

Smith, Ruth

From: nwhite@creditlink.com.au

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To: rsmith@treasury.gov.au

Subject: Submission on compensation for loss in the financial services sector

Miss Ruth Smith

Financial System Division

The Treasury

Parkes

ACT

Submission on compensation for loss in the financial services sector.

At the outset it is important to note that this submission is made in respect of credit unions and their deposit taking services only. It is also submitted that deposit takers sit in a unique position in relation to the provision of financial services and the risk of loss to consumers.

The intense prudential supervision of authorised deposit taking institutions (ADI's) under the Australian Prudential Regulation Authority (APRA), which imposes the strictest array of prudential standards, is one of the reasons for deposit takers being in a unique position, in this context.

It is submitted that no other potential financial service licensees are in the same category, due to the high level of capital reserves, which are required to be held.

When compared to many other types of financial services, the circumstances where a consumer may suffer a loss as a result of depositing funds with a credit union, bank, or building society are extremely remote.

The envisaged circumstances in which loss can result are as follows:

1. Misappropriation of a deposit (cash or cheque).
2. Misappropriation of funds from a depositor's account.
3. Failure of an ATM to deliver cash, when the ATM records maintain that the cash was dispensed.
4. Collapse of an ADI and insufficient assets to cover all deposits.

Note: Under the Banking Act, depositors have a statutory first priority over all other creditors.

The processing and receipting procedures for deposits of all ADI's make it virtually impossible for staff to steal deposit funds. If such funds were stolen, the theft would in all probability be from the ADI, not the depositor, assuming that a receipt was issued.

Misappropriation of funds from a depositor's account, while initially representing a loss to a depositor is clearly a case where the ADI, as custodian, is liable to make good of the funds.

The failure of an ATM to deliver cash, as is alleged from time to time by depositors is a complex matter, due to the allegation being at odds with the ATM record and cash reconciliation. These issues are considered to fall outside the scope of a normal loss for a depositor, due to the difficulty in establishing that an actual loss has occurred.

The collapse and liquidation of an ADI is the most likely scenario where losses could be incurred by consumers. The loss would have to be materialised and assumes, even with the statutory depositor priority, the assets are insufficient to repay depositors in full.

Professional indemnity insurance and other insurance covers are comprehensively held by Credit unions in Australia. We would be pleased to provide details of the type and extent of such insurance coverage, should you require it. Due to the existence of these present insurance arrangements, no other similar demands should be required or considered for credit unions.

As most OECD countries have some form of deposit insurance scheme, it seems that this concept is the most appropriate to be considered in the context of this review.

Therefore, given the high level of reserves, which ADI's are required to hold, it is generally only in the most extraordinary circumstances of the financial collapse of an ADI that the probability really arises for consumers to suffer an actual loss with an ADI.

APRA has already indicated that it is addressing the matter of deposit insurance for Australian ADI's, given that Australia is one of the very few OECD countries not to have such a scheme. In addition to the level of reserves held, a depositor scheme is perhaps the most significant step that could be taken towards achieving a capacity to provide compensation for loss in the financial services sector involving an ADI.

This association has supported this concept since the announcement of the Wallis inquiry into the Australian financial system and still holds that view.

It is therefore submitted that the issue of providing compensation for loss in the financial services sector is a very simple and straightforward one when it comes to ADI's. On a broader front the matter of deposit insurance, which it is envisaged can not be implemented as a result of this review would potentially provide the ultimate compensation scheme in respect of ADI's.

It is envisaged that this review may well provide additional impetus to the matter of deposit insurance for ADI's and bring the matter to the attention of the government.

Yours sincerely,

P Elliott
CEO, NCUA Inc
PO Box 21, Indooroopilly Qld 4068

per
Nicole White
Personal Assistant to CEO

National Credit Union Association Inc.
PH: 07 38703877

FAX: 07 38703343
EMAIL: nwhite@creditlink.com.au