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Dr Kathleen Dermody
Committee Secretary
Senate Economics References Committee
Parliament House
CANBERRA ACT 2600

By email: economics.sen@aph.gov.au

Dear Dr Dermody

Inquiry into the performance of ASIC

Question on notice

On 20 February 2014, at the public hearing for the inquiry, the Financial Ombudsman Service (FOS) and the Credit Ombudsman Service were asked the question on notice set out below.

Questions on Notice for the Credit Ombudsman Service and Financial Ombudsman Service

1. (pp 23-25)

CHAIR: As you outlined in your introductory remarks, you are now dealing with hundreds of thousands of complaints, either on the phone or personal visits. You are exposed to all aspects of this industry and there is clearly growing demand on your services to resolve complaints. What would be your reaction if we did recommend to the government that it reverse the presumption that a loan is valid if there is any level of fraud or malfeasance involved on the part of the loan provider?
Mr Field: You could not do it retrospectively, I would have thought. Again, when we resolve disputes, we apply the relevant legal principles and if the parliament says that that is the relevant legal principle—
CHAIR: I understand that, but I am asking a policy question.

Mr Field: My view is that you have entrenched provisions in the National Consumer Credit Protection Act. They have been in for three or three and a half years, depending on what sort of institution is involved. We have not seen a lot of cases arise yet. We are a rear-view organisation. People come to us sometimes many years after the original event. We are just starting to get disputes around responsible lending under the National Credit Code. My feeling is that it is actually working quite well. That is my best guess at it. I would like to see how it works. I would like to give it a chance to see how it settles down in terms of changing lender behaviour. I think it probably has fixed up a lot of these issues that were raised before the legislation came in. I think it should be given an opportunity to work. There was a lot of work involved. As Raj says, we were both involved in the negotiations around getting this legislation into place. It probably took the best part of two or three years of negotiations and roundtable meetings to get it into place and get people on board. There were all sorts of stakeholders—consumers, lenders, brokers and so on. It would be good to give it a fair opportunity to work to see if it actually solves the problem.

Mr Venga: I think the problem is with retrospectivity. I cannot see any government going down that track. But, at the end of the day, if EDR schemes are required, as they are, to have regard to the law—and the law was changed and it was retrospective—certainly we would be able to look at it. Having said that, the one qualification is that we still have to show fraud. That is the hard one. It is a very high standard to show. An EDR scheme is not like a court. We cannot subpoena witnesses, we cannot cross-examine people and we cannot take evidence under oath. That makes it very difficult for us to establish that level of fraud. That is why we tend not to look at it. That is the qualification.

CHAIR: That uniform legislation—that has been in place since 2010?

Mr Field: The responsible lending obligations came in for non-authorised deposit-taking institution on 1 July 2010 and for ADIs on 1 January 2011. ADIs, being banks and mutuals, had a pre-existing code of practice anyway and that code had a similar obligation. So they were given a bit of extra time to—

CHAIR: So we now have three, four or five years of facts and figures emerging?

Mr Field: Three years. Where someone has been given a loan that they cannot afford, you would generally expect that that would become readily apparent within the first or second year, depending on the nature of the loan. If it is self-funding, they would realise when the self-funding runs out.

CHAIR: Another alternative would be for us to recommend an early review of the implementation success of that legislation in terms of this issue—to get the facts out. That is another suggestion.

Senator WILLIAMS: On that issue, when these loan application forms are being filled in by a finance broker, he or she clearly wants to get the loan over the line because he or she gets a commission for setting up the loan.

Who is responsible for wrong information—doctoring cash flows and figures and incomes and assets—in the case of a broker doing that and then forwarding it on to the bank or financial institution. I have heard about plenty of cases of that happening. What do you do to solve that problem?

Mr Venga: I think both have liabilities. The finance broker surely cannot simply benefit from putting forward a dodgy loan like that and—

Senator WILLIAMS: They have.

Mr Venga: I am not saying they have not. What I am saying is that, if it is shown that they have done it and that came to us, we would certainly be doing something about it.

Mr Goodison: In a recent determination that Raj issued in respect of a complaint of exactly that nature, the award that was made was to find the broker liable for 80 per cent of the cost of the loan. So, for the loan that they knew they should not have put forward—

Senator WILLIAMS: So for, say, a $500,000 loan, he would have had to cough up $400,000?

Mr Goodison: It was within the boundaries of our compensation limit, which is $280,000. But we considered that the consumer also had some responsibility for going in with eyes wide open. She still had to pay back the money she had borrowed, but the liability for the holding costs, or the interest costs, of the loan were 80 per cent apportioned to the broker for his wrongdoing in that instance. That is an approach our service takes—where we can establish a broker has knowingly misrepresented the consumer's financial position for the purposes of getting the loan and so obtaining a financial incentive.

Senator WILLIAMS: Which is fraud.

Mr Goodison: At best it is misleading or a misrepresentation.

Senator BUSHBY: You mentioned that it is within your monetary limit. If the loan is larger than that, can you look at it at all?

Mr Venga: Yes, but we are still limited by the—

Senator BUSHBY: You are limited in terms of the compensation—fining somebody. But it does not stop you from looking at, say, a $600,000 or a 700,000 loan?

Mr Venga: Correct.

CHAIR: Are those figures indexed?

Mr Venga: Yes.

CHAIR: The $500,000 and $280,000 figures are indexed?

Mr Venga: No, the $280,000 is.

Mr Field: Ours will be indexed, I think, from 2015 under the terms of reference. It was set, when our terms of reference came into place in 2010, at $280,000 and $500,000, with a provision that they be indexed from 2015.

CHAIR: So those figures are static for the first five years. And after 2015 are they indexed annually?

Mr Field: I cannot recall off the top of my head.

CHAIR: Could you take it on notice and advise us when those figures are indexed and on what basis.

$500,000 limit on jurisdiction

$500,000 is the monetary limit to the jurisdiction of FOS. This limit is set in paragraph 5.1o) of our Terms of Reference, which are on our website www.fos.org.au.[1] Paragraph 5.1o) states that FOS may not consider a dispute where the value of the applicant's claim in the dispute exceeds $500,000.

The $500,000 limit is not indexed. The limit meets a requirement imposed on external dispute resolution schemes through ASIC's Regulatory Guide 139[2], to which we referred in our submission to the inquiry and at the public hearing on 20 February 2014. Paragraph 164 of the Regulatory Guide requires an external dispute resolution scheme to cover complaints involving amounts up to $500,000 and notes that this is the value of the retail client test under section 761G of the *Corporations Act 2001*.

$280,000 compensation cap

$280,000 is the current compensation cap for claims in a range of disputes considered by FOS, including banking disputes. Different compensation caps apply to claims in some other categories of disputes. If full details of our compensation caps are required, please refer to section 9 of our Terms of Reference and our Operational Guidelines, which explain how that section operates.[3]

The $280,000 compensation cap is indexed. The cap is scheduled to be adjusted on 1 January 2015 and every three years thereafter, and may also be adjusted at other times.

The indexation arrangements are stated in paragraph 9.8 of our Terms of Reference, which is set out below. (The $280,000 compensation cap is one of the limits in the Schedules to the Terms of Reference referred to in paragraph 9.8.)

> **9.8 Review of monetary value of remedies**
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> a) On 1 January 2015 and every 3 years thereafter, the monetary amounts specified in paragraph 9.3a) and Schedule 2 (as then in force) will be adjusted by the higher of the percentage increase in:
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> (i) the Consumer Price Index, weighted average of eight capital cities, for the 3 year period ending with the September quarter in the previous year; and
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> (ii) the Male Total Average Weekly Earnings for the 3 year period ending with the September quarter in the previous year,
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> with rounding to the $100.00, in the case of paragraph 9.3a) and where the monetary amount represents a monthly limit, or otherwise to the nearest $500.00.

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[1] See "Terms of Reference" in "About Us".

[2] On the ASIC website, www.asic.gov.au, under "Regulatory Documents" in "Publications".

[3] On the FOS website, www.fos.org.au, under "Terms of Reference" in "About Us".

b) In addition to these adjustments, the Board of FOS will, in consultation with Financial Services Providers and other stakeholders including key consumer, community and industry organisations, periodically review the limits in the Schedule and the Board will change these limits as it considers appropriate.

Further information

If you require any further information relating to FOS, we would be happy to assist. Please direct any requests or queries to our Policy Manager, Carolyn Bruns.

Yours sincerely

Shane Tregillis
Chief Ombudsman