ASIC
Australian Securities & Investments Commission

REPORT 308

Response to submissions on CP 172 Review of EDR jurisdiction (debt recovery legal proceedings)

October 2012

About this report

This report highlights the key issues that arose out of written submissions and informal discussions, as well as the findings of our review, commenced by Consultation Paper 172 *Review of EDR jurisdiction over complaints when members commence debt recovery legal proceedings* (CP 172).

This report accompanies Consultation Paper 190 *Small business lending complaints: Update to RG 139* (CP 190).

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- describing the principles underlying ASIC's approach
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This report does not contain ASIC policy. Please see Regulatory Guide 165 *Licensing: Internal and external dispute resolution* (RG 165) and Regulatory Guide 139 *Approval and oversight of external dispute resolution schemes* (RG 139).

Contents

A Overview/Review process

Complaints handling by EDR schemes

1 As a condition of their licence, Australian financial services (AFS) licensees and credit licensees must have a compliant dispute resolution system for handling retail client complaints. The dispute resolution system must consist of:

(a) internal dispute resolution (IDR) processes that meet ASIC's approved standards and requirements; and

(b) membership of an external dispute resolution (EDR) scheme approved by ASIC (unless the Superannuation Complaints Tribunal (SCT) can handle all of the licensee's retail client complaints).

2 We have issued guidance on how:

(a) licensees can meet their dispute resolution obligations in Regulatory Guide 165 *Licensing: Internal and external dispute resolution* (RG 165); and

(b) EDR schemes can obtain ASIC's approval and continue to remain approved in Regulatory Guide 139 *Approval and oversight of external dispute resolution schemes* (RG 139).

3 ASIC-approved EDR schemes currently exist to handle financial services and credit complaints. They are:

(a) Financial Ombudsman Service Limited (FOS), formed by the merger of five pre-existing ASIC-approved EDR schemes in 2008–09; and

(b) Credit Ombudsman Service Limited (COSL).

4 Both FOS and COSL are approved by ASIC for the purposes of the *Corporations Act 2001* (Corporations Act) and the *National Consumer Credit Protection Act 2009* (National Credit Act), and must continue to meet the requirements of RG 165 and RG 139 as a condition of their approval.

Note: See Class Order [CO 09/340] *External dispute resolution schemes* and Class Order [CO 10/249] *External dispute resolution schemes (credit)*.

Jurisdiction for complaints involving debt recovery legal proceedings

5 From 1 January 2010, EDR schemes must also maintain a specific jurisdiction under their terms of reference or rules so complainants can access EDR, even if a scheme member has commenced legal proceedings to recover a debt or recover possession of an asset used as a security for a loan (usually a residential property): see RG 139.77–RG 139.79. In this report, we refer to this as a 'debt recovery legal proceedings jurisdiction'.

6 Where a scheme member commences these legal proceedings, complainants must be able to complain to, and access an EDR scheme, at least during the early stages of the debt recovery legal process (i.e. up until the point where the complainant has *not* taken a step beyond lodging a defence or defence and counter claim).

> Note: For the avoidance of doubt, the complainant will not be considered to have taken a 'step' if they attend a directions hearing or agree to consent orders of a procedural nature only being filed in those legal proceedings: see RG 139.79.

7 To allow the EDR scheme process to properly run its course, once a complaint involving debt recovery legal proceedings has been lodged with an EDR scheme, the terms of reference or rules of the scheme must require that the scheme member *not* pursue the debt recovery legal proceedings beyond the minimum necessary to preserve its legal rights.

8 In practice, this requires an EDR scheme member to stay or discontinue the legal proceedings while the complaint is being handled at the EDR stage.

9 While this jurisdiction mainly affects lenders regulated by the National Credit Act, it may also apply to complaints involving:

(a) lenders mortgage insurers who are seeking to recover a shortfall debt; and

(b) margin loan providers and other financial product and service providers regulated by the Corporations Act (i.e. insurers) where the scheme member is seeking to recover a debt from the complainant.

Rationale for the jurisdiction

10 The purpose of the requirement in RG 139.77–RG 139.79 was to ensure that EDR schemes were meeting the overarching principles of 'accessibility' and 'effectiveness' for credit and margin lending.

> Note: When considering whether to approve an EDR scheme, ASIC must consider the principles of accessibility, independence, fairness, accountability, efficiency and effectiveness: see regs 7.6.02(3) and 7.9.77(3), Corporations Regulations 2011 and reg 10(3), National Credit Regulations 2010. A more detailed discussion of these principles is set out in RG 139.

11 These principles can be summarised as follows:

(a) *Accessibility:* Consumers of credit and margin lending providers should have adequate access to EDR so hardship issues may be addressed.

(b) *Effectiveness:* EDR schemes must be able to handle the vast majority of types of complaints in a particular industry sector or sectors covered by the scheme.

12 In the lead up to the transfer of credit regulation to the Commonwealth, consumer representatives expressed particular concern that consumers of credit should not be disadvantaged by losing important complaints rights, given the loss of access to relevant state and territory tribunals.

13 Under previous state and territory credit regimes, complainants could make hardship applications in the Victorian Civil and Administrative Tribunal (VCAT) and NSW's Consumer, Trader and Tenancy Tribunal (CTTT), even when the lender had already commenced legal proceedings in court to recover an outstanding debt or recover possession of an asset provided as security for a loan. In these cases, the court proceeding would be stayed while the VCAT or the CTTT exercised its exclusive jurisdiction to deal with the hardship issues.

14 By contrast, under the national credit regime, access to EDR replaced access to state and territory tribunals (i.e. VCAT and CTTT).

15 Such access to EDR, similar to VCAT and the CTT, was considered important as consumer representatives reported that many consumers do not realise they have a problem or only seek financial hardship assistance once they are served with a writ or statement of claim.

16 During our review of EDR jurisdiction (see paragraphs 27–33), consumer representatives further reiterated the importance of this post-statement-of-claim jurisdiction at the EDR stage, and added that this jurisdiction also assists consumers with debt collection issues (e.g. when they are being pursued by a debt collection agency for a statute barred debt), or when particularly vulnerable and disadvantaged consumers have been granted loans in breach of responsible lending requirements.

Approach to jurisdiction

17 ASIC approved both FOS's Terms of Reference and changes to COSL's Rules as meeting the minimum requirements in RG 139.

18 FOS's approach to its debt recovery legal proceedings jurisdiction is expressed in paragraph 13.1 of its Terms of Reference, which states that:

> (a) Subject to paragraph (b), where an Applicant lodges a Dispute with FOS, the Financial Services Provider:
>
> (i) must not instigate legal proceedings against the Applicant or any Other Affected Party relating to any aspect of the subject matter of the Dispute;
>
> (ii) must not pursue legal proceedings relating to debt recovery instituted prior to the lodging of the Dispute with FOS save to the minimum extent necessary to preserve the Financial Services Provider's legal rights and, in particular, must not seek judgment in those legal proceedings provided the Dispute is lodged before the Applicant takes a step in those legal proceedings beyond lodging a defence or a defence and counterclaim (however described);
>
> (iii) must not take any action to recover a debt the subject of the Dispute, to protect any assets securing that debt or to assign any right to recover that debt,
>
> while FOS is dealing with the Dispute.

(b) Notwithstanding paragraph (a), with FOS's agreement and on such terms as FOS may require, the Financial Services Provider may:

(i) issue proceedings where the relevant limitation period for such proceedings will shortly expire—but those proceedings may not be pursued beyond the minimum necessary to preserve the Financial Services Provider's legal rights; or

(ii) exercise any rights it might have to freeze or otherwise preserve assets the subject of the Dispute.

(c) If the Dispute is subsequently decided by FOS and becomes binding upon the Financial Services Provider, the Financial Services Provider will abandon any aspect of proceedings against the Applicant or Other Affected Party that are inconsistent with that decision.

19 FOS's *Operational guidelines* further explain its approach, including how a lender may seek to issue proceedings to preserve their legal rights (e.g. if the limitations period is about to expire) and to preserve assets that are the subject of the complaint.

Note: A copy of this document is available at www.fos.org.au.

20 COSL's approach to its debt recovery legal proceedings jurisdiction is reflected in Rules 17.2–17.6 of its current rules (8th edition), which state that:

Rule 17.2 Once COSL records a Complaint and for as long as COSL deals with the Complaint:

(a) the Member must not initiate enforcement action against the Complainant in relation to any aspect of the subject matter of the Complaint;

(b) where the Member commenced such enforcement action before the Complaint was recorded as received by COSL, the Member must not continue the enforcement action and, in particular, must not:

(i) seek judgment in the legal proceedings; or

(ii) where default judgment has been entered, seek to enforce the default judgment;

(c) the Member must not sell the debt that is the subject of the Complaint to a debt buy-out business or otherwise assign any right to recover the debt; or

(d) if it has not already listed a default, the Member must not list a default on the Complainant's credit reference file.

Rule 17.3 Despite Rule 17.2, COSL may at its discretion and on such terms as it may require, permit the Member to:

(a) issue proceedings, but only where the relevant limitation period for the proceedings will shortly expire, and then only to the minimum extent necessary to preserve the Member's legal rights; or

(b) exercise any rights it might have to freeze or otherwise preserve assets the subject of the Complaint; or

(c) continue or resume legal proceedings if the Complainant has taken a step in the legal proceedings beyond lodging a defence or a defence and counterclaim (however described).

Note: The Complainant will not be considered to have taken a 'step' if they merely attended a directions hearing or agreed to consent orders of a procedural nature being filed in the proceedings.

Rule 17.4 The Member must not do anything, including:

(a) initiating or resuming enforcement action; or

(b) seeking judgment for the debt or taking possession of an asset securing the debt; or

(c) assigning any right to recover the debt; or

(d) listing a default on the Complainant's credit reference file,

which is inconsistent with:

(i) a decision by COSL in the Complainant's favour; or

(ii) an agreement by the parties to the Complaint to settle the Complaint on agreed terms; or

(iii) in the case of a financial hardship application, an agreement between the parties on a variation of the payment terms; or

(iv) in the case of a financial hardship application, a direction by COSL to the Member to vary the terms of a Credit Contract under Rule 9.6(h).

Rule 17.5 The Member may initiate or, subject to Rule 17.6, resume enforcement action if:

(a) COSL determines it has no jurisdiction to deal with the Complaint; or

(b) COSL considers that the Complaint is not made out; or

(c) the Complainant declines to accept COSL's determination of the Complaint.

Rule 17.6 Where the Complainant was served with a statement of claim or other initiating process before COSL recorded the Complaint, the Member may only resume enforcement action under Rule 17.5 if it first allows the Complainant 21 days in which to file a defence or a defence and counterclaim (if they have not already done so).

21 We consider that COSL's approach is consistent with the requirement in RG 139.77–RG 139.79 and achieves a higher standard than the requirement because COSL may become involved in complaints at later stages of the debt recovery legal process, beyond when a complainant lodges a defence or defence and counterclaim (i.e. once a default judgment is entered).

Phase II credit reforms

22 The Consumer Credit Enhancements Act (Enhancements Act) passed both the House of Representatives and the Senate on 20 August 2012 and was assented to on 17 September 2012. The Enhancements Act seeks to refine the National Credit Act from 1 March 2013.

23 Of relevance to our review of EDR jurisdiction, the Enhancements Act:

(a) removes the $500,000 value of the loan threshold for a consumer to apply for a hardship application or postponement of enforcement proceedings;

(b) makes it easier for a consumer to give notice that they seek a hardship variation (i.e. either in writing or verbally and on broader grounds, if the consumer is unable to meet their obligations under a credit contract); and

(c) requires lenders to not progress enforcement proceedings until a consumer's request for a hardship variation has been properly considered.

24 We anticipate that these reforms will reduce the number of complaints coming to EDR schemes under their debt recovery legal proceedings jurisdiction. However, this jurisdiction is likely to continue to be relevant, particularly if consumers continue to not recognise they have a problem or only seek assistance for hardship after a writ or statement of claim has been served (i.e. they are not aware they can make a hardship application earlier when they begin to experience financial difficulty, they are being pursued for a statute barred debt, or the loan granted did not meet responsible lending requirements).

25 As part of Phase II credit reforms, the Australian Government is also considering the extent to which the National Credit Act and Sch 1 of that Act (National Credit Code) will apply to the provision of credit to small business borrowers and the provision of credit for investment purposes (other than margin loans).

26 We understand that there may be some time yet before Phase II credit reforms for small business and investment lending are finalised.

Our review of EDR jurisdiction

27 In December 2011, we commenced a review of EDR jurisdiction in this area by releasing Consultation Paper 172 *Review of EDR jurisdiction over complaints when members commence debt recovery legal proceedings* (CP 172).

28 In CP 172, we sought feedback from stakeholders on their experiences with this jurisdiction.

29 We also sought feedback on the following issues, among others:

(a) Should the requirement in RG 139.77–RG 139.79 for EDR schemes to handle complaints where debt recovery legal proceedings have already commenced remain in its current form?

(b) What refinements should be made to this requirement?

(c) Are any refinements needed given proposed changes to the National Credit Act as part of Phase II credit reforms?

(d) Should complaints about certain types of financial or credit products be excluded from a scheme's debt recovery legal proceedings jurisdiction and instead be more appropriately handled in court?

(e) Do certain court processes and procedures prevent a member from being able to reasonably comply with FOS's and COSL's debt recovery legal proceedings jurisdiction?

(f) Is there a class of complainant that should not be allowed to access an EDR scheme's debt recovery legal proceedings jurisdiction?

30 In May–June 2012, after all written submissions to CP 172 were received, we met separately with key industry associations, consumer representatives and EDR schemes that had made submissions to informally discuss their views.

31 We also held a joint roundtable discussion with key stakeholders in July 2012. For a list of attendees who participated, see the appendix.

32 This report highlights the key issues that arose out of written submissions to CP 172 and informal discussions, as well as our findings of the review.

33 This report is not meant to be a comprehensive summary of all responses received from submissions and informal discussion. It is also not meant to be a detailed report on every question asked in CP 172. We have limited this report to the key issues.

Submissions to our review

34 We received 27 written submissions (three confidential) in response to CP 172 from a diverse range of stakeholders, including industry, ASIC-approved EDR schemes and consumer representatives. For a list of respondents who made public submissions to CP 172, see the appendix. Copies of submissions are available on ASIC's website at www.asic.gov.au/cp under CP 172.

35 Table 1 gives a breakdown of the stakeholders from whom the 24 non-confidential submissions were received.

Table 1: Stakeholders who made public submissions to CP 172

Stakeholder	No. of submissions
Industry (including 10 businesses, 6 industry associations and 1 law firm representing industry clients)	17
Consumer representative organisations Note: Consumer organisations that contributed to the joint consumer submission and separately made their own submission have not been counted twice.	9
EDR schemes	2

36 Written submissions generally took different positions on the requirement in RG 139.77–RG 139.79. Table 2 summarises these positions.

Table 2: Views on the requirement in RG 139.77–RG 139.79

View	Explanation	Submissions that expressed this view
Access to EDR should be expanded	The scope of RG 139.77–RG 139.79 needs to be broadened so complainants can access EDR schemes at later stages of the legal process for debt recovery (e.g. where a default judgment has been entered).	Most consumer representatives (7 out of the 9 consumer organisations who made submissions)
No change required	The requirement in RG 139.77– RG 139 should remain unchanged.	A few submissions (COSL, Redfern Legal Centre, CCLC NSW)
Some refinements are necessary	There are a number of problems and issues with how EDR schemes currently operate their debt recovery legal proceeding jurisdiction. Some fine-tuning of the requirement in RG 139.77– RG 139 is necessary.	Most submissions
Access to EDR should be removed	The requirement in RG 139.77–RG 139.79 should be removed so that the pre-1 January 2010 position for FOS is reinstated. Note: However, during the joint roundtable discussion (see paragraphs 46–50), all industry associations expressed support for EDR and the debt recovery legal proceedings jurisdiction.	Two industry submissions (AFMA, ABA)

Summary of our response to submissions

37 Because most of the submissions asked for refinements to EDR schemes' debt recovery legal proceedings jurisdiction, our review focuses on the key areas for enhancement.

38 Given the nature and number of requests for refinements, we do not propose to broaden the scope of RG 139.77–RG 139.79 at this time.

39 Some industry submissions raised concerns about how EDR schemes handle credit complaints more generally, even when a lender may not have commenced debt recovery legal proceedings. While these matters are outside the scope of this review, we encourage both FOS and COSL to consider this feedback as part of each scheme's ongoing schedule for improvement (including as part of their short-term business plans, development of key performance indicators and next independent review of operations, as required by RG 139).

40 A few industry submissions (ABACUS, AFMA and Bransgroves Lawyers) called for ASIC to conduct a broader review or 'wholesale stocktake' of EDR schemes and the requirements in RG 165 and RG 139, to make sure that schemes do not become inefficient and ineffective by delivering unsatisfactory outcomes to consumers and industry.

41 We have carefully considered this request and consider that it is too early for a full-scale review of the requirements in RG 165 and RG 139, given the short time that has passed since EDR scheme membership became mandatory for credit in 2010 and since our last major review of the dispute resolution system, which ended in May 2009, and subsequent updates for credit in 2010.

42 Instead, we think that EDR scheme efficiency and effectiveness can be best enhanced in the following ways:

(a) Each EDR scheme has an ongoing schedule for improvement (see paragraph 39), which should consider ways to address the feedback provided to this review. We will continue to liaise with users of EDR schemes (both consumer organisations and industry associations) to monitor concerns and work with the schemes to ensure that the dispute resolution system is operating efficiently and effectively for credit.

(b) Any further refinements to the dispute resolution system for Phase II credit reforms may also address some of these issues.

43 Given the benefits for consumers in being able to access an EDR scheme's debt recovery legal proceedings jurisdiction, we do not propose to remove the requirement in RG 139.77–RG 139.79 altogether, so FOS can return to its pre-1 January 2010 position whereby consumers were unable to access FOS after scheme members had initiated debt recovery legal proceedings.

44 This is because:

(a) during the joint roundtable discussion (see paragraphs 46–50), stakeholders expressed support for the EDR process and the useful role an EDR scheme's debt recovery legal proceedings jurisdiction plays;

(b) both consumer groups and EDR schemes have reported that this jurisdiction continues to be useful in helping consumers to obtain hardship assistance or further time to sell their home (without the need to proceed to court); and

(c) removing the jurisdiction altogether would detract from the Government's policy intention that as many credit complaints as possible be addressed through IDR and EDR.

Note: '*Wherever possible, parties will be encouraged to resolve disputes without resorting to litigation. It is expected that courts would generally only be utilised where internal dispute resolution (IDR) and EDR processes have not resolved the matter, or where EDR is considered inappropriate.*' See Revised Explanatory Memorandum to the National Consumer Credit Protection Bill 2009 (Explanatory Memorandum), para 4.9.

45 Removing this jurisdiction may also cause significant consumer detriment and might result in some consumers being disadvantaged by differences in EDR scheme approaches, particularly if COSL continues to meet the requirement in RG 139.77–RG 139.79 (it had this jurisdiction before 1 January 2010).

Roundtable discussion

46 The purpose of the joint roundtable discussion was to enhance stakeholder understanding of each other's perspectives, to reach a collective solution and to help ASIC further develop options to refine the requirement in RG 139.77–RG 139.79.

47 All attendees expressed support for the EDR process and acknowledged the useful role an EDR scheme's debt recovery legal proceedings jurisdiction plays.

48 Attendees agreed that some of the problems raised by written submissions to CP 172 could be best addressed by EDR schemes adjusting their approach to this jurisdiction, rather than by ASIC adjusting our guidance in RG 139. It was also agreed that any solution would need to be collective, with all stakeholders taking steps to do their part to make the dispute resolution system work better.

49 This would include:

(a) better early identification of hardship by licensees and better resourced and more efficient and effective complaints handling teams;

(b) enhanced EDR scheme operations and processes;

(c) enhanced consumer understanding of how an EDR scheme's debt recovery legal proceedings jurisdiction can assist a consumer and a consumer's continued obligation to make repayments where possible; and

(d) some relatively minor refinements to ASIC guidance in RG 139.77–RG 139.79.

50 In this report, we discuss the key feedback received from submissions, informal discussions and the joint roundtable session, and our findings on:

(a) EDR scheme operational issues (see Section B);

(b) possible refinements to our guidance in RG 139.77–RG 139.79 (see Section C); and

(c) suggestions for improving the IDR process (see Section D).

B EDR scheme operational issues

Key points

Both industry and consumer submissions identified delays at the EDR stage as an area for improvement.

Many industry submissions also identified specific areas of improvement for EDR schemes to help minimise delay when handling complaints under their debt recovery legal proceedings jurisdiction. These were that EDR schemes should be:

- more proactive in assisting the parties to find early resolutions;
- quicker at identifying 'serial' complainants; and
- quicker at identifying whether a complaint is outside the scheme's jurisdiction.

Some industry submissions suggested that ASIC should consider introducing time limits for EDR schemes to handle complaints under their debt recovery legal proceedings jurisdiction. We have decided against introducing a time limit because this could undermine the effectiveness of this jurisdiction if scheme members do not genuinely respond to a complaint at the EDR stage before the time limit expires, or further time is needed for this process to achieve an outcome.

Because many concerns related to EDR scheme operational or process issues, we encourage schemes to engage in further dialogue with scheme users to explore how to best enhance scheme processes to minimise delay.

Addressing delays

51 Industry and consumer submissions identified undue delays at EDR as an area for improvement.

52 ABACUS's submission reported delays of 3–4 months at FOS. The Australian Securities Ltd's submission reported that the EDR process can take up to 6–12 months longer than if the same matter is addressed in the Supreme Court. We consider that the short time in court may perhaps be because the consumer has not contested the matter in court, most likely because they do not have the resources nor legal representation to be able to do so.

53 One industry submission (AFMA) expressed particular concern that delays can make it more difficult for lenders to realise their security (AFMA) and this can be aggravated by consumers not making regular payments while the complaint is addressed at EDR (AFC).

54 This needs to be considered, given the types of complainants who may routinely need the greatest assistance at the EDR stage under a scheme's

debt recovery legal proceedings jurisdiction. FOS has suggested that some consumers in extreme hardship may not be able to make regular repayments (e.g. where an unsuitable loan has been granted) or a statute barred debt is being pursued.

55 FOS also reports that delays are primarily caused by members who do not follow their expedited processes for debt recovery legal proceedings complaints.

56 This is reflected by FOS statistics on its debt recovery legal proceedings jurisdiction, which indicate that where members fail to meet FOS timeframes under its expedited process—perhaps because the member's complaints handling team is under-resourced—the complaint ceases to be expedited.

57 FOS reports that complaints that fall off the expedited track generally take longer to resolve than those that remain expedited. Expedited debt recovery legal proceedings complaints are on average resolved within 90 days at FOS.

> Note: See FOS's report at www.fos.org.au/centric/home_page/publications/debt_recovery_legal_proceedings_statistical_report.jsp.

58 We also note the concerns of Genworth in its submission that COSL's expedited process under its rules only applies to low value complaints (under $3,000) if the COSL member pays a fee. Genworth suggests that this process could be expanded to cover debt recovery legal proceedings complaints.

59 During discussions and the joint roundtable session, COSL advised that while their rules do not specifically refer to an expedited process for debt recovery legal proceedings complaints, their practice is to treat these complaints urgently, given the implications for members in having to stay debt recovery legal proceedings.

60 To address delays, which can contribute to prolonged stays of enforcement proceedings, some industry submissions (ABA, ABACUS and MFAA) suggested that ASIC should consider introducing a maximum time limit for EDR schemes to handle debt recovery legal proceedings complaints. Such a maximum timeframe could be as short as 60 days (Ezy Mortgage) or up to 9 months (MFAA). After the expiry of the timeframe, scheme members would be free to pursue their debt recovery action in court. That is, a stay of legal proceedings would no longer apply or the scheme member would be free to reinitiate legal proceedings.

61 Other submissions and comments made during informal discussions (ABACUS and Ezy Mortgage) suggested that ASIC should introduce more prescriptive maximum timeframes for interim steps in the EDR process (i.e. for an EDR scheme to assess a complaint and refer the matter to the scheme member).

62 Other submissions suggested alternative ways for schemes to reduce delay, including:

(a) better resourcing of the schemes so they can more efficiently carry out their complaints handling functions, with more experienced and highly skilled staff handling complaints at the earlier stages of the scheme process (CCLS WA and Redfern Legal Centre); and

(b) quicker identification of 'serial complainants' and complaints outside a scheme's debt recovery legal proceedings jurisdiction. We discuss this further at paragraphs 66–73.

63 Consumer submissions commented that there is no evidence in FOS's statistical report of delay when FOS handles complaints under its debt recovery legal proceedings jurisdiction (CCLC NSW). CCLC NSW also suggested that a solution to perceived industry delay could be that lenders refer consumers to a financial counsellor or consumer lawyer by calling Financial Counselling Australia's advice line on 1800 007 007. This could assist consumers to seek more realistic outcomes.

64 Some submissions suggested that if a scheme member's complaints handling team could be better resourced and trained, some of the pressures on EDR may be alleviated. We discuss improving the IDR process in Section D of this report.

Schemes should more proactively offer solutions

65 Some industry submissions (ABACUS, AFMA and Fox Symes Home Loans Group) expressed concern that the EDR schemes seem to provide a service of 'passing shuttle negotiation', whereby passing offers and counteroffers are exchanged between the parties instead of the scheme proactively suggesting options for resolution. This wastes time instead of focusing on early resolutions.

Schemes should more quickly identify 'serial complainants'

66 Some industry submissions (AFC, AFMA, Angas Securities, Credit Corp Group, GE Capital, Fox Symes Home Loans Group and MFAA) raised concerns about complainants who lodge subsequent complaints at EDR to delay the inevitable and stop debt recovery enforcement proceedings indefinitely. They considered these complaints to be either 'frivolous' and 'vexatious' or an abuse of the EDR process, especially if complainants stop making loan repayments altogether.

67 The Consumer Action Law Centre joint consumer submission and the Legal Aid NSW submission commented that FOS and COSL statistics suggest there is little or no evidence of abuse of EDR schemes' debt recovery legal

proceedings jurisdiction. Rather, complainants often feel confused and paralysed by the complex legal process they find themselves in. Furthermore, as both FOS and COSL have clear provisions under their respective terms of reference or rules to exclude 'frivolous and vexatious' complaints, it is unlikely that such complaints would be able to proceed at the EDR stage.

> Note: See paragraph 5.2(d), FOS Terms of Reference (effective 1 January 2012) and Rule 10.1(t), COSL Rules (8th edition).

68 Other industry submissions also raised concerns about 'serial' complainants who continue to lodge subsequent complaints, often about new issues which were not identified at the start of the EDR process or which are unconnected with the resulting hardship. This then further delays a scheme member's ability to recover possession of a security and indefinitely stops debt recovery legal proceedings.

69 Some consumer submissions (e.g. Redfern Legal Centre) believed that concerns about delay and EDR processes potentially being open to abuse by serial complainants were overstated.

70 Industry groups expressed concerns that prolonged stays of legal enforcement proceedings are problematic, not only in terms of costs to scheme members, but also in terms of costs to complainants (many of whom may find themselves in a worse financial position, even having to declare bankruptcy, compared with if the matter had proceeded to court).

71 This may be further exacerbated when complainants stop making repayments (whether in full or in part under a hardship arrangement) while the complaint is at the EDR stage.

Schemes should more quickly identify complaints outside their jurisdiction

72 Several industry submissions (ABACUS, Genworth) suggested that EDR schemes should more quickly and appropriately identify and exclude complaints outside a scheme's jurisdiction.

73 At the joint roundtable discussion, it was considered that these complaints could include where a court would be the more appropriate forum for handling a complaint involving debt recovery legal proceedings (i.e. there would be no reasonable prospect of success or assistance being able to be provided at the EDR stage).

Options for improvement

74 During informal discussions and the joint roundtable discussion, attendees suggested a range of options EDR schemes could consider to reduce delay:

(a) EDR schemes could look at ways to better capture all of the complainant's issues at an earlier 'triage' or complaint assessment stage so as to reduce the number of complaints where new issues are subsequently raised by the complainant (e.g. by reiterating the complainant's concerns over the phone to confirm they are complete and correct and to draw out any other issues that may not have been elucidated by the consumer's written complaint).

(b) EDR schemes could better cross-check whether a complainant is raising new issues about a complaint that has already been addressed so the matter may be handled by the same EDR scheme staff member.

(c) FOS could consider introducing a similar process to COSL, whereby the scheme does not reopen a complaint for a new issue if the complainant would not be likely to be able to be able to meet their repayment obligations (even if the contract was varied). Instead, the complaint may be opened as a query (with the lender being able to continue enforcement action) while the complaint is being assessed. The query may then only be reopened as a complaint if there is a real prospect of refinance or sale without a shortfall or if the complainant is now able to demonstrate they will be able to meet their payment obligations if the contract is varied.

(d) COSL could consider introducing a formal expedited process under its Rules for debt recovery legal proceedings complaints in addition to their current approach to treating these complaints as urgent.

ASIC's response

We encourage both FOS and COSL to engage in further dialogue with all scheme users to explore how to best enhance scheme operations and processes to minimise delay.

As part of these further discussions, we encourage the schemes to consider:

- how to more proactively offer early resolutions;
- the options suggested in paragraph 74 to reduce delay; and
- how to practically determine whether a complaint would be outside the scheme's jurisdiction because it could be more appropriately dealt with in court.

We encourage scheme members to utilise and comply with expedited processes, given that avoiding unnecessary delay is in the interest of all parties.

We encourage the schemes to reconsider whether they have the right levels of resourcing and whether more experienced and highly

skilled staff should be employed to handle complaints at the earlier stages of the scheme process (e.g. assessment and triage).

We will follow up with the schemes on how this is progressing as part of our regular and ongoing liaison.

After careful consideration, we have decided against introducing maximum and specific timeframes within which a scheme must handle complaints involving debt recovery legal proceedings. This is because these timeframes may create disincentives for scheme members to promptly respond to and cooperate with EDR scheme processes. We would be concerned that this could undermine a scheme's debt recovery legal proceedings jurisdiction.

C Refinements to RG 139

Key points

A number of industry submissions recommended that the obligation for a stay on debt recovery legal proceedings should be directly connected to the subject matter of the complaint.

Other industry submissions and FOS suggested that ASIC limit the scope of RG 139.77–RG 139.79 to allow EDR schemes to exclude certain types of complaints from their debt recovery legal proceedings jurisdiction, including certain types of commercial/small business complaints, which may involve more complex issues (and which may be more appropriately addressed in court).

Consumer submissions strongly opposed limiting the scope of a scheme's debt recovery legal proceedings jurisdiction for certain types of financial products, scenarios or groups because this may arbitrarily deny access to EDR.

We have decided to consult on a discrete proposal to refine our guidance in RG 139.77–RG 139.79 for small business complaints only: see Consultation Paper 190 *Small business lending complaints: Update to RG 139* (CP 190).

Stays on legal proceedings

75 A number of industry submissions (ABA, ABACUS, AFC, Credit Corp Group, Ezy Mortgage and MFAA) commented that a stay on debt recovery legal proceedings under RG 139.77–RG 139.79 should only be permitted when a complaint at the EDR stage relates to hardship or enforcement action. For example, a stay should not apply to complaints where there are peripheral issues to hardship or enforcement action—that is, separate complaints about direct debit fees, penalty fees, interest or enforcement fees that have no direct correlation with hardship or enforcement action should not invoke a stay.

76 The AFC commented that a stay of legal proceedings should only be granted on condition that the consumer maintains a regular repayment schedule or makes reasonable payments while the complaint is at the EDR stage.

77 During informal discussions and the joint roundtable discussion, consumer representatives and FOS expressed strong concerns that complainants in extreme hardship may not always be able to make any repayment, especially if they have been granted an unsuitable loan. To deny these complainants access to EDR might prevent the most vulnerable and disadvantaged from obtaining this assistance when they may need it the most.

78 CCLC NSW's submission commented that it is not clear how fee complaints would not relate to hardship or enforcement action and this should be clarified by those who seek the exclusion.

79 During informal discussions and at the joint roundtable discussion, consumer representatives and FOS commented that it is practically impossible to distinguish fee complaints from hardship and enforcement action issues. Participants in the roundtable discussion were invited to provide further information and examples to illustrate the distinction.

Exclusion of certain types of complaints

80 Consumer submissions (the Consumer Action Law Centre joint consumer submission and the separate CCLC NSW submission) opposed limiting the scope of RG 139.77–RG 139.79 to exclude particular financial products, scenarios or groups from EDR because this will arbitrarily deny access to EDR and may create confusion.

81 Submissions from industry (ABA, Ezy Mortgage, Fox Symes Home Loans Group and MFAA) and comments raised during informal discussions suggested that the following types of complaints should be excluded from an EDR scheme's debt recovery legal proceedings jurisdiction:

(a) complaints where the complainant has already had their loan contract varied, but is unable to meet the varied terms;

(b) complaints where the complainant fails to make regular repayments or makes intermittent repayments;

(c) complaints involving enforcement action regarding an unsecured credit facility (i.e. over a car, furniture);

(d) complaints involving fees only (and unrelated to hardship or enforcement action); and

(e) complaints involving investment property loans (unless the borrower/guarantor's primary residential property is at risk).

82 Table 3 sets out these types of complaints and why, after discussion at the joint roundtable session, it was considered inappropriate to exclude them.

Table 3: Proposals to limit an EDR scheme's debt recovery legal proceedings jurisdiction

Type of complaint	Reasons for not excluding these types of complaints
The complainant has already had their loan contract varied, but is unable to meet the varied terms	Under national credit laws and the Enhancements Act, borrowers may properly seek more than one hardship variation during the life of the loan if new and different circumstances arise. Industry's current standard practice of offering an initial hardship variation for 3 months, before further reviewing the borrower's circumstances on a longer term basis, may mean that borrowers may reasonably need to come back for a further hardship application.
The complainant fails to make regular repayments or makes intermittent repayments	Consumers who are genuinely in hardship may be unable to make any repayment, however small. They should not be denied access to an EDR scheme's debt recovery legal proceedings jurisdiction.
Complaints involving enforcement action regarding an unsecured credit facility (i.e. over a car, furniture)	For EDR schemes to meet the principles of 'accessibility' and 'effectiveness', under RG 139, they must be able to handle the *vast majority* of types of complaints in the particular industry or industries covered by the scheme. If these types of complaints are excluded from EDR, there could be a significant number of consumers who would be disadvantaged in that they would be unable to access an EDR scheme for assistance. If this were to happen, it is highly likely that the requirement for access to EDR in RG 139 would not be met.
Complaints involving fees only (and unrelated to hardship or debt recovery)	Some industry submissions suggested that complaints about a direct debt fee, penalty fee, interest or enforcement fee that are not directly connected to the resulting hardship should be excluded from an EDR scheme's debt recovery legal proceedings jurisdiction. During discussions, consumer representatives and EDR schemes raised concerns that fee issues are commonly intertwined with hardship issues and it would be practically impossible to easily determine when a fee issue is unconnected with hardship. Because no particular examples of cases where a fee issue would be clearly unconnected with hardship could be provided, there did not seem to be evidence to support excluding such complaints.
Complaints involving investment property loans (unless the borrower/guarantor's primary residential property is at risk)	The Australian Government has brought investment property loans within the scope of the National Credit Code so that borrowers have certain consumer protections, including access to EDR. It would detract from the Government's policy intention if these complaints were excluded.

Complaints involving commercial or small business loans

83 Submissions from commercial lenders (Angas Securities, Banksia Mortgages Limited, Fox Symes Home Loans Group and Southern Finance Ltd) and industry associations (ABACUS and MFAA) expressed concerns that there has been unintended 'jurisdictional creep' as FOS's and COSL's debt recovery legal proceedings jurisdiction extends to non-National Credit

Code regulated commercial loans, when the rationale for this jurisdiction was to assist consumer borrowers in hardship.

84 Both the FOS and COSL submissions clarified that currently, under their respective terms of reference or rules, small businesses (i.e. businesses that meet the definition of a small business under the Corporations Act) can complain to the schemes and access their debt recovery legal proceedings jurisdiction. COSL commented that where a complainant appears to have similar resources to a scheme member, COSL will assess whether the loan that is the subject of the dispute, and if the loan value exceeds the current $500,000 limit in Sch 1 of the National Credit Act (National Credit Code), COSL will consider whether to exercise its discretion not to handle the complaint under Rule 10.1(p), as another forum such as a court would be more appropriate.

85 A number of industry submissions (Ezy Mortgage, Fox Symes Home Loans Group, MFAA) suggested that all debt recovery legal proceedings complaints (whether brought by individual borrowers or small businesses borrowers) where the loan value exceeds $1 million should be excluded from accessing an EDR scheme's debt recovery legal proceedings jurisdiction. This is because these types of complaints would be more appropriately addressed in court.

86 The ABA in its submission suggested that all loans where the value of the security exceeds $1 million should be excluded from this jurisdiction.

87 During the roundtable discussion, FOS suggested that complaints where the loan value exceeds more than $5 million could be excluded from its jurisdiction as being more appropriately addressed in court.

88 CCLC NSW's submission commented that the assumption that borrowers with loans over $1 million are sophisticated is not correct. Many problems have occurred over the last decade due to poor lending standards and many unsophisticated borrowers have been granted high value loans. These borrowers should not be denied access to EDR.

Proposed refinement to RG 139

ASIC's response

We have decided against limiting the scope of RG 139.77–RG 139.79 to exclude certain types of complaints from an EDR scheme's debt recovery legal proceedings jurisdiction for the reasons summarised in Table 3. If these limitations were introduced, we would be concerned they would compromise a scheme's ability to continue to meet the overarching principles of accessibility, efficiency and effectiveness.

However, we believe there is merit in considering further whether an EDR scheme's jurisdiction should exclude certain types of small business lending complaints because they would be more appropriately dealt with in another forum (i.e. court).

We think that all small business borrowers should not be totally excluded from accessing this jurisdiction. This is because:

- Phase II credit reforms may extend the credit laws to cover small business lending; and
- it would be inconsistent with current banking practice—for example, the ABACUS Mutuals Banking Code of Practice (clause 24) and ABA's Code of Banking Practice (clause 25.2) currently commit to assisting small business complainants in hardship.

Certain small business borrowers may also benefit from being able to access this jurisdiction.

We are consulting further on how small business lending complaints may be legitimately excluded. In particular, we seek feedback on where to appropriately draw the line so that certain types of small business lending complaints are more appropriately dealt with in court.

We do not consider that excluding small business lending complaints based on the value of the security would be practically workable, given that the value of the security may change during the life of the loan and this may create disputes about whether the EDR scheme has jurisdiction to handle the complaint. It may be more practically workable to exclude small business lending complaints based on the value of the loan granted.

We seek feedback on these issues in Consultation Paper 190 *Small business lending complaints: Update to RG 139* (CP 190).

D Improving the IDR process

Key points

Feedback from consumer representatives, EDR schemes and some industry associations suggest AFS licensees and credit licensees could do more to:

- proactively assist consumers in the earlier stages of hardship;
- better train and resource their frontline staff to identify and consider hardship issues; and
- better resource their complaints handling teams to respond to complaints involving debt recovery legal proceedings at the EDR stage.

Consumer representatives reported that consumers they assist who indicate they have hardship issues are not always able to access IDR because frontline staff are not trained or empowered to identify hardship issues, nor are they able to consider hardship applications.

This suggests that consumers are not able to benefit from a hardship variation at earlier stages when they are experiencing hardship. This creates pressures at later stages of the loan term, causing potentially more complaints under an EDR scheme's debt recovery legal proceedings jurisdiction.

Licensees could do more to enhance their hardship processes

89 COSL's submission and industry and consumer submissions highlighted the role of IDR in helping to reduce pressures on EDR.

90 The IDR process may not be working as effectively as it could to assist borrowers in the earlier stages before debt recovery legal proceedings are commenced. This may be because of a range of factors, including that:

(a) some consumers do not recognise early on that they may need hardship assistance (some of these consumers may be particularly vulnerable and disadvantaged and need special assistance);

(b) consumers may not be aware they can seek assistance directly from their lender through the IDR process; and

(c) a lender's enforcement/debt recovery or collections staff may focus only on seeking repayment, and be unable to properly identify whether a borrower is experiencing hardship issues or whether they have made a complaint, and so refer the consumer to IDR teams that are better able to deal with hardship issues. This places more pressures on an EDR scheme's debt recovery legal proceedings jurisdiction.

ASIC's response

We encourage AFS licensees and credit licensees to:

- consider ways to more proactively assist consumers to recognise that they are in financial hardship at earlier stages when they experience hardship;
- better resource and train their frontline and collections staff to properly identify and consider hardship issues; and
- better resource their complaints handling teams so they can respond to complaints at EDR in a timely manner (and, in FOS's case, so that a complaint under its debt recovery legal proceedings jurisdiction can continue to be expedited).

Hardship and the IDR process will continue to be a priority for ASIC in 2012–13.

Appendix: Attendees and respondents

List of attendees at the joint roundtable discussion

- ABACUS Australian Mutuals
- Australian Financial Markets Association (AFMA)
- Australian Bankers' Association (ABA)
- Australian Finance Conference (AFC)
- Consumer Action Law Centre (Vic)
- Credit Ombudsman Service Limited (COSL)
- Financial Ombudsman Service Limited (FOS)
- Genworth
- Legal Aid NSW
- Mortgage & Finance Association of Australia (MFAA)

List of non-confidential respondents

- ABACUS Australian Mutuals
- Australian Financial Markets Association (AFMA)
- Angas Securities
- Australian Bankers' Association (ABA)
- Australian Collectors & Debt Buyers Association
- Australian Finance Conference (AFC)
- Australian Securities Limited
- Banksia Mortgages Limited
- Bransgroves Lawyers
- Consumer Action Law Centre (joint consumer submission)
- Consumer Credit Legal Centre NSW (CCLC NSW)
- Consumer Credit Legal Service (WA) Inc (CCLS WA)
- Credit Ombudsman Service Limited (COSL)
- Credit Corp Group
- Ezy Mortgage
- Financial Ombudsman Service Limited (FOS)
- Fox Symes Home Loans Group
- GE Capital
- Genworth
- Legal Aid NSW
- Mortgage & Finance Association of Australia (MFAA)
- Provic
- Redfern Legal Centre
- Southern Finance Ltd