

## Policy Bulletin 5

### CANCELLATION OF DIRECT DEBITS

This article summarises the responsibilities of both financial service providers (FSP's) and consumers in regard to the cancellation of direct debits.

#### Credit Cards

In regard to the issue of cancelled direct debits this office believes a FSP can take action on behalf of an account holder when

- An account holder has disputed the transactions debited by a merchant
- The credit limit of the card has been exceeded
- The merchant is continuing to debit the account periodically.

This office understands that it may not be technically possible for an FSP to stop a merchant processing a direct debit to the account. However, given that the debit has been cancelled by the account holder, the FSP is obliged contractually to accept this cancellation. Consumers should be told to confirm such cancellations in writing.

In some instances disputes have been avoided where the FSP has forwarded a copy of the cancellation through to the third party on behalf of the account holder. Good industry practice requires that when an FSP has been notified of the cancellation it should ensure all future transactions under the direct debit authority are charged back to the creditor/merchant by the FSP on behalf of the account holder.

This issue is particularly significant where the credit limit has been exceeded.

An account holder is contractually entitled to withdraw any authority given to a third party by notice to the FSP not to accept a particular debit request. In the absence of specific provisions in a credit card contract, an account holder is not compelled to revoke the previously provided authority directly with the third party (although common sense dictates the consumer should also advise the third party in writing).

It should be noted that the majority of FSPs have Conditions of Use which stipulate an account holder must cancel a direct debit authority directly with the third party. The minority of FSPs who do not have this in their Conditions of Use should seriously consider an amendment to maximise their own protection.

A term in the general or "Using Your Card" section of the Conditions of Use requiring an account holder to cancel the direct debit authority with the third party may be enforceable. If such a term is limited by its words or by its placement to the "Cancellation of Card/Closure of Account" section (and the account to which debits continue to be processed is not being closed or the card cancelled) the term is unlikely to be enforceable.

This office's view is that usually provisions found in the "Cancellation of Card/Closure of Account" section of the Conditions of Use apply only to situations in which a card is being cancelled or an account closed.

An instruction to cancel an authority directly with the third party is limited by its wording or the placement in the "Cancellation of Card/Closure of Account" section of the Conditions of Use

- Will usually be an inadequate warning to the account holder that all direct debits must be cancelled in this way because the account holder may not be cancelling or closing the account and
- Will usually be unenforceable or unable to be relied upon by the FSP in a dispute about the acceptance of a direct debit to an on-going credit card account.

In summary, the approach of this office is that

Where an account's Conditions of Use do not include cancellation of direct debit authorities, an account holder is entitled to instruct the FSP not to accept direct debit requests from a particular third party.

Where an account's Conditions of Use include, in the "Cancellation of Card/Closure of Account" section, an instruction directing an account holder to cancel an authority directly with a third party, and the card is not being cancelled or the account closed, usually the instruction would not apply to an account if it was not being closed or cancelled and therefore may not be relied upon by the FSP.

Where an account's Conditions of Use include an unlimited instruction or an instruction in the general or "Using Your Card" section advising an account holder to cancel an authority directly with a third party, the FSP can usually enforce or rely on such a clause.

Some of the questions asked by this office will include

- Did the account holder instruct his or her FSP, but not the third party, that direct debits from the third party to the account should not be accepted by the FSP?
- Do the Conditions of Use for the card specify the account holder must also advise the third party of the direct debit cancellation?
- Is this instruction to the account holder specified in the Conditions of Use?

This office will continue to accept disputes from customers of FSPs relating to unauthorised debits to accounts. Consumers should **not** be told that any dispute is a matter between them and the third party. While consumers can be requested to try to resolve a dispute with the third party first, they must be advised of their right to lodge a dispute with this office if they are not satisfied with the outcome of any claim made through an FSP.

### Direct Debits and Transaction Accounts

An FSP has an obligation to process only those debits which the consumer has authorised. The consumer is entitled to withdraw any authority given to a third party by

notice to the FSP not to accept a particular debit request. If such an instruction is received by a consumer's FSP it should then be forwarded by it to the third party.

This office will encourage consumers to first seek to resolve any dispute by completing the necessary forms at their FSP. FSPs in turn should ensure that customers are advised of their right to lodge a dispute with this office should they not be satisfied with the outcome of any claim to the FSP.

The FSP has no authority to accept instructions in relation to the operation of the account from third parties in the absence of

- Written instructions from the customer
- An enabling clause in the contract between the FSP and consumer.

In the absence of appropriate terms and conditions it is, in the view of this office, an open question as to whether the FSP is entitled to debit a customer's account solely on the assertion, made by a third party, that it has authority to debit a customer's account.

The circumstances in which this office will regard a debit as unauthorised include the following

- The third party making the request did not hold a current direct debit authority from the account holder
- The amount debited exceeded the amount authorised in writing by the consumer or was debited in breach of a condition of the authority (such as a billing advice or that notification of debit be sent first)
- The third party increased the amount or frequency of the debit without the consumer's express agreement in writing. Provisions in service agreements allowing debit users to change authority simply by giving notice to the consumer, but without the consumer's written approval for the variation may not be enforceable
- The consumer withdrew the authority or stopped the particular debit, whether by notice to the third party debit user or to the FSP.

If the debit is unauthorised the FSP can be held liable to the consumer for losses. These can include

- Interest
- Dishonour fees – ie if other transactions are dishonoured because the account balance is not what it should have been and/or
- Expenditure incurred because of the lack of access to funds.

In some cases, the loss can be greater than the amount actually debited. The length of time it takes to reverse the debit will also affect the amount of the loss.

As can be seen from the above text the responsibility of FSPs **and** consumers is quite clear.

The above text illustrates the potential downside for FSPs in regard to issues surrounding direct debits. However, the risk of liability for FSPs can be reduced with sensible directions to staff and appropriate wording in the conditions of use made available to consumers.