FINANCIAL OMBUDSMAN SERVICE

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BFSO is considering a number of issues that will be the subject of future Bulletins. These include:

- Systemic Issues: Concurrent investigations by BFSO and ASIC; and
- Mistaken payments in internet banking.

BFSO is currently engaged in discussions with ASIC about our systemic issues investigations that may also become the subject of an ASIC investigation. We are discussing with ASIC the different roles and responsibilities of the two organisations and will publish the outcome of those discussions so there is clarity for both financial services providers and consumers when it becomes apparent that there are concurrent investigations.

In our BFSO Bulletin No. 35 and supplementary Bulletin No. 39, we raised some then emerging issues in electronic banking. We are reviewing the issues that arise when there are mistaken payments in the internet banking environment.

Colin Neave

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Banking and Financial Services Ombudsman

** On 1 July 2008, the Banking & Financial Services Ombudsman (BFSO), Financial Industry Complaints Service (FICS) and Insurance Ombudsman Service (IOS) merged to form the Financial Ombudsman Service (FOS).*

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Banking and Financial Services Ombudsman Limited

ABN 48 050 070 034

FINDING 1*

DATE: **15 October 2004**

SUBJECT MATTER: **Home loan with redraw facility – special repayments made and then loan split into variable rate with redraw facility and fixed rate loan – disputants claim that repayments on variable rate loan set too low to repay interest when redraw facility used – loan balance increased despite repayments**

The following is the finding I have reached in the case of the disputants and the bank.

Investigation

I have reviewed all of the information provided by the disputants and the bank.

Background Information

In December 1999, the bank offered the disputants a home loan product. The amount of credit was $470,000.00, the loan term was 30 years from the funding date and the interest rate was the bank's standard variable rate. A redraw facility, whereby any repayments made in addition to the required regular payments could be redrawn, was available. These repayments are called "special repayments" and may be redrawn at any time prior to the full repayment of the loan facility. Mortgages over two properties were security for the loan.

The loan was funded on 19 January 2000. The loan account number was [1]. On 24 March 2000, $251,654.43, being the proceeds from the sale of one of the security properties, was credited to the loan account. The account balance then stood at $217,774.97 DR.

In January 2002, when the account balance was $238,338.32 and special repayments available to be redrawn were $123,815.00, the disputants applied to split their loan. They requested that the interest rate applicable to $200,000.00 of their borrowings be fixed for a three year period.

The bank agreed to the request. The loan account number for the fixed interest rate portion of $200,000.00 was [2.] The account number for the remaining portion of the loan remained as [1]. The special repayments remained with the variable rate loan.

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* This Finding has been edited for external publication and the parties de-identified.

At the time when the split of the original home loan was negotiated, the disputants told the loans officer that they would be redrawing the special repayments for renovations to their property. It was apparent to the disputants that they would not have sufficient special repayments to complete the renovations so they applied for another home loan of $70,000.00 for this purpose. Their application was approved. The loan account number for this loan was [3].

The Dispute

The dispute is:

1. The disputants *"were led to believe that the repayment schedules for each of* (their) *three loans were set to accommodate both the loan and redraw requirements . . ."*. However, some time after negotiating the splitting of their home loan into two components and taking out the additional loan for $70,000.00, they discovered that the total advised monthly repayment amount *"did not cover the redrawn funds"*;

2. As a consequence of 1 above, the balance of their variable rate loan [1] *"increased by approximately $6,000"* in a 12 month period; and

3. The disputants believe that the bank is obliged to refund the increased interest they will be required to repay as a result of the failure of the bank's loan management procedures to detect the *"shortfall in the repayment amount"*.

Bank Response

In response to the dispute, the bank said:

1. It has not sought to disadvantage the disputants. *"The loan repayments set were reflective of the amount outstanding at the time they were adjusted, and the Bank is not able to assess at the review when the client is likely to access special repayments made on the account"*;

2. Under the terms of the contract between it and the disputants there *"is no contractual or legal obligation for the Bank to automatically recast the monthly repayment amount of* (the disputants') *loan when* (they) *redraw out of the special repayments made on* (their) *loan account"*;

3. "[A]*ll amounts of interest debited to the loan account and the amount of monthly repayments were clearly disclosed"* in the disputants' loan statements. At any time the disputants could request in writing that the repayment amount be increased. *"It is* (the disputants') *responsibility to ensure that* (their) *monthly repayments are sufficient to cover the interest debited to* (their) *loan account"*;

4. *"By making a lower monthly repayment,* (the disputants) *have benefited from the use of the funds"*; and

5. It sought to resolve the disputants' concerns by restructuring their loans in November/December 2003. It does *"not accede to* (the disputants') *request for a refund of interest"*.

Questions

The questions raised by the case include:

1. Does the available information indicate that the bank in its discussions with the disputants in January 2002 gave them an undertaking that the advised required monthly loan repayment for account number [1] would cover interest debited to the account as a result of them redrawing special repayments?

2. Is a borrower entitled to expect a bank to bring to his/her attention the fact that his/her loan repayments are not covering interest debited to his/her account and therefore his/her loan balance is increasing?

3. Is page 1 of each of the Statements 6, 7 and 8 for loan account [1] misleading?

4. Have the disputants incurred a financial loss as a result of not covering interest debited to loan account number [1] from 1 July 2002 to 5 August 2003? and

5. What is a fair resolution of this dispute?

Assessment

Matters relevant to the above questions will be discussed below under six headings.

1. <u>Loan Discussions, Loan Variation and Loan Approval in January/February 2002</u>

   I have studied the bank files for the disputants. There are no notes of the disputants' discussions with any bank officers in early January 2002. There is a completed loan switch form dated 8 January 2002 and a copy of the bank's letter dated 21 January 2002 to one of the disputants.

   Information in the loan switching form included the loan balance, remaining loan term, fortnightly direct debit repayment amounts and a direction that special repayments were to be left in the variable portion of the loan.

   The letter dated 21 January 2002 advises that the bank is prepared to change the terms of the disputants' loan contract. It states that the new required monthly loan repayment amount for:

   (a) loan account number [2] is $1,224.00; and

   (b) loan account number [1] is $233.0.

   The bank has not been able to locate its loan file for the home loan of $70,000.00 (account number [3]). The required monthly loan repayment amounts stated in (a) and (b) above together with the disputants' statement

as to their advised total loan repayment commitments being $1,838.00 indicates that the required monthly repayment amount for the $70,000.00 loan was $381.00.

The disputants applied for the loan of $70,000.00 when it was apparent that they would not have sufficient funds from the redraw facility to complete proposed renovations. Having discussed their intention to use the funds available in the redraw facility with a Personal Banker I can appreciate why they understood that the advised loan repayment amounts for the three loans were set to accommodate both the loan balances and the available redraw funds.

At the same time I accept the bank's advice that it was not able to assess at the time of the discussions when the disputants were likely to access the special repayments.

Given the amounts of credit, loan terms and the then relevant interest rates applicable to loan account numbers [2] and [3] I am satisfied that the repayments of principal and interest advised, in January/February 2002, were appropriate for those loans.

Additionally I am satisfied that the advised required monthly repayment amount for loan account number [1] was sufficient to repay a loan of $38,338.32 (i.e. the loan balance before special repayments were redrawn), at the then current interest rate, in the remaining loan term of 28 years.

I understand why the disputants believed that the total of the loan repayment amounts they were advised would take into account the withdrawal of special repayments. I do not, however, consider that the bank gave the disputants any undertaking in January 2002 that the advised required monthly loan repayment amount for account number [1] would be sufficient to cover interest on the loan balance at that date plus the withdrawal of special repayments. The disputants' understanding was based on what may be considered a reasonable expectation after their discussions with the bank.

2. Adjustment of Required Repayment Amount and Loan Term

The bank says that it had no contractual or legal obligation automatically to recast the monthly repayment amount when the disputants redrew special repayments from their account. It also states that the "*loan term*" as stated in the loan schedule "*can be varied either by mutual agreement with the customer or by unilateral change by the Bank by giving the customer 20 days' prior written notice*".

Recalculating Required Monthly Repayment Amount

I agree that there is no reference in the contract to the bank automatically recalculating the monthly repayment amount if the borrowers withdrew special repayments. There are, however, documents on the bank file which support the disputants' understanding of the advice of local branch staff that "*as they redrew funds for* (their) *renovations during 2002* (their) *loan*

repayments should have been … adjusted by the bank to account for the increased outstanding principal on the loan".

A note in the bank file says that the bank's internal guidelines/manuals, state that "*each three month period the system will automatically recast the repayments to align them to the interest rate, loan balance and remaining term*". I consider that such an approach is consistent with good industry practice

Notwithstanding the above reference to the policy to recast repayment amounts every three months, the bank, in response to a recent survey conducted by this office, has advised that it is its policy to recast loan repayments every six months. Further, I have been advised verbally by a bank officer that no system audit was conducted by the bank during the period when the disputants' monthly payments were insufficient to cover the interest being debited to loan account number [1]

Loan Term

The contract for loan account number [1] states that the period over which repayments are to be made is 30 years from the funding date. The bank file does not contain any documentation showing that there was any agreement with the disputants about an extension in the loan term or that the disputants were given any written advice about an extension.

The bank has a duty under the banker-customer contract *"to exercise reasonable care and skill in carrying out* (the bank's) *part with regard to operations within its contract with its customer".* The standard of care for a bank is that of *"the reasonable competent banker* acting in *accordance with accepted current practice."* (*Selangor United Rubber Estates Ltd v Cradock (No 3)* [1968] 1 WLR 1555).

Summary

In the light of the bank's failure:

(a) to act in accordance with its advised policy of recasting loan repayments every six months (if not every three months); and

(b) to give written notice to the disputants, in the period March 2002 to July 2003, that loan term had been extended,

it is my view that it failed to act as a reasonable and competent banker when managing the disputants' loan account.

3. Required Repayments as per Account Statements

Attachment A* to this Finding includes pages 1 of Statements 6, 7 and 8 for account number [1] and an estimate using this office's Loan Calculator of the

* Attachments have been excluded from this copy of the Finding for de-identification reasons.

monthly repayment required to repay the disputants' loan account balance at 30 June 2002, 31 December 2002 and 30 June 2003 in a period of 27 ½ years, 27 years and 26 ½ years respectively.

Page 1 of each of the statements is a summary page. It includes information on repayments made in the relevant six month period, the withdrawal of special repayments, interest debited, the relevant interest rate charged on the account and the "*Required Repayments*" per month.

All three statements advise that the "*Required Repayments*" per month is $228.00. The Loan Calculator estimates, using the account closing balance at 30 June 2002, 31 December 2002 and 30 June 2003, that $228.00 was between $750.00 to $820.00 less than the repayment amount required to repay the loan balance in the loan term as per the initial contract.

As:

(a) the disputants had not been advised by the bank that the loan term had been extended; and

(b) the statements of account did not advise the "*remaining loan term*",

I consider that the required monthly repayment amount stated in the statements of account in Attachment A was misleading.

4. Calculation of Loss

The disputants believe that they should not be required to repay the increased interest debited to their account as a result of the failure of the bank's audit procedures to detect the "*shortfall in the repayment amount*". I acknowledge their view and I consider that they should not be disadvantaged by the bank failing to act in accordance with its contractual and statutory duty to exercise due care and skill.

I asked the banking adviser to calculate the likely loss that the disputants have incurred and will continue to incur as a result of the bank's failure to advise the monthly repayment amount required to repay their loan in the contracted loan term. The banking adviser used the Financial Loss Calculator developed by this office in conjunction with its Repayment Errors policy[*].

The banking adviser's calculations are Attachment B to this Finding. The banking adviser's estimate of loss is $2,290.45. This is the current value of future loss (additional amount which will be owing on the loan including capitalised interest), $12,012.88, less the current value of past benefit (financial benefit of payments not made), $9,722.42.

5. Restructure of Loans

[*] See BFSO Policies and Procedures available on http://www.bfso.org.au

On 21 July 2003 the disputants wrote to the bank regarding their concern about the bank's failure to "*keep* (them) *properly informed regarding the repayment requirements of* (their) *housing loan*".

Following discussions and correspondence the bank offered in November 2003 to amalgamate the disputants' variable interest rate loans (loan account numbers [1]and [3]) into a single loan with a honeymoon interest rate capped for 12 months. The loan establishment fee and the monthly service fee were waived. The loan term was extended to 30 years to reduce the required monthly repayments. On 14 November 2003 the disputants accepted the bank's offer.

There are no file notes indicating that the bank referred in its discussions with the disputants to its offer being in full and final settlement of their concerns. It is, however, apparent from the bank file that the officers who discussed the matter with disputants believed that the bank's loan restructure proposal had resolved the dispute.

6. Proposed Resolution

There is no dispute that the disputants' have suffered and will suffer a loss as a result of the bank's failure to advise them prior to August 2003 that the loan repayments they were making were insufficient to repay their loan within the original term.

There is also no dispute that the bank by restructuring their two variable interest rate loans and offering a one year honeymoon rate plus a waiver of the monthly account keeping fee attempted to satisfy the disputants' concerns. This equated to a financial benefit of $1,490.45.

In my opinion, however, the restructuring of their loans and the associated monthly account keeping fee waiver in late 2003 did not adequately compensate them for their actual and possible financial loss.

I believe that a fair resolution of this dispute would be for this office's financial loss calculation ($2,290.45) to be discounted by $1,490.45 to take into account the benefit to the disputants of the lower interest rate for 12 months and the waiver of the monthly account keeping fee. This amounts to a total loss of $800.00 ($2,290.45 - $1490.43 = $800.00).

Finding

In my view:

1. The bank did not give the disputants an undertaking in January/February 2002 that the required loan repayments for their three accounts would be sufficient to repay the accounts in the original contracted term in the event that they withdrew special repayments;

2. Good banking practice nevertheless requires that a bank advise its customers by letter if their loan repayments are not covering the interest being debited to their account;

3. Bank statements of account that do not state a "*Required Repayments*" amount that would enable the repayment of the loan in the contracted term are misleading;

4. The disputants have incurred, and will continue to incur, a financial loss as a result of not covering interest debited to loan account number [1] from 1 July 2002 to 5 August 2003; and

5. A fair resolution of this dispute would be for the bank to credit $800.00 to the disputants' new amalgamated loan.

Banking and Financial Services Ombudsman Limited

ABN 48 050 070 034

FINDING 2*

DATE: **3 September 2004**

SUBJECT MATTER: **Disputant and his live-in carer obtained a secured line of equity facility to purchase a four-wheel drive vehicle – disputant's son, on behalf of father, claimed disputant did not understand facility features, could not afford the repayments and should not have been given the facility**

The following is the finding I have reached in the case of the disputant and the bank. The disputant's son lodged the dispute on his father's behalf. The disputant has subsequently provided information to this office regarding the dispute.

Investigation

I have reviewed all of the information provided by the disputant, his son and the bank.

Background Information

In May 2003 the disputant, a 62 year old pensioner in poor health, had a live-in carer, Mr H. The disputant has known Mr H, a friend of the family, for over 25 years. In addition to his carer's pension Mr H also received a disability pension.

Mr H wished to purchase a four-wheel drive vehicle to use for transport for both of them. The disputant was in agreement with the idea. The two men approached the disputant's bank and discussed the possibility of a loan to purchase the vehicle. The disputant's bank was not prepared to advance the required funds.

The disputant and Mr H then decided to pursue funds from an alternative source. They approached the bank's agent in the local town and spoke with an accountant, Mr A with whom the disputant had previously had a business relationship. Mr A said that he felt that if the disputant and Mr H both paid half their pensions in repayments they would be able to repay a loan for a four-wheel drive vehicle.

The disputant and Mr H obtained a $44,000 interest-only line of credit facility secured by the disputant's property. In late 2003, as a result of disagreements, Mr H left the disputant's home and took the vehicle with him. After this dispute was lodged, the disputant's son regained the vehicle. Mr H has signed papers transferring the ownership of the vehicle to the disputant.

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* This Finding has been edited for external publication and the parties de-identified.

The Dispute

The disputant says:

1. On 14 May 2003 he and Mr H attended an interview at the bank's [name of suburban] branch. On that day he was ill and felt giddy. He was forced to leave the interview room on a number of occasions. He has no idea what Mr H may have told the bank officer during his absence;

2. The bank subsequently offered him and Mr H a $44,000.00 line of credit facility. The loan offer referred to the facility as a [bank name] variable rate home loan;

3. He:

   (a) "*did not understand that he had a line of credit setup and not a car loan*";

   (b) receives a pension of $440.00 per fortnight and cannot afford repayments;

   (c) was unaware that his home was security for the approved line of credit;

   (d) could not read the loan offer as at the time he *"had cataracts on both eyes"*; and

   (e) has subsequently been advised by a bank officer that the loan approved was inappropriate for his requirements; and

4. The bank took advantage of his ill health and "*has convinced him to take out a loan that is not suitable to his financial situation*".

Bank Response

In response to the dispute, the bank said:

1. The joint loan *"application was approved based on the combined income of both applicants"*;

2. The contract and Letter of Offer clearly state the loan type and security for the debt. The loan type was also explained during the application process;

3. The interviewing officer noted in the loan application that the disputant's property was going to be sold *"in early course"*;

4. Both joint borrowers attended the loan interview. Neither indicated that *"they did not understand the information that was being discussed"* and neither applicant advised that they could not read the documentation;

5. *"Both applicants were encouraged to seek independent legal advice if they were unsure of anything stated within the contract or Letter of Offer"*. Neither applicant sought such advice;

6. *"It is normal practice for the lending officer to advise* (bank) *customers of the different loan facilities available. The options are put forward, however it is then up to the customer to decide on which facility would suit their current needs. The applicants accepted the Line of Credit facility which* (it) *assume*(s) *to have met their needs at that time"*;

7. It has taken action to limit the disputant's exposure to further loss;

8. The disputant advised the manager of its [name of suburban] branch that *"he understands the way in which the loan facility operates and is aware of his obligations toward the debt"*; and

9. While it is not prepared to waive the disputant's debt it is prepared to negotiate a repayment arrangement.

Questions

Given the disputant's claims detailed at points 3 and 4 on page 2 of this Finding the principal questions raised by this dispute are:

- Was there maladministration involved in the bank's decision to approve the disputant's and (Mr H's) credit application or was it a proper exercise of the bank's commercial judgement;

- Was the bank's conduct unconscionable; and

- If there was maladministration involved in the decision to lend and/or the unconscionable conduct how should this dispute be resolved?

Assessment

Matters relevant to my consideration of the above question will be discussed below under four headings.

1. <u>Maladministration In Lending</u>

   The Ombudsman cannot consider a dispute that relates solely to a bank's commercial judgement in decisions about lending or security. He can, however, investigate a dispute that alleges that maladministration has been involved in the bank's decision about lending or security.

The Decision to Lend

When dealing with disputes this office has regard to the fact that a bank has a duty under the banker-customer contract to exercise reasonable skill and care when making a decision about lending. We are mindful that a banker should be satisfied

that there is a clear repayment source when determining that a loan application be approved

Commercial Judgement in a Decision to Lend

While an assessment of the applicant's ability to repay a loan is the most critical factor a banker takes into account when he or she decides if a loan application will be approved, other factors are also taken into account to varying degrees. These factors include the character of the applicant, the loan amount and term, the purpose of the loan and the security.

Criteria for Assessment of a Bank's Decision to Lend

This office has developed criteria for assessing whether the required standard of care has been met when making a decision to lend. The criteria are:

(a) was the loan made outside the bank's normal guidelines for lending;

(b) did the bank's officers express doubt and concern about the application;

(c) does the balance of information suggest that the sale of the security property provided was the only real prospect for repayment of the loan from the outset; and

(d) if the answer to any of the above questions is "yes" is there a reasonable explanation as to why that fact was ignored?

2. Review of the Bank's Decision to Lend and the Loan Product

I have examined the bank's lending file in order to be able to address the criteria outlined above and the disputant's claim as detailed in point 3(e) on page 2 of this Finding.

The Loan Interview

The disputant and Mr H attended a suburban branch of the bank on 14 May 2003 and were interviewed by Ms B, a bank officer who had had over four years' lending experience at the time of the loan interview.

Ms B recorded in her "*Interview Comments*" that:

(a) the applicants required a line of credit for $44,000.00 to purchase a four wheel drive vehicle;

(b) the disputant's property was on the market as the disputant and Mr H were planning to move to far North Queensland;

(c) the applicants requested minimal payments (interest only) as the facility would be cleared once the disputant's property was sold; and

(d) the disputant had supplied the Certificate of Title for his property.

Credit Assessment and Loan Approval

The disputant and Mr H's loan application contains details of their assets, liabilities and income. Documentation attached to the application supported the applicants' stated income and included details of rates and insurance for the disputant's property.

At the time of the interview the applicants' joint monthly income was $2,180.00. Ms B calculated that a monthly repayment of $253.00 would cover interest for a line of credit facility. Thus the applicants' monthly commitments, being a joint monthly living allowance of $1,420.00, Mr H's monthly loan repayment of $253.00 and the line of credit interest payment were estimated as being $1,999.00.

The bank's credit assessment model includes a "buffer" which takes into account whether the applicants would be able to meet their loan commitments if the interest rate applicable to any existing and the proposed new credit facility were to increase by 2% per annum. The bank file indicates that after the inclusion of the "buffer" there was $31.00 of disposable income remaining each month. The application was approved because it "passed" the bank's serviceability assessment.

I have noted that Ms B's comments on the application included references to the applicants' stability of residence, absence of other debts, unblemished credit rating and low loan valuation ratio.

Bank records indicate that no bank officer besides Ms B was involved in the assessment of the application or the decision to approve the loan. This is not untoward as the approval of the disputant's loan was within Ms B's delegated lending discretion.

The Loan Product

A line of credit facility is a flexible product in that the customer can elect to make interest only repayments or interest repayments plus contributions to reducing the principal amount.

Given the information recorded by Ms B in her *Interview Comments* (page 5), and the considerations discussed below under 'The Banking adviser's advice', I consider that the line of credit product was the most appropriate product for the applicants' circumstances at the time. In expressing that view I am aware of the conflict between the disputant and the bank regarding the loan interview discussions. The differing accounts will be discussed further under heading 3.

The Banking Adviser's Advice

The Ombudsman's banking adviser has advised me that he does not consider that the applicants would have met the bank's credit guidelines on serviceability for either a secured or unsecured personal loan. He said that it is his view that the bank could only have considered the application on the basis that the sale of the disputant's property was pending, and this would be the source of clearance. In such cases it is usual to take a mortgage over the security to control funds at settlement to clear the outstanding debt.

Given the banking adviser's view on the applicants' inability to service a principal and interest facility, I questioned the bank's statement, detailed at point 6 on page 3 of this Finding, that various loan options were outlined to the disputant and Mr H prior to them choosing an interest only facility.

The bank is aware of the banking adviser's opinion and has stated that the applicants would have qualified for alternative principal and interest products. It has provided Serviceability Calculator Spreadsheets to support its advice. It is noted that the alternative products were repayable over 30 year terms.

I have discussed the latest information provided by the bank with the banking adviser. He said that an "unwritten" principle of lending for asset purchases is that the loan term does not exceed the life of the asset to be purchased with loan funds. He said that seven years is normally the maximum allowable term for a loan approved to enable the purchase of a motor vehicle. I consider the "unwritten" principle to be commonsense.

Thus it is my opinion, given the disputant's age at the time when the application was made and the "life" of a motor vehicle, that the approval of a principal and interest home loan repayable over a 30 year term would not have been good banking practice. In other words it is my view that a line of credit facility was the only product that the bank should have approved. Good banking practice, however, required that the bank was satisfied as to the repayment source.

Sale of the Security Property

The bank says that sale of the security property was noted in the *Interview Comments* because the information was tendered by the applicants. Sale of the disputant's property was not a condition of the loan and the bank points out that even if it had been a condition it would have had no means of controlling its sale.

The bank emphasises that the loan was approved on the basis that the applicants met the bank's serviceability assessment. The serviceability test that the applicants met was the ability to meet the monthly interest only payments of $253.00.

The line of credit was approved to enable the applicants to purchase a four-wheel drive vehicle. There was no assessment of the applicants' ability to

repay the loan principal from their income in the anticipated "life" of the vehicle. Repayments of the required amount for a seven year principal and interest facility and indeed any significant repayments of principal to the line of credit were well beyond the means of the disputant and Mr H. In my opinion from the outset the sale of the security property was the only possible way in which the $44,000.00 facility could be repaid.

Summary

The disputant and Mr H submitted a joint loan application. The application took into account the advised, and verified, income of both applicants. The application was assessed using the bank's Serviceability Calculator and it met the bank's normal lending guidelines for a line of credit application. I consider that this product would have been a suitable product for the applicants if the disputant had already signed a contract to sell his property and the applicants were moving to Queensland. In such circumstances the bank would have been able to satisfy itself that the applicants would have the ability to repay the facility.

In this case the disputant's property had not been sold and indeed its sale, by some stated date, was not a condition of the loan. In effect the bank's approval of the facility ignored the fact that sale of the property was the only real prospect for repayment of the loan principal from the outset. I do not consider that the bank exercised "*the care and skill of a diligent and prudent banker*" when it approved the line of credit. I consider that there was maladministration involved in the lending decision.

3. Unconscionable Conduct

The disputant's son believes that the bank took advantage of his father's ill health and convinced him that a line of credit was suitable for his requirements. The disputant's son emphasises that his father did not understand the mechanics of the approved facility and that he had difficulty reading at the time when the loan offer was made. Additionally, the disputant has advised me that he was unwell on the day of the loan interview. He says that the interviewing officer was aware of his illness as he was forced to leave the interview room on a number of occasions.

The bank advises that the operation of the facility was discussed in the loan interview. The reason why the bank approved the line of credit has been discussed under heading 2.

With regard to the disputant's son's claim that his father was in poor health at the interview and could not read the loan offer, Ms B stated that "*The disputant did not indicate that he was ill, nor did he display symptoms of illness or discomfort during the loan interview. He did say that he had cataracts on his eyes, however this did not appear to affect his ability to complete the interview*

process. …The disputant did not leave the room at any time throughout the interview'.

Approach to assessing conflicting written information

There is significant conflict between the written accounts of the discussions and understandings provided by the disputant's son representing his father and the bank. In the light of the conflict and as this office cannot take evidence on oath nor cross-examine the parties I have:

(a) discussed:

(i) with the disputant his recollections of the loan interview and his knowledge and understanding of the terms and conditions of the contract; and

(ii) with Ms B her record of the loan interview and any other recollections she had of the loan interview; and

(b) looked for any objective information that may cast light on the discussions and understandings,

in order to reach a view as to whether at the time when the disputant entered into the contract:

- he suffered from a special disadvantage vis – vis the bank;
- the special disadvantage seriously affected his capacity to protect his own interests, and
- the bank was aware of the special disadvantage and took advantage of the opportunity presented by the disadvantage in circumstances where it was unconscionable to do so.

My discussions with the disputant

I have discussed the dispute on several occasions with the disputant. He told me that

(a) prior to applying for the loan he had known Mr H for over 25 years;

(b) he and Mr H were <u>both</u> keen to purchase a four-wheel drive vehicle and after discussions with a bank agent in the local town he and Mr H were hopeful that they would qualify for a loan to enable the purchase of a vehicle. He and Mr H told Ms B that they wanted to purchase a four-wheel drive;

(c) prior to the loan interview, on 14 May 2003, he travelled into the Melbourne Central Business District ("CBD") to collect the title deeds

to his property;

(d) he was feeling sick and giddy on the day of the loan interview and was forced to leave the interview room on several occasions;

(e) he was aware that his property was security for the loan;

(f) he did not take any legal advice regarding the loan or the loan condition that his property be security for the loan advance because he did not consider that there was any risk in his property being security as he did not think that there would be any problems;

(g) he did not tell Ms B that his home was going to be sold and that the line of credit would be cleared from the sale proceeds; and

(h) prior to the interview in May 2003 he had been thinking about visiting his nephew in Queensland but it was never certain that Mr H would make the trip and he did not tell Ms B he was going to Queensland.

Notwithstanding points (g) and (h) I am mindful that the disputant's son told me in a discussion on 17 May 2004 that he understood that his father had told the bank that he may be selling his house in the future to go and live in Queensland.

Discussion with Ms B

I discussed the loan interview with Ms B on 6 August 2004. She told me that she remembers the interview with the disputant and Mr H.

Ms B disputes the disputant's statement that he left the room on a number of occasions. She has no doubt that her loan interview comments accurately reflect what she was told in the interview. She told me that she would not have written that the disputant 's house was on the market and that he and Mr H were planning to move to Queensland if she had not been told, by both applicants, that this was the position.

Objective Information

The loan application completed by Ms B recorded the points detailed at (a), (b), (c) and (d) under the heading *The Loan Interview* on page 5 of this Finding. Based on Ms B's recommended approval of the facility a letter of offer and contract were generated on the afternoon of 14 May 2003.

The letter of offer advised the disputant that the bank had approved the credit application. It recommended that the disputant obtain legal advice regarding the terms and conditions of the loan offer prior to signing the loan documents. The loan contract includes details of the credit limit, refers to the facility as an

"*overdraft*", states the annual percentage rate applicable to the credit limit and nominates the disputant's property as security for the advance.

On 21 May 2003 the disputant and Mr H signed the loan contract and mortgage documents at the office of the bank's agent in the local town. The disputant has known Mr A for many years and if he had chosen he could have clarified any term or condition with Mr A. On the same day both loan applicants signed an Acknowledgment of Loan Protection Options form. The disputant also signed a Loan Contract Form of Acknowledgment (Attachment A). The disputant indicated on the form that he had read the loan contract, elected to sign the contract after deciding not to obtain legal advice and that he understood his obligations under the contract.

Special Disadvantage that affected the disputant's capacity to protect his own interests?

The parties disagree as to whether the bank was on notice that the disputant felt ill on the day of the interview. The disputant in one of our discussions advised me that he was not in a sound state of mind when he decided to go ahead with the loan. I understood the disputant to be referring to not feeling well at the time of the interview and/or his forthcoming eye operation. Ms B knew about the disputant's cataracts but advises that it did not affect his ability to complete the interview process.

Given that Mr H is a generation younger than the disputant I have looked for any information that may indicate that the disputant was under the influence of Mr H at the time when he entered into the contract.

The disputant in discussions with me was clear. He, as well as Mr H, wanted the vehicle and he was aware that his home would be security for the advance. Prior to the loan interview he had visited the CBD to collect the title deeds. He did not consider that legal advice was necessary because he did not believe that anything would go wrong.

The disputant told me that as 2003 progressed he became increasingly dissatisfied with Mr H's behaviour and his failure to carry out his duties as his carer. On 19 December 2003 the disputant evicted Mr H from his home and notified Centrelink that Mr H was no longer his carer.

I am satisfied, after speaking with the disputant and Ms B, that the disputant did not suffer from any special disadvantage that affected his capacity to protect his own interests. I am satisfied that the bank's conduct in approving the loan was not unconscionable.

4. <u>Benefit from the Line of Credit</u>

The disputant and Mr H benefited from the line of credit in that they purchased a vehicle in May 2003. Unknown to the bank, the vehicle was initially registered in Mr H's name.

In December 2003 Mr H left the disputant's home and took with him the vehicle. In early February 2004 the disputant's son took possession of the vehicle and in May 2004 Mr H signed transfer papers and the ownership of the vehicle was transferred to the disputant.

In late May 2004 the disputant advised this office that he planned to carry out some necessary repairs to the vehicle, have it detailed, use it for several weeks and then sell it and pay the sale proceeds to the joint line of credit account.

On 8 July 2004 the disputant's son advised this office that as he and his father were unable to obtain a fair and reasonable price for the vehicle he, with his father's consent, had traded the vehicle in on another vehicle for himself. The price obtained as a trade in was $26,000.00. The disputant's son said that he had arranged to repay the $26,000.00 to his father on a monthly basis. No issue has been raised by the disputant in relation to this arrangement and I must assume that it has been made with his informed consent.

The disputant has subsequently stated to me that he and his son did not attempt to sell the vehicle privately but rather elected to sell it to a car dealer. While it is not possible to say with any precision what price may have been received for the vehicle if it had been sold privately I am mindful that no attempt was made to sell the vehicle by that means. 'The Age' classified section provides a vehicle valuation service. That service indicates that for the particular vehicle private sale prices are in the order of $3,000.00 to $4,000.00 higher than trade-in values.

A claimant such as the disputant has a duty to mitigate any direct loss he has suffered as a result of the bank's decision to approve the line of credit facility. In agreeing to use the vehicle as a $26,000.00 trade in on a vehicle for his son, rather than sell the vehicle and apply the proceeds to reduce the principal debt and limit interest, the disputant has failed to mitigate his loss in that amount. Unless the repayments the disputant's son pays to his father are paid by the disputant direct to the loan account the disputant will have taken no action to mitigate the interest charge debited to his line of credit account.

The present rate applicable to the disputant's joint facility is 7.6%. In effect the additional monthly interest charge as a result of the disputant's decision to effectively "gift" the $26,000.00 to his son rather than pay $26,000.00 to his account, is approximately $165.00.

Notwithstanding:

(a) the loan approval enabled the disputant and Mr H to purchase a vehicle they desired; and

(b) the contemporaneous documents indicating that sale of the security property was discussed at the loan interview,

I consider the bank's decision to approve an open ended secured credit facility for two pensioners with no significant asset besides the disputant's property was maladministration in lending.

The disputant has benefited from the approval in that the vehicle was transferred to his name in May 2004 and subsequently used as a trade-in on a vehicle for the disputant's son. After taking into account my view on maladministration in lending and the benefit the disputant has received (and gifted to his son) I consider that the disputant 's liability for the line of credit facility secured by a mortgage over his home should be reduced to $29,500.00. This amount reflects the $26,000.00 received as a trade in for the land cruiser and a $3,500.00 allowance for an additional amount that may have been received via a private sale.

Finding

In my view:

1. The information available indicates that the sale of the disputant's property was the only real prospect for the repayment of the joint line of credit. The bank did not exercise sufficient care when making the decision to approve the loan ;

2. Notwithstanding point 1 the bank's decision to approve the loan was not unconscionable; and

3. The disputant's line of credit debt should be reduced to $29,500.00 as from 30 September 2004.

Banking and Financial Services Ombudsman Limited

ABN 48 050 070 034

FINDING 3*

Date: **2 August 2005**

Subject matter: **EFT Code dispute – unauthorised withdrawals – whether reasonable attempt to protect the security of a code record that was stored with a card – whether unreasonable delay in notifying bank that card lost or stolen**

The following is the Finding I have reached in the case of the disputant and the bank.

Investigation

I have reviewed all of the information provided by the disputant and the bank.

Background Information

1. The disputant had a line of credit account facility ("the account");

2. On 24 November 2004 a card that accessed the account was stolen;

3. A total of $5,800 was withdrawn from the account on the day of the theft and the following day, as per the table below:

Date	Time	Location	Amount	Response
24/11/04	12:28:40	[name of bank]ATM [name of] Hotel	$ 200.00	Approved
24/11/04	12:29:24	" "	$ 500.00	Approved
24/11/04	12:30:03	" "	$ 500.00	Approved
24/11/04	12:30:40	" "	$ 500.00	Approved
24/11/04	12:31:18	" "	$ 500.00	Approved
24/11/04	12:33:42	" "	$ 500.00	Approved
24/11/04	17:50:06	Credit Union ATM [location]	$ 100.00	Approved
25/11/04	04:40:30	Credit Union ATM [location]	$2,000.00	Approved
25/11/04	04:41:30	" "	$1,000.00	Approved
		Total amount withdrawn	**$5,800.00**	

4. The disputant does not accept that he should be liable for the losses resulting from the unauthorised transactions.

The Disputant's Position

* This Finding has been edited for external publication and the parties de-identified.

The disputant's position, summarised from different sources, is as follows:

1. In a letter to the bank dated 3 December 2004 he said that:

    a) fraudulent activity had taken place on the account, resulting from a burglary at his home on 24 November 2004 and the subsequent theft of his card;

    b) he was not aware of the theft of the card until 3 December 2004, when he was informed that his account had been drawn to the limit; and

    c) all [card] transactions since the burglary were fraudulent and were not made by him;

2. In a statutory declaration dated 13 December 2004 he said that:

    a) the burglary happened between the time he left for work at 7:30am and the time he arrived home at 5:30pm;

    b) he had never used the card;

    c) the card was stolen from his top dresser drawer together with the PIN; and

    d) no other person had access to his card and PIN;

3. In a letter to the bank dated 13 December 2004 (that accompanied the statutory declaration) he said that:

    a) he only ever operated the account through the cheque book attached to the account;

    b) the card had been stored with the original correspondence, which apparently included the PIN; and

    c) he was anxious about the extent of his liability with respect to the debt;

4. After the bank allocated liability to him by letter dated 25 January 2005, the disputant wrote to the Ombudsman on 14 February 2005. In that letter he made the following additional points:

    a) on his return home on 24 November 2004 and his discovery of the burglary, he telephoned the bank (around 5:30/6:00pm) to ascertain whether a card was attached to the account. He did this because he had never used a card on the account, and he was unsure whether a card had been issued. He wanted to be sure that fraud could not be undertaken in the event that a card had been stolen;

b) the bank informed him [on 24 November 2004] that a card did not exist on the account;

c) he had not unreasonably delayed in notifying the bank because he contacted the bank on the day of the theft. In any case, he again notified the bank as soon as he became aware of the fraudulent transactions [on 3 December 2004];

d) the bank's terms and conditions stated that, in the event of theft, any liability was restricted to the daily transaction limit – which he understood to be $500; and

e) he considered that the inadvertent holding of the card and PIN in a locked drawer should not in itself make him liable for any subsequent fraudulent activity.

Bank Response

The bank's response to the dispute was as follows:

1. Information about the card and PIN included that:

   a) the card was first issued on 14 October 1994;

   b) the PIN was generated by the bank and issued about five days after the card;

   c) the most recent card [the card that was stolen] was issued on 18 July 2003;

2. Information about the daily withdrawal limit included that:

   a) prior to April 2000, the card had a daily withdrawal limit of $1000;

   b) from April 2000, the daily withdrawal limit was increased to $3,000; and

   c) from February 2005, the daily withdrawal limit was reduced back to $1,000;

3. In its letter dated 25 January 2005, the bank allocated liability to the disputant because:

   a) there was unreasonable delay in notifying the bank about the theft of the card because the unauthorised withdrawals commenced on 24 November 2004 but the bank was not notified until 3 December 2004; and

   b) the card and the PIN were liable to loss or theft simultaneously because both card and PIN were situated in the top dresser drawer at

the time of the theft;

4. After the dispute was lodged was lodged with the Ombudsman, the bank continued to maintain that the disputant was liable for the unauthorised withdrawals; and

5. In response to the disputant's claim that he had rung the bank on 24 November 2004, the bank said that it had searched its phone logs for contact from the disputant during November and December 2004 and the only record of contact was on 3 December 2004. Consequently, the bank did not accept the disputant's statement that he rang the bank on 24 November 2004.

Documents

I have reviewed the following documents:

1. Statements for the disputant's credit account from 15 July 2004 to 14 December 2004;

2. Transaction logs summarising all attempts to use the disputant's card, whether successful or unsuccessful;

3. Statutory declaration made by the disputant on 13 December 2004;

4. Various items of correspondence originating from the disputant, the bank, and this office; and

5. Extract from tax invoice issued by AAPT Ltd, listing calls to "13" numbers from 19/11/04 to 3/12/04.

A copy of the extract from the AAPT Ltd invoice is attached to this Finding.*

Other Information

I have also taken into account the following information:

1. There were unsuccessful attempts to access the account, in addition to the successful attempts noted above. The table below lists all attempts, including the unsuccessful attempts (which are shaded in order to distinguish them).

Date	Time	Location	Amount	Response
24/11/04	12:28:40	[name of bank] ATM, [name of hotel]	$ 200.00	Approved
24/11/04	12:29:24	" "	$ 500.00	Approved
24/11/04	12:30:03	" "	$ 500.00	Approved
24/11/04	12:30:40	" "	$ 500.00	Approved
24/11/04	12:31:18	" "	$ 500.00	Approved
24/11/04	12:33:42	" "	$ 500.00	Approved
24/11/04	12:34:19	" "	$ 500.00	Denied: Exceeds

* Not attached to this copy of the Finding for de-identification reasons

				withdrawal limit
24/11/04	17:50:06	Credit Union ATM [location]	$ 100.00	Approved
24/11/04	17:50:38	" "	$ 500.00	Denied: Exceeds withdrawal limit
24/11/04	17:50:49	" "	$ 100.00	Denied: Exceeds withdrawal limit
24/11/04	17:50:58	" "	$ 100.00	Denied: Exceeds withdrawal limit
24/11/04	17:51:07	" "	$ 100.00	Denied: Exceeds withdrawal limit
25/11/04	04:40:30	Credit Union ATM [location]	$2,000.00	Approved
25/11/04	04:41:30	" "	$1,000.00	Approved
		Total amount withdrawn	**$5,800.00**	

2. Information from AAPT Ltd, the disputant's telephone service provider, shows that the disputant called the bank's "13" number on 24 November 2004 and on 3 December 2004. The duration of the call on 24 November was 8 minutes 48 seconds.

Issues

The issues raised by the case include:

1. Were the disputant's card and PIN liable to loss or theft simultaneously?

2. Had the disputant made a reasonable attempt to protect the security of his PIN record?

3. Was the daily transaction limit exceeded?

4. Can it be ascertained whether the disputant contacted the bank on 24 November 2004 and, if he did so, had he effectively notified the bank about the theft of his card?

5. How should liability for the unauthorised transactions be allocated between the disputant and the bank?

Electronic Funds Transfer Code of Conduct

When considering complaints about disputed EFT transactions, the Ombudsman takes into account the requirements of the Electronic Funds Transfer Code of Conduct ("EFT Code").

A summary of the liability provisions of the EFT Code is attached as Appendix A.

The provisions that are most relevant to this dispute include that:

1. The account holder is liable if the user contributes to losses by:

   a) unreasonably delaying notification after becoming aware of the misuse, loss or theft of a device [i.e. a card] forming part of the access

method; or

b) keeping a record of the code [i.e. the PIN] (without making any reasonable attempt to protect the security of the code record) that is liable to loss or theft simultaneously with the device;

2. The account holder has no liability for losses resulting from unauthorised transactions occurring after notification to the account institution that a device has been misused, lost or stolen; and

3. An account holder's liability does not include that portion of the losses incurred on any one day that exceeds the applicable daily transaction limit.

Safety of the Electronic Payments System

The safety and efficiency of the electronic payments system in Australia is the responsibility of the Payments System Board. The Ombudsman does not have the power to monitor the security of the system himself.

However, this office approaches disputes on the basis that the Payments System Board is satisfied that the electronic payments system has reasonable security standards.

In the case of a disputed transaction made with a card and PIN, this office is satisfied that:

1. In order to successfully withdraw funds electronically two elements must be present, i.e. a card and the PIN for that card number; and

2. It is not possible to gain knowledge of a PIN through mere possession of a card, because the PIN is not recorded on a card's magnetic strip.

Application of the EFT Code to the Dispute

<u>Were card and PIN liable to loss or theft simultaneously?</u>

The Ombudsman's policy with regard to the meaning to be given to the word "simultaneously" is that "simultaneous" loss or theft would occur where a card and a PIN record are:

- in the same receptacle which itself can be lost or stolen (for example, a handbag, briefcase or suitcase); or

- in the same location within the same room (for example, on the same desktop or tabletop, or in the same drawer or box) so that the card and PIN record can be seen together and taken at the same time.

On the information provided, both the card and the original PIN record were stored together in the same top dresser drawer.

Consequently, I am satisfied that the PIN record was liable to loss or theft simultaneously with the card.

Was a reasonable attempt made to protect the security of the PIN record?

Keeping a PIN record that is liable to loss or theft simultaneously with a card is sufficient to make an account holder liable for unauthorised transactions, **unless** a reasonable attempt was made to protect the security of the code record.

Clause 5.8(a) of the EFT Code explains that "reasonable attempt to protect the security of a code record" includes either or both of:

- making any reasonable attempt to disguise the code within the record; or
- taking reasonable steps to prevent unauthorised access to the code record.

An endnote to the EFT Code further explains that "reasonable steps to prevent unauthorised access" may involve hiding or disguising the code record among other records or in places where a code record would not be expected to be found, by keeping the record of the code in a securely locked container, or preventing unauthorised access to an electronically stored record of the code.

On the information provided, no attempt was made to disguise the PIN record. Accordingly, it is only necessary to consider whether or not the disputant took reasonable steps to prevent unauthorised access to the PIN record. This depends on whether the top dresser drawer in which the PIN was stored could be regarded as a "securely locked container".

The first mention of the way in which the PIN was stored is in the statutory declaration dated 13 December 2004, in which it is stated that:

> *"The relevant card had never been used and was stolen from my top dresser drawer together with PIN."*

The first mention of the drawer being locked is in the letter to the Ombudsman dated 10 February 2005, in which it is said that:

> *"Accordingly, I contend that the inadvertent holding of the card and PIN in a locked drawer…should not in itself make me liable for any subsequent fraudulent activity."*

During the course of the investigation, I asked the disputant if he could substantiate that the drawer was locked. I also asked him to explain how a thief could have gained possession of both card and PIN if the drawer was locked. His response was that:

> *"I cannot now substantiate that the drawer was locked – the drawer was jemmied (easily done) and was the only drawer in the 8 drawer dresser that was disturbed, as evidenced by the Police when they attended shortly after to fingerprint the residence. Since my move to another residence, the dresser has been disposed of."*

After considering all this information, including that the drawer was easily jemmied even if it had been locked, my view is that the PIN record was not kept in a securely locked container.

As the PIN record was neither disguised nor kept in a securely locked container, I am satisfied that the disputant had not made a reasonable attempt to protect the security of the PIN record.

Consequently, I am satisfied that the disputant contributed to the losses resulting from the unauthorised transactions by contravening the requirement not to keep a PIN record (without making a reasonable attempt to protect the security of the PIN record) that was liable to loss or theft simultaneously with the card.

Was the daily transaction limit exceeded?

The EFT Code does not prescribe what the transaction limit should be for card and PIN transactions. Each financial institution that issues cards in Australia has the right to set its own daily and periodical transaction limits, and the right to vary limits from time to time. The only circumstance in which the Ombudsman would be concerned about the quantum of a daily transaction limit would be if a particular financial institution applied a daily limit that was not reasonable having regard to prevailing industry practice.

In the experience of the Ombudsman's office, typical daily transaction limits set by financial institutions that are members of the Banking and Financial Services Ombudsman scheme range from a low of $800 to a high of $3,000. The Ombudsman regards daily limits within this range as being reasonable having regard to prevailing industry practice.

The information provided by the bank indicates that the daily limit for the disputant's card was $3,000 at the time of the unauthorised transactions. I acknowledge that the bank reduced the daily limit to $1,000 some three months later. However this reduction does not mean that the daily limit that applied in November 2004 was not reasonable.

On balance, I am satisfied that the unauthorised withdrawals (of $2,800 on the first day and $3,000 on the second day) did not exceed the daily transaction limit for the card and the account.

When did the disputant report the loss of his card?

The time at which the disputant reported the theft of his card to the bank has an important bearing on the extent of his liability for the unauthorised transactions. This is because the disputant is liable for the losses on the grounds of keeping a PIN record that was liable to loss or theft simultaneously with the card. However, his liability ceases from the time that he notified the bank that his card was lost or stolen.

Accordingly, if the disputant did not notify the bank until 3 December 2004, he is liable for the full amount withdrawn from his account. However, if it was substantiated that

he called the bank on the evening of 24 November, he might only be liable for the amount withdrawn ($2,800) before his call.

According to the bank, it searched its phone log records during November and December 2004 for all record of contact from the disputant. The bank says that the only record it has is of the disputant's call on 3 December 2004.

During the course of the investigation, the disputant was asked to detail the number on which he had called the bank. He was also invited to substantiate from phone company records that he had called the bank on 24 November 2004. In response, the disputant has provided an extract from a tax invoice issued by AAPT Ltd. The record of calls to "13" numbers substantiates that:

1. The disputant placed a call to the bank on its "13" number on 24 November 2004 at 6:28pm, with the duration of the call being 8 minutes 48 seconds; and

2. The disputant placed three calls to the bank on its "13" number on 3 December 2004, starting at 11:14am and with the duration of the longest call being 24 minutes 10 seconds.

With regard to the content of the call on 24 November 2004, the disputant said, in a fax dated 2 August 2005, that:

> *"I appraised the operator of the reason for my call, that I had been broken into and a number of goods stolen, and enquired of the Bank whether I had a card attached to my [name of] account, as I was not sure whether I had such a card as I had always operated the account via a cheque book and, in view of the mess in my home, was not sure what had been stolen.*
>
> *The staff member handling my query, after looking at my file stated that no, I did not have any credit card with the Bank and that I had no credit card debt with the Bank. I then assumed (wrongly) that my name of facility] was not at risk as the check book was located in amongst the mess on my bed where the drawer had been upturned."*

In considering this issue, I note from information provided from the bank that:

1. The account is a revolving line of credit account that is comparable to a Visa or MasterCard account; however

2. The card that accessed the account was a debit card rather than a credit card.

The main difference between the card and a bank-issued Visa card or MasterCard lies in the way purchase transactions are transacted. Both the card and a Visa/MasterCard can be used to withdraw cash at ATMs, with authorisation being made by PIN entry. However, when it comes to purchases, it seems that transactions using the particular card would also be authorised by PIN entry, whereas Visa/MasterCard transactions would be authorised by signature.

If the disputant had asked a bank operator if he had a bank-issued credit card, it would have been technically correct for the operator to advise that there was no credit card issued on the account. However, as the disputant say he asked *"whether I had a card attached to my [name of] account"*, the expectation of this office is that a bank operator would have checked for both debit cards and credit cards attached to the account.

As the disputant has substantiated that he called the bank on 24 November 2004, whereas the bank has not apparently logged the call and therefore cannot provide any summary of the call, my view is that I should accept the disputant's account of the content of the call.

Accordingly my view is that the disputant's call to the bank at 6:28pm on 24 November 2004 can be taken as effective notification that the card had been stolen because:

- any search of the bank's data base should have turned up the card; and
- if the existence of the card had been mentioned to the disputant, there seems no doubt that he would have reported it as stolen.

Consequently, my view is that the disputant's liability for the unauthorised transactions should be taken as having ceased at 6:28pm on 24 November 2004, and that the disputant is not liable for any unauthorised transactions made after that time.

How should liability for the unauthorised transactions be allocated?

For the reasons discussed above, I am satisfied that the disputant contributed to the losses resulting from the unauthorised transactions because he contravened the requirements of the EFT Code (and the bank's Conditions of Use) by keeping a record of the PIN that was liable to loss or theft simultaneously with the card, without making any reasonable attempt to protect the security of the PIN record.

Therefore, the disputant is liable for all unauthorised transactions made before the time that he notified the bank that his card was lost or stolen.

For the reasons discussed above, I am satisfied that the disputant should be taken as having effectively notified the bank that his card was lost or stolen at 6:28pm on 24 November 2004.

Therefore, my view is that the disputant is liable for the unauthorised withdrawals that were made prior to 6:28pm on 24 November, in the amount of $2,800. However, the disputant is not liable for the unauthorised withdrawals that were made on 25 November 2004, in the amount of $3,000.

Finding

In my view:

1. The disputant is liable for the unauthorised withdrawals amounting to $2,800 made on 24 November 2004;

2. The disputant is not liable for the unauthorised withdrawals amount to $3,000 made on 25 November 2004; and

3. The bank should refund $3,000 to the disputant, together with an adjustment for interest on this amount that was charged to the account from 25 November 2004 to the date of settlement.

Appendix A: Summary of liability provisions of the EFT Code

The Electronic Funds Transfer Code of Conduct ("EFT Code") is a government-sponsored code of conduct that is administered by the Australian Securities & Investments Commission ("ASIC"). The EFT Code is binding on account institutions that notify ASIC that they have subscribed to the EFT Code. The full text of the EFT Code can be downloaded from the ASIC website: www.asic.gov.au

The bank, as a subscriber to the EFT Code, warrants in its Terms and Conditions for electronic banking that it will comply with the requirements of the EFT Code. Those requirements include that the bank's Terms and Conditions will not provide for or be effective to create liabilities and responsibilities of users which exceed those set out in the EFT Code. (A "user" means a person, including the account holder, who is authorised to access an account).

Allocation of liability for unauthorised transactions

The EFT Code contains a number of provisions about the allocation of liability for unauthorised transactions. These provisions, however, do not apply to any transaction carried out by the user or by anyone performing a transaction with the user's knowledge and consent.

Clause 5 of the EFT Code deals with the allocation of liability for unauthorised transactions. The main points are:

1. Where it is clear that the user has not contributed to the losses, the account holder has no liability for losses resulting from unauthorised transactions;

2. The account holder also has no liability for losses that occur after notification to the account institution that a device [i.e. a card] forming part of the access method has been misused, lost or stolen or that the security of codes [e.g. a PIN or password] forming part of the access method has been breached;

3. The account holder is liable for losses where the account institution can prove on the balance of probabilities that the user contributed to the losses through:

   - fraud; or

   - contravention of certain requirements; or

   - unreasonably delaying notification after becoming aware of the misuse, loss or theft of a device or that the security of codes has been breached.

   Where a user has contributed to losses by unreasonably delaying notification, the account holder is liable for the actual losses which occur between when the user became aware (or should reasonably have become aware in the case of a lost or stolen device) and when the account institution was actually notified.

4. Even where an account holder is otherwise liable for unauthorised transactions, their liability does not include:

    - that portion of the losses incurred on any one day that exceeds the applicable daily transaction limit;

    - that portion of the losses incurred in a period that exceeds any other periodic transaction limit applicable to that period;

    - that portion of the total losses incurred on an account which exceeds the balance of that account (including any prearranged credit); and

    - all losses incurred on any accounts which the account institution and the account holder had not agreed could be accessed using the access method;

5. Where the account institution cannot prove on the balance of probabilities that the user contributed to the losses, and provided that a code was required to perform the unauthorised transaction, the account holder is liable for no more than $150.

The EFT Code states that when determining whether an account institution has proved on the balance of probabilities that a user has contributed to losses, all reasonable evidence, including all reasonable explanations for the transaction occurring, must be considered. The EFT Code also states that the fact that the account has been accessed with the correct access method, while significant, will not of itself constitute proof on the balance of probabilities that the user contributed to the losses through fraud or through contravening certain requirements of the EFT Code.

<u>Contravention of specified requirements</u>

The user contravenes the requirements of the EFT Code if the user:

1. Voluntarily discloses one or more of the codes to anyone, including a family member or friend; or

2. Where the access method uses a device, indicates one or more of the codes on the outside of the device, or keeps a record of one or more of the codes (without making any reasonable attempt to protect the security of the code records) that are liable to loss or theft simultaneously with the device; or

3. Where the access method comprises a code or codes without a device, keeps a record of all the codes (without making any reasonable attempt to protect the security of the code records) on the one article, or on several articles so that they are liable to loss or theft simultaneously; or

4. Selects a code which represents the user's birth date or a recognisable part of the user's name, provided that immediately before the user's selection or change of the code the account institution specifically instructed the user not to do so and warned the user of the consequences of such a selection; or

5. Acts with extreme carelessness in failing to protect the security of all the codes.

Self selection of code

With regard to selection of a code that represents a user's birth date or name, the onus is on the account institution to prove on the balance of probabilities that it gave the specific instruction and warning to the user at the time specified and in a manner designed to focus the user's attention specifically on the instruction and the consequences of breaching it.

Reasonable attempt to protect the security of a code record

For the purposes of the EFT Code, a reasonable attempt to protect the security of a code record includes either or both of:

1. Making any reasonable attempt to disguise the code(s) within the record; or

2. Taking reasonable steps to prevent unauthorised access to the code record.

End note 20 to the EFT Code explains that "reasonable steps to prevent unauthorised access" may involve hiding or disguising the code record among other records or in places where a code record would not be expected to be found, by keeping a record of the code in a securely locked container or preventing unauthorised access to an electronically stored record of the code.