



Bulletin No 12
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DEBIT ORDERS

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Debit order payment facilities are used by the majority of banking customers. In relation to the number of debit orders which are processed each month, we receive a very low number of complaints regarding this issue. It is however important to alert the banks and their customers to the debit order process and the types of complaints which we are receiving in this regard.

Background

The debit order facility serves as a very convenient and useful manner of paying accounts. The vast majority of bank customers use this facility on a daily basis and rarely encounter any problems. It is however when a debit order is disputed that a bank customer encounters problems with his/her bank regarding the reversal or cancellation of the debit order. Based on the complaints we receive it has become apparent that many bank staff are unaware of the process to follow when dealing with a disputed debit order. Often bank customers are merely told to take the matter up with the company or institution that is debiting the account. This creates the impression that bank customers have no control over their accounts and are left at the mercy of unscrupulous companies that abuse the debit order facility.

Code of Banking Practice

The Code of Banking Practice (the Code) contains the following provisions relating to debit orders:

“4.2 Products, services and account operations

When you become a client and on reasonable request, we will make available to you:

- ◆ information on how your account works, including:

how *debit orders* and *stop orders* work, the difference between the two and how to stop and/or cancel them;

8. USEFUL DEFINITIONS

8.7 Debit order:

An agreement between you and a company or a third party in which you authorise the company or third party to take money out of your banking account for services that entity provides to you. Debit orders may be for fixed or variable amounts.

8.18 Stop order:

An instruction given to your bank to pay funds to a nominated third party, at a fixed amount on a regular basis. The bank acts on your instructions and the third party is not given authority to debit your account as is the case with a debit order.”

The debit order process

How is the debit order system administered?

All the major banks are parties to a joint agreement titled “Rules governing the clearance of debit and credit electronic funds transfer payment instructions”. The agreement is administered by the Payments Association of South Africa (PASA) and sets out the rules and procedures to be followed when a customer disputes a debit order. Debit orders fall under a category of banking payment systems known as Electronic Funds Transfer (EFT).

Who may use the debit order system?

Any organization may use the debit order system to enable it to collect payments from its customers, but it would first need to approach its own bank for approval. Its bank, known as the sponsoring bank, will only give its approval once certain laid down criteria are met. The sponsoring bank is only expected to approve financially sound organizations with good track records with the bank. A contract between the organization (which is then known as a “user”) and the sponsoring bank is then signed. Customers can then sign a debit order instruction with the user granting it permission to debit their account. The customer’s own bank where their account is held is known as the “homing bank”.

The responsibility of the user

The user must obtain a written authority from the customer before any transactions can be processed through the EFT system.

There is also provision for users to use voice-recorded authority under certain circumstances. If a voice recording is used, the user should thereafter confirm the authorization in writing.

If a debit order is unpaid for lack of funds, the user may resubmit the item but may not adjust the value of the transaction. Should no funds be available, the homing bank will return a debit order marked as “not provided for” to the user’s nominated account at the sponsoring bank.

If the client closes the account from which the debit order is paid, the debit is returned “account closed”. The user is then not permitted to process any more debits against that account.

If a debit order is unpaid on two consecutive occasions for lack of funds, the user must remove it from the system.

If there are not enough funds in the customer’s account to meet a debit order, the company can re-submit the debit order the next month. It cannot adjust the value of subsequent transactions to recover arrears. Separate debit orders must be submitted for the current and arrears payments.

If the customer has closed the account, the company must stop submitting debit orders with immediate effect.

Once a customer has authorized a debit order, the user concerned cannot transfer any of its rights to the debit order to a third party without the customer's prior consent.

Users must produce auditor's certificates at 12-monthly intervals confirming to the banks the existence of their authority to debit the customers' bank accounts.

The banks have introduced a process to identify those companies who have not conformed to the rules of the debit order system. These companies would then be disqualified from further use of this facility.

The customer's rights

A customer can give their bank a written stop payment instruction to prevent a debit order for a specific amount being processed on the account. When a debit order is returned "payment stopped" on the instruction of a customer, the user may not process further debits under the system.

A customer can instruct his or her bank to reverse a disputed debit order. If the disputed debit order is reported within 40 days of it appearing on the account, the bank will reverse it immediately.

If the customer only queries the debit after more than 40 days of it having been debited to his account, he or she may apply to his or her bank (the homing bank) to have it reversed. The homing bank will query the validity of the transaction with the sponsoring bank that debited the account. The sponsoring bank will be given 30 days written notice to prove the validity of the transaction after which it will be cancelled if invalid, and the funds manually returned to the customer's account. If the sponsoring bank does produce a valid mandate for the transaction, then the debit will not be reversed. The banks are only expected to check for an apparent authorization – which will normally be the client's signature on an authorization to debit form. The banks are not generally expected to act as a court in deciding on disputed signatures, services not provided or any other dispute between the user and the client. Disputes of this nature are between the client and user to resolve by litigation or any other legitimate method.

An instruction to cancel a debit order only remains on the bank's system for a limited period (three to six months depending on the bank). After this period a user may again attempt to debit the account and it will be processed. It is important that clients check their statements regularly for fraudulent debits.

Wrong code used

We recently dealt with a number of cases where the incorrect code was used by the bank when canceling a debit order. In one typical case, the bank placed a "payment stopped" instruction on a short term insurance debit on request of its client, who did not have enough money for the debit that month. The bank, in an effort to save the client the penalty fees that are payable for a returned debit order due to lack of funds, placed a code on the instruction indicating that the debit order was cancelled by the client. The insurance company took this to mean that the insurance was no longer required and cancelled the insurance policy. The client's claim that occurred in this time was then denied. Although the bank's intentions were honorable, it led to a substantial loss for the client.

Banks are cautioned to apply the correct code to any cancelled debit order and explain the possible consequences to the client. It should be explained that if a client wishes the bank to stop a debit order from being paid the bank must use the code “payment stopped”.

Penalty fees

The banks charge a specific penalty fee per debit order that is returned due to a lack of funds. While it is within the control of the bank customer to avoid these penalties, we urge the banks to consider reversing these fees in appropriate circumstances.

We have found that the penalty fees charged tend to put the account holder in an even worse financial predicament, from which there is often little hope of recovery. In certain cases we have recommended that the banks reverse the fees in question.

Assessment

It is therefore clear that rules and procedures are in place to deal with disputed debit orders. The banks have access to this information and should apply it in every case where it is applicable. The banks are further able to monitor user accounts for repeated abuse of the debit order system and to take appropriate action where necessary. They are encouraged to do so in appropriate circumstances.

When receiving any complaint on this issue we will expect the bank to have applied the procedures as mentioned above. Any failure to apply the procedure or delay in assisting the customer may result in an award being made for the distress and inconvenience suffered. Each case will be evaluated on its own merits.

**Adv NJ Melville
Ombudsman**