

Comments by Ombudsman for Banking Services on Competition Commission Report: The National Payment System and Competition in the Banking Sector 2006

INTRODUCTION

The Ombudsman for Banking Services (OBS) will confine its comments on the report to the issues of bank charges and the OBS's possible role in dealing with complaints or the regulation thereof.

BANK CHARGES

At page 29 of the report it is concluded, 'from a scanning of the press', that consumers feel that they are being overcharged [by the banks]. Before any intervention is considered, this assumption should be tested.

The OBS is well placed to provide information in this regard. A 2004 survey by Markinor of "big four bank" customers who had complaints revealed that 29% of those questioned had complained about pricing, charges and fees (see figure i) below). This category was the third largest cause of complaints.

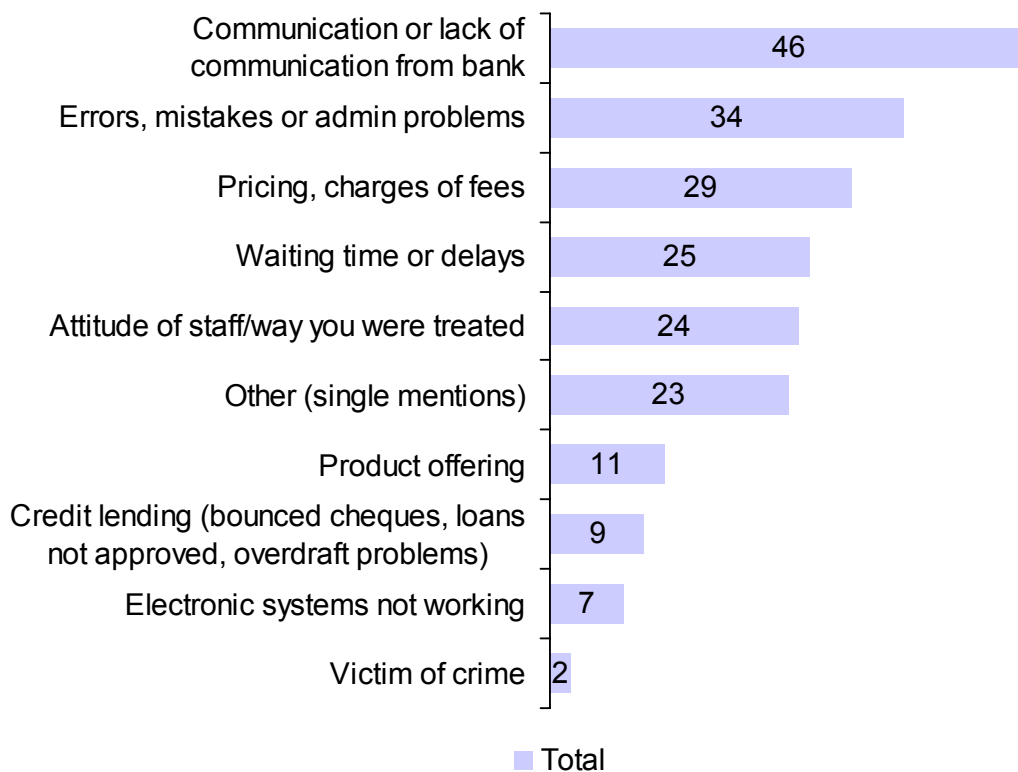


Figure i: Markinor Survey 2004: Pricing

A further finding of the survey (which was commissioned by the OBS) was that, when asked about pricing, most believed their banks were expensive.

Thinking about your Bank's fees.....	%
Low	7
Moderate	35
High	48
Don't know/ Refused	9

Table I: Markinor Survey 2004: Pricing

Also, as regards overall quality and value for money, twice as many complainers said they believed they had received negative value as those who said they believed they had received positive value. These results were published on the OBS website, www.obssa.co.za.

	EXCELLENT	VERY GOOD	GOOD	FAIR/POOR
OVERALL QUALITY	15	22	32	31
VALUE FOR MONEY	7	15	36	42

Table II: Markinor Survey 2004: Overall Quality and Value for Money

Although the OBS's mandate precludes it from considering general complaints regarding pricing and charges (for reasons that will be explained more fully later), many of the complaints that reach it are about bank fees, charges and penalty charges. The details of such matters are generally not captured on the system, so it is not possible to say what percentage they constitute of all the complaints received. However, a tally was kept of all pricing related complaints received between 12 May 2006 and 19 May 2006.

During that period, 20 pricing related complaints were received, out of a total of 825 (2.4% of complaints). Of the 20, the OBS was able to deal with 13.

A further source of such comments is a marketing promotion run by the OBS, which asks members of the public to express their views as to how the banks could improve themselves. Out of the 15 525 responses received so far, 7 875 have referred to bank charges.

Those complaints that the OBS does concentrate its energies on generally have a far greater financial impact on complainants than do pricing complaints. The top categories are shown below.

CATEGORIES	TOTAL
Mortgage Finance	724
ATM	716
Consumer Finance	421
Investments	284
Credit and Debit Cards	234
Savings Account	199
Payment Systems	178
Current Accounts	154
Insurance	147
Cheques	144

Table III: The Top Ten Categories of Complaints 2004

From this it can be concluded that bank charges are indeed a concern to many bank customers. They are not, however, a concern to all customers and they are by no means the most serious or main concern.

REDRESS

The report notes that bank customers who feel they are being overcharged 'appear to lack ability for redress'. The report refers in particular to the lack of an 'independent banking adjudicator to which consumer complaints can be directed'.

The implication of this assertion is that the existing mechanism for dealing with the complaints of bank customers, the OBS, does not deal with complaints relating to charges because it is not independent (i.e. it is beholden to the banks) but that a statutory adjudicator would be able to deal with such complaints.

The report's premise is, with respect, faulty. It is not based on research of any description or any interaction with the OBS and should accordingly be regarded as the opinion of the authors of the report.

The assumption that there is nowhere for complainants to turn is not entirely correct. The OBS does deal with complaints relating to a fee or charge being incorrectly applied by the bank, having regard to any scale of charges generally applied by that bank (i.e. there has been some maladministration in applying the charges). Even in cases where a charge may technically fall outside the OBS's jurisdiction, the OBS does, in appropriate circumstances, persuade the bank to waive the charge. Usually, the charge is incidental to the main complaint.

INDEPENDENCE

As far as independence is concerned, the Ombudsman Association of USA defines independence in the following terms:

The ombudsman is and appears to be free from interference in the legitimate performance of duties and independent from control, limitation, or a penalty imposed for retaliatory purposes by an official of the appointing entity or by a person who may be the subject of a complaint or inquiry.

In assessing whether an ombudsman is independent in structure, function, and appearance, the following factors are important: whether anyone subject to the ombudsman's jurisdiction or anyone directly responsible for a person under the ombudsman's jurisdiction (a) can control or limit the ombudsman's performance of assigned duties or (b) can, for retaliatory purposes, (1) eliminate the office, (2) remove the ombudsman, or (3) reduce the budget or resources of the office.¹

The OBS is a section 21 company with a Board consisting of a Chairman who is independent of the banks (currently Advocate John Myburgh S.C.), four representatives of civil society and a minority of three representatives of the banking industry as a whole. This means the OBS is a separate legal entity which must be governed in compliance with the requirements on the Companies Act. The profiles of the board members are attached as Appendix "A".

It is the Board that is responsible for appointing and dismissing the Ombudsman and setting the OBS's budget, to which the banks are contractually obliged to contribute, in the ratio of the number of complaints dealt with by the OBS relating to them respectively.

The Board has a similar composition to that of the largest statutory (our emphasis) financial ombudsman organisation in the world,

¹ American Bar Association Report to the House of Delegates http://www.usombudsman.org/documents/MSWord/References/ABA/ABA_Standards.doc.

the Financial Ombudsman Service (FOS) in U.K. Significantly, the FOS's activities are also funded by the financial institutions based on a formula that takes into consideration the number of cases per firm.

The Terms of Reference of the OBS further protect the independence of the Ombudsman:

The Ombudsman acts independently and objectively in resolving disputes and is not influenced by anybody in making his or her decisions. The Ombudsman enjoys security of tenure and can only be dismissed on the ground of incompetence, gross misconduct, or inability to effectively carry out his or her duties. The Ombudsman may not be dismissed for being unpopular with the banks or the consumer groupings.

The independence of the OBS scheme is further assured by the fact that the Ombudsman and employees of the Ombudsman for Banking Services are:

- (a) entirely responsible for the handling and determination of complaints;*
- (b) accountable only to the Board; and*
- (c) adequately resourced to carry out their respective functions.*

It is misleading to place reliance on the fact that the funding required for the OBS to operate is derived from the banks. The statutory Pension Funds Adjudicator and FAIS Ombud are both funded by the Financial Services Board from funds obtained from the financial industry through levies. The source of the income is irrelevant if it does not influence the way in which the ombudsman operates.

The OBS could also set up a structure to ensure that it did not receive funds directly from the banks, but all this would serve to achieve would be the generation of additional bank fees of the sort that the report was concerned about.

There is ample evidence in the public domain to show that the Banking Ombudsman does indeed operate independently. For instance, the OBS's report for 2005 shows that 53% of disputes were settled in favour of the complaints.

The report contains summaries of the binding determinations made against banks during the year, some of which have far reaching consequences for the banks.

For instance, in the case of *HR Morrow v First National Bank*, the Ombudsman refused the bank's request to make an order that the matter should be disposed of by a court, on the grounds that the bank's motivation was to avoid having to implement the terms of the OBS's final recommendation, on the assumption that there is little real prospect of the complainant actually pursuing the matter in court. The Ombudsman went on to make a decision against the bank on the merits.

The complainant had claimed the value of a motor vehicle that he had handed over to a third party after the latter presented him with an authentic duplicate original deposit slip that indicated an amount equivalent to the price had been paid into his (the complainant's) account in cash. In fact, it was a cheque deposit and payment was subsequently stopped. The ombudsman ruled that legally a bank owes a duty to its customer to issue only duplicate slips that correctly show the actual amount of cash received.

Further, the bank was required to pay the complainant R10 000 for delaying the resolution unnecessarily. The power to make such awards is unique to the OBS.

Most importantly, although the OBS was not created by statute, legislation in the form of the Financial Services Ombudsman (FSOS) Act of 2005 will regulate the OBS's activities once the Act is implemented (which should be in the near future). The FSOS statutory Council may monitor the activities of those ombuds recognised under the Act and develop best practices for them.

One of the requirements for recognition (section 10 (1) (e)) is that the ombud must be able to act independently. Once the OBS is recognised (contrary to the impression created by the report, there is no reason to believe that it will not be), the Council will have the power to require an independent assessment of the scheme (section 8 (2) (b)).

EXCUSION OF FEES AND CHARGES

It is not because the OBS is not independent that it does not deal with complaints relating purely to fees and charges, but because its mandate prohibits it from consider a complaint or dispute that relates to a practice or policy of a bank (for example, a bank's general interest rate policy or fees and charges policy), unless maladministration was involved (as was explained above).

In must be emphasized that this prohibition was approved by the committee chaired by Judge Navsa (as he then was) that was convened to restructure the banking ombudsman's office in 1999.

The committee consisted of the then Public Protector, Advocate Selby Baqwa S.C., and representatives of the Department of Trade and Industry, Treasury and the Financial Services Board. It accordingly ill-behoves representatives of another statutory body, the Competition Commission, to point fingers at the OBS.

The OBS approach of not dealing with pricing issues is in step with the practice of ombudsmen internationally, as is alluded to in the quote from Cirasino on page 59 of the report. It is a strongly held view of financial ombudsmen worldwide that redress and regulation should be kept separate² and that fees and charges are regulatory issues.

There have been media reports regarding tensions between the U.K. regulator (the Financial Services Authority) and the FOS over the latter's apparent intrusion into the former's domain through making binding rulings against financial institutions.

The report is incorrect in assuming that a statutory adjudicator would have the authority to determine fees. While the Pension Fund Adjudicator has issued decisions regarding the penalty charges associated with early withdrawal from a fund, these decisions were based on the legality of the charges in terms of the rules applicable. This fact was checked with him.

PREFERRED APPROACH

As far as we are aware from our interactions with financial ombudsmen internationally, the central banks in most countries do not prescribe fees and charges, although apparently in Ireland the central bank recommends a range of charges.

It appears that the preferred approach is to allow market forces to regulate charges. It seems from information on the internet that the strong consumer lobby in U.S.A. brought about the abolition of fees in respect of certain types of bank accounts.

The comments in the report regarding the transparency of charges are well made and supported by the OBS. Although customers are able to compare charges through services such as www.bankmonitor.co.za, this information is not broadly available in easily accessible form.

A further consideration, which was raised by the OBS some time ago and which has been confirmed by Markinor research,

² This is derived from the doctrine of the separation of powers which is central to democracy. In terms of the doctrine, the legislative, executive and judicial branches of government are kept distinct, to prevent abuse.

is that even if alternatives are available, customers feel trapped by the various barriers to moving accounts, such as debit orders for insurance policies and credit history. Much has been done in the UK to remove similar barriers.³ We suggest that the Competition Commission gives this aspect further attention.

When the incumbent South African Banking Ombudsman raised the issue of bank charges with a high ranking official at the Reserve Bank, it was explained that the Reserve Bank does not prescribe bank charges in order to avoid the banks turning to it to bail them out if they cannot operate profitably as a result. We do not know whether this is the official position of the Reserve Bank or the expression of a personal view. Nevertheless, if bank charges should be regulated by any organisation, the appropriate body to do so would be the Reserve Bank.

The Cruickshank report mentioned previously makes the point that regulation in itself poses a threat to competition.

We profess no expertise in the area of regulation (our expertise is in resolving disputes), but we are of the view that, if charges are to be regulated, it would not be ideal to do so on a case by case basis. The particular circumstances that impact on the outcome of an individual case might not apply to all cases. Further, in order to arrive at a conclusion as to whether a particular charge was reasonable, or what the appropriate charge should have been, calls for a broad enquiry into economic and other factors beyond the scope and current capacity of a mechanism designed for the inexpensive, informal and speedy resolution of disputes.

The Hawkins report itself concedes that it was unable to fully explore the question of costs, having to base its conclusion on information in the public domain.⁴ It would thus be unrealistic and inadvisable to expect the OBS to, in effect, fix prices (thereby inhibiting competition) through a series of ill informed snap decisions.

From a purely practical point of view, we shudder to imagine what impact an invitation to bank customers at large to complain to the OBS if they are dissatisfied with any bank fees or charges would have on our operations. It is reasonable to assume that no one wants to pay a fee or charge to deposit, withdraw, transfer or otherwise deal with their own money. We would be inundated.

This does not mean to say that the OBS has no role to play. On the contrary, the FSOS Act acknowledges the capacity of the non-

³ The removal of barriers followed the Cruickshank report on competition in UK banking services. An article regarding that report is included as Appendix 'B'.

⁴ Presentation to the Press at page 16.

statutory financial sector ombudsmen to gather data relating to problems within the financial institutions by requiring in section 10(1)(e)(v) that they report to the [FSOS] registrar and to a body representative of the relevant category of financial institutions on matters which may be of interest to them.

In anticipation of this and also out of a desire to provide a more comprehensive service to consumers in the South African context, the OBS is involved in ongoing negotiations with the Banking Association of South Africa, with a view to expanding the OBS's role and relevance into the banking sector. The possibility of extending the OBS's mandate to include the consideration of penalty charges is one of the issues that are under discussion between the two entities. The Board of the OBS will be approached to ratify any such extension.

A consideration of penalty charges will not entail the same caveats as a consideration of fee structures generally as these are finite and are the exception. They lend themselves more to a case by case evaluation of their reasonableness and fairness in terms of the OBS's general jurisdiction.

If it is decided that the ombudsman/ adjudicator should deal with complaints regarding the level of fees and charges, the regulator should nevertheless set the guidelines or parameters within which the ombudsman/ adjudicator must work. All ombudsmen/ adjudicators give effect to the law and codes in existence: they do not regulate.

PARTICIPATION ON BANKSERV BOARD

The recommended inclusion of the 'banking adjudicator' onto the board has obvious merits.

There are also dangers associated with such a step: although the adjudicator might have voting rights, the likelihood that the majority would outvote the adjudicator would create the impression that the adjudicator was part of unpopular decisions; participation on the board might taint the perceived neutrality (/ independence that was the concern of the report) of the adjudicator and it would offend against the separation of the regulatory and enforcement functions referred to in footnote 2.

CONCLUSION

Assuming that the Competition Commission does not find that there is collusion on the part of the banks, competitive market forces are the preferred means of keeping fees and charges at reasonable levels. For competition to be effective consumers must be able to make informed comparisons of costs and there must be no barriers to moving bank.

The OBS provides a valuable, effective service to bank customers with complaints, including complaints regarding wrongly applied charges. It should not be the function of a redress body to regulate (it would be undemocratic for it to do so).

There is no objective evidence to suggest the OBS does not operate independently. If there were, the OBS would not be eligible for recognition under the FAIS Act, which will regulates it.

Careful consideration needs to be given to the recommendation that the 'banking adjudicator' participates on the Bankserve board: it has merits and demerits.