

# **Australian Banking Industry Ombudsman**

## **Submission to the Financial System Inquiry**

**4 September 1996**

### **Views of the Ombudsman**

The views expressed in this document are the views of the Ombudsman and not the views of the Council or the Board of the Australian Banking Industry Ombudsman Scheme (Scheme).

### **The Scheme**

The Scheme was announced in 1989 as a joint initiative of the banking industry, government and consumer organisations. It commenced operations in 1990. It is the first industry funded, independent alternative dispute resolution scheme established in Australia.

The Scheme provides a free service for the independent resolution of consumer complaints about the provision of banking services by member banks.

### **Summary of Recommendations**

1. Access to alternative dispute resolution (ADR) should be available to all retail consumers in the financial services sector.
2. ADR schemes in the financial services sector need to be independent, well resourced, efficient and able to ensure high quality and consistency in their decision making.
3. Non bank financial institutions (NBFIs) providing retail financial services and products should fund their own ADR schemes.
4. An ADR organisation, such as the Scheme, should operate a central referral service for all consumers of retail financial products and services and that referral service should be funded by retail financial service providers.

5. An appropriate authority should have responsibility for ensuring the security of the electronic payment system.
6. ADR schemes in all sectors of the finance industry should play a role in improving communication between consumers and financial service providers.

### **Recommendation 1:**

**Access to alternative dispute resolution (ADR) should be available to all retail consumers in the financial services sector.**

#### ***Discussion:***

##### **Value of ADR**

There remains a need to ensure that the individual consumer, small investor or small business operator is not substantially disadvantaged by market power.

In summary, ADR for customers who have a complaint, means providing an alternative to the courts. It is a process which embodies:

*...the preference for harmony over conflict, for mechanisms that offer equal access to the many rather than the unequal privilege to the few, that operate quickly and cheaply, that permit all citizens to participate in decision making rather than limiting authority to the professionals, that are familiar rather than esoteric, and that strive for and achieve substantive justice rather than frustrating it in the name of form.<sup>1</sup>*

Effective ADR also yields practical and commercial benefits to member service providers. These include the benefits of savings through the avoidance of litigation, increased consumer satisfaction and assistance in identifying product and service deficiencies. It acts as a catalyst for streamlining complaints handling.

##### **Commitment to ADR**

The most recent reflection of the banking industry's commitment to ADR is enshrined in section 20.4 of the Code of Banking Practice which provides:

*A Bank shall have available for its Customers free of charge an external and impartial process (not being an arbitration), having jurisdiction similar to*

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<sup>1</sup> Abel, R. "The Contradictions of Informal Justice" in the Politics of Informal Justice, vol. 1 (ed. Abel, R) Academic Press, NY 1982.

*that which applies to the existing Australian Banking Industry Ombudsman Scheme, for resolution of a dispute that comes within the jurisdiction and is not resolved in a manner acceptable to the Customer by the internal process referred to in Section 20.1.*

There are separate codes of practice in place for credit unions and building societies. These appear to be modelled on the Code of Banking Practice and commit both credit unions and building societies to providing their customers with a free ADR process. However, they have not yet been implemented.

### **Electronic Funds Transfer (EFT) Complaints**

The existence of an ADR service is especially important in relation to EFT complaints.

EFT complaints are determined by application of the EFT Code of Conduct (EFT Code) and the bank's terms and conditions of use to a factual situation. The amounts involved in these disputes generally vary between approximately \$100 to \$5000. The Ombudsman is the primary person actively interpreting and applying the EFT Code to dispute resolution.

The Ombudsman has been largely responsible for the development of policy in relation to interpreting the EFT Code because the amounts involved frequently preclude costly litigation, so that courts have not contributed to interpretation in this area.

Information is disseminated on a regular basis to educate consumers and their banks about PIN security and the application of the EFT Code. This area of banking always raises comment in the press, among consumer advocates and financial counsellors.

As the primary decision maker in this consumer sensitive area, the types of complaints received about EFT are closely monitored. The expansion of this area of banking including banking on the Internet and telephone banking are areas in relation to which policy is being developed.

The Scheme has also established a web site on the Internet for receipt of complaints.

The Scheme is inquisitorial in nature and this means that banks provide all the information which may be relevant to a complaint including policy, procedure manuals and security information on a confidential basis.

This kind of Scheme is therefore vital in continuing to maintain the level playing field and maintaining consumer confidence as these technologies increase.

## Conclusion

In summary, if there is to be:

- an expansion in electronic banking
- different types of outlets to replace branch networks
- a reliance on telephone banking
- greater development of banking on the Internet
- more options offered by a wider range of financial institutions

the impact if problems arise will be that both consumers and their financiers:

- will need access to ADR
- will look for equality of treatment in dispute resolution.

Options currently offered to consumers of financial services seeking redress depend primarily on the institutional classification of the service provider. This means that some consumers with the same financial product will have access to ADR and some will not.

The real effect for consumers is that a significant issue for them in terms of choice of service provider and product is not appreciated until it is too late.

Consumers and small businesses need access to personal, housing and business finance; they also need to be able to resolve any problems in a fair, efficient and cost effective way. ADR provides that option.

## Recommendation 2:

**ADR schemes in the financial services sector need to be independent, well resourced, efficient and able to ensure high quality and consistency in their decision making.**

### *Discussion:*

#### **Independence**

It is axiomatic to the effectiveness of any industry based scheme, that the independence of the decision maker is preserved.

This Scheme has a tripartite structure: a Council, a Board and the Ombudsman. The Council consists of equal numbers of consumers and bankers and an independent chairman. The Ombudsman reports to the Council.

The Board is a separate entity which levies the member banks for the funds to run the Scheme. Those banks are members of the company and the board members are directors of that company.

### **Complaint Handling Expertise**

The Scheme has excellent systems, processes, technology and skills to efficiently handle substantial volumes of enquiries and complaints including:

- customised computer tracking of cases
- compliance with international standards for telephone response
- independent auditing of the decision making process
- quality assurance.

### **Funding**

The banks have provided resources sufficient to meet increased demands to maintain the Scheme's pre eminent role in ADR.

### **Binding Nature of Decisions**

The Scheme operates effectively and efficiently because the member banks agree to be bound by the final decision of the Ombudsman.

### **Conclusion**

It is fundamental to the fair, efficient and cost effective operation of industry based ADR schemes that they be well funded; the decision maker's independence is preserved and that the members of the scheme agree to be bound by the decisions of the decision maker.

### **Recommendation 3:**

**Non bank financial institutions (NBFIs) providing retail financial services and products should fund their own ADR schemes.**

#### ***Discussion:***

#### **Level of Complaints**

Market research conducted by the Scheme has confirmed that the implementation of the Scheme has proved effective in terms of increased consumer confidence in obtaining access to justice and increased customer retention for the banks. Complaints are received in writing and over the telephone.

Year	Telephone enquiries	New written complaints
1993 - 1994	26,000	3,115
1994 - 1995	28,000	3,451
1995 - 1996	31,000	3,509

#### **Excluded Complaints**

Of the complaints received by the Scheme, a significant percentage do not fall within the jurisdiction of the Scheme. Of the complaints received, the following percentages were complaints which fell outside the Scheme's Terms of Reference:

Year	Telephone complaints	Written complaints
1993 - 1994	35.2%	35.7%
1994 - 1995	22.4%	28.9%
1995 - 1996	28.2% (or 8,742)	29.2% (or 1,024)

There is a high level of frustration for complainants when they discover that their complaint does not fall within the jurisdiction of the Scheme.

The highest percentage of these complaints were outside the Terms of Reference because they were complaints about NBFIs.

Another significant reason for exclusion was because the Scheme does not extend to small businesses which have been incorporated. Of the complaints received, which fell outside the Terms of Reference, the following percentages show the proportion of complaints which were outside the Scheme's jurisdiction because they concerned NBFIs or were made on behalf of corporations:

Year	NBFI telephone	NBFI written	Corporation telephone	Corporation written
1993 - 1994	15.7%	12.5%	9.9%	19.4%
1994 - 1995	28%	14.4%	8.7%	18.3%
1995 - 1996	27.1% (or 2,369)	11.3%	9.6%	15.9%

## **Conclusion**

The expansion of NBFIs into traditional banking areas has already generated a significant level of complaints. Further expansion and an increase in the number of players will add to the confusion among consumers about their avenues of redress and increase the number of complainants looking for a forum for their complaints.

While banks have long held the primary role in traditional retail banking, they have also fulfilled their commitments to their stakeholders by funding efficient and independent ADR. It is hoped that NBFIs, who provide a diverse range of financial services, will view the provision of an ADR service as an investment in corporate responsibility.

## **Recommendation 4:**

**An ADR organisation, such as the Scheme, should operate a central referral service for all consumers of retail financial products and services and that referral service should be funded by the retail financial service providers.**

## ***Discussion:***

### **Liaison**

The Scheme acts as a conduit for the referral of complainants to other forums.

As a corollary to the service provided to customers of banks, a high level of understanding of the jurisdictions of other forums which may be appropriate for complaint referral has been developed. These forums include:

- Financial Planning Association Complaints Resolution Scheme (FPA),
- EFT Credit Union Arbitrator
- Credit Union Services Corporation (Australia) Ltd (CUSCAL)
- Credit Union Dispute Reference Centre Ltd
- Australian Finance Conference
- Life Insurance Complaints Service Limited
- General Insurance Enquiries and Complaints Scheme,
- Superannuation Complaints Tribunal

- National Insurance Brokers Association of Australia's Insurance Broker Dispute Facility
- Office of the Privacy Commissioner.

Whenever possible, complaints about building societies, credit co-operatives, credit unions, friendly societies, housing co-operatives and other NBFIs are referred to an appropriate forum. The Scheme's systems allow for appropriate referrals to the Commonwealth and State Ombudsmen, community legal centres, the Credit Reference Association of Australia and financial counselling services throughout Australia.

The Ombudsman meets regularly with other managers of ADR schemes and other Ombudsmen. This group has developed mechanisms for referral and provides information about access to these schemes through formal presentations. The Ombudsman has also chaired a working party looking at the overlap of ADR schemes in traditional banking products, financial and insurance advice and services.

The Scheme has developed an informal memorandum of understanding with the FPA for referral of cases between offices and has initiated discussions with the office of the Privacy Commissioner for the development of the same. We have also provided advice regarding the development of the CUSCAL dispute resolution scheme, whose Terms of Reference are closely modelled on the Scheme's.

### **Costs**

Non-member financial institutions reaping benefits from this Scheme should be charged a transfer price for the referral of complaints. This would ensure that service providers take responsibility for their market conduct whilst benefiting from the central service's integrity and investment in infrastructure.

### **Conclusion**

It is inevitable that there will be a continued expansion of both NBFIs and banks into historically non traditional service areas. As the functional distinctions disappear, from the consumer's perspective, there may be merit in the establishment of a central clearing service for all complaints from consumers of financial services. This is of course predicated on the expectation that responsible financial service providers will establish and fund effective ADR schemes which satisfy the criteria identified in this submission.

As discussed, this Scheme presently provides a comprehensive but informal complaint referral service. Given the Scheme's expertise and community standing, the Ombudsman sees the opportunity for the Scheme or a similar entity to adopt a formalised role in providing a centralised referral service. It

is envisaged that such a service would utilise advanced telephone referral systems and facilities for electronic transmission of information for secure, efficient and expedited referrals.

### **Recommendation 5:**

**An appropriate authority should have responsibility for ensuring the security of the electronic payment system.**

### ***Discussion***

#### **Nature of Complaints**

Since the commencement of the Scheme in 1990, this office has consistently received the highest proportion of complaints about housing loans, personal loans and payment systems including ATM and EFTPOS.

Year:	Housing Finance:	Consumer Finance:	Payments Systems:
1990 - 1991	22.6%	17.4%	11.7%
1991 - 1992	20.9%	20.8%	20.6%
1992 - 1993	24%	18%	16%
1993 - 1994	22.7%	20.8%	15.3%
1994 - 1995	21.1%	17.6%	18.1%
1995 - 1996	28.4%	19.5%	18.9%

The scope of complaints has increased as banks have expanded the services they offer. These include complaints about financial and investment advice, insurance products and electronic banking services.

#### **The Future of Electronic Banking and the impact on ADR**

Given the nature of the complaints the Scheme receives, one of the most significant issues for the Scheme concerns the development of electronic banking.

Concerns about the security and reliability of electronic networks are paramount for consumers and for this office which cannot supervise these networks. At present, the Ombudsman relies on the advice of the Australian Payments System Council that the ATM and EFTPOS system is secure, and, accordingly, has no grounds for believing that the system is not secure.

It also appears that much work must be done to develop standard security protocols for Internet banking to ensure secure key encryption and digital authentication.

### **Conclusion**

The need for a watchdog/regulator in this area is of significant importance in order to encourage use of the systems; the advantages they offer being readily available and the positions of the finance providers and the consumers being secure in terms of understanding, reliance and recourse.

### **Recommendation 6:**

**ADR schemes in all sectors of the finance industry should play a role in improving communication between consumers and financial service providers.**

#### ***Discussion:***

##### **Product Disclosure and Bank Feedback**

The Scheme has a unique role in the financial system by virtue of its intimate knowledge of the workings of the banker-customer relationship. In addition, the Scheme has first hand knowledge of the problems facing consumers and is able to provide feedback to banks about particular products and the marketing of financial services.

With the expected rapid development of financial services and anticipated outsourcing of the sales of financial products and services through agents, kiosks, mortgage brokers and the like, there is a greater potential for misunderstanding between consumers and providers.

The value of choice can be lost if the provider cannot educate its customers about what is being offered. For example as a result of increased competition in the home loan market, consumers have been offered a much wider range of products with a broader range of features, than was the case prior to deregulation. These include:

- honeymoon rates
- various switching options
- two in one accounts
- portability
- redraw options

However, the cases referred to the Scheme confirm that the increase in the choices available has not necessarily meant that consumers are able to make informed decisions about which product to select.

In this environment, the potential benefits of a formal feedback relationship between ADR schemes and the financial service providers cannot be underestimated. Similarly, the ADR schemes can play an important role in

educating consumers to understand the options they have through formal reporting to consumer organisations and informal coverage in the media.

## **Conclusion**

The key issue for financial service providers and their customers will continue to be communication:

- consumers want the finance provider to understand their financial needs
- finance providers are seeking to fulfil all of the disclosure requirements associated with the sale of a product
- consumers are looking for tailored products
- the success of the relationship depends on the effectiveness of the parties' communication
- the new forms of communication will be electronic and telephonic
- complaints and concerns will need to be addressed
- finance providers and their customers will need to adapt to the changing environment of financial services and

this will require high levels of confidence, communication, training and feedback.

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