

Review of the financial system external dispute resolution framework – Supplementary Issues Paper

Legal Aid NSW submission to the Treasury

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NEW SOUTH WALES

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About Legal Aid NSW

The Legal Aid Commission of New South Wales (**Legal Aid NSW**) is an independent statutory body established under the *Legal Aid Commission Act 1979* (NSW) to provide legal assistance, with a particular focus on the needs of people who are socially and economically disadvantaged.

Legal Aid NSW provides information, community legal education, advice, minor assistance and representation, through a large in-house legal practice and private practitioners. Legal Aid NSW also funds a number of services provided by non-government organisations, including 32 community legal centres and 28 Women's Domestic Violence Court Advocacy Services.

Legal Aid NSW welcomes the opportunity to provide a submission to the Treasury's *Review of the financial system external dispute resolution* Supplementary Issues Paper about the establishment of a compensation scheme of last resort, and providing access to redress for past disputes.

The Legal Aid NSW Civil Law Division focuses on legal problems that impact most on disadvantaged communities, such as credit, debt, housing, employment, social security and access to essential social services. Consumer issues constitute the largest category of service for our Civil Law Division.

In 2014-15 Legal Aid NSW provided 4,887 in house advice and 5,477 minor

assistance services in consumer law matters. More than one quarter of these matters dealt with credit products, including consumer leases. This submission draws on the casework experience of civil law solicitors in providing these services.

This submission addresses the questions in the Supplementary Issues Paper. In responding to these questions, we also refer to our previous submissions made in October 2016 and January 2017 to the Review. We follow the numbering of the questions in the Supplementary Issues Paper in our submission.

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Introduction

Legal Aid NSW supports the proposal to establish a compensation scheme of last resort. We consider that the model proposed by the Financial Ombudsman Scheme (**FOS**) should be adopted, provided that it applies to all unpaid determinations (external dispute resolution (**EDR**) determinations, and court and tribunal decisions). It should be accessible to both individuals and small businesses, and cover all financial services claims, not only financial advice. Compensation should be paid to consumers as quickly as possible, up to the limits of the EDR scheme (if relevant). Compensation should be available for both legacy and future unpaid determinations.

In our view, the scheme will reduce the number of unpaid determinations, promote fair treatment of consumers and build confidence in the financial system. It should be introduced alongside better regulation and oversight of professional indemnity insurance and stronger obligations on firms to have adequate compensation arrangements in place. These measures will ensure that the scheme is sustainable and is not overwhelmed by claims.

Legal Aid NSW supports the Government's consideration of a process for consumers to access redress for past disputes. The process should be available where a financial services consumer has attempted to access redress but has been unsuccessful within the prescribed EDR timeframe due to the conduct of the firm. This may include circumstances where the firm is insolvent or not a member of an EDR scheme when they ought to be. There should be a discretion for the decision maker to hear a claim where they are satisfied that refusing access would cause hardship to the consumer.

Scope and principles

Question 1

Is the Panel's approach to the scope of these issues appropriate? Are there any additional issues that should be considered?

Legal Aid NSW supports the Panel's approach to the scope of the issues.

Question 2

Do you agree with the way in which the Panel has defined the principles outlined in the Review's Terms of Reference? Are there other principles that should be considered?

Legal Aid NSW supports the Review's principles.

Existing compensation arrangements

Question 3

What are the strengths and weaknesses of the existing compensation arrangements contained in the Corporations Act 2001 and the National Consumer Credit Protection Act 2009?

Legal Aid NSW supports the obligation on firms to maintain adequate compensation arrangements. However, given the significant unpaid determinations that exist, we consider that the current compensation arrangements are not adequate to ensure that consumers are compensated where they have proven a loss.

In particular, the current arrangements do not effectively protect consumers where firms refuse to honour decisions, engage in phoenixing activity or are insolvent. Legal Aid NSW often acts against firms whose business model preys upon vulnerable and disadvantaged consumers. As the case study below shows, these kinds of firms with questionable business models are likely to end up insolvent or deregistered, with consumers left with no access to compensation.

Case Study – Vendor finance provider

Legal Aid NSW has acted for a number of clients in dispute with a vendor finance provider.

The provider appears to have targeted disadvantaged people, including those with low education, low financial literacy, low income and Aboriginal people. The provider marketed its product to consumers living in regional and remote areas and positioned the product towards people with poor credit histories. The provider also relied on referrals within client families and kinship relationships to promote their product.

Our clients have claims under various consumer protection laws, but as the provider has now gone into liquidation, they have limited access to redress.

Any compensation scheme of last resort should be accompanied by stronger obligations on firms to ensure consumers are adequately compensated for losses. We also recommend that the regulators be adequately resourced to investigate and enforce breaches of these obligations.

The Supplementary Issues Paper discusses professional indemnity insurance in the context of existing compensation arrangements. However, as the paper notes, the purpose of professional indemnity insurance is not to provide compensation directly to consumers.¹ Legal Aid NSW submits that while reforms to professional indemnity

¹ [61].

requirements could improve the position of some consumers,² this would not be an adequate response to the risk of uncompensated losses. Consumers cannot make a claim directly on a firm's professional indemnity insurance, receive no information about why a firm's claim might be refused, and have no standing to challenge that refusal. Insurers may refuse a firm's claim if there is evidence of fraud—exactly the circumstance in which a consumer is likely to have suffered loss.

Evaluation of a compensation scheme of last resort

Question 6

What are the benefits and costs of establishing a compensation scheme of last resort?

Legal Aid NSW strongly supports the establishment of a compensation scheme of last resort to address current and future uncompensated losses incurred by consumers.

The benefits of the scheme include:

- providing consumers with access to redress where a firm fails to compensate consumer loss following a decision in the consumer's favour
- helping restore public trust in dispute resolution and in the financial system more generally, and
- reducing the burden on public institutions, such as Centrelink, and the wider community to support consumers with unpaid awards.

In our view, the significant benefits of establishing a compensation scheme of last resort justify the regulatory, administrative and industry costs involved in establishing the scheme.

We note in particular the concern that a compensation scheme may encourage consumers to be complacent about the risks of participating in the financial services market. We do not consider that this is a likely outcome given that the scheme is intended to be a scheme of last resort only where the consumer has proven a loss. Should the consumer's behaviour have contributed to their loss, the decision maker will apportion liability appropriately. Further, the design of the scheme will include eligibility criteria and time limits to ensure an equitable process for both firms and consumers. More detail is found in our response to Question 8.

There is an additional concern that a scheme will induce riskier behaviour in some firms, such as providing inappropriate products to consumers or refusing to pay awards. This risk should not be an impediment to the establishment of the scheme, but should guide the design of its safeguards. For example, the scheme could include a process where a

² See further our response to Question 14.

firm that fails to pay an award in certain circumstances is referred to the regulator for investigation. More detail is found at our response to Question 27.

Question 7

Are there any impediments in the existing regulatory framework to the introduction of a compensation scheme of last resort?

No, Legal Aid NSW does not consider that there are any major impediments in the existing regulatory framework to the introduction of a compensation scheme of last resort.

Question 8

What potential impact would a compensation scheme of last resort have on consumer behaviour in selecting a financial firm or making decisions about financial products?

Legal Aid NSW considers that the introduction of a compensation scheme of last resort will lead to increased consumer confidence in the financial system and therefore increased consumer participation in the market. This is likely to have a broader economic benefit to Australia's financial system.

It is unlikely that a compensation scheme will result in riskier or complacent consumer behaviour as the current consumer protection obligations operate effectively to mitigate this outcome. More detail can be found at our response to Question 6.

The establishment of the compensation scheme should be accompanied by a targeted communication strategy to consumers, especially vulnerable consumers, to ensure they are properly informed about the scheme. This communication should include information about:

- the function and goals of the scheme
- eligibility requirements
- limitation periods, and
- how to access the scheme.

Question 11

What flow-on implications might be associated with the introduction of a compensation scheme of last resort? How could these be addressed to ensure effective outcomes for users?

Legal Aid NSW submits that the introduction of a compensation scheme will place a greater burden on the regulator as it oversees the functioning of the scheme and takes investigative and enforcement action where appropriate. The Australian Securities and Investments Commission (**ASIC**) should be adequately resourced to manage the increased regulatory burden.

In addition, adding another process to financial services dispute resolution may be confusing to consumers. To mitigate this risk, it is important that the roll-out of the scheme be accompanied by a targeted and thorough campaign to consumers. More detail is provided at our response to Question 8.

A concern has been raised that the establishment of the scheme will increase the financial burden on industry, which may then be passed on to consumers. We submit that this cost should not be passed along to consumers of financial products. Again, we consider that the regulators will have a role in ensuring that financial products remain affordable for consumers.

The cost of the scheme can be minimised by the proper regulation of the financial system. In particular, given that half of FOS unpaid determinations concern financial advice, there should be continued efforts to improve the professional and ethical standards of this sector. Legal Aid NSW supports the comments made by the Australian Banking Association that the success of a last resort scheme would be promoted by reforms to Australian financial services licensing standards, enhanced ASIC enforcement powers and the professionalisation of financial advice.³

Question 12

What other mechanisms are available to deal with uncompensated consumer losses?

Question 32

What existing mechanisms are available for individuals who have legacy unpaid EDR determinations to receive compensation?

Consumers can commence court proceedings or negotiate directly with a firm to recover uncompensated losses. Similarly, consumers who have legacy unpaid EDR determinations may still be able to bring an action in court against the firm, provided their claim is within time and the firm is still operating. We note that the EDR scheme may also be able to pursue the firm for breach of contract in failing to pay the award.

In our view, these mechanisms are inadequate as they are expensive, time-consuming and often not viable options for many of the vulnerable and disadvantaged consumers seeking assistance from Legal Aid NSW. Specifically in respect of legacy claims, as a significant number remain unpaid, it is likely that consumers have already determined that court action is not a feasible process for them.

Legal Aid NSW notes the additional mechanisms referred to at paragraphs 64–82 of the Supplementary Issues Paper. These mechanisms are targeted to specific disputes and do not adequately address the broad range of financial disputes experienced by

³ Treasury, *Review of the financial system EDR framework* Supplementary Issues Paper May 2017, [87].

consumers. Further, in our experience, eligible consumers generally have a very low awareness of the availability of these mechanisms for redress.

Legal Aid NSW submits that the establishment of a compensation scheme that covers both future and legacy unpaid determinations will provide a fair and accessible mechanism for consumers with uncompensated losses.

Question 13

What relevant changes have occurred since the release of Richard St. John's report, Compensation arrangements for consumers of financial services?

Richard St. John's report concluded that the establishment of a statutory compensation scheme for financial services was inappropriate in the context of minimal regulation to protect retail clients, particularly in financial services.

Since the report was published in 2012, there have been significant changes to consumer protection law and practice in financial services. For example, the *National Consumer Credit Protection Act 2009* (Cth) came into force in mid-2010 and placed responsible lending obligations on credit providers. Our observation is that changes in conduct took some time to flow through, and may not have been evident during Mr St John's inquiry.

Further obligations were placed on small amount credit providers under the *Consumer Credit Legislation Amendment (Enhancements) Act 2012* (Cth). This regulation has led to vast improvement in the behaviour of firms with regard to the provision of credit that is suitable for their clients' needs.

Despite these enhancements to consumer protections, many consumers are still unable to access redress in circumstances where a decision against a firm remains unpaid, with the result that consumer losses have increased to the current figures.

We support the recommendation of the St. John Report that existing compensation requirements of firms should be strengthened. In our view, this should be implemented alongside the establishment of a compensation scheme of last resort. We consider that the improvement in consumer protection laws, which provide strong rights to dispute resolution, will limit the number of potential claims to the scheme, therefore ensuring that it is financially viable and sustainable.

Potential design of a compensation scheme of last resort

Question 14

What are the strengths and weaknesses of the ABA and FOS proposals?

Question 23

What compensation caps should apply to claims under any compensation scheme of last resort?

Legal Aid NSW broadly supports the FOS proposal, subject to our comments below.

ABA proposal

The ABA proposal has the following strengths:

- It applies to small businesses as well as individual consumers.
- It recognises the need for other reforms and measures, alongside the scheme, to reduce the amount of unpaid determinations in the first instance.
- The proposed governance structure includes a legal expert, in addition to an independent chair and an equal number of industry and consumer representatives.

It has the following weaknesses:

- The scheme will only be available to individuals and small businesses who have received poor personal and/or general financial advice on certain financial products.
- The reason for non-payment of the EDR determination needs to be specifically due to the insolvency or winding up of the financial advice business with evidence being required that the assets of the financial advice business will not cover the determination. This could create a considerable evidentiary burden, particularly for individual consumers.
- The scheme is prospective with no provision to cover unpaid EDR determinations or court or tribunal decisions made before the scheme becomes effective. This would exclude a large number of determinations.
- The structure of the scheme provides that it will not operate on a full-time basis and will respond to claims only as they arise. This may cause delays in processing claims and there may be inadequate resourcing should there be a large influx of claims.

FOS proposal

The FOS proposal has the following strengths:

- The scheme would cover claims by retail clients, as defined in Chapter 7 of the *Corporations Act*. The scheme would also cover EDR determinations and court and tribunal decisions.
- Firms who provide financial services to retail clients would be required to be members of the scheme.

- The scheme would be industry funded.
- There is no requirement for the consumer to establish that the firm is insolvent or wound up.
- The scheme would address the significant amount of unpaid past consumer losses.
- Legacy unpaid determinations made since 1 July 2008 are covered.

It has the following weaknesses:

- Small businesses are not included in the scope of the scheme.
- Compensation received by consumers could be limited, or payment could be spread over a period of time.

Should the Panel adopt the FOS proposal, Legal Aid NSW recommends that the scheme apply to all unpaid EDR determinations and court and tribunal decisions (within certain time limits, outlined in response to question 29). Legal Aid NSW does not consider that compensation received by consumers should be spread over a period of time, nor should it be limited to a portion of the EDR scheme limits. Instead, Legal Aid NSW recommends that consumers be compensated as quickly as possible, and that their payments are within the limits of the EDR scheme, to the extent that this approach is financially viable for the compensation scheme. We also consider that the compensation scheme should be introduced alongside better regulation and oversight of professional indemnity insurance. More detail can be found in our responses at Questions 16-18.

Question 15

What are the arguments for and against extending any compensation scheme of last resort beyond financial advice?

Legal Aid NSW strongly supports extending the scheme beyond financial advice. We assist the most vulnerable consumers in NSW, most of whom do not have claims relating to financial advice. Our casework experience shows that unpaid decisions relate to a wide range of financial products, such as payday loans, consumer leases and vendor finance contracts.

Narrowing the scope of the compensation scheme to financial advice decisions appears to prioritise the claims of those consumers with enough money to need advice about how to manage it. We are concerned that limiting the scope of the scheme in this way risks further entrenching disadvantage for a very vulnerable class of consumers and would allow some of the most egregious conduct in the financial services sector to go uncompensated.

We recommend that the scheme should cover all financial services, products and advice. Taking a broader approach to eligibility for compensation is essential to building trust and confidence in the community towards the financial sector as a whole. A wider scope also has the benefit of reducing consumer confusion about eligibility to access the scheme.

Individuals and small businesses

Question 16

Who should be able to access any compensation scheme of last resort? Should this include small business?

Legal Aid NSW considers that the compensation scheme should be available to individual consumers and small businesses.

Types of claims covered

Question 17

What types of claims should be covered by any compensation scheme of last resort?

As noted in Question 15, Legal Aid NSW considers that the scheme should cover all financial services, products and advice.

EDR, court and tribunal decisions

Question 18

Should any compensation scheme of last resort only cover claims relating to unpaid EDR determinations or should it include court judgments and tribunal decisions?

Legal Aid NSW considers that the compensation scheme of last resort should include claims relating to unpaid EDR determinations, court judgments and tribunal decisions. The category of court judgments should include awards to consumers from class actions and regulatory action.

Structuring the scheme in this way would build trust and confidence in dispute resolution processes and the financial services sector. What is important to a consumer is that their loss is compensated when they have proven their complaint. It does not matter if the forum used to resolve the dispute is EDR, a tribunal or court. Additionally, having one set of consistent and broad rules about which disputes are eligible to access the compensation scheme would reduce confusion for consumers, and would again contribute to trust and confidence in the sector.

Including court and tribunal decisions in the scheme would ensure that a consumer's ability to obtain compensation is not limited by the forum in which their dispute was heard. It would also prevent the design of the scheme from affecting a consumer's choice about forum, particularly in circumstances where a court or tribunal is the appropriate place for the matter to be heard.

Importantly, there are times when a consumer must take a financial services dispute to court because the firm is not in an EDR scheme when they should be, or is trading without a licence. These consumers are denied access to EDR because of the misconduct of the

firm. It would compound the injustice to also deny them access to the compensation scheme of last resort if the court or tribunal finds in their favour but they are unable to recover from the firm.

In our experience, consumers do not usually choose to take their dispute to court where EDR is available, so it is unlikely that broadening the scheme's scope to include court and tribunal decisions would increase the burden on the scheme significantly. However, as the case study below shows, there are circumstances where a consumer receives a favourable court decision without receiving compensation from the other party.

Case Study – Vendor finance decision in Supreme Court of NSW

In 2016, the Supreme Court of NSW awarded Ms Clarke \$114,000 to be paid by Evolution Lifestyles on the basis that the contract that Evolution Lifestyles entered into with Ms Clarke was unjust. Shortly after the Supreme Court handed down its decision, Ms Clarke was notified that Evolution Lifestyles had gone into liquidation. As a result, Ms Clarke may not recover any of her award from Evolution Lifestyles.

Preconditions for access

Question 19

What steps should consumers and small businesses be required to take before accessing any compensation scheme of last resort?

Legal Aid NSW considers that consumers and small businesses should be required to:

1. attempt to engage in internal dispute resolution with the firm, and
2. engage in an external dispute resolution process, such as an Ombudsman scheme, court or tribunal, and
3. obtain a decision or determination that the consumer's loss flows from the misconduct of the firm.

The next step to be taken depends on whether the firm is solvent, and whether the award relates to an EDR determination or a decision of a court or tribunal:

- Where the award relates to an EDR determination and the firm is solvent, the consumer should receive certification from the EDR scheme that the award remains unpaid after a reasonable period of time.
- Where the award relates to an EDR determination and the firm is insolvent, the consumer should receive certification from the EDR scheme that the consumer is entitled to proceed directly to the compensation scheme.

- Where the award relates to a court or tribunal decision and the firm is solvent, the consumer should take reasonable steps to enforce the award, such as attempting to garnishee the bank account of the firm.
- Where the award relates to a court or tribunal decision and the firm is insolvent, the consumer should contact the administrator or liquidator requesting payment.

Question 20

Where an individual has received an EDR determination in their favour, should any compensation scheme of last resort be able to independently review the EDR determination or should it simply accept the EDR scheme's determination of the merits of the dispute?

We do not consider that the compensation scheme should be required to re-determine liability of the firm prior to accepting a consumer's application for compensation. The process of applying for and receiving compensation from the scheme should be as streamlined and timely as possible for the consumer, particularly as the consumer may have already suffered considerable expense, hardship and delay in waiting for payment from the firm.

The process involved in reaching a decision through an EDR process is independent, there is a full exchange of information and an opportunity for all parties to participate. In light of this, it would be sufficient and appropriate for the compensation scheme to accept the findings of the determination or judgment.

To go through a further review will delay the process and may increase the administrative costs of the scheme unnecessarily. As noted above, a further review could inconvenience and distress consumers who have already been through a comprehensive dispute resolution process.

Question 21

If a compensation scheme of last resort was established and it allowed individuals with a court judgment to access the scheme, what types of losses or costs (for example, legal costs) should they be able to recover?

Legal Aid NSW considers that individuals with a court judgment should be able to recover their legal costs from the scheme, otherwise they would be left considerably out of pocket. If necessary, the legal practitioner should be able to recover their fees from the individual consumer under the contract between those parties.

Question 22

Should litigation funders be able to recover from any compensation scheme of last resort, either directly or indirectly through their contracts with the class of claimants?

Legal Aid NSW considers that litigation funders should be able to recover from a compensation scheme, but only indirectly, through their contracts with the class of claimants.

Class actions play an important role in providing access to justice for consumers who may not otherwise have access to redress due to the size of their individual claim, limited knowledge of their claim or their lack of resources. A compensation scheme that did not allow litigation funders to recover from class members might discourage class actions, to the detriment of consumers. On the other hand, we do not consider that litigation funders should take compensation directly from the scheme before the consumer has had the opportunity to receive any benefit.

This maintains the status quo as if the individual had received compensation directly from the defendant in proceedings. This would also be consistent with the primary purpose of the compensation scheme, which is to ensure consumers themselves get access to compensation for their losses.

Question 24

Who should fund any compensation scheme of last resort?

Question 25

Where any compensation scheme of last resort is industry funded, how should the levies be designed?

Legal Aid NSW considers that the compensation scheme should be industry funded.

It is paramount that the funding model ensures that the scheme is financially sustainable, and that the cost of the scheme is borne by industry and not passed on to consumers.

The design of the levies should be decided by the scheme board and should be consistent with the principles set out above.

Question 26

Following the payment of compensation to an individual, what rights should a compensation scheme of last resort have against the firm who failed to pay the EDR determination?

Legal Aid NSW recommends that the compensation scheme take on the rights of the consumer and/or EDR scheme to recover against the firm who failed to pay. It is important that the scheme is adequately funded to cover any enforcement actions, so that its compensation function is unaffected by costs related to enforcement.

The scheme should be required to notify ASIC when a firm fails to pay. Further, the scheme should be required to report systemic issues and serious misconduct to ASIC.

Question 27

What actions should ASIC take against a firm that fails to pay an EDR determination or its directors or officers?

When notified by the scheme that a firm has failed to pay an EDR determination, ASIC should investigate the reason for the failure and notify the scheme of the results of the investigation. The firm will not be compliant with the membership terms of the EDR scheme and will therefore be expelled from the scheme. Where the firm's licence requires EDR membership, the licence should promptly be revoked.

Where appropriate, ASIC should take regulatory action against the firm and/or the directors, such as disqualification of directors or the imposition of a penalty on the firm. Where ASIC recovers a penalty from the firm, this amount should be contributed to the compensation scheme.

It is important that ASIC is adequately funded and resourced to allow for an increase in its responsibilities in respect of the compensation scheme.

Question 28

Should any compensation scheme of last resort be administered by government or industry? What other administrative arrangements should apply?

Legal Aid NSW recommends that the compensation scheme of last resort be administered by industry, with regulatory oversight. Structuring the scheme in this way would ensure that it has the necessary adaptability to change its processes when appropriate.

The scheme should be governed by a board comprised of an independent chair and an equal number of directors with consumer and industry backgrounds. In appointing the board, the qualifications and experience of the proposed directors should be taken into account.

The scheme should be funded and resourced appropriately to ensure that claims are processed in a timely manner.

Question 29

Should time limits apply to any compensation scheme of last resort?

Yes, Legal Aid NSW recommends that the following time limits should apply:

- If a decision is made in favour of the consumer after the scheme commences, the consumer should have six years from the date of the decision to apply to the compensation scheme.

- If a decision is made in favour of the consumer before the scheme commences, the consumer should have six years from the date of the establishment of the compensation scheme to apply to the compensation scheme.

The above time limits correspond with statutory limitation periods. This will maintain consistency in the financial services complaints process and reduce consumer confusion.

We note that in respect of court judgments, a consumer has 12 years from the date of the decision to enforce the debt against the firm. In our view, a time limit of six years for future and legacy claims balances the need to allow enough time for consumers to become aware of the scheme and attempt to recover payment from a firm with the need to ensure the scheme is able to resolve applications within a reasonable timeframe.

Further, a defined period of time within which a consumer can make a claim provides certainty for industry in planning for future enforcement action from the compensation scheme, particularly in respect of legacy claims.

Question 30

How should any compensation scheme of last resort interact with other compensation schemes?

The compensation scheme of last resort should operate alongside, and in addition to, any existing compensation schemes.

Where a consumer has a claim for which they are able to access two or more compensation schemes, the consumer should only be allowed to access one scheme. Double dipping could be prevented by including screening questions in the application process for the compensation scheme, such as 'have you already received compensation for your claim?'

The compensation scheme should provide information for consumers about what other schemes are available, to help consumers identify the appropriate compensation scheme for their dispute.

Legacy unpaid EDR determinations

Question 33

Is there a need for an additional mechanism for those with legacy unpaid EDR determinations to receive compensation? If so, who should fund the payment of the legacy unpaid EDR determinations?

Legal Aid NSW strongly supports the inclusion of legacy unpaid EDR determinations and court and tribunal decisions in the scheme of last resort. We support the proposal made by the FOS for the scheme to be available to consumers with determinations and decisions made since the establishment of the FOS on 1 July 2008. As noted in the

Supplementary Issues Paper, the impact on a consumer where they have invested time and money into the dispute resolution process, only to have their award remain unpaid, can be significant.

We consider that industry should fund the scheme to pay legacy claims, with the scheme taking on the right to pursue enforcement action against the firms.

We recommend that the compensation scheme should take active steps to advise all consumers with a legacy unpaid EDR determination of the establishment of the scheme and the timeframes in which the consumer should make an application to the scheme.

Providing access to redress for past disputes

Question 34

Other than circumstances that may be covered by a compensation scheme of last resort (such as outstanding unpaid determinations), what kinds of circumstances have given rise to past disputes for which there has not been redress? Are there any other classes besides those identified by the Panel?

Beyond the scenarios listed in the Supplementary Issues Paper, other circumstances leading to consumers being unable to seek redress include:

- where a firm is trading while unregistered or unlicensed, and is therefore not required to be a member of an EDR scheme
- where a firm has been expelled from an EDR scheme and has not become a member of the alternative scheme
- where a consumer has commenced a dispute in EDR, but the EDR scheme did not make a determination prior to the member leaving or being expelled from the EDR scheme, and
- where a firm has closed down (not necessarily becoming insolvent) and is uncontactable.

Question 35

What evidence is there about the extent to which lack of access to redress for past disputes is a major problem?

Legal Aid NSW advises a number of consumers each year who have been unable to obtain adequate redress through EDR processes, often for the reasons outlined at Question 34. We consider this to be a major problem based on our casework experience, especially as there is likely to be a number of consumers who never reach out for legal advice.

Legal Aid NSW has had to advise Aboriginal clients living in regional NSW not to pursue dispute resolution due to the unlikelihood of success because we were aware that a particular trader was insolvent.

Further, as the case study below shows, we assisted a group of clients to seek internal dispute resolution with a firm because the firm was not a member of an EDR scheme while trading. During the dispute, the firm briefly became a member of an EDR scheme due to ASIC involvement, but has since been expelled from the scheme due to poor conduct. This has meant that the only redress available to our clients is an action in the courts or tribunals.

Case Study – Household rentals

Legal Aid NSW has a group of Aboriginal clients who have been unable to obtain redress through the EDR process. These clients live in a remote town and Aboriginal mission with a high Aboriginal population and a high incidence of economic disadvantage. The clients include a single parent with young children, several large families wholly dependent on Centrelink, and an older Aboriginal man. Most of the clients have never worked, remain reliant on Centrelink income, have low levels of literacy and extensive family carer responsibilities.

These consumers were targeted by a small business (that is now trading under a new business name) selling rental contracts for household goods. Many of the clients received unsolicited home visits to sign them up for contracts.

Legal Aid NSW considered that the business may have engaged in unconscionable conduct and multiple breaches of consumer protection laws. Due to the failure of the trader to engage in internal dispute resolution, Legal Aid NSW assisted clients to lodge disputes with an EDR scheme. The EDR scheme subsequently failed to advance or determine the matters in a timely manner, or take action against the trader for failing to meet deadlines. Due to lack of engagement, the trader was expelled from the scheme and is not currently a member of any ASIC-approved EDR scheme.

As the EDR scheme did not determine the matter prior to the member's expulsion, this dispute remains unresolved and many of the time limits for alternative legal claims have now expired. The clients now have little or no prospects of obtaining financial or legal redress. The clients were seeking a modest refund of approximately \$15,000 in total for their combined loss, which would be of significant benefit, given their vulnerability and disadvantage.

Approaches to providing access to redress for past matters

Question 36

Which features of other approaches established to resolve past disputes outside of the courts (whether initiated by industry or government) might provide useful models when considering options for providing access to redress for past disputes in the financial system?

Legal Aid NSW considers that the current EDR model is an effective approach to replicate when considering options for providing access to redress for past disputes. We note our response at Questions 44 and 46 that the mechanism for dealing with past disputes should be incorporated into the new EDR scheme.

When designing a process to access redress, Legal Aid NSW recommends that the following features should be considered:

- *Accessibility*: The process should be easy for consumers, especially vulnerable consumers, to access. The process should also be well-publicised to ensure that consumers are aware of their rights to seek redress.
- *Obligation to provide documents*: The firm should have an obligation to participate in the redress process and to provide documents. If they fail to participate, the matter should move to a timely determination. Consideration should be given to a presumption in favour of the consumer if the firm fails to participate and provide documents.
- *Reporting systemic issues and misconduct*: The administrator of the redress process should record and report issues of misconduct to the EDR scheme and the regulator.
- *Efficiency*: The redress process should focus on timely resolution, noting that slow outcomes contribute to consumer dispute fatigue, consumers settling for lower amounts than they would otherwise be entitled and the expiry of statutory timeframes for other avenues of legal redress.

Evaluation of providing access to redress for past disputes

Question 37

What are the benefits and costs associated with providing access to redress for past disputes?

Question 39

What impact would providing access to redress for past disputes have on the operations of financial firms?

Question 41

Would there be any flow-on implications associated with providing access to redress for past disputes? How could these be addressed in order to achieve effective outcomes for users?

Access to redress for past disputes has a number of benefits to consumers, industry and the community. Most importantly, consumers who have been excluded from accessible dispute resolution are given access to justice. We are confident that a redress process would build consumer confidence in the financial services industry.

We note the concerns outlined in the Supplementary Issues Paper about introducing a redress process for past disputes. A key issue is that a large and unknown number of disputes may need to be handled in a relatively short period of time. This can be managed by properly designing and funding the scheme at the outset to ensure a significant number of disputes can be progressed simultaneously.

Another issue is the potential cost of a large number of determinations and how this interacts with the compensation scheme of last resort. We consider that this concern can be managed by:

- having clear eligibility criteria so that industry can gauge the size of potential claims against them
- an application window which will ensure an end date for past disputes to be ventilated
- capping the value of disputes at the EDR compensation cap
- only allowing matters where the consumer or small business genuinely has not had access to redress to be heard by the scheme (for further detail, see our comments at Questions 43–45), and
- properly resourcing the compensation scheme of last resort at the outset so that a spike in determinations for past disputes can be paid, if required.

Ensuring the scheme is not overwhelmed with inappropriate past disputes will also be important. This can be managed by:

- community education and plain language information about eligibility and process
- a warm referral process from consumer advocates, and

- a system to check the eligibility of disputes up front.

Other considerations may arise depending on the types of past disputes made eligible for redress. For example, where the firm is insolvent, consideration will need to be given to how these matters will be determined in light of limited documentary evidence.

Question 38

Are there any legal impediments to providing access to redress for past disputes?

Legal Aid NSW considers that the two main legal impediments to a process for providing redress for past disputes are time limits and eligibility. We recommend that these issues be considered carefully in the design of any process of redress for past disputes.

Time limits

Under the existing EDR framework, disputes can generally be heard by an EDR scheme if the dispute was lodged within six years of when the consumer first became aware that they had suffered loss or within two years of receiving an internal dispute resolution response from a firm, whichever is the earlier.

A procedural fairness issue may arise if people who are now unable to apply to EDR schemes because of the established time limits are, in future, able to apply to those schemes. More detail can be found in our response to Questions 44 and 45. In summary, we consider that consumers with past disputes should be able to access EDR where the consumer was unable to resolve the dispute within time due to the conduct of the firm (such as failing to be a member of an EDR scheme).

Eligibility

Consumers are often unable to resolve their disputes where the firm is insolvent or is not a member of an EDR scheme when they should be. If the redress process allows consumers to access EDR in these circumstances, it is important to consider how this will operate practically. In particular, consideration should be given to

- how the firm will be notified and participate in the process
- if the firm will be charged fees if they do participate in the process, and
- how the EDR scheme will enforce determinations against firms who are not members of the scheme.

Design issues for providing access to redress for past disputes

Question 42

What are the strengths and weaknesses of the Westpac proposal?

While we support the Westpac proposal of a scheme for redress for bank-related financial advice or maladministration in lending matters, Legal Aid NSW considers this proposal to be too limited in scope.

Many of the consumers assisted by Legal Aid NSW are excluded from mainstream financial products offered by banks, and their disputes do not concern financial advice or maladministration in lending disputes. For example, our clients' disputes frequently relate to small amount credit contracts, consumer leases and insurance, particularly life and home and contents insurance claims. To build consumer trust and ensure consistency in financial services dispute resolution, it is critical the full range of disputes is included in any scheme for redress for past disputes.

We also consider that the process for access to redress for past disputes should be open to consumers who were unable to ventilate their dispute in EDR due to the firm's conduct (for example, the firm was insolvent or not a member of an EDR scheme when it should have been), and now are outside of the EDR time limits. More detail can be found at our response to Questions 43–45.

As stated in our response to Question 48, access to the redress process should be limited to disputes within the EDR monetary threshold at the time the dispute arose. However, if industry is willing to put additional funding to extend the monetary threshold in the category of banking-related financial advice and maladministration in lending disputes, we would support that proposal.

Question 43

What range of parties should be provided with access to redress for past disputes? Should all of the circumstances described in paragraphs 133-144 be included?

Consumers and small businesses who have entered into contracts for financial products, services and advice should be provided with access to redress for past disputes. This will maximise the forum's reach, ensure consistency with EDR schemes and meet the objective of building trust in the financial services industry by providing consistent options for redress regardless of the product purchased.

In forming our view as to the categories of disputes that should be included, Legal Aid NSW has considered the following principles:

- the consumer was unable to resolve their dispute within the relevant timeframe because of the conduct of the firm
- the consumer now has no avenue for redress for their dispute
- the consumer should be placed in the position that they would have been were it not for the firm's misconduct, and
- where it is not possible to fully compensate all claimants, a rationing mechanism based on financial hardship should be used to allocate resources.

We consider that matters that are within time and within EDR guidelines should be determined in the usual way in EDR. To ensure that consumers are able to access the benefits of the compensation scheme of last resort, we consider that EDR schemes must determine matters whether or not the firm is solvent or actively participates in the scheme.

Our response to the circumstances described in paragraphs 133–144 is outlined in the table below:

Circumstance	Discussion
<p>The firm was insolvent or otherwise unable to pay</p>	<p>Where the matter is within time, these matters should be resolved through the ordinary EDR process—a specific past disputes forum is not required.</p> <p>In light of the proposed compensation scheme of last resort, EDR should consider disputes even where the firm is insolvent, is not participating in the dispute resolution process or is otherwise unable to pay.</p>
<p>The monetary value of the dispute exceeded the EDR scheme’s monetary limits</p>	<p>Legal Aid NSW does not consider this category warrants inclusion in a past disputes forum. While some consumers with high value disputes will find access to the court system difficult, it is not accurate to describe these as matters where the consumer or small business has not had access to redress. Disputes outside the monetary limits but within statutory time limits can be filed in court.</p> <p>We are also concerned that including these matters would, in practice, be a retrospective change to EDR terms of reference. This creates unfairness for those consumers and small business who have already incurred the time and cost in ventilating these matters in court. One exception may be banking-related financial advice and maladministration in lending disputes given the systemic issues identified in this sector and industry’s potential willingness to specifically compensate these matters (as outlined in the Westpac proposal).</p> <p>Should this group of consumers be able to access the scheme, Legal Aid NSW suggests that it could be by way of a discretion to allow access when there has been exceptional circumstances, for example, loss of a home.</p>
<p>The dispute was outside EDR time limits</p>	<p>Legal Aid NSW proposes that certain matters that are outside EDR time limits be included in the past disputes forum.</p> <p>To be eligible, the reason for the failure to take action within the prescribed time limit must be one of the following:</p> <ul style="list-style-type: none"> • The firm was insolvent or otherwise unable to pay; or • The consumer experienced legal disability (as defined in section 11(3) of the <i>Limitation Act 1969</i> (NSW); or

	<ul style="list-style-type: none"> The firm was not a member of an EDR scheme (for example because the firm was trading unlicensed, or its membership was cancelled or lapsed).
<p>Complainant did not pursue their dispute with the EDR scheme for other unspecified reasons (for example, because of personal circumstances or dispute fatigue).</p>	<p>Legal Aid NSW does not consider these factors in and of themselves warrant inclusion of a matter in a past disputes forum.</p> <p>We note that overcoming these barriers should be a key feature of the design of the new EDR regime.</p> <p>Legal Aid NSW would support access for these complainants in exceptional circumstances, for example, when the complainant can demonstrate particular hardship.</p>

We also propose that the Panel should consider including the circumstance where the firm is not a member of an EDR scheme when it ought to be. In this circumstance, the consumer’s only recourse is the courts. To put consumers in the position that they would have been except for the firm’s misconduct, we propose that consumers and small business should have access to a past disputes forum in circumstances where the firm is not a member of an EDR scheme (for example, because the firm is unlicensed, has been excluded from an EDR scheme or had its membership lapse).

Question 44

What mechanism should be used to resolve the dispute and what criteria should be used to determine which disputes can be brought forward?

Legal Aid NSW suggests that a ‘past disputes’ division within the new EDR scheme be established to deal with these matters. It would be helpful to have specialists in this team providing expertise about particular products, such as financial advice, and particular perspectives, such as consumer advocates.

Where possible, for example where the firm is still trading, disputes could follow the same dispute resolution process as other matters in the new EDR scheme with an additional initial step to confirm whether the dispute is within the forum’s jurisdiction.

Given the extensive experience of the current EDR bodies and the desire for consistency, this proposal will promote the high quality, cost effective and speedy resolution of past disputes.

Our views about the criteria used to determine which disputes should be included are discussed at Question 43.

Question 45

What time limits should apply?

Legal Aid NSW supports an application window of two years to lodge past disputes. To ensure accessibility, there would need to be extensive community education about the process for redress, including appropriate advertising, communication with key agencies assisting consumers in financial distress and outreach to particularly vulnerable communities, such as remote Aboriginal communities.

In terms of the age of the dispute, Legal Aid NSW proposes the following:

- Matters within time for EDR are ineligible and must be lodged in EDR in the usual way.
- Matters outside the time limit for EDR can be lodged, but only where the cause of action arose within 10 years, and one of the following circumstances exist:
 - action was not taken by the consumer or small business because the firm was insolvent or otherwise unable to pay, or
 - the consumer or small business did not take action within the time limit because of a legal disability as defined by section 11(3) of the *Limitation Act 1969* (NSW), or
 - the firm was not a member of an EDR scheme when it should have been (for example because the firm was trading unlicensed, had their membership cancelled or lapsed).
- There is an ultimate bar for matters older than 10 years.

Question 46

Should any mechanism for dealing with past disputes be integrated into the new Australian Financial Complaints Authority (once established) or should it be independent of that body?

Yes, Legal Aid NSW recommends that any mechanism for dealing with past disputes be integrated into the new Australian Financial Complaints Authority. The mechanism could be a separate unit within the Authority that exists on an interim basis due to the fact that decision making relating to past disputes will have an end date.

Being part of the Authority will encourage consistency in decision making processes, ensure efficient use of resources and avoid duplication.

Safeguards should be put in place so that there is no conflict regarding decisions that may have been made by existing dispute resolution schemes.

Question 47

Who should be responsible for funding redress for past disputes? Is there a role for an ex gratia payment scheme (that is payment by Government)?

Legal Aid NSW considers that industry should be responsible for funding redress for past disputes. We do not, at this stage, consider that government has any role in funding this process.

Question 48

Should there be any monetary limits? If so, should the monetary limits that apply be the EDR scheme monetary limits?

Yes, Legal Aid NSW considers that there should be monetary limits to ensure the financial viability and sustainability of the process. We consider that the monetary limits that apply should be the EDR scheme monetary limits at the time the dispute occurred to ensure that the consumer is placed in the position that they would have been if they had had the opportunity to resolve their dispute.

Question 49

Should consumers and small businesses whose dispute falls within the new (higher) monetary limits of the proposed Australian Financial Complaints Authority but was outside the previous limits be able to apply to have their dispute considered? Should access to redress for past disputes be provided through a transition period whereby the higher monetary limits are applied for a defined period retrospectively? If so, what would be an appropriate transition period?

Legal Aid NSW does not consider that consumers who have past disputes that fell outside the old EDR monetary limits should now be able to apply to have their dispute considered under the new, higher EDR monetary limits. The previous limits were considered reasonable at the time and the new limits should not apply retrospectively.

To allow such disputes to be heard would risk increasing the liability of the compensation scheme to an unknown amount, and possibly affect the sustainability of the scheme.

Further, allowing such disputes to be heard may lead to inequitable outcomes between consumers who went to court to resolve their dispute, and those who would be entitled to access the past disputes forum if a higher threshold was allowed.

Question 50

If it is not possible to fully compensate all claimants, should a 'rationing' mechanism be used to determine the amounts of compensation which are awarded? Should such mechanism be based on hardship or on some other measure?

Yes, if it is not possible to fully compensate all claimants, Legal Aid NSW recommends that a rationing mechanism based on financial hardship should be used to determine the amounts of compensation awarded.