be a costless jurisdiction for consumers and small

business in which case the Scheme must have capacity to absorb the costs of frivolous, vexatious or incomplete claims. Members should only be charged once a valid claim is identified and is pursued by the consumer.

QUESTIONS FOR DISCUSSION

22. What requirements relating to accessibility should be included in AFCA's terms of reference?
23. Having regard to the current FOS terms of reference and CIO rules, what principles and topics are of sufficient ongoing significance that they should be addressed in the AFCA terms of reference?
24. Are there any matters not currently included in the FOS terms of reference/CIO rules that warrant inclusion in AFCA's terms of reference?

FBAA Response

Under present IDR/EDR guidance issued by ASIC, licensees are expected to provide assistance to consumers where they are unable to put their complaint in writing or where they require other assistance to fully enunciate their complaint.

While we appreciate that the Scheme cannot insist on consumers providing a written complaint, the Scheme must assist the consumer to organise their complaint and to reduce it to writing so that the other party(ies) can adequately respond. Additionally, AFCA must not coach the consumer or embellish the complaint.

PART 2 – SUPERANNUATION

The FBAA makes no submission under questions 25 – 27 that relate to superannuation.

PART 3 - GOVERNANCE

(see over)

QUESTIONS FOR DISCUSSION

28. What measures could be put in place to secure sufficient knowledge of how different parts of the industry operate, while avoiding the representative tag for directors?

29. What measures should be put in place to ensure the AFCA Board appropriately balances the considerations of currency of director knowledge of particular industry sectors, conflict of interests, and breadth of competencies required?

30. What needs to be addressed at a Board/constitution level and what can be addressed through additional governance arrangements established by AFCA such as industry sector advisory panel(s) for transition?

FBAA Response

We believe many of these issues are self-explanatory. An independent director must be exactly that. Conflicts of interest can operate in multiple directions and at multiple levels. Other members of the board should hold each director to account.

We believe the merits of having independent directors with subject matter expertise outweighs the risk of conflicts or compromise of independence.

QUESTIONS FOR DISCUSSION

31. Are there additional functions or responsibilities of the AFCA board that are not reflected in the constitutions of the existing schemes?

32. What benchmarks should AFCA have in relation to matters addressed in the ASX corporate governance principles, including:

- board renewal;
- diversity;
- procedures for assessing board performance;
- management of conflicts of interest or of duty on the part of directors and executive staff; and
- remuneration policy?

33. Should the Constitution or governing rules provide that neither the board nor individual directors can direct a decision-maker with regard to the outcomes of a particular dispute or class of disputes?

FBAA Response

We provide no response to questions 31 and 32.

We support a measure in Q33 to ensure the board and directors cannot direct a decision-maker with regard to outcomes of a particular dispute or class of disputes.

PART 4 - FUNDING

QUESTIONS FOR DISCUSSION

34. In addition to matters identified in paragraphs 1-3 above, what other material should a company seeking authorisation to operate the AFCA scheme provide to demonstrate that it has satisfied the requirements of adequate funding and sufficient funding flexibility?

35. Are there any principles beyond those identified in paragraph 2 above that should underpin AFCA's funding model?

36. Should the funding arrangements for superannuation and non-superannuation disputes be separate and distinct, given the very different nature of these disputes?

FBAA Response

It is unclear what community outreach role AFCA might play and whether this would duplicate the community outreach roles played by ASIC and other organisations. Members are already required to inform consumers of their dispute resolution rights and of their member EDR scheme through their disclosure documentation. We have reservations about AFCA needing to play an external outreach role noting that this activity would essentially be industry funded.

There is an inherent conflict with an industry funded model where the complaints scheme of which it is mandatory to be a member is funded through membership fees and a user-pays approach. This is exacerbated by the Scheme having discretion to initiate its own investigations and to charge members for embarking on such investigations regardless of the outcome.

On behalf of our members, we support a modest membership fee with the bulk of revenue being derived from a user-pays system where costs are only levied against members where a genuine case to answer is made out. The 'cost' trigger must be set around a valid issue being made out. We do not support a model that permits the scheme to charge members a fee for matters entirely outside of their control – for example where a consumer bypasses IDR and goes direct to EDR, tactical complaints or where any claim is baseless.

QUESTIONS FOR DISCUSSION

37. If an interim funding arrangement were put in place, what features should it have and when would it be appropriate to transition to a long-run funding model?
38. What special considerations might need to be factored into an interim funding model to balance the need for adequate resources (certainty) with the principles (accuracy)?

FBAA Response

Each of the three existing schemes must continue to operate their own schemes to manage run off claims. Our understanding and belief is that Government would provide interim funding for the establishment and early operation of AFCA until EDR is fully transitioned to the new scheme.

FOS and CIO are “forward funded” from membership subs. There is currently no pro-rata refund offered to members who cancel their membership part way through the year. We expect AFCA will operate on a similar basis and Government should fund the upfront establishment and transition costs of the scheme until this amount can be recovered over the course of the first few years as member renewals are collected.

QUESTIONS FOR DISCUSSION

39. Who are the key stakeholders AFCA is accountable to? What is the key objective and measure of importance to each stakeholder?
40. In addition to the accountability measures in the Bill, are there additional measures that should be embedded in AFCA's Constitution and/or terms of reference or reflected in ASIC guidance to ensure accountability to stakeholders?

FBAA Response

Key stakeholders include members, Government, consumers and industry associations. We can only speak for our own interests and that is the key objective and measure is fair and appropriate outcomes in a timely manner.

Our experience as an industry association is that we rarely receive feedback from the existing schemes regarding member conduct. We encourage more communication or information sharing between the new Scheme and industry associations.

QUESTION FOR DISCUSSION

41. Are there other conditions that could be put in place to ensure the scheme is accountable to members in relation to fees?

A fair and equitable system that only takes fees off members where it is appropriate. We would like to see members incur no cost where there is no fault. Many licensees go through their careers with no EDR disputes. It is often beyond the control of a licensee as to whether a consumer follows correct dispute resolution processes by going through IDR first or whether a consumer provides further particulars about an alleged complaint where the basis of the initial complaint is unclear or not supported by any evidence. In addition to no charges being levied for baseless or vexatious claims, members should not be charged any fee for the first complaint brought to EDR against them each year. This to some extent ameliorates the artificial leverage consumers have against members to extort a settlement amount from them on the basis that defending matter to EDR will be costly.

END.

Yours faithfully



Peter J White CPFBS FMDI MAICD
Executive Director

Advisory Board Member – Small Business Association of Australia (SBA)