The Role of Financial Dispute Resolution Schemes in Enhancing Consumer Trust and Confidence

Perspective of Canada’s Ombudsman for Banking Services and Investments (OBSI)

HKMA-SFC-OECD Asian Seminar

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Agenda

- Does Financial Dispute Resolution (FDR) Build Trust and Confidence?
- What FDR Does Well, and Does Not
- FDR Accessibility
- Complaint Issues in Canada
- Canada's OBSI
  - What we do and how we do it
  - Governance
  - Operating statistics
  - Challenges
Does FDR Build Trust and Confidence?

- Yes, but only when part of a broader and effective legal and regulatory framework.
- Bank and investment firm solvency and market stability are bigger issues/concerns in the public’s mind.
- Only an issue when a problem is encountered; then it matters a great deal.
- FDR is no substitute for good consumer-facing market conduct regulation.
Does FDR Build Trust and Confidence?

FDR is also no substitute for good internal firm-level dispute resolution

- Canada adopted a 2-tier system from the beginning in banking and investments (internal firm complaint handling, escalation to industry-level dispute resolution - OBSI)
- Vast majority of complaints appear to be resolved at the firm level
- Good internal complaint data is not obtained from the financial service providers (would be very useful for public policy development)
- Prevent inappropriate use of the term "Ombudsman" for firms' internal FDR
What FDR Does Well

- Gives elected officials a credible, impartial place to refer consumer and investor complaints about their financial service provider.

- An independent and impartial review provides “closure” even for complaints where we say “no” – usually ends the matter which benefits the participating firms.

- Provides an accessible way to address complaints that would not otherwise be resolved through the courts due to factors such as cost, time, intimidation/fear of court process.
FDR Accessibility

- Make it free, informal, and non-legalistic; adopt a fairness standard; employ well-trained consumer-facing staff
- No impact on legal rights of the consumer or firm
- Stops the limitation period clock
- Language - OBSI conducts investigations in English and French; inquiries handled in over 170 languages – contracted service
- Audited processes to be senior-friendly; TTY access for the deaf; website readability for the blind
FDR Accessibility

How to make the public aware of their ability to access FDR?

- Difficult to make FDR well-known, but very important to be able to find it when a problem arises
- Low unaided public awareness (<2%); CAD 1,000,000 per 1% increase
- Very reliant upon firm disclosure and referrals backed by rules
Other Benefits to Society from FDR

- Lower cost process for all parties (consumers/investors and financial services providers)

- Diverts many consumer/investor complaints away from the already overburdened court system – likely averts class actions

- Learnings from complaint cases provide valuable feedback that helps financial service providers to improve
Individual complaints can identify systemic problems that firms and regulators may not be aware of.

Issues highlighted in complaints are valuable for public policy development by regulators and legislators.

Enables the state to deal effectively with regulatory priorities without mixing in compensation.

Allows a different standard to be applied for compensation (fairness).
What FDR Does Not Do Well, Nor Should It

- Ineffective tool against financial sector corruption
- Does not address concerns over the pricing of financial products and services
- Does not deal with concerns about access to credit
- Does not deal with regulatory breaches; different issues and different standards ("fairness" versus "legality")
- Punishment of individuals or firms
Banking Complaint Issues in Canada

- One-third of OBSI’s banking complaints involve debit and credit card fraud (banking complaints up 100% 2008-2010)
- Mortgage pre-payment penalties
- Payment scams
- Collection activity
- Privacy and service issues
Investment Complaint Issues in Canada

- Two-thirds of OBSI’s investment complaints involve unsuitable investments (investment complaints up 200% 2008-2010)
- Duty of care to provide suitable investment advice and recommendations
- “Know your client” requirements are the foundation
- Disconnect between client’s situation, know your client process, and the investments recommended will likely lead to a conclusion of unsuitable investments and a recommendation for compensation
- How to value the losses has been a very large issue (opportunity costs, benchmark performance, risk rating of individual investments)
Investment Complaint Issues (cont’d)

- Outside business activities ("off-book" investments)
- Unauthorized transactions
- Account churning
- Transaction errors
- Account fee disputes (especially deferred service charges on mutual funds)
- Likely taking on the exempt-market complaints starting late 2013
Who We Are at OBSI

- An independent national dispute resolution service established as a not-for-profit corporation (an NGO)
- An alternative to the legal system for banking services and investment firms’ customers with an unresolved complaint
- Started in 1996 covering major chartered banks; in 2002 became the Ombudsman for Banking Services and Investments when the mandate expanded to all members of the:
  - Investment fund companies (mutual funds)
  - Investment dealers (brokerages)
  - Mutual fund dealers
Currently have over 600 participating firms in OBSI

Banks, federally-regulated trust companies, investment dealers, mutual fund dealers, mutual fund companies, and scholarship plan dealers

Some credit unions have joined, under consideration by others

Accessible by toll-free phone and fax; bilingual investigation services (English and French), customer inquiries can be handled in over 170 languages
What We Do at OBSI

- Informal, confidential and independent review of complaints not resolved to the satisfaction of consumer

- We look primarily at cases of direct financial loss as a result of error, misleading information or bad advice

- Review industry standards, firm policies, regulations, laws... and decide what would be “fair under the circumstances”

- Goal is to make the client “whole” where maladministration is found to have occurred
What We Do at OBSI (cont’d)

- We make recommendations to the firm; not binding on either party

- Clients do not forfeit their legal rights; may reject our findings and start legal proceedings

- “The Olive Branch” - Gives participating firms an impartial service to which they can refer their unresolved complaints

- “The Stick” - We will make public any participating firm’s refusal of a recommendation, has only happened once since OBSI’s creation in 1996 – That has recently changed, 4 in the last 5 weeks
How We Work at OBSI

Member firms must:

- Have an internal complaint-handling system
- Inform their clients about their internal complaint handling system
- Inform their clients about OBSI and refer after completion or after 90 days
- Co-operate in OBSI investigations; and
- Pay their share of OBSI’s operating costs
Firm has the first responsibility to resolve a complaint

OBSI is an informal service, not bound by judicial rules

We are not a regulator; we do not fine or punish firms

Usually investigate; sometimes mediate

Objective is to determine "Fairness in the circumstances" and recommend compensation
Investigative Process at OBSI

- Review escalated file for mandate and timeliness
- Assess file based on final response letter from firm and any other material provided by the client
- If an investigation is warranted, client and firm sign a letter agreement with provisions for privacy release, confidentiality, and no subsequent use
- Firm sends us their complete client/investigation file
Investigative Process at OBSI (cont’d)

- Investigations based on interviews and document review
- Compensation recommendations will take into account actual costs or losses, mitigation issues and accrued interest
- Some non-financial recommendations are also considered (e.g., corrections to negative credit bureau reports)
- Sometimes recommend limited compensation for inconvenience
- Discuss findings with both parties, and finish with a comprehensive report outlining OBSI’s reasons.
Controversial power introduced by senior regulators in 2008; in force starting 2010

Strongly opposed by industry and some regulators who saw it as a matter of regulatory jurisdiction

Conducted 10 “systemic investigations” in 2010-11, 3 resulted in recommendations; refused by firm – reported to regulator

Voluntarily withdrawn by OBSI Board in June of 2012 under pressure from industry and regulators; reintroduced by federal government in recent regulations as a whistleblower requirement (no investigation)
Governance of OBSI

- Independent Board of Directors
- Chair of the Board is a non-industry (community) Director
- Community Directors must not be associated with either industry or government for two years prior
- Community Directors are the majority of the Board (7 of 10) and a majority of them are required to approve OBSI’s budget and control hiring and firing of Ombudsman
- Directors not involved in investigations, decisions or appeals
Canada Has a Unique Legal and Regulatory Environment for Financial Services

Less developed legal framework for consumer protection in financial services:

- No legal duty of care imposed on banks by Canadian law, different situation for investment issues
- Bankers not fiduciaries, no fiduciary duty for “pure” banking transactions
- Special duty may apply where financial advice is given, but not in normal “lending” or transactional situations
- So where can an Ombudsman look to determine what is fair under the circumstances?
Canada’s Unique Environment for a Financial Sector Ombudsman

Canada’s federal-provincial sharing of powers that apply to our work:

- Banking is federal; trust companies can be federal or provincial
- Credit unions are provincial, but that system is currently evolving
- Non-bank consumer credit is provincial
- Securities regulation (investment leverage loans) is provincial (for now)
- Consumer protection issues are predominantly provincial
- Criminal Code provision restricting interest rates to 60% is federal
Current Challenges

Unstable Environment

- Competition in banking dispute resolution and banks seeking cost and scope reductions
- Uneven regulator support across sectors and jurisdictions
- Under-resourced for complaint volumes post-global financial crisis
- Lack of regulatory clarity re expectations and systemic (mass) cases
- Need to expand mandate of investment sector dispute resolution coverage to smaller firms operating in more difficult areas
Further Information

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