THE FINANCIAL OMBUDSMAN SERVICE

circular

ISSUE 10 - WINTER 2012

CONTENTS

CHIEF OMBUDSMAN'S MESSAGE

Welcome to the Winter 2012 issue of *The Circular*.

You'll notice that this issue looks quite different to previous issues. We have refreshed the design, format and structure of The Circular to make it even more engaging and easy to navigate.

So that you will be able to quickly peruse the contents of each issue and find the articles you are most interested in, we will be using a consistent set of sections in every issue. The new sections – and an idea of what they will cover – are as follows:

- **The FOS Approach** – articles on our dispute-handling process and our approach to specific types of disputes and issues
- **FOS News** – the latest information about our training programs, events, publications, resources and major projects
- **FOS Forum** – broader and more personal discussions about dispute resolution in the financial services sector, including 'day in the life' profiles, interviews and tips
- **Systemic Issues** – quarterly updates on the systemic issues we are investigating or have resolved
- **Case Studies** – examples of how we approach specific types of disputes
- **Statistics** – quarterly reports on the numbers of disputes we have received and closed.

The dispute statistics are a new feature. We want to publish quarterly updates so that you can follow the trends in the volume and types of disputes we receive and the volume and outcomes of the disputes we resolve. We are also planning, in future issues, to include extra data reports that spotlight particular products or issues.

You will also see a renewed focus on case studies in *The Circular*. We have always included case studies in *The Circular*, but we wanted to include more of them and make them easier to find. Most articles in the 'FOS Approach' section will include a case study. You can also find all the case studies in an issue grouped together in the 'Case Studies' section.

One of the FOS News articles in this issue, 'Changes at FOS', outlines some structural changes we are making at FOS – in particular, the introduction of three Executive General Manager roles and a new Senior Leadership Group. These changes, which will take effect in July/August this year, are designed to ensure that FOS has the structure and resources to thrive over the next three years.

We hope you like the new *Circular* and we welcome your feedback on it. You can email feedback and suggestions to publications@fos.org.au.

Regards,

Shane Tregillis

NOTIFYING THIRD PARTY BENEFICIARIES OF DEROGATIONS FROM PRESCRIBED TERMS OF INSURANCE CONTRACTS

A financial services provider (FSP) can provide a contract of insurance that derogates (ie deviates) from the terms and conditions prescribed in the *Insurance Contracts Regulations 1985*.

Third party beneficiaries may derive a benefit under an insurance policy but are not an actual party to the insurance contract. For example, in the case of travel insurance that a consumer obtains through their bank, the bank is a party to the insurance contract and the consumer is a third party beneficiary.

Examples of the types of insurance contracts that can extend to third party beneficiaries are travel insurance, income protection insurance and group personal accident and sickness insurance. This is not an exhaustive list.

The *Insurance Contracts Act 1984* (ICA) has defined certain classes of insurance contracts as 'prescribed contracts'. These are:

- home building
- home contents
- motor vehicle
- travel
- personal accident and sickness
- consumer credit.

The *Insurance Contracts Regulations 1985* outlines the terms and conditions applicable to each class of prescribed contract.

If an FSP wishes to derogate from a prescribed term in a prescribed contract (for example, by excluding flood cover under a home building policy), section 35 of the ICA requires the FSP to clearly inform the insured in writing of the derogation before the contract is entered into. If it is not reasonably practicable to give written information within that timeframe, section 69 of the ICA extends the timeframe where certain conditions are met. Section 69 may operate, for instance, if a policy is entered into over the telephone. Section 13 of the ICA requires parties to a contract of insurance to act towards each other with utmost good faith.

We recognise that sections 13 and 35 of the ICA do not apply in relation to third party beneficiaries. While the legislation is silent on whether an FSP should clearly inform third party beneficiaries of derogations from prescribed terms, common law principles relating to 'good faith' and 'fair dealing' are sufficiently broad in application to extend to third party beneficiaries.

Paragraph 8.2 of our Terms of Reference requires us, when deciding a dispute and deciding whether a remedy should be provided, to do what in our opinion is fair in all the circumstances, taking into account:

- legal principles
- applicable industry codes or guidance on practice
- good industry practice
- previous decisions made by us or our predecessor schemes (although they are not binding).

FOS takes the approach that to meet the principles relating to 'good faith and fair dealings' FSPs must be able to show they have provided adequate notification to potential third party beneficiaries of any derogation from standard cover.

We will not allow an FSP to rely on a derogation from prescribed terms that adversely affects a third party beneficiary if the beneficiary has not been adequately notified of the derogation. Adequate notification will not necessarily involve providing documentation to third party beneficiaries. However,

to establish adequate notification, an FSP would at least need to demonstrate that a clear process was in place with the insured to ensure the contract's terms and conditions were made available to third party beneficiaries.

If an FSP fails to ensure third party beneficiaries are adequately notified of any derogation from prescribed terms, it runs the risk that it will not be able to rely on the derogation in any dispute that comes before FOS.

The following case studies are practical examples of how we approach this issue.

CASE STUDY 1:

DEVIATION FROM A PRESCRIBED CONTRACT – TRAVEL INSURANCE

An insurer provided Sharon's bank with travel insurance for her and other customers who held a bank credit card.

While Sharon was overseas, her travel bag, laptop and a number of other items were stolen from a train's baggage storage area. The insurer rejected Sharon's insurance claim, relying on a policy exclusion for items left unattended in a public area. Sharon brought her dispute to FOS.

FOS noted that travel insurance is a 'prescribed contract' for which the Insurance Contracts Regulations 1985 set out prescribed terms. The prescribed terms for travel insurance contracts do not exclude unattended baggage.

Neither the bank nor the insurer could show they had made a copy of the insurance policy available to Sharon. FOS said it would have been fair in these circumstances for the credit card holders to have been informed of this exclusion.

FOS also said the insurer could have informed the credit card holders directly through appropriate documentation. Alternatively, the insurer could have directed credit card holders to a publication of the relevant exclusion on its or the bank's website.

FOS considered that it was not fair in these circumstances for the insurer to rely on its policy exclusion.

CASE STUDY 2:

DEVIATION FROM A PRESCRIBED CONTRACT – CONSUMER CREDIT INSURANCE

Sean, who ran a small business, held a credit card provided by a bank. The bank informed consumers about an insurance policy provided by an insurer. The policy provided cover to repay a credit card balance where the card holder became involuntarily unemployed or permanently disabled or died during the period of insurance. In this arrangement, the card holder was a 'third party beneficiary' under a contract of insurance between the bank and the insurer. Sean decided to take out the insurance.

Sean had a large balance on his credit card when his business went into liquidation. He could not repay any of the balance and made a claim under the insurance policy.

The insurer denied the claim, relying on an exclusion clause in the policy. It stated the policy did not cover anyone who was self-employed when the event giving rise to their claim occurred.

Sean lodged a dispute with FOS, arguing that the insurer could not rely on the exclusion clause. He said he was unaware of the terms of the policy and would not have obtained the cover if he had known of the exclusion clause. He also said he had told the bank about his working arrangements when he obtained the cover.

Neither the bank nor the insurer could show that they had made a copy of the policy available to Sean.

Could the insurer rely on the exclusion clause to deny the claim?

The policy is a consumer credit insurance contract, which is a 'prescribed contract', for which the *Insurance Contracts Regulations 1985* set out prescribed terms. The prescribed terms for consumer credit insurance contracts do not exclude cover for self-employed people. So the exclusion in this case amounts to a derogation (that is, a deviation) from the prescribed terms.

Sean had established he had become involuntarily unemployed. The insurer had not taken any action to notify Sean of the exclusion clause. Therefore, it was not fair for the insurer to deny the claim.

We required the insurer to pay the balance on Sean's credit card and interest in accordance with section 57 of the *Insurance Contracts Act 1984*.

STATEMENTS OF ADVICE MUST BE CLEAR, CONCISE AND EFFECTIVE

The Corporations Act 2001 generally requires financial services providers (FSPs) to give a Statement of Advice[1] (SOA) to retail clients who receive personal financial advice.1 This requirement is designed to ensure retail clients are given enough information for them to understand the personal advice given to them and decide whether or not to rely on it.[2] The statements and information in an SOA must be worded and presented in a "clear, concise and effective" manner.[3]

We handle many financial advice disputes in which a retail client says they did not understand the advice they received from the FSP. In these disputes, the quality and clarity of the information in the SOA is a critical issue.

THE ISSUE OF INFORMED CONSENT

The question of whether a retail client has given their informed consent to take up the FSP's advice is a critical issue in the majority of financial advice disputes handled by FOS.

Where this issue is raised, we will look at all of the disclosures made by the FSP to the client. A key document in this regard is the SOA.

If the information in the SOA is not "clear, concise and effective", then FOS might find that the client did not understand the advice and the FSP had failed to secure the client's informed consent to take up the advice.

WHAT DOES "CLEAR, CONCISE AND EFFECTIVE" MEAN?

The phrase "clear, concise and effective" is not defined in the Corporations Act. This means the words must be given their natural meaning.

According to the *Macquarie Concise Dictionary*:[4]

- "clear" means "free from obscurity … confusion, uncertainty or doubt" and "in plain language"
- "concise" means "brief and comprehensive; succinct; terse"
- "effective" means "producing the intended or expected result".

When looking at whether information in an SOA is clear, concise and effective, we will consider whether the information:

- is expressed in plain language
- is brief yet comprehensive
- promotes understanding of the adviser's recommendations.

This approach is consistent with:

- ASIC's guidance in Regulatory Guide 175: Financial Product Advisers – Conduct and Disclosure[5]
- the Financial Planning Association's Code of Professional Practice.[6]

WHAT FACTORS DOES FOS CONSIDER?

When we consider whether or not an FSP secured a client's informed consent to take up advice, we will examine the SOA provided to the client and consider the following questions:

1 Section 946A of the *Corporations Act*
2 2ASIC *Regulatory Guide 175* at RG 175.153.
3 Subsections 947B(6) and 947C(6) of the *Corporations Act*.
4 3rd edition (2004), Macquarie Press.
5 Published April 2011. See paragraphs RG175.188 to RG175.192 (inclusive).
6 See Rules 4.11 and 4.12.

1. Did the FSP consider the client's experience, language skills, literacy and numeracy?

FSPs that do not make a reasonable assessment of a client's experience, language skills, literacy and numeracy are much more likely to prepare an SOA that the client will not understand and more likely to be found to have breached their duty to secure the client's informed consent to take up the advice.

Remember, each client is unique.

2. Did the SOA use language the client was likely to understand?

An SOA which does not use language the client is likely to understand cannot be effective.

It is important to note that the question is an objective one. In other words, we do not consider whether the client subjectively understood the information in the SOA. We only need to be satisfied that the client was likely to understand the language used in the SOA, assessed objectively, having regard to their experience, language skills, literacy and numeracy.

See the case study below for an example of how FOS objectively assesses a client's understanding of an SOA.

3. Did the SOA use legal, industry or technical language?

This question is closely related to question 2.

SOAs that use legal, industry or technical language are less likely to be "clear, concise and effective" if the client is unfamiliar with these types of language. If the use of legal, industry or technical language in an SOA is unavoidable, the concepts must also be accurately explained in plain English.

4. Was the information in the SOA in a logical sequence?

SOAs which are not logically set out are not clear or effective as they tend to confuse clients.

In broad terms, SOAs must have:

- a beginning – the client's objectives, available assets, timeframe and risk tolerance
- a middle – an analysis of strategies and/or products that are likely to meet the client's objectives given their available assets, timeframe and risk tolerance
- an end – an explanation of a recommended strategy and/or products that are likely to achieve the client's objectives given their available assets, timeframe and risk tolerance.

5. Did the SOA identify the client's objectives in quantitative terms and explain how the advice would achieve those objectives?

An SOA that identifies the client's objectives in quantitative terms (eg "to retire at age 60 with sufficient savings to generate a retirement income of $40,000 a year") is much more likely to be effective than an SOA that does not identify the client's objectives with such attention to detail (eg "to retire at age 60").

The latter type of SOA is very unlikely to contain any meaningful analysis of, or conclusions about, the strategies and/or products that will achieve the client's objectives.

6. Did the SOA contain irrelevant information?

Clients are likely to be confused by SOAs that contain irrelevant information.

For example, if a client has only sought advice about investment products, and does not wish to borrow to fund the proposed investment, the SOA need not include information about margin loans and insurance products. If the SOA includes this information, it is less likely to be clear, concise and effective.

7. Is the SOA a template document?

In our experience, a template SOA is more likely to include:

- language the client will not understand (see question 2)
- legal, industry or technical language (see question 3)
- irrelevant information (see question 6).

Template documents can be helpful, but the FSP must take care to tailor the language used in the template to the client and delete irrelevant information.

CASE STUDY:

UNCLEAR AND INAPPROPRIATE FINANCIAL ADVICE

Esme was a very elderly war widow; she had exceeded the life expectancy of an Australian female. Her financial situation was uncomplicated. She received more than enough income from her pension and from a small annuity to meet her needs.

Esme received a significant legacy from her sister's estate. This was the first time she had received a large sum of money. She had previously obtained financial advice about her annuity from a financial adviser, but she was otherwise inexperienced in financial matters.

Esme sought financial advice from her regular adviser. She told the adviser that she wanted to top up her annuity with $100,000 and sought her advice about how to invest the balance of the inheritance.

During her discussions with her adviser, Esme said she wanted to invest a small amount in her granddaughter's name, but later she changed her mind because she was concerned about how other family members would view the investment when she passed away and they were dealing with her estate.

The adviser recommended that Esme invest the balance of the inheritance in a managed growth fund. The SOA prepared by the adviser stated the investment in the managed growth fund was "not capital guaranteed", "the balance may fluctuate daily due to changes in unit prices" and there was a risk of capital loss if Esme withdrew from the investment early.

Esme accepted the advice and made the recommended investment. The investment performed badly and suffered significant losses. Esme lodged a dispute with FOS, claiming she did not understand the advice provided to her and the managed growth fund was not an appropriate investment in her circumstances.

We noted that an SOA is a disclosure document that is intended to help a retail client understand advice and decide whether to rely on it. Client understanding of the advice is a critical part of the advice process.

After investigating the case, we drew the following conclusions:

- Esme was inexperienced in financial matters and had very limited knowledge of financial markets and products (as shown by her uncomplicated financial arrangements prior to receiving the inheritance).
- Esme's primary objective was to leave a legacy for her sons and grandchildren and therefore she wanted to place the money into a secure, capital-protected investment (as shown by her concern about how a proposed investment in a granddaughter's name would be perceived).
- The information in the SOA about capital volatility associated with the managed growth fund was generic in nature and was not likely to alert Esme to the potential for capital loss. It would have been prudent to put these warnings in language Esme was likely to understand.

We found that if the SOA had been expressed in language Esme was likely to understand, she would not have made the investment. We ordered the adviser to pay compensation to her.

NEW WORKFLOW ASSESSMENT PROCESS

Our Early Resolution Team, which handles disputes in the early stages of our dispute resolution process, will soon be implementing a new Workflow Assessment Process. This is a key initiative for improving organisational efficiency and reducing dispute resolution timeframes.

The Workflow Assessment Process will ensure that:

- disputes are promptly directed to the most suitable FOS team for resolution
- the most effective dispute resolution methods are used for each dispute.

The Workflow Assessment Process will be used for disputes that remain unresolved after they have been through internal dispute resolution and after the financial services provider (FSP) has provided their initial response about the dispute to us.

Under the new process:

- Certain types of disputes may be referred directly for decision. We will not first try to resolve these disputes using negotiation, conciliation or assessment. We may, however, exercise discretion to still progress some of these disputes through negotiation, conciliation or assessment first, where it appears clear that the matter may be resolved by agreement.
- For financial difficulty disputes, certain types of disputes may be referred directly to conciliation.
- Disputes that are considered suitable for negotiation, conciliation or assessment will be reviewed to establish their level of complexity. This will enable us to more effectively match dispute profiles with caseworkers' levels of experience and skill sets.

The types of disputes that may be referred directly for decision (or conciliation for financial difficulty disputes) are set out in the table on the next page. In our experience, detailed investigation and a formal decision (or conciliation for financial difficulty disputes) are normally the most effective means of achieving a resolution for these types of disputes. By referring these disputes earlier in the process, we expect that dispute resolution timeframes will be reduced and disputes will be handled more efficiently and effectively. The FSP and the applicant will be advised if a dispute is being referred directly to decision (or conciliation for financial difficulty disputes).

Workflow assessments will be overseen by our Workflow Team. Any queries about the new process may be directed to Michael Ridgway, General Manager, Early Resolutions: mridgway@fos.org.au.

DISPUTES SUITABLE FOR DIRECT REFERRAL TO DECISION (OR CONCILIATION FOR FINANCIAL DIFFICULTY DISPUTES)

TEAM	DISPUTE TYPES
Banking and Finance and Financial Difficulty	• EFT or unauthorised withdrawal disputes with claims greater than $10,000 • Allegations of forgery with claims greater than $10,000 • Disputed liability under a guarantee • Clearout listings on consumer credit files • Claims of maladministration in lending for secured debts relating to home loans, reverse mortgages and business lending (lodged by borrower or guarantor) where the Applicant claims: » they did not understand the agreement or were misled in relation to the lending » they could not afford the credit facility » they did not receive the benefit of the funds lent, or » the credit facility was unsuitable at the time of lending (where the Responsible Lending provisions of the National Consumer Credit Protection Act apply) • Claims of misconduct by FSP as mortgagee in possession • Retrospective claims for financial difficulty in relation to secured loans where there are no current arrears • Disputes where the applicant is experiencing financial difficulty, accepts liability for the debt and there are: » significant arrears (over $100,000) on a secured facility, and the parties' proposals for repayment are vastly different » cross-securitised multiple facilities with significant outstanding balances (over $1 million), or » secured debts where there are also Family Court proceedings, bankruptcy or company liquidation
General Insurance	• Medical indemnity • Driving under the influence • Fraud
Investments, Life Insurance and Superannuation	• Financial planning and investment/stockbroking disputes with multiple claims totalling more than $300,000 • Financial planning advice disputes involving more than one FSP who denies liability for the claim

CHANGES AT FOS

As part of our business planning, we have been looking at what we need to do to build on our significant achievements and thrive over the next three years.

FOS has grown rapidly since it formed in 2008. We are now a larger, more complex organisation, operating in a more demanding environment. We face the increasing volume and complexity of disputes, a growing expectation of rapid responses and volatile and changing financial markets – to name just a few of the challenges. Accordingly, we need a continued focus on developing both our technical expertise and our management capabilities.

As such, we have made some internal changes that include the introduction of three new senior executive roles – Executive General Managers – that will be part of a revamped Senior Leadership Group (SLG). The SLG will consist of the Chief Ombudsman, three Lead Ombudsmen and the three Executive General Managers.

The SLG will work closely with staff to position FOS to deliver service excellence in all that we do over the next three years. We will also be moving some teams within the organisation, to better align our structure with our goals, priorities and processes.

The organisational changes will take effect from July/August 2012, when the new executives are appointed. In the meantime, you should consider it business as usual in terms of how you contact and deal with FOS.

In around a month we will be publishing on our website our 2012-2013 Business Plan, which will contain more detail on our goals and initiatives.

RECENT EVENTS

We organise or attend hundreds of events every year, to educate our stakeholders about FOS and learn about their needs, and to contribute to policy discussions. Here is a sample of where we've been and what we've done between March and May.

MEMBERS/INDUSTRY

- **General Insurance Open Forums** (Sydney and Brisbane)

  We hold regular Open Forums around the country to discuss our Determinations in general insurance disputes. The forums are run by our Manager, Dispute Resolution, Graham Warner and our Ombudsman – General Insurance, John Price. See the 'Upcoming Events' article for details of upcoming forums.

- **Professional Indemnity Insurance Seminar** (Brisbane)

  The Brisbane seminar was run by Alison Maynard, our Ombudsman – Investments, Life Insurance & Superannuation. This seminar is for insurers and insurance brokers; it explains how we handle disputes about professional indemnity insurance. The same seminar is being run later in the year in Melbourne (31 October) and Sydney (1 November). Registration will open four to six weeks before the events. Check our Events Calendar for more information closer to the time.

COMMUNITY

- **Flood Insurance Information Session** (Numurkah)

  Following the flooding of Numurkah in early March, we held an information session for people whose homes, farms or businesses had been affected, to answer their questions about insurance claims and disputes.

- **Royal Easter Show** (Sydney)

  We had a stall on the two Seniors Days at the show, to raise awareness of FOS and answer questions about what we do.

CONSUMER REPRESENTATIVES

- **Financial Counsellor Conferences** (Melbourne and Palm Cove)

  We gave presentations and had stalls at conferences held by the Financial Counsellors Association of Queensland and Financial Counselling Australia. Our aim was to help financial counsellors understand our dispute resolution process and to help us understand the needs and concerns of counsellors and their clients.

- **External Dispute Resolution (EDR) Forum** (Melbourne)

  This event, hosted by Financial Counselling Australia, gives financial counsellors and consumer advocates a chance to meet with staff from FOS and other EDR schemes. Several FOS staff gave presentations at the forum.

GOVERNMENT BODIES AND OMBUDSMEN SCHEMES

- **Australian and New Zealand Ombudsman Association (ANZOA) 2012 Conferenc**e (Melbourne)

  Several FOS people attended and/or gave presentations at this conference, at which Ombudsmen schemes analyse industry trends and share ideas on best practice in dispute resolution.

- **Consumer Law User Group Panel** (Federal Magistrates Court, Melbourne)

  FOS was included in a consultation panel looking at the changes in the consumer law regime. It examines how things are shaping up for stakeholders such as consumer advocacy groups and EDR schemes and the issues arising from the new processes and procedures.

UPCOMING EVENTS

GENERAL INSURANCE OPEN FORUMS

Adelaide – 21 August
Perth – 22 August

The aim of the Open Forums is to bring together those involved in the industry to discuss FOS Determinations and share insights. Based on members' input at registration, our decision makers, where appropriate, prepare papers for discussion at the forums. These events are very popular, so registration is essential.

Registrations for both Perth and Adelaide will open in July.

See our Events Calendar for further details or email cbeattie@fos.org.au to register your interest.

RESOLVING CUSTOMER COMPLAINTS WORKSHOP

Perth – 27-28 August

This internal dispute resolution (IDR) workshop is one of our most popular training programs. Run in conjunction with Nina Harding Mediation Services, it is designed to enhance the complaint-handling skills of customer-facing staff.

The workshop will cover the following topics:

- the nature of conflict
- effective communication and understanding
- the elements of a good experience
- how to avoid, manage and resolve complaints
- identifying issues and building rapport
- preparing for a negotiation
- dealing with high needs complainants
- understanding your strengths
- working as a team
- identifying personality types
- advanced communication skills, including understanding the deeper meanings of words.

See the IDR Workshop page on our website for more details.

FOS NATIONAL CONFERENCE

Melbourne – 16-17 October

Our 2012 National Conference is being held at the Melbourne Convention Centre. Our aim is to deliver you a conference that deepens your understanding of best practice in dispute resolution and helps you strengthen your relationships with customers.

In the previous edition of *The Circular*, we asked you what was important to your professional development. Thank you to those of you who filled out the short survey. We have strived to develop a program that meets your requests and is exciting and forward-looking.

Our National Conference will:

- expand your dispute resolution toolkit
- help you to increase the efficiency of your internal and external dispute resolution systems
- explain FOS's decisions in past cases so you can understand the consistency in our approach
- illustrate what best practice dispute resolution looks like
- examine the trends, issues and challenges faced by all players in the financial services sector.

The conference will be a forum for us to share our experiences of dispute resolution to help achieve a broader business goal that we should all share – building service excellence.

Registrations for the 2012 FOS National Conference will open in July.

If you have any questions, please email us at nationalconference@fos.org.au.

FOS BOARD APPOINTMENTS

Following the expiration of the first terms of office of its Directors, the FOS Board has recently finalised appointments of directors to the Board in accordance with Clause 4 of its Constitution and Board Charter. FOS placed public advertisements seeking applications from individuals interested in being considered as Consumers' Directors and professional and industry bodies were requested to nominate individuals willing to serve as Industry Directors. Pursuant to the Board Charter, Selection Committees were established to short-list and interview potential candidates.

The following re-appointments and appointments have been made.

- Independent Chair (re-appointed pursuant to Clauses 4.6 and 4.7 of the FOS Constitution): Professor The Honourable Michael Lavarch AO.
- Industry Directors (appointed / re-appointed pursuant to Clauses 4.8 and 4.9 of the FOS Constitution): Ms Jennifer Darbyshire, Mr Russell McKimm, Mr Chris McRae. Mr Robert Belleville continues his first term as a director until February 2013.
- Consumer Directors (re-appointed pursuant to Clauses 4.10 and 4.11): Mr David Coorey, Ms Catriona Lowe, Ms Jenni Mack, Mr Denis Nelthorpe.

Pursuant to Clause 4.12, appointments are made for a maximum of a three-year term of office. Professor Michael Lavarch, Mr David Coorey and Ms Catriona Lowe were re-appointed for a further three-year term. Ms Jenni Mack, Mr Russell McKimm and Mr Denis Nelthorpe have agreed to be re-appointed for a two-year term of office to allow a staggering of the appointments schedule. Ms Jennifer Darbyshire and Mr Chris McRae were appointed for three-year terms of office.

On behalf of the Board, Professor Lavarch thanks Dr Brendan French for his valuable contribution as a director of FOS in its formative first three years. Dr French did not apply for re-appointment to the Board of FOS. Professor Lavarch would also like to acknowledge the valuable contribution of the late Mr David Squire as a FOS director during his term of office, which came to a premature end in October 2011.

The strong field of applicants indicates a high level of support for the role FOS plays in providing an important community service – resolving disputes between customers and financial services providers in a way people can trust.

FOS would like to thank all those who expressed an interest in being considered as a FOS director.

TOP 10 TIPS FOR FINANCIAL ADVISORS

1. TAKE DETAILED FILE NOTES

FOS relies on evidence provided by the parties to a dispute. Documents created at the same time as the activity or advice in question are usually given more weight than later recollections of what was said or done.

This means contemporaneous file notes of conversations and actions are solid gold when a dispute comes to us.

Whenever possible, confirm verbal instructions from a client in writing (eg send them an email after a telephone conversation confirming what was said).

2. USE A CLIENT'S OWN WORDS

We do not consider client objectives and instructions written in industry terms that few clients would understand to be a reliable record.

Write down a client's objectives in the words the client has used in answering your questions about their objectives and how to quantify those objectives. This demonstrates that you have heard and understood the client's goals in seeking advice – eg "to retire at age 65 with an income of $50,000 per year".

3. TURN CLIENTS AWAY WHEN APPROPRIATE

If your services are not suited to a particular client (eg they are seeking advice about direct shares and you don't provide that service), you must tell them so and send them away. Don't try to shape the client to your offering.

If a client is seeking a return which does not match their risk profile and you can't convince them to change their expectations, either send them away or see tip 4.

4. EXPLAIN THE RISKS TO CLIENTS WHO CHOOSE TO ACT AGAINST YOUR ADVICE

You must be very clear in explaining the risks and documenting that the course of action is against your advice. Explain the risks in language the client understands make a contemporaneous file note and have the client sign it.

5. EXPLAIN WHAT TYPES OF SERVICE YOU ARE PROVIDING

Clients don't know the difference between information, general advice, personal advice and execution-only services.

If you don't give the appropriate explanations and warnings or you are unclear, then you could be found liable for advice or activities that you had not intended to provide.

6. USE TEMPLATE FORMS AND DOCUMENTS CAREFULLY

Make sure template forms and documents about strategies, products and risks are appropriate to the client you are advising.

It is very difficult to convince us that you have selected the right strategies and financial products for a client if the documents contain errors, are missing information or contain copious amounts of irrelevant material.

You will also have some trouble convincing us that the client understood your documents if they contain pro-forma jargon or complex concepts.

Tailor documents to your client's financial literacy. (See the article "Statements of Advice must be clear, concise and effective" in this Circular for more about this important topic.)

7. USE RISK PROFILING TOOLS CAREFULLY

Make sure that the strategy and asset allocation you recommend to a client is consistent with risk profile generated by the risk profiling tool you use. If there are inconsistencies, you must clearly explain them.

Remember, risk profiling tools are only tools. They all have inherent flaws that must be recognised and addressed by the adviser. (See the article "Risk profiling in financial advice disputes" in Issue 6 of *The Circular*.)

8. DON'T GIVE COOKIE CUTTER ADVICE

This is really a reiteration of tips 6 and 7.

You should not put all or most of your clients into the same strategy and products, especially not gearing strategies. For example, we saw a Statement of Advice for a client with taxable income of $42,000 that stated: "Your reasonable level of surplus income and high tax rate should make gearing an appropriate option for you".

9. UNDERSTAND AND EXPLAIN THE PRODUCTS

Understand any products you are recommending. Don't advise on products you don't understand.

Don't just hand over a Product Disclosure Statement (PDS) – you must explain the PDS to your client and record your discussion in the Statement of Advice (SOA).

Don't cut and paste PDS disclosures into your SOAs. Show you understand the products by using the same words you use to verbally explain the products to your clients!

10. BE CLEAR ABOUT THE ADVICE RELATIONSHIP WITH CLIENTS YOU KNOW

If you are giving advice to a friend, relative, colleague or employee, it is critical to formalise and document the process as you would for any other client.

In addition; declare any conflicts of interest as you would for any other client.

SYSTEMIC ISSUES UPDATE – JANUARY-MARCH 2012

This article summarises systemic issues that we identified during the March quarter of 2012 and reported to the Australian Securities and Investments Commission (ASIC). It also provides an update on some current and recently resolved systemic issue investigations.

The FOS process for identifying and resolving systemic issues was outlined in Issue 4 of *The Circular*. The process is in line with our obligations to ASIC.

To learn more about our approach to systemic issues, you can do our online training module.

NEW DEFINITE SYSTEMIC ISSUES

Flood disputes: failure to clearly inform

FOS determined a number of flood disputes in favour of the applicants on the ground that the financial services provider (FSP) failed to clearly inform the applicants of the limited flood cover under their policies, contrary to the requirements of section 35 of the *Insurance Contracts Act 1984* (Cth). FOS raised this matter as a possible systemic issue with the FSP.

The FSP confirmed there were 64 flood claims dating back to 2007 which would have to be reviewed to ascertain if the customers were clearly informed about the limited flood cover. The FSP agreed to review the claims and provide a report to FOS.

After the FSP sent us a report, we decided this was a definite systemic issue. The FSP is now taking steps to resolve the systemic issue by improving their disclosure documents and procedures and by identifying and reimbursing customers that were affected by the issue in the past.

Error in credit listings (case A)

We received several similar disputes in which applicants raised concerns about serious credit infringement listings an FSP made on their personal credit files.

We referred the FSP to sections 6 and 18E of the *Privacy Act 1988 (Cth)*, which define "serious credit infringement" and specify the circumstances in which such an infringement can be listed. We informed the FSP that in each case we investigated, it appeared that serious credit infringements had been listed, even though the FSP had not conducted sufficient tracing to determine that the applicants' actions indicated that they intended to no longer comply with their obligations in relation to credit. We also informed the FSP that we would review whether it had made serious credit infringement listings against any other customers that were not based on actions that a reasonable person would consider to indicate that the customers no longer intended to comply with their obligations in relation to credit.

The FSP responded by providing, as requested, copies of its policies and procedures for making a serious credit infringement listing against customers. It also confirmed that all disputes cited by FOS had involved third party tracing agents.

We reviewed the information and asked the FSP to review a sample of listings that involved the use of external field agents. After the FSP confirmed that a high proportion of the serious credit infringement listings reviewed had been made incorrectly, we decided that the issue was definitely systemic.

In order to move towards a resolution of this systemic issue, we asked the FSP to tell us how many serious credit infringement listings had been removed completely as well as the date the removal and/or re-listing took place. We also asked the FSP to formally undertake to consider, case by case, any claims for non-financial loss from customers whose listing was made in error.

Error in credit listings (case B)

The applicant in one dispute complained that the FSP had not correctly assessed his application for hardship assistance regarding the hire purchase agreement for which he had acted as guarantor. During our investigation of the dispute, we found that the FSP had listed a commercial debt on the applicant's personal credit file. In our view, a commercial debt could not be considered credit under the relevant legislation and therefore the listing had been made inappropriately.

We asked the FSP to tell us whether it had made any other default listings relating to commercial credit on a customer's personal credit file. We also asked it to provide copies of its policies and procedures regarding commercial credit listings.

We reviewed the information submitted by the FSP and determined that this was a definite systemic issue due to the number of incorrect default listings made. The FSP has been asked to correct the incorrect listings and to send us copies of its policies and procedures relating to default listing business guarantors on their personal credit files.

Failure to advise customers about FOS

In its final decision letter to a customer who had made a complaint, an FSP said that no further review of the complaint was available under the general insurance industry's alternative dispute resolution process. Specifically, it said that the matter was outside FOS's jurisdiction, due to the time that had elapsed since the original complaint.

We raised the matter as a possible systemic issue with the FSP and asked:

- whether it had issued internal dispute resolution (IDR) responses to other customers which informed them that they did not have a right to take their complaint to FOS
- whether it had failed to provide FOS's contact details to other customers on the basis that FOS did not have jurisdiction to deal with the complaint due to the amount of time that had elapsed.

ASIC's *Regulatory Guide 165: Licensing: Internal and External Dispute Resolution* requires an FSP, in its final response to a complainant, to include information about:

- their right to take their complaint to an external dispute resolution (EDR) scheme
- the name and contact details of the EDR scheme to which they can take the complaint.

This means that any final decision letter must explain that the complainant may take their complaint to the EDR scheme to which the FSP belongs, which deals with complaints made by its retail clients in relation to the financial services it provides. The existence of the 'right to take' a complaint to FOS does not depend on whether the complaint is within our jurisdiction. Whether a matter falls within our jurisdiction can only be determined by us after the matter is referred to us.

We have consistently expressed the view that it is a matter for us to determine whether we have jurisdiction to deal with a complaint. An FSP should not unilaterally make that decision and inform a customer that it does not have the right to take their complaint to FOS.

We reviewed this matter and found that it was a definite systemic issue. We asked the FSP to:

- remove any wording from IDR responses that inappropriately discourages customers from taking a complaint to FOS
- redraft its IDR responses so that they meet the requirements of *Regulatory Guide 165* (outlined above)
- indicate the approximate number of customers who, in the last six years, would have received IDR responses that did not meet these requirements.

INVESTIGATIONS

Some of the ongoing systemic issues investigated in the March quarter are summarised below.

Methodology and disclosure of break costs on fixed interest loans

One investigation relating to this matter remains on foot; another has been closed following completion of a detailed remediation timetable. No new possible systemic issues relating to this matter were identified during the March quarter.

Errors in credit listings and inaccurate credit file enquiries

This continues to be an area that raises systemic issue referrals, particularly in relation to serious credit infringement listings and the form of default notices. There were a number of continuing investigations during this quarter that have yet to be resolved to our satisfaction.

Recovery of costs of dealing with FOS from an applicant

This issue has been resolved by the identification and remediation of the affected customers in relation to two FSPs. Correspondence has been sent to one other FSP regarding a possible systemic issue in relation to this matter.

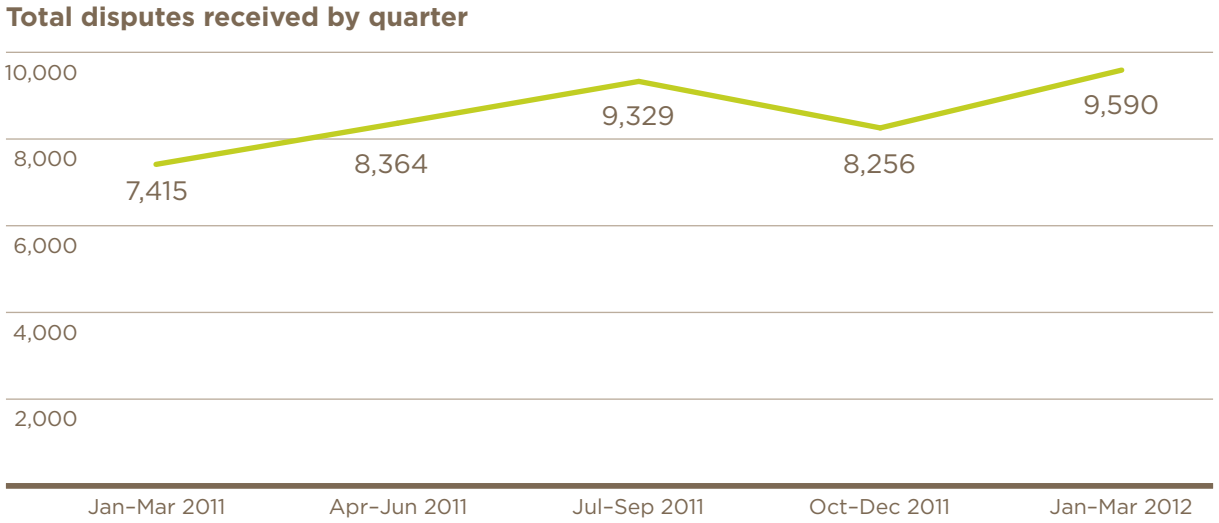
Failure to advise customers about FOS

There have been disputes which illustrate that FSPs in some instances have not advised customers about FOS or have provided incorrect information about FOS. As explained above, FSPs have to provide certain information about FOS in IDR responses.

STATISTICS REPORT: JANUARY-MARCH 2012

TOTAL DISPUTES RECEIVED

We received 9,590 new disputes in the January-March 2012 quarter. This is up 16% on the previous quarter and up 29% on the January-March 2011 quarter. As the chart below shows, the number of disputes we have received has increased steadily over the past year, except for a slight dip in October-December 2011.



Note: disputes received' includes disputes that enter our dispute resolution process at the Registration stage and disputes that entered the process at the Acceptance stage.

TOTAL DISPUTES RECEIVED BY PRODUCT LINE

Almost half of the new disputes we received in January-March 2012 were credit disputes and another 29% were general insurance disputes. We started handling disputes about traditional trustee services this quarter, but we only received 9 disputes in this new product line.

DISPUTES RECEIVED BY PRODUCT LINE, JAN-MAR 2012		
PRODUCT LINE	**NUMBER**	**%**
Credit	4,810	49%
General insurance	2,814	29%
Payment systems	631	6%
Deposit taking	587	6%
Investments	535	5%
Life insurance	299	3%
Products outside our Terms of Reference	167	2%
Traditional trustee services	9	<1%
Unclassified	11	<1%
Total	9,863	

Note: The total number of disputes received in this table exceeds the total for this quarter in the chart above. The total in that chart is based on counting each case, even if it is about multiple products and issues, as one dispute. The total in this chart is based on counting cases about multiple products and issues as multiple disputes.

REGISTERED DISPUTES

Registration is the first stage in our dispute resolution process. When we register a dispute, we record the basic details and refer them on to the financial services provider (FSP). The FSP then has an opportunity to resolve the dispute with its customer without our involvement. Click here for more information about our process.

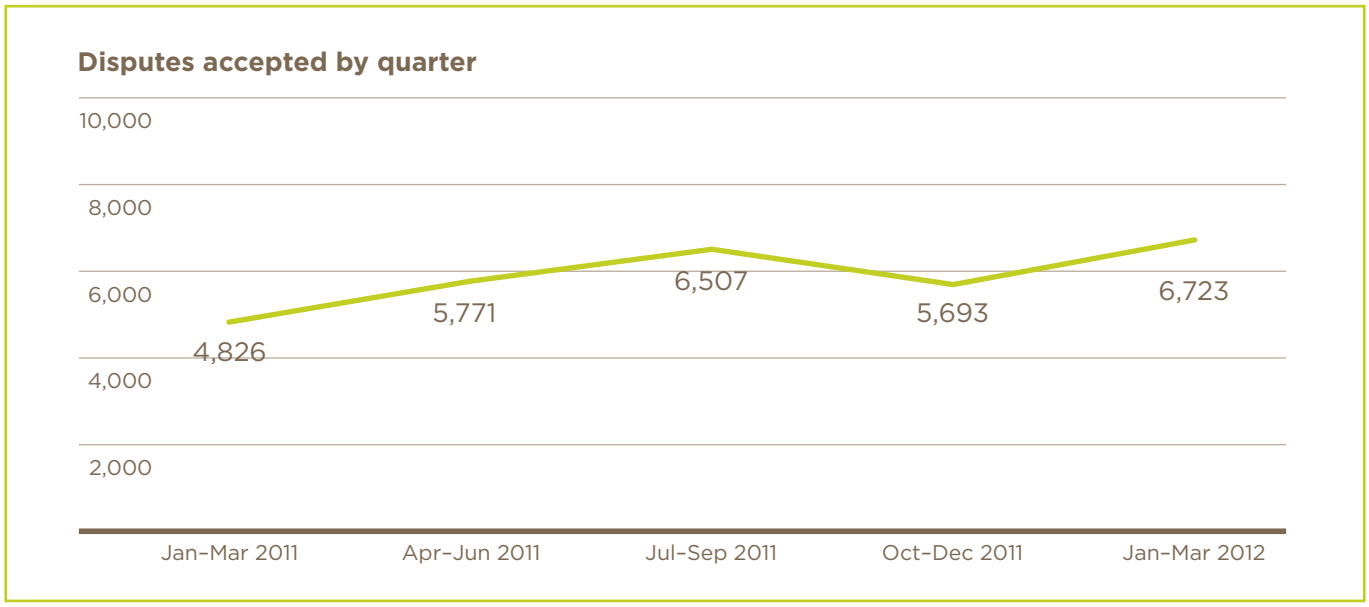
We registered 4,885 disputes in January-March 2012. At the end of the quarter, half of these disputes were still open in Registration, 23% had been resolved by the FSP, and 24% had progressed to the Acceptance stage of our process.

REGISTERED DISPUTES AND THEIR OUTCOMES/STATUSES		
OUTCOME/STATUS	**NUMBER**	**%**
Resolved by the financial services provider	1,111	23%
Discontinued	18	<1%
Outside our jurisdiction	121	2%
Still open – in Registration	2,447	50%
Still open – progressed to Acceptance	1,188	24%
Total	4,885	

ACCEPTED DISPUTES

Acceptance is the second stage in our dispute resolution process. It is the point at which we start playing an active role in trying to resolve a dispute. Click here for more information about our process.

We accepted 6,723 disputes in January-March 2012. This is up 18% on the previous quarter and up 39% on the January-March 2011 quarter.



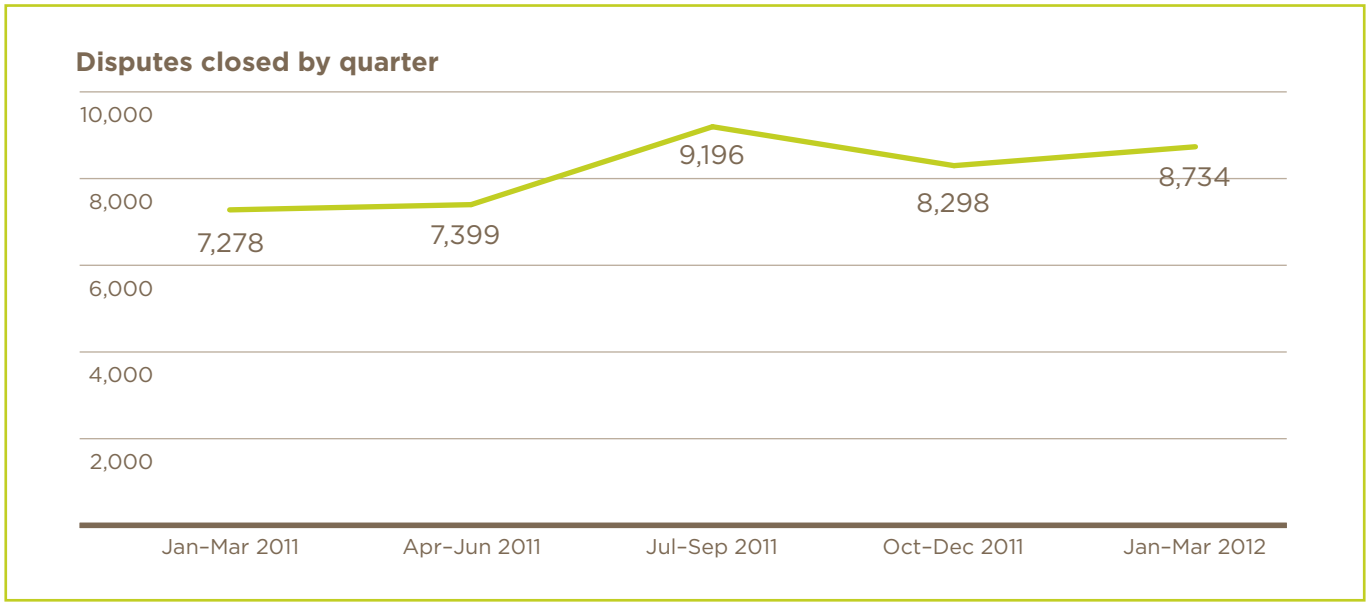
The breakdown of accepted disputes by product line is similar to the breakdown of all received disputes.

ACCEPTED DISPUTES BY PRODUCT LINE, JAN-MAR 2012		
PRODUCT LINE	**NUMBER**	**%**
Credit	3,460	49%
General insurance	2,012	29%
Investments	466	7%
Deposit taking	352	5%
Payment systems	384	5%
Life insurance	240	3%
Products outside our Terms of Reference	90	1%
Traditional trustee services	4	<1%
Total	7,008	

Note: The total number of disputes accepted in this table exceeds the total for this quarter in the chart above. The total in that chart is based on counting each case, even if it is about multiple products and issues, as one dispute. The total in this chart is based on counting cases about multiple products and issues as multiple disputes.

CLOSED DISPUTES

We closed 8,734 disputes in January-March 2012. This is up 5% on the previous quarter and up 20% on the January-March 2011 quarter.



OUTCOMES OF CLOSED DISPUTES

Three-quarters of the disputes closed in January-March 2012 were resolved through an agreement between the financial services provider (FSP) and the consumer. Only 8% of the closed disputes required a formal decision by FOS.

The proportion of closed disputes that were discontinued has been trending down over the last two years, from 9% in 2010-2011 to 6% in the January-March 2012 quarter. A dispute is recorded as having been discontinued if the applicant (the consumer who lodges the dispute) either decides to discontinue their dispute or pursue it in another forum, or the applicant fails to respond to several requests from us for contact and information. We have a follow-up process in place for situations in which an applicant does not respond to communication from us.

OUTCOMES OF CLOSED DISPUTES, JAN-MAR 2012		
OUTCOME	**TOTAL**	**%**
Resolved by agreement		
Assessment	150	2%
Conciliation	161	2%
Negotiation	322	4%
Resolved by financial services provider (FSP)	5,912	68%
Resolved by FOS decision		
Decision in favour of applicant	285	3%
Decision in favour of FSP	402	5%
Decision confirming FSP offer/action	59	1%
Discontinued	500	6%
Outside FOS Terms of Reference	943	11%
Total	**8,734**	