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Industry dispute management in financial services

Dispute systems in the financial services industry — Part 2

Anna Everett

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Statutory requirements for external dispute resolution

There are several approved external dispute resolution (EDR) schemes available to banking customers in Australia. The largest EDR scheme is the Banking and Financial Services Ombudsman (BFSO) Scheme.

As background to the BFSO Scheme, the Australian Banking Industry Ombudsman scheme was established in 1990 on the initiative of the Australian Banker's Association. Under the Code of Banking Practice (1996), banks agreed to provide for their personal customers an EDR service. This meant that all retail banks operating in Australia were members of the Ombudsman scheme.

The business of 'banking' has expanded over recent years to include non-bank financial service providers. In August 2003, the Australian Banking Industry Ombudsman (ABIO) changed its name to the Banking and Financial Services Ombudsman (BFSO) in order to reflect this change in the financial services environment. The BFSO is an external dispute resolution scheme which has been approved by the Australian Securities and Investments Commission (ASIC).

The scheme is open to individuals and also to small businesses that use financial services on a retail basis. The terms of reference of the BFSO state that the ombudsman can consider disputes where the individual or small business has:

- received the financial service that is the subject of the dispute; or
- provided security for a financial service and either the security or the financial service is the subject of the dispute; or
- provided information which is the

subject of the dispute relating to confidentiality (both individual and small business) and privacy (individual).

The BFSO cannot consider a dispute if the claim for loss exceeds \$250,000.¹

On receipt of a dispute, the BFSO will refer the dispute back to the financial service provider. The BFSO considers that, even if the dispute has already gone through the financial service provider's customer relations department, referral back by the ombudsman can sometimes resolve the dispute without further external involvement.²

Under the terms of reference, the BFSO will encourage the parties to resolve their dispute via negotiated settlement. This is achieved by facilitating communication between the parties, clarifying the issues in dispute, and pointing out the strengths and weaknesses of each party's position.³

Another option for resolving a dispute is a conciliation conference between the disputant and the financial service provider. This may be convened by the case manager and/ or the BFSO. This is an informal meeting in which the parties are assisted in order to resolve the dispute.⁴ The decision to have a conciliation conference rather than a negotiation is up to the case manager, not the consumer or financial institution.⁵

The case manager/ombudsman then sets down their views about the merits of the dispute. This is known as a 'finding'. Neither party is bound to accept the views set out in the finding.⁶ A finding includes:

- a summary of the dispute and the financial services provider's response;
- a summary of the issues raised by the dispute;
- the case manager's analysis of the case; and
- the case manager's conclusion about



how the matter should be resolved.⁷

If the parties do not agree to the finding, then the BFSO may proceed to issue a recommendation which sets out how the BFSO considers the dispute should be resolved. The BFSO will give the parties one month's notice of its intention to issue a recommendation. Both parties have one month in which to accept or reject the recommendation.⁸

If the disputant rejects the recommendation there is no further right of appeal and the BFSO cannot assist the disputant further. The disputant may pursue the matter at this stage through the courts.

If the disputant accepts the recommendation, but the financial service provider does not, the BFSO will issue a determination. If the disputant accepts the determination, then the financial service provider is bound by the determination. Only the disputant has the option of rejecting the determination.⁹

In summary the BFSO Scheme involves four steps:

1. Referral back to the financial institution. If the dispute is not resolved at this stage,
2. Negotiation/conciliation resulting in a finding. If the dispute is not resolved at this stage,
3. Consideration by the BFSO resulting in a recommendation. If the consumer rejects the decision at this stage, he or she can pursue the dispute through the courts. If the financial institution rejects the decision at this stage,
4. Further consideration by the BFSO resulting in a determination. If the consumer accepts the decision, then it is binding on the financial institution.

A practical example – investigation of Mr S's case

The investigation by the Banking and Financial Services Ombudsman showed that:

- *Mr S was the victim of a fraud which involved the opening of the new account, the depositing of part of the net proceeds of sale to the new account, and the withdrawal of the proceeds of*

sale from the new account.

- *Mr S was living in another state when the account was opened and could not have opened it.*
- *Mr S did not receive the PIN or the card for the new account, which were given, and sent, to the person who opened the new account.*

Resolution

The case manager issued a finding that concluded that Mr S had not performed the ATM withdrawals or authorised them and that the [bank] had not proved on the balance of probabilities that Mr S had contributed to the losses resulting from the unauthorised transactions by breaching the EFT Code. It was recommended that Mr S's liability be limited to \$150.

The [bank] accepted the finding and reimbursed Mr S the \$23,000 which had been withdrawn from the account.¹⁰

External dispute system evaluation

The majority of cases heard by the BFSO in the year under review concerned consumer finance (1355 cases), followed by housing finance (1087 cases) and payment system (874 cases).¹¹

Table 1 below shows a breakdown of the products and disputes over the last year.

The BFSO Scheme involves a four-step process which involves negotiation/conciliation only at the second step. In so doing, the scheme only allows for the involvement of the consumer at one stage.

The fact that an ombudsman scheme has been implemented by the financial services industry is commendable. The problem is that, when analysed, the scheme could do more to satisfy the concerns of the consumer. In a recent address¹² to the ASIC stakeholder forum, Goodman-Delahunty outlined the types of complaints received by the financial services sector. In it, she went as far as to say that the fiduciary duty once extended by banks has been replaced by *caveat emptor*¹³ (buyer beware), so that the onus is placed on the consumer when he or she enters into

Product group	Product (% within product group)	Types of disputes
Consumer finance (28.3% of all cases)	Credit cards (81.2%)	1. Unauthorised transactions 2. Maladministration in granting credit
Housing finance (22.7% of all cases)	Home loan – variable rate (69.5%)	3. Delays (loan approval or settlement) 4. Contractual breach, written instruction not carried out
	Home loan – fixed rate (14.1%)	5. Early repayment fee excessive, inappropriate or wrong 6. Delays (loan approval or settlement)
Payment system (18.2% of all cases)	ATM (48.4%)	7. Unauthorised transactions 8. Incorrect cash given
	Periodical payments, direct debits (15.3%)	9. Contractual breach, written instruction not carried out
	Cheques (12.2%)	10. Dishonoured transactions, lost funds
	Computer banking (8.8%)	11. Unauthorised transactions.

Table 1: Breakdown of products and disputes 2003-04

a contractual relationship with a financial service provider.

Goodman-Delahunty highlights the under-reporting of complaints about financial service providers. In her paper she notes that the percentage of complaints lodged to third parties may be as low as five per cent,¹⁴ with only 30 per cent¹⁵ of consumers lodging complaints with their financial service providers directly. The reports relied on were published prior to the implementation of the financial services reform requirements and there is not much scope to suggest whether the changes in the financial sector have brought about a change in consumer complaint behaviour. The reports do, however, highlight the general reticence of consumers to make complaints to financial service providers.

The most recent annual report¹⁶ from the BFSO noted that the number of complaints received by the dispute resolution scheme had dropped. For the second consecutive year there had been a decline of 15.5 per cent in new cases.¹⁷ There had also been an increase in the number of cases that were resolved prior to investigation by the BFSO (90.1% from 87.0% in 2003).¹⁸

The BFSO suggests that this is the result of improved internal dispute resolution systems.¹⁹ This is not conclusive. The reason that there is a decline in new cases received by the BFSO could be that more consumers are dissatisfied with the entire dispute resolution system put in place by the financial service providers along with the BFSO scheme itself. Another reason may be that consumers are confused and are uncertain about the avenues available to them for making a complaint.

If Goodman-Delahunty's statistics are illustrative of the present consumer sentiment, then a very small minority of all consumers actually lodge a complaint. The BFSO suggests that a decline in consumer complaints is indicative of the internal dispute resolution schemes' success. As it stands, the BFSO's suggestion that internal dispute resolution schemes are resolving more disputes now than in previous years is inconclusive. An obligation on the financial service providers to report on all complaints made internally would at least clarify this position in relation to formal complaints, if not in relation to complaints and general dissatisfaction



where the customer does not pursue any dispute resolution option.

Models for dispute system design

Since the 1980s, theorists have developed models for dispute system design. An overall analysis of a particular dispute resolution process must be tested against these various models if it is to be empirically evaluated. However, the various models differ slightly in their emphasis; they have all developed from the influential work *Getting Disputes Resolved*²⁰ by Ury, Brett and Goldberg. The authors proposed six principles for dispute system design:

1. Put the focus on interests
2. Provide 'loop-backs'
3. Provide low-cost rights and power backups
4. Build in consultation before and feedback after the dispute resolution is completed
5. Arrange the procedures in a low-to-high sequence
6. Provide the motivation, skills and resources necessary.²¹

Since then, several theorists have added to this model. In *Designing Conflict Management Systems*,²² Constantino and Merchant emphasised the fact that the nature of the design process itself could influence the success of the system.²³ While in *Dispute Resolution in the Non-Union Environment*,²⁴ Rowe places an emphasis on the need for options.²⁵ Finally, in *Controlling the Cost of Conflict*,²⁶ Slaikeu and Hasson focus on the methods used rather than a description of the design process,²⁷ adding that another option for resolving conflict can be avoidance.²⁸

The dispute resolution system put in place for the financial sector can be evaluated on the basis of these models.

Interests

Initially, the theorists suggest that the focus should be placed on 'interests'. The preference here is for interest-based resolution such as mediation at the first instance.²⁹ The guidelines set out for the internal dispute resolution process in the financial sector does not allude to a need for mediation at the first instance. As stated earlier, the reliance

on a set of standards relating to 'complaints handling' suggests that the initial contact a consumer makes with a financial service provider is not interest-based; rather it is power-based. This may be due to the fact that the financial sector is, by its very nature, more powerful than the individual consumer. Another reason may be that in providing only for complaints handling at the initial step, the financial sector may filter out superfluous complainants.

The BFSO scheme does, however, provide for mediation at the initial stage. If a dispute cannot be resolved through the IDR scheme with an individual financial institution, the ombudsman will convene a mediation or a conciliation conference, where the disputants will be brought together to discuss their differences with the aid of a case manager. At any stage during the process, the consumer or the financial institution may request a conciliation conference. The ombudsman, however, notes that not all disputes are suitable for a conference.³⁰

Loop-backs

There is a need to provide for 'loop-backs' in the dispute resolution process. A loop-back is the process by which a disputant can have the option to return to less costly means of resolving their dispute. The object of the financial sector dispute resolution process is to resolve disputes at the earliest stage. When a dispute is received by the BFSO, the ombudsman will initially refer the dispute back to the financial institution. The process does not suggest that the consumer can choose this option at will, but the broader scheme attempts to oblige a 'loop-back' stage in the resolution process. This would appear to disassociate the consumer from the dispute resolution process but once again, within such a large environment as the financial sector, an element of control by the regulatory bodies may be necessary.

Low-cost rights and power backups

A dispute resolution system should provide for low-cost rights and power backups. This means that if the interest-based processes do not resolve the dispute, an alternative to litigation

is available.³¹ The object of the dispute resolution scheme is that disputants are encouraged to resolve their disputes without resorting to litigation. The BFSO scheme in particular, attempts to inhibit the need for litigation in the later stages of its process through repeated intercession.

Consultation before and feedback after

The need for consultation and evaluation has been a statutory requirement. ASIC can evaluate and revoke a financial institution's IDR scheme if it does not meet the necessary standards and the BFSO has recently gone through a period of consultation and evaluation. Whilst consumers are not consulted individually, the recent push via consumer groups and the heightened competition between financial institutions has influenced changes in consumer complaint practice. The process of feedback through the scheme is ultimately achieved through the *Banking and Financial Services Ombudsman's Annual Report*. This report provides an overview of the numbers and types of disputes brought before the ombudsman during the year. At an individual level, at each stage of the dispute resolution process, the consumer is notified of the investigation.

Low to high sequence

The dispute resolution process is free to all consumers, the reason being that all consumers can be given the opportunity to have their dispute settled. Only if the dispute remains unresolved at the end of the process would the disputants incur legal costs.

Motivation

The motivation provided for consumers is that the IDR and EDR schemes are the only avenues available to them when they wish to lodge a complaint. Individual financial institutions are encouraged to provide information to their customers about the dispute resolution schemes available to them.

Interest-based conflict management

Constantino and Merchant stress that dispute resolution systems should be

designed *with* stakeholders, rather than *for* them.³² The concept is called 'interest-based conflict management systems design.'³³ Under such a design system, Constantino and Merchant state the importance of the stakeholders having an 'active and integral role in creating and renewing the systems they use'.³⁴ There is an acceptance of the fact that conflicts will arise and, as such, the best method of designing an effective system is to involve the stakeholders, rather than having a system imposed on them. The authors stress that the best resolution to conflicts is the one developed by the parties who have vested interests.³⁵

The financial sector dispute resolution process involves stakeholders as best it can. When designing a system that can cover the broad range of consumer disputes, the financial sector has developed a consistent approach to consumer concerns. The financial institutions, as stakeholders, have been involved in designing the system with discussion papers and feedback through regulatory bodies. Consumers, as stakeholders, have not been involved in the design process as such. The requirement for a dispute resolution scheme came through the recognition of a need for a consumer dispute system. It could be said that consumers were involved in the instigation of the scheme, but not in the design process.

The financial sector dispute resolution scheme does not adhere to 'interest based conflict management system design' concepts as the environment is too broad for such a consultative process. The scheme alludes to such concepts in that it has a regular consultative process built into its evaluation obligations. The principles of 'participation, openness and feedback'³⁶ are lacking particularly in the individual financial institutions' IDR schemes.³⁷

Multiple options

Rowe adds that a dispute resolution system must allow for options.³⁸ This, in practice, refers to the need for a fluidity of process; allowing the disputants a choice of avenues in order to resolve their dispute. She advocates a series of options for the disputants where the formality rises incrementally from informal negotiation to formal



investigative and adjudicative procedures, depending on the nature of the dispute and the will of the disputants. Unfortunately, such fluidity could not be available to disputants in the financial sector. As all consumers would hope to be treated on an equal basis and in a consistent manner, the regulatory mechanisms required to achieve this would necessarily restrict a consumer's options somewhat. Rowe does, however advocate a 'loop-forward' option in her model. A 'loop-forward' is where a disputant can opt for the dispute to be resolved in a more formal or more rights-based arena. As with all financial disputes, the consumer can at any stage during the resolution process opt for the dispute to be adjudicated in the courts. Whilst the dispute resolution scheme is available to all consumers, this does not mean that all disputes must be resolved via the dispute resolution procedures put in place by the regulatory bodies.

Preferred path

Slaikeu and Hasson advocate a 'preferred path'³⁹ towards dispute resolution. The object of this approach is to focus on the methods used, rather than a description of the dispute system design. The authors acknowledge that most procedures are 'weighted toward higher-authority resolutions, and many unknowingly encourage avoidance and power-play resolutions'.⁴⁰ It could be said that the present financial sector dispute resolution scheme does, in fact, encourage avoidance. The resolution process is, in most stages, unilateral and may lead to the conclusion that the scheme encourages power-play resolutions. This may be the case in some circumstances. However, the fact that the system leads the consumer from the individual financial institution into the independent BFSO Scheme should alleviate fears that the financial institutions could continue to intimidate consumers once the ombudsman was involved.

Evaluation of dispute resolution systems

Further, Ury, Brett and Goldberg outline four criteria to be used when

evaluating a dispute resolution system:

1. Transaction costs
2. Satisfaction with outcomes
3. Effect on the relationship
4. Recurrence of disputes.⁴¹

Transaction costs

This refers to the resources consumed in disputing.⁴² Disputes between consumers and their banks waste valuable time and money for both parties. As banking is a highly competitive industry, a bank does not want to receive a bad name among consumers.

Costs are most important for the consumer. A consumer who has a dispute with a bank is faced with enormous costs if he or she wishes to pursue the matter through the courts. If he or she wins the case, they will still be faced with large legal costs and would have expended a lot of time that could have been used in other areas.

The initiation of a dispute resolution scheme for the financial services industry must be commended. The procedure, however, could allow for more involvement with the consumer.

Satisfaction with outcomes

This depends on whether the disputants believe that the dispute system is fair and that the outcomes meet their needs.⁴³ It is difficult to evaluate the level of satisfaction consumers have with the financial sector dispute resolution scheme on a subjective basis. The best way to estimate consumer's satisfaction would be to compare the numbers of consumers using the scheme over recent years. The Banking and Financial Services Ombudsman's Annual Report 2003-04 states that there has been a decline in the number of new cases referred to the scheme.⁴⁴ The report suggests that this is because disputes are being resolved by the individual financial institutions.⁴⁵

Slaikeu and Hasson⁴⁶ suggest that avoidance is another means of dealing with disputes. This could be another reason why there has been a decline recently in the number of consumers accessing the BFSO Scheme. Consumers may have decided that it is better to avoid conflict with their financial institution and as there is a

lot of competition between the financial institutions, simply taken their business elsewhere.

Effect on the relationship

This refers to whether the outcomes of disputes affect the way the disputants relate in the future.⁴⁷ The increased awareness of consumer interests by the financial sector has had a beneficial effect on the relationship between financial institutions and their customers. It could not be said that the implementation of a dispute resolution scheme has changed the relationship. What could be said is that consumers are aware that they can access a free and independent scheme if they have a dispute with their financial institution. This then gives the consumer a sense of power when dealing with their financial institution. The fact that an independent ombudsman will hear their concerns and has remedies in place with which to 'punish' a recalcitrant financial institution puts consumers in a better position when dealing with such powerful companies. The more that consumers are aware of the outcomes of individual disputes, the better the ongoing relationship between financial institutions and their customers will become.

Recurrence of disputes

This looks at whether disputes reoccur in the future.⁴⁸ In other words, whether there is a systemic problem that should be addressed. The object of the BFSO Scheme is not only to resolve individual disputes, but also to identify and address systemic problems when they arise.⁴⁹ In doing so, the BFSO can identify problems which could potentially affect a large number of consumers over and above those who have lodged a complaint with the scheme. In the last annual report, the BFSO had conducted 19 investigations into systemic problems, with 15 of these being resolved.⁵⁰

Constantino and Merchant admit that conflict is unavoidable⁵¹ and that conflict management should be seen as a necessary part of any corporate framework. The identification of systemic problems is not of itself a panacea but an integral element of any dispute resolution system. The ability of

a system to allow for the identification and resolution of broader problems must be a fundamental goal of any dispute resolution system. Whilst the BFSO Scheme has achieved this goal, the same cannot be said for the individual financial institutions. Until the Code Compliance Monitoring Committee (CCMC) releases its first report, the state of the individual internal dispute resolution scheme's success will not be known.

Conclusion

In evaluating the financial sector dispute resolution scheme on the basis of dispute system design, it has become clear that the system is not perfect. The implementation of a Banking Ombudsman has changed the way financial institutions deal with their customers.

On a dispute systems design basis, the financial sector dispute resolution system does not allow for the bilateral and interest-based procedures that should be included at the initial stages. Having said that, an industry-wide dispute resolution system could never achieve the fluidity required by a perfect dispute resolution system. The restrictions faced by the regulatory bodies are that the dispute resolution systems must be broad enough to cover all conceivable consumer disputes brought before all financial service providers. The guidelines set out by the regulatory bodies suggest that the standards the financial institutions must achieve are only a base line or a good starting out point.

Once the CCMC releases its first Annual Report, it would be interesting to see whether some individual financial service providers are setting their IDR standards higher than the guidelines set out by ASIC. A move away from unilateral decision-making into bilateral and interest-based procedures would be a welcome sight for consumers of financial services. ●

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Endnotes

1. Banking and Financial Services



- Ombudsman *Terms of Reference*, cl 5.1(e). This is an increase from a limit of \$150,000 which took effect on 1 December 2004.
2. Banking and Financial Services Ombudsman *Guidelines to the Terms of Reference*, p 42.
 3. Above note 1, cl 7.3.
 4. Above note 1, cl 7.3.
 5. Above note 2, *Guidelines to the Terms of Reference*, p 55.
 6. Above note 1, *Terms of Reference*, cl 7.5.
 7. Above note 2, p 55.
 8. Above note 1, cl 7.6-7.8.
 9. Above note 1, cl 7.9-7.13.
 10. *Banking and Financial Services Ombudsman: Annual Report 2003-04*, p 32
 11. Banking and Financial Services Ombudsman: *Annual Report 2003-04*, p 22.
 12. Goodman-Delahunty J *Promoting Consumer Complaints in the Financial Sector* ASIC's Stakeholder Forum, *Capitalising on Complaints: insights into handling finance sector complaints*. Sydney, 14 November 2001.
 13. Above note 12, p 3.
 14. Above note 12, p 5 (referring to Liu and McClure (2001) *Journal of Consumer Marketing*, 18(1), 54-74).
 15. Above note 12, p 5 (referring to Stephens N and Gwinner K P (1998) *Academy of Marketing Science Journal*, 26 (3), 172-89).
 16. Banking and Financial Services Ombudsman *Annual Report 2003-04*, p 1.
 17. Above note 16, p 1.
 18. Above note 16, p 1.
 19. Above note 16, p 1.
 20. Ury W, Brett J, Goldberg S *Getting Disputes Resolved*, Jossey-Bass, San Francisco, 1988.
 21. Above note 20, p 41.
 22. Constantino C and Merchant C S *Designing Conflict Management Systems*, Jossey-Bass, San Francisco, 1996.
 23. Above note 22, p 121.
 24. Rowe M *Dispute Resolution in the non-Union Environment* in Gleason S (ed) *Frontiers in Dispute Resolution in Labor Relations and Human Resources*, Michigan State University Press, East Lansing, 1997.
 25. Above note 24, p 86.
 26. Slaikeu K and Hasson R *Controlling the Costs of Conflict*, Jossey-Bass, San Francisco, 1998.
 27. Above note 27, p 49.
 28. Above note 27, pp 23-24.
 29. Conbere J P 'Theory Building for Conflict Management System Design', *19 Conflict Resolution Quarterly* 215 (2001) p 217.
 30. Banking and Financial Services Ombudsman Ltd *Investigation Process*, available at <www.abio.org.au>.
 31. Above note 29, p 218.
 32. Above note 22, p 49.
 33. Above note 22, p 49.
 34. Above note 22, p 53.
 35. Above note 22, p 54.
 36. Above note 22, p 57.
 37. While researching this paper I contacted the Commonwealth Bank and Suncorp-Metway via their 'Customer relations' departments in order to access information about their IDR schemes. The Commonwealth Bank has not yet replied and Suncorp-Metway stated that 'it is not our policy to furnish this type of request for information as it is commercially sensitive' (email from the manager of the Group Customer Relations Unit, Suncorp-Metway dated 11 January 2005).
 38. Above note 24, p 86.
 39. Above note 26, p 44.
 40. Above note 26, p 44.
 41. Ury W, Brett J, Goldberg S 'Designing Systems for Resolving Disputes in Organisations: Developing and Maintaining Competitiveness' *American Psychologist* Vol 45(2), Feb 1990, p 4. available at <<http://gateway.ut.ovid.com>>.
 42. Above note 41, p 4.
 43. Above note 41, p 4.
 44. Banking and Financial Services Ombudsman: *Annual Report 2003-04*, p 1.
 45. Above note 44, p 1.
 46. Above note 26, pp 23-24.
 47. Above note 41, p 4.
 48. Above note 41, p 5.
 49. Above note 44, p 24. BFSO is obliged, under its terms of reference and as an ASIC approved alternative dispute resolution scheme, to report systemic issues to ASIC on a quarterly basis.
 50. Above note 44, p 24.
 51. Above note 22, p 49.