



Reform of Home Building Compensation Fund

Financial Ombudsman Service Australia Submission

February 2016



Contents

Executive summary	3
1 Overview	3
2 Role of FOS	4
3 Issues raised by Models 4 and 5	5
3.1 <i>Suggestion relating to dispute resolution</i>	5
3.2 <i>Suggestion relating to consumer protection generally</i>	6
Appendix 1- About FOS	7

Executive summary

Financial Ombudsman Service Australia (FOS) is an ASIC-approved independent external dispute resolution (EDR) scheme that covers disputes across the financial sector.¹

FOS welcomes the opportunity to comment on the potential reforms to the NSW Government's statutory insurance scheme for residential building work outlined in the Discussion Paper *Reform of the Home Building Compensation Fund* released in December 2015.

This submission²:

- explains that FOS could play a role in the consumer protection framework for residential building work by providing EDR services³
- highlights the possibility that Models 4 and 5 in the Discussion Paper could reduce the level of consumer protection provided in relation to residential building work
- suggests that, if Model 4 or 5 is implemented, any private insurer which provides insurance for residential building work should be required to –
 - have dispute resolution processes that meet the standards for internal dispute resolution (IDR) set by ASIC and
 - be a member of an ASIC-approved EDR scheme and
- suggests the examination of Models 4 and 5 should take into account consumer protection mechanisms under the *Corporations Act 2001* (Corporations Act) which apply to financial products comparable to any insurance for residential building work private insurers could provide.

If FOS can provide further input or assistance, please contact us.

1 Overview

FOS provides free dispute resolution services to consumers of financial services. FOS forms part of the consumer protection framework in Australia's financial services legislation.

¹ FOS is approved by ASIC under its *Regulatory Guide 139 Approval and oversight of external dispute resolution schemes* available on www.asic.gov.au under 'Regulatory Resources'.

² This submission has been prepared by the Office of the Chief Ombudsman and does not necessarily represent the views of the Board of FOS. It draws on the experience of FOS and its predecessor schemes in the resolution of disputes about financial services.

³ To explain this, the submission includes information about our current role in the consumer protection framework under Commonwealth financial services legislation.

FOS handles disputes about a very broad range of financial services, including general insurance. For example, we consider disputes about home building insurance products, which are contracts that provide insurance cover in respect of destruction of or damage to a home building. FOS has expertise in dealing with disputes related to defective building work.

Although our current jurisdiction covers home building insurance, it does not cover all of the area of residential building work addressed in the Discussion Paper. We could provide dispute resolution services regarding defective building work if certain changes were made to our [Terms of Reference](#).⁴ If there is scope for FOS to play a role in relation to disputes about insurance for residential building work, we would be happy to discuss possible arrangements.

In recent years, residential building work has been covered by mandatory insurance schemes with funds established under State and Territory legislation. Two of the models in the Discussion Paper – Models 4 and 5 – involve moving from a situation where scheme insurance is mandatory to a situation where insurance is voluntary or partly voluntary and could be provided by private insurers.

Models 4 and 5 could have unintended consequences by reducing the level of consumer protection in relation to insurance for residential building work. For example, consumers may not have access to satisfactory dispute resolution systems. The Corporations Act may not require a private insurer which provides insurance for residential building work to meet standards set by ASIC in respect of IDR and EDR.

2 Role of FOS

FOS serves the community by resolving disputes between consumers, including small businesses, and their financial services providers in a way people can trust. In performing our role as an ASIC-approved independent EDR scheme, FOS:

- acts as an impartial and independent third party in resolving disputes
- shares our experience to help prevent future disputes
- identifies systemic issues and works with financial services providers to address the effect these systemic issues have beyond the consumer who brought the dispute to FOS and
- plays a role in the way financial services providers interact with consumers.

⁴ The Terms of Reference specify the jurisdiction of FOS and govern our operations by setting out rules and processes. The Terms of Reference form a contract between us and our members.

FOS and other industry-based dispute resolution schemes have been developed over the last 25 years to give the Australian community a cheaper, quicker and less formal alternative to the courts.

We share our experience with all of our stakeholders to help reduce the number of disputes that arise in the future. This collaborative approach is one of the strengths of the current arrangements for EDR in Australia.

Information about FOS is set out in full on our website at www.fos.org.au. Appendix 1 summarises key points.

3 Issues raised by Models 4 and 5

Pursuant to subsection 761G (5) of the Corporations Act, insurance for residential building work is **not** provided to a consumer as a retail client for the purposes of Chapter 7 of the Corporations Act. This means that certain consumer protection measures for retail clients, such as measures to ensure access to satisfactory IDR and EDR services, are not in place for consumers of any insurance for residential building work that a private insurer could provide. A private insurer could provide this insurance without meeting the standards ASIC sets in respect of IDR and EDR through its Regulatory Guides 139 and 165⁵.

The Terms of Reference of FOS reflect the position under the Corporations Act. Paragraph 4.3 of the Terms of Reference⁶, read together with subsection 761G (5) and the related Regulation 7.1.12, exclude disputes about insurance for residential building work from FOS's jurisdiction.

All States and Territories have had statutory schemes for residential building work to protect consumers.⁷ On page 10, the Discussion Paper notes the NSW scheme includes dispute resolution mechanisms.

If Model 4 or 5 is implemented, the NSW scheme may be dismantled fully or partly. This could result in a reduction in consumer protection if other adequate and fair dispute resolution arrangements are not in place.

3.1 Suggestion relating to dispute resolution

To address potential problems in relation to dispute resolution, FOS suggests any private insurer which provides insurance for residential building work is required to:

⁵ See ASIC's *Regulatory Guide 139 Approval and oversight of external dispute resolution schemes* and *Regulatory Guide 165 Licensing: Internal and external dispute resolution* available on www.asic.gov.au under 'Regulatory Resources'

⁶ Terms used in paragraph 4.3 are defined in paragraph 20.1 of the Terms of Reference.

⁷ Tasmania has moved from a mandatory scheme to a system of voluntary insurance under which, in practice, no insurance is available.

- have dispute resolution processes that meet the standards for IDR set by ASIC and
- be a member of an ASIC-approved EDR scheme such as FOS.

Before FOS could provide EDR services for disputes about insurance for residential building work, we would need to alter our jurisdiction. This alteration would require amendments to our Terms of Reference. Amendments would need to accord with the Corporations Act and ASIC's guidance on dispute resolution.

Terms of Reference amendments can only be made in accordance with the process specified in our Constitution⁸, which requires consultation with ASIC, our members and other stakeholders.

FOS notes the NSW scheme provides for payments of compensation up to \$340,000. The compensation FOS may award is capped at a lower level, as explained in the guidelines to paragraph 9.7 of our Terms of Reference.⁹ In simplified terms, our compensation (excluding any compensation for costs and interest) is capped at \$309,000. FOS could have a higher compensation cap for disputes about insurance for residential building work but this would require an amendment to our Terms of Reference to provide for that cap.

3.2 Suggestion relating to consumer protection generally

If private insurers were to provide insurance for residential building work, given subsection 761G (5) of the Corporations Act, consumers would not receive the benefit of all of the consumer protection measures in the financial services legislation. This submission focusses on dispute resolution matters, reflecting our perspective and expertise. Dispute arrangements are only one element of consumer protection however.

The examination of Models 4 and 5 should include a full assessment of the level of consumer protection provided under each model, taking into account consumer protection mechanisms under the Corporations Act which apply to financial products comparable to any insurance for residential building work private insurers could provide, such as set out in other categories of general insurance. It may be appropriate to incorporate aspects of the Corporations Act approach in reforms.

⁸ See clause 14 of the [Constitution](#) of FOS.

⁹ See [guideline](#) to paragraph 9.7.

Appendix 1- About FOS

FOS was formed in 2008 from the merger of three predecessor schemes organised largely along industry sector lines. The original participants were:

- the Banking and Financial Services Ombudsman
- the Financial Industry Complaints Service, and
- the Insurance Ombudsman Service.

On 1 January 2009, two other schemes joined FOS, namely:

- the Credit Union Dispute Resolution Centre, and
- Insurance Brokers Disputes Ltd.

FOS is an ASIC-approved independent EDR scheme that covers disputes across the financial sector. Our service is free to consumers and is funded through a combination of levies and case fees paid by our members, which are financial services providers.

Our operations are governed by our Terms of Reference that form a contract with our members. The Terms of Reference are available on our website.

FOS and its predecessor schemes have over 20 years' experience in providing dispute resolution services in the financial services sector. FOS provides services to resolve disputes between member financial services providers and consumers, including certain small businesses, about financial services such as:

- banking
- credit
- loans
- general insurance
- life insurance
- financial planning
- investments
- stock broking
- managed funds, and
- pooled superannuation trusts.

As well as its functions in relation to dispute resolution, FOS has responsibilities to identify and resolve systemic issues and obligations to make certain reports to ASIC. FOS also provides code monitoring, administration and secretariat services to four Code Compliance Committees who monitor financial services providers' compliance with industry codes of practice.

FOS is governed by a board with an independent chair and:

- four 'industry directors' appointed based on their expertise in and knowledge of the financial services industry, independence and capacity and willingness to consult with the industry, and
- four 'consumer directors' appointed based on their expertise in consumer affairs, knowledge of issues pertaining to the industry, independence and capacity and willingness to consult with consumer organisations.