

Credit Ombudsman Service Limited

ABN 59 104 961 882

ANNUAL REPORT 2008

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Corporate Information

Credit Ombudsman Service Limited ('COSL') is a company limited by guarantee, not having a share capital. The Company was incorporated as Mortgage Industry Ombudsman Service Limited ('MIOS') on 18 June 2003 and commenced operations on 1 July 2003. The Company adopted its current name on 17 February 2004.

The Company operates the Credit Ombudsman Service, an external dispute resolution ('EDR') scheme approved by the Australian Securities and Investments Commission ('ASIC'). Under ASIC's Regulatory Guide 139, the Credit Ombudsman Service is required to be impartial, accessible and independent.

The Company's primary aim is to provide consumers and members with an alternative to legal proceedings for resolving finance-related disputes.

The Company's services are funded by a combination of membership fees and complaint fees paid by its members.

Membership

During the year, membership of the Company comprised:

Category A Member

MFAA Full Member or Life Member to whom the MFAA Code of Practice and the Rules of the Credit Ombudsman Service apply.

Category C Member

- Mortgage Broker
- Finance Broker
- Employee, agent or independent contractor of a Mortgage Broker or Finance Broker
- Mortgage Manager
- Credit Provider
- Aggregator
- Any person who conducts such credit-related business as the COSL Board approves and who is not a member of the MFAA.

Category D Member

As approved by the COSL Board on 27 April 2005 Resolution 2005/12.

Category E Member

As approved by the COSL Board on 29 June 2005 Resolution 2005/22.

Category G Member

Banks and other credit providers, and other MFAA members to whom the MFAA Code of Practice and the Rules of the Credit Ombudsman Service do not apply, but who undertake to contribute to the resources of the company.

Board of Directors

The Board of Directors of the Company ('COSL Board') comprises:

- ❑ An independent Chairman appointed by the MFAA
- ❑ Not less than one and not more than three Member Directors appointed by the MFAA to represent members
- ❑ Not less than one and not more than three Consumer Directors appointed by Consumers' Federation of Australia or other consumer representative body approved for the purpose by ASIC to represent consumers.

Credit Ombudsman Service Rules and Guidelines

Complaints about members of COSL are dealt with by the Credit Ombudsman Service in accordance with the Rules and Guidelines promulgated by the COSL Board.

Credit Ombudsman

The Credit Ombudsman is responsible for the day-to-day operations of the Credit Ombudsman Service and is empowered to make Determinations and issue binding Awards in relation to consumer complaints made against members of COSL.

About 99% of complaints received by COSL are resolved by non-adjudicative means, that is, by conciliation. However, the Credit Ombudsman can and does exercise his power to make Determinations, the terms of which are then published on COSL's website. Like all ASIC RG 139 approved schemes, Determinations made by the Credit Ombudsman bind members but not consumers.

Consumer and Member Communications

COSL maintains its website at www.cosl.com.au.

The COSL website:

- ❑ publicises its Annual Report on Operations, public submissions, Determinations, case studies and media releases
- ❑ has a dedicated member section for viewing information about COSL membership, applicable fees, complaint and internal dispute resolution processes and member resources
- ❑ allows a person to check if a person against whom they have a complaint is a member of COSL or a contractor of such a member
- ❑ provides consumers with a 'jurisdiction checker' to see if their complaint can be dealt with by COSL under its Rules
- ❑ allows consumers to lodge complaints on-line and provides guidance as to how a complaint can be made to COSL
- ❑ allows access to corporate information about COSL, such as its Constitution, Rules, Guidelines and Annual Report.

The COSL's Annual Report on Operations 2008 is published on its website.

Contact Information

Membership

Level 7, 287 Elizabeth Street
Sydney NSW 2000.
Phone: (02) 9273 8455
Fax: (02) 9261 2792
Website: www.cosl.com.au
Email: members@cosl.com.au

Case Management

Level 7, 287 Elizabeth Street
Sydney NSW 2000.
Phone: (02) 9273 8400
Interstate callers: 1800 138 422
Fax: (02) 9261 2798
Website: www.cosl.com.au
Email: info@cosl.com.au

Chairman's Report

On behalf of the Board of the Credit Ombudsman Service Limited, I have the pleasure of presenting the Company's Annual Report for 2008.

Highlights of 2007/2008

Highlights of the fifth year of the Company's operations are:

- ❑ COSL membership reaches almost 8,500 (up almost 8% from 2006/2007)
- ❑ 894 new complaints received (up 264% from 2006/2007)
- ❑ Number of complaints received by COSL now approaching level of housing finance complaints heard by the Banking Ombudsman
- ❑ COSL's membership represents 68% of the entire membership of all EDR schemes in the finance sector.

Membership

COSL is the largest EDR scheme in Australia by membership, with 8,354 Members (7,737 in the previous year), and covers about 16,000 loan writers. Importantly, about 36% of all home loans written in Australia are written by members of COSL or their loan writers.

COSL's membership comprises mostly mortgage brokers, but also includes non-bank lenders, mortgage managers, mortgage originators, aggregators, wholesale funders, securitisation trustees, housing co-operatives, credit unions, mortgage insurers and finance brokers.

When its operations commenced on 1 July 2003, COSL's membership was only about 1,200 and comprised Full Members and Life Members of the Mortgage and Finance Association of Australia ('MFAA').

The impressive growth in membership in the last five years can be attributed to the MFAA requiring certain categories of its members to be members of an ASIC-approved scheme, such as COSL. Furthermore, a number of lenders, large broker organisations and other credit industry participants require their contracted brokers to be members of an ASIC-approved EDR scheme.

Implementation of recommendations of independent review

All ASIC-approved EDR schemes are required to have their operations independently reviewed. The Company's independent review was completed in 2006 by the Navigator Group. The report made a number of significant recommendations, all of which have been successfully implemented, including:

- ❑ integrating COSL's complaints and membership functions, co-locating them and drawing them together under a Chief Executive Officer
- ❑ moving to a single Ombudsman/CEO structure
- ❑ developing a long-term membership relationship strategy, with the aim of establishing COSL as a recognised value proposition for members
- ❑ investing in a new computer system for COSL's membership and case management functions, and in particular, one which facilitates complaint tracking, reporting and the identification of systemic issues
- ❑ developing best practice complaint-handling processes and fee structures.

Although the commissioning of the review and the implementation of its recommendations were at some cost to the Company, it has allowed COSL to emerge as a mature fully-fledged EDR scheme which has gained credibility and acceptance amongst both its Members and other stakeholders.

It is pleasing to note, for example, that the number of complaints received by COSL is fast approaching the level of housing finance complaints received by the Banking and Financial Services Ombudsman Scheme. This is in no small part attributable to the increased support COSL receives from the industry. It is no coincidence that about 22% of all complaints heard by COSL are referred to it by its own Members.

COSL's Annual Report on Operations will be available on its website (www.cosl.com.au) by the end of October 2008. It provides a comprehensive review of COSL's case management operations for the year 2007-2008.

COSL's membership relationship strategy focuses on actively engaging its Members; affording transparency in the handling of complaints; and, given the present state of the industry, keeping its fees to a minimum.

Indeed, membership fees have not increased since 1 August 2005.

The new discounted complaint fees and free complaint voucher that the Company introduced in early 2007 have been warmly welcomed by Members. This has served as a significant plank in developing a long-term membership relationship strategy, with the aim of establishing COSL as a recognised value proposition for its Members.

I am pleased to say that 87% of complaint fees charged in the 2007/2008 year were within the \$0 to \$500 band. Significantly, this does not include the use by our Members of the free complaint voucher which allows them to completely offset the cost of complaint fees that may be charged for a complaint. Each Member receives one voucher each membership year provided fees are paid by their due dates.

Consolidation of EDR schemes

The merger of the Banking and Financial Services Ombudsman Scheme with two other large EDR schemes has created the very large Financial Ombudsman Scheme (FOS). It is said that the new scheme will handle 80-90% of all complaints in the finance sector.

Not surprisingly, COSL was invited to merge with the new FOS.

The COSL Board considered the invitation at length but resolved to remain independent.

This is consistent with the recommendation of the Navigator Group which acknowledged that COSL operates effectively as an independent EDR scheme and that, in the interest of its relationship with Members, COSL should ensure that it maintains an independent identity and branding.

The Board continues to consider whether joining FOS would be in the best interests of the company as a whole. However, the board believes that at this time there are a number of reasons why this should not occur:

1. There is a concern that COSL's membership (being the largest amongst all EDR schemes) would cross-subsidise FOS members if a merger were to occur.

COSL can offer its members the free complaint voucher and discounted fees precisely because it has a large membership base and, unlike other EDR schemes, complaint fees do not represent a significant proportion of its revenue.

One of the key findings of the independent review of COSL's operations made it quite clear that a 'user pays' model for complaint fees was deeply resented by COSL's membership. It found that complaint fees are often a shock to and represent a significant financial impost to small operators (95% of COSL's membership).

COSL's new fee structure is the sort of flexible, innovative and cost-effective response to industry-specific concerns which will be difficult to achieve in the larger, multi-industry bureaucracy which is the new merged FOS.

2. The MFAA, to which almost all COSL Members belong, does not support a merger of COSL with FOS. Its members have proudly differentiated themselves from banks and would be unwilling to participate in a scheme that is heavily geared towards very large institutional members. Indeed, about 95% of COSL Members comprise 1 to 5 loan writers.
3. The Productivity Commission recommended in April 2008 that governments should improve the effectiveness of alternative dispute resolution ("ADR") services for consumers by "further enhancing financial ADR services through.....integration of the existing bodies into

a single umbrella scheme to provide one referral and complaint pathway, while allowing independent governance of its subsidiary schemes.”

This has already been achieved with the FOS common telephone call centre and website to which COSL willingly subscribes. Consumers already have a single point of entry, with one referral and complaint pathway that leads to subsidiary schemes with independent governance.

The Productivity Commission itself expressed some scepticism about possible gains from an institutional merger, noting:

- the lack of flexibility in complaints handling;
- the differences between industry groups and types of complaints;
- given the consolidation and integration already occurring in the sector, there was only a “remote” likelihood that further convergence would achieve any real economic benefits through economies of scale.

Commonwealth legislation

Industry has for some years been bracing itself for the introduction of broker regulation. While it seemed that this would eventuate in late 2008 given the release of the template Finance Broker Bill by the NSW Government, the impending transfer of credit to the Commonwealth has meant that any legislation regulating the industry is unlikely to see the light of day until late 2009 at the very earliest.

The nature of the credit marketplace continues to cause difficulties in resolving complaints where a chain of different credit industry participants may be involved in arranging credit, each of which bears responsibility for the performance of different, but interdependent, roles. Unless each participant is a member of COSL or another EDR scheme, the consumer may be left without a remedy. This hinders comprehensive coverage of the credit marketplace.

Consequently, COSL is keen to see the Commonwealth enact broker and lender legislation such that all participants to a credit transaction are required to become members of an ASIC-approved EDR scheme.

Progress towards a national approach to broker and lender regulation has been slow, but nonetheless encouraging and keenly awaited.

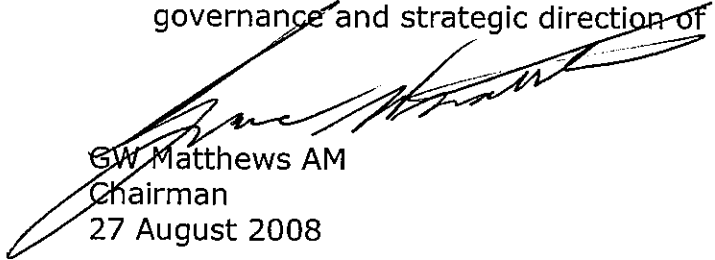
Conclusion

2008/2009 will see further significant challenges for the Company as it prepares for the introduction of Commonwealth broker and lender legislation.

Acknowledgements

I would like to record my sincere appreciation for the sustained commitment, professionalism, enthusiasm and diligence that my Chief Executive and his staff bring to their roles every day.

I would like to extend my thanks to my colleagues, Ms Katherine Lane and Ms Catherine Uhr (Consumer Directors) and Mr Jon Denovan and Mrs Vicky Edema (Member Directors), for their valuable contributions to the governance and strategic direction of the Company.



GW Matthews AM
Chairman
27 August 2008

Chief Executive's Report

The last twelve months have seen COSL continue to focus on raising its profile amongst its Members; developing best practice complaint-handling processes; and acquiring deeper expertise in its case management capabilities.

COSL has strived to respond quickly to changes in the market. Its philosophy is grounded in continuous improvement and being more transparent, accessible and accountable to its Members and other stakeholders.

COSL's membership has increased in the past 12 months by almost 8%, a good outcome given the difficult conditions faced by the non-bank sector and the fact that COSL's membership is voluntary.

In the five years since COSL was incorporated in 2003, three factors have impacted on the Company's finances:

- the growth in membership;
- more latterly, the significant increase in complaints received by COSL; and
- the independent three-year review of COSL's operations (this was required by ASIC as a condition of their approval of COSL as an EDR scheme).

The COSL Board accepted all the recommendations made by the independent review. The implementation of these recommendations has since been completed.

Growth in COSL membership

COSL's membership has grown from 1,200 to 8,500 in a period of five years. This has required the establishment of a dedicated member service department, adequately staffed and resourced.

The cost of COSL's member services has risen from \$117,414 in 2004 - when the MFAA was undertaking much of the work as part of the handover to COSL (then known as MIOS) - to \$615,491 in 2008.

Member services currently maintain records covering some 16,000 operators, including contractors.

Member relations

One of the recommendations of COSL's independent review was to devise a member relations strategy. This saw COSL raising its profile amongst its membership, promoting its value proposition to Members, providing Members with COSL brochures to hand to their clients and taking every opportunity to meet with Members at industry functions, broker conferences and professional

development days. This has proved very successful, but has cost nearly \$150,000 over the past two years. For example, member services now spend some \$50,000 each year on printing and postage costs alone.

A significant plank of COSL's member relations strategy was the introduction in February 2007 of discounted complaint fees and the free complaint voucher. For example, where a Member has received no more than three complaints in a membership year, no complaint fees are payable at the Referral Stage. Further, although complaint fees are payable in the unfortunate event that an unresolved complaint is progressed to the Conciliation or Determination Stages of the COSL process, the free complaint voucher can be used to off-set these fees entirely.

Given the difficult times our Members are presently facing, this is a welcome initiative in reducing costs to Members. This initiative, however, has been at a cost of \$65,230 to the Company.

Proposed broker legislation

COSL has also incurred costs because of its active engagement with regulators and others in the development of the draft broker legislation. This involved, among other things, the CEO and Chairman visiting State Government officials and conferring with industry participants, resulting in an increase in travel-related expenses.

Increase in complaints

Case management was originally outsourced to the Australian Commercial Disputes Centre (ACDC) for a fee of \$429,052 in 2004.

In October 2006, on the recommendation of the independent review, case management was brought in-house and co-located in the same premises as COSL's member service department, under a single chief executive/ombudsman structure. The total cost of case management in 2006 rose to \$724,840.

The rapid growth in complaints since then has placed considerable strain on our case management resources. For example, in the last twelve months, COSL has received 264% more complaints than it did in the previous 12 months.

The increase in member services staff and the subsequent transfer of case management in-house, saw the cost of office premises rise from \$32,591 in 2005 to \$159,527 in 2008.

COSL has a total staff compliment of 14.5, comprising 10 professional staff and 4.5 non-professional staff – a stark contrast from the small number of para-legals and administrative staff it employed in 2004.

The increase in professionally-qualified staff and the corresponding increase in salary levels have meant that salaries accounted for a total of \$ 1.25m (\$1.44m including overheads) in 2008.

COSL's membership and case management system

A further recommendation of the independent review was to replace COSL's antiquated computer system with a system specifically designed to meet best practice complaints handling and membership requirements. Consequently, a robust 'best of breed' system was acquired; one which is also presently used by the Commonwealth and various State and Territory Ombudsmen, and the Energy Ombudsmen in Victoria and New South Wales.

The cost of the new system was about \$173,361. However, it has already paid dividends and significant productivity gains have been achieved since its implementation in January 2008.

The new system was also necessitated because of the nature of COSL's membership base which is entirely different from other EDR schemes. The constant movement of contractors, loan writers and brokers within the industry means that COSL has to be able to track their movements when they cease to represent a particular COSL Member or when they commence a role (or another role) with another COSL Member.

Not only does COSL need to record each relationship between a Member and a contractor, it also needs to record inter-member relationships, which include loan writers associated with multiple Members, and mortgage managers associated with multiple memberships.

Conclusion

While membership has grown by a factor of seven and complaints by a factor of almost 11, total expenditure has only risen by a factor of 3, demonstrating a significant gain in productivity.

Importantly, the financial performance of the Company continues to be at a very sound level, despite the considerable level of costs associated with its core activities.

With thanks

I have been fortunate in having the dedicated support of a young, enthusiastic, passionate and committed team without whom none of our achievements would have been possible. They are also responsible in no small part for the Company's new profile, outlook and culture.

I would also like to express my appreciation to the Chairman and the non-executive directors of the Company. Their whole-hearted support and guidance throughout the year has been unparalleled.

Significantly, the continued support of our Members is immensely appreciated.

Directors' Report

Your Directors submit their Directors' Report for the Financial Year ended 30 June 2008. This report is made in accordance with a resolution of the Directors passed on 27 August 2008.

1. Directors

The names of the Directors, the periods during which they were in office during the financial year and on the date of this Report, are:

Graeme William Matthews AM (whole year and current) - Chairman

Katherine Gizelle Lane (whole year and current) - Consumer Director

Jonathan Alexander Denovan (whole year and current) - Member Director

Catherine Louise Uhr (whole year and current) - Consumer Director

Victoria Anne Massey Edema (whole year and current) - Member Director.

2. Nature of the Company's operations and principal activities

The principal activity of the Company during the financial year was to operate as an external dispute resolution scheme in the finance industry. The Company's membership comprises mortgage and finance brokers, mortgage managers, aggregators, originators, non-bank lenders, wholesale funders, housing co-operatives, trustees and credit unions, most of which are members of the Mortgage and Finance Industry Association of Australia ("MFAA").

The Company has operated as an ASIC-approved EDR scheme since 17 December 2003.

3. Review of Operations

The operations of the Company during the year resulted in an operating surplus of \$124,117.

4. Significant changes in the Company's state of affairs and principal activities

There have been no significant changes in the Company's state of affairs or principal activities, other than those referred to in the Chairman's Report above.

5. Significant matters or circumstances since balance date

No matter or circumstance has arisen since the end of the financial year that has significantly or may significantly affect the Company's operations in future financial years, or the results of those operations in future financial years, or the Company's state of affairs in future financial years.

6. Likely developments in the Company's operations in future financial years

As noted in the Chairman's Report, the Company's operations in future financial years and the results of those operations are likely to be affected by the proposed enactment of Commonwealth legislation, likely to be in late 2009/early 2010, which will require the licensing and regulation of finance brokers and lenders.

7. Environmental regulation and performance

The Company is not subject to any particular and significant environmental regulation under a law of the Commonwealth or of a State or Territory.

8. Dividends

The Company's Constitution prohibits the paying of any dividend or distribution to members and no dividend or distribution was paid to any member during the financial year.

9. Company Officers

During the year no officer of the Company was a partner in an audit firm or a director of an audit company that is an auditor of the Company.

10. Options

The Company is a company limited by guarantee without a share capital and therefore no options were or were able to be granted over unissued shares or unissued interests.

11. Indemnities and insurance

During the year no indemnities were given for any person who is or has been an officer or auditor of the Company. The Company has paid directors and officers insurance cover for all directors at a cost of \$ 6,616, exclusive of GST. The Company did not pay any insurance premiums in respect of insurance for auditors.

12. Remuneration and Benefits

No Director or other officer of the Company has during the year or since the end of the year received or become entitled to receive any benefit other than those benefits included in the aggregate amount of emoluments received or due and receivable by the Directors and other Officers as shown in the COSL accounts.

13. Directors and Secretary qualifications, experience and special responsibilities

GW Matthews

AM FAIBF FAICD FAIM AFAMI - Chairman. Company Director

JA Denovan

LL.B - Member Director. Partner, Gadens Lawyers

VA M Edema

BA LL.B - Member Director. Company Director

KG Lane

BA LL.M - Consumer Director. Principal Solicitor, Consumer Credit Legal Centre (NSW)

CL Uhr

LL.B - Consumer Director. Solicitor, Legal Aid Queensland

RA Venga

LL.B(Hons) LL.M - Company Secretary.

14. Meeting attendance

Name	Meetings held whilst a Director	Meetings Attended
Graeme William Matthews	4	4
Victoria Anne Massey Edema	4	4
Katherine Gizelle Lane	4	4
Catherine Louise Uhr	4	4
Jonathan Alexander Denovan	4	3

15. Proceedings on behalf of the Company

During the year, no proceedings were either commenced by or against the Company and accordingly no application for leave under section 237 of the Corporations Act 2001 was made.

16. Registered Membership

As at 27 August 2008, the registered membership of the Company was 8,193.

On behalf of the Board


GW Matthews AM
Sydney, 27 August 2008