

# **HALSEY LEGAL SERVICES**

## **BARRISTERS & SOLICITORS**

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26 July 2007

Mr Michael D'Árgaville  
Financial Industry Complaints Service  
31 Queen Street  
MELBOURNE Victoria 3000

Dear Mr D'Áragville

### **FICS REVIEW OF MONETARY LIMITS**

We refer to your email dated 4 May 2007, and to the "*Review of the FICS Monetary Limits – Consultation Paper – May 2007*" (the "**Monetary Limit Review**"). FICS has invited comment and submissions in relation to the Monetary Limit Review. The following is our submission in relation to the Monetary Limit Review.

We will address the issues in the Monetary Limit Review in the order in which they have been raised by FICS. In commenting on the issues, we have made a brief summary of our understanding of FICS' proposal, and then offered our comments. If you believe that our understanding of FICS' proposal is either inaccurate or incomplete we would appreciate you alerting us to that fact because it may cause us to reconsider our comments.

#### **1. Application of the monetary limits**

##### **FICS position**

It would appear to be FICS' proposal that the future process for FICS considering complaints would be to ignore the issue of monetary limits as a means of establishing FICS' jurisdiction. Instead, what FICS appears to be suggesting is that FICS will have jurisdiction to hear ALL complaints placed before it without regard to monetary limits.

The monetary limit would then only apply to the size of the award that FICS could make after hearing the complaint.

FICS states that this has been the model in the UK for over 7 years.

FICS' logic behind this proposed change is that the process of establishing the monetary limit jurisdiction at the commencement of a complaint has somehow become too complex, time consuming and expensive.

## **Our response**

We strongly object to this proposal on the following grounds.

Ground 1: It has long been the understanding of a substantial part of the financial services industry that FICS (and other similar bodies) were designed to provide a forum where consumers may resolve disputes involving relatively small to medium amounts (in monetary terms) more quickly and cheaply than through the formal legal process.

The overall concept of the alternative dispute resolution forum was set out in ASIC Policy Statement PS 139. A common understanding of its application to complaints involving relatively small to medium monetary values was evidenced by the fact that each scheme had strict upper monetary limits attaching to their jurisdiction.

There was not, and has never been, an understanding or acceptance by the broader financial services industry that the external dispute resolution schemes would somehow become an alternative court system for financial advisers.

The proposed removal of the monetary limit jurisdiction condition at the commencement of the complaint process would result in the unacceptable removal of a key filtering process and result in this scheme having an almost "universal" application.

The lack of an effective appeals mechanism from the schemes to the nation's formal judicial system effectively denies financial advisers a basic legal right afforded to other Australians. This disadvantage is a key reason why it is not desirable that this type of scheme should have "universal" application and should not apply to effectively ALL disputes between financial advisers and their clients.

Another problem of such a "universal" application is that AFS licensees would be required to shoulder the **entire** burden of the cost of dispute resolution which can be thousands of dollars per claim (in the form of mandatory FICS case management, conciliation and Panel fees) for disputes where the monetary limits have been exceeded, and where arguably, it may be appropriate for the complainants to shoulder at least some of the costs of the process in a similar way as that of the Federal and State court systems.

A further negative consequence of the "universal" application is that FICS and similar systems operate at a qualitatively "lower level" in the administration of the law. By this we mean that significant legal protections and processes for persons and entities in the financial services industry have been stripped away in the name of forming a "quick, cheap and easy" system to assist certain retail clients with lower amounts in dispute. The legal protections I

refer include the adherence to the strict rules of evidence, rights of joinder by parties to the dispute, the right of appeal etc...

To the full credit of the financial services industry it has not only tolerated, but has supported these schemes because the industry recognised the need to provide a *segment* of the broader community with access to “cheap and easy” remedies even if those remedies risked some level of “rough justice” to financial services industry participants. An example of this “rough justice” includes the fact that FICS has made determinations that have been contrary to Australian legal principles (I refer to the previous determinations relating to disputes involving financial products in joint names and related disputes involving financial products held by trustees which the Federal Court subsequently found were made incorrectly by FICS).

We reject any further movement towards a more “universal” approach to all financial services dispute handling by what is effectively a privatised tribunal which, because of its Rules, will have the effect of substantially reducing the ability of financial advisers to access the nation’s proper judicial system.

We believe that there is a crucial need to have the overall system altered to provide members a formal right to appeal to the courts against any FICS decision relating to a question of law.

Ground 2: Virtually every Federal and State court, tribunal and other similar dispute resolution body – including all Australian external dispute resolution bodies approved by ASIC within the financial services system - operate under rules that require an initial determination as to whether a complaint falls within the relevant scheme’s monetary jurisdiction. If all of these other bodies are able to continue to operate under their existing arrangements, how has it suddenly become too “...complex, time consuming and expensive ...” for FICS to do so? If this really is an issue for FICS, it is probably more appropriate that FICS concentrate on reviewing its own processes and capacities.

Ground 3: A further reason to reject the proposal can be found in ASIC Policy Statement PS 139 at paragraph 139.5. ASIC nominates a public policy goal of seeking to harmonise the standards and operational processes (to the extent possible) of the ASIC approved external dispute resolution schemes. Since none of the other approved schemes in Australia appear to be following FICS’ proposed process of dispensing with the monetary limit jurisdiction condition, this proposal would seem contrary to that policy.

## 2. “Two-tier” Approach

### **FICS position**

In recognition of the difference between AFS licensees in terms of financial capacities and resources, FICS queries whether it may be appropriate to introduce a two-tier structure on monetary limits. Presumably the smaller licensees would be subject to lower monetary limits than the larger licensees.

Consumers would be advised which monetary limit applied to their complainant at the point of entry to FICS.

### **Our response**

We generally support this proposal. Differing financial capabilities and resources between AFS licensees are a fact of life, and should be acknowledged.

However, this issue should be disclosed to consumers much earlier in the overall process to ensure that consumers have the opportunity to make an informed choice. It is arguably too late to advise a consumer about monetary limits at the point of claim. This is potentially a matter that could be capable of influencing an informed consumer's choice at the time of selecting an adviser. It should therefore be made clear on pre-contractual documents such as the relevant Financial Services Guide ("**FSG**"). You will appreciate that the new Corporations Regulation 7.6.02AAA relating to mandatory professional indemnity insurance ("**PII**") prescribes disclosure of PII arrangements in the FSG. It may therefore also be appropriate to include the disclosure of the relevant FICS member's monetary limits as it applies to potential complaints in the same section in the FSG.

### **3. Level of limits**

#### **FICS position**

FICS believes that the monetary limits must be increased. FICS states that it is supported by both its external independent consultants who performed the FICS independent review in 2002, as well as by ASIC. FICS do not offer any suggested increased dollar values.

#### **Our response**

Generally, the financial services industry recognises the need for increases in monetary limits over time, and hence the concept of an increase is generally supported (subject to certain conditions). However, any proposed increased monetary limit should only be adopted where the changes have the support of the insurers that provide the financial services industry's PII. There cannot be an increase in monetary limits with the optimistic hope that the PII insurers will somehow "follow". Our concern in this area relates to the relatively questionable handling of the existing PII arrangements referred to below.

The current PII issue that causes us concern relates to the current FICS Rules monetary limits for **advice** in relation to life insurance of \$250,000. This FICS Rule exists in the context where most PII policy terms and conditions only provide for insurance cover of \$100,000 in relation to FICS awards or determinations. An obvious problem relates to the creation of a potentially significant underinsurance problem for AFS licensees who are involved in life insurance and have PII policies with the terms referred to above. We believe

that not enough has been done to provide the financial services industry with comfort on this matter, given that we first raised this issue with FICS over two years ago.

It has been suggested that the higher limit \$250,000 limit (instead of the “usual” \$100,000 limit) was not intended to apply to “F” Class Members. However, we have seen no action or proposal by FICS to amend the wording to the FICS Rules to reflect that position, notwithstanding several FICS proposals to amend the FICS Rules from time to time (including the current proposal).

This position should be corrected as a matter of urgency.

In summary, whatever increased monetary limit FICS adopts, it should only do so with the support of the PII insurer market. If that does not occur the system will break down.

Based on our comments on point 1 and conditional on support from the PII insurers, we would not wish to see the “normal” adjusted monetary limit (which is currently \$100,000) exceed \$150,000 as a consequence of this Monetary Limit Review.

A period of 12 months after the passage of the FICS Rule change should be allowed as a transition period so as to enable PII insurance policies taken out by AFS licensees under the “old” FICS Rules to expire and for new policies to be taken out with terms to reflect the new limits. Naturally, any renewing PII policies after the date of announcement of the FICS Rule change (and during the transition period) would need to adopt the “new” monetary limits.

#### **4. Indexing the limits**

##### **FICS position**

FICS believes that it is essential to increase the monetary limits on an ongoing basis by indexation rather than seeking periodic FICS Rule changes.

##### **Our response**

We broadly accept the FICS position and believe, as with many other fiscal matters that require indexation, the national CPI would be the appropriate index. The grounds for this position relates to the need to ensure that the change in the level of potential compensation for investors over time should be adjusted to ensure that it keeps pace within the changing cost of living of the investor/ complainant over time. An index reflecting the changes in value of investments or asset class would seem inappropriate for two reasons:

- Typically a fall in such asset values (hence a fall in the relevant assets' indices values) may coincide with potentially consumer claims. Would it be appropriate to actually lower monetary limits at this time? and

- An index based on increasing asset values may not reflect the purpose of a consumer compensation arrangement – which one would expect should ensure the maintenance of consumers complainants purchasing power. This index should not reduce to reflect adverse conditions (as mentioned above) or increase in good conditions to provide for “windfalls”.

Thank you for the opportunity to comment on the proposed changes. If you would like to discuss these comments further please feel free to contact me on (08) 9382 4128.

Yours sincerely

**MARK HALSEY**