



23 November 2020

Ms Claire McKay
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The Treasury
Langton Crescent
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Dear Ms McKay

ABA response to Treasury consultation on Consumer Credit Reforms

The Australian Banking Association (ABA) supports the Government's Consumer Credit Reforms. These important reforms will strike the right balance between maintaining strong consumer protections while providing credit into the economy at a critical time.

Australia's banks remain committed to the ongoing and efficient flow of credit to consumers and small businesses, and these reforms provide lenders with greater flexibility to make faster credit decisions. The ABA endorses the Government's proposals to retain strong protections for consumers, including the licensing and conduct requirements of the National Consumer Credit Protection Act (NCCP Act), APRA lending standards, our Banking Code of Practice (BCoP), external dispute resolution provided by AFCA, and customer and regulator recourse to the courts.

The reforms acknowledge the significant changes in the regulatory and economic environment since the introduction of the NCCP Act in 2008, such as the rewrite of the Banking Code of Practice, the introduction of the Design and Distribution Obligations and ASIC's Product Intervention Power for credit products, the enhanced protections for credit card customers, and the best interests duty for mortgage brokers.

Key points in our submission

Maintaining strong consumer protections

The ABA supports the retention of strong consumer protections under the consumer credit framework, in particular the proposed provisions regulating small amount credit contracts and consumer leases, the retention of the requirement to assess whether a customer can repay their credit card limit within a reasonable period, and the consumer protections relating to reverse mortgages.

The consumer credit framework is also complemented by the licensing and conduct provisions of the NCCP Act and the unconscionable conduct and consumer protection provisions in the ASIC Act, which provide further avenues for regulatory enforcement and customer redress.

Consistent consumer protection and level playing field

It is important that there is proper alignment between the new non-ADI framework and the APRA framework for ADIs, to provide certainty and consistent protection for customers and to maintain a level playing field between ADI and non-ADI credit providers. This is necessary to maintain a competitive credit industry that provides the same protections for customers regardless of credit provider and



delivers a range of benefits to customers including competitive pricing, improved service and ongoing innovation in products and technology.

Simplification and removing duplication

A critical benefit of the reforms is simplification of the regulation relating to credit decisions and removal of regulatory duplication. To achieve this, the ABA recommends that all credit decisions for consumer loans, including 'low limit credit contracts' offered by ADIs are regulated by a single regime supervised by APRA to ensure there is no unnecessary duplication of regulation. Accordingly, the concept of 'low limit credit contract' should be removed from the Bill so that these loans, like all other consumer loans, are subject only to APRA's framework.

Support for complementary reforms

Implementation of the consumer credit reforms also provides an opportunity to progress complementary reforms related to e-transactions and comprehensive credit reporting.

Our detailed comments on the draft exposure Bill, Regulations and Non-ADI Credit Standard are included below.

The ABA believes the Government's changes will simplify the loan process for customers making it more robust and efficient, but less onerous and intrusive.

The ABA and our member banks look forward to continuing to work with Treasury through the development of these reforms. Please contact me on 0400 681 407 or at justin.mining@ausbanking.org.au if you have any questions or would like to discuss this submission in further detail.

Yours sincerely

Justin Mining
Policy Director



Appendix – ABA comments on Consumer Credit Reforms

1. ABA guiding principles of consumer credit reforms

The ABA and our member banks have identified some guiding principles that underpin our review of the proposed changes to the consumer credit framework:

- the reforms should strike the right balance between maintaining strong consumer protections while supporting the efficient flow of credit into the economy
- the regulatory approach should maintain consumer protections across ADIs and non-ADIs through consistent standards and ensuring ongoing financial system stability
- as banks need to consider a customer's financial information as part of their assessment, customers can help by providing accurate information
- consistent special conduct provisions for reverse mortgages and credit cards should be retained for both ADIs and non-ADIs as important consumer protection measures
- reforms should encourage product innovation and the use of new and improved data sources to efficiently verify customer details, and
- customers should continue to be able to bring complaints to the EDR scheme (AFCA) in respect of any type of credit.

2. Proposed consumer credit framework – maintaining level playing field and ensuring efficient flow of credit

The ABA understands that the Government's announced reforms to the consumer credit framework contained in the *National Consumer Credit Protection Act 2009* (NCCP Act) are aimed at reducing the time it takes for individuals and small business to access credit by enabling lenders to take a more risk based approach while maintaining strong protections for customers.

The reform package consists of three specific components:

- the National Consumer Credit Protection Amendment (Supporting Economic Recovery) Bill 2020 ('the Bill')
- the National Consumer Credit Protection Amendment (A New Regulatory Framework for the Provision of Consumer Credit) Regulations 2020 ('Regulations'), and
- the National Consumer Credit Protection (Non-ADI Credit Standards) Determination 2020 ('Non-ADI Credit Standard').

2.1 Risk based approach to responsible lending

The Government has indicated that the key objective of its reforms is to amend the existing responsible lending framework with its focus on individual loan assessment to a risk-based regime with system-level obligations. This provides lenders with greater flexibility to make credit decisions based on the characteristics of the borrower and the type of credit. The ABA has consistently supported a responsible lending framework where lenders can take a scalable approach to determining the inquiries and verification steps needed to be taken before making a suitability assessment. This approach should be proportional to customer harm and risk factors.

These reforms if implemented appropriately alongside amendments to APRA guidance should enable lenders to reduce red tape to support and assist customers through the credit approval process in certain circumstances while providing further clarity on requirements when providing credit. For example, a bank should be able to undertake lower levels of inquiries and verification steps for an



existing customer with a positive repayment history and declared information in line with expectations for their profile.

The focus of ABA member banks will be on delivering efficiency benefits in the provision of credit while ensuring that appropriate consumer protections remain in place to ensure prudent lending standards across the economy.

2.2 'Low limit credit contract'

The ABA recognises the potential for small loans to have a significant impact on customers given these types of loans generally account for a proportionately significant part of a customer's available income to service. When provided by an ADI, appropriate safeguards are prescribed through the APRA framework.

The Bill creates the concept of a 'low limit credit contract' for where an ADI provides an unsecured loan of under \$2000 that is not a continuing credit contract, and with a term of between 16 days and one year. Under the current proposal, an ADI will be subject to the responsible lending obligations under the NCCP Act for these types of loans. The ABA notes that the current NCCP Act settings for small loans differ between ADIs and non-ADIs, with Small Amount Credit Contracts being defined to exclude credit provided by ADIs.

This means that for low limit credit contracts, ADIs would be subject to both the responsible lending obligations under the NCCP Act and APRA's standards contained in its guidance for these types of loans. Supervision and enforcement of these loans will also remain the responsibility of ASIC as well as APRA. This approach complicates the consumer lending framework, rather than simplifying it.

This duplication in regulation is unnecessary as APRA's framework provides sufficient consumer protection. The increased complexity and cost of having to manage two different sets of standards may act as a disincentive to ADIs to enter into small loans and disadvantage a category of customers that already struggle to access safe and affordable credit. Under APRA credit risk management standards, ADIs could appropriately tailor their credit assessment processes to extend these loans to customers according to their serviceability capability.

ADIs generally offer small loans at competitive interest rates, backed by robust hardship policies and processes.¹

ABA recommendation: the ABA recommends the removal of responsible lending obligations for all consumer loans offered by ADIs. This can be achieved through removing the concept of 'low limit credit contract' from the Bill so that these loans are subject to APRA's framework.

2.3 Borrower responsibility principle

The Government intends to introduce a 'borrower responsibility' principle into the consumer credit framework to improve efficiency in the credit assessment process. The ABA supports introducing this principle. However, the ABA notes this principle will only be reflected in legislation for non-ADIs and there will not be a mirroring principle included in the regulatory framework for ADIs. In order to achieve the Government's intent, the principle should be reflected in requirements for both ADIs and non-ADIs.

ABA recommendation: *The borrower responsibility principle needs to be specifically referenced in the new framework for ADIs. The Government's policy intention should be referenced within the Explanatory Memorandum as applying across the finance sector including to ADIs.*

2.4 Electronic transactions

On 23 July this year, the Government repealed the *Electronic Transactions Regulations 2000* and replaced it with the *Electronic Transactions Regulations 2020* (2020 ET Regulations), which had the effect of removing the requirement for financial institutions to get express consent to receiving NCC

¹ For example, an ABA member offers unsecured loans over \$1000 at a comparison rate of 12.49%.



documents electronically, to provide certain warnings before that consent is obtained and to remove other prescriptive requirements about methods of communication. Under the 2020 ET Regulations, most NCC documents can be given more broadly in accordance with the Electronic Transactions Act 1999 (ET Act).

However, under s195 of the NCC, banks are unable to communicate electronically unless they have obtained the customer's address in writing. In addition, Regulation 28L in the NCCP Regulations imposes a strict consent requirement for electronic communication of NCCP disclosure documents similar to the previous requirements under the repealed Electronic Transactions Regulation 2000.

These inconsistent requirements have made it difficult for customers to understand and manage how they receive information or documents and has led to a delay of the processing of customer applications. In this regard, to give full effect to the Government's intent of facilitating technology neutral communication between entities and their customers through the Electronic Transaction Regulations 2020, the ABA suggests that s195 of the NCC be amended to remove reference to the requirement to nominate an address in writing, and Regulation 28L be amended so that the NCCP disclosure documents covered by that regulation can be given in accordance with the ET Act and 2020 ET Regulations.

ABA recommendation: *Treasury remove references to requiring an address to be nominated in writing in section 195 of the NCC and amend Regulation 28L in the NCCP Regulations to align with the 2020 ET Regulations as part of the Government's intent of improving efficiency in the provision of credit.*

3. Maintaining strong consumer protections

The ABA supports the Government's intention to maintain strong consumer protections under the consumer credit framework. The ABA notes the following significant protections are being maintained in the exposure draft materials as well as the broader regulatory and self-regulatory framework.

3.1 Credit card term

The ABA supports the retention of the requirement to assess whether a customer can repay their credit card limit within a reasonable period. This is being imposed through sections 8 and 9 of the Non-ADI Credit Standard and clause 60 of the BCoP.

3.2 Reverse mortgages

The ABA supports the draft Bill's retention of the special conduct provisions as they relate to reverse mortgages as the risk associated with these mortgages can be significant.

We note that the Bill has maintained the requirement to give equity projections, but from 1 March 2021, this obligation is required prior to the licensee providing credit assistance or entering the credit contract. In addition, we note and support the requirements of the licensee to:

- ask the consumer about their expected future aged care accommodation costs, and
- present the consumer's expected future aged care accommodation costs alongside the equity projection, in a manner allowing the consumer to understand how the equity expected to be left in the home may impact their ability to afford aged care.

The ABA submits that there are some APRA standards relating to reverse mortgages that should apply to non-ADIs. This is because these standards, while also prudential in nature, have a direct consumer protection effect and are necessary to protect all consumers.

APRA's APG 223 outlines specific guidance on the appropriate measures that ADIs need to take to address operational, legal and reputation risks around consumer protection and loan enforceability in relation to reverse mortgage loans. This includes:

- LVR caps related to the age of the borrower



- cautioning borrowers against waiving independent legal and financial advice, and
- higher levels of controls and monitoring when marketing such loans through third party channels.

We believe that these are essential customer protections that should apply whether a reverse mortgage is entered into by an ADI or non-ADI lender.

ABA recommendation: *Treasury augment the Non-ADI Credit Standard with obligations that reflect the following aspects of APG 223:*

- *LVR caps related to the age of the borrower*
- *cautioning borrowers against waiving independent legal and financial advice, and*
- *higher levels of controls and monitoring when marketing such loans through third party channels.*

3.3 Banking Code of Practice

The ABA's BCoP sets standards of practice for ABA member banks and other subscribing institutions by providing safeguards and protections for certain customers. The BCoP contains several provisions that align with the obligations in the NCCP Act. Protections for customers in the BCoP include, but are not limited to:

- clause 49 - provides that ABA subscribing banks will exercise the "care and skill of a diligent and prudent banker" when providing credit to an individual or small business customer
- clause 50 – stipulates that this 'prudent and diligent banker' standard requires banks to comply with the law for individual customers
- clause 51 - for small business lending this 'prudent and diligent banker' standard requires banks to consider the customer's circumstances involving the financial position and account conduct
- clause 54 – stipulates that ABA subscribing banks will not approve a co-borrower if they will not receive a substantial benefit from the loan, unless the subscribing bank meets certain requirements including the need to take reasonable steps to ensure the customer understands the associated risk; the need to take into account the reason for the customer wanting to be a co-borrower; and the bank is satisfied that the customer is not experiencing financial abuse
- clause 61 – stipulates that a customer can advise the subscribing bank of their preferred credit card limit and restricts the subscribing bank from giving the customer a limit that is more than the customer requested, and
- clause 38 – commits subscribing banks to taking extra care with customers who are experiencing vulnerability.

The guiding principles of the BCoP commit subscribing banks to, among other things, acting honestly and with integrity, being fair and responsible in dealings with customers, and taking a responsible approach to lending.

The BCoP is enforced by an independent Banking Code Compliance Committee that is responsible for investigating breaches of the BCoP. It applies as a matter of contract between the bank and the customer, which means a customer can institute legal proceedings for a subscriber's non-compliance with the BCoP. In addition, customers can seek redress for a subscriber's non-compliance with the BCoP through an external dispute resolution determination by AFCA. As a standard of 'good industry practice', AFCA can consider the BCoP in matters involving ABA subscribing member banks and can also refer (but not necessarily apply) the BCoP to disputes involving non-subscribing financial firms. We note that there are some ADIs that are not subscribers to the BCoP.



3.4 Australian Securities and Investments Commission Act

The Australian Securities and Investments Commission Act 2001 (ASIC Act) applies to suppliers of credit products and services, including suppliers of business credit and investment credit. It imposes prohibitions against misleading or deceptive conduct, unconscionable conduct, implied terms in the supply of financial services and unfair contract terms.

The ASIC Act also provides ASIC with extensive enforcement and redress powers in response to any contravention of the prohibitions. These powers include undertakings, substantiation notices, public warning notices, injunctions, damages, compensatory orders, redress for non-parties, non-punitive orders, while also providing ASIC with the ability to impose civil and criminal penalties. In addition, under section 50 of the ASIC Act, the regulator has broad powers to begin a civil action to recover damages or property for persons (including companies) who have suffered loss provided those persons give their consent.

3.5 Design and Distribution Obligations and Product Intervention Powers

The Government has also introduced a new design and distribution obligation (DDO) for financial institutions which is set to commence operation on 5 October 2021. The DDO will require financial product issuers and credit providers to develop and distribute products to appropriate consumers by requiring issuers and distributors to have a targeted and principles-based approach to designing and distributing products. This will reduce the risk of consumers acquiring or being mis-sold products that do not meet their needs.

In addition, the Government has provided ASIC with a product intervention power that will allow ASIC to ban, or amend, a credit or financial product where that product has resulted, or is likely to result, in a significant consumer detriment.

3.6 Comprehensive Credit Reporting

The ABA supports the Government's Comprehensive Credit Reporting legislation as an important mechanism for lenders to access richer data sets about their customers from credit bureaus to make more informed lending decisions.

The major banks are now participating in the CCR regime and the ABA supports passage of the legislation through the Parliament.

4. Consistent regulatory framework across industry

The ABA supports a level regulatory playing field and the Government's intention to extend relevant APRA requirements to non-ADIs. At present, ADIs appropriately have additional prudential regulation to protect deposits with several prudential regulatory requirements relating to serviceability such as those found in APG 223. These require ADI lenders to have systems and processes in place to assess whether customers can afford to repay a loan over its term.

In addition to being prudential measures, some of these requirements have a direct consumer protection effect. The ABA proposes that those prudential measures that significantly strengthen consumer protection should also be reflected in the Non-ADI Credit Standard to ensure consistent consumer protections, serviceability assessments and regulatory compliance requirements across all lenders and lending markets. This will reduce any differences in regulation, contribute to a more level playing field for all credit providers, and ensure customer protections.

4.1 Consistency of ADI and non-ADI requirements

The ABA welcomes the application of some ADI prudential standards on non-ADIs as proposed in the Non-ADI Credit Standard. We note that these system-level obligations for non-ADIs are consistent with the Government's intent to move away from a prescriptive approach focused on individual loans.



While we appreciate the Government's intention to simplify the existing APRA requirements required by APG 223, APG 220 and APS220 for non-ADIs, we highlight below some inconsistencies between the standards imposed on ADIs and non-ADIs that may negatively impact on competition and result in adverse customer outcomes.

Specifically, the ABA proposes that the Non-ADI Credit Standard include obligations for non-ADIs to:

- consider potential upwards changes to a customer's interest rate through the application interest rate buffers and floors, and
- apply appropriate adjustments when assessing seasonal or variable income sources and considering future changes in a borrower's circumstances, such as a likely lower income and repayment capacity during the impending retirement of a borrower.

For example, assessment of the customer's sensitivity to the effect of an increase in interest rates on repayments is identified in RG209² indicating that such assessment has a clear consumer protection aspect. Further, applying adjustments to seasonal or variable income will assist in avoiding substantial hardship brought about by the overstatement of income by the customer.

ABA recommendation: *Treasury consider how these important consumer protections and level playing field measures could be applied in the non-ADI framework.*

4.2 Impact on non-ADI subsidiaries

Banks often have non-ADI subsidiaries within their corporate group and the ABA have identified that the proposed reforms to the framework may result in some of these subsidiary entities (those which undertake the relevant credit activities) being subject to both APRA's APS 220 as well as the Non-ADI Credit Standard. This is because APRA applies APS 220 to not only the ADI but also other entities within the 'Level 2 ADI Group' such as non-ADI subsidiaries.

We submit that this would result in unnecessary duplication and be inconsistent with the Government's intention to simplify the regulatory framework, and without change will result in a distortion in the landscape for a competitive market.

ABA recommendation: the Bill to define ADI to include the 'Level 2 ADI Group' to ensure that relevant subsidiaries are not regulated by both APS 220 and the Non-ADI Credit Standard.

5. APRA and the consumer credit reforms

The consumer credit reforms rely on ADIs no longer being subject to NCCP Act responsible lending obligations and instead to the APRA standards, including those requirements contained in:

- APS 220 - Credit Risk Management (updated standard to come into effect on 1 January 2022)
- APG 220 - Credit Risk Management (existing guidance), and
- APG 223 - Residential Mortgage Lending (existing guidance).

The ABA supports maintaining APRA's role in developing and enforcing a robust prudential framework that promotes prudent behaviour by ADIs. We also believe that a fundamental objective of these reforms is to enable prudent risk taking by ADIs, including allowing the nature of an ADI's assessment to be scalable and flexible according to the nature of the product as reflected in APG 220.

5.1 Amendment to APS 220

The ABA notes that Treasury has indicated in the Explanatory Memorandum to the Non-ADI Credit Standard that APRA plans to consult on a minor amendment to APS 220 with the addition of a

² RG209.205

sentence that would require an ADI “to assess an individual’s capacity to repay credit without substantial hardship.”

We support this addition to APS 220 as this is in line with existing practice and aligns to the ‘prudent and diligent’ lending obligations in the BCoP. The ABA anticipates that APRA would supervise this requirement consistent with its current approach of considering the adequacy of the institution’s systems and processes (rather than assessing outcomes at the level of an individual credit contract).

5.2 Further engagement with APRA

Given APRA’s role under the proposed reforms, the ABA acknowledges that the banking industry will need to work directly with APRA on the operation of its standards and guidance as the new framework comes into effect.

6. Small business lending – mixed purpose loans

In its original announcement of these consumer credit reforms, the Government indicated an intention that “where a proportion of an application for credit is for a business purpose, irrespective of the proportion, the new framework will not apply”.³ The application of responsible lending obligations to small business customers where loans often cover a mix of regulated and non-regulated purposes (mixed purpose loans), and multiple sources of income and expenses has created complexity for lenders.

While the responsible lending obligations are being removed from the NCCP Act (other than for SACCs and consumer leases), the consumer credit reforms do not alter the ‘predominant purpose test’ and as a result, mixed purpose loans will continue to be subject to the other obligations under the NCCP Act, (e.g., general conduct and disclosure obligations).

Further, under the proposed framework, the non-ADI Credit Standard will not apply to small business credit where a “not merely minor or incidental” part of the overall purpose of the loan or increase is for a business purpose. This will mean that the assessment of mixed purpose loans by non-ADIs is effectively unregulated under the new framework, while the same loans when offered by an ADI are subject to the APRA framework. This not only creates an uneven playing field but provides an inconsistent set of requirements for customers to satisfy depending on whether they are dealing with an ADI or a non-ADI lender.

7. Role of AFCA in proposed consumer credit framework

The ABA notes that AFCA’s role in making determinations on disputes involving the provision of credit will be critical to whether the consumer credit reforms meet the Government’s stated policy intentions.

At present, AFCA considers a range of sources in considering lending disputes, including the NCCP Act requirements, ASIC’s responsible lending guidance, the ‘diligent and prudent banker’ standard under the BCoP, previous relevant determinations, and what is “fair and reasonable in all the circumstances”. The consultation materials provided by Treasury do not offer an insight into whether AFCA’s role in making determinations in respect of credit complaints will change under the proposed reforms.

ABA recommendation: *the ABA recommends that clear guidance needs to be provided to AFCA in the Explanatory Materials as to how it should consider both non-ADI and ADI credit related customer complaints, including the lending standards that are to be applied.*

Further, we recommend that AFCA commence consultation on the development of its Approach to responsible lending as soon as practicable after the finalisation of the consumer credit reforms.

³ Australian Government, *Fact sheet: Consumer Credit Reforms*, available at: <https://ministers.treasury.gov.au/sites/ministers.treasury.gov.au/files/2020-09/Consumer-credit-reforms-fact-sheet.pdf>



8. Best interest duty for credit assistance providers

The ABA notes that the consumer credit reforms will extend the mortgage broker best interest duty to other credit assistance providers and will require those providers to comply with the duty in relation to credit contracts.

This duty will not apply where the credit representative or licensee performs the obligations or exercises the rights of a credit provider in relation to the majority of the credit contracts or where the credit assistance provider is offering credit contracts from one credit provider. While we understand that this is intended to exclude the duty from applying to bank staff in the proprietary channel, we suggest the Explanatory Memorandum to the Bill be amended to make this clearer. At present, it refers to “all credit assistance providers” while the Bill has been drafted to clearly exclude some credit assistance providers from being within the scope of the duty.

The ABA also seeks clarification on the scope of the best interest duty if responsible lending obligations are removed from the NCCP Act. The duty was introduced in the context of responsible lending and was not intended to include an assessment of affordability, in light of the borrower’s overall financial position. The duty should apply to the assessment of the product and it should be up to the lender to determine whether the applicant can afford that loan in accordance with that lender’s criteria and risk appetite. The lender should be able to elect to rely on the information provided by the credit assistance provider unless it has reasonable grounds to believe the information is unreliable.

Further, it is unclear to the ABA if this duty will apply to an individual where they are providing credit assistance in relation to the products of multiple credit providers under the same corporate group. We believe that the drafting should explicitly exclude the duty applying where an individual provides credit assistance regarding the products of credit providers within their corporate group (as opposed to single credit provider). In addition, some ABA member banks operate franchising models, whereby the individual / community own the bank branch and have entered into a franchising agreement with the financial institution, while other member banks provide credit assistance in relation to white labelled credit cards, where they are not the credit provider. On this basis, we seek further clarity that these types of arrangements will not be captured by the proposed extension of the best interest duty.

ABA recommendation: *the ABA recommends that the Explanatory Memorandum provide greater clarity on the application of the best interest duty to credit assistance providers, outlining that this duty will not apply to those providers who assist with the products of entities in the same corporate group, bank branch franchising arrangements, and those arrangements where a bank acts as a credit assistance provider in relation to white labelled credit cards.*

Further, it should also stipulate that a lender when receiving loan application information from credit assistance providers may choose to rely on the information provided by the credit assistance provider unless it has reasonable grounds to believe the information is unreliable. Any such provision included in the non-ADI framework should be reflected in APRA guidance for ADIs.

9. Application and transitional provisions

The transitional provisions of the draft Bill outline that the consumer credit reforms will commence operation on 1 March 2021 and that the new regulatory framework will apply to credit contracts entered into on or after that date. The ABA fully supports this proposed application date as it will ensure consistent implementation across the industry and provides necessary certainty for customers.