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Submissions on discussion paper: review of the approved financial dispute resolution schemes' rules

Our submissions are informed by our role as one of the four approved financial dispute resolution schemes. In the year ended 30 June 2020, we referred 768 complaints back to financial service providers' internal complaints processes and completed formal investigations of 298 disputes. In FSCL's 10 years of existence we have completed investigations of 1,988 disputes and awarded over $6M in compensation.

We are actively involved in the promotion of alternative dispute resolution for financial complaints, and in educating both consumers and participants about the value of complaints. We regularly submit, and give feedback to policy-makers and regulators, on legislative changes relevant to our work. We share the lessons learned from complaints in our case notes published on our website and in our training events for scheme participants and consumers.

We welcome the Ministry's review of the schemes' rules and consider increased consistency across the schemes will ultimately lead to better consumer outcomes. We provide our submission on the discussion paper below, based on the discussion paper's numbered parts.

We request the two appendices to these submissions (referred to below at paragraph 2.26) are held in confidence by the Ministry and not publicly published.

1. Discussion paper part 2 – Objectives and criteria for the review

Question 1: What is your feedback on the proposed objective and criteria for the review? What is your feedback on the proposed weighting of the criteria?

1.1. We agree with the Ministry's proposed objective and criteria for the review, and the weighting of the criteria.

2. Discussion paper part 3 – Financial caps

Question 2: Are you aware of any instances of consumer harm due to the issues outlined?
Question 3: Do you have any feedback on the problems outlined?

Cases where our financial cap was relevant

2.1. One of the issues FSCL faces in terms of assessing any consumer harm caused by our financial cap, is that we cannot know the number of people who never contacted FSCL about their complaint because of the financial cap.

2.2. We have about 3-4 cases a year where a consumer contacts us, and we decline jurisdiction because their claim is over the financial cap. In general, consumers are not so familiar with our rules that they would necessarily know about our financial cap. However, there may be participants and lawyers representing consumers in larger claims who are aware of the financial limit and so do not refer the complaint to FSCL (because they know we will have to decline jurisdiction). In other words, we have no real idea how many complaints do not come to us, because the amount of the loss is over $200,000.

Other feedback?

2.3. Our rules state that a complainant cannot limit their claim to $200,000 to fit within the financial cap (although, conversely, the participant can agree to waive jurisdiction in relation to the financial cap). We understand that one scheme does allow a consumer to waive the part of their claim that exceeds the financial cap.

2.4. A risk in removing that restriction could be that consumers (who do not need to accept any decision we issue) use the scheme's process as a 'test run' before going to court. Consumers may use the process to obtain access to documents and gain a better understanding of the strength of their case, when their intention was always to go to court.

2.5. On the other hand, it could be argued that if a participant is able to waive the jurisdiction in relation to the financial cap, a consumer also ought to be able to

reduce the amount of their claim to bring the claim within the financial cap. We simply raise these points for the Ministry to consider.

2.6. Further, we approach participants when we receive a complaint that is over cap, to see whether they want to waive jurisdiction. Occasionally a participant will waive. This is one consumer-harm mitigating factor.

2.7. Another point we raise is that in a recent complaint received by FSCL (which has not yet reached the formal investigation stage), there is a question about whether our financial limit includes GST that may be payable on an insurance settlement payment. If GST is included, it could take the complaint over FSCL's financial cap, and vice versa. It would be helpful if the Ministry considered GST and other relevant tax implications when looking further at the issue of financial caps.

Comments on specific paragraphs of the discussion paper

2.8. With reference to paragraph 33 of the discussion paper, we disagree with the suggestion that the schemes do not have the resources to deal with complex and technical complaints, and that high value complaints are necessarily more complex.

2.9. It is possible that where more money is involved, the issues may be more complex, but that is not necessarily the case. Very often the underlying issues we are asked to determine are the same, whether the alleged loss is $20,000 or $200,000 (or more). Complex cases take longer to be resolved through our process than standard cases, but we submit that the complex case would take as long or longer to proceed through the court system. Even at a fundamental level – obtaining a court date can take a significant length of time and cost.

2.10. We can decline jurisdiction if we consider there is a better forum for the dispute to be resolved – including court. However, we only usually suggest that court would be a better forum if there is a novel question of law, or if it is critical to the resolution of a dispute that the parties have the benefit of the cross-examination of expert witnesses. In our experience, these circumstances seldom arise in complaints we investigate.

2.11. With reference to paragraph 40 of the discussion paper (bullet point 4), we doubt an increase to the financial cap will increase our caseload significantly. And, in any event, if there was a significant increase in our case load, we have the resources to recruit more staff.

Question 4: Do you have any feedback on the option of increasing the financial cap to $350,000?
Question 5: Are there any other costs or benefits of this option?

Proposed cap increase to $350,000

2.12. We support the increase in the financial limit to $350,000, because our current cap of $200,000 is too low (being based on a figure set in 1992 that has not been adjusted for inflation and changed market conditions). Moreover, there should be consistency across the schemes. In addition, it was always the purpose of the schemes to be an alternative to court as a forum to resolve disputes (due in part to high litigation costs). Therefore, it makes sense to increase the schemes' caps to the District Court limit. Although we note that with the current cost of financial products, (particularly life insurance and mortgages), the proposed $350,000 cap may still be too low.

2.13. In Australia, the Australian Financial Complaints Authority (AFCA) has a financial cap for most products/services of $500,000, with this amount being higher for complaints from small businesses ($1M), and 'primary producers' ($2M). AFCA's rules also state that they must review their caps every 3 years and increase them to match either the CPI increase or the increase in average Australians' weekly earnings (based on information from the Australian equivalent of Statistics New Zealand).

2.14. We suggest the Ministry considers the Australian approach to financial caps, and considers building into the regulations a mechanism for the schemes to regularly (and consistently) increase their financial caps and/or peg the cap to the District Court limit.

Weekly alternative to a lump sum cap

Question 6: Do you have any feedback on this option?
Question 7: Do you agree that a weekly payment alternative should be introduced for all schemes? Why/why not?
Question 8: Is $1,500 an appropriate weekly payment alternative? Why/why not?
Question 9: Are there any other costs or benefits of this option?

2.15. We agree that, to maintain consistency between the schemes' rules, all schemes should include a weekly alternative to the financial cap and the new rule could be based on the existing clause in IFSO's rules. Although FSCL does not have risk insurers as participants, and so the weekly alternative is not as

relevant for the disputes we investigate, we are regularly investigating financial advice complaints about risk insurance.

2.16. In those cases, the consumer may have had a claim declined by their insurer and then they make a complaint that their adviser provided poor advice which meant the claim was declined. The consumer then seeks the amount they would have received under the insurance policy, from the adviser.

2.17. In these adviser cases, it is common for a professional indemnity insurer to be involved who appoints a lawyer to act on behalf of the insurer and the adviser in the dispute. In our experience, professional indemnity insurers prefer to resolve claims involving benefits payable in regular instalments, by way of a global, and full and final, settlement.

2.18. Our anecdotal view is that professional indemnity insurers do not want to be involved in regular payments to the consumer (potentially for decades), if FSCL were to uphold the complaint, or if the parties were to reach a negotiated resolution. We suggest that the Ministry could consider speaking with professional indemnity insurers to gain a better understanding of their views on the weekly alternative option in terms of financial advice complaints.

2.19. Despite these comments, we consider it would be helpful to have the option of awarding compensation based on the weekly alternative, as another tool to help parties reach complaint resolutions. However, we would not support the weekly alternative to a lump sum being the **only** method of awarding compensation where the product being complained about is one that provides regular payments.

Raising the weekly cap amount

2.20. We submit that the weekly alternative limit of $1,500 ($78,000 per annum) is far too low and is an unrealistic amount. To provide context, the people who tend to have income protection or similar risk insurance products, where accepted claims are paid in regular instalments, are those on high incomes of at least $120,000 per annum (because these policies are expensive).

2.21. We therefore suggest that the weekly alternative cap be increased to better reflect the weekly incomes of people in a high-income bracket. We suggest that $4,000 per week is a more appropriate weekly amount. And, similar to the lump sum financial cap, there should be a mechanism to increase the weekly alternative cap over time. That mechanism should reflect that income increases

for people in a high-income bracket tend to be larger than average increases over short periods of time (compared to people in lower income brackets).

Inconvenience and interest awards

Question 10: Do you have any feedback on the problems outlined?
Question 11: If a consistent special inconvenience award was to be introduced, in what circumstances should it be awarded. Should this be discretionary or strictly prescribed?
Question 12: If an interest award was to be introduced how should it be calculated?
Question 13: What are the benefits and costs of the options?

Awards for non-financial loss

2.22. Firstly, with reference to paragraph 42 of the discussion paper, the inconvenience award is described as a 'special' inconvenience award. In our view, the insertion of the word 'special' is unnecessary. It suggests that only where there is some extreme inconvenience or stress will an award of compensation will be made.

2.23. FSCL's approach is that, if there is inconvenience or stress caused by a participant's actions, we assess the amount of compensation to be awarded, along a scale from $0 to $2,000, taking into account different factors, including stress, embarrassment and lost opportunity. We discuss this further below.

2.24. Fundamentally, in relation to compensation for non-financial loss we consider there should be a consistent amount across all the schemes. We support an increase from our current limit of $2,000 to the proposed limit of $10,000. Although in most cases where we award compensation for non-financial loss an amount up to $2,000 is appropriate, we have investigated complaints where the upper $2,000 limit is not adequate to compensate for the extreme stress or inconvenience caused.

2.25. We also consider there should be consistency in how the schemes apply their discretion to award non-financial loss compensation by making it clear that compensation can be awarded where a consumer has suffered stress, embarrassment, and lost opportunity as a result of the participant's actions, but we would not want to see an overly-prescriptive approach.

2.26. Attached as appendices one and two are our compensation guides (one for complainants and one for participants)[1] which set out some of the factors we take into account when considering awarding compensation for inconvenience, including:

- The amount of financial loss a complainant has suffered.
- The length of time involved (both before and after the complaint has reached the scheme, or any undue delays caused by the participant).
- Whether there were any impacts on the complainant's health.
- Other consequences, for example being unable to pay a debt when due.
- How much the complainant will be affected by the inconvenience in the future.

Interest

2.27. We have very rarely awarded interest on financial loss awards. As outlined in our compensation guides – we generally only award interest if the complainant provides strong evidence that they would have earned interest on the funds if those funds had not been unavailable because of the dispute.

2.28. With reference to paragraph 45 of the discussion paper, we do not agree with the statement: 'The BOS can only award interest where it is a part of direct financial loss'. However, we note that the BOS can, as part of the compensation award for financial loss, say that the bank must forgive all the interest on a loan. But this is a different type of interest compensation than the interest award. FSCL also can, and regularly does, recommend that a lender forgives the interest charged on a loan in circumstances where there has been a breach of responsible lending laws.

2.29. In any event, we suggest standardising the approach to making an interest award. We submit that the regulations clearly delineate the non-financial loss award, and the interest award. In our view they are quite distinct types of award and they should not interrelate.

2.30. Lastly, we suggest the Ministry develops a consistent interest rate for the schemes to apply when making an interest award, or a consistent way of determining the rate. One option would be to use the Judicature Act rate.

[1] Which we request MBIE keeps confidential.

3. Discussion paper part 4 – Timing of membership and jurisdiction

Question 14: Are you aware of any specific situations where providers have switched between schemes resulting in the situation described above? If so, what happened?
Question 15: Do you agree with the potential problems that may occur as a result of inconsistent scheme rules about the timing of membership/jurisdiction?

3.1. Very occasionally, we encounter difficulties where a participant has changed schemes and it means that no dispute resolution scheme has formal jurisdiction to investigate the complaint. However, we cannot recall any situation where this jurisdictional issue was not resolved between the schemes. Ultimately a financial service provider has taken responsibility for the complaint. We agree that when this issue arises it causes a delay, which is not a good consumer outcome.

Questions 16 & 18: Do you have any feedback on these options?
Questions 17 & 19: Are there any other costs or benefits of these options?

3.2. There should be consistency across the schemes in terms of the rules about the timing of membership and jurisdiction. At a practical level it makes sense for complaints to be dealt with by the scheme the participant belongs to at the time the complaint is made. That is, the timing of the event leading to the complaint is not determinative as to which scheme has jurisdiction to investigate the complaint.

The adviser liability gap

3.3. A similar but slightly different, and more serious, problem has been caused by the move to the financial advice licensing regime. This is because individual financial advisers no longer need to be registered with a dispute resolution scheme – as long as they are covered by a Financial Advice Provider's (FAP) licence (whether because they are engaged directly by a FAP or indirectly engaged through an Authorised Body).

3.4. Because there has been significant movement from an individually based dispute resolution scheme membership regime, to an entity level membership regime, we now have a situation where many financial advisers are now members of a dispute resolution scheme in a completely different capacity.

3.5. To use a hypothetical example, an adviser has been a FSCL member up to 14 March 2021, but from 15 March 2021 ceased that membership because they are now engaged by XYZ Limited who holds a transitional licence. XYZ Limited is a FSCL member (although for the purposes of this example, it would not matter whether XYZ Limited was another scheme's member).

3.6. Say a complaint arises about the advice the financial adviser provided in December 2020. FSCL would not have formal jurisdiction to investigate a complaint made about the adviser after 15 March 2021, because they are no longer a FSCL member. XYZ Limited may also say it has no liability for the complaint because, although the adviser is now covered by XYZ Limited's transitional licence, when engaging the adviser, XYZ Limited never agreed to take on liability for any complaints made about the adviser's advice provided before 15 March 2021. Moreover, section 63(1)(ba) of the FSP Act does not apply because it is not XYZ Limited failing to take the remedial action directed by a scheme, it is the adviser failing to take the action.

3.7. The problem is that no scheme has the ability to terminate the adviser's membership (which is the only enforcement tool the schemes have to ensure compensation awards are paid). This is because the adviser is no longer a member of **any** scheme in their own right, post 15 March 2021. A similar problem arises when an adviser leaves the industry altogether.

3.8. The adviser liability gap represents a **significant access to justice issue** that should urgently be addressed by the Ministry. Many hundreds of financial advisers have ceased their scheme memberships in their own right post 15 March 2021. This represents a significant potential consumer cohort who could have no access to a scheme should they have a complaint about advice an adviser provided prior to 15 March 2021.

4. Discussion paper part 5 – Applicable time periods (limits) for bringing a claim

Question 20: Do you have any feedback on the problems outlined?
Question 21: Are you aware of instances of consumer harm from the problems outlined?
Questions 22 – 29 – Do you have feedback on the options? What are the costs or benefits of the options?

Time period I – when the scheme becomes available for consumers

4.1. We firmly believe that the more quickly complaints are addressed, the greater the likelihood of complaints being resolved and that those resolutions are enduring. We therefore support a consistent timeframe for time period I, as being a maximum of 2 months (40 working days). This would also be consistent with the Insurance Council of New Zealand's Fair Insurance Code 2020's complaints section.

4.2. We disagree with the reference at paragraph 74 bullet point 3 of the discussion paper, that a reduction in time frames to address complaints could mean complaints are rushed through internal dispute resolution. In our experience, 40 working days provides participants, in most situations, ample time to consider complaints through their internal complaints process.

4.3. In any event, the 40 working day period can be extended because of extenuating circumstances. For example, it may be that the participant needs to seek information from a third party, or they need to extract records from a computer system administered by a third-party provider, both of which take time.

4.4. In those situations, where the resolution of the complaint is not time critical, the complainant is not materially prejudiced if they have to wait another, say, two weeks for the participant to have all the information they need to be able to properly assess the complaint.

4.5. In those circumstances we usually allow the participant a longer period to try and resolve the complaint. This is on the premise that if FSCL were to commence a formal investigation of the complaint, we would also likely need the information the participant seeks to be able to meaningfully investigate the complaint.

Time period II – limit on consumers bringing complaints to the scheme following deadlock

4.6. There have been instances where we have declined jurisdiction to investigate a complaint because the consumer has been outside the 2-month time limit to bring the complaint to FSCL, given by the participant when they deadlocked the complaint.

4.7. In some cases however, the participant has agreed to FSCL looking at the complaint. One example from the past 12 months was a consumer with a travel

insurance complaint who did not contact FSCL within 2 months of the deadlock letter from their insurer which included the 2-month time limit. The reason the consumer was delayed in contacting FSCL was because they were an essential worker during the height of the Covid-19 lockdown in March/April 2020. The consumer also only missed the deadline by a slim margin and the participant agreed to FSCL investigating the complaint.

4.8. In other circumstances, where the consumer has no cogent reasons for their delayed contact with FSCL, the participant has advised they will not agree to FSCL investigating the complaint.

4.9. We know that for larger participants, particularly insurers who often include the 2-month time limit in deadlock letters, they include the limit so they have some idea about the number of deadlocked complaints that could end up going to FSCL for investigation. This helps larger participants plan and budget in terms of their dispute resolution costs.

4.10. We see value in participants being able to include a time limit in which consumers must contact the scheme following deadlock. We agree that a 3-month limit would be more consumer friendly than our existing 2-month limit. We also agree with option three outlined at paragraph 76 of the discussion paper – to include a discretion to extend the period to say, an absolute maximum of 6 months in cases of extreme vulnerability or extenuating circumstances.

Time period III – total deadline for consumers to bring complaints to the schemes

4.11. We also agree with paragraph 77 of the discussion paper, that it would be preferable to have a consistent maximum time period for consumers to bring complaints to the schemes. We submit that the approach adopted must include reference to paragraph 8.1(i) of FSCL's terms of reference, in terms of the date the consumer first became **aware**, or should **reasonably have become aware** of the event leading to the complaint.

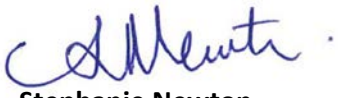
4.12. If the 'awareness' provision is not included, many of the complaints we consider about financial advisers would be outside jurisdiction. This is because it is often more than six years ago that the advice that is the subject of the complaint was provided, but the consumer does not become aware of the deficient advice until many years later. Some aligning of the schemes' rules

with the timeframes under sections 11 and 14 of the Limitations Act 2010 could be considered by the Ministry.

If you wish to discuss our submissions in more detail, please contact us.

Yours sincerely

Susan Taylor
Chief Executive Officer



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