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INTRODUCTION

This compendium consists of notes of cases drawn from the 360 dispute investigations completed during the year to 30 June 2001.

Although there was no single cause of complaint that was particularly prominent this year, a significant feature was the number of complaints lodged by the victims of crime. I have collected examples of such complaints in a single chapter, rather than under the different areas of business in connection with which they arose. For this reason there is no separate chapter on debit and credit cards: all significant investigations in this area had to do with fraudulent activity on cards.

The remaining chapters each cover a different area of banks' activities. Some cases have been selected as typical examples of a common type of complaint, others because they demonstrate an approach to issues and questions that may arise in a number of different contexts. Some cases, Case 7 for example, will be of limited interest to the general public but may be useful to banks and to legal practitioners, others are more broadly based to serve as reminders that bank customers are first and foremost human beings whose financial affairs cannot always be neatly separated from the rest of their complex lives and treated in clinical isolation.

I hope that this compendium will provide useful guidance to banks, their customers, and those called upon to advise both banks and customers. In using the case notes, however, it must be remembered that they are not precedents. Paragraph 16 of my Terms of Reference provides that the Banking Ombudsman shall not be bound by any previous decision made by him or her or by any predecessor in his or her office. Law, industry practice, and general concepts of fairness are all subject to change over time. Some of the early cases considered by this office would have a different result if considered today, and no doubt the cases comprised in this compendium will sooner or later also become dated.

1 SURVEYS OF BANKING PRACTICE

Unusually, only in one case this year did I carry out a survey of the banking industry in order to establish the principles of good banking practice in relation to a complaint. In previous years it was common to conduct five or six such surveys. This tends to confirm the view expressed in my Annual Report that the year's intake of complaints has raised no major new issues.

Operation of account held in trust for a young child

The one survey conducted arose out of a complaint from the mother of a young child. Funds were regularly credited to an account in the child's name and the mother, as trustee, regularly drew an amount out of the account for the child's maintenance. On a number of occasions when she sought to withdraw funds from the account, she was questioned by bank staff about the purpose for which the withdrawal was made. She considered the perpetual questioning an unnecessary intrusion into her daily life. The bank, however, was concerned about its liability as a constructive trustee if it did not ensure that the account was operated in the interests of the child.

Banks were asked whether, in such circumstances:

1. It was considered good banking practice to question the trustee of the account every time a withdrawal from the account was made.
2. It would be good banking practice to come to some kind of arrangement with the trustee so that she did not need to be questioned on every occasion.

3. If the answer to the second question was in the affirmative, how should such an arrangement be structured.

Five banks responded to the survey. Four of the five considered it was not good banking practice to question the trustee of the account every time a withdrawal from the account was made. The fifth bank had some reservations but indicated that regular questioning might not be appropriate when withdrawals of regular amounts occurred at regular intervals or the customer was a regular customer known to branch staff.

In response to the second question, the three banks that considered that no such arrangement was necessary either repeated that response or did not respond. The remaining two banks considered that it would be good banking practice to come to some kind of arrangement.

In response to the third question, those banks that had regarded no arrangement as necessary either repeated that response or did not respond. The remaining two banks indicated that they would accept an explanation in writing from the trustee to be recorded at the bank or produced when withdrawals were made, alternatively, a flag of some type on the account record on the bank's computer system.

2 OPERATION OF ACCOUNTS

In view of the increase in complaints about the operation of current or transaction accounts, I have selected a number of case notes that illustrate the complex nature of modern banking and the many different ways in which problems can arise.

Honour Fees

Some banks have recently introduced an “honour fee” which is charged when the bank honours a cheque or accepts an electronic transaction which overdraws the customer’s account and there is no overdraft arrangement or the arranged overdraft limit is exceeded.

While most customers see some benefit in paying a fee to avoid the embarrassment of a dishonoured cheque the same does not apply to declined electronic transactions. Many customers have been in the habit of controlling their spending by using their debit cards to make EFTPOS purchases and ATM withdrawals until the available credit is exhausted and a transaction is declined. Such customers see no advantage in having a transaction honoured when there are no credit funds to meet it and a considerable disadvantage in being charged a substantial fee.

It is no part of the Banking Ombudsman’s role to regulate the level of banks’ fees and charges. Accordingly, where I have investigated complaints about honour fees, the investigation has generally been directed at banks’ rights to alter the terms and conditions under which they offer their services and at the adequacy of notice to customers of the alteration (*Cases 1 and 2*).

I remain concerned that for some customers there is no obvious advantage in the honouring of ATM and EFTPOS transactions that a bank would be entitled to dishonour, and that the fee charged is seen as out of all proportion to any benefit that there may be. In many cases banks offer the alternative of an account where no overdraft can occur, but the fee structure of such accounts is not always acceptable

to customers who are trying to operate on a tight budget. *Case 3* was a complaint about lending on overdraft, but illustrates the sort of difficulties that have caused consumers to approach me over the issue of honour fees.

Freezing an Account

There are circumstances in which a bank may refuse to allow a customer to operate an account in the usual manner, thus denying access to the funds in the account, usually until after the resolution of a dispute over the ownership of the funds. The current Code of Banking Practice provides some information about banking practice in this respect in Clause 4.2.1(v), but only in the context of joint accounts. As *Case 4* indicates, banks can and do freeze accounts owned and operated by a sole customer or entity. It would be helpful to have a summary of practice in this respect in the reviewed Code.

Automatic Payments

A perennial complaint is that a bank has not set up an automatic payment as instructed. This does not necessarily mean that a customer has suffered a loss to the amount of the unpaid automatic payments. In most cases the funds that were intended to meet the automatic payments remain in the customer’s account and at most the customer has been inconvenienced by the bank’s failure to follow instructions. Occasionally, however, the client uses the funds in the account, unaware that they represent the unpaid automatic payments, and claims a refund on the basis that the bank’s action has caused a direct financial loss. *Case 5* illustrates the approach to such a complaint and also contains a consideration of the phrase “*direct loss or damage*” appearing in the relevant part of my Terms of Reference (paragraph 14).

Payment by Mistake

A relatively common type of complaint is that a bank has paid funds into a customer’s account by mistake, the customer has spent the funds and the bank now requires repayment. The approach to this

type of complaint has been outlined in previous annual reports and *Case 6* is included as a further illustration. It also makes the point that a **genuine** belief that the funds belong to the customer may not amount to a **reasonable** belief that this is the case.

Miscellaneous

Two further cases are included in this section for very different reasons. *Case 7* deals with a point that

may be of interest to solicitors or others winding up the estate of a deceased bank customer. *Case 8* also relates to problems arising after the death of a bank customer and it includes mention of some of the steps that may be taken when there is difficulty in locating funds thought to be have been held by a bank.

CASE 1 – APPLICATION OF HONOUR FEE

Mr C contacted my office after his bank charged him \$30 for honouring two transactions which overdraw his account. He considered such a charge unacceptable. He had not asked for the service, did not want an overdraft facility and certainly did not want to pay for it. He wrote:

“It seems that “The Bank” is still unable to understand the issue, which is that if it doesn’t have a contract with me to supply an overdraft, I should not get one and I should not pay for one. ...

If I dropped a flyer in your letterbox offering to paint your house, and you did not respond, and I painted your house and billed you, I’m sure you would be most unimpressed. The same scenario applies, and I am not impressed.”

Mr C’s analogy does not stand up to scrutiny. He did indeed have a contract with his bank, on terms and conditions which were supplied to him when he opened his account.

It is settled law that when a customer writes out a cheque that will exceed the available credit in an account the customer is effectively asking for an overdraft. A bank may accept a request for an overdraft and honour the transaction, or if after assessment of the risk a bank determines that it does not wish to advance this customer credit, the cheque will be dishonoured.

As technology changes traditional ways of doing business, settled law must be used to resolve new issues. Attempting to make an electronic transaction which would overdraw an account is a request for an overdraft, in the same way that a cheque is a request for an overdraft.

The terms and conditions of Mr C’s contract with his bank allow the bank to vary the terms of the contract, provided this information is communicated to its customers either directly or by notice in newspapers or branches. The bank chose to change the way Mr C’s account operates and now charges a fee for every transaction which exceeds the available credit. It also offered its customers the option of transferring to a type of account with a different fee structure. I am satisfied that the bank communicated the changes directly to its customers in accordance with the terms and conditions. Although information provided when the fee was introduced was adequate, I noted my concern that a brochure produced since that time does not provide information about the accounts to which the honour fee does not apply.

It was my proposed recommendation that Mr C withdraw his complaint against the bank. The bank accepted this proposal but Mr C did not respond and I discontinued my investigation.

CASE 2 – HONOUR FEES NOT A BREACH OF CONSUMER GUARANTEES ACT

Mr D challenged his bank's right to change the way his account operated. He wrote to my office complaining that the bank's introduction of honour fees had rendered his account unfit for the purpose for which it was provided, in breach of sections 29(a) and 29(b) of the Consumer Guarantees Act 1993. Mr D considered that he was no longer able to use the account for EFTPOS transactions, as he was unable to check his account balance from an EFTPOS terminal, and so be certain that a proposed transaction would not overdraw his account and incur an honour fee.

The bank did not accept Mr D's view. It said that it is the customer's responsibility to manage accounts within arrangements. Customers can obtain an account balance via a branch, an ATM terminal, telephone and internet banking. It said it had always had the discretion to honour transactions which exceeded arrangements. The only change was that customers are now charged a fee for this service.

Subject always to the terms and conditions of their contract with their customers, banks may change the way an account operates. In this case the terms and conditions of the account applicable at the time Mr D opened his account with the bank specifically allowed it to make changes to the operation of the account and to introduce new charges. I was satisfied that information provided directly to Mr D about the charges met the requirements of the terms and conditions and also of the Code of Banking Practice in that it was sufficient to explain what was going to change and what Mr D needed to do if he wished to avoid the effects of the change in policy by the bank.

A customer cannot expect that the terms on which an account operates will never change. The introduction of the honour fee did not render Mr D's account unfit for everyday banking. Although Mr D can no longer rely on the bank to monitor the amount of money he has available to spend he does have three alternatives if he wishes to avoid incurring honour fees. He can apply for an overdraft, change to an account to which the honour fee does not apply or keep a close watch on his account balance to ensure that he does not accidentally exceed the available funds in the account.

Although the bank accepted my assessment of his complaint Mr D did not and has chosen to pursue the matter through other avenues open to him.

CASE 3 – THE COMPLICATIONS OF HONOUR FEES

Mr L had difficulty understanding or managing his financial affairs. His local branch arranged automatic payments to go out of his account immediately after his benefit was received to ensure that all his expenses were paid. Mr L then used the remaining money in his account as he pleased. He understood that when he had spent all his money EFTPOS or ATM transactions would be declined. He had no cheque book.

The bank's introduction of an honour fee changed the way Mr L's account operated. Instead of transactions being declined when he exhausted the available funds the bank allowed him to overdraw the account and charged him an honour fee accordingly. Over six months, he accumulated honour fees of about \$300. Mr L could not understand what was happening. When he lodged a complaint with my office he maintained that he had not spent this money and so did not owe it to the bank. He had difficulty comprehending that although he had not spent \$300 on something tangible, he had received a service from the bank because a transaction which would otherwise have been dishonoured was honoured.

Within days of the introduction of the honour fee Mr L had asked his local branch for an overdraft. Branch staff knew his limitations and the application was declined. Mr L then approached his bank's telephone banking service and a \$100 overdraft facility was approved. Within a month the \$100 overdraft had been extended by

telephone banking to \$500, and within six months to \$1000. Mr L acknowledged that he had asked the bank for the overdraft extensions, but could not repay the overdraft.

Mr L contacted my office when the bank commenced recovery action. He was unable to repay the amount demanded by the bank. By good fortune, during the course of my investigation he won a Lotto prize and repaid the debt in full, but the investigation continued as Mr L considered he should be refunded the honour fees he had incurred.

I accepted that the bank had correctly charged the honour fee and that it was, strictly speaking, entitled to recover the debt owed. I also accepted that Mr L had received excellent service from his local branch where staff had explained the honour fee on numerous occasions and had gone out of their way to help him. However, I was concerned that the bank had contributed to his problems. Although the local branch was aware of his financial and conceptual difficulties this information was not made available to the staff Mr L dealt with through the telephone banking service. While Mr L's income may have been sufficient to service a \$100 overdraft, I did not accept that it was able to meet the demands of a \$1,000 overdraft. A bank has an obligation under Clause 9.2 of the Code of Banking Practice only to provide credit where the information available leads it to believe that the borrower is able to service the debt.

It also appeared to me that Mr L's account was inappropriate for his needs as he had difficulty understanding an overdraft. Unfortunately once he had an overdraft he was no longer eligible for an account which could not overdraw.

I concluded that a fair result would be for the bank to refund half the honour fees in recognition of its contribution to Mr L's situation. In view of evidence of the effect the problem had on Mr L's health, I also recommended a payment of \$100 by way of compensation for inconvenience. The bank and Mr L accepted my recommendation.

CASE 4 – ACCOUNT OPERATION – FREEZING

Ms A was the administrator of a company. She received on behalf of the company a demand for a debt which it could not pay. Immediately after receiving the demand, she prepared two cheques in her own favour totalling \$39,000 for signature by one of the company directors. These cheques were to repay loans she said she had advanced to the company. She immediately deposited the cheques into her bank account. She then closed it and obtained a bank cheque for the total funds in the account, approximately \$60,000. The next day Ms A deposited the \$60,000 into a new account she had opened with another bank. On the same day, the company was placed in receivership.

Over the next week she withdrew \$12,500 from her account. Her bank then received a call from the bank where she had previously held her account advising that the receiver of the company might have a claim on the funds which she had deposited with the bank. The new bank immediately placed a warning code on the account, effectively freezing the remaining funds. It attempted unsuccessfully to telephone the complainant to advise her of the status of her account. Later that day when she attempted to withdraw \$10,000 from her account she was told about the bank's action.

Over the next two weeks there was considerable contact between the bank, Ms A's solicitors and the solicitors for the receiver. Ms A was permitted to withdraw \$500, and the bank then advised the receiver's solicitors that it would freeze any funds in her account up to \$39,000 for a further 14 days, but unless it was served with a court order to freeze the funds, it would thereafter release any remaining funds. A week later the bank released \$8,340 to the complainant.

At this stage it appears that Ms A and the receiver for the company reached an agreement that \$39,000 in her account should remain frozen. She and the bank were served with copies of the relevant court papers. The bank

therefore advised Ms A, in response to a request that it release to her the funds held in her account, that it would only agree to a partial release. Some months later as a result of court proceedings, the bank released \$35,000 to the liquidator and the balance to Ms A.

The complaint lodged with me shortly after the account was first frozen was that the bank should not have frozen the account when it had no claim to the funds in the account and no legal right at that time to freeze the account.

Ms A also complained that it had taken the bank sixteen days to decide what funds could be released to her, and this was unacceptable, as was the manner in which the bank communicated with her. She said that from the time the account was frozen, all contact with the bank had been verbal and she had had to initiate any calls to the bank to obtain information. She did not accept the bank's view that it would have been liable to the receiver had it released the funds to her. Had the funds been released to her, she would have been solely responsible in terms of any action taken by the receiver. She claimed she had not only lost \$39,000, but due to the bank's actions, she had incurred unnecessary legal costs and suffered stress and inconvenience attempting to obtain the release of the funds.

In considering this complaint I had regard to the relevant general law which is set out in *Renshaw v Post Office Bank Limited* (1992) NBLC 99-273. In this case the High Court considered the circumstances in which a bank is entitled to decline to allow a customer to withdraw funds from the customer's account. It found that while a bank is not ordinarily concerned to enquire into the source of a customer's funds, a bank may be put on enquiry (because of the obligation to exercise reasonable care and skill in transacting a customer's business) as to the presence of some possible impropriety, eg, a fraud on a third person. In *Renshaw* Master Williams explained the rationale for the rule:

"The reason for a bank being able in the circumstances outlined ... to refuse to meet its customer's demands is because, if it meets the demands, the bank may later become liable as a constructive trustee for claims by third parties against it for meeting the demand."

The key issue in this case was whether the bank behaved honestly and reasonably when it declined to allow Ms A unrestricted access to the funds in her account from the date of the first freeze to the final release of funds. On the basis of the evidence made available by both Ms A and the bank, there was no suggestion that the bank behaved other than honestly and in good faith. In considering whether the bank acted reasonably, account had to be taken of the circumstances that prevailed at the relevant time. First, the bank had been advised that the cheque *"may have been drawn against fraudulently obtained funds"*. Secondly, the receivers advised the bank that the company had potential rights to the funds. Finally, the bank was aware that there was a possible voidable preference issue in respect of the cheques obtained by Ms A from the company should the company be put into liquidation. In the light of the foregoing, I considered that the bank behaved reasonably in declining to allow the complainant access to her funds.

As to the related issue of whether the bank took an unreasonable amount of time to resolve the matter as to the distribution of the funds in the account, throughout the period the bank held the funds, it and Ms A were in regular contact and, at least initially, she co-operated with the bank's enquiries. She made unsuccessful efforts to obtain the consent of the company to the release of the funds. I also had regard to the comments made by Master Williams in *Renshaw* to the effect that where a bank is making enquiries about funds in an account to determine whether it is appropriate to pay out those funds, *"the obligation to satisfy a reasonable enquiry made by a bank in those circumstances is on the customer"*. At no stage did Ms A produce any evidence to support her assertion that she had advanced funds to the company by way of a loan. In the circumstances, had the bank allowed Ms A to draw on the account, it would have run the risk of being liable to the company for assisting an unauthorised person to misappropriate funds from the company's account. I therefore concluded that the bank did not take an unreasonable period of time to decide the amount of the disputed funds and to release the balance.

CASE 5 – AUTOMATIC PAYMENT NOT SET UP

Mr B was a new customer of the bank. He gave the bank written instructions about the types of accounts he wished to have and how they were to be set up. He also told the bank that his salary would be credited to the cheque account and advised that rent would be paid from that account to his landlord's account each fortnight. He gave the number of the landlord's account and details of the amount of the fortnightly payment but he did not complete an automatic payment authority form.

Upon receipt of Mr B's letter, the bank forwarded to him relevant application forms to establish the accounts. He duly signed these and returned them to the bank. He subsequently received a telephone call from a bank staff member confirming that his accounts had been set up as he had requested. This was followed by a letter from the bank which included an ATM card for the accounts as well as instructions as to how to operate the accounts and information about when statements would be issued.

Some months later, Mr B discovered that the rent payments had not been made to his landlord's account. He had not noticed that he had extra funds available to him as a result of the non-payment of the rent as his account experienced many inconsistent and unpredictable changes for various reasons. The bank confirmed that no automatic payment had been set up for the rent. It apologised to Mr B and offered him a payment of compensation for the inconvenience he had experienced. Mr B declined the bank's offer and brought the matter to my office, claiming compensation in the sum of \$3,300, which was the amount of rent that had not been paid. He had had to borrow money from friends to pay the outstanding rent and considered that the bank should reimburse him.

The Bank submitted that it had found Mr B's instructions ambiguous and it was not clear that he was requesting it to set up an automatic payment. I considered that good banking practice required that the bank should have contacted Mr B to clarify his instructions if that were the case. I found, however, that the bank had not made any representation to Mr B that it had set up the automatic payment. In the conversation with Mr B and the subsequent letter, the bank had advised what it had done in relation to the accounts set up for Mr B. It did not mention the automatic payment.

I found that Mr B had not suffered any direct financial loss as a result of the bank's actions. Although the money had not been used for the rent, it was not possible to say that Mr B had lost it when it had not been taken from his account otherwise than by his withdrawals for personal spending. Mr B had obviously suffered a disruption to his financial planning and deserved to be compensated for that. I therefore proposed to recommend that the bank pay him \$250 to compensate him for the inconvenience its actions had caused him.

Mr B then argued vehemently that he might not have suffered a direct loss as a result of the bank's actions but he had suffered damage in terms of paragraph 14 of my Terms of Reference. He took the view that the Terms of Reference provide for compensation for "direct loss" or for "damage suffered" and that he had suffered damage to the extent of the unpaid rent.

I am of the view that "direct loss or damage" covers all economic disadvantage that may have occurred to a complainant as a direct result of the actions of a bank. In some cases there is clearly a direct financial loss, such as where a bank loses funds entrusted to it. In other cases, the damage may not be such that it can be properly described as a loss. Into this category may fall such disadvantages as costs incurred in attempting to resolve a complaint, physical damage to articles entrusted to the Bank for safe keeping, damage to reputation (defamation), some types of lost opportunity and interest on compensation awarded. "Direct loss or damage" does not include less tangible forms of loss or damage such as distress, embarrassment or disruption of financial plans. Loss under those heads is covered by paragraph 14A.

Accordingly I recommended that the bank compensate Mr B for the inconvenience he had suffered but that otherwise the complaint should be withdrawn. The bank accepted the recommendation but Mr B did not.

CASE 6 – BANK ERROR IN YOUR FAVOUR – DO NOT COLLECT \$500

Ms G, after checking her account balance, decided to splash out and purchase a musical instrument. It transpired that there was \$500 too much in the account as a result of a bank error. The reversal of the error left Ms G's account in overdraft. Ms G was unable to repay the overdraft and asked that I investigate the matter.

The legal position I had to consider was that in order to make a case for retaining the funds, Ms G would have to show that she had a reasonable belief that the funds in the account were hers, that she spent them on something she otherwise would not have and that it would be unfair for her to have to repay that money.

Although Ms G may have spent the funds on a luxury item, which, if the money had not been available, she would not have purchased, I could not agree that she had a reasonable belief that the funds in the account were hers. Ms G trusted that the bank balance recorded by the bank was accurate, and did not know exactly how much money was in her account. She did not regularly obtain account balances or receipts when she made ATM withdrawals. It was my view that, given the usual low balance in her account, it would have been reasonable for her to notice an additional \$500. She had benefited from the bank's error, she now possessed an instrument that she otherwise would not have, and although she was having difficulty servicing the debt I could not agree that it would be unfair for her to repay the debt.

It was my initial view that the bank and Ms G ought to discuss how she could repay the debt on terms generous to her, in recognition of the bank's error. By the time she received my initial assessment of her complaint Ms G had repaid the debt by consolidating it with other debt in a personal loan from the bank. However she did not accept that she should have to repay the debt at all and asked that I reconsider her submissions.

On reconsideration there was still no evidence that Ms G had a reasonable belief that the funds were hers. On the other hand it had always been clear that she had genuinely believed the funds were hers and that an error on the bank's part had misled her and caused her to incur a debt that she otherwise would not have incurred. I recommended that a compensatory payment to Ms G of \$100 was appropriate to recognise the on-going inconvenience and stress associated with the debt. Both Ms G and the bank accepted my recommendation.

CASE 7 – DEALING WITH FUNDS HELD TO CREDIT OF AN ESTATE

A solicitor acting in an estate complained that a bank would not release funds held to the credit of the late account-holder. The sole beneficiary of the estate was in difficult financial circumstances and the solicitor was trying to avoid incurring extra costs which would diminish the value of the inheritance she would receive.

The total amount in the account at the date of the death of the account-holder had exceeded \$11,000 which was the threshold above which a grant of probate was required. The bank, with the consent of the beneficiary, had released funds from the account to pay the funeral director and thereby reduced the balance of the account below \$11,000.

The solicitor claimed that section 65 of the Administration Act 1969 appeared to give the bank the right to release funds below the threshold level without a grant of probate. He also claimed that the Act permitted a bank to settle funeral expenses from an estate to which section 65 applied, provided that no other applications for the funds had been made. He claimed that the bank had relied on section 65 to pay the funeral expenses but had then refused to release the balance of the funds on the basis that section 65 did not apply because the balance before the payment to the funeral director had been above the threshold.

I advised the solicitor that, while I was not able to make binding determinations on points of law, it was my view that the bank was correct in its interpretation of section 65. The balance which determined whether or not

probate would be required was the balance at the time of the account-holder's death, not the reduced balance. A grant of probate was therefore required. I therefore considered that the bank had not breached any obligation or duty owed to its customer, the estate, and I declined to consider the matter further. The solicitor accepted my view and subsequently obtained a grant of probate to enable the funds to be released to the beneficiary.

CASE 8 – SEARCH FOR THE MISSING \$10,000

In 1991 Mrs and Mr D placed \$10,000 on term deposit with a bank for twelve months. On maturity both interest and principal were to be reinvested. Some years later Mr D died. The last time Mrs D could recall seeing any paperwork relating to the term deposit was towards the end of 1997.

In June 2000 Mrs D went to the bank with the term deposit certificate. The bank officer could not find any record of the deposit, however he asked for copies of the Resident Withholding Tax certificates. It was hoped the term deposit could be traced by looking at the amount of tax paid on interest Mrs D had earned. Mrs D obtained the certificates but her tax records did not reveal the existence of the term deposit.

In July 2000 Mrs D rang the Ministry of Consumer Affairs Bankline, and was referred to my office. As the complaint had not been considered by the bank's internal complaints process the matter was forwarded to the bank. The bank responded to Mrs D's complaint in August advising that it could find no record of the term deposit. The bank had obtained copies of Mrs D's bank statements and the only references to term deposits were to ones still in existence. Mrs D remained convinced that there was another deposit that the bank had failed to trace.

I then commenced my investigation. The bank submitted that the matter fell outside my jurisdiction pursuant to Paragraph 22(d) of my Terms of Reference, as the bank considered that it would be prejudiced by the passage of time since the term deposit was first made. I did not accept that the matter was outside my jurisdiction as Mrs D's complaint was the bank's current failure to provide her with a satisfactory explanation of what had become of her funds.

The bank advised that it had searched all its records, including her lending file, without locating anything to suggest the whereabouts of the term deposit. The bank was asked to confirm that it had looked for accounts under Mr D's sole name, Mrs D's sole name and Mr and Mrs D's joint names. The bank had only looked for records under Mrs D's name, and so conducted additional searches. These also proved fruitless. It was unable to search Mr D's accounts. As they had been closed the bank required an account number to conduct the search. Mrs D was unable to supply the bank with this.

Mrs D mentioned that she and her husband had had a number of Bonus Bonds over the years, and wondered whether he had invested the money in Bonus Bonds. A request was made to Bonus Bonds to search their records. Initially Bonus Bonds advised that neither Mr nor Mrs D had ever held Bonus Bonds. On further enquiry it transpired that Bonus Bonds had been searching under a different spelling of Mr and Mrs D's surname. When the correct name was searched, the records of the Bonus Bonds held by them were produced. However, this also was of no assistance in locating the funds. At this point Mrs D accepted there was nothing further either the bank or this office could do to assist her and so withdrew her complaint.

3 LENDING

Lending, whether secured or unsecured, continues to feature in the majority of complaints made to me. This year there is no single issue that dominates the caseload, but it is possible to identify certain circumstances in which complaints seem more likely to arise.

Mistakes and poor administration

A common cause of complaint is that a bank has made a mistake in the loan documentation or in the administration of the application and approval process and has then failed to correct it to the customer's satisfaction. In *Case 9*, I consider the doctrine of rectification in this context and in *Case 10*, the relative responsibilities of a bank and a customer in ensuring that sufficient funds are available to settle a proposed purchase.

Case 11 is again a case about a bank's mistake, this time in the administration of a loan drawn down in stages. Any disruption to draw down arrangements for building is likely to cause serious difficulties, and in this case the distress and inconvenience suffered by the complainants were so substantial that I recommended the bank pay the maximum I can award for such a claim. I also suggested it consider increasing the amount on an ex-gratia basis.

Joint Borrowing

Joint borrowing continues to be the background to a number of complaints, especially when the relationship between the joint borrowers has broken down. *Case 12* is a case where the bank's attempt to remedy its initial poor handling of its customers' affairs caused even more problems. *Case 13* illustrates some of the difficulties that can occur when a former partner's consent is needed for further borrowing.

Business Lending

For the first time, I have this year received several complaints where there was a question of compliance with the Statement of Principles "*Banks & Small, Medium Sized and Farming Business*

Working Together". Most investigations are still under way at 30 June 2001 and the cases will be reported next year. *Case 14* has a background in the breakdown of a joint borrowing relationship and the events in question occurred before the Statement of Principles came into force, but part of the problem was the bank's failure to alert its customer to its concerns about his business borrowing. I considered the case on the basis that the standards set by the Statement of Principles were at least a guide to good practice at an earlier date.

Commercial borrowing in the context of small scale investment property ownership is another area that gives rise to complaints, sometimes as a result of a bank assuming its customer has a wider knowledge of banking procedures and lending processes than is reasonable, or than is in fact the case. In *Case 15*, the bank made the unreasonable assumption that its customer should have known that he had not completed the loan application process. In *Case 16* there were also failures in communication but the complainant was largely responsible for the problems with his borrowing.

Case 17 involved more extensive property ownership and was also a complaint about the cost of early repayment of a fixed interest rate loan. Interest rates have been fairly stable during the 2000/1 year, and I am not receiving complaints about early repayment costs to the extent that I did in previous years. They do, however, still feature in many complaints about lending.

Rural Lending

Case 18 concerns issues in rural lending and is an example not only of the complexities that can occur as a result of alterations in inter-related lending products but also the extremely difficult nature of an investigation when the relationship between the bank and its customer has broken down to the extent that the customer is not prepared to accept any explanations provided by the bank.

Irresponsible Lending

Clause 9.2 of the Code of Banking Practice provides that banks will only provide credit when information available to them at the time of a lending decision leads them to believe that the borrower is able to service the debt and meet the terms and conditions of the loan. It was applicable in *Case 3* as well as the cases noted below.

Case 19 is included because there is anecdotal evidence of concern (unfounded in this case) that banks may be acting irresponsibly in lending on credit cards when the customer has insufficient income to service the borrowing. I have received very few complaints of this nature although I could certainly consider such a complaint as an alleged breach of 9.2 of the Code.

Concerns have also been raised in the context of standard account packages which include a small overdraft facility. Banks will normally conduct a credit check when opening such an account, and there is unlikely to be a breach of clause 9.2 if a small overdraft is provided on the basis of a clear credit check. *Case 20* is a case in point.

Mortgage Brokers

I continue to receive complaints which, upon investigation, appear to be directed at mortgage brokers rather than at banks. *Case 21* is a case where the mortgage broker was not acting as the agent of a bank and accordingly the bank could not be held responsible for the misleading advice its customer received.

CASE 9 – A MISTAKE IN THE LOAN AGREEMENT – RECTIFICATION

This complaint arose from a mistake by a bank in documenting a term loan. In November 1995 the bank advanced Mr F \$73,000 secured by a mortgage over Mr F's property. The loan was to be repaid over 25 years at an interest rate of 8.75% for the first three years. The monthly repayments were \$600.16. In March 1996 the bank advanced Mr F a loan of \$82,000 which he used to repay the existing loan and undertake further building work. The new loan was also for a period of 25 years and the interest rate was fixed at 10% for three years. However, the loan agreement stated that the monthly repayments were \$339.64. Mr F said he had asked the bank staff when he signed the second loan agreement if the repayment figure was correct and had been assured that it was. He therefore budgeted for monthly loan repayments of \$339.64.

Repayments were made by automatic payment from Mr F's cheque account on a fortnightly rather than a monthly basis. Mr F said that he had been so busy he had not noticed that the payments were being made on a fortnightly basis, even though he obtained a further personal loan of \$8,000 from the bank in May 1996.

In April 1997 the bank advised Mr F that his cheque account was overdrawn. The bank acknowledged that an error had been made in the loan documentation regarding the loan repayments. It approved a temporary overdraft facility to cover Mr F's expenses and Mr F then sought legal advice.

Over the next eighteen months there were unsuccessful attempts to reach agreement on a resolution of the complaint. In June 1998 Mr F said he would not accept the bank's latest offer and that he would refer his complaint to the Banking Ombudsman. This he did not do.

In March 1999, the bank advised Mr F that if the loan arrears and cheque account overdraft were not cleared within 14 days, it would commence recovery action. The same month Mr F signed an agreement to sell his property for \$130,000. The final settlement figure of \$109,266.50 was paid to the bank on 23 April 1999 on a "without prejudice" basis as Mr F had by this time lodged a complaint with it.

Mr F complained that the bank had unilaterally varied the loan agreement which clearly stated that the loan repayments were to be paid monthly. He said this had caused him serious financial difficulties. He calculated he owed the bank \$91,252.22 at settlement date, but that the bank should compensate him for legal and other costs he had incurred.

In considering the complaint I had regard to s 5(2) of the Contractual Mistakes Act 1977 which preserves certain areas of the law that impinge on mistake in contract cases, including rectification. Rectification is an equitable doctrine permitting the Court, in appropriate circumstances, to alter the terms of a written document to accord with the intentions of the parties to it. In *Farmers' Mutual Insurance Ltd v QBE Insurance International Ltd* [1993] 3 NZLR 305 at 314 the Court held there is a severe evidential burden on the party seeking rectification. There needs to be established, on the balance of probabilities, not merely that the contractual document is incorrect, but that there existed an agreement in different terms. If there was an earlier contractual agreement in the same terms as the one sought to be rectified, there is a heavy onus to show the common intention of the parties had altered since the earlier agreement. In *Westland Savings Bank Ltd v Hancock* [1987] 2 NZLR 21 the Court held rectification may also be available where only the applicant for relief was mistaken as to the contents of the contractual document, provided that the Court is satisfied that it is inequitable for the document to apply in its current form. This may be because one party realises an error has been made and keeps silent in order to obtain a benefit under the document which would otherwise not have been received. The Court held the issue is whether enforcement of the document in its terms would be inequitable.

In the case under investigation, there was a drafting error on the part of the bank in the documentation for the March 1996 loan advanced to Mr F. There was no suggestion that Mr F and the bank had agreed that the repayments would be \$339.64 per month. The common intention of the parties was to refinance the existing loan on the same terms and conditions, that is monthly repayments for a term of 25 years.

I had some difficulty accepting that Mr F genuinely believed that even though he was borrowing \$9,000 more than his November 1995 loan, his monthly repayments would almost halve. I considered that he should have questioned the bank more closely than he apparently did about the repayment figure before signing the agreement. Notwithstanding how busy he was, I also believe that it would be reasonable to have expected him to have noticed that repayments were being debited from his account on a fortnightly rather than a monthly basis and to have raised the matter with the bank at a much earlier stage.

In the circumstances, I came to the view that the bank would have been entitled to obtain relief from a Court by way of rectification of the agreement. I also considered the offer extended to Mr F in August 1997 and found it to be a generous one. The bank at that point had offered several options, including an offer to maintain the low repayment rate for the time being and an alternative offer to amalgamate Mr F's two loans at a low fixed interest rate. Any one of the options offered would have alleviated Mr F's difficulties to some extent.

I did not accept Mr F's claim for losses and inconvenience. However, with respect to the legal fees he had incurred, I found that the bank had failed in August 1997 to advise him of available complaints procedures (including the Banking Ombudsman) resulting in Mr F consulting a solicitor, perhaps unnecessarily. I therefore concluded that the bank should meet half the relevant costs. As Mr F did not respond to my initial assessment of the complaint, I did not proceed to a final recommendation.

CASE 10 – DEPOSIT NOT HELD BY USUAL AGENTS

This complaint arose from an unfortunate, but innocent failure in communication. Mr and Mrs V, who had limited funds, had decided to sell their existing property and purchase a cheaper one. They had loans from the bank secured by way of first and second mortgages of \$90,000 and \$45,000 respectively over their existing property. The property was sold at auction in March 2000 for \$172,000 with a 60 day settlement period. The balance of the deposit, approximately \$12,000 after deduction of the real estate agent's commission, was paid by the purchasers directly to Mr and Mrs V and deposited into their cheque account.

They found a suitable property and provided the bank with a valuer's report which valued the property at \$125,000. The bank advised it could lend up to \$102,000 and Mr and Mrs V negotiated to purchase the property

for \$126,000. Shortly after making their unconditional offer, they approached the bank to check that they had sufficient funds to meet the price. Upon settlement, it was discovered that they were approximately \$12,000 short of the necessary funds to settle. It transpired that the bank had not been aware that Mr and Mrs V had received and spent the deposit paid by the purchasers of their former property. It had assumed it was available as part of the purchase price for the new property. The bank agreed to arrange a temporary overdraft to enable settlement to proceed.

Mr and Mrs V complained to the bank that as a result of the wrong advice it had given them about their financial position, they had an additional \$12,000 to repay. In addition, they had had to pay penalty interest to the vendors of their new property because they had been unable to settle the purchase on time. They asked the bank to write off the \$12,000 debt. The bank declined to do so, but it offered to reimburse the penalty interest; consider renegotiating the shortfall as a loan secured by the new mortgage; and waive the establishment charge for setting up the loan. Mr and Mrs V did not accept the bank's offer and lodged a complaint with me.

Mr and Mrs V said they had sought and relied on the bank's advice that they had sufficient funds to purchase the replacement property. They also said they had made it clear on at least two occasions to the bank that the deposit on their former property had been paid directly to them. They believed the bank should have realised this, as it was the only deposit in their account in excess of \$1,000. They did not realise that it was most unusual that the purchasers of their former home had paid the balance of their deposit directly to them rather than to their real estate agent or solicitor.

The bank advised that its calculations of Mr and Mrs V's funding for the purchase of their new property had included the deposit for the sale of their former property. The officers to whom Mr and Mrs V had spoken denied having been told that those funds had already been spent. The bank pointed out that it did not monitor customers' daily account transactions and could not have been expected to realise that the deposit into their account represented the deposit from the purchase of their former property. It believed it had acted reasonably on the basis of the information provided.

It was clear that the bank's calculations had been based on the figures for the respective sale and purchase prices of the two properties. It had not occurred to the bank staff that the deposit on the sale of the former property would not be available. If Mr and Mrs V had told the bank that they had received the deposit, the bank officers would likely have understood this to mean that it had been paid to their solicitor.

I did not consider that the bank staff could be said to have been negligent, nor did I think they could have been expected to be aware from Mr and Mrs V's account statements that the deposit had been paid to and spent by them. Furthermore, the ultimate responsibility for working out whether they could meet their commitments on settlement day rested with Mr and Mrs V and their solicitor.

Having found that there was an innocent failure in communication and no negligence on the part of the bank, there was no basis for requiring the bank to write off the sum of \$12,000. The bank had made a reasonable offer to settle the complaint, and I concluded that the complainants should accept that offer.

CASE 11 – FINANCE WITHDRAWN WHEN BUILDING UNDER WAY

In May 1998, the bank agreed to lend Mr and Mrs M \$330,000 bridging finance to enable them to purchase a new property pending the sale of their existing property. The existing property sold and the bridging finance was not required, but Mr and Mrs M required a loan of \$70,000 to enable them to settle the purchase of the new property.

Instead of drawing up a new loan agreement, the bank used the existing \$330,000 loan agreement to allow settlement to proceed. Mr and Mrs M understood from discussions with their local branch that the balance of

the \$330,000 loan was available to be drawn against as they required for the development of their new property. Their belief was reinforced by the fact that over the next eight months they were able to draw a total of \$65,000 against the loan. In April 1999 they opened a separate building account at their local branch and on 30 April the balance of the loan, \$195,000, was paid into that account. However, on 4 May, without any prior notice, the bank reversed the credit and telephoned Mr and Mrs M to advise that the \$195,000 was no longer available.

Mr and Mrs M were then left without funds to cover the financial commitments made in reliance on the availability of these funds. They discussed their predicament with the bank and were advised the facility had been withdrawn because funds had been drawn down outside the six month period set out in the loan agreement. Temporary overdraft facilities were arranged and they submitted a fresh loan application.

The bank required more information, including plans, about the proposed development before approving the new application and Mr and Mrs M could not provide this without access to funds. In recognition of its error, the bank offered to refund its charges for establishing the overdraft; refund the interest difference between the home loan interest rate and the overdraft interest rate; refund interest and late payment charges on Mr and Mrs M's credit cards; and pay \$500 for stress and inconvenience.

Mr and Mrs M felt they had no option but to obtain finance from another source and lodged a complaint with me about the bank's conduct towards them, seeking compensation from the bank for all the extra costs and fees they had incurred. In particular, they requested compensation for the distress and embarrassment caused by the unexpected withdrawal of funding. They had been reasonably comfortably off, but for a substantial period found themselves living hand to mouth as they struggled to meet their own living expenses as well as their commitments to the tradesmen working on the house.

The bank acknowledged that it had erred in allowing Mr and Mrs M to draw against the bridging finance instead of requiring them to complete a fresh loan application. However, the bank's explanation of its decision to reverse the final draw down overlooked the fact that it had previously allowed a draw down of two other amounts outside the six month period. I concluded that while, in a strict legal sense, the bank may have been entitled to reverse the amount, it was wrong by any standards for it to have done so without giving notice to Mr and Mrs M.

Given the very considerable inconvenience, stress and embarrassment, I recommended that the bank pay \$2,000 in addition to Mr and Mrs M's direct loss in extra costs and fees. This is the maximum amount authorised by paragraph 14A of my Terms of Reference. I suggested that in this case, in view of the very substantial inconvenience caused by its actions, the bank might consider increasing the payment, but it was not prepared to do so.

The complaint was therefore settled on the basis of a payment representing compensation for the direct loss together with a further \$2,000 compensation for inconvenience.

CASE 12 – A CASE OF LIMITED SECURITY

When Ms B and her husband separated, her brother, Mr C, added his name to her loan and mortgage to satisfy the bank's lending criteria so that she could retain her home. Mr C signed an acknowledgement that he had no interest in the property and Ms B was responsible for all expenses associated with it. Mr C banked with the same bank as Ms B.

A year later Mr C's business ran into financial difficulties and the bank referred both his and Ms B's accounts to credit management. Ms B was extremely concerned when the bank claimed to be able to use her property as security for Mr C's debts. Neither of them had intended that Mr C's assistance should in any way make Ms B responsible for his debts. She contacted the bank officer managing Mr C's accounts, as she was terrified that she would lose her home. She asked what would happen if she sold the property, as she was hoping to do. The

bank officer told Ms B that the bank would hold the equity in the property until it was satisfied that Mr C's indebtedness to the bank would be repaid.

Ms B sought advice from a banking consultant and later wrote to me. The matter was referred to the bank's internal complaints process. The bank confirmed that its security over her home was limited to her borrowing only. The bank apologised for the stress and difficulties she had experienced and offered her a three-month mortgage holiday as a gesture of good will. Ms B did not consider this to be sufficient. She had suffered severe stress and had required medical attention. This stress was compounded when the bank failed to correctly process the mortgage holiday application and as a result transactions were declined and cheques dishonoured. She sought \$2,000 compensation for stress and inconvenience, costs associated with the banking consultant and a refund of toll calls to her sister for help and support.

The bank agreed to meet the costs associated with the banking consultant and the telephone calls to Ms B's sister. It offered her \$100 for the stress associated with incorrectly processing the mortgage holiday. The bank did not consider compensation was appropriate for the stress associated with the bank's decision to hold her liable for Mr C's debts.

At this point the matter was referred back to me. I found it incredible that the bank had attempted to rely on its mortgage over Ms B's home to secure loans to Mr C and his business. Even if this was legally possible, which was doubtful, it was unfair and contrary to good banking practice where there had been no disclosure to Ms B of Mr C's indebtedness. I was also concerned that the bank did not contact Ms B to explain why her accounts had been transferred to credit management. Ms B had been very upset and stressed to discover that she could lose the equity in her home through no fault of her own. This stress had been exacerbated by the bank taking over six weeks to confirm in writing that it would not use her home as security for Mr C's debts. The bank then declined to take any responsibility for this stress. I considered that \$1,200 was an appropriate amount to compensate Ms B. I also considered that the bank's offer of \$100 for the stress associated with the mortgage holiday was insufficient; \$250 was a more accurate reflection of the degree of stress caused to her. Both Ms B and the bank accepted this.

CASE 13 – A LATE REQUIREMENT DELAYS SETTLEMENT

Mr G and Ms H, both of whom were coming out of matrimonial property situations, wished to purchase a property. On 23 June 2000 a mortgage broker applied for and obtained an offer of 100% finance from the bank to be secured by a mortgage over the property and a first and only charge over a superannuation fund belonging to Mr G. The offer was accepted and details were forwarded to the complainants' solicitor on 27 June. On 7 July, one week before settlement date, the bank sent loan documentation to the solicitor together with a form for completion by the former wife of Mr G waiving her rights under the Matrimonial Property Act to claim against the superannuation fund. When this waiver was not forthcoming, the bank declined to advance the mortgage finance as originally offered. Instead it revised its offer, increasing the interest rate on part of the loan. It also required payment of a processing fee.

Mr G and Ms H were then faced with either accepting the revised offer or incurring considerable expenditure by not being able to settle the purchase. They therefore accepted the revised offer. Following settlement, they approached the bank seeking reconsideration of its decision to impose the processing fee when they considered that the bank had had all the relevant information available to it from the outset and had not raised the question of obtaining the waiver until after their offer to purchase had gone unconditional. The bank offered to refund half the fee once the relevant part of the loan had been repaid. Mr G and Ms H were not happy with this offer and asked me to investigate their complaint.

The bank believed that the solicitor would have been aware of the current status of the matrimonial property settlement and should have realised that Mr G could not provide the security needed in terms of the charge over the superannuation funds without his former wife's consent. The solicitor should therefore have obtained the necessary waiver without waiting for the bank to ask for it.

The solicitor argued that the bank had been aware from the outset that the matrimonial property situation had not been finalised. Accordingly, if the waiver requirement was a condition of the loan, it should have been specified by the bank when the initial loan offer was made. An applicant cannot make an informed decision on an offer unless all conditions are specified.

The mortgage broker who assisted Mr G and Ms H said he had discussed the loan application with the bank and had explained the matrimonial property situation. He believed the bank understood the position, and had not asked whether matrimonial property agreements had been signed. He considered that if this was relevant to the bank's consideration of the application, it should have addressed the issue before approving finance.

These comments were put to the bank for consideration. In reply, the bank offered to settle the complaint by refunding the full application fee. Mr G and Ms H accepted this offer.

CASE 14 – A FAILURE IN COMMUNICATION

Mr O and his former wife jointly owned a farm which was mortgaged to the bank. They also had a joint working overdraft with the bank of \$35,000. The couple separated in 1996 and their marriage was dissolved in 1998. However, settlement of the matrimonial property was not achieved until June 1999. In 1996 Mr O extended the overdraft to \$75,000 to enable a preliminary settlement payment to be made to his former wife. The bank agreed to obtain the former wife's signature on the relevant documents, but failed to do so.

In August 1998 Mr O applied to increase the overdraft to \$110,000, but when the papers were sent to his former wife for signature in October she refused to sign. In the meantime, Mr O had operated his account in the belief that the overdraft agreement was \$110,000. In October 1998 the bank advised Mr O that in order to protect its position it was stopping the existing overdraft. It said Mr O would have to open a new account and operate it in credit. In the event of any default the bank would take recovery action. Mr O immediately visited the bank and, following a discussion with the branch manager, was left with the impression that provided he took steps to reduce the overdraft, nothing further would happen. However, at the beginning of December 1998 the bank advised Mr O that his account had been frozen. He had further discussions with the bank during December and January 1999 in an attempt to restructure his financial position. He applied to increase his mortgage by \$50,000 but this was declined although the bank did offer to increase his overdraft limit for a limited period. When Mr O decided to refinance his borrowing with another bank, his arrangements were delayed as a result of the bank's temporary misplacement of relevant documents.

Arising out of this sequence of events Mr O considered that the bank had mismanaged his accounts by failing to assist him in establishing a plan of action following the breakdown of his marriage, in particular, a plan to buy out his former wife's share in the farm. He was also concerned about the delay in advising him that his former wife had declined to agree to the increase in the overdraft limit to \$110,000 and complained about the bank's decision to freeze his accounts and its delay in advising him that his application for additional finance had been declined.

It was clear from the bank's files that it had had concerns about Mr O's accounts for some time before it froze them. By September 1998 it was noted that the debt level was too high for the farm to service comfortably. Matters were brought to a head when the former wife declined to consent to any extension of the farm overdraft limit.

Although the bank gave Mr O notice on 6 October 1998 that no further increases in the overdraft would be permitted, it did not set out its expectations regarding reduction of the existing overdraft debt. Furthermore, there did not appear to have been any contact between the bank and Mr O between 6 October and 2 December when he was advised that this account had been frozen. Had the Statement of Principles relating to the relationship between banks and small, medium sized and farming businesses been in operation at this time, this failure to communicate would have been a breach of Principle 6 which requires banks to alert businesses in writing when they have concerns about the business. On the other hand when it froze the account the bank acted immediately to assist Mr O by opening a new account to enable the farm business to continue operation.

My overall impression was that Mr O had somewhat unrealistic expectations of the bank, but that the bank's administration of his affairs was not always of a good and professional standard. While these shortcomings undoubtedly caused inconvenience, I was not persuaded that they caused any direct financial loss. I therefore concluded that a fair and just settlement of the dispute would be for the bank to pay Mr O \$700 compensation for inconvenience. This finding was accepted by both parties.

CASE 15 – LATE ADVICE OF DECISION TO DECLINE LOAN

Mr H planned a major restructuring of his financial affairs. He set up a company and transferred a number of his properties to the new company. He was also in the process of purchasing further properties, which were to be transferred into the company on completion of the purchase, and of selling other properties.

As well as the restructuring, Mr H required further finance to develop one of his properties.

Mr H visited his bank branch and discussed his plans and the need for funding in addition to his current borrowing. The branch recommended that Mr H take out a revolving credit facility. Mr H understood that in return for the provision of a revolving credit facility of \$100,000, the bank would take security over three of his properties. The bank specifically advised Mr H that there would be no problem with the security properties being owned by the company as Mr H could provide a personal guarantee to the bank.

Mr H was not asked to sign any documentation and understood that an agreement had been reached as discussed. Mr H's lawyer was to write to the bank outlining details of the restructuring and the branch was to arrange implementation of the agreement by the bank's credit centre. This involved arranging for the transfer of the securities to the company, restructuring the existing loan plus additional finance into the revolving credit facility, and obtaining a personal guarantee from Mr H.

Mr H's solicitor wrote to the bank confirming details of the proposed restructure of ownership of the properties.

Four days before settlement of Mr H's purchases and sales of properties, Mr H visited the branch on another matter and was advised as an aside that everything was in order for settlement.

A day later the bank telephoned Mr H and advised him that the bank could not provide the facility. Mr H incurred additional legal costs as a result of attempting to find an alternative financier three days before settlement. He was also severely inconvenienced.

The bank says it provided no commitment to lend on the basis discussed; at most it only indicated that the proposal may be worth pursuing. Further, Mr H made no formal loan application, which was necessary given that he was seeking increased funding.

I was of the view that Mr H reasonably believed that the bank had agreed to provide the facility. While it is usual practice to require the completion of an application form, the bank did not ask Mr H to complete one. Further, Mr H was a current customer of the bank and it was not unreasonable for him to believe that no forms needed to be completed. He was not aware of all the details of the bank's lending process.

Mr H's and the bank officer's recollections of their meeting were very similar. There was nothing in either the bank officer's diary note or Mr H's own diary note to suggest that Mr H was to take the initiative about further action. Mr H did what he was supposed to do; he arranged for his lawyer to provide details of his restructuring. The bank did not do what it was supposed to do. The bank officer's instruction to the credit centre remained unactioned. It appears the credit centre believed that a formal application was on its way. Mr H was not responsible for this misunderstanding. The bank had several opportunities to correct the situation. The credit centre, on receipt of the bank officer's instructions, could have asked for the application form. Alternatively, it could have assessed Mr H's application as set out in the bank officer's instructions, advised that it could not lend on the basis requested by Mr H and provided its reasons. Mr H could then have submitted a modified application. The branch could have contacted Mr H after receiving the letter from the solicitor which clearly indicated that Mr H believed that approval had been granted.

I recommended that the bank reimburse Mr H for the legal costs incurred due to the bank's late advice of its decision to decline to provide the facility. I also recommended that the bank make a payment to Mr H in recognition of the stress and inconvenience he suffered as a result of the late advice.

The bank accepted my recommendation.

CASE 16 – PART REPAYMENT OF A LOAN

Mr W owned two rental properties purchased with loans from the bank, each loan being secured by a mortgage over the relevant property. In November 1998 he sold one property and his solicitor asked the bank for a discharge of mortgage and settlement statement in time for settlement. The solicitor undertook to retain the documents until the bank's "...mortgage is repaid in full as to that property". The settlement statement forwarded by the bank showed the amount of \$42,420 to be repaid as a "bulk reduction". The bank also faxed the solicitor asking to which of Mr W's two loan accounts the "bulk reduction" was to be applied, and later sent a further message confirming the amount required on settlement, again using the words "minimum bulk reduction".

Although there had been an earlier occasion when Mr W had sold a property and the bank had not required settlement of the loan in full, the wording used by the bank did not alert the solicitor to the fact that the payment required by the bank would not repay the mortgage in full. Following settlement of the sale, the solicitor forwarded \$42,420 to the bank in the belief that this amount was full repayment of the loan originally taken out to purchase the property now sold.

In March 1999, a Property Law Act notice was served on Mr W by the bank's solicitors in respect of loan arrears of approximately \$4,700. Mr W paid the amount, but made no enquiries about the nature of the arrears. In May 1999, a second Property Law Act notice was served. At this stage, Mr W discovered that approximately \$22,000 was still owed in respect of the property he had sold in November 1998, the bank having secured the liability against the second rental property. He then arranged to sell that property, but settlement was delayed because the bank was not prepared to withdraw action under the Property Law Act until it received an undertaking from Mr W's solicitor that all monies owing to it would be repaid in full upon settlement of the sale.

Mr W considered that the bank had acted unreasonably. He had understood that his only obligation to the bank, after repaying the \$42,420, was in respect of the loan for his second rental property. As a result of the bank's actions he had incurred penalty interest, costs resulting from the delay in settling the sale of his second property and legal fees relating to the Property Law Act action.

Having carefully considered all the evidence, I concluded that there had been a lack of communication at various times. For example, the bank did not advise Mr W or his solicitor following settlement of the sale of the first property that some \$22,000 remained outstanding in respect of the loan and that this would be secured against

the second property. In the belief that he had cleared the first loan Mr C made no provision for paying the residual amount. The situation was further complicated by the fact that he stopped repaying the loan for the second property. The bank wrote to him twice in February 1999 about the arrears, but received no reply. It therefore issued a notice under the Property Law Act which he satisfied, but he made no provision for future loan repayments. As a consequence, the bank took further action under the Property Law Act to recover arrears. In addition, correspondence which Mr C's solicitor sent to the bank was not answered.

I came to the view that the bank ought to have advised Mr W or his solicitor that the loan for the first property had not been repaid in full. I concluded that it should refund the interest in respect of the loan for the first property for the period from the date of settlement of the sale in November 1998 until 24 February 1999. This was the approximate date Mr W ought to have received the bank's second letter about the arrears and become aware of the situation. I also concluded that the bank should pay \$200 towards the legal costs Mr W incurred in trying to resolve the situation with respect to the first property.

I concluded that the prime responsibility for the problems lay with Mr W. Notwithstanding the bank's failure to advise him that the first loan had not been repaid in full, he had an ongoing obligation to make payments in respect of the second property. He did not make any payments and the bank therefore took recovery action under the Property Law Act. For this reason I did not consider that his claim for reimbursement of the legal costs associated with the Property Law Act notices was reasonable.

CASE 17 – UNFAIR TO RECOVER EARLY REPAYMENT COST

XYZ Ltd, a property company, considered that the bank had treated it unreasonably in requiring it to pay the cost of early repayment of its loans following its decision to refinance with another bank. It maintained that the bank had left it with no option but to refinance and had led it to believe that no additional charges would be levied upon repayment of its outstanding loans.

Consideration of the relevant papers led me to the view that, while the bank did not specifically require XYZ to refinance, it was certainly the bank's preferred option. XYZ's directors' discussions with bank staff left it in no doubt about this.

When XYZ asked whether any penalty interest would be charged if it refinanced, the bank advised that it might be prepared to negotiate the application of the break fee. The indicative settlement statement provided by the bank made no mention of a break fee nor was it included in the actual settlement statement prepared later. Arguably this omission amounted to misleading conduct on the bank's part in breach of the Fair Trading Act 1986. On the other hand, it had to be said that XYZ was aware that a break fee could apply but did not seek further clarification on this point. In the end, the bank did not negotiate with the company over the break fee but simply recovered the full amount. The eventual date of settlement and repayment of the loans occurred about five months before the expiry of the fixed rate period. The bank might therefore reasonably have pointed out to XYZ that it could defer refinancing until that time, thereby avoiding the break fee that would otherwise apply. Equally, if XYZ had been aware that a break fee was to be charged, it could itself have considered postponing its refinancing.

I concluded that while the bank had the contractual right to charge XYZ the full amount of the break cost, in the circumstances it was unfair to recover the total sum. In estimating what direct loss the company had suffered, account had to be taken of the fact that it had benefited from a lower interest rate on refinancing. I therefore deducted from the break fee the interest savings the company made over the five month period the original loan still had to run. I also considered that XYZ was entitled to a contribution towards the costs it had incurred and a payment for inconvenience.

After considering both the company's and the bank's views on my conclusions, I recommended that the bank refund 80% of the direct loss I calculated XYZ had suffered as a result of the bank's failure to include the break fee in its settlement statement. In addition, I recommended that the bank pay interest on that sum, \$1,500 towards XYZ's costs and \$1,000 for compensation for inconvenience. The complaint was settled on this basis.

CASE 18 – WHAT WAS THE REAL INTEREST RATE?

Mr and Mrs Q had a rural term loan and were unhappy that when their bank reviewed the farming operations from time to time, it sometimes added an additional margin to the advertised floating interest rate to compensate it for additional risk. The term loan contract terms allowed for this and Mr and Mrs Q decided to take their business to another bank.

Their new bank offered a loan package made up of a five-year term loan at a floating interest rate with no risk margin and an overdraft at the same interest rate as the term loan.

After the loan had been running for about three years, Mr and Mrs Q received a letter from their bank manager advising that the bank had changed its policy with regard to charges for rural overdraft facilities and that the interest rate on their overdraft would now be higher than the rate on the term loan. The term loan interest rate was also increased. Mr and Mrs Q noted that the new interest rate was higher than other banks' rates. They complained to their manager and were told that the bank had changed its policy and was now adding a margin. After being told by the bank that it would not reduce this margin, they complained to the Banking Ombudsman.

Later, during the course of the investigation, Mr and Mrs Q were given some information by the bank about its interest rate policy that was subsequently found to be incorrect. They voiced their concern about this discrepancy and formed the view that the bank was deliberately misleading both them and the Banking Ombudsman.

The Banking Ombudsman concluded that the loan contract between the bank and Mr and Mrs Q did not permit the bank to add a risk margin to the interest rate on the term loan. Effectively the bank had agreed that the interest rate would be the lowest rate it normally charged to its rural customers. She also concluded that the bank could not increase the overdraft interest rate above the term loan rate. She proposed that the bank should refund the overcharged interest. Both parties accepted the proposal, but there was disagreement about the date at which the bank had begun adding a risk margin and the amount of the margin.

Some time during the three years after the loan was first set up, the bank had changed its method of calculating the relevant floating interest rate. Mr and Mrs Q were of the view that from that time onwards they had been charged a risk margin, in contravention of the terms of their loan agreement. The bank was of the view that the risk margin had been added at a later date when it reviewed their business and decided to charge interest in accordance with a different point on its standard scale.

The bank provided the Banking Ombudsman copies of an internal policy document which included a detailed table of bank interest rates, including information about the calculation of these rates. The calculation methods were said by the bank to be commercially sensitive and were provided to the Banking Ombudsman on a confidential basis, as permitted by Paragraph 6 of her Terms of Reference. The bank also provided a summary of part of the information, showing the specific sections which affected the complainants, and agreed to release this summary to Mr and Mrs Q. They refused to accept it as genuine, believing it had been fabricated for the purposes of the investigation.

The Banking Ombudsman then undertook a review of rural term loan interest rates for several banks over the disputed period. Given the competitive nature of rural lending, it could be expected that different banks' rates would follow similar trends and provide a benchmark against which the movement of the relevant bank's rates could be assessed.

In making her formal recommendation, the Banking Ombudsman found that the bank had not added the risk margin at the time it changed its method of calculating interest rates, and the likelihood was that the margin had been added at the date specified by the bank. The bank had not, however, been able to supply an explanation of a substantial discrepancy at an earlier date between the rate charged to Mr and Mrs Q and rates generally charged to rural borrowers by other banks. The only available information about the bank's rates during the relevant period was part of the information that the bank required to be kept confidential. For this reason, the Banking Ombudsman recommended that the bank reimburse Mr and Mrs Q overpaid interest back to the date of the first appearance of the discrepancy.

Mr and Mrs Q remained of the view that the bank had fabricated evidence and generally acted in a misleading and dishonest manner, but reluctantly agreed to accept the recommendation.

CASE 19 – NOT IRRESPONSIBLE LENDING

Mr M wrote to me on behalf of his daughter, Ms M. He said he was concerned that the bank had provided Ms M with a credit card without properly checking his daughter's financial history. Ms M was a solo mother with health problems and on a low income. The Bank had, three months earlier, approved a home loan application and then offered her a credit card with a \$10,000 limit, which his daughter spent and was now unable to repay.

After obtaining Ms M's authority for her father to act on her behalf I commenced my investigation. As part of this process the bank produced a report, including a copy of the original loan application. This was in turn made available to Mr M. After consideration of the information available to the bank when the decision to lend was made Mr M considered that it had acted reasonably and could not have known that his daughter's financial circumstances had changed between completion of the loan application and the offer of the credit card. He advised he did not wish to pursue the matter any further and thanked both my office and the bank for taking the time to provide the information.

CASE 20 – PROVISION OF OVERDRAFT

Prior to leaving New Zealand Mr K opened a current account with a bank. As part of the standard package the account had a \$500 overdraft. While he was overseas his mother deposited funds into his overseas bank account. He thought that the funds were in his New Zealand bank account so he withdrew and spent the money. The foreign ATM through which he made the withdrawal did not give him an account balance so he was unaware that he was overdrawing his account.

When the bank commenced recovery action for the overdraft Mr K lodged a complaint. He said that the bank had no right to recover the money from him as he had not asked for an overdraft and was unaware that there was an overdraft on the account. He said that any transactions made in New Zealand in excess of his credit balance had been declined. In addition, Mr K considered that the bank had acted negligently in providing him with an overdraft when it had no assurance that he would be able to pay it back.

I formed the view that it was appropriate for Mr K to repay the overdraft. While Mr K's lack of knowledge about the balance of his account at the time he made the transactions might explain why he overdrawed the account, it did not affect his obligations to operate the account in accordance with the terms and conditions upon which the account was opened. He did not explain why, on discovering his mistake, he did not repay the overdraft using the funds in his overseas account.

I did not consider that the bank had acted negligently in providing Mr K with an overdraft. I observed that banks routinely provide young people with small overdrafts. There was nothing to suggest to the bank that Mr K was

a credit risk. I accepted the bank's submission that it would not have provided Mr K with an account if anything untoward had been revealed when it conducted a credit check. Mr K did not dispute this finding.

Mr K maintained that he did not apply for an overdraft with the account. The bank was unable to locate the account application form which would show categorically whether or not an overdraft had been applied for. Another way of determining whether an overdraft operated on the account would be to check if, before Mr K left New Zealand, any transactions had been declined when Mr K had exhausted the credit funds in the account. Mr K said this had been the case but provided no further details. The bank advised that without specific dates, given the large number of transactions which are processed every day, it was impossible to provide this information.

The bank's inability to provide either the account opening form or the other information did cast some doubt over whether or not the overdraft had been provided. On this basis I recommended that the bank waive all interest which had accrued on the overdraft if Mr K was prepared to repay the original debt. While the bank accepted my recommendation Mr K did not and chose to pursue his complaint through other legal channels available to him.

CASE 21 – MISLEADING ADVICE FROM A MORTGAGE BROKER

In this case Ms L complained that a mortgage broker, whom she had approached to arrange a home loan, had advised her, in response to a specific enquiry she made, that the cost of the early repayment penalty in her case would be approximately \$3,000. This advice was incorrect. A few months before Ms L had made her enquiries the bank had changed the way it calculated the cost of early repayment of fixed rate loans and had advised the broker by letter of the changes.

Approximately six months after arranging the loan, interest rates had fallen and Ms L enquired about refinancing at the lower rates. She discovered that the cost of early repayment would be approximately twice the amount she had been told by the broker. She complained to the bank about the misleading advice she had received from the broker, but the bank was not willing to remedy the situation. She therefore approached me for help.

Having considered all the evidence I came to the view that the broker was not the agent of the bank when arranging Ms L's loan. Accordingly, the bank could not be held responsible for the misleading advice she received from the broker about the cost of early repayment.

I also considered whether the bank had any responsibility to inform Ms L directly of its policy regarding early repayment fees. In this respect I had regard to the fact that the bank had instructed Ms L's solicitor to act for it in having the loan documentation signed. It later received a certificate from the solicitor that he had explained the nature and effect of the documents to Ms L. The bank therefore reasonably assumed that the solicitor would have explained the early repayment provisions to her.

In the circumstances, I concluded that the bank was not responsible for the situation in which Ms L found herself and did not uphold the complaint.

4 FRAUD & ROBBERY

I am seeing more and more cases where the complainant has been the victim of fraud in circumstances where he or she believes the bank has some responsibility for the loss.

Non-card fraud

In most cases the bank can only be held responsible for loss when it has been at fault in some way, either in creating the opportunity for fraud to occur or by some failing on the part of its staff or systems to effect the normal precautions against fraud (*Cases 22 and 23*). In one case, a victim of a bank robbery complained about the lack of security in the branch as well as about misleading advice on the service offered (*Case 24*).

Case 25 was a particularly unfortunate and complex case which brought into question the practice of banks permitting loan documentation to be taken away for signature by one of joint borrowers. It is pleasing that, with goodwill on the part of both banks concerned, it was possible to arrange a negotiated settlement with the fraud victim.

Card fraud

Five years ago, in 1995-96, I considered 15 cases of fraud involving the unauthorized use of a debit or credit card. The highest claim was for just over \$3,000.

In the year to 30 June 2001, I investigated 71 similar cases. In 19 of these cases, the claim was over \$5,000 and in 4 of them it was over \$20,000.

It is clear that not only is there an increased level of fraud involving cards, but the sums involved are considerably greater.

A customer's entitlement to reimbursement when there has been the unauthorised use of a debit or credit card, is largely governed by the provisions of the Code of Banking Practice. Even if the bank has not been at fault in any way, it must reimburse the loss provided its customer has observed the terms

and conditions on which the card is issued and those terms and conditions comply with the requirements of the Code of Banking Practice.

The general obligation of the cardholder is to take reasonable care of the card and PIN and to report any loss of the card or compromise of the PIN without undue delay. Each bank has its own terms and conditions on which it issues cards, and these differ slightly in detail.

If a bank wishes to exclude liability in all those circumstances where such exclusion is permitted by the Code of Banking Practice, it is important that its own terms and conditions make this absolutely clear. If, for example, a bank does not wish to reimburse cardholders for loss caused through the choice of an unsuitable PIN, such as a birth date, then its terms and conditions must contain a specific exclusion to this effect. It is not sufficient to include a warning about the choice of unsuitable PINs without any explanation of the effect of such a choice on liability for loss. A similar situation arose in *Case 26*.

A new problem that has arisen out of card fraud concerns the situation where a cardholder's card has been lost or stolen along with PIN information and the account number. The possession of these three items enables an offender to deposit stolen or forged cheques to the account and then (if the bank permits its customer to draw against uncleared funds) to withdraw the proceeds almost immediately through an ATM. *Case 27* illustrates the approach to such cases.

The majority of cases that come to me show a clear breach by the customer of the terms and conditions on which the card was issued. *Case 28* is a good illustration of a case of this kind.

While cardholders have an obligation to observe the terms and conditions on which their card is issued, banks also have obligations under the Code. In *Case 29* there is discussion of the weight to be given to

the obligations of bank and cardholder in circumstances where a bank has failed to advise its customer about PIN choice.

Finally, it is all too easy for bank staff to assume that customers prefer to use electronic banking and to

issue debit cards and PINs almost automatically. As *Case 30* illustrates, there are circumstances in which this is not good practice and may unnecessarily expose the customer to the risk of fraudulent activity on an account.

CASE 22 – A WITHDRAWAL FROM AN ACCOUNT IN ANOTHER NAME

Mr C operated three accounts with his bank. There were two term deposit accounts, and one savings account. Mr C provided the Bank with written authority for his sister (Mrs S) to operate the savings account only.

A little later Mrs S opened an additional term deposit account with the bank in Mr C's name and signed the new account authorities so that she could operate that account herself. Mr C was not aware of the account and did not consent to it.

Shortly afterwards Mrs S transferred some money from one of the original term deposit accounts, which had matured, into the new term deposit account. A few days later, she withdrew the money from the new term deposit account, apparently by telephoning the bank with instructions to make the withdrawal, and to send the money by telegraphic transfer to her account with a different bank in the UK.

Later, Mr C discovered what had happened, and having complained to the bank, then brought his complaint to the attention of the Banking Ombudsman.

In the absence of any statutory exception, it is accepted that a bank account can only be operated by the account holder or with his or her authority. To allow someone other than the account holder to access the account is breach of the customer's mandate. The one exception to this rule is when the account holder specifically provides another person with express permission to operate an account. Mr C did not provide Mrs S with permission to open a new account, nor to transfer the funds from one of the other term deposit accounts into the new account.

The Banking Ombudsman considered the bank had not followed Mr C's instructions. It should not have allowed Mrs S to operate the term deposit account and therefore it ought to return the money to Mr C, together with interest calculated at the term deposit rate from the date it had been withdrawn until payment was made. She also recommended that Mr C should be compensated for the inconvenience that the bank's actions caused him.

The Banking Ombudsman expressed some concerns about the bank's actions in permitting Mrs S to open an account in Mr C's name without instructions from Mr C, but as the events in question took place before the Financial Transactions Reporting Act 1996, she did not take this aspect of the complaint further.

The bank accepted the suggested recommendation, and settled the complaint on that basis. With the agreement of the Banking Ombudsman it reserved the right to take steps to recover the unauthorised withdrawal from Mrs S.

CASE 23 – FRAUD WITHIN THE FAMILY

Mr D had a son and a daughter and had set up term deposit accounts, one in his and his son's names and the other in his and his daughter's names. Both account mandates required the joint signatures of the account holders to operate the accounts.

In December 1999 Mr D's son withdrew all the funds from his joint account, claiming that his father had died. Bank staff did not require production of a death certificate before actioning the withdrawal. In January 2000 Mr D's son and daughter (then aged 17 and 15 respectively), visited the bank and, after advising the staff that their father had died, the daughter withdrew all the funds from her joint account. Again the bank did not require production of a death certificate.

The bank offered to reimburse Mr D half the funds withdrawn. Acting on legal advice, he did not accept this offer. He considered that both accounts were joint accounts and that the legal nature of joint ownership of property is that both co-owners have ownership and possession rights of the whole of the property, not half each. The bank later offered to refund the funds in full on condition that Mr D took legal action against his son and daughter. This offer was also rejected. The son was currently in prison and there was little chance of a reparation order being made against either him or his sister.

In reporting to me on the complaint, the bank appeared to believe that it had no liability because the complainant's children had set out to defraud both it and Mr D. In my view the withdrawals by the children were only possible because of the bank's failure to discharge its obligation to check the truth of the children's claim.

The question I then had to consider was whether the bank's error caused Mr D a direct loss in the sum of the funds in the two joint accounts thereby entitling him to compensation. I was of the view that provided Mr D was able to produce evidence to establish that the funds paid into the two accounts were his own property and provided the bank was prepared to accept that evidence, the bank should reimburse him the full amount of the funds in the two accounts plus interest up to the date of reimbursement. In the absence of evidence to establish that the funds paid into the accounts were Mr D's property, I considered that the bank should reimburse half the amount wrongly paid to the children. I was also prepared to recommend reimbursement of legal costs incurred by Mr D up to the time the complaint was lodged with my office.

The bank accepted my views on the complaint. Mr D produced evidence to satisfy the bank that the funds were his property and it refunded to him the full amounts withdrawn from each joint account together with interest on those amounts. It also refunded the legal costs he had incurred up to the time he lodged his complaint with my office.

CASE 24 – A SAFE DEPOSIT LESS SAFE THAN EXPECTED

Mr and Mrs L arranged a safe custody box with the bank for the storage of family heirloom jewellery and valuable documents. The box was stolen during a robbery at the bank and Mr and Mrs L sought compensation for their loss. The bank denied liability for the loss on the basis of the terms and conditions of the safe custody agreement. Under that agreement the bank had no liability in relation to the loss of the box or its contents except to the extent that the Consumer Guarantees Act 1993 might apply. The bank did not consider that Act applied in a situation where a box was lost as a result of a robbery rather than any act or omission on its part.

Mr and Mrs L, whose understanding of English was very limited, were concerned at the level of the bank's security. They said at no time had the bank advised them to obtain insurance for the contents of the safe custody box. They had assumed that their valuables would be safe in the bank. They also said that they were given no explanation about the safe custody agreement when they made the safe custody arrangements and in particular were not told of the recommendation that the owner of the contents of a safe custody box should arrange insurance. They said they had simply been asked to sign the form that had been completed by a bank staff member.

After considering the facts in the case, reviewing the videotape of the robbery and inspecting the physical layout of the bank, I formed the view that that there were two major elements to this dispute which I had to consider.

The first concerned the adequacy of the explanation given to Mr and Mrs L when they entered into the safe custody agreement and the second was whether the bank contributed to or caused their loss by acting negligently or failing to act in accordance with usual banking practice.

I noted that the promotional brochure describing the bank's safe custody services stated that the bank would only accept liability, if loss or damage was caused "*by a negligent act of the bank*". On the other hand, the safe custody agreement stated that the bank was only liable if it had been **grossly** negligent. On this basis, the information as to the level of the bank's liability in its promotional brochure appeared to be misleading and possibly in breach of the Fair Trading Act 1986. Accordingly, to the extent that the terms of the agreement were inconsistent with the brochure, the brochure prevailed and the bank was liable if loss or damage was caused by a negligent act on its part.

Both the brochure and the agreement stated that the customer needed to arrange his or her own insurance. While it may not have been incumbent on the bank officer attending the complainants at the time they made the safe custody arrangements to explain every clause in the agreement, it was important to ensure that they understood the extent to which the bank would accept liability for loss and that they should insure their valuables if they considered it desirable to do so. By the same token, Mr and Mrs L had an obligation to ensure that they read and understood the terms of the agreement before signing it.

On the question of negligence, having inspected the safe deposit facilities at the branch concerned, I concluded that the secure storage facility did not provide the level of protection that was represented in the bank's promotional brochure. In particular, the brochure indicated that the same level of protection would be provided for customers' valuables as for the bank's own supplies of cash. In this case, the robbery had been committed with apparent ease in less than three minutes without having to threaten or obtain the forced co-operation of bank staff. The cabinet containing the safe custody boxes was quite flimsy and appeared to have been forced easily. The cabinets containing the bank's own cash and valuable items were constructed of heavier duty metal and had been left intact. I therefore concluded that the bank failed to provide the level and nature of security it purported to offer for safe custody deposits.

Clearly, irrespective of the level of security offered, armed robbers can force bank staff to deliver up safe custody deposits and in any event, the safety of its staff is quite properly a bank's first priority in considering measures to protect against robbery. However, the circumstances of this particular case were such that the low level of security considerably assisted the robbers to complete the robbery and the robbers targeted the lighter weight metal cabinet containing the safe custody boxes. I therefore concluded that the bank should compensate Mr and Mrs L for their loss. The bank accepted my finding in this case.

CASE 25 – SEXUALLY TRANSMITTED DEBT – A BAD CASE OF FRAUD

Mr T and his wife had a housing loan from bank A secured by way of mortgage over their jointly owned property. Mr T also had a savings account with bank A.

Some years after taking out the loan Mr T arrived home one day to find that his wife had disappeared. She had left him a note apologizing for the "financial mess" she had left behind.

To his dismay Mr T discovered that his wife had developed a drug dependency. In order to finance the purchase of her drugs she had, over a period of eight months, obtained six top-ups totalling \$48,000 on their housing loan. On each occasion the bank officer had given Mrs T the loan agreement for her to take home for Mr T to sign. Mrs T had forged Mr T's signature on the forms and returned them to the bank.

It was also discovered that Mrs T had withdrawn over \$10,000 from Mr T's savings account at first by forging his signatures on the withdrawal slips and later by having her name added as a signatory to the account following a suggestion from the bank officer.

To add to his problems Mr T also found out that Mrs T had obtained a Mastercard credit card in his name from another bank, bank B, and had used the card to make substantial cash withdrawals from ATMs. The debt on the account had accumulated to over \$22,000. Several years earlier Mr T had paid the balance owing on the card, destroyed it and had told the bank to close the account. The bank had, however, sent him a replacement card in the mail. The card had been intercepted and used without his knowledge by Mrs T. Mrs T had also obtained access to a Visa card Mr T had with bank B and had used this card (although to a far lesser extent) to obtain cash withdrawals. Mrs T had deposited money into the Visa card account so that when Mr T checked the balance on the account he would not notice the cash withdrawals she had made. The deposits had come from the top-ups she had obtained on the housing loan without Mr T's knowledge.

In the cases of both banks Mrs T had intercepted bank statements in the mail so that Mr T did not see them.

Mr T complained about the actions of both banks to the Banking Ombudsman.

Bank A maintained that Mr T was liable for the full amount of the housing loan, including the "top-ups" obtained fraudulently by Mrs T, pursuant to the terms of its "all obligations" mortgage, even if that eventually led to a mortgagee sale of the property.

The Banking Ombudsman accepted that, on the face of things, bank A was entitled to rely on the terms of its mortgage. On the other hand, when considering what was fair in all the circumstances, it was arguably most unfair that Mr T should bear the responsibility for Mrs T's fraudulent borrowing. It was of concern that Mrs T had been able to obtain loan "top-ups" of over \$48,000, or nearly as much again as the original loan, in the space of eight months and against a security property with a government valuation of \$112,000. The Banking Ombudsman also had regard to the results of a bank survey she had conducted which tended not to support bank A's view that it was usual for banks to allow customers to take loan documents for signing outside the branch.

The Banking Ombudsman formed the preliminary view that a fair resolution to the complaint against bank A would be for settlement on the basis that Mr T retained a "protected amount" to the value of his half share in the equity of the property at the time that Mrs T began her fraudulent activity. She then considered the question of contributory fault on the part of Mr T. Although Mr T had relied on Mrs T to manage the household finances, he still should have looked at bank statements from time to time both on the current account from which loan payments were being made and on the loan account. Had he done so he would or should have immediately noticed that the loan principal was far higher than expected. The Banking Ombudsman assessed the level of his contributory fault at 10%, thus reducing his "protected amount" in the house.

After considerable negotiation between Mr T and bank A and having obtained an updated valuation of the jointly owned property it was agreed that Mr T would refinance the housing loan with another financial institution and that bank A would, in effect, write off a sum of about \$12,000. It also agreed to reimburse Mr T for the \$10,000 withdrawn without his knowledge or authority from his savings account. Mr and Mrs T were also to close all accounts they held with bank A. Mr T's complaint against bank A was settled on this basis.

After considering the evidence in Mr T's complaint against bank B, the Banking Ombudsman found that Mrs T had been able to use the Mastercard without Mr T's consent or knowledge and that a request to close the account had been received by the bank in September 1998 at which time the balance of the account was in credit. The bank had failed to close the account at that time. All of the current outstanding debt on the account accrued after October 1998 and thus after the bank had received a firm instruction to close the account. The

Banking Ombudsman therefore concluded that bank B should write off the total accumulated balance, including all interest and charges, on the Mastercard account.

The Banking Ombudsman found that Mr T also had absolutely no idea that Mrs T was accessing his Visa account and saw no reason in principle to treat the fraud on the Visa account any differently from the fraud on the Mastercard account. However the one main difference in this instance was that Mr T knew that the Visa account was operational and the Banking Ombudsman considered that he should have checked his account statements from time to time. Had he done so he would have discovered the use of the account by Mrs T. She assessed the degree of Mr T's contributory fault at 50% and proposed to recommend that the bank write off half of the sum, approximately \$1,850, from the Visa account.

Both Mr T and bank B agreed to settle his complaint on the basis proposed by the Banking Ombudsman.

CASE 26 – LATE NOTIFICATION OF UNAUTHORISED TRANSACTIONS

Mr and Mrs A's complaint concerned unauthorised transactions on their Visa card whilst they were living in Europe. Prior to departing New Zealand in 1994 they arranged for their son to manage their bank accounts.

In November 1997 the Visa card was stolen. Mr and Mrs A reported the theft to the bank within three hours of its occurrence.

In 1999 Mr and Mrs A returned to New Zealand and upon reviewing statements held by their son discovered over \$2,000 in unauthorised Visa card transactions that had occurred in 1997. When notified of the disputed transactions, the bank declined re-imburement on the basis that they had not reported the unauthorised transactions to the bank within sixty days, as required by the account terms and conditions of use and the Visa card Rules and Regulations. Mr and Mrs A rejected the bank's decision on the basis that the terms and conditions did not state that they would be held liable for the disputed amounts if unauthorised transactions were not reported to the bank within sixty days.

The Banking Ombudsman found that the customer contract, as set out in the account terms and conditions of use, is entirely separate from the contract between the bank and Visa International as set out in the Visa card rules and regulations. Consequently the Visa card rules and regulations have no direct relevance to the rights and obligations between a customer and the bank. Furthermore, the bank's conditions of use did not specify that the assumption by the bank for losses arising from disputed transactions is contingent upon notification of such transactions to the bank by the customer within sixty days. Nor does the Code of Banking Practice place any requirement on a bank customer to monitor card accounts for unauthorised transactions.

The Banking Ombudsman proposed that the bank refund Mr and Mrs A their total loss, less the \$50 cardholder's liability. The complaint was settled on that basis.

CASE 27 – UNCLEARED CHEQUE FUNDS NOT PART OF AVAILABLE FUNDS

Ms Q received her bank statements and discovered a large number of fraudulent transactions had been conducted on her account. She also realised her card was missing. She had used it to make an ATM withdrawal about a week earlier and had not needed to use it since then.

Ms Q's bank statements revealed the first disputed transaction was on a Sunday. Two days after her own last withdrawal, \$10 was withdrawn via EFTPOS. On Monday \$2,200 was deposited by cheque into Ms Q's account. On Tuesday \$1,500 was withdrawn and another cheque for \$4,900 was deposited. On Wednesday \$840 was withdrawn. On Thursday a further \$1,500 was withdrawn and the first cheque was dishonoured as stolen. On

Friday \$1,160 was withdrawn. On the following Monday the second cheque was also dishonoured as stolen. During this time Ms Q's own pay continued to be credited to the account and was the only cleared funds in the account.

The bank declined Ms Q's claim for reimbursement on the grounds that the offender had the card, PIN and account number. The bank was particularly concerned that she had selected an unsuitable PIN (her husband's birth date), failed to take reasonable care of the card and delayed in notifying the loss of the card to the bank. The bank said it had made a decision in the exercise of its commercial judgement to allow access to the uncleared funds represented by the proceeds of the stolen cheques; it confirmed that there was no pre-arranged credit. It required Ms Q to repay the overdraft created by the dishonour of the cheques.

In the circumstances of the case Ms Q's selection of her husband's date of birth as a PIN was unlikely to have contributed to the loss. I was, however, concerned that Ms Q did not notice that her card was missing. She usually used her card early in the week and I was surprised that she had not done so on this occasion. I considered it would have been reasonable for her to notice the card was missing and formed the view that she had unreasonably delayed in notifying the loss of her card. I was also concerned that she did not appear to have taken reasonable care of the card.

Although Ms Q had contributed to the loss by the delay in reporting the card stolen, in the absence of fraud her contract with the bank limited her liability to the maximum amount she would have been **entitled** to access during the relevant period. Ms Q's contract with the bank stated that she had no entitlement to draw against uncleared funds. The bank allowed her to do so only at its discretion. Her maximum liability was therefore the original balance of her account plus any cleared credits to her account during the relevant period. The bank had assumed the risk in this situation and it was my view that it ought to refund the full amount stolen, less the cleared funds in her account. Both Ms Q and the bank accepted my decision.

CASE 28 – FRAUD NOT A LIKELY EXPLANATION OF WITHDRAWALS

Mr S discovered that a number of unauthorised withdrawals had been made from his bank account, but said that the card had never left his possession. He had also never told anyone his PIN, written it down anywhere or based the PIN on personal information. The withdrawals were made typically around 9 pm from a number of bars and brothels around town. He insisted that he had not made the transactions, and his mother, Mrs S, advised that on at least one of the occasions her son was staying at her home. In between the disputed transactions were withdrawals which Mr S said that he had made.

The bank's electronic records showed that it was definitely Mr S's card used to make the transactions and that the PIN was entered correctly on the first attempt. Although I did not agree that the bank's records were absolute proof that the customer had either made the transactions himself or had allowed someone else to use his card and PIN it was my view that in the circumstances of the case this was the only reasonable explanation.

Mr S suggested that his card had been removed from his wallet, replaced with a replica card, and then used to make the transactions. I did not consider this explanation as likely. The pattern of offending did not fit the usual opportunistic crime. In addition Mr S's bank statements revealed that thousands of dollars had been withdrawn from Mr S's account from the same locations at approximately the same time of day during the previous three months. These transactions were not initially disputed by Mr S or included in his complaint to the police. I also considered that a thief would be unlikely to risk discovery by stealing and replacing the card on numerous occasions as suggested by Mr S.

I recommended that the complaint be withdrawn.

CASE 29 – THE IMPORTANCE OF ENSURING THAT CUSTOMERS ARE PROPERLY ADVISED ON SUITABILITY OF PINS

Ms P's wallet containing her card was stolen from her home. The wallet also contained other cards and Ms P's driver's licence. Ms P discovered the theft the following day and reported the loss to the bank. A stop was placed on the card but by this time the thief had already stolen over \$6,000 from Ms P's accounts by using the card to make cash withdrawals from ATMs and large EFTPOS transactions.

The bank declined to reimburse Ms P for her loss. It transpired that Ms P had used her year of birth as her PIN and the bank said that in doing so she had breached the terms and conditions of use for the card. Ms P said that she had had her EFTPOS card for a number of years but could not recall ever having received a warning from the bank not to use her date or year of birth as her PIN, not even when she visited the bank to load a new PIN onto her replacement card, following the theft.

The Banking Ombudsman noted that pursuant to clause 5.3.4 of the Code of Banking Practice the bank had an obligation to advise customers as to what PINs are unsuitable, for example, birthdates. In order to make such advice meaningful, the advice should be given, or at the very least repeated, at the time a customer calls into the bank branch to select a PIN. She was concerned as to the extent of the advice (if any) Ms P received from the bank regarding PIN selection. It was clear that Ms P did not receive a verbal warning at the time of selecting her PIN. In the Banking Ombudsman's view, in order to properly "advise" a customer as to unsuitable PINs, the bank should either specifically draw the customer's attention to the relevant clause in the terms and conditions of use when sending the customer a copy of the terms and conditions of use and/or verbally advise the customer at the time of selecting a PIN what numbers should be avoided when selecting a PIN. There was no evidence that any of this had been done in this case. Whilst it could be argued that Ms P had an obligation to read the terms and conditions, which contained advice as to what are unsuitable types of PIN, the Banking Ombudsman did not consider that this obligation was as high as the bank's obligation to advise a customer at the actual time of PIN selection of the types of PIN to avoid.

The Banking Ombudsman proposed to recommend that Ms P's complaint be settled by the bank reimbursing her for 75% of the loss. Ms P and the bank agreed to settle the complaint on this basis.

CASE 30 – NO NEED FOR A PIN

This case concerned the unauthorised use of a bank card. The card was stolen from Mrs X, an 85 year old woman, along with her purse which also contained her PIN written down in jumbled form along with the four digit birth dates of her grandchildren. The theft was not noticed until the following day when the bank and the police were notified. In the meantime, the thief, after one unsuccessful attempt, had used the card to withdraw a total of \$6,594.50 from Mrs X's current and savings accounts. The withdrawals exhausted the funds in both accounts and overdraw her current account by \$222.55. Her son-in-law complained on her behalf to the bank, seeking reimbursement of the amount of Mrs X's loss. The bank declined to reimburse the loss apart from the unauthorised overdraft of \$222.55.

The points made in support of the complaint were:

- The bank had issued the bank card to Mrs X. She had never requested a PIN. She had never used the card at an ATM or EFTPOS outlet. The only reason she required a card was for identification purposes when writing out a cheque.
- The bank had failed to give Mrs X adequate advice on the use of the card or exactly what the PIN was for.
- In the circumstances it was unrealistic of the bank to expect her to remember her PIN without writing it down.

For its part the bank relied on the terms and conditions of use for the card which provide that the maximum customer liability limit of \$50 does not apply where the customer has kept his or her PIN in a form that can be readily identified as a PIN. It believed Mrs X had breached this provision. Although the PIN number may have been recorded in a jumbled fashion, it had only taken the thief two attempts to access the account. The bank noted that Mrs X had selected the PIN and had agreed at the time of selection to protect her PIN. It also denied that it had required her to have a PIN.

This case highlighted the problems many elderly people face in PIN selection. Mrs X had selected her year of birth in reverse. While this could be said to be an unsuitable PIN under the terms and conditions of use of the card, the number was not, in fact, her year of birth.

Of greater concern was the fact that Mrs X had been issued with a PIN at all, given that she did not need to use the PIN function on the card. All she required was a card for identification purposes when cashing cheques.

Had the bank staff who issued the card given a little more care and thought to Mrs X's requirements, they would have realised she did not need a PIN. At the very least, they should have been aware that she did not use ATM and EFTPOS facilities and should have discussed the need for a PIN with her. In failing to do so, I considered the bank had failed to comply with its obligations under clauses 1.7.2(i), 5.1.1 and 5.1.4 of the Code of Banking Practice.

Furthermore, it did not appear that Mrs X had received any verbal advice regarding the choice of PIN or any warning that the PIN should not be written down. This was a breach of the bank's obligations under clauses 5.3.1 and 5.3.2 of the Code of Banking Practice. I was also concerned that both her cheque and savings accounts were linked to the card. There was no evidence to suggest this had been discussed with her in the context of the greater risk to which she was exposed by having more than one account linked to the card.

I came to the view that the bank should reimburse Mrs X for the amount of her loss, less the \$222.55 already refunded and less the customer's \$50 liability. This view was based on my concerns that she had been issued with a PIN when she had not requested nor required one. Furthermore, she had not received any verbal advice about the choice of a PIN nor any warning that the PIN should not be written down. Finally, it was clear that had a PIN not been loaded on to her card the fraud would and could not have taken place.

Although the bank made some further representations in support of its position, these did not cause me to alter my view and I therefore recommended that the bank settle the complaint by reimbursing the sum of \$6,321.95.

5 CHEQUES

It is increasingly common to receive complaints that a bank has dishonoured cheques when there are sufficient funds in an account to cover them. Often a customer has become confused about cheque clearance times, or has expected funds transferred electronically to be immediately available in circumstances where they too are subject to a clearance period. In *Cases 31 and 32* the customers' problems were compounded by the bank's inconsistent administration of their accounts. When there are uncleared funds in an account, honouring

cheques drawn in excess of available credit is not unnaturally interpreted by the customer to mean that the funds in the account are clear and available, especially if the bank usually enforces the credit limit on the account.

Wrongly dishonouring a customer's cheque can have a seriously damaging effect, particularly on a small business. I have been concerned to find some banks acknowledging that cheques have been wrongly dishonoured but considering the damage to

the customer can be remedied by an apology and by explaining the mistake to the payees of the dishonoured cheques. There may be cases where such action is sufficient, but *Case 33* is more representative of those which come to my office. In

some cases the wrongful dishonour of a cheque may amount to defamation, and it is always likely to cause considerable embarrassment. Many suppliers will refuse to accept cheques after a dishonour, even if an explanation has been provided.

CASE 31 – CHEQUES INCONSISTENTLY AND WRONGLY DISHONoured

JKL Ltd had had a number of cheques dishonoured during three periods in the latter half of 1998. The dishonours resulted from its bank cancelling the company's overdraft limit without notice, dishonouring cheques drawn against uncleared funds, and dishonouring cheques drawn against a cheque cleared by the bank by way of a special answer.

A bank is exercising its commercial judgement when deciding whether or not to provide an overdraft facility or to allow a customer to draw cheques against uncleared funds. Such decisions are therefore outside my jurisdiction in terms of paragraph 18(b) of my Terms of Reference. However, in this case I came to the view that the bank's actions involved maladministration.

Due to a breakdown in communication within the bank, JKL Ltd was not advised that its overdraft facility had been withdrawn. Although this was acknowledged by the bank and reasonable steps were taken to remedy the situation, the company lost access to two suppliers and it took some time to locate alternatives.

I was also concerned that the bank was inconsistent in its decisions to dishonour fourteen cheques drawn against uncleared funds in November 1998. Some were dishonoured and some were not. Again it appeared that part of the problem arose from unclear communication between the bank and the company.

Finally, four cheques were dishonoured because the bank had not recorded the fact that in depositing a cheque in December 1998, JKL's director had requested and obtained a "special answer" on the cheque. A special answer ensures that the customer is advised whether a cheque has been paid the day after it is presented and does not have to wait for the normal five-day cheque clearance period. While the bank believed JKL should have alerted its branch to the fact that the funds were cleared, in my view it was not the customer's responsibility to do so nor could it have been expected to know that such advice was necessary.

I therefore concluded that the bank should refund the dishonour fees of \$450 on the eighteen dishonoured cheques, and pay \$500 compensation for inconvenience. The complaint was settled on this basis.

CASE 32 – MORE DISHONoured CHEQUES

This complaint arose from a bank's decision to dishonour a number of cheques drawn by its customer, Mr X. He believed he had sufficient funds to cover the cheques. In support of this view, he drew attention to various deposits he had made to his account which he said were by way of cash or "cash transfer" during the period in question.

In explaining its actions the bank advised that Mr X had a \$500 overdraft facility on his account, but that he had regularly exceeded that limit. At the time the decisions were made to dishonour the cheques in question, the account was in excess of the overdraft limit. Although funds had been deposited to the account, at the time the decisions were made to dishonour the cheques the funds (with one exception) were not cleared. Detailed examination of the account transactions showed that most of the deposits to Mr X's account had been cheques,

not cash as he suggested. When cheques are deposited into an account, the funds are not immediately available to the account holder. It takes up to five working days to clear the funds.

In this case, one deposit had been a transfer from Mr X's savings account with the bank and those funds should have been immediately available to him. The bank acknowledged this error. However, given the balance in the account, even if the bank had treated the deposit as cleared funds, the funds in the account would only have covered one of the cheques in question. The bank therefore reimbursed the \$25 dishonour fee charged for one cheque.

My assessment of the information led me to the view that, with the exception of the cheque referred to above, the bank's decisions to dishonour the cheques in question were justified. I was, however, concerned about inconsistencies in the bank's management of Mr X's account. Although it was entitled to dishonour most of the cheques to which the complaint related, during the same period it had honoured other cheques even though they caused the account to exceed the overdraft limit by similar amounts to the dishonoured cheques. Although in this case I did not uphold the complaint, it is not surprising that Mr X became somewhat confused about the availability of cleared funds in his account.

CASE 33 – COMPENSATION WHERE CHEQUES WERE WRONGLY DISHONoured

Mrs S had a rural business. She had an arrangement with her bank to collect cheque books for her business from the local branch. She visited the bank several times to collect a new cheque book, but was advised on each occasion that one was not in stock but would be ordered. Eventually she was told that her cheque books had been misfiled and that there were three books at the branch. She collected all three.

The next month Mrs S wrote a number of cheques for her creditors from a cheque book which was not one of those she had recently uplifted from the branch. A few days later she started receiving calls from her creditors advising her that the cheques had been returned, having been stopped by the bank. This caused her serious embarrassment.

Mrs S then attempted to find out why the cheques had been stopped. She called her branch a number of times but her calls were not answered. She therefore visited the branch and spoke to a teller who found that the three cheque books which had been misfiled had been stopped by the bank as it was thought they had been lost in the mail. The cheque book she was using had also been stopped. Arrangements were made to remove the stop from that cheque book and the others were destroyed. Mrs S then reissued the cheques that had been stopped. While she explained to the payees that the cheques had been stopped as a result of a bank error, she felt that she was not necessarily believed. A few days later, she discovered that one of her reissued cheques had been stopped. The bank was unable to explain why this had happened. A further cheque was also stopped and the payee referred the matter to a collection agency.

Eventually Mrs S made a formal written complaint to the bank about its management of her account. In its reply the bank acknowledged that the cheques had been dishonoured as a result of its error. It noted that it had apologised to her in writing, had refunded the dishonour fees and sent letters of apology to the recipients of all the dishonoured cheques. At that point the bank also offered her a goodwill payment of \$250 in full and final settlement of her claim.

Mrs S rejected the bank's offer. She did not believe the bank had taken due account of the effect its actions in stopping the cheques had had on her reputation within the industry in which she worked.

The bank did not dispute its responsibility. It said it greatly regretted its error and the consequences of it. However, it did dispute the quantum of Mrs S's claim. It considered the steps it had taken to rectify its error were reasonable.

It was clear that Mrs S had spent a considerable amount of time pursuing a solution to her problem with the bank and this must have had some impact on her business. I was therefore prepared to recommend that in addition to accounting and legal costs and travelling expenses, amounting to \$358.90, the bank should also make a 50% contribution to her personal costs in terms of telephone calls, letters written and lost income.

On the question of a reasonable payment to compensate Mrs S for the inconvenience she had suffered as a result of the bank's error, I accepted Mrs S's submission that both her own reputation and that of her business had suffered as a result of the bank's placing a stop on her cheques. A bank can be liable in defamation for dishonouring a cheque in such a way as to suggest that the drawer has insufficient funds when this is not the case. In *Hill v National Bank of New Zealand* [1985] 1 NZLR 736, Eichelbaum J commented as follows when discussing the notation "Refer to Drawer" on a dishonoured cheque:

"I have concluded that dishonour of a cheque remains a serious matter and that the majority of reasonable people would think that in all probability the bank had done so on good grounds founded on some circumstances discreditable to the drawer of the cheque."

In this case, there were stops placed on the cheques. Mrs S said this action defamed her as the payees of those cheques assumed that she had issued the stop order, presumably in breach of her contracts with the payees. In considering whether the reference on the cheques is capable of defamatory meaning, I had regard to the test outlined in *Hill*, namely:

"The test to be applied is that of the fair and natural meaning which would be given to the words by reasonable persons of ordinary intelligence, in the circumstances in which the writing was published."

In my view a reasonable person would consider that the customer had placed a stop order on the cheques. The payees did not receive any prior explanation from the drawer as to the reason for the stop order, and in the absence of an explanation, could reasonably assume that the drawer did not intend to pay for the goods or services received. This could have serious consequences for a business person.

On the other hand, the bank had done what it could to correct the mistake it had made. In assessing compensation I am concerned with the effect of a bank's actions on a complainant rather than the extent of a bank's wrongdoing. I have only limited powers to award compensation for inconvenience and if the bank had not taken action to limit the damage done by its stopping of the cheques, I would be contemplating compensation considerably greater than I have power to award.

In this case, despite the bank's efforts to control the damage to Mrs S, it was more than likely that doubts about her financial standing had circulated beyond the recipients of the stopped cheques. I was therefore satisfied that she had suffered and continued to suffer substantial apprehension and embarrassment. I recommended that the bank pay compensation for her direct losses and \$2,000 for the inconvenience she suffered as a result of the bank's error.

6 FOREIGN EXCHANGE

Immigration, overseas travel, trade and investment all lead to increased dealings in foreign currency. No significant cases were investigated this year in connection with business dealings in foreign currency, although some of the issues that arose in connection with a personal banking could equally well apply in the business context.

Most personal customers do not deal frequently in foreign currency and it is particularly important that banks make their processes and policies clear to such customers (*Case 34*).

Case 35 is also a case where inexperienced customers were involved and were provided with

travellers' cheques that proved to be almost impossible to use on their holiday.

Mistakes sometimes occur in converting foreign currencies into New Zealand currency and if a customer receives an overpayment of this nature, it is considered a payment made by mistake. Accordingly the customer is usually liable to repay the overpaid amount. If, however, the bank is responsible for the mistake it should arrange to

accept payment by affordable instalments and/or compensate the customer for the inconvenience involved as in *Case 36*.

Finally, *Case 37* concerns an unusual type of investment in foreign currency, and not one that is to be recommended. The customer was fortunate in that a thorough investigation resulted in the discovery of information that had not surfaced during the bank's initial enquiries.

CASE 34 – THE DIMINISHED DEUTSCHMARK

Ms E had an account with a New Zealand bank. While Ms E was away on holiday, a relative in Europe forwarded a substantial remittance in deutschmarks to her New Zealand dollar account. The incoming payment message directed to the New Zealand bank contained full details of the customer's name and bank branch account number, and clearly requested the bank to credit Ms E's account.

When the bank received the funds, it firstly attempted to contact its customer to seek confirmation that the remittance should be converted to New Zealand dollars and credited to her account. It received no reply to a phone call, and left a voicemail message to contact a nominated person at the bank.

After seven days had elapsed and the bank had been unable to contact its customer, it then converted the funds to New Zealand dollars, crediting the account as directed on the remittance advice. The amount credited was less than it would have been if converted to New Zealand dollars on the date of arrival.

When Ms E returned from her holiday she requested the bank for an explanation of the late deposit. She was told that it was bank policy to obtain approval from customers to convert funds for substantial incoming remittances. The bank declined to reimburse the estimated foreign exchange loss.

When considering the complaint and arriving at a suggested resolution, the Banking Ombudsman considered that the Code of Banking Practice provides that banks will *"make timely and adequate provision of information to help (customers) understand how bank accounts and banking services operate"* and also that banks will *"provide you with details of exchange rates and commission charges that will apply, or if this is not possible at the time, the basis on which the transaction will be completed"*.

The bank had submitted that it was policy only to convert monies after the customer gave his or her approval, since in the past customers had made claims to the bank for losses sustained where conversion had been effected without approval. It agreed that it had not publicised the policy.

The bank's policy was a sensible one, but it needed to make it known to its customers, who could otherwise be disadvantaged. In this particular case the Banking Ombudsman was also of the view that where the payment advice contained explicit instructions to lodge proceeds to a New Zealand dollar account, then if the bank was unable to contact its customer it could reasonably be expected to give effect to those instructions. Given that there was no ambiguity in the instructions, the Banking Ombudsman proposed that the bank should reimburse the customer with the difference between the value applicable on the day of receipt and the value subsequently credited.

The complaint was settled on that basis.

CASE 35 – NOT A HOLIDAY TO REMEMBER

Mr and Mrs M planned a trip to Bali in 1999. Shortly before their departure they visited the local branch of their bank to organise funds to take with them. According to Mr M he requested travellers cheques in Australian or US dollars in accordance with advice provided both by their travel agent and a friend who had recently been to Bali. The bank officer said she did not think the bank stocked US travellers cheques and suggested that they would be better off with NZ dollars because this would eliminate or reduce the possibility of exchange rate losses. Mr M recalled that he asked the bank officer about New Zealand dollar travellers cheques and specifically whether they could be cashed in Bali. He was informed that *“if you go to a bank they will cash them.”*

The day after their arrival in Bali Mr and Mrs M tried to cash a travellers cheque at their hotel but were told that while NZ cash was acceptable NZ dollar travellers cheques were not. They approached two local banks and met with the same response. They contacted the Australian Consulate and an employee tried to assist by ringing all the local banks, without success. They then contacted their bank in New Zealand. After a great deal of difficulty and several days delay funds were made available to them, a week after their arrival in Bali and with only two days of their holiday remaining. Due to the limited funds at their disposal for the majority of their holiday, Mr and Mrs M were unable to undertake the sightseeing trips they had planned or to eat anywhere other than at their hotel which was expensive. In addition they were obliged to spend a considerable amount of time in the hotel awaiting telephone calls from the bank in New Zealand as they attempted to arrange alternative funds. In effect their holiday was ruined.

Upon their return to New Zealand Mr and Mrs M complained to the bank about the advice provided about the acceptability of New Zealand dollar travellers cheques in Bali and sought compensation for their spoiled holiday. The bank denied any liability and in particular disputed Mr and Mrs M's version of the discussion with the bank officer which led to the purchase of NZ dollar travellers cheques. According to the bank, it was their decision to take NZ dollar travellers cheques to reduce the possibility of exchange rate losses whereas the bank officer had advised the use of US or Australian dollars.

In the course of the investigation of this complaint, the Banking Ombudsman interviewed Mr and Mrs M at some length but was not able to interview the bank officer involved. The Banking Ombudsman was unable to determine what passed between Mr and Mrs M and the bank officer when the travellers cheques were issued. However, given that Mr and Mrs M had been advised both by their travel agent and a friend that US dollars or Australian dollars were the most suitable currency to take to Bali, the Banking Ombudsman considered it most unlikely that they would have acted contrary to the advice given and specifically requested New Zealand dollar travellers cheques. In addition there was sufficient evidence from both sides to show that there was a discussion about the intended destination and the customers' need for the most appropriate kind of travel funds. Section 29 of the Consumer Guarantees Act 1993 provides that where services are supplied to a consumer there is a guarantee that the service provided will be of such a nature and quality that it can be reasonably expected to achieve the result that the consumer makes known to the supplier. It was not disputed that Mr and Mrs M had made known to the bank that they needed funds for a holiday in Bali. The Banking Ombudsman concluded that the service provided by the bank did not, and could not, achieve the result made known to the bank prior to their departure. Section 29 of the Consumer Guarantees Act applied.

The Banking Ombudsman found that Mr and Mrs M suffered the complete loss of the enjoyment expected from their holiday in Bali because they could not spend the money purchased from the bank. Therefore the most just resolution of their complaint would be the cost of a replacement holiday. The Banking Ombudsman's Terms of Reference did not allow her to make such a recommendation as she can only award costs for direct loss sustained together with a maximum award for inconvenience of \$2,000. The direct loss in this case did not extend to the travel and accommodation Mr and Mrs M paid for, given that they did receive that travel and accommodation. In the circumstances the Banking Ombudsman recommended that the bank pay to Mr and Mrs

Mr M the direct loss that could be established including the costs of the telephone calls etc, together with the maximum award of \$2,000 for inconvenience. The bank vigorously challenged the Banking Ombudsman's findings, contending that NZ dollar travellers cheques could be cashed by Indonesian banks. The Banking Ombudsman did not dispute the bank's advice but pointed out that it was at variance with both Mr and Mrs M's experience and other expert sources consulted. Under protest the bank accepted the Banking Ombudsman's recommendation and the complaint was settled accordingly.

CASE 36 – A DRAFT IN WHICH CURRENCY?

Mr O came to live in New Zealand a number of years ago. He decided to transfer his superannuation from his original country to New Zealand. He did not know how much the superannuation was worth. When Mr O received the bank draft from the superannuation fund he took it to a bank. Mr O was not familiar with receiving funds from overseas so he asked the bank staff member to do whatever was necessary to give him access to the funds. Mr O also signed a form which he thought was converting the funds from the currency of the country of origin into New Zealand dollars. In fact the form was authorising conversion from United States dollars into New Zealand dollars.

It transpired that the bank in the country of origin had used the wrong form when writing out the bank draft, and although 'USD' was printed on the form in the space allowed for numerals, the draft was actually in New Zealand dollars and did not require conversion at all. The effect of this was that Mr O's account was credited with approximately \$2,000 more than it should have been and about four times as much as if the funds had been converted from the currency of the country of origin into New Zealand dollars.

Mr O did not notice this error until he received a letter from the bank advising that the funds would be transferred out of his account. By this time Mr O had spent the money on major household appliances. Up until this time Mr O had been borrowing these items from friends. Mr O did not understand why his account had been debited and spent some time trying to find out from the bank what had occurred. Eventually Mr O took time off work and met with a staff member at the branch. The error was fully explained to Mr O and he agreed to repay the debt at \$10 a week, which was all he could afford, provided the bank did not charge him any fees or interest. The staff member agreed to this, but fees and interest were charged and Mr O started to receive letters from the bank threatening recovery action despite the fact that he was repaying the debt at the agreed \$10 a week. At this point Mr O contacted my office.

Mr O's complaint had not been fully considered by the bank's internal complaints procedure and so the matter was referred back to the bank. The bank offered Mr O \$1,000 in compensation for inconvenience (to be deducted from the debt), agreed that he could continue to repay the debt at \$10 a week but refused to waive interest and fees. Mr O considered that the charging of interest and fees was unreasonable and asked that I commence my investigation.

I accepted that Mr O was not someone who could be expected to be familiar with the transfer of funds between countries. He contacted the bank for assistance in negotiating the draft and was genuinely confused when the bank later advised him that the extra funds would be debited to his account. However if Mr O had thought that the funds were in the currency of the country of origin I was surprised that he did not question the large amount of money that resulted from the exchange. If the draft had indeed been in the currency of the country of origin the amount he would have been given would have been less than the face value of the draft, instead it was significantly more. Although Mr O may have believed the funds were his I did not consider the belief was reasonable.

I was, however, satisfied that the purchases made using the funds would not have been made if Mr O had not had the additional funds. He was previously borrowing the items from friends and no doubt would have continued to do so. I also considered, given Mr O's financial situation, that repayment of the debt with interest and charges accruing, would take a long time. I concluded that although the bank was largely responsible for Mr O's problems it was entitled to recover the overpaid funds.

However, it was my view that Mr O had been inconvenienced by the bank converting the funds into US dollars when no conversion was required. He had incurred a debt which was going to take him quite some time to repay. In addition the bank's initial handling of the error caused Mr O stress and inconvenience. I proposed, and both Mr O and the bank accepted, that the bank pay him \$1,000 in compensation for inconvenience, refund all interest and fees resulting from the overpayment and that he continue to repay the debt at \$10 a week, free of all interest and fees.

CASE 37 – A VALUABLE DRAFT IN A SAFE PLACE

In 1985 Mr F purchased a US dollar draft from a bank for the sum of about \$1,200, drawn on a New York bank. The draft was made payable to the order of the purchaser (Mr F) and he then placed it in a safe deposit box and left it there untouched through to the end of 1999.

When he tried to sell the draft back to the issuing bank it refused to repurchase the draft, saying that it was too old for presentment and also that the bank was unable to determine whether or not a duplicate draft had been issued at some time in the past fourteen years. It is general practice for banks when issuing a duplicate draft to obtain a signed indemnity from the purchaser of the draft indemnifying the bank against the possibility of future representation.

When I asked the bank for its report on the complaint, and its reasons for declining to repurchase, it cited section 45B of the Bills of Exchange Act 1908 which provides that bills of exchange, (which includes drafts), should be presented within a "reasonable time". The bank had earlier also referred to the Limitations Act 1950, which applied to negotiable instruments, and it submitted that a limit of six years from the date of issue applied in this situation. The Financial Transactions Reporting Act 1996, section 29(iii) states that:

"Every financial institution shall retain records kept by that financial institution ... in relation to a transaction for a period of not less than five years after the completion of that transaction".

The bank was therefore also saying that it was not obliged to keep records for more than five years after the completion of the transaction.

During the course of the investigation, enquiries were made of some other major banks about record keeping as it applies to unrepresented drafts. One of these banks was able to access records up to twelve years or more after the event, notwithstanding that there was no legal obligation for it to access archived material this far back.

At that point in the investigation the bank was asked again to check its archives for unrepresented items. By then it had been discovered that the bank had initiated some changes in its record keeping system approximately eight years earlier. I asked it at that point to peruse its records to see whether there were any amounts for the missing value carried forward. The bank made further enquiries and it was discovered that the US dollar value for the amount of the missing draft had been converted to local currency for the purposes of entering the amount into the bank's books at that time. It was therefore clear that the draft had not been paid out at any time before 1991, and it was a simple matter to check that it had not been paid at a later date.

The bank then made Mr F an offer calculated upon the amount of the draft converted as at the date he had first asked for it to be negotiated, together with interest to date. Mr. F was very pleased to accept the offer on that basis.

7 INVESTMENTS

Unit trusts and other managed funds products provided by banks participating in the Banking Ombudsman scheme have produced reasonably satisfactory returns recently. As complaints usually arise out of less than satisfactory returns, it is unlikely that I will receive many complaints about such products until the next downturn in the market.

In the meantime, *Case 38* is a reminder that banks may be liable for poor information given some years prior to the complaint and also a reminder that unit trusts are not familiar to many small investors and need to be explained carefully to dispel any preconceptions that may be held about products offered by banks.

CASE 38 – AN UNWANTED INVESTMENT

Mr and Mrs Q, a retired couple, approached their bank in October 1993 with a view to investing \$20,000 which they had on term deposit at an annual interest rate of 6.5%. They wanted a better return on their money. A bank representative visited them at their home and although they told her they did not want shares or unit trusts, she recommended the funds be invested in a bank unit trust. They were told the investment would pay them a quarterly return of 8% per annum plus tax imputation credits. They say they signed an application form and wrote a cheque for \$20,550 which included the entry fee of \$550. The bank sent them a certificate dated 29 October 1993 for the investment.

Three days later Mr and Mrs Q discussed the investment with their local branch manager who referred them to the representative who had visited them. They were concerned that their money had been deposited in an investment they did not want. They discovered that the unit exit price was less than they had paid, so if they sold the units they would lose not only the entry fee but also a substantial sum on the units. They asked the bank's representative to return their funds. The representative assured them that it was a sound investment and that they would not lose money.

Mr and Mrs Q were not satisfied with the representative's response to their concerns and again complained to the branch manager who sent another financial consultant to discuss the matter with them. This consultant confirmed that they would incur a considerable loss if they sold the units. They made a further complaint in December 1993, but received the same advice. None of these bank staff told them that they could complain to my office if they were not satisfied with the bank's response, even though the Banking Ombudsman scheme commenced on 1 July 1992. In the circumstances, Mr and Mrs Q decided to see if the investment would improve over time as they had been told it would.

Over the next six years Mr and Mrs Q received regular quarterly distributions from which imputation tax credits were deducted. In 1999 they received a letter from the bank advising that the unit trust in which they had invested their funds was to be wound up. They complained again to the bank and ultimately to me.

Mr and Mrs Q said that they had been poorly advised by the bank's representative and had been sold an investment they did not want. They believed the representative was motivated to sell them the unit trust investment by the prospect of an incentive the bank offered its staff. They said they had not been given a copy of the prospectus at the time of the investment. They also said that nothing had been done when they had complained several times to the bank and that they were not told at that time that they could lodge a complaint with my office.

The bank said it had searched its records but had found no trace of Mr and Mrs Q's complaints during the period 1993 to 1999. It believed that Mr and Mrs Q, having been advised that the unit trust was closing, had attempted

to recoup the funds they had lost and their actions were influenced by market conditions and not by mismanagement by the bank. During the course of my investigation, however, information came to hand which confirmed that they had expressed concern about the investment at an early stage.

I came to the view that the selling process used by the bank's representative in October 1993 had been deficient. I was not satisfied that the representative had explained adequately the details of the investment in the unit trust. While there was no evidence that she had engaged in misleading conduct, there was evidence that she did not provide the bank's services with the requisite degree of care and skill. Although Mr and Mrs Q told me they said that they did not want shares or units, the evidence suggested that they were aware that they had invested in a unit trust. The application form they signed clearly relates to units and the butt for the cheque they wrote clearly shows the cheque was for "unit trusts".

It seemed to me that although Mr and Mrs Q may have been aware they were applying for an investment that comprised units, they thought that the capital sum would remain at \$20,000, and that they would receive a consistent return of 8% per annum. It was only when they received the investment certificate that they found the capital had been converted to units, and if they were to exit from the investment at that time they would incur a loss. In other words, this was when they first understood the nature of their investment and that it was not what they wanted. The fact that they complained about the investment immediately reinforces the view that the investment was not suitable. Had they been given a more detailed explanation of the nature of the investment at the time they discussed it with the bank's representative Mr and Mrs Q may well have decided not to proceed.

Irrespective of what was said or done when Mr and Mrs Q signed the application form for the bank's unit trust, the focus of my concern was on what occurred after they had approached their branch manager on receiving the investment certificate. Despite three people being aware of their concerns, no attempt appeared to have been made to resolve the complaint, nor were Mr and Mrs Q referred to my office. It appeared that they were assured that if they remained in the investment they would do as well as if they had a term deposit. In the event, they made a capital loss on exit.

On this basis, I recommended that Mr and Mrs Q be paid:

- (a) the difference between the gross interest they would have received had their funds been invested on term deposit for the whole of the period and the amount of distribution payments they had actually received during that period, less tax.
- (b) their capital loss and entry fee.
- (c) \$1,000 - for the inconvenience they had suffered.
- (d) the costs of letters and telephone calls in pursuing their complaint.

My views were accepted by all parties and the complaint was settled on this basis.

8 INSURANCE

I am indebted to the Insurance & Savings Ombudsman, Karen Stevens, and her staff for their assistance and advice in matters of insurance law and practice and also in ensuring that complainants who approach their office with complaints more appropriately considered by the Banking Ombudsman are speedily referred to this office. For details of the arrangements where there is a

potential overlap of jurisdiction, please see my annual report for 1995/96 at pages 34 and 35.

For no very obvious reason, there has been a small increase in complaints relating to insurance sold and/or provided by banks participating in the Banking Ombudsman scheme.

Many of these complaints relate to events that took place at the point of sale of the insurance policy in a bank and I am concerned that I am still receiving cases where the training of the relevant bank staff is in question. *Cases 39, 40, 41 and 42* all raise questions on this issue, although in *Case 39* the bank more than compensated for any deficiencies there may have been in its initial process. That case is a good example of a bank working with the Banking Ombudsman to achieve the satisfactory resolution of a complaint in circumstances where the relationship between the bank and the complainant has broken down to such an extent that there is no possibility of a resolution through the bank's internal complaints process.

A failure to disclose relevant information either at the time of application for insurance cover or at the time of making a claim is at the root of many insurance complaints. *Cases 41 and 42* were cases of this kind where I was not satisfied that the bank officer in

question had given appropriate advice to the complainant on the duty of disclosure. In *Case 41* the conviction record that had not been disclosed dated from many years previously and was not necessarily relevant to the current application. The complainant may well have been able to obtain equivalent cover through another insurer but lost the opportunity to do so. In *Case 42*, the complainant would probably not have been able to obtain cover from any insurer for the relevant condition.

Case 43 illustrates another question that is commonly raised in complaints about insurance: the extent of cover under a disability policy. When a return to work is a gradual process after a period of disability, it is sometimes difficult to establish the point at which the insured has resumed his or her usual occupation and is no longer entitled to benefits under the policy. It would be helpful to see policy wording that clearly covered the question of entitlement in such circumstances.

CASE 39 – LIFE INSURANCE – THE NEED TO ENSURE ADEQUATE STAFF TRAINING AND THE PROPER ESTABLISHMENT OF THE POLICIES

This complaint highlighted firstly, the need for bank staff involved in selling insurance to have updated and comprehensive training in their selling of insurance and the types of product available to customers, and secondly, the way in which the Banking Ombudsman's office and a bank can work together to achieve a prompt and fair outcome.

In this case Ms C was living in a de facto relationship. She and her partner, both in their early twenties, had bought a home with the aid of a loan from the bank and at the same time had taken out life insurance policies to ensure that the loan was repaid in the event of the death of either partner. Unfortunately, for reasons that were not immediately clear, each partner was named as the owner of the policy on his/her own life rather than the more usual arrangement whereby each partner owns the policy on the other partner's life.

Ms C's partner died suddenly and as he had not made a will the beneficiary of his estate, including the proceeds of his life policy, was not Ms C but his estranged father with whom he had had no contact for more than twenty years, and whose whereabouts were unknown.

Ms C was thus left with a substantial loan and only a limited income. She faced the almost certain prospect of losing her home. Her father was firmly of the view that the situation had come about because of negligence on the part of the bank in the sale of the life policies. He believed that the staff member who had sold the insurance policies had received little or no training in the sale of insurance and that there was no sense at all in setting up the policies in such a way that one co-borrower was not protected in the event of the death of the other. He said this was contrary to common sense and usual practice.

The bank denied that it had been negligent and maintained that it was not uncommon for an individual to be

both the life insured and the policy owner. If Ms C's partner had had a will in place, then his intentions would have become clear.

Nevertheless the bank wanted to do all it reasonably could to see if there was a way for Ms C to receive the insurance policy proceeds. After obtaining legal advice and after considerable negotiation with Ms C and her father, at first directly and then through the Banking Ombudsman's office, an agreement was facilitated which saw Ms C receive the policy proceeds, but with some protection for the bank against the possibility of a future claim from the estranged father of Ms C's partner.

CASE 40 – FOUR WEEKS IS NOT A MONTH

Mr J took out a bank insurance policy with the intention that the insurance would cover his mortgage repayments if he became incapacitated. He had previously been unable to work following an accident and had faced a difficult financial situation which he wished to avoid in future. He therefore explained to the bank that he wanted an insurance policy that would cover his mortgage payments. The policy offered by the bank provided disability cover of up to \$1,500 per calendar month for a maximum of thirty months.

Some years later Mr J was involved in a motor vehicle accident and was hospitalised. He lodged a claim under the insurance policy and payments commenced effective from 30 days after the accident. Nearly two years afterwards, the bank advised him that arrears were outstanding in respect of his loan. It transpired that there had been a difference of approximately \$95 per month between the amount of Mr J's loan instalment and the amount of the insurance payment. He believed the bank should waive the arrears on the grounds that he had asked the bank to provide him with an insurance policy that covered his mortgage repayments and he had assumed that the policy he had taken had done so.

The bank's file contained no information about what was discussed when Mr J took out the insurance policy. However, given his past experience, I did not doubt that he intended to take out comprehensive loan insurance and I considered it more than likely that he would have made this clear to the bank. As the insurance was not purchased at the same time as the loan was taken out, it seemed to me very likely that neither the bank officer nor Mr J turned their mind to the question of whether \$1,500 per month would be adequate to cover his loan instalments. In my view the bank officer should have realised that the policy would not cover the loan instalments in full and should have pointed this out. At the time of the accident Mr J's fortnightly loan repayments were \$736.42 and I do not think he could reasonably have been expected to realise that while this was less than \$1,500 per four weeks, it was more than \$1,500 per calendar month.

I therefore concluded that the bank should cover the shortfall on Mr J's loan for the period from the time the insurance payment commenced until the end of the period for which he was eligible for disability cover under the policy. It should also refund any penalty interest or charges as a result of the loan being in arrears during this time. The complaint was settled on this basis.

CASE 41 – NON-DISCLOSURE OF CONVICTIONS ON INSURANCE PROPOSAL – MODIFICATION OF DUTY OF DISCLOSURE

In October 1998 Mr and Mrs C insured their car with their bank. An employee of the bank assisted them in completing the proposal. The proposal asked under a heading "General Questions" whether there was any information that may affect the acceptance of the insurance, for example, "*criminal activity or associations or convictions, apart from driving*". Mr and Mrs C answered "No" to this question. A policy was issued.

When the car was stolen about eight months later Mr and Mrs C made a claim under the policy. The claim was declined by the bank on the basis that Mr C had failed to disclose his past criminal convictions.

Mr and Mrs C then lodged a complaint with the Banking Ombudsman. They were adamant that when completing the insurance proposal they advised the bank's employee that Mr C had criminal convictions but they were over twelve years old. None of the convictions related to vehicle criminal activity and all were for minor offences. They said that the bank employee told them that as the convictions did not relate to vehicle criminal activity and were more than ten years old they did not have to be disclosed for the purposes of the vehicle insurance.

The bank was unable to identify the staff member who had assisted Mr and Mrs C in completing the proposal. The staff member had failed to sign the insurance proposal in the space provided. However it said that its staff members received training in the selling of insurance products and were told to specifically advise that the customer must answer all questions in full. Staff were also informed that it was not their place to advise of exceptions to any of the questions. Mr C's prior convictions had clearly not been disclosed on the proposal and this was a breach of the customer's duty of disclosure. The bank said that had it been aware of Mr C's criminal convictions it would have declined the proposal.

On balance, the Banking Ombudsman preferred the evidence of Mr and Mrs C. They had been consistent from the beginning that they were told by the bank employee that they did not have to disclose Mr C's criminal convictions. It appeared that the proposal had been completed by the bank officer rather than Mr and Mrs C. A major difficulty on the bank's part was that it had been unable to identify the staff member involved. Quite apart from not being able to seek comments from the bank employee, the Banking Ombudsman had been unable to determine how long he had been working for the bank and what experience he had in selling insurance and completing proposal forms. The fact that the staff member failed to sign the proposal form did not provide confidence that he gave Mr and Mrs C correct advice. Therefore the Banking Ombudsman concluded that the bank had effectively waived and/or modified Mr and Mrs C's duty of disclosure. It was also strongly arguable that the bank, through its employee, had breached the provisions of section 9 of the Fair Trading Act 1986 (in that it had engaged in misleading conduct) and the Consumer Guarantees Act 1993 (guarantee as to due care and skill).

The Banking Ombudsman said that she proposed to recommend that the bank pay Mr and Mrs C the market value of the car at the time it was stolen, a sum of \$7,500. Both the bank and Mr and Mrs C accepted the Banking Ombudsman's proposed recommendation and the complaint was settled on that basis.

CASE 42 – THE NEED TO TAKE CARE WHEN COMPLETING INSURANCE PROPOSALS – MATERIAL DISCLOSURE

In December 1997 when Mr J and his wife refinanced their home loan with the bank, their mobile mortgage manager (Mr Z) suggested that Mr J also take out loan protection insurance. Mr Z assisted Mr J in completing the insurance proposal. The proposal contained a general question regarding medical history, including visits to the doctor and medication taken during the last five years. Mr J told Mr Z that he had visited his doctor several times during this period for minor ailments, including mild depression. Mr Z thought for a moment and said that it was not necessary to enter these on the proposal form.

In October 1999 Mr J lodged a claim under the policy for a temporary disability benefit, having ceased work in September 1999 due to a mental disorder with symptoms of depression, panic, worry and anger. The bank declined the claim on the ground of significant non-disclosure in relation to a number of medical matters, in particular Mr J's visits to the doctor for stress and depression.

Mr J complained to the Banking Ombudsman. Mr J was adamant that he had made a full verbal disclosure to Mr Z of his visits to the doctor but had been told that it was not necessary to declare his visits to the doctor

for depression and the medication for depression. On the other hand the bank pointed out that Mr J's medical records showed a consistent incidence of depression dating back to 1996. The non-disclosure on the proposal form was considered by it to be significantly material to Mr J's claim and on that basis it had declined the claim. Mr Z said that he was sure that he would have told Mr J to disclose a visit to the doctor for stress or anxiety attacks if it had been mentioned to him.

On balance the Banking Ombudsman preferred the evidence of Mr J on the issue of non-disclosure of the doctor's visit for mild depression. His evidence had been corroborated by his wife. Further, Mr J had disclosed other potentially more serious matters including his asthma and the death of a grandparent from cancer. He had also disclosed his smoking and consumption of alcohol.

The bank said that had Mr J's visits to the doctor been properly disclosed, it would have imposed an exclusion for depression and anxiety related illnesses. After enquiry from other industry sources, the Banking Ombudsman accepted that this was likely to have been the case. Therefore it was difficult to say that Mr J had suffered any direct loss as a result of the advice given to him by the bank officer because, had the mild depression been disclosed, an exclusion would have been imposed and Mr J would not have been entitled to any cover for the depression and anxiety related illnesses from which he was now suffering. The Banking Ombudsman suggested that the bank refund that portion of the premium paid relating to disability cover. The Banking Ombudsman also considered that compensation for inconvenience was warranted. Mr J had faced the disappointment and shock of having his claim declined due to material non-disclosure, when in fact he had relied on the advice of the bank officer in not disclosing depression. He had lost the opportunity to explore alternative insurance cover although in the circumstances alternative cover was unlikely to have been forthcoming. The Banking Ombudsman found that a sum of \$1,000 would be fair compensation for the inconvenience suffered.

Both Mr J and the bank accepted the Banking Ombudsman's conclusions and the complaint was settled.

CASE 43 – WHERE REHABILITATION INVOLVES A RETURN TO WORK – DISABILITY CLAIM

This complaint turned on the interpretation of an insurance policy arranged by Mr K with the bank to cover a home loan. The policy provided cover for his loan repayments in the event that he suffered permanent or temporary disability resulting from accident or sickness. Mr K suffered an accident in May 1999. He did not return to full-time work until the end of August 2000. Before then, at his doctor's suggestion, he returned to work in a limited capacity gradually increasing his hours as his ability to cope improved.

In February 2000, the bank advised Mr K that as he had been cleared to work for 20 hours or more a week, he no longer fell within the policy definition of "*temporary disablement*" and that loan repayments would cease at the end of March 2000. Mr K told the bank that he was only remunerated for 5 hours a week and considered the bank's decision unreasonable. However, the bank maintained its position.

In considering this complaint I had to form a view on the point at which a disabled person involved in a staged return-to-work programme could be said to have resumed his or her usual occupation. The insurance policy was silent on the question of coverage during any period of rehabilitation, but the bank had decided that the policy no longer applied once the insured was able to work for more than 20 hours per week. The bank offered no explanation for this threshold.

The key phrases in the policy document were "*Temporary Disability*", "*Temporarily Disabled*" and "*usual occupation*". The first two are defined as meaning the inability of an insured by reason of illness or injury to carry out his or her usual occupation. "*Usual occupation*" is not defined. In this case, the question was whether it could reasonably be said that, by being at his place of work for twenty or more hours a week and doing his pre-accident type of work for only five hours, Mr K was "*engaged in his usual occupation*". My view was that it could not be

so said. He was there as part of a planned programme of rehabilitation. His “usual occupation” required him to attend his place of employment for a set number of hours per week and perform particular tasks. In this case, while he was able to attend his place of employment, and in the final part of his period of recuperation was there for up to forty hours a week, he was not able to perform his pre-accident duties on a full time basis until medically cleared to do so on 29 August 2000. He could not therefore reasonably have been said to have been engaged in his “usual occupation” until that time. I considered that a reasonable person would have understood that the policy would cover loan repayments during a period of recuperation until an insured was medically cleared to be able to resume his or her usual occupation to a reasonable degree. If the bank wished to impose limitations on what the reasonable person would understand, those limitations should be clearly stated in the policy document.

I therefore concluded that the bank’s decision to decline to pay Mr K’s loan instalments for the whole period of his incapacity following his accident was not reasonable and that it should reimburse him the loan instalments he paid for the period from the date the bank ceased payments until 29 August 2000. The complaint was settled on this basis.

9 TERMS OF REFERENCE

Several cases this year raised issues as to the interpretation of my Terms of Reference. *Case 44* concerned a somewhat unfortunate situation where initially it seemed that neither the New Zealand nor an overseas Banking Ombudsman would be able to consider the complaint, even though, on the face of it, the complainant had been poorly treated by a bank.

Case 45 concerns the interpretation of 22(c) of my Terms of Reference. This provision requires that a complaint be made to me no later than two months after the relevant bank has informed the complainant that deadlock has been reached and has also given information about the existence of the Banking Ombudsman and of the two months’ limit. In the early days of the Banking Ombudsman scheme, it

was comparatively unusual for a bank to invoke this provision but more recently its use has become commonplace. This has led to some questions as to the precise extent and nature of the two month limit. In this case I had to consider whether a complaint was made to me at the time the complainant first wrote to me, even though at that stage the complaint fell outside my Terms of Reference as it had not been through the relevant bank’s internal complaints process, or whether the complaint was made to me at a later date after some consideration by the bank’s internal complaints process.

Material relevant to the interpretation of my Terms of Reference will also be found in *Cases 5* (paragraph 14) and *8* (paragraph 22(d)).

CASE 44 – AN OVERSEAS LENDER

Mr J obtained a housing loan during 1999 from a loan company. The company was a subsidiary of an overseas bank that owns one of the banks participating in the Banking Ombudsman Scheme. Mr J experienced a number of difficulties with the administration of the loan and believed that the lender was in breach of the loan agreement. He wrote to the loan company on several occasions without receiving a satisfactory response. Mr J then wrote to the Banking Ombudsman and the complaint was notified to the New Zealand bank concerned.

The bank submitted that the complaint was not within the New Zealand Banking Ombudsman’s jurisdiction as the lender involved was not a subsidiary of the New Zealand bank. It confirmed that the lender was actually a subsidiary of the bank’s overseas counterpart and had been operating in New Zealand without the knowledge

of the New Zealand bank. The bank believed the complaint would need to be considered by the Banking Ombudsman for the country in which the lender was domiciled.

It therefore appeared that the complaint would be unable to be considered by the New Zealand Banking Ombudsman as it was about a subsidiary of an overseas bank, not about a member of the Banking Ombudsman scheme, and unable to be considered by the overseas Banking Ombudsman as it was about a banking service provided in New Zealand.

After further investigation the Banking Ombudsman determined that the complaint was within her jurisdiction on the basis that Mr J's loan documents specifically named the New Zealand bank as mortgagee. At this point the New Zealand bank agreed to consider the complaint through its internal complaints process. After doing so, it made Mr J an offer that included an apology, an explanation for the difficulties he had experienced and a financial payment that would place him back in his previous financial position.

Mr J agreed to accept the offer in full settlement of the complaint.

CASE 45 – THE TWO MONTH LIMIT

A complaint was received in June 1999. The bank did not appear to have had an opportunity to consider the complaint and it was therefore referred to the bank pursuant to Paragraph 22(b) of my Terms of Reference. The complainant, Mr F, was invited to refer the matter back to me if he was not satisfied with the bank's response to his complaint. The bank investigated the matter and advised me in July that the complaint had been satisfactorily resolved.

In fact, Mr F had not been satisfied with the bank's response and later asked the bank to reconsider his complaint. He also made a second complaint. The bank responded to both complaints on 14 September 1999 and advised Mr F that if he was dissatisfied with the response he should advise my office within two months from the date of that letter.

Mr F wrote to me on 24 November 1999 about both complaints. The complaints were referred to the bank. The bank drew attention to the contents of its letter of 14 September and said that it believed the complaints were outside my jurisdiction in terms of Paragraph 22(c).

On the basis of the information provided by the bank I formed the preliminary view that the complaints fell outside my Terms of Reference by virtue of Paragraph 22(c). Mr F did not accept this view. He argued that he had lodged his original complaint in June and it had not been resolved by the bank. He also maintained that his second complaint, made in August, had not been addressed. The bank, on the other hand, considered that its letter of 14 September 1999 had addressed both matters, and that as Mr F had not referred either complaint to me within two months of receipt of that letter, the matter fell outside my jurisdiction.

Mr F considered that his letter of June 1999 constituted the lodgment of his first complaint with my office and that the two month time limit imposed by Paragraph 22(c) did not therefore apply. However, I have no jurisdiction to consider a complaint until it has been through the bank's internal complaints procedure and deadlock has been reached. It is implicit in my Terms of Reference that, before I can commence an investigation, a complainant must refer the matter back to my office if he or she is dissatisfied following consideration by the bank's internal complaints procedure. Paragraph 22(b) provides that I may commence an investigation only after a complainant has reached deadlock with a bank. It is impossible for me to know whether complainants have accepted or rejected a settlement unless they advise me. They have two months from the advice of deadlock to make contact and this should be more than adequate.

In the circumstances I confirmed my preliminary view that the complaints were outside my Terms of Reference, pursuant to Paragraph 22(c) because they were not made to my office within two months of the bank's letter of 14 September 1999.