



Australian Financial Services Sector: Review into the Effectiveness and Shortcomings of The External Dispute Resolution Frameworks and Compensation Mechanisms from 2008 to 2020

SR Group Paper

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## Abbreviations and Key References

AFCA	Australian Financial Complaints Authority
APRA	Australian Prudential Regulatory Authority
ASIC	Australian Securities and Investments Commission
CIO	Credit and Investments Ombudsman
CSLR	Compensation Scheme of Last Resort
EDR	External Dispute Resolution
Finance	Department of Finance
FSRC	Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry
FOS	Financial Ombudsman Service
SCT	Superannuation Complaints Tribunal
Treasury	Department of the Treasury

The *Review of the financial system external dispute resolution and complaints framework* chaired by Professor Ian Ramsay is heavily referenced in this paper. This review is subsequently referred to as ‘the Ramsay Review’.

Additionally, the following documents are referred to extensively:

- The Final Report of the Ramsay Review.
- The Supplementary Financial Report of the Ramsay Review.
- Volume 1 of the Final Report of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry.

### About the SR Group

The SR Group is a financial advisory and advocacy firm based in Sydney, Australia which strives for a fair and accessible Australian financial system for all participants. Through our advocacy division, the SR Group represents approximately 5,000 consumers who have suffered financial losses due to misconduct in the financial services sector. SR Group assists these consumers in seeking access to redress, compensation, and justice.

The SR Group represents consumers with claims for compensation arising from misconduct which occurred from 1 January 2008 onwards. The SR Group considers that the imposition of a suitable timeframe is necessary when considering access to redress for past disputes. We consider a suitable timeframe to be complaints arising from misconduct which occurred on or after 1 January 2008, consistent with the period examined by the Royal Commission. This timeframe is also consistent with the time frame afforded to AFCA to consider historical ‘legacy’ complaints.

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## Introduction

The financial system plays an important role in Australia, with its ultimate purpose to facilitate sustainable economic growth by meeting the financial needs of its users. The financial system's role in the economy and the lives of individual Australians continues to grow and evolve, particularly with the introduction of compulsory superannuation<sup>1</sup>. The increase in interactions between consumers and the financial system inevitably increases the demand for dispute resolution. Although the number of disputes remains small proportionate to the overall number of interactions, the impact of financial disputes on consumers can be immense.

As a result, external dispute resolution (EDR) providers play an essential role in the Australian financial system, allowing participants to access fair and impartial dispute resolution in a cost effective and timely manner. It is therefore critical that the external dispute resolution framework and complaints mechanism within the Australian financial system functions accurately and delivers appropriate outcomes to its users.

To ensure this, in August 2016 the Government commissioned the '*Review of the financial system external dispute resolution and complaints framework*' ('the Ramsay Review'), a comprehensive review into the contemporary EDR framework in Australia. The Ramsay Review authored a Final Report and subsequently a Supplementary Final Report which initiated a series of reforms to the EDR framework. These reforms have strengthened consumer protections and the financial services sector as whole.

However, our experiences as a consumer advocacy firm have illustrated that some aspects of the legislation and EDR framework have had unintended consequences whereby some consumers have been excluded from accessing redress, either through an EDR provider or alternative avenues. It is unfortunate that elements of the EDR framework between 2008 and 2020 have precluded consumers from accessing redress in situations where they have fallen victim to financial misconduct. This misconduct has resulted in significant financial losses for the affected consumers, the impact of which is compounded by the consumers inability to access redress.

Through the Ramsay Review and subsequent Financial Services Royal Commission, refinements have been made to Australia's EDR framework to address these deficiencies and improve redress mechanisms going forward. While necessary, there remains a cohort of consumers who have suffered considerable financial losses that have to date not been able to access redress whatsoever.

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<sup>1</sup> Ramsay Review Final Report (pg. 7)

## Background to the Current Dispute Resolution and Compensation Environment: Ramsay Review and the Royal Commission

In this section, the paper will explore the relevant reviews, commissions and reports which have shaped the EDR framework and compensation mechanisms of today.

### Ramsay Review: Final Report, 3 April 2017

The Ramsay Review was the first comprehensive review into the EDR and complaints framework in the Australian financial system, conducted by a panel chaired by Professor Ian Ramsay, as well as Ms Julie Abramson and Mr Alan Kirkland (“the Panel”).

On 8 August 2016, the Terms of Reference of the Ramsay Review were released. The Panel conducting the review was required to consider whether the contemporary EDR mechanisms in the Australian financial system were providing appropriate outcomes to consumers, and whether changes to the EDR mechanisms were necessary to facilitate their ongoing effectiveness.

As noted by the Panel, the Ramsay Review was both timely and important<sup>2</sup>. The Panel acknowledge the importance of the financial system in Australia as its role in the lives of Australians grows and evolves, particularly with the introduction of compulsory superannuation.

For effective operation of the financial system, it is important that consumers have access to EDR mechanisms when disputes arise between themselves and other participants in the financial system. Further, EDR mechanisms must deliver effective and appropriate outcomes to their users, or risk compromising consumers trust in, and potentially their engagement with, the Australian financial system. The necessity of a well-functioning EDR mechanism in the Australian financial services landscape is outlined by the Panel:

This increase in interactions between individuals and the financial system inevitably increases the demand for dispute resolution. Although the number of disputes remains small compared to the overall size of the system and the number of interactions individuals have with it, the impact of financial disputes on the lives of individuals and their families can be devastating.

...

When things go wrong, it can have distressing consequences for individuals and families. There have been a number of financial collapses in the past 10 years that have affected over 80,000 consumers, with losses totalling more than \$5 billion, or \$4 billion after compensation and liquidator recoveries. Common factors have been consumers receiving poor advice, having difficulty understanding complex documents and products and, in some cases, being taken advantage of for their lack of financial literacy. In these and other circumstances, it is important that people have access to effective redress mechanisms. (Ramsay Review Final Report, pg. 7-8)

During their review, the Panel found that the contemporary EDR framework was ineffective, obsolete, and requiring amendment. Users of the EDR framework were in some cases unable to achieve the appropriate resolution to their disputes, and in other cases, not able to achieve a

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<sup>2</sup> Ramsay Review Final Report (pg. 7)

resolution at all. Similarly, flaws in the legislation created loopholes in the EDR scheme requirements which resulted in inconsistent outcomes across comparable or identical situations.

Following their review, the Panel declared that:

A number of features of the design of the current system mean that it is not producing the best possible outcomes for some users, in particular, consumers.

...

The Panel found that the current framework is the product of history rather than design and, in significant areas, reform is needed. The existence of multiple EDR schemes with overlapping jurisdictions means: it is difficult to achieve comparable outcomes for consumers with similar complaints; it is more difficult for consumers to progress disputes involving firms that are members of different schemes; and there is an increased risk of consumer confusion. Multiple EDR schemes also result in duplicative costs for industry and for the regulator. (Ramsay Review Final Report, pg. 8)

As a result, the Panel delivered its primary recommendation that a new, single EDR body for all financial disputes (including superannuation disputes) be established to replace the existing EDR bodies; the Financial Ombudsman Service (FOS), the Credit and Investments Ombudsman (CIO), and the Superannuation Complaints Tribunal (SCT). The Panel also delivered further recommendations to close the loopholes and address the inconsistencies identified in the contemporary EDR framework.

In total, the Panel made 11 recommendations for the enhancement of the EDR framework in the Australian financial system. These recommendations were structured to reflect the evolving nature of financial services in Australia and facilitate greater access to dispute resolution for financial system participants. Salient design features included recommendations that:

- The new EDR body should be governed by an independent chairperson and board, consisting of an equal number of directors with industry and consumer backgrounds.
- Membership of the EDR body should be compulsory through a licensing condition or equivalent requirement for financial firms.
- The new EDR body should have higher monetary limits and compensation caps than the previous EDR schemes, to facilitate greater access to redress for consumers.

The Panel's view was that the implementation of these recommendations would allow more disputes to be resolved and ultimately provided greater access to redress for viable claims.

On 3 April 2017, the Panel provided to the Government its Final Report on the matters covered by the Ramsay Review's initial terms of reference. On 9 May 2017, the Government released the Panel's April 2017 Final Report and the Government's response to that Report. The Government accepted all 11 recommendations in what was termed a 'radical overhaul' of the EDR framework<sup>3</sup>.

In accordance with the Panel's recommendations, a new EDR body, the Australian Financial Complaints Authority (AFCA), was established to take the place of FOS, CIO and SCT. AFCA commenced operating in November 2018.

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<sup>3</sup> Scott Morrison Media Release, 'Building an accountable and competitive banking system', 9 May 2017 (<https://ministers.treasury.gov.au/ministers/scott-morrison-2015/media-releases/building-accountable-and-competitive-banking-system>)

## The Ramsay Review: Supplementary Final Report, 6 September 2017

On 2 February 2017, the Minister for Revenue and Financial Services, The Honourable Kelly O'Dwyer, amended the Ramsay Review's Terms of Reference to include recommendations on the establishment, merits and potential design of a CSLR<sup>4</sup>. The Panel was also asked to consider the merits and issues involved with providing access to redress for past disputes. From the outset, the Panel highlighted the importance of access to redress in the financial system:

In its April 2017 Report, the Panel noted that access to redress is critical. If consumers and small businesses are unable to access redress, this can lead to severe financial hardship and, more broadly, subsequent loss of trust and confidence in the EDR framework and the financial system. (Supplementary Final Report, page 24)

In delivering the Supplementary Final Report, the Panel structured the report in three parts<sup>5</sup>. The separation of the three parts of the Supplementary Final Report represent small but important distinctions between the consumers affected by each section and their circumstances.

In Part 1, the Panel assesses and makes recommendations on the establishment, merits, and potential design of a CSLR. The consumers affected by Part 1 are future consumers who receive determinations for compensation from an EDR provider (i.e. AFCA), though do not receive their compensation from the perpetrating firm due to insolvency or other reasons. Part 1 of the Supplementary Final Report considers and makes recommendations on whether establishing a CSLR to compensate such consumers is appropriate, and if so, how a CSLR should be designed.

In Part 2, the Panel discusses and makes observations on legacy unpaid EDR determinations. Consumers affected by Part 2 are past consumers who have previously received a determination for compensation in their favour from an EDR provider scheme (i.e. FOS, SCT or CIO) which remains unpaid. Part 2 considers how these consumers should be dealt with.

In Part 3, the Panel makes observations on the merits and issues involved in providing access to redress for past disputes. Consumers affected by Part 3 are past consumers who have not previously been able to access an EDR provider and have their case considered due to circumstances beyond their control. Part 3 considers how these consumers should be dealt with. The consumers represented by the SR Group are primarily those consumers affected by Part 3 of the Supplementary Final Report.

As required by the Terms of Reference, the Panel makes recommendations in respect of the issues considered in Part 1 of the Supplementary Final Report, and observations in respect of the issues considered in Parts 2 and 3.

### **Part 1: A Compensation Scheme of Last Resort (CSLR)**

In Part 1 of the Supplementary Final Report, the Panel makes four recommendations, the most salient of which is that a 'limited and carefully targeted' CSLR should be implemented into the Australian EDR framework. Specifically, the Panel recommends that in situations where consumers have compensation awarded to them through AFCA, a court or a tribunal, but are unable to receive payment after taking reasonable steps, the CSLR is to step in and pay the awarded compensation to the consumer.

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<sup>4</sup> Ramsay Review Supplementary Final Report (pg. vii)

<sup>5</sup> Ramsay Review Supplementary Final Report (pg. 27)

The Panel also makes further recommendations regarding the design, operation and eligibility criteria for an Australian CSLR.

## **Part 2: Legacy Unpaid EDR Determinations**

In Part 2 of the Supplementary Final Report, the Panel makes observations about how to address legacy unpaid EDR determinations. The situations of the consumers in Part 2 of the Supplementary Final Report, where consumers receive a determination but do not receive payment, are the situations that the Panel has sought to eliminate in future through the implementation of a CSLR.

Notwithstanding the CSLR reforms recommended by the Panel, there remained the issue of consumers who possess a determination for compensation in their favour, though despite reasonable efforts, have been unable to receive that compensation. For these consumers, the Panel observed that there is a strong case for such consumers being paid their awarded compensation<sup>6</sup>.

The Panel also observed that the key challenge to addressing legacy unpaid EDR determinations was the appropriate source of funding, noting that it may not be appropriate nor desirable for current industry participants to contribute to compensation arising from the conduct of former industry participants. The Panel concluded that determining the appropriate funding source for such claims was a matter for Government to address.

## **Part 3: Providing Access to Redress for Past Disputes**

In Part 3 of the Supplementary Final Report, the Panel makes observations of the merits and issues involved in providing access to redress for past disputes. It is noted from the outset that providing access to redress for past disputes is a challenging issue, with no easy solutions.

The Panel considered the greatest challenges involved in providing access to redress for past disputes to be: a lack of complete, reliable data to enable the scale of the problem to be quantified; and determining the appropriate funding source for any compensation awarded, noting that in many situations the financial firm responsible for past misconduct was now insolvent or otherwise unable to pay<sup>7</sup>.

The Panel also noted that the contemporary EDR framework raised concerns about equity and comparability of outcomes across consumers. Specifically, the contemporary EDR framework contained deficiencies which in some cases prevented consumers from accessing redress due to factors beyond the control of the consumer.

While action has and continues to be taken to improve the dispute resolution framework and the regulatory landscape for financial services, there remains the complex issue of addressing the past, where a number of consumers and small businesses may not have had access to redress (Supplementary Final Report, pg. 133)

The Panel concluded that there is merit in providing access to redress to consumers who had a viable claim against a financial firm at the time of the dispute, had taken reasonable steps to obtain redress at the time and were precluded from accessing redress due to circumstances outside of their control<sup>8</sup>.

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<sup>6</sup> Ramsay Review Supplementary Final Report (pg. 17)

<sup>7</sup> Ramsay Review Supplementary Final Report (pg. 18)

<sup>8</sup> Ramsay Review Supplementary Final Report (pg. 17)



The Panel noted that such consumers included those in situations where:

- the financial firm was no longer operating, having ceased trading, gone insolvent or being otherwise uncontactable or unable to pay; and/or
- the financial firm was not a member of an EDR body, because it was either trading while unlicensed or had been expelled by an EDR body; and/or
- the monetary value of the dispute exceeded the EDR body's monetary limits and the consumer or small business lacked the resources to access the courts, tribunals or other dispute resolution bodies; and/or
- the consumer or small business was not in a position to pursue their dispute with the EDR body due to exceptional circumstances<sup>9</sup>.

The Panel also observed that there was no merit in providing access to redress to consumers who had losses arising from market risk, investment performance and/or business decisions; or to consumers who previously received an EDR determination, court decision or deed of settlement and were unsatisfied with the outcome. In summary, the Panel found that there was no merit in providing access to redress to consumers who were not victims of misconduct.

The Panel's findings arrived at a challenging intersection, whereby there was evident merit in providing access to redress to past consumers in certain circumstances, while concurrently significant complexities existed in the practical application of providing such redress.

It is noted that the Panel was required only to make observations in Part 3 of the Supplementary Final Report and not recommendations. Notwithstanding, the Panel presented four options to address the issue of providing access to redress to past consumers, three of which are Government-led and the remaining option industry-led. The Panel does not specifically endorse any one of the options and states that they may be adopted in addition to other options, in that they are not mutually exclusive. Finally, the Panel concludes that any mechanism implemented to provide access to redress for past disputes must be simple, accessible and seek to minimise costs for all stakeholders.

#### The Announcement of the Royal Commission, 30 November 2017

On 30 November 2017, the Government announced a Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry<sup>10</sup>.

Following the announcement of the Royal Commission, on 21 December 2017 the Government also announced that it would defer its consideration of the findings of the Ramsay Review until the conclusion of the Royal Commission<sup>11</sup>.

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<sup>9</sup> Ramsay Review Supplementary Final Report (pg. 18)

<sup>10</sup> Scott Morrison Media Release, 'Royal Commission – Banks and Financial Services', 30 November 2017 (<https://ministers.treasury.gov.au/ministers/scott-morrison-2015/media-releases/royal-commission-banks-and-financial-services>)

<sup>11</sup> Kelly O'Dwyer Media Release, 'Release of the external dispute resolution framework Supplementary Final Report' 21 December 2017 (<https://ministers.treasury.gov.au/ministers/kelly-odwyer-2016/media-releases/release-external-dispute-resolution-framework>)

## The Final Report of the Financial Services Royal Commission, 1 February 2019

The Financial Services Royal Commission was conducted from 14 December 2017 to 4 February 2019. The Honourable Kenneth Madison Hayne AC QC, former Justice of the High Court of Australia, served as a sole commissioner. As part of its work, the FSRC conducted seven rounds of public hearings over 68 days, called more than 130 witnesses and reviewed over 10,000 public submissions<sup>12</sup>.

On 1 February 2019, Commissioner Hayne handed his Final Report to the Governor-General of Australia, along with 76 separate recommendations. The Final Report and the Government's response to the Final Report were made public on 4 February 2019.

As per the Terms of Reference of the FSRC, Commissioner Hayne was required to consider 'the effectiveness of mechanisms for redress of consumers of financial services who suffer detriment as a result of misconduct by financial services entities'<sup>13</sup>. Part of Commissioner Hayne's consideration was to review the recommendations made by the Ramsay Review and provide commentary as to their suitability.

In considering the effectiveness of redress mechanisms for victims of financial services misconduct, Commissioner Hayne referred to the findings of Ramsay Review Final Report and the Panel's recommendation for the establishment of a new, consolidated EDR provider in the financial services industry. It is noted that, in February 2019 when Commissioner Hayne delivered the Final Report, AFCA had begun operating approximately three months prior, in November 2018.

In 2016–2017, a panel appointed by Government reviewed external dispute resolution (EDR) and complaints arrangements in the financial system. The panel delivered a final report in April 2017. In accordance with the panel's recommendations, a new EDR body, the Australian Financial Complaints Authority (AFCA), was established to take the place of the Financial Ombudsman Service (FOS), the Credit and Investments Ombudsman, and the Superannuation Complaints Tribunal. AFCA commenced operating in November 2018.

AFCA should be permitted to set about its work. I make no recommendation for any change in its operations. Elsewhere in this Report, I have recommended that Australian financial services licence (AFSL) holders should be obliged to take reasonable steps to co-operate with AFCA in its resolution of particular disputes including, in particular, by making available to AFCA all relevant documents and records relating to the issues in dispute. (Royal Commission Final Report, pg. 482)

Commissioner Hayne then turned his attention to the Supplementary Final Report of the Ramsay Review and the issues considered by the Panel in regards to the establishment, merits and design of a compensation scheme of last resort, as well as considering the merits and issues involved in providing access to redress for past disputes.

The Supplementary Final Report of the Ramsay Review made clear distinctions between the items of consideration as referenced earlier, with Part 1 focused on the CSLR, Part 2 on legacy unpaid EDR determinations, and Part 3 on providing access to redress for past consumers previously unable to have their case considered by an EDR provider or similar service. In the FSRC Final Report, the distinction between these matters are not as clearly defined.

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<sup>12</sup> Restoring Trust in Australia's Financial System (pg 1)

<sup>13</sup> Letters Patent, FSRC

After considering the findings of the Supplementary Final Report, Commissioner Hayne concurred with the recommendations of the Panel in respect of Part 1, recommending the establishment of a CSLR as recommendation 7.1 of the FSRC:

### **Recommendation 7.1 – Compensation scheme of last resort**

The three principal recommendations to establish a compensation scheme of last resort made by the panel appointed by government to review external dispute and complaints arrangements made in its supplementary final report should be carried into effect.

Commissioner Hayne also made the following comments in respect of the observations made in Parts 2 and 3 of the Supplementary Final Report and the merits of providing access to redress for past disputes:

I make only four points about redress for past disputes.

First, cases in which redress has been directed or ordered but not paid stand apart from all other cases of redress for past disputes. Where a claimant has not been paid the amount that an EDR body (or court) found should be paid, the central issue becomes whether Government or industry should now pay what was owing. As the panel said, a necessary first step would be to identify the scale of the problem before deciding how best to approach providing redress in those cases.

Second, the panel accepted, and I agree, that there would be no merit in allowing further access to redress in any case where the consumer or small business concerned has already resorted to dispute resolution by a court, tribunal or EDR body or has settled the dispute.

Third, limiting access to redress to those who ‘had a viable claim’ would be of little practical effect. The merit of the claim could rarely be determined without detailed examination of the facts and circumstances.

Fourth, if there is to be any access to redress for past disputes, there must be some time limit imposed. (FSRC Final Report, page 487)

Though the distinction in the issues underlying Parts 1 and 2 of the Supplementary Final Report are not made in the FSRC Final Report, Commissioner Hayne does declare that ‘cases in which redress has been directed or ordered but not paid’, i.e. the issue of legacy unpaid determinations as per Part 2 of the Supplementary Final Report, stand apart from other cases of redress for past disputes.

In addressing legacy unpaid determinations, Commissioner Hayne concurs with the findings of the Panel in that there is strong merit for these determinations to be paid, and the central issue remaining was the appropriate source of funding for this compensation.

The Final Report also refers to the merit found in providing access to redress for past disputes per Part 3 of the Supplementary Final Report. Commissioner Hayne does not provide any further consideration than was done by the Panel, though does endorse the Panel’s proposal for further consideration of these issues:

The panel proposed further consideration of the issues and there is evident merit in that being done. (FSRC Final Report, page 486)

## Restoring Trust in Australia's Financial System – The Government response to the Royal Commission, 4 February 2019

On 4 February 2019, the Government published the FSRC Final Report and the Government's response to the Final Report, titled 'Restoring Trust in Australia's Financial System'<sup>14</sup>. As part of its response to the Final Report, the Government agreed to take action on all 76 recommendations of Commissioner Hayne, and in some areas, went beyond the recommendations of the FSRC.

One area where the Government went beyond the recommendations of the FSRC was by compensating those individuals who had a legacy unpaid determination in their favour by an AFCA predecessor body. The Government agreed to fund the payment of legacy unpaid EDR determinations, supporting the findings of the Ramsay Review Supplementary Final Report and FSRC Final Report which both found that there was a strong case for such determinations to be paid. The Government committed to paying approximately \$30 million to almost 300 consumers to address these legacy unpaid determinations<sup>15</sup>.

As part of the Government's commitment to implement the recommendations of the FSRC, an industry-funded, forward looking compensation scheme of last resort will be established. The Government announced that the CSLR will be implemented no later than December 2020, be designed consistent with the recommendations of the Ramsay Review Supplementary Final Report and will extend beyond disputes in relation to personal financial advice failures. The CSLR will operate as a last resort mechanism to pay out compensation owed to consumers and small businesses that receive a court or tribunal decision in their favour or a determination from AFCA, but are unable to get the compensation owed by the financial firm – for example, because the firm has become insolvent.

The Government also announced that, for a finite one-year period, AFCA's remit would be extended to allow complaints dating back to 2008 to be considered. Generally, AFCA's Rules allow AFCA to consider complaints dating back up to six years. Complaints made in the one-year period regarding conduct dating back to 2008 are termed as 'legacy complaints'. The establishment of legacy complaints within AFCA was, ostensibly, intended to allow consumers who had previously suffered from misconduct but had not yet had their case heard to have their case considered by AFCA.

### Compensation Scheme of Last Resort – Developments

On 20 December 2019, Treasury released a discussion paper for public consultation, inviting stakeholders to make submissions on four key design areas of the CSLR<sup>16</sup>. On 8 May 2020, the Government announced a six-month deferral to the implementation of commitments associated with the FSRC, as a result of the impacts of the coronavirus pandemic. Under the updated timetable, the CSLR is to be established by June 2021<sup>17</sup>.

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<sup>14</sup> Restoring Trust in Australia's Financial System

<sup>15</sup> Josh Frydenberg Media Release, 'Restoring trust in Australia's financial system', 4 February 2019 (<https://ministers.treasury.gov.au/ministers/josh-frydenberg-2018/media-releases/007-2019>)

<sup>16</sup> Treasury; Compensation Scheme of Last Resort (<https://treasury.gov.au/consultation/c2019-43848>)

<sup>17</sup> Josh Frydenberg Media Release, 'Update on the implementation of Banking, Superannuation and Financial Services Royal Commission, 8 May 2020 (<https://ministers.treasury.gov.au/ministers/josh-frydenberg-2018/media-releases/update-implementation-banking-superannuation-and>)

## No Further Consideration into Providing Access to Redress for Past Disputes

The structure of the Ramsay Review Supplementary Final Report makes important distinctions between three related but different areas of the EDR framework. For the purposes of this correspondence, we have retained the distinctions between the three aspects made by the Panel in the Supplementary Final Report.

The EDR framework in the Australian financial system today has been shaped largely by the findings of the Ramsay Review in the Final Report and subsequent Supplementary Final Report, as well as the findings of Commissioner Hayne in the FSRC Final Report. The recommendations and observations of the Ramsay Review Panel, and subsequently Commissioner Hayne, have eventuated to become fundamental aspects of the EDR framework today.

The Ramsay Review Final Report recommended that a new, consolidated EDR scheme be established to take the place of the contemporary EDR schemes in place at the time the Final Report was written. This recommendation has eventuated into the establishment of AFCA, which now operates as the sole EDR scheme in the Australian financial services sector.

Part 1 of the Supplementary Final Report recommended that a limited and carefully targeted CSLR be established, to compensate future consumers who receive determinations but are not able to receive the payment awarded to them. Part 1 also included recommendations that the CSLR should operate prospectively; be funded by scheme members; operate independently of AFCA; among other design features. These recommendations were endorsed by Commissioner Hayne in his Final Report and eventuated into the establishment of an industry-funded, forward-looking compensation scheme of last resort, designed consistently with the findings of the Ramsay Review.

Part 2 of the Supplementary Final Report observed that there was a strong case for the payment of legacy unpaid EDR determinations. The Panel observed that the central remaining issue was the source of funding for the legacy EDR determinations to be paid. This observation was endorsed and repeated by Commissioner Hayne in his Final Report. This observation eventuated into the Government announcing it would fund the payment of legacy unpaid EDR determinations.

Part 3 of the Supplementary Final Report observed that there is merit, but complex issues, involved with providing access to redress for past disputes. To balance these merits and complexities, the Panel hypothesised a number of potential options to provide access to redress for past disputes and proposed further consideration in this area. In his Final Report, Commissioner Hayne agreed that further consideration of the issues and merits in this area was appropriate. This observation has never eventuated into further consideration in this area and that is the subject of this paper.

Despite the proposal of the Panel, and the declaration of the Royal Commissioner, no further consideration has been given to these issues following the completion of the Royal Commission approximately eighteen (18) months ago.

<b>Findings of the Ramsay Review Supplementary Final Report and the Royal Commission Final Report – Shaping the EDR Framework of Today</b>			
<b>Supplementary Final Report Consideration Area:</b>	<b>Supplementary Final Report Recommendations &amp; Observations:</b>	<b>FSRC Final Report Recommendation &amp; Comments:</b>	<b>Government Response:</b>
Part 1: The establishment, merits and potential design of a CSLR.	That a limited and carefully targeted CSLR be established.	The three principal recommendations of the Panel be carried into effect. [Recommendation 7.1]	The Government will establish an industry-funded, forward-looking CSLR, consistent with the recommendations of the Ramsay Review.
Part 2: Legacy unpaid EDR determinations.	There is a strong case for the payment of legacy unpaid EDR determinations.	Cases in which redress has been awarded but not paid stand apart from all other cases of redress for past disputes. Where a claimant has not been paid the amount that an EDR body found should be paid, the central issue becomes whether Government or industry should now pay what was owing.	The Government agrees to fund the payment of legacy unpaid determinations from the Financial Ombudsman Service and Credit and Investments Ombudsman.
Part 3: Providing access to redress for past disputes.	There is merit, but also complex issues, in providing access to redress for past disputes.	The panel proposed further consideration of the issues and there is evident merit in that being done.	No further consideration has been afforded to this issue.

As shown in the above table, the issues considered in Parts 1 and 2 of the Supplementary Final Report have been addressed, through the implementation of legislation and through Government funding. However, Part 3 of the Supplementary Final Report remains unaddressed.

#### Shortcomings of AFCA Legacy Complaints – Do not Provide Access to Redress

As part of their response to the Financial Services Royal Commission, the Government announced that, for a one-year period, AFCA's remit would be amended to allow AFCA to consider complaints dating back to 2008 (i.e. the period reviewed by the FSRC)<sup>18</sup>. Such historical complaints are referred to as legacy complaints.

The establishment of the legacy complaints framework was intended to allow consumers with complaints that had not previously been considered to now be considered by AFCA under the current AFCA Rules. Ostensibly, the legacy complaints framework was intended to provide access to redress to consumers for past disputes for those consumers who had not yet had their dispute considered. While this move was well-intentioned, its effectiveness in providing access to redress for past disputes has been limited.

<sup>18</sup> Josh Frydenberg Media Release, 'Restoring trust in Australia's financial system', 4 February 2019 (<https://ministers.treasury.gov.au/ministers/josh-frydenberg-2018/media-releases/007-2019>)

The AFCA Rules set out the rules and processes that apply to all complaints submitted to AFCA, including legacy complaints. Legacy complaints are not subject to the time limits stipulated in AFCA Rule B.4, in order to allow complaints dating back to 2008 to be considered. Legacy complaints are, however, subject to all other AFCA Rules.

AFCA Rule A.4.2 requires AFCA complaints to be made about a financial firm that is an AFCA member at the time that the complaint is submitted to AFCA<sup>19</sup>.

In the context of legacy complaints and providing access to redress for past disputes, this rule is highly prohibitive and excludes the majority of complaints about historical misconduct from being considered. As outlined by the Ramsay Review, perpetrators of historical financial misconduct are largely no longer active participants in the financial system, for example, due to insolvency. As the financial firm responsible for the conduct no longer operates, the firm will not be a current AFCA member, and a consumer seeking to lodge a dispute against such a firm is unable to do so under the AFCA Rules. This feature of historical misconduct is one of the inherent challenges which make providing access to redress such a complex undertaking.

AFCA Rule A.4.2 and the requirement for legacy complaints to be made about current AFCA members precludes a large proportion of consumers who require access to redress for past disputes from having their complaint considered through the AFCA legacy complaints framework. By extension, AFCA Rule A.4.2 prevents a large proportion of consumers who require access to redress for past disputes from actually accessing redress for their past disputes.

Unfortunately, despite the well-intentioned nature of its establishment, the practicalities of the AFCA legacy complaints framework prevent it from effectively performing the purpose it was intended to serve.

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<sup>19</sup> Australian Financial Complaints Authority Rules, 25 April 2020;



## The Issue Must be Addressed

It is noted that the Panel proposed further consideration of the issues comprising Part 3 of the Supplementary Final Report, and Commissioner Hayne endorsed this proposal in his Final Report. Further to simply carrying out the proposal of the Panel and Commissioner Hayne, there are also important moral and ethical reasons for why the issue of providing access to redress for past disputes is important.

### Hardship & Losing Confidence and Trust in the Australian Financial System

Firstly, and most importantly, the consumers affected by Part 3 of the Supplementary Final Report have never been able to access redress previously. This creates situations where consumers have been devoid of their funds for extended periods of time without the ability to seek redress, compensation or even a resolution for the misconduct perpetrated upon them.

This lack of redress has significant and devastating consequences on these consumers. Many consumers suffer significant and ongoing financial hardship due to the misconduct they have faced. Ongoing hardship can be destructive to people in many respects, including but certainly not limited to financial, emotional, social and health consequences. The opportunity costs of these consumers being without funds, and without access to redress, compounds the effects of the misconduct. Points 7.1 to 7.7 of the Supplementary Final Report capture just some of the repercussions felt by consumers and the greater public when access to redress is not available<sup>20</sup>.

Further, the lack of access to redress for consumers can result in disenfranchisement on the behalf of consumers, losing confidence and trust in the Australian EDR framework. Ultimately, this loss of faith in the EDR framework will result in disengagement from consumers in the financial system more generally. Consumers losing confidence and trust in the financial system is an undesirable outcome, especially in the context of compulsory superannuation when consumers have no choice but to be active participants.

As summarised by the Ramsay Review, access to redress is critical.

### Reforms were Required, now Redress

The Final Report of the Ramsay Review found that the EDR framework which existed at the time was not always achieving effective outcomes for its users.

A number of features of the design of the current system mean that it is not producing the best possible outcomes for some users, in particular, consumers.

...

The Panel found that the current framework is the product of history rather than design and, in significant areas, reform is needed. The existence of multiple EDR schemes with overlapping jurisdictions means: it is difficult to achieve comparable outcomes for consumers with similar complaints; it is more difficult for consumers to progress disputes involving firms that are members of different schemes; and there is an increased risk of consumer confusion. (Ramsay Review Final Report, pg. 8)

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<sup>20</sup> Ramsay Review Supplementary Final Report (pg. 131-132)



Reforms were recommended by the Panel and subsequently implemented by the Government. That the reforms were considered necessary by the Panel, and subsequently the Government, is indicative of an EDR framework which was not performing effectively or appropriately. If the contemporary EDR framework was performing effectively, reforms to the EDR framework would not have been required.

The consumers who fall into Part 3 of the Supplementary Final Report and who require access to redress for past disputes are the consumers which indicated that the reforms to the EDR framework were necessary. That consumers were not being able to access to redress was the catalyst for the EDR framework to be reformed. Now, these same consumers are currently excluded from compensation arrangements.

These consumers are victims of an ineffective EDR framework which, clearly, is beyond their control or fault. To exclude these consumers from access to redress is unmerited and unfair.

#### Lack of Equity & Comparability of Outcomes

The inefficiencies of the previous EDR framework has resulted in some situations where consumers with similar or identical circumstances, such as being members of the same investment scheme, received vastly different outcomes to their dispute.

For example, there are situations where consumers within an investment scheme received different outcomes because the financial firm which was the subject of their dispute entered insolvency prior to finalisation of some complaints. Under the guidelines of the contemporary EDR framework, disputes involving an insolvent entity were discontinued immediately. Under these guidelines, active disputes were immediately closed if the financial firm entered insolvency before the dispute was resolved or determined. The current EDR framework has been amended to close this loophole and continues complaints through to determination in the case of the financial firm entering insolvency.

The outcome of this ineffective EDR framework is that some consumers may have received a determination against the financial firm, while other consumers with active disputes against the financial firm at the time it entered insolvency, did not receive a determination. The effect of this ineffective EDR framework was compounded in the Supplementary Final Report, as these consumers, although having identical circumstances, were now treated as two separate classes of consumers, in accordance with Parts 2 and 3 of the report.

These 'Part 2' consumers who possessed legacy unpaid EDR determinations were then compensated by the Commonwealth under *'The Paying Legacy Unpaid External Dispute Resolution Determination program'*. Meanwhile, the 'Part 3' consumers whose complaints were discontinued due to the ineffective EDR framework, have not been compensated and have no avenues currently available to them from which to seek redress. Please refer to the 'Prime Trust Case Study' for a clearly illustrated example of such.

## Prime Trust Case Study

One example of SR Group represented consumers being excluded from compensation arrangements, despite having identical circumstances to consumers who have received compensation, is in the Prime Retirement and Aged Care Property Trust (“Prime Trust”).

The Prime Trust was a managed investment scheme which collapsed in July 2011. In 2012, ASIC launched legal proceedings against the Prime Trust directors, alleging breaches of the Corporations Act and director obligations to unitholders. In 2018, the High Court found in favour of ASIC, and each of the Prime Trust directors was disqualified from managing corporations and fined<sup>21</sup>.

Prior to Prime Trust’s collapse, some investors lodged disputes through the Financial Ombudsman Service (FOS). Following the appointment of Liquidators to Prime Trust in July 2011, any unitholder who sought to lodge a complaint through FOS was unable to do so, as the FOS guidelines at the time did not allow complaints to be lodged or continued if the financial firm was insolvent.

A small number of investors received determinations through FOS before Prime Trust entered liquidation in July 2011. All remaining disputes still ongoing were discontinued under the FOS guidelines at the time. For the complaints which received determinations, every single determination was in favour of the investor<sup>22</sup>. Each investor was awarded compensation for the full value of their investment, plus applicable interest.

An important factor in the FOS determinations handed down was that the Prime Trust Product Disclosure Statement (PDS) were found to be misleading and deceptive, and therefore defective. Further, the defective PDS was determined to be grounds for compensation as the PDS was relied upon by each complainant making their investment in the Prime Trust. Seemingly, this reasoning would apply to all investors in the Prime Trust who reviewed and relied on the defective PDS in making their investment.

However, not all investors were afforded the opportunity to have their case considered by FOS, due to the FOS guidelines which are clearly beyond the control of the individual consumer. Without the opportunity to have their complaint considered by FOS, Prime Trust investors were not able to access ‘*The Paying Legacy Unpaid External Dispute Resolution Determination program*’.

The result is that there is a clear discord in the comparability of outcomes for consumers who have identical investment circumstances. For some Prime Trust investors, full compensation has been awarded and received. For other Prime Trust investors, zero compensation has been awarded and there are no avenues available for these investors to seek compensation from, due to no fault of their own.

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<sup>21</sup> ASIC Key Matters: Prime Trust (<https://asic.gov.au/about-asic/news-centre/key-matters/prime-trust/>)

<sup>22</sup> FOS Determination 212722, (<https://service02.afca.org.au/CaseFiles/FOSSIC/212722.pdf>)