13 November 2007

By email: vplrc@parliament.vic.gov.au

The Executive Officer
Victorian Parliament Law Reform Committee
Parliament House
Spring Street
East Melbourne VIC 3002

Dear Sir/Madam

Alternative Dispute Resolution – Discussion Paper

Consumer Action Law Centre (**Consumer Action**) is pleased to be given the opportunity to comment on the Alternative Dispute Resolution Discussion Paper (the **Discussion Paper**) prepared by the Victorian Parliament Law Reform Committee (the **Committee**). In particular, Consumer Action has a number of suggestions to make in relation to the role of industry-based External Dispute Resolution (**EDR**) schemes in the broader context of Alternative Dispute Resolution (**ADR**).

Consumer Action is strongly engaged in the consumer dispute resolution process through making complaints to various industry-based EDR bodies on behalf of Victorian consumers. These include the Banking and Financial Services Ombudsman, the Credit Ombudsman, the Telecommunications Industry Ombudsman and the Energy and Water Ombudsman (Victoria) among others. In Consumer Action's experience, industry-based EDR schemes have been an effective method of ADR from the perspective of resolving consumer/business disputes to the satisfaction of consumers. The majority of this submission relates to the role, place and future of industry-based EDR. We also make submission regarding costs of ADR, and mandatory ADR as a pre-requisite to court action.

Below is an outline of Consumer Action's submission:

Preliminary points

The Discussion Paper covers a very broad range of processes in its review of ADR, and this generality makes it difficult to relate issues in the Discussion Paper to the consumer context. Consumer Action does not think it is appropriate or possible to treat all types of ADR processes the same. In relation to consumer-trader disputes, consumer Action does not

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think it desirable that industry-based EDR practitioners are regulated in the same way as other types of ADR.

The nature and role of industry-based EDR

Industry-based EDR schemes are an important method of ADR that is distinct from other forms of ADR in significant ways. Because of the structure and characteristics of industry-based EDR, it has been, from the perspective of consumers, very successful in resolving disputes between consumers of businesses.

Examples of successful dispute resolutions using industry-based EDR

Consumer Action has represented many consumers with their complaints to industry-based EDR schemes through our legal practice section. Looking at four case studies, the capacity for EDR to assist in achieving concrete results for consumers can be seen.

The advantages of industry-based EDR

The success of industry-based EDR schemes is due to a number of advantages it has over other dispute resolution processes. The advantages of EDR include:

i. EDR schemes are typically a condition of holding a relevant licence, so all businesses in an industry must participate in EDR,
ii. EDR is funded by industry, so industry has a financial incentive to minimise consumer disputes,
iii. EDR schemes typically have independent boards with 50% representation from consumers so the dispute resolutions processes are fair and balanced,
iv. the EDR process provides flexible solutions to disputes but also has 'teeth' because the Ombudsmen can make findings binding upon the trader,
v. EDR Ombudsmen are typically required to investigate and report on systemic problems, and
vi. EDR Ombudsmen keep detailed records and make detailed reports that assists the advancement of consumers' interests

Possible expansion of EDR

As EDR is generally successful at resolving consumer disputes, it is appropriate to consider the possible areas of commerce into which it could be expanded. Expanding EDR into areas where an individual or company requires a licence to carry on business (for example, motor traders) may be appropriate, and the Victorian Government should consider promotion of expanding the areas of commerce that are covered by EDR schemes.

Mandatory pre-action alternative dispute resolution (ADR) and user pays ADR

Consumer Action does not support the proposal to require mandatory pre-action ADR, especially in relation to consumer disputes. Consumer Action's view is that such a scheme is unlikely to lead to a more timely and cost effective resolution of consumer/trader disputes, and is likely to disadvantage consumers by placing a barrier that will cause attrition of valid claims.

Preliminary points

The scope of the Committee's inquiry into ADR is very broad and covers such disparate topics as ADR within courts and tribunals, ADR through the Victorian public service, industry-based EDR schemes, ADR provided by barristers and solicitors, and restorative justice. From Consumer Action's point of view, this breadth is unfortunate, as the sheer difference between these categories makes it unlikely that they can be usefully treated as combined for reform or regulatory purposes. Consumer Action makes submissions in relation to ADR as it affects consumers, and particular in relation to industry-based EDR schemes.

Industry-based EDR schemes are very different from the other ADR processes considered in this Discussion Paper. It is not appropriate, possible, or helpful to treat it in the same manner as other ADR.

Consumer Action believes that, unless there is a compelling reason, any recommendations the committee makes should not apply to the industry-based EDR schemes, nor the conciliators employed by the schemes. Industry-based EDR schemes are subject to regular and ongoing review under their constitutional documents and generally have consumer representation through their boards. Any further regulation of industry-based EDR schemes might impinge upon their effectiveness and impact the industry and consumer confidence that is so vital for their ongoing success.

Unlike some of the other forms of ADR covered in the Discussion Paper, industry-based EDR employ conciliators and it is the actual Ombudsman or scheme that makes any final determination. Considering this, Consumer Action does not believe industry-based EDR scheme employees should be subject to prescriptive training and/or accreditation processes. Any question about employee standards relates, in Consumer Action's view, to the effectiveness of the EDR organisation and is best dealt with at the organisational level.

The nature and role of industry-based EDR

Industry-based EDR schemes are a form of ADR. It has been noted, however, that describing industry-based EDR as ADR is 'misleading' because it incorrectly locates EDR within the mediation and conciliation industries.[1] While EDR schemes use mediation and conciliation, they have ultimate power to make a decision that is binding upon an industry member. This determinative power distinguishes industry-based EDR from other forms of ADR, and is likely an important ingredient in their success.[2] Another important distinguishing factor is that consumers are never charged for EDR.

[1] O'Shea, Paul & Rickett, Charles, *In Defence of Consumer Law: The Resolution of Consumer Disputes*, [2006] SydLRev 7.
[2] Colin Neave, Banking and Financial Services Ombudsman, Lessons from a public and private divide, Presented to the Commonwealth Ombudsman 30th Anniversary Seminar, Wednesday 8 August 2007, Canberra.

Membership in an EDR is compulsory for businesses in certain areas of commerce because it is a condition of holding a necessary licence to carry on business in that area.[3] Many areas of commerce are covered by EDR schemes, including financial services, energy and water.[4]

The role of industry-based EDR schemes is to resolve disputes between traders and consumers in their area of jurisdiction. For example, the constitution of the Energy and Water Ombudsman (Victoria) Limited (**EWOV**) states that its objects are "to receive, to investigate and to facilitate the resolution of…complaints…".[5] Industry-based EDR schemes usually make decisions 'on paper', using only written and telephone communication, and rarely involving face-to-face meetings between the two sides. This contrasts with conciliatory ADR generally, which typically involves the face-to-face meeting of the two sides.

Industry-based EDR has in common with other ADR schemes the object of resolving disputes outside a court process. However, industry-based EDR is distinct from other forms of ADR in a number of ways. EDR schemes can make findings that are binding upon trader members. For example, EWOV can make a determination or determination up to $20,000 (eg. order a scheme member to pay compensation of $20,000 to a consumer).[6] By contrast, the Banking and Financial Services Ombudsman (**the BFSO**) can make determinations of up to $280,000.[7]

Scheme members are bound by any determination an EDR scheme makes. The determinations of schemes are enforceable on trader members, because if a trader does not comply with a determination that trader can be expelled from the scheme, and membership of the scheme will be a condition of holding the relevant license.[8]

As well as resolving individual consumer disputes, EDR schemes also have a role investigating and reporting on systemic problems within their jurisdiction. For instance, the Australian Securities and Investment Commission (**ASIC**) requires all schemes providing EDR to financial services providers to identify systemic problems and report them to ASIC.[9] Thus, EDR schemes are involved in identifying and investigation systemic problems, and reporting them to the relevant regulator.

A number of sources set standards for EDR schemes. In 1997, benchmarks for industry-based EDR schemes were released by the Minister for Customs and Consumer Affairs.[10] The benchmarks require schemes satisfy principles of accessibility, independence, fairness,

[3] Eg. All holders of AFS licenses who provide services to retail clients must be members of an IEDR. *Corporations Act 2001 (Cth)*, section 912A (1) (g).
[4] Bond, Carolyn, *Elements of Industry External Dispute Resolution Schemes (EDR)*, Consumer Action Law Center, July 2007, page 4.
[5] Constitution of Energy and Water Ombudsman (Victoria) Limited, 30 May 2006, article 3, page 5.
[6] Energy and Water Ombudsman Charter, 30 May 2006, article 6.1, page 6.
[7] Banking and Financial Services Ombudsman, Terms of Reference, clause 5.1(e).
[8] O'Shea, Paul & Rickett, Charles, *In Defence of Consumer Law: The Resolution of Consumer Disputes*, [2006] SydLRev 7.
[9] ASIC Regulatory Guide 139, *Approval of external complaints resolutions schemes*, 8 July 1999, RG 139.62, page 13.
[10] Minister for Customs and Consumer Affairs, *Benchmarks for Industry Based Customer Dispute Resolution*, August 1997.

accountability, efficiency and effectiveness.[11] Under the benchmarks, industry-based EDR schemes must require their members to inform customers about the scheme,[12] determination makers must not be appointed by or responsible to scheme members,[13] and the scheme must have a mechanism for referring systemic problems to the regulator.[14] The benchmarks are supplemented by regulator specific standards, such as those contained in ASIC's Regulatory Guide 139.[15] Despite these standards, it has been the experience of Consumer Action that schemes do differ in effectiveness, and particularly in areas such as accessibility and reporting some EDR schemes are better than others.

Examples of successful dispute resolutions using EDR

Consumer Action's legal practice is regularly involved in making complaints to industry-based EDR schemes on behalf of consumers. While industry-based EDR does not always provide a satisfactory solution for consumers, it is a valuable consumer protection tool that often provides excellent outcomes for consumers. Industry-based EDR is particularly important because it can provide conciliated or arbitrated decisions at no cost to consumers. Below are examples of some of the excellent outcomes that industry-based EDR has assisted consumers represented by Consumer Action to achieve.

Case study 1

A major bank was a linked credit provider and provided credit for a consumer who used the credit to pay for education services. Shortly after the credit was extended, administrators were appointed to the education service provider. The education service provider failed to provide the consumer with the services paid for. In addition, a number of written misrepresentations had been made by the education service provider (including misrepresentations about the cost of the loan). As a linked credit provider, the bank was potentially liable for these misrepresentations.

After the consumer received assistance from the Consumer Credit Legal Service (as it then was), who referred the matter to the Banking and Financial Services Ombudsman (**BFSO**) the bank agreed to release the consumer for all liability under the loan (which amounted to approximately $10,000). The role of the BFSO as an EDR provider, and its power to make determinations binding on the bank, greatly assisted the attainment of this excellent outcome for the consumer.

Case study 2

The consumer attended a seminar held by a holiday 'timeshare' provider. At the conclusion of this seminar the consumer signed a contract to purchase 'Holiday Credits' and entered into a credit contract to fund this purchase. The consumer was not given the opportunity to read many of the required documents prior to signing the purchase and credit contracts, and

[11] Ibid, page 10.
[12] Ibid, article 1.4, page 11.
[13] Ibid, article 2.3, page 14.
[14] Ibid, article 6.4, page 22.
[15] ASIC Regulatory Guide 139, *Approval of external complaints resolutions schemes*, 8 July 1999.

disclosure was not sufficient to comply with the *Uniform Consumer Credit Code* and the *Corporations Act*.

The timeshare provider and the credit provider were linked. The consumer paid more than $2,000 as a deposit upon signing the contracts, and was required to repay a loan of more than $22,000. The timeshare arrangement gave the consumer no financial return, but allowed him to free accommodation in specific locations at specific times.

The timeshare and credit providers initially refused to release the client from the contracts. However, once the matter was brought before the Financial Industry Complaints Service Limited (**FICS**) the timeshare and credit providers agreed to release the consumer from all future obligations, which resulted in the consumer paying a total of approximately $4,500 instead of the substantial principal and interest payments that would otherwise have been payable. The fact that the matter was before FICS prevented the timeshare or credit providers from taking any court enforcement action against the consumer.

Case study 3

A mentally ill consumer entered into a mobile telephone contract. The usage costs for the phone amounted to approximately $200 per month, and the consumer was unable to pay this. The consumer was then charged large termination fees, such that a total of approximately $2,000 was claimed by the telecommunications provider. Legal representatives of the telecommunications provider threatened court action. By lodging a complaint with the Telecommunications Industry Ombudsman (the **TIO**), the telecommunications provider was prevented from taking court action until the external dispute resolution process was resolved.

Negotiations are continuing, but the complaint with the TIO has protected the consumer from potential legal costs had the telecommunications provider issued legal proceedings.

Case study 4

The consumer, who was profoundly deaf and in receipt of a disability pension, took out two loans as co-borrowee (with her parents) secured over her house. Significant portions of the loan amounts did not benefit her, but benefited her mother. The bank providing the loans was aware that the consumer was deaf but had not provided an interpreter, nor suggested the consumer seek independent legal advice. After taking the matter to the BFSO, and after some negotiation, the bank agreed to discharge the consumer's liability for one loan and reduce the consumer's liability for another loan. In the end, the consumer paid approximately $12,000, whereas the amount outstanding on the loans was slightly over $100,000. This result was very beneficial for the consumer, for she was at risk of losing her house.

The above case studies demonstrate the capacity of industry-based EDR processes to resolve disputes to the satisfaction of consumers. In the above cases, consumers have achieved concrete results that are probably equivalent (or better) than the results a favorable court outcome would give, but without the corresponding risks of losing and being liable to legal costs.

The advantages of industry-based EDR

Industry-based EDR schemes have a number of advantages for consumers when compared with ADR generally. Consumer Action takes the view that it is these advantages that makes industry-based EDR an effective dispute resolution scheme for trader/consumer disputes. A useful outline of some of the advantages of EDR is provided in a recent submission by EWOV to a UK consultation on consumer redress.[16] Among the advantages of industry-baed EDR that EWOV notes are flexibility, non-legalistic style, independent governance structures, funding that is industry derived, and binding decisions.[17] This submission expands on several of these advantages, and identifies others.

(i) Industry-based EDR membership is mandatory in certain industries

Membership of an EDR scheme is mandatory for particular industries (due to their being a condition of holding a license to carry on business in those industries). Thus in most industries where industry-based EDR applies, it applies comprehensively. Thus, regardless of which business a consumer is contracting with, the business will be subject to EDR.

Unlike voluntary codes of conduct, membership of an industry-based EDR scheme is mandatory not voluntary, and compliance by the member with the determinations of the scheme is also mandatory. Thus, for industries for which industry-based EDR schemes exist, consumers can be certain that their contracts with businesses are subject to redress, and that any determination made by an EDR scheme is binding on the trader.

(ii) Industry-based EDR is funded by industry

A common characteristic to all industry-based EDR schemes is that they are funded by industry, and there is never a charge to consumers.[18] Typically, industry members pay an annual fee, and an additional fee for each complaint about it that is lodged with the scheme. It has been noted that industry funding provides industry members with an economic incentive to resolve disputes to the satisfaction of customers internally.[19] The fee the EDR schemes charge members per complaint is a very quantifiable incentive for members to resolve consumers' disputes internally.

(iii) Independent governance structure

All EDR schemes have an independent governance structure. For all but two of the EDR schemes, their boards have equal consumer and industry representation.[20] The other two schemes, the TIO and the Energy and Water Ombudsman NSW (**the EWON**) have a Board

[16] Department for Business, Enterprise and Regulatory Reform (UK), Consumer Redress Consultation, submission by the Energy and Water Ombudsman (Victoria) Limited to *Consumer Redress Schemes in Gas, Electricity and Postal Services: A Consultation Document*, July 2007, pages 1-2.
[17] Ibid.
[18] Ibid.
[19] Ibid.
[20] Bond, Carolyn, *Elements of Industry External Dispute Resolution Schemes (EDR)*, Consumer Action Law Center, July 2007, page 2.

with mainly industry representatives, and a Council with consumer representation.[21] For instance, the TIO Board is made up primarily of directors appointed by members, while its Council is made up by equal numbers of member and consumer representatives.[22] There has been pressure the TIO and the EWON to abolish their Council and Board structure, and replace this with a single Board with equal industry and consumer representation. Consumer Action strongly supports the amendment of the structure of these two EDR schemes to bring them into line with the best practice of having equal consumer and industry representation.

The independence of EDR schemes should be contrasted with other industry schemes that do not share this level of independence. For instance, the Australian Retail Association (the **ARA**) takes consumer feedback (for instance, complaints about scanning errors under the Code of Practice for Computerised Checkout Systems in Supermarkets) but the ARA is clearly an industry representative body.

(iv) Flexible non-legalistic dispute resolution

It has been noted that industry-based EDR schemes are not judicial bodies, and as such do not need to rely on fixed rules, but are able to apply flexible standards and principles of (eg. of fairness).[23] As a non-judicial process, the EDR process averts the disadvantage consumers would otherwise suffer as a less powerful party in court litigation (eg. limited resources, limited capacity to bear costs). In other words, EDR can resolve disputes fairly irrespective of the relative power of the parties to the dispute.

Industry-based EDR schemes allow for flexible dispute resolution as a result of their structure. As non-government regulators, they are not bound to prescriptions in Acts which means it is easier for them to change to adapting marketplace conditions, they are structured to maximise results for consumers and industry, and their constitutions typically endow them with enormous flexibility in resolving disputes.[24] There is obviously a need for government regulators, but in many instances the most beneficial regulatory structure involves the EDR scheme as the main complaints resolver, with the government regulator overseeing (and providing a check) on the conduct of the EDR scheme.[25]

(v) The EDR schemes investigate and report on systemic problems

A role of all industry-based EDR schemes is to investigate systemic problems, and report substantiated systemic problems. The requirement for financial services EDR schemes to report systemic problems to ASIC (pursuant to ASIC Regulatory Guide 139) is outlined above.

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[21] Ibid.
[22] Telecommunications Industry Ombudsman Constitution, 27 April 2007, article 1.3, page 2.
[23] O'Shea, Paul & Rickett, Charles, *In Defence of Consumer Law: The Resolutiono f Consumer Disputes*, [2006] SydLRev 7.
[24] For example, the Banking and Financial Services Ombudsman's Terms of Reference allow it to resolve disputes by agreements, recommendations, determinations and "such other means as seem expedient". Terms of Reference, 1 December 2004, article 1.2, page 2.
[25] For example, the relationship of the various financial services IEDR schemes and ASIC, and the relationship of the Essential Services Commission and the Energy and Water Ombudsman (Victoria) Limited.

This contrasts with purely voluntary industry dispute resolution schemes, which have no such charter (and may, if they are industry controlled, have a strong disincentive to notify the regulator of systemic problems). Government regulators obviously have the power to investigate systemic problems themselves, but for the reasons described above, government regulators have limitations that mean that cooperation between them and EDR schemes is advisable.

(vi) The EDR schemes keep records and publish reports and other information

All industry-based EDR schemes keep records and publish information that improves the understanding of both consumers and industry as to particular issues they face. Thus, consumers and industry can determine the EDR schemes' previous approaches to particular disputes, and its views on current or emerging issues. For instance, the Insurance Ombudsman Service (the **IOS**) and FICS publish determinations and their reasons for determinations.[26] While not precedents, obviously the publishing of such material has qausi-precedential force, and provides consumers and industry an understanding of how the schemes go about achieving the goal of fairness. The BFSO, on the other hand, produces case studies, and detailed guidelines which give an indication of the sorts of determinations the BFSO is likely to make in the future.

While all schemes keep records and publish information, there are some inconsistencies between schemes in quality and usefulness of information. The Credit Ombudsman Service Limited (the **COSL**) provides a faq[27] and case studies on its website.[28] Another financial services EDR, the BFSO, provides a faq, case studies, detailed findings where a determination was made, and other publications including Bulletins that outline's the Ombudsman's attitude to particular issues.[29] Whereas the BFSO (and many other EDR schemes) has information in a number of languages, some schemes such as COSL only have information in English.

Possible expansion of EDR

From the discussion above it should be apparent that industry-based EDR schemes have largely been an effective non court forum resolving consumer/trader disputes. Consumer Action would like to see industry-based EDR expanded to other 'licensed' industries within Victoria. Two specific industries in which we believe industry-based EDR would be appropriate are motor vehicle trading and consumer credit.[30]

The Victorian Government has recently supported moves to make membership of an EDR scheme mandatory for all providers of consumer credit.[31] Consumer Action strongly supports this position. Consumer Action believes that motor trading is another industry that

[26] O'Shea, Paul & Rickett, Charles, *In Defence of Consumer Law: The Resolutiono f Consumer Disputes*, [2006] SydLRev 7.
[27] http://www.cosl.com.au/4520,01,1-0-FAQ's.php
[28] http://www.cosl.com.au/4521,01,1-0-Case+Studies.php
[29] http://www.bfso.org.au/ABIOWeb/abiowebsite.nsf
[30] COSL does provide dispute resolution services in relation to consumer credit, but it is not currently mandatory for providers of consumer credit to be members of COSL.
[31] Consumer Affairs Victoria, *Government Response to the Report of the Consumer Credit Review*, 2006, page 16.

could be subject to an industry-based EDR scheme, which could easily be achieved by making membership of an EDR scheme a condition to holding the relevant license. Considering that the purchase of a motor vehicle is typically the second biggest purchase a consumer will make,[32] it is in the interest of Victorian consumers that they have access to affordable and efficient dispute resolution should a dispute arise.

Mandatory pre-action ADR and user pays ADR

Consumer Action would not support user pays ADR so far as it requires Victorian consumers to pay for ADR services. As pointed out above, industry-based EDR is free for consumers, and any system that required consumers to pay would be retrograde, in that it would favour business that has the funds to pay for ADR and disadvantage consumers who may not have the funds to pay. Consumer Action does not make a submission regarding user-pays for ADR outside the consumer context.

One proposal in the Discussion Paper was to make attendance at ADR a condition precedent to commencing legal proceedings. Consumer Action does not support this proposal. In consumer/trader disputes it needs to be remembered that the dispute is between parties of unequal power. The trader is likely more familiar than the consumer with the relevant law, and frequently has significantly greater financial resources. When there is a power imbalance, a common legal tactic of the stronger party is to wear the other party down, so that the legal merits of a case are 'trumped' by the financial limits of the weaker party.

If ADR was a condition precedent to commencing legal action, there would be an attrition of valid consumer claims by consumers who give up because of all the 'hoops' they are forced to 'jump through'. It has been the experience of Consumer Action's legal practice section that many traders only begin serious negotiation for settlement once an application has been issued in the Victorian Civil and Administrative Tribunal (**the VCAT**). For these traders, pre-commencement ADR would simply be used as a delaying tactic.

Conclusion

Consumer Action has made a number of comments and recommendations above in relation to the discussion paper. The terms of the discussion paper are very wide, and this submission has focused on industry-based EDR, and other matters that are of particular concern to consumers.

[32] Consumer Affairs Victoria, *Issues Paper: Introducing Victorian motor vehicle lemon laws*, 2007, Introduction, page 03.

Should you have any questions about this submission, please contact Gerard Brody or Neil Ashton on 03 9670 5088.

Yours sincerely
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