afca
Australian Financial Complaints Authority

# Systemic issues insights report

## Quarters 1 and 2 Financial year 2022–23

Edition 2

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# About this report

Regulatory Guide 267 *Oversight of the Australian Financial Complaints Authority* requires AFCA to identify, refer and report systemic issues arising from complaints to the regulators. AFCA must also report any serious contraventions of the law and other reportable matters listed in section 1052E of the *Corporations Act 2001* (Cth).

AFCA's work in this area, and the reports we make to relevant regulators, helps them to take regulatory action as appropriate.

In this report, AFCA shares recent case studies, findings and key insights from a range of systemic issues cases across the financial services industry.

# Summary of outcomes delivered

Identified and investigated systemic issues resulting in remediation to **186,924** consumers

Conducted **106** detailed systemic issues investigations

Resolved **39** systemic issues (including those identified in prior years) with financial firms

**$38,882,124.58** in refunds were made to consumers

Facilitated financial firms to provide other outcomes for consumers such as:

- Reinstatement of incorrectly lapsed life insurance policies
- Paying out claims made under credit card travel insurance policies
- Corrections to default listings made on consumer's credit files
- Corrections to erroneous credit scores for consumers
- Removal of incorrect default listings on consumer credit reports
- Corrections to the Consumer Price Index (CPI) increase applied to life insurance premiums policyholders
- Refinancing of loans incorrectly categorised from business loans to retail home loans
- Refunding of incorrectly processed payments to consumer.

# Reporting to regulators

**83** matters reported in the first half of financial year 22–23

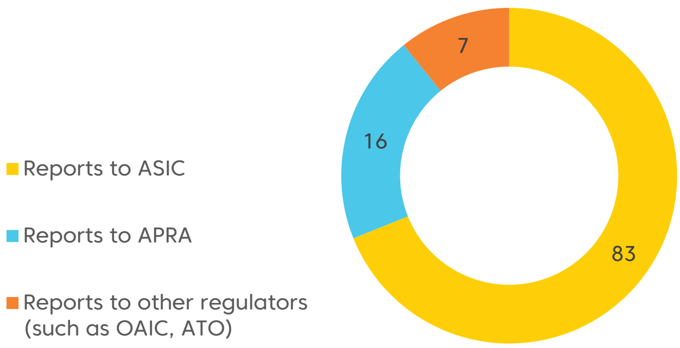
**50** systemic issues reported

**33** other matters reported (referrable under section 1052E of the *Corporations Act 2001* (Cth)) including:

- **7** serious contraventions of the law
- **22** refusals or failures by parties to give effect to an AFCA determination, and
- **4** settlements that may require investigation.

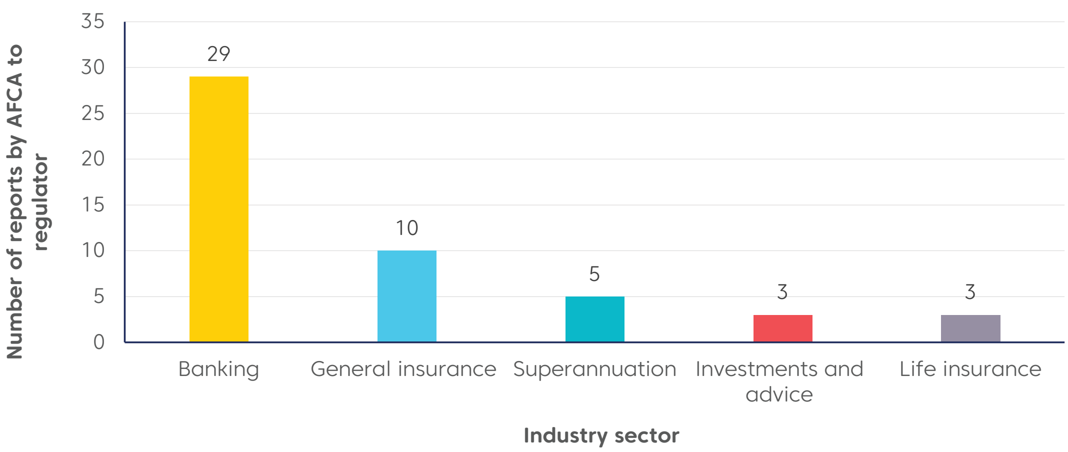
### Total reports to regulators across the financial year

Refers to total reports made in the first half of the financial year including systemic issues and other matters reported, with some reports provided to more than one regulator.




### Systemic issues across industry sectors

Refers to number of systemic issues identified and confirmed across industry sectors.



# Best-practice responses to address systemic issues

We observe that firms that take accountability for systemic issues and make changes to their culture and ways of working (alongside implementing fixes for immediate issues) not only solve specific systemic issues quickly, but also protect against issues in the long term.

## Best-practice response to a systemic issue relating to scams

Scams are becoming increasingly sophisticated and can cause customers significant harm. Where there are warnings provided by the Australian Transaction Reports and Analysis Centre (AUSTRAC), financial firms should take immediate action. Where firms have dedicated processes to manage scams, risk-based systems and teams dedicated to scam prevention and awareness, customer protections are greatly improved.

In this case study, a financial firm worked quickly to resolve a systemic issue once AFCA had identified it and took a proactive and collaborative approach to making changes and resolving the issue. Some key cultural and behavioural traits the firm demonstrated included:

- taking responsibility and accountability for the issue
- actioning a range of holistic solutions to the problem rather than implementing quick fixes or one-off changes, and
- setting up for sustainable and long-term improvement in systems, processes and complaints handling, by establishing a dedicated team and education program.

### Case study

### Sustainable solutions to resolving a systemic issue

In this case, the financial firm had received AUSTRAC scam warning notices (which are issued to financial firms on behalf of the Australian Securities and Investments Commission or ASIC) which seek to prevent transfers being made by Australian consumers to the entities listed in the notices. Each notice recommends that the firm establish a process to act on the warning and detect and block any future fund transfer requests to the entity listed in the notice. The financial firm did not establish such a process and had no measures in place to prevent consumers from transacting with entities that appeared in the scam warning notices.

In a complaint brought to AFCA, the complainant had transacted 31 times with a scam entity. The financial firm acknowledged it had received a scam warning notice about this entity but did not have processes in place to prevent its customer transferring funds to the scam entity. It had to remediate the customer more than $400,000.

The financial firm worked collaboratively with AFCA once we identified the issue and initiated our investigation. A series of measures to prevent the issue recurring were then implemented. The firm established a robust process, which included swiftly reviewing and actioning AUSTRAC scam warning notices and uploading them into a risk-based software program, designed to improve security of real time payment processing for customers. The financial firm also developed an internal team dedicated to increasing awareness of, and education about, scams for its customers.

# Common systemic issues across industry sectors

Below are some case studies involving systemic issues across different areas of the financial services industry. They impacted groups of consumers who had not lodged a complaint with AFCA.

Some systemic issues impacted large numbers of consumers while others impacted a small group. No matter the size of impacted consumers, financial firms worked to ensure that consumers were remediated fairly and appropriately.

## Banking and finance

### Transaction processing errors

#### Duplicated visa debit fees and charges

A financial firm had a system outage that resulted in visa debit card transactions being duplicated and unwarranted charges and fees being incurred. There were two separate incidents.

Incident one was caused by a program coding error which was introduced via a scheduled system release. The error resulted in pending visa debit transactions being incorrectly deleted in overnight batch runs, when one of the pending transactions became authorised. This meant customer account balances didn't reflect correct information. This incident saw some customers granted access to funds they shouldn't have had access to, resulting in overdrawn accounts. The firm detected the incident and rectified the issue.

Incident two was generated by the system fix of incident one. An additional system parameter change was applied in error, resulting in 1.2 million visa debit card transactions becoming duplicated. These duplications were later reflected in accounts. The impact of incident two was that another customer cohort had duplicate visa debit payments posted on their account and balances reduced. Some customers were impacted by both incidents one and two. The firm had not identified these impacts during testing, before installing the system fix to rectify the first incident.

These incidents and the overall systemic issue impacted 954,974 accounts. The financial firm paid a total of $1,859,676.67 to customers, which included remediation and goodwill payments.

### Take note

We frequently see a lack of adequate testing before installing system fixes. This can lead to ongoing and compounding issues.

#### Failure to recognise loan terms for customers experiencing financial hardship

A financial firm was incorrectly direct debiting the whole of an outstanding balance on the expiry of loan terms. The system did not recognise prior payment deferrals on loans and failed to adjust repayments to allow for extended loan terms, arrears capitalisation and/or payment moratoria. The system error impacted customers who had accessed hardship moratoria and restructures prior to COVID-19 and during the pandemic.

The firm acted quickly to implement a system solution to prevent the issue recurring. The financial firm also commenced a remediation and correction program, first correcting repayments and terms on loans impacted by Covid deferrals. The remediation program is ongoing.

The firm did not initially self-report this matter to ASIC but is reconsidering.

#### Business sale impacts customers' international fund transfers

Following the sale of a business unit (consumer banking accounts) from one financial firm to another firm, changes were made to the way international funds transfers would be made. In particular, the Identifier Code used by participants of the SWIFT payments system was changed. This resulted in hundreds of international funds transfers being rejected or failing to process. The financial firm did not have sufficient controls in place to mitigate the foreseeable risk of banks failing to use the new payment details.

The financial firm contacted banks and impacted customers to explain that payments were being returned due to incorrect payment details being used. It also advised the steps to take to ensure deposits were successfully made. The systemic issue impacted at least 348 customers. The total dollar value of remediation is unknown.

## Take note

When businesses are sold and customers are transferred to a new company, new owners should conduct adequate testing and ongoing monitoring of all end-to-end systems and processes to ensure customers aren't impacted.

### Privacy and credit reporting

#### Incorrect reporting of repayment history impacts customers experiencing financial hardship

A financial firm was incorrectly reporting repayment history information on customers' credit files during active hardship arrangements. The systemic issue had several causes, including a process gap, a data logic error in the firm's comprehensive credit reporting and a hardship exit-date issue impacting all COVID hardship deferrals.

While the total number of impacted customers has not yet been confirmed, we are aware that at least 314 home loan customers who were granted COVID hardship deferrals on their accounts were affected, as well as approximately 16 accounts per month that were under a hardship arrangement.

The financial firm resolved the systemic issue through various means, including updating processes, implementing a new automatic suppression of repayment history information where hardship exists and applying interim system fixes. The financial firm also plans to complete a strategic system fix.

## Take note

Customers facing financial hardship are more vulnerable when issues arise. Dedicated focus, prioritisation and care in monitoring vulnerable customers helps to ensure they are protected from errors and systemic issues.

### Coding change creates credit report errors

A credit reporting body was displaying errors and incorrect factors on customer credit reports. The error occurred because the firm had made coding changes to implement the introduction of Buy Now Pay Later account types. The coding change meant that incorrect assessments (credit scores) were loaded when customers accessed their consumer credit scorecard. The financial firm confirmed that it had undertaken post deployment testing of the coding changes however this had revealed no errors. There were 90,700 customers impacted by the issue and the financial firm received 240 complaints.

Upon becoming aware of the issue, the financial firm undertook detailed analysis and within a month had successfully deployed correction logic to resolve the issue. It also conducted a full review of each customer's credit file and undertook remedial steps directly with customers which included apologising, amending or deleting incorrect reports and ensuring lending decisions relating to business-to-business (B2B) customers weren't based on incorrect reports and were made soundly.

## Take note

When introducing new features and changes through coding and other upgrades, customer processes and experiences need to be closely tested and monitored end-to-end following implementation for potential impacts to customers.

### Delays in correcting credit reporting errors

A financial firm was delayed in handling complaints from customers about credit reporting information. In particular, the firm was late to action correction requests from customers relating to their credit files. The delay was caused by a breakdown in communication between the firm and the credit reporting body, as a process for communicating rejected corrections requests from the credit reporting body to the financial firm had lapsed. Despite receiving several customer complaints, the financial firm failed to identify that the process had broken down. AFCA formed the view that the financial firm should have identified this breakdown far earlier than it had. At least 832 customers were impacted by delays.

While the financial firm implemented a new process relating to rejected correction requests, AFCA viewed this control as ineffective. AFCA received further complaints about ongoing delays following the control being implemented.

Given the breakdown related to the contractual arrangement between the financial firm and a credit reporting body, AFCA reported the matter to the appropriate regulators and ceased its investigation. It is not AFCA's role to monitor agreements between credit providers and credit reporting bodies. We did nonetheless recommend that the financial firm consult with the Australian Retail Credit Association (ARCA) on this issue, together with the credit reporting body, to find a workable solution.

## Take note

Having manual workarounds and processes leaves financial firms open to issues if there is human error or failure to follow manual steps in a process. When systems between two companies connect as part of a customer journey or process, robust controls are integral to ensuring mutual accountability and responsibility for customer service and care.

## Credit

### Incorrect provision of business loans

A financial firm was incorrectly providing business loans to customers where they should have received consumer protections. Examples where this occurred included loans for the purchase of residential investment properties or loans for the improvement of a home. The unsuitable loans resulted in customers being charged more interest and fees than if they were given consumer loans.

When AFCA identified the issue through an EDR complaint, the financial firm had already identified the systemic issue, self-reported the matter to ASIC and established a remediation program to compensate impacted consumers. The remediation program returned more than $7.84 million to 402 customers.

Given the steps the financial firm had already taken, and as it was continuing to engage with ASIC on the matter, AFCA ceased its investigation to ensure there was no overlap in action taken by ASIC and AFCA.

### Inadequate controls in mobile banking

A financial firm had inadequate controls in place to ensure its mobile bankers provided accurate financial information during loan applications.

When AFCA raised the possible issue with the financial firm, it reviewed several lending files relating to a particular mobile banker and identified inconsistencies in customers' financial information across numerous files. There were signs of potential suspicious activity by the mobile banker. For example, there was evidence that the mobile banker had failed to identify falsified pay slips submitted by a customer for a loan application.

To resolve the issue and prevent its recurrence, the financial firm implemented controls to flag potential misconduct in a timely manner. In particular, the financial firm implemented a data model to monitor the conduct of its mobile bankers based on statistical differences in lending behaviour and patterns. The financial firm believes this data insights model will aid in flagging potential broker misconduct in a timely manner, so that the firm can investigate as appropriate.

The financial firm put in place a remediation program, working with potentially impacted consumers, to identify any financial detriment incurred.

## Take note

We have seen that problems can occur when financial firms have insufficient controls or processes in place to monitor the conduct of authorised representatives or employees. In some cases, for example, the authorised representative may act outside the scope of authority without the licensee being aware of the conduct, causing potential loss to customers.

Using a data model to measure statistical patterns against risk parameters may help to enhance the monitoring of employees and authorised representatives.

# General insurance

## AFCA Engagement

### Failing to implement AFCA determinations

A financial firm failed to give effect to AFCA determinations. This was caused by a new staff member failing to appropriately follow processes for implementing determinations. This impacted several AFCA determinations, although low in number.

It is a serious issue where a financial firm fails to give effect to an AFCA determination, for example by failing to take action or make payment within the timeframe outlined by an AFCA decision maker. It is a condition of AFCA's membership and AFSL licensing requirements that a financial firm will give effect to AFCA determinations if they have been accepted by a complainant. AFCA has a legislative obligation to report to appropriate regulators, including ASIC, where we identify that a financial firm has refused or failed to give effect to an AFCA determination.

The financial firm advised that feedback and coaching had been provided to the staff member and it had recently introduced a critical issue monitoring process whereby the leadership team monitor complaints with critical activities such as AFCA determinations.

### Administrative oversights cause two reportable matters

Another financial firm failed to give effect to two AFCA determinations in separate cases. AFCA raised the failures with the financial firm and let them know they were matters which had to be reported to ASIC.

The insurer said that in the first case, the determination was not implemented due to an 'administrative oversight' by a team member which it considered an isolated incident. In the second case, the insurer said it substantially complied with the determination except for completing one action required by the determination. Again, this was due to an 'administrative oversight'.

The insurer said the team member in the first case undertook remedial training and its investigations revealed that no other customers were affected. The insurer believed the two cases were isolated instances. AFCA determined that the matter was a systemic issue because the firm appeared to have inadequate controls and processes for implementing AFCA determinations and this had impacted more than one consumer. As a result, the insurer conducted a review of its dispute resolution processes and identified opportunities where they could be strengthened. The insurer engaged well with AFCA during the investigation.

### Take note

Administrative oversights or one-off human errors can indicate that a firm does not have effective controls and adequate processes in place. Good governance and ensuring team members are clear on processes is key to avoiding issues that may impact a broader group of customers.

### Policy interpretation and claim denial

#### Ineffective project governance and change management

A financial firm failed to comply with its own policy definition of 'market value' when settling total loss motor vehicle claims for vehicles insured for market value. Staff were not including relevant stamp duty and transfer fees to purchase a replacement vehicle in their assessments of the settlement sum.

The financial firm said that it had made a business decision some years ago to change the definition of 'market value' to include the reasonable costs associated with the replacement of the vehicle and the Product Disclosure Statement (PDS) was updated to reflect this. Despite the PDS being updated, ineffective project governance and change management meant that the change failed to be properly implemented into work practices. The financial firm did not become aware of this until AFCA's systemic issues investigation raised the issue. The financial firm is working to identify the number of affected customers. Remediation is expected to cost over $6.6 million.

## Take note

When making changes to policies, as well as other key documents and procedures, firms must take appropriate steps to implement and embed changes holistically to ensure successful implementation and ongoing compliance.

#### Unclear policy definitions

A financial firm was incorrectly handling claims made under a pet insurance policy. The financial firm was reading various definitions together under the policy to give a restrictive interpretation to how it dealt with claims relating to pre-existing conditions. AFCA found that the insurer's interpretation of the policy wording was unclear and most people would not be able to easily understand the way the various policy definitions interacted with each other. The policy was unclear about the cover provided and when claims would be excluded.

The financial firm acknowledged AFCA's view and accepted AFCA's interpretation of how the policy should be read and applied to claims. The financial firm agreed to undertake a review of historical claims and re-assess affected claims.

## Life insurance

**Calculation of premium and premium overcollection**

A financial firm was incorrectly applying a Consumer Price Index (CPI) increase to the sum insured resulting in a higher premium for policyholders. The issue arose due to a manual process used to update the CPI rate in the financial firm's policy administration system. Subsequent updates in the policy administration system for quarterly CPI rates did not occur, which resulted in the incorrect calculation of the indexation rate.

The financial firm self-reported the issue to the regulator and implemented a remediation program to compensate 3,582 impacted consumers. $175,170.49 in premiums was subsequently refunded by the financial firm and a new process to avoid the issue recurring was implemented. Controls included a quarterly review of policy anniversary letters, incorporating a review of the CPI rate utilised in its policy administration system and a validation of premiums on the letters.

## Investments and advice

**Breach of Corporations Act 2001**

**Incorrectly assessing client suitability to trade**

A financial firm was failing to assess a client's suitability to trade in contracts for difference (CFD) on its platform, which is a high-risk investment product. The financial firm didn't have processes and practices in place to ensure only eligible clients with skill and knowledge of CFDs could open an account and trade. AFCA's review identified several complaints where clients were unskilled at trading in CFDs and had suffered financial losses as a result.

Throughout our investigation, the financial firm provided unclear and inaccurate information about its policies and practices. Given the firm's poor engagement and cooperation with AFCA, along with our concern that the firm hadn't met its regulatory obligations for an extended period, AFCA formed the view that we would not be able to reach a resolution. For these reasons, AFCA referred the matter to ASIC to take steps as appropriate.

### Take note

Firms are required by law to properly classify customers as retail or wholesale. The law provides greater protections to retail clients and requires firms to prevent unsophisticated investors from being able to trade in high-risk products.

When a firm has immature or inadequate processes in place to assess a client's risk profile and suitability to trade, losses can occur for consumers.

### Misleading information, poor controls and incorrect categorisation of clients

A financial firm was engaging in discretionary and unauthorised trading, providing incorrect and misleading financial information to clients and incorrectly categorising clients as wholesale. The issues occurred over several years, indicating poor controls by the financial firm. The financial firm appeared to have inadequate training and supervision of its authorised representatives. AFCA also formed the view that the method used by the financial firm to categorise clients as wholesale did not correspond to legislation.

Throughout AFCA's investigation, the financial firm's responses did not give confidence that sufficient controls or steps had been taken to prevent the reoccurrence of these issues. The firm also held a difference of opinion over the correct categorisation of wholesale clients.

Given the financial firm's poor engagement and lack of cooperation on key issues in the investigation, AFCA formed the view that it would not be able to reach a resolution. AFCA referred the matter to ASIC for it to take action as appropriate.

# Superannuation

## Insurance attached to superannuation funds

### Failure to provide relevant client records and documentation

A financial firm was unable to satisfy AFCA that it had complied with legislative obligations to provide MySuper fund members with permanent incapacity and death insurance benefits. Superannuation law requires firms to provide these insurance benefits unless the fund member 'opts out'. The financial firm did not provide MySuper insurance benefits to certain fund members and was unable to provide AFCA with records showing that the members had opted out. Without these records, AFCA was unable to validate that all members without insurance benefits had opted out of cover or that the fund had appropriately excluded members from these insurance benefits.

Throughout the investigation, the financial firm engaged with AFCA on the issue but was unable to readily access and declined to provide relevant records, saying that to locate and access them would come at significant cost, and require extensive time and resources. This raised further concern about the financial firm's record keeping.

Given the potential scope of the issue under investigation and the lack of available records, we referred the systemic issue to ASIC and APRA to take action as appropriate.

## Take note

Keeping accurate client records and providing for efficient access to client records are an integral aspect of customer care that's expected of every financial firm.

### Inappropriately allowing default insurance to lapse

A financial firm was inappropriately allowing members' default insurance to lapse. The firm didn't tell members that they could retain default insurance cover by either increasing their account balance to at least $6,000 or completing and returning a form electing to continue the insurance cover. This was in breach of its obligation to provide an opt-in opportunity to members before cancelling default insurance cover.

The issue arose from compliance concerns over the treatment of partially subsidised plans and was limited to members of a corporate plan which provided partially subsidised cover. The financial firm conducted a review and found only a small number of members had been impacted. The financial firm remedied this by developing processes and procedures to prevent the reoccurrence of the issue.

## Any questions?

AFCA is available to help answer questions and discuss our approach to systemic issues. For more information on systemic issues or for any questions, you can contact us at **systemicissues@afca.org.au**