Financial Ombudsman Service
Terms of Reference
Submission to the Financial Ombudsman Service

Financial Planning Association of Australia

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Introduction

The Financial Planning Association of Australia (FPA) is the peak professional organisation for the financial planning sector in Australia. With approximately 12,000 members organised through a network of 31 Chapters across the country, the FPA represents qualified financial planners who manage the financial affairs of over five million Australians with a collective investment value of more than $630 billion.

The vast majority of the FPA members are also members of the Financial Ombudsman Service (FOS), falling within the Investments Life Insurance and Superannuation Division (ILIS) of the scheme. The FPA acknowledges and supports the requirement for FOS to genuinely merge the existing schemes under its new Terms of Reference and is optimistic about the opportunities this merger will provide.

Effectively resolving complaints through the Internal Dispute Resolution (IDR) process is a core aim of the financial planning profession. FPA members also recognise that EDR mechanisms are intended to provide a useful and cost effective alternative to the courts for consumers. The FPA and its members consider the role of FOS as a vital part of the successful operation of the financial services industry in Australia.

The overarching statement for our submission is that we understand and support the intention to harmonise and simplify the rules, terms and processes across all the schemes so as to provide a single, simple, and cost effective mechanism for consumers. However, it is the FPA’s fundamental contention that disputes arising in the provision of financial advice are by their very nature complex and deal with issues of trust and human and market behaviour which are not easily reduced to the traditional ombudsman models of dispute resolution. Certainly, they are more complex than claims of transactional, policy or computational error that form the basis of disputes in other jurisdictions within FOS.

The FPA urges the FOS Board to reflect these differences in its Terms of Reference, rules and policy formulation, in order to ensure measurable and equitable outcomes for all FOS stakeholders.

Due to these differences, the harmonisation across the three schemes will undoubtedly lead to operational complexities and the FPA suggests it may be necessary for FOS to provide greater clarity on the practical implementation of the Terms of Reference in the future.

The FPA believes a fundamental goal of the FOS Terms of Reference should be to increase consultation, dialogue and engagement between the complainant and the provider, and to seek resolution and settlement opportunities throughout the External Dispute Resolution (EDR) process. The following recommendations would achieve this goal and ensure better dispute resolution outcomes for both consumers and providers.

1. Summary of recommendations

The attached submission follows the order of the FOS Terms of Reference Issues Paper and responds to the questions raised by FOS. It also highlights key issues for consideration in the development of the Terms of Reference. The FPA has made reference in this submission to some of the proposals raised by the Australian Securities and Investment Commission (ASIC) in its consultation paper CP 102: Dispute resolution—review of RG139 and RG165, as we recognise that the ASIC review would have a profound influence on the drafting of the FOS Terms of Reference.

Access to the scheme

1. The FPA recommends the exclusion of those defined as ‘sophisticated investor’ in the Corporations Act 2001, as well as the exclusion of subsidiary companies and Local Government authorities. The FPA supports the definition of small business proposed by FOS.

2. The FPA does not support the proposal for FOS to commence an investigation if a complaint remains unresolved in a department of the provider for more than 45 days.

3. The FPA agrees that it would be appropriate for FOS to refer disputes to the member’s IDR area if the complaint has been raised in another area of the provider’s business and remains unresolved after 45 days.
**Types of disputes that FOS can consider**

4. The FPA strongly rejects the inclusion of privacy and confidentiality complaints within the FOS jurisdiction.

5. The FPA recommends FOS be given the authority to refer complaints about privacy and confidentiality to the Office of the Privacy Commissioner.

6. The FPA considers it would be inappropriate for FOS to consider disputes in relation to contracts created outside Australia.

7. The FPA supports the exclusions proposed in the FOS Issues Paper, with some recommended additions/changes.

8. The FPA recommends the time limit for lodging a complaint should start from the date of the cause of the action only, as per general statutory limitations.

9. The FPA supports the FOS proposal not to consider disputes in those circumstances detailed in the Issues Paper (page 28), with some additions/changes.

10. The FPA considers it a fundamental responsibility of FOS to ensure the professional indemnity insurers can and will provide appropriate cover at an affordable premium, for all EDR scheme participants, prior to any increase in the monetary limits.

11. Before any consideration to increasing the FOS monetary limits, issues of the EDR scheme’s transparency and processes need to be addressed.

12. The FPA recommends that any increases to FOS monetary limits should be set on a reasonable and measurable basis with a methodology transparent to both consumers and providers.

13. The FPA does not support the FOS proposal to automatically increase the monetary limits in line with the CPI rate or the Male Total Average Weekly Earnings (MTAWE) every three years.

14. The FPA does not support the introduction of an opt-in system or an award caps system.

**Dispute resolution**

15. The FPA believes the decision making model of FOS should increase consultation, dialogue and engagement between the complainant and the provider, and seek resolution and settlement opportunities throughout the EDR process.

16. The FPA recommends a hybrid of the Ombudsman and Panel decision making models (see Box 1).

17. The FPA recommends an alternative appeal mechanism to that proposed in the Issues Paper.

18. The FPA recommends the introduction of timeframes for the various stages of the EDR decision making model.

19. The FPA supports the dispute resolution process proposed by FOS in the Issues Paper, with recommended amendments.

20. The FPA recommends additional provisions should be included in the FOS Terms of Reference which require FOS, the decision making Panel and the Ombudsman, to take into account the severity of the cause of the inappropriate advice, misrepresentation or non-disclosure, as well as the role of the complainant and other parties, in its consideration of financial advice disputes.

21. The FPA recommends the FOS determinations provide detailed reasons explaining why FOS considers the financial planner is at fault.

**Awarding compensation**

22. The FPA recommends the awarding of compensation for non-financial and consequential loss be excluded from the EDR jurisdiction.

23. The FPA recommends any award of interest should be included within the monetary limit and that the mechanisms used to calculate interest should be robust, transparent and should not extend to consequential loss.
Test cases

24. The FPA supports the preferred option for test cases proposed by FOS in the Issues Paper, and recommends an amendment to allow flexibility for circumstances when the court may provide a direct ruling in relation to the payment of costs.

Reporting externally

25. The FPA welcomes FOS guidance on what constitutes ‘serious and systemic’ issues, as proposed in the Issues Paper and recommends the new FOS guidance be developed in consultation with industry.

26. The FPA recommends FOS clearly identify and provide regular reports to members giving detailed information on the underlying causes of complaints.

Other issues

27. The FPA recommends the transition to the new Terms of Reference or any increase in the monetary limits should be sufficient for FOS to:
   - ensure affordable and appropriate professional indemnity insurance will be available to all scheme participants;
   - address the issues of transparency and process;
   - develop and publish ‘specific criteria’ for decision making; and
   - identify an appropriate formula to determine the validity of any monetary increase.

2. FOS guiding principles and constraints

The FPA highlights and welcomes the acknowledgement in principle 1 that the “regulator expects a genuine merger with a genuine potential for improvement”. We are optimistic that material and operational change will occur, and would encourage FOS to ensure the intent of the provisions in the new Terms of Reference filter down to an operational level.

The FPA also suggests FOS consider amending guiding principle 2 for the development of its Terms of Reference. It would be more equitable for principle 2: *Consumers must not be disadvantaged by the merger* to apply to all FOS stakeholders, not just consumers. We are also concerned by the assumption made in this principle that “there will be some increase in EDR dispute jurisdictions for some providers”. The FPA believes it is inappropriate for guiding principles to prejudge the outcome of the consultation process.

3. Access to the scheme

3.1 Proposed definition of ‘consumer’ and ‘small business’

FOS proposes to accept a dispute brought by the following parties to the EDR scheme:

a) An individual; or

b) A small business – defined as a business entity (including companies in the same group of companies):
   i) that is involved in manufacturing goods and has less than 100 full-time or equivalent employees in the group; or
   ii) is involved in activities other than manufacturing and has less than 20 full-time or equivalent employees in the group.

The FPA has assessed the main differences between the existing FICS coverage and the proposed FOS definitions:

a) Under FICS most corporations could lodge a complaint (except for those described in b) below). The FOS proposal would limit access to the scheme to those corporations with less than 20 full-time or equivalent employees, or less than 100 full-time or equivalent employees in the case of a manufacturing business.

b) The FICS Rules provided a discretionary exclusion to “a corporation whose interest arose only out of a security, debt or a lien over property which is involved in the dealing or transaction”. The FOS proposal removes this discretionary exclusion.
c) Under its Rules, FICS was allowed to decide not to deal with a complaint by a person who was not a ‘retail client’ as defined by the Corporations Act 2001. Therefore, complaints by ‘sophisticated investors’ had the potential to be excluded from FICS. The FOS proposal would remove this discretion giving non-retail consumers such as ‘sophisticated investors’ the right to use FOS (subject to the monetary limit and other exclusions).

The FPA supports the definition of small business proposed by FOS. However, we recommend the exclusion of those defined as ‘sophisticated investor’ in the Corporations Act 2001, as well as the exclusion of subsidiary companies and Local Government authorities.

The FPA considers the EDR system is designed to provide protection and a consumer compensation mechanism for ‘retail clients’. The inclusion of ‘sophisticated investors’, subsidiaries of group companies, and Local Government authorities, goes beyond this purpose and would detract resources from those ‘retail clients’ most in need of assistance, to those who would have the means to access other jurisdictions.

Planners are subject to different rules and requirements under the Corporations Act (Act) for non-retail clients, such as ‘sophisticated investors’. For example, if a client is identified as a ‘sophisticated investor’ and notified of this status, it is assumed under the Act that the client has an informed level of knowledge, experience and an ability to assess:

(i) the merits of the product or service;
(ii) the value of the product or service;
(iii) the risks associated with holding the product;
(iv) the client’s own information needs; and
(v) the adequacy of the information given by the licensee and the product issuer.

Planners are not required to maintain the same records for ‘sophisticated investors’ that are required to be given to a ‘retail client’ under Chapter 7 of the Act. Should non-retail clients be permitted to access FOS, it would force planners to change documentation and record keeping practices beyond the requirements of the law and in line with those for ‘retail clients’, at significant expense and in contradiction to the intent of the Corporations Act. This would drive up the cost of financial advice for all consumers. In addition, resources would be diverted from the intended users of FOS (‘retail clients’) in favour of ‘sophisticated investors’ and other non-retail clients who have the means and knowledge to access other avenues for compensation.

Similar inequitable issues would also arise in disputes involving subsidiary companies and Local Government authorities.

It would be difficult, costly and inefficient for an EDR scheme to operate under a jurisdiction open to ‘sophisticated investors’, subsidiaries of group companies and Local Government authorities. The FPA considers it inappropriate and unnecessary for FOS to extend its jurisdiction to such clients.

### 3.2 Lodging a dispute with FOS

FOS proposes including flexibility in its Terms of Reference to allow a consumer to lodge a dispute with FOS if they have already made a complaint to any area or department of the financial services provider, and the dispute remains unresolved after the required 45 days. FOS would then be able to make a judgment as to referral of such a dispute directly to the IDR department of the provider or whether to commence investigation if the time limit for IDR has elapsed.

The FPA does not support the proposal for FOS to commence an investigation if a complaint remains unresolved in a department of the provider for more than 45 days. The IDR process should be encouraged and allowed to work. The FPA considers it inappropriate for FOS to investigate a dispute until the provider has completed the IDR process.

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1 Section 761GA(d)
To facilitate effective IDR consideration, the FPA agrees that it would be appropriate for FOS to refer disputes to the member’s IDR area if the complaint has been raised in another area of the provider’s business and remains unresolved after 45 days.

4. Types of disputes that FOS can consider

4.1 Inclusion of privacy and confidentiality complaints

FOS has proposed extending the EDR scheme jurisdiction to consider privacy and confidentiality complaints. This would include giving FOS powers to make determinations, awards, declarations, orders or directions, and impose sanctions that the Privacy Commissioner may make for breaches of the Privacy Act under section 52 of the Act.

The FPA strongly rejects the inclusion of privacy and confidentiality complaints within the FOS jurisdiction. Privacy is a specialised area of law with a dedicated statutory body empowered to consider complaints in this area, and accordingly it would be inappropriate for FOS to duplicate the work of the Office of the Privacy Commissioner.

In addition, the Australian Law Reform Commission is currently considering new sanctions for breaches of the Privacy Act, which include criminal sanctions. The FOS proposal to extend its powers to impose sanctions similar to that of the Privacy Commissioner, would therefore give FOS the ability to impose criminal sanctions or at the very least confuse the jurisdictional environments. FOS is a ‘company limited by guarantee’ and an EDR scheme. It is not a regulator or a statutory body and therefore should not be given executive statutory powers relating to the enforcement of laws and particularly criminal sanctions.

The FPA suggests that FOS be given authorisation to refer complaints about privacy and confidentiality to the Office of the Privacy Commissioner.

4.2 Contracts and obligations created outside Australia

The FPA supports the FOS preferred option to “Require that the financial service must originate from a contract formed or an obligation arising under Australian law”. The FPA considers it would be inappropriate for FOS to consider disputes in relation to contracts created outside Australia.

The FPA recommends the only appropriate role for FOS in disputes relating to contracts and obligations created outside Australia would be to facilitate access to information about overseas external dispute resolution schemes.

4.3 Exclusions

FOS has proposed listing the following exclusions in its new Terms of Reference:

a) Non-participating financial services providers of FOS – at the time a dispute is received by FOS.

b) Disputes relating to a financial service provider’s commercial judgment, with the exception of medical indemnity disputes, but including:

   i) The management of a fund or scheme as a whole;

   ii) A decision as to how to allocate the benefit of a financial product between competing beneficiaries;

   iii) The assessment of risk in relation to the provision of a financial service unless there was maladministration in lending in relation to the provision of a banking service, or an insurance proposal rejection was indiscriminate, malicious or based on incorrect information; and

   iv) Variations to a credit contract under the Uniform Consumer Credit Code.

c) The performance of an investment product, except a dispute concerning non-disclosure or misrepresentation.

d) The practice or policy of a financial services provider, including general interest rate policy, the level of an insurance premium or fees and charges policy. FOS can consider a dispute about the application of a fee or charge in breach of contract.

The FPA supports the exclusions proposed in the FOS Issues Paper. However, we are concerned that use of the term ‘commercial judgment’ in exclusion b) may be ambiguous and difficult to understand for some consumers.
The FPA recommends the inclusion in section b) above, the following additional exclusion the FOS jurisdiction, as per the current FICS Rules:

b) Disputes relating to a financial service provider’s commercial judgment, with the exception of medical indemnity disputes, but including:

v) Decisions of the trustees (in their capacity as trustees) of approved deposit funds and of regulated superannuation funds.

The FPA considers it inappropriate for FOS to be able to review commercial decisions of trustees of superannuation funds.

The FPA also recommends the term ‘financial product’ as defined in the Corporations Act replace the term ‘investment product’ in exclusion c). This will ensure a consistent use of terminology with the law within which providers must operate and provide clarity around the application of this provision.

c) The performance of a financial product, except a dispute concerning non-disclosure or misrepresentation.

4.4 Time limit on lodging complaints

FOS proposes to set a single timeframe of six years from the date of the cause of action or from when the consumer should have reasonably known of all the facts, whichever is the later.

The FPA recommends the timeframe should be from the date of cause of the action only, as per general statutory limitations. Inconsistency with the legal statute of limitation would hinder the ability to apply for a ‘test case’ and put at risk the provider’s right to go to court if the limitations period has lapsed.

4.5 Alternative proceedings

The FPA supports the FOS proposal not to consider disputes in those circumstances detailed in the Issues Paper (page 28):

a) proceedings are underway in a Court or Tribunal or another EDR scheme in relation to the dispute;

b) the dispute was the subject of an arbitration or a decision of a Court, Tribunal or another EDR scheme;

c) the parties have agreed to settlement of the dispute; or

d) FOS considers another forum appropriate.

The FPA recommends the following addition to this list:

e) notice has been received that proceedings may be instituted or under consideration for litigation, until such time that the ‘opt-in’ timeframe has closed.

The FPA strongly supports the proposal for FOS or the Ombudsman to have the power to decline to consider a dispute if there is a more appropriate forum.

In answer to question 15 in the Issues Paper, the FPA suggests that where the parties have agreed to settle, as per the proposed clause c) above, such disputes should not be considered by or re-opened by FOS.

4.6 Increasing monetary limits

The significant and unavoidable concerns of the FPA and its members in relation to any increase in the FOS monetary limits include the impact on professional indemnity insurance, the transparency and fairness of the EDR scheme, the method used to determine the limits, and appropriate transition arrangements. These concerns must be addressed by FOS.

4.6.1 Professional indemnity insurance

The FPA has consistently stated it’s objection to a monetary limit increase as an acknowledgement that financial planners are disadvantaged by the lack of competitive, commercially available professional indemnity insurance which the Corporations Act compensation regulations rely on. Such insurance is generally available to other professions outside of this environment.
The FPA strongly believes that monetary limits (at any level) must be supported by the broader consumer compensation system underpinned by professional indemnity insurance. The FPA strongly recommends that FOS must guarantee the availability of appropriate and affordable professional indemnity insurance for all participants of the scheme prior to any increase in the monetary limits. This responsibility should be included in the FOS Terms of Reference.

In July this year, the monetary limit for financial advice disputes was increased from $100,000 to $150,000. This increase, along with other factors such as market conditions, played a role in the significant increases in professional indemnity insurance premiums experienced by financial planners.

The FPA is particularly concerned about the impact on professional indemnity insurance premiums and the subsequent threat to small licensees. For some of our members their small business serves as their major asset for their family. The impact of rising professional indemnity insurance premiums poses a significant threat to the financial survival of these members and could lead to greater consolidation in the industry and reduced competition in the market, which would be detrimental for all stakeholders, especially consumers. Both the Government and ASIC, have on many occasions, stated their support for ensuring healthy competition in the financial services sector.

If the monetary limits increase further, it would inevitably increase the annual professional indemnity premiums for providers. The FPA notes the submission provided to FOS by the Insurance Council of Australia which states:

“…that there are practical reasons why at least for non-insurance disputes in the ILIS Division the current limit of $150,000 should be maintained. Pursuant to the Corporations Act the availability of professional indemnity insurance is a requirement for Australian Financial Services Licensees. Professional indemnity insurance depends on risks to the insurers being quantifiable and manageable. When significant issues which require careful legal consideration are settled instead in an EDR context, it becomes difficult for insurers to quantify such risks across AFS licenses. …EDR schemes do not provide the certainty of process and precedent necessary for important general insurance issues which may have wider application to insurers thereby impacting the availability of some classes of insurance.”

The FPA consider it a fundamental responsibility of FOS to consider and address the broader impacts of any monetary increase. FOS must ensure the professional indemnity insurers can and will provide cover compliant with ASIC requirements detailed in RG126: Compensation and insurance arrangements for AFS licensees at an affordable premium, for all EDR scheme participants, prior to any increase in the monetary limits.

4.6.2 Transition arrangements for increases in monetary limits

The FPA recommends that any changes to the FOS monetary limits or operations should include adequate transition arrangements to ensure providers and other parties to the broader consumer compensation mechanism, such as the professional indemnity insurance market, have the time to respond and comply. The timeframe for any monetary increase should be long enough to allow FOS to:

- ensure that affordable and appropriate professional indemnity insurance will be available to all scheme participants;
- address the issues of transparency and process; and
- identify an appropriate formula to determine the validity of any monetary increase.

4.6.3 Transparency and process

Before any consideration to increasing the FOS monetary limits, issues of the EDR scheme’s transparency and processes need to be addressed. There is a significant concern amongst FPA members that the FOS processes do not provide sufficient transparency for providers to assess the quality of and reasons for decisions.

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A sizeable proportion of the FPA’s membership recently surveyed hold the view that FOS limits should not be changed without significant improvements in process and transparency. The FPA supports its members in highlighting the need for greater consistency of decision making, improved transparency in its findings, and further attention to be given to the valid concerns raised by licensees, particularly small licensees.

The merger and establishment of FOS provides a significant opportunity for the scheme to address the very real concerns about the transparency of the EDR process and decisions, and to ensure the industry’s confidence in its operation. As stated previously, principle 1 of the Issues Paper states that the “regulator expects a genuine merger with a genuine potential for improvement”. We strongly encourage FOS to ensure this improvement occurs at both the Governance (Terms of Reference) and operational level.

While the FPA acknowledges the considered efforts the FOS ILIS Division has made in this regard, we believe there is still a need for substantial improvement. The FPA would welcome the opportunity to work with FOS to continue to address these issues and to improve the operation of the EDR scheme for the benefit of all parties.

4.6.4 Determining monetary limits

A clear methodology must be established for determining the monetary limits of the EDR scheme. The FPA considers that any increases to FOS monetary limits should be set on a reasonable and measurable basis with a methodology transparent to both consumers and providers. Determining the monetary limit should not be an arbitrary process of aligning to other schemes with fundamental different operating environments.

The FPA believes there is a need to develop a robust mechanism to determine and to justify any monetary limit increases in the future. The FOS monetary limits should be set on a firm, measurable and reasonable basis and specifically not linked to market events. To facilitate such an objective approach the FPA proposes the adoption of a formula-based methodology to determine any change to the limits.

In coming to this position, the FPA recognise that a thorough analysis should be applied when drawing up a sound and transparent methodology for determining monetary limits for FOS. The FPA recommends FOS conduct and publish research to determine the average claim amount. Aggregate data on compensation amounts would provide appropriate data on whether the monetary claim limits are suitable for the FOS jurisdiction.

The FPA suggests it would be fair and reasonable to implement a monetary limit based upon 95 per cent of compensation claims received by FOS. This methodology would be transparent, fair and easily understandable for both consumers and providers.

The FPA also recommends that the level of monetary limits should be specifically quarantined from linkage to market events. Financial planners should not be held responsible for events they do not cause and which are outside their control. (See section 5.2.3 Product performance for further information on this issue.)

4.6.5 Indexation and monetary reviews

The FPA does not support the FOS proposal to automatically increase the monetary limits in line with the CPI rate or the total average weekly earnings (MTAWE) every three years. As stated above, the FPA recommends monetary limits be determined by using an appropriate formula to ensure the limits reflect market conditions and consumer needs. We also recommend the monetary limits be reviewed every three years by the FOS Board using an appropriate formula and involving a thorough stakeholder consultation.

4.7 Monetary limit system versus an award cap system

The current monetary limits system means that any complaints with claims above the maximum compensation award are not able to be accepted into the scheme for investigation. The FPA notes that ASIC and FOS are considering replacing the monetary limit system with an award cap system.

An award cap system would allow FOS to accept and investigate all disputes but only make compensation awards up to a maximum monetary amount. The FPA believes that a cap system would increase the amount of vexatious claims, as well as claims more appropriately
deal with by alternative jurisdictions, significantly diverting resources away from those consumers with valid EDR claims and in need of assistance.

A cap system would place even greater and unnecessary pressure on the professional indemnity insurance market and lead to a further increase in premiums in an already very tight market. We remind FOS of the economic impact of professional indemnity insurance premiums particularly on small licensees. Many small licensees have an overriding concern of being forced to 'close the doors' to independent ownership due to the impossibly high and ever increasing professional indemnity premiums.

Subject to the suggestions noted in 4.7 above, the FPA recommends maintaining the current monetary limits approach.

4.8 Consumer ‘opt-in’ provision

As part of the ‘cap system’, the FPA notes that FOS and ASIC are considering the introduction of an ‘opt-in’ system which will allow consumers to reduce the amount of their claim to fall within the monetary limit of the scheme so they can access EDR. Under the opt-in system, if the consumer accepts the EDR decision, that decision would be binding on the complainant and the provider, and the consumer would be required to relinquish any future claim in any jurisdiction for any amount in excess of the scheme’s determined compensation award. However, the consumer may reject the scheme’s decision.

The FPA believes that an opt-in system would significantly increase the amount of vexatious disputes and consequently increase the pressure on the professional indemnity insurance market, which will drive up premiums and reduce the availability of appropriate cover, as well as threaten the independence of many small licensees.

The purpose of the EDR system is to provide a low cost alternative to the court system for small claims. The introduction of an opt-in system may defeat that by creating an influx of disputes which should be dealt with by alternative jurisdictions.

The FPA also believes that allowing any consumer to lower their claim amount to access the EDR jurisdiction is counter to the ASIC EDR principles of:

- fairness\(^3\) - an opt-in system ignores the ‘principles of procedural fairness’ for all stakeholders;
- efficiency\(^4\) - an opt-in system is inefficient as it opens the doors to disputes more appropriately dealt with in another forum; and
- effectiveness\(^5\) - an opt-in system would result in the development of inappropriate Terms of Reference which is not effective.

The FPA believes the introduction of the proposed opt-in system is likely to result in negative consequences for consumers, in particular inflexible compliance practices that will increase the cost of all advice and limited access to advice.

The FPA does not support the introduction of an opt-in system or an award caps system.

5. Dispute resolution

5.1 Decision making model

The FPA understands the aim of FOS to adopt an integrated model for decision making across disputes from all sectors and appreciates the proposal to introduce an appeal mechanism for EDR decisions. The FPA suggests that the decision making model of FOS should increase consultation, dialogue and engagement between the complainant and the provider, and seek resolution and settlement opportunities throughout the EDR process.

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\(^3\) RG139.151.3 Fairness – The scheme produces decisions which are fair and seen to be fair by observing the principles of procedural fairness, by making decisions on the information before it and by having specific criteria upon which its decisions are based

\(^4\) RG139.151.5 Efficiency – The scheme operates efficiently by keeping track of complaints, ensuring complaints are dealt with by the appropriate process or forum and regularly reviewing its performance

\(^5\) RG139.151.6 Effectiveness – The scheme is effective by having appropriate and comprehensive terms of reference and periodic independent reviews of its performance
Given that a major adverse determination by FOS can have a devastating impact on a small licensee, it is vital that the process, decision making model and EDR outcome is fair.

The FPA has previously raised concerns about frivolous and vexatious claims. Such disputes can have a significant impact on small financial planning practices as they consume a large percentage of their resources. These disputes drive up the cost of advising for all providers, which is ultimately borne by all consumers. The decision making model of FOS should encourage transparency, fairness and assist in reducing the number of vexatious claims.

The FPA suggests there is merit in a combination of the proposals provided in the FOS Issues Paper and recommends a hybrid of the Ombudsman and Panel decision making models (see Box 1).

The FPA believes FOS could significantly improve the transparency and understanding of its decisions if it adopted a more consultative approach to its pre-decision investigations. It would also assist in addressing the issue of invalid vexatious claims, enabling FOS resources to focus on those complainants with well-founded disputes. Hence, the FPA has recommended an ‘investigation/consultation stage’.

As there are a variety of industry practices that are acceptable ways of fulfilling financial planning objectives, there is significant subjectivity in how good and appropriate financial advice is provided to consumers. This subjectivity and the diverse and in-depth nature of financial advice can result in very complex disputes. The FPA suggests a panel of appropriate and diverse expertise is required to effectively consider and make decisions on financial planning disputes. The FPA considers the Ombudsman model, where one individual is responsible for decision making, is insufficient to meet the objectives of this stage of the EDR process, particularly for financial planning disputes.

The Panel at the ‘decision stage’ should consist of one consumer, one industry and one legal representative. The FPA recommends Panel members from all FOS divisions should meet regularly with industry bodies to discuss current market and industry developments and issues. This would provide a vital training opportunity for both the FOS panel members and industry participants.

Box 1: FPA recommended Decision Making Model

i) **Investigation/consultation stage** – senior FOS staff would analyse the merits of a complaint and demonstrate that a reasonable basis has been made based on the case evidence, for the claim to proceed through the EDR process. The complainant and provider should be offered mediation as an alternative resolution mechanism. FOS would provide both parties with a written assessment of the dispute and suggested recommendations for settlement for the consideration of the parties to the dispute and the Panel. At this stage, both parties should be given the opportunity to make a submission in response to the secretariat findings, prior to the dispute progressing to a Panel for a ‘decision’. Both parties to the dispute may agree to settle under this FOS recommendation and conclude the dispute. To enhance transparency, FOS submissions and recommendations to the Panel should also be provided to the complainant and the provider.

ii) **Decision stage** – a tripartite Panel makes a decision which is binding on the provider but subject to an appeal mechanism. The appeal mechanism should have strict guidelines and require an application process which should ensure only contestable Panel decisions are reviewed. There should be a time limit to lodge an application for appeal.

iii) **Appeal mechanism** – should the appeal application be accepted, a determination would be made by an individual Ombudsman or Panel but should not include those representatives who made the initial decision. The appeal determination would be binding on the provider if accepted by the complainant.
5.1.1 Appeal procedures

The FPA recommends an alternative appeal mechanism to that proposed in the Issues Paper (page 42). The appeal mechanism proposed by FOS is strictly aligned to the Ombudsman decision making model however the FPA believes a hybrid model would be more effective and would deliver better outcomes for consumers.

As detailed in Box 1, the FPA recommends a hybrid decision making model which includes an ‘investigation/consultation stage’, a ‘decision stage’ and an ‘appeal mechanism’. The FPA believes the ‘investigation/consultation stage’ should be consultative and offer opportunities to assist the parties to the dispute to reach a resolution. It is important to note that this stage is not an appeal mechanism. Under the FPA’s proposed model a formal decision on the dispute which is binding on the provider would still be pending at this ‘investigation/consultation stage’, hence an appeal cannot yet be offered.

The appeal mechanism must be available following the formal decision of the Panel in the decision making stage of FPA’s model. The appeal mechanism should have strict guidelines and require an application process which should ensure only contestable Panel decisions are reviewed. There should be a time limit to lodge an application for appeal and, should the application be accepted, a determination would be made by an individual Ombudsman or Panel but should not include those representatives who made the initial decision. The decision would be binding on the provider if accepted by the complainant. If an appeal application is accepted, both parties should be permitted to make submissions to the Appeals Panel for consideration.

5.1.2 Timeframes

RG139 and FOS Terms of Reference prescribe a limit for the length of time a complaint can remain within the financial service provider’s IDR process, after which a consumer may lodge a dispute with an EDR scheme. However, no such timeframes exist for the EDR process.

The FPA is concerned that some previous complaints have taken up to two years to be resolved through the EDR process. We acknowledge that the complexity of financial planning disputes take time to properly investigate and consider to ensure a fair outcome, however this delay significantly increases anxiety for consumers and the cost of EDR for providers.

Improving the efficiency of FOS, encouraging consultation between the complainant and the provider, and seeking resolution and settlement opportunities throughout the EDR process, would greatly assist in ensuring disputes are resolved in a more timely manner.

The FPA recommends the introduction of timeframes for the various stages of the EDR decision making model. Timeframes would enhance consumer understanding and expectations of the process, provide greater certainty of the EDR requirements for both the complainant and the FOS member, and ensure dispute resolution is achieved in a timely manner for both the complainant and the provider.

The EDR timeframes should be pragmatic, realistic and serve as a guide for complainants and providers. This would ensure there is flexibility in the timeframes for FOS and the parties to the dispute when it is critically needed to deliver a fair outcome.

5.2 Dispute resolution process

The FPA supports the dispute resolution process proposed by FOS in the Issues Paper (page 37) as complying with ASIC’s requirements for an EDR scheme. While we agree with the principle of limiting the amount of procedural detail in the Terms of Reference, we recommend the following amendments.

5.2.1 Exchange of information and confidential information

The FOS proposal states that “All information and documentation ... will be provided to all parties to a dispute”. The FPA recommends the provision of “all information and documentation” by FOS should be limited to “the complainant and the provider party to the dispute”. Witnesses who provide information and evidence to the dispute should not be provided with such information and documentation.
The FPA acknowledges that ASIC only requires the EDR scheme to “identify...using a list of the documents available, and provide on request, the information and documents relied on in making decisions” (RG139.48). However, the FPA believes that the provision of the actual documents and information to both parties is paramount as a matter of natural justice.

The FPA recommends that all information and documentation be provided to the complainant and provider party to the dispute, if confidentiality consent is granted. To enable this to occur both the claimant and the provider should be required to sign an agreement that forbids the use of the documentation in any other manner or forum (for example, in future legal proceedings).

Access to documentation would greatly assist in achieving transparency and fairness in the EDR scheme.

5.2.2 Criteria for decision making

i) Good industry practice

The FOS proposal states that “In making any decision in relation to a dispute FOS must have regard to iii) good industry practice”.

The FPA believes the complaints process and decisions of the FOS should recognise that there are a variety of industry practices that are acceptable ways of fulfilling financial planning objectives and there is currently no standard best industry practice. Hence, there is significant subjectivity in how good and appropriate financial advice is provided to consumers. The FPA recommends recognition of the diversity of good industry practice be included in the FOS terms of reference and the ILIS Division Rules.

ii) Fairness

The FOS proposal also states that “In making any decision in relation to a dispute FOS must have regard to iv) fairness in all the circumstances”.

Under the EDR principle of fairness ASIC requires that “The scheme produces decisions which are fair and seen to be fair by observing the principles of procedural fairness, by making decisions on the information before it and by having specific criteria upon which its decisions are based” [RG139.151.3]. The process of natural justice requires that the claimant and member understand the criteria on which they will be judged.

The FPA recommends that the ‘specific criteria’ upon which FOS bases its EDR decisions should be stated in its Terms of Reference. As such criteria should be industry specific, the FPA suggests the following addition to the proposed dispute resolution process in the FOS Terms of Reference:

c) In making any decision in relation to a dispute FOS must have regard to the:

  v) specific criteria detailed in the Terms of Reference or Rules of the FOS Divisions.

The FPA recommends FOS work with industry and consumer representatives to develop the industry specific criteria. These criteria should be made available to claimants, providers and the public in the Rules of the FOS divisions.

5.2.3 Product performance

As previously stated, the characteristics of financial advice disputes are different to disputes in other financial services. For example, most banking and general insurance services are bound by contract and therefore disputes relate to breaches of contract/policy, or to transactional and computational errors.

In financial advice, the Statement of Advice (SOA) is the legally defined, documented output of the advice for the client. It should not and cannot capture the detail of the inputs that inform the depth of the relationship between client and adviser and all of the communication that transpires between them. The inputs cover the financial planning process including the fact find, the analysis, the research, and the development of recommendations which are pre-requisites to the formulation of the advice and the production of the SOA. There are a variety of industry practices that are legally and professionally acceptable ways of fulfilling the financial planning process and objectives and there is significant subjectivity in how good and
appropriate financial advice is provided to consumers. All of these factors create 'shades of grey' in financial advice disputes.

Another characteristic of financial planning disputes is the consumer motivation for the dispute. Many consumers hold their planner responsible for any financial loss suffered in the market, no matter how it occurred, and commonly disregard any responsibility they initially accepted for their decision to invest.

The FPA believes the EDR system requires substantial breadth and depth in its consideration of disputes to ensure consumers are protected and compensated in cases of clear and extreme negligence or inappropriate advice, while providing a fair outcome in disputes of less significant wrongdoing.

For example, if a planner is found to have breached their disclosure obligations by inaccurately and unintentionally misrepresenting one feature of a product, the FPA suggests the severity of this action and the impact on the consumer’s decision should be given weight in determining the appropriate level of compensation. In this instance, if a product were to fail through an event outside of the planner’s control, the planner should not be responsible for compensating the full loss of the product failure. Any compensation payable by the planner should correspond to the materiality of the planner’s breach. The planner should not be responsible for compensation for factors outside their control or loss caused by other parties. This is comparable to proportionate liability under the law.

ASIC acknowledges the scope for proportionate liability as demonstrated by its actions in response to the Westpoint collapse. ASIC has pursued charges and sought consumer compensation from Westpoint directors, the CEO and founder, and even the auditors of Westpoint for their role in the loss incurred by investors from the collapse. However, to date, the only compensation paid to investors has been from planners.

The FPA is also concerned about the impact on disputes before FOS of the consumers changing levels of comfort with and responsibility for their investment decision. Anecdotal evidence shows consumers’ attitude and level of comfort with an investment decision has been seen to change depending on the performance of the product. A consumer may be comfortable with a product when the advice is given, even if they are aware that the investment may be in a high risk category. This attitude changes if the product performance is unsatisfactory. Clients also accept responsibility for their decision at the time of the initial investment, but reject this responsibility when the product performance is unsatisfactory.

FOS proposes to exclude “The performance of an investment product, except a dispute concerning non-disclosure or misrepresentation” from its jurisdiction. However, the FPA notes that this clause currently exists in the FICS Rules yet planners are continuing to fully compensate clients for product failures.

The FPA recommends additional provisions should be included in the FOS Terms of Reference which require FOS, the decision making Panel and the Ombudsman, to take into account the severity of the cause of the inappropriate advice, misrepresentation or non-disclosure, as well as the role of the complainant and other parties, in its consideration of financial advice disputes. The FPA strongly believes the FOS decision and compensation should be commensurate with the action/inaction of the financial planner.

Consideration should also be given to the consumer’s level of comfort with the product at the time of investment and their responsibility for the investment decision at the time the advice was given.

5.2.4 Mediation

The FPA recommends the inclusion in the Terms of Reference dispute resolution procedures, a provision that states that FOS will promote to complainants and providers the availability of mediation and conciliation services for disputes. We believe the complaints handling process should encourage the use of mediation between the IDR and EDR stages.

Introducing a mediation stage into the complaints handling process prior to participation in the EDR process, would provide a less confrontational approach to complaint resolution. This would allow the member and consumer greater control in determining the outcome of the complaint and reduce the need to continue through the EDR process. It would also reduce the use of legal representation as a requirement of the member’s professional indemnity insurer.
5.3 Reasons for decisions

Part of the requirement of the principle of fairness in an EDR scheme is to provide the basis for its belief that the provider has done something wrong. High level generic explanations such as ‘inappropriate advice’ or ‘breach of duty of care’ do not provide appropriate, adequate, or understandable reasons for the basis for the EDR decision.

The FPA suggests the FOS determinations should provide detailed reasons explaining why FOS considers the financial planner is at fault. This should include a detailed response to each of the ‘specific criteria’ used in the decision making process required under the principle of EDR fairness (RG139.151.3), as discussed above. This would significantly enhance the transparency, fairness and process of the scheme for both the complainant and the provider.

Providing detailed reasons for decisions would also assist the profession to minimise the possibility of re-occurrence and improve the quality of advice for consumers.

As previously stated, the FPA also believes that it is inappropriate for FOS to award compensation that has been calculated on the basis of market loss and losses from product failure, elements which are outside the control of the planner. There is a need for the EDR scheme to clearly differentiate between financial loss suffered from circumstances that were not caused by the financial planner, such as product failures and market downturn, and financial loss resulting from inappropriate advice.

FOS Terms of Reference clearly delineate the boundaries of the coverage of complaints. Only complaints or the part of the complaint relating to the appropriateness of the advice should be investigated and considered by the EDR scheme. FOS compensation should only be awarded if the loss has been the result of inappropriate advice or planner misconduct. Product performance should be excluded from FOS’s decisions making process and reasoning of their decisions.

6. Awarding compensation

6.1 Compensation for non-financial and consequential loss

FOS proposes to broaden its compensation powers to include non-financial and consequential loss. FOS would also set out detailed guidance as to its approach in awarding compensation for non-financial and consequential loss.

The FPA considers it to be inappropriate for FOS to have the ability to award non-financial and consequential loss. This would be against the concept of fairness, potentially open-ended, and practically difficult to determine.

The inclusion of compensation for non-financial and consequential loss in the FOS jurisdiction would undoubtedly cause an escalation of professional indemnity premiums, which may devastate small licensees and reduce advice options for consumers.

It would require experts to examine, prove and explain how/what/why non-financial and consequential loss has occurred and the impact of such loss. The FPA considers this cannot be adequately dealt with in the EDR forum as such claims could be very contentious and would require a substantial amount of evidence and specialist knowledge to consider. The inclusion of non-financial and consequential loss in the FOS jurisdiction would significantly impact on the timeliness of the EDR process and has the potential to create excessive delays in the EDR system.

The FPA recommends the awarding of compensation for non-financial and consequential loss be excluded from the EDR jurisdiction.

6.2 Awarding interest

Currently the cap for interest amounts for advice disputes is $50,000 under the FICS Rules\(^6\). If this were to be awarded in addition to the monetary limits, it would effectively increase the compensation award by 33 per cent. This would have a significant impact on professional indemnity premiums and inevitably impact on the cost of advice for consumers and the ability for small licensees to maintain their business.

\(^6\) In the case of a disability income policy the interest awarded may not exceed the lesser of $50,000 or five times the monthly benefit under the policy. FICS Rules clause 34.1
The FPA recommends any award of interest should be included within the monetary limit and that the mechanisms used to calculate interest should be robust, transparent and should not extend to consequential loss.

7. **Test cases**

The FPA supports the preferred option proposed by FOS in the Issues Paper (page 44), which states:

“Provided that an appeal stage is built in to the processes, a financial service provider may give notice of a ‘test case’ in response to an initial written decision by FOS. The criteria for the test case would be:

a) an issue which may have important consequences for the business of the financial service provider or financial service providers generally;

b) an important or novel point of law.

The financial services provider will pay the consumer’s costs in relation to the initial proceedings and any appeal on a solicitor/client basis.”

The FPA believes the proposed provisions provide a balance between the needs of all parties. However, in relation to the payment of costs there may be some circumstances when the court may rule otherwise and therefore flexibility should be permitted. The FPA suggests the following addition:

“The financial services provider will pay the consumer’s costs in relation to the initial proceedings and any appeal on a solicitor/client basis, unless the court rules otherwise.”

8. **Reporting externally**

The FPA would welcome FOS guidance on what constitutes ‘serious and systemic’ issues, as proposed in the Issues Paper. We recommend the new FOS guidance be developed in consultation with industry.

The FPA recommends FOS clearly identify and provide regular reports to members on the underlying causes of complaints. The FPA suggests this should include detailed information relating to the underlying cause(s) of disputes, rather than generic categorisation of disputes. This would facilitate appropriate operational change and assist the FPA and its members to identify appropriate business changes to minimise the occurrence of disputes and assess the effectiveness of past modifications.

Collection of information relating to the underlying cause of the disputes is already required under RG139.83 and should therefore not impose any additional burden on the EDR scheme.

9. **Other issues**

9.1 **FOS Constitution – Removal of member veto powers**

The FPA notes that this consultation is about the FOS Terms of Reference, not the FOS Constitution, however the FPA feels strongly about development of the Constitution.

The FPA is disappointed that FOS did not conduct a robust member consultation to develop its Constitution. The removal of the member voting rights relating to changes to the Scheme’s Terms of Reference and Rules was removed without a serious consideration of member views.

FOS is a ‘company limited by guarantee” and therefore removing members’ powers to veto substantially undermines the rules of good corporate governance and members’ basic rights of a company.

The FPA does not support the removal of members’ ability to veto proposed amendments to the EDR scheme’s Terms of Reference and Rules. As an alternative, we recommend the retention of the veto provisions with the introduction of more stringent restrictions to members’ vetoing rights. The FPA suggests a ‘special resolution’ of 75 per cent of members who are eligible to vote on a matter, be required to veto a particular change to the FOS Terms of Reference and Rules. This would ensure the principles of good corporate governance expected of a guaranteed company are adhered to.
The FPA also notes ASIC’s proposal to remove members’ vetoing powers from the EDR system.

9.2 Transitional arrangements

The FPA is concerned that the FOS Issues Paper is silent on the vital matter of transition arrangements.

The FPA recommends that any changes to the FOS monetary limits or operations should include adequate transition arrangements to ensure providers, and other parties to the broader consumer compensation mechanism, have the time to respond and comply. The FPA suggests that FOS has a responsibility to develop transition arrangements reflective of the markets capacity to support the new Terms of Reference. The FPA recommends the transition to the new Terms of Reference or any increase in the monetary limits should be sufficient for FOS to:

- ensure affordable and appropriate professional indemnity insurance will be available to all scheme participants;
- address the issues of transparency and process;
- develop and publish ‘specific criteria’ for decision making; and
- identify an appropriate formula to determine the validity of any monetary increase.

The FPA would caution FOS against a blanket ‘12 month shift’ approach to transition. We would welcome the opportunity to work with FOS to identify appropriate transition arrangements.