Independent Review

Code of Banking Practice

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1. INTRODUCTION

1.1. Nature of Review

The Code of Banking Practice (the Code) is an industry initiative which sets standards of good banking practice. The Code took effect on 1 November 1996. It was most recently reviewed in 2008 with amendments taking effect on 1 February 2014.

My review of the Code follows Terms of Reference from the Australian Bankers' Association Inc. (ABA) dated 7 July 2016. Those Terms of Reference are at Attachment 1 to this Report and include:

> *"The banking industry recognises that customers and the wider community expect banks to make sure they have the right culture, the right practices, and the right behaviours.*
>
> *The Code review will make sure the offer of banking products and services is done in a way that further lifts standards, accessibility and transparency across banking and bolsters the existing strength of the regulatory framework.*
>
> *Banks are committed to improving their practices and continuing to meet customer needs and community expectations. We want to make sure our Code of Banking Practice is effective in enhancing banks' capacity to serve consumer interests and to building trust and confidence in banks."*

My review has encompassed submissions from the public, community organisations, small business representative organisations, consumer representative organisations, banks, the ABA and other stakeholders. I have also drawn upon Parliamentary Inquiry and government reports published during the last 5 years probing matters relating to the banking sector. In addition, I have met with a large number of stakeholders both in one-on-one meetings and in group forums. The ABA, banks, government officials, consumer representatives and many other organisations have also been most helpful in providing information. I have also spoken extensively with others currently conducting related reviews. I gratefully acknowledge much assistance.

1.2. Structure of Review report

This report had to deal with a wide range of issues and a significant level of detail, with submissions including over 150 specific proposals. In order to make the Report reasonably digestible, it begins with a series of chapters that are designed to convey the overall thinking and principles that I have used to guide the key findings and recommendations.

There is a brief Executive Summary and the body of the Report is divided into 20 Chapters covering the main propositions put to me. Not every observation made to me is exhaustively dealt with – I have tried to focus on what I thought was most important. My apologies to those whose issues were not covered in detail, however I have made 100 detailed recommendations, already too many for readers to absorb, I fear.

I have also made a number of observations and suggestions in the body of the Report that I did not choose to turn into a firm recommendation. In some cases, this was because I was not entirely convinced, in some cases because I think that there is already enough change contemplated in that area of the Code and in some cases because I think some other change must be made and embedded before it is sensible to go any further. These comments are for the ABA and signatory banks in considering their response, to show stakeholders what the thinking process was – and perhaps for a future reviewer of the Code.

I have been conscious that readers will have differing levels of knowledge of banking practice and law and the issues I have been grappling with. In drafting, I have tried to accommodate that range of knowledge whilst keeping the discussion of each issue as succinct as possible. To aid readers, I have a list of defined terms as Attachment 3.

I have also been conscious that there will be readers who are interested in all issues and others who are just interested in a subset of issues. Hopefully the division of my Report into Chapters should assist those focused on a specific topic. To aid those interested in small business issues, I have included as Attachment 4 a list of the recommendations that I consider are most important for small business.

1.3. Banks importance

My Report deals with a number of issues of principle about the role and importance of banks in our community. It also deals with much of the community criticism of banks – arising from the past decade or so.

While all of that is important context for the Review, it is not my role to 'put the banks on trial' – however much that may disappoint some. My task is to identify ways that the Code can be strengthened and in particular used to improve levels of trust between banks and the community.

1.4. A Code at all?

Early in my initial enquiries, I realised that a threshold question for the Review was whether there should be a Code at all. A number of stakeholders asked the question as to whether the Code continued to add value and whether it produced sufficient value to be worth the effort.

It is apparent that the Code is perceived by stakeholders to have 'shrunk' in its impact and influence over time. A number of new legal requirements have overtaken the Code (discussed at Chapter 3.2.) leaving some of it redundant for some customer groups – and making its impact more difficult to distinguish from other sources of obligation.

In addition, the existing Code was drafted in 'first-generation' plain English, a style that is no longer good practice and has been overtaken by more modern codes, by regulatory guides and policy and by the Industry's own policy documents. I think that this adds to some stakeholders' sense that the Code may have passed its 'use-by' date.

While I accept these sceptical observations, I have not been persuaded that it would be sensible to abandon the Code. Even within its current reach, there remain Code provisions that would have to be maintained by some other means – presumably by new law. The process of developing new law in financial services is neither quick nor efficient and would not be a burden welcomed by government. Of course, such law reform would also have to wait to reach the 'top of the pile' of highly fluid government legislative priorities.

More important to my mind is the difference between legislative obligation – an imposition by the community on the banks, and a voluntary code – a promise by the banks to the community. This distinction is often forgotten, particularly during consultative processes such as this Review, where stakeholders often frame their proposals as if they were black-letter obligations imposed on the banks.

For the industry's part, they have expressed considerable support for the continuation of the Code as a self-regulatory component to the overall framework for banking services. For industry, the idea of the Code being made up of promises made on a voluntary basis by banks to the community is important.

My Report discusses many of these characteristics of a Code in some detail, however, my view about the question of the Code's continuation has not changed. The Code has achieved things for both industry and customers over the past couple of decades that could not have been done in legislation and for so long as this remains possible, then in my view, it is worth the effort of developing, maintaining and monitoring a voluntary Code.

The signal challenge in front of signatory banks today is one of restoring trust and I see a voluntary Code, framed as promises to the community as a better vehicle to achieve this than government-imposed legislation. I also see a voluntary Code as able to be more flexibly framed than legislation, easier to understand than the law and in theory at least, much faster to update and evolve over time.

I understand that there are many challenges ahead of the banking industry. Interests of different stakeholders must be balanced, there are legal, practical, system and cost issues to navigate in implementing change and of course, all of this in a highly fluid environment. The banking industry have told the community that "we hear you, we are delivering change now[1]". For the restoration of trust that the industry wants, the Better Banking initiatives, including a new version of the Code, must, in my view, deliver on these two statements. To the best of my ability, I have prepared this Report to provide Code signatory banks with a path that will give them the best chance of achieving this.

[1] http://www.betterbanking.net.au/

2. EXECUTIVE SUMMARY

I have been asked by the banking industry to provide an independent review of the Code of Banking Practice at a time when community pressure on the banking industry is high. The industry has acknowledged this pressure and has made a significant commitment to win back a greater level of trust. This environment has added complexity to my task, however in many ways it is perhaps the best of times to be a reviewer. The essential elements of this Report are very briefly summarised below.

1. Value of a Code

I have listened to a range of views, both positive and sceptical, about the value that the Code currently provides, and aspirations that industry and stakeholders have for improving trust and confidence in signatory banks. I think that a new Code (along with other Better Banking initiatives) will provide the industry with an opportunity to signal a new way of working and will be a worthwhile endeavour.

2. Building trust

I have focused my review as much on the challenge of rebuilding trust between banks and their customers as I have on the many technical and specific fairness issues raised with me. Taking into account views put to me by small business and consumer representatives, bank customers, politicians, regulators and others, I have made recommendations aimed at meeting community expectations of banking practices that are seen as fair, predictable and trustworthy. Some of the proposed changes will mean some cost and effort for signatory banks to implement, however I see significant benefits in the long term for the community and for banks.

3. A broader scope

The current Code is only a part of a complex tapestry of obligations that also come from other codes and the law. My recommendations envisage a new Code that reaches further within that tapestry – in the breadth of issues that it covers, in the depth of some of its provisions and the customers that it provides protection to.

4. Code language, structure and authority

My view is that the Code could be much more effective if redrafted in a modern structure, based on key principles, in a plain-speaking style with fewer carve-outs and exceptions, and with supporting detail in linked Industry Guidelines.

This is not to imply that the new Code should be any less enforceable. I have recommended that the new Code be approved by ASIC and a substantially strengthened role for Code monitoring – in particular, in providing assurance to the community that the Code is being complied with.

5. Small business issues, including impaired loans

A primary issue for the review, my recommendations address some of the issues raised at government inquiries – in particular, better information for businesses applying for credit, more time to respond to changes imposed by banks, extending protections to small businesses in financial difficulty or whose loans are in default, access to valuers and accountants reports and improvements in access to dispute resolution.

I am conscious that there are others looking at small business and banking - notably the Australian Small Business and Family Enterprise Ombudsman and Financial Ombudsman Service and they will report after my report is due. Their recommendations will of course, have to be taken into account where they impact on the Code.

6. Responsible lending and credit cards

Responsible lending and credit cards have been subject to previous government reviews and were a focus of submissions to the Review. I have had the benefit of considering analysis from Treasury and the Australian Securities and Investments Commission.

I have recommended improved information and transparency for customers in a few places in the credit process. I recommend some restriction on the way credit card credit is marketed and provided, including a more responsible approach to credit limit increases and making it easier for customers to reduce or cancel their credit card accounts. I have also recommended some changes to interest charging and payment application practices that I think would be simpler for customers to understand and perceived as fairer.

I did not go as far here as some asked me to, as I think that some customer behavioural issues are not as clear cut as they might first appear. I look forward to the results of Treasury's testing of some possible further reforms and would expect the industry to engage with those on release.

7. Borrower default

My focus in this area has been on recommendations that will help borrowers who are in trouble with their credit to be given a fair chance to put things right, that they have fair access to information that would assist them and information about adverse credit reporting made about them.

8. Joint account holders and guarantors

There has been increasing concern in the community about financial exploitation and although guarantors already derive substantial protections under the Code, I have recommended some further enhancements to the Code for their benefit. I have also recommended better protections for joint account holders (recognising issues that can arise particularly after a relationship breakdown).

9. Financial difficulty

Submissions to my Review recognise that the banks' financial hardship processes provide very significant assistance to large numbers of consumers and went on to make requests for further enhancements to the Code provisions. This is an area where similar language has made the interplay between the Code and the law quite confusing and improving clarity and understanding about this would be a step forward in itself.

I have recommended more clarity about any assistance that is being provided by the bank and the potential consequences for the customer. While recognising that there are limits to what banks can do, I have also recommended more effort in the area of prevention - to proactively identify customers at risk of financial difficulty and to offer them assistance to avoid their circumstances deteriorating.

10. Banking terms and conditions, fees, cancellations

This is an area where I think a good deal of the community's mistrust arises from. Excessively legalistic terms and conditions, provisions that give the bank what seems to be unfair power, fees that are seen to be 'hidden' or out of proportion and so on, all contribute to a sense that a customer cannot 'just trust' their bank.

While I am not able to make recommendations about the level of specific fees, I have made a couple of recommendations for the Code that address the overall approach by banks to setting fees and informing customers.

Stakeholders also reported niggling and continuing problems experienced by a comparatively few customers with day-to-day issues such as direct debits and recurring credit card payments. These issues simply must be fixed, otherwise they will continue to undermine goodwill towards the banks. Some of these are technically complex issues that are enmeshed with the operation and rules of the quite separate credit card schemes, which I understand will take some time for banks to resolve. Other issues seem to be a problem with staff understanding of customer rights. I have recommended that signatory banks' new Customer Advocates take on the challenge of these latter issues.

11. Marketing and sales practices

A big part of this issue is being reviewed separately by Stephen Sedgwick AO – and I have left the issues of incentives and remuneration to that eminently qualified reviewer. I have made recommendations about customer practices in cross-selling (in particular, consumer credit insurance) and in lenders mortgage insurance – two areas of concern amongst regulators and consumer advocates.

12. Consumers with special needs

The Code and industry have already done much to recognise customers with special needs, however the community's understanding of these needs continues to evolve. I received a number of submissions suggesting improvements to recognise additional groups of customers and additional specific needs, including access to basic bank accounts.

I have recommended a principles-based approach to this aspect of the Code, with Industry Guidelines to pick up the specific requirements of different groups – much as the Industry Guideline on Financial abuse and family and domestic violence policies.

13. Code Monitoring

The current code-monitoring mechanism for the Code, the Code Compliance Monitoring Committee, came in for some criticism from stakeholders – its role, positioning and mandate were widely seen as inadequate. I have included a lengthy discussion of the issues and recommended a different and strengthened role focused on 'monitoring' – both for compliance and good practice and for much improved assurance to the public that industry is complying with the Code.

14. Conclusion

A full summary of the Recommendations I have made is in Attachment 6.

Finally, having completed the easy part, I am conscious that the hard work now falls to signatory banks. I have made a few observations reflecting stakeholder concerns about the implementation process, the redrafting of the Code, drafting of new supporting guidelines, transition to new requirements and so on – and offered any assistance I am able to give to get the implementation process off on the right foot.

3. ROLE OF THE CODE

3.1. Application of the Code

The ABA has 25 member banks, of whom 13 bank groups are signatories to the 2013 (latest) version of the Code. The remaining members are either signatories to an earlier version, are new members awaiting the next version of the Code or have chosen not to subscribe to the Code. The ABA advises that over 95% of banking services in Australia are provided by banks that are signatories to the Code (see information provided at Chapter 4.1).

The Code is also important because the Financial Ombudsman Service (FOS), in its decision making about banking complaints, may have regard to the Code as a representation of good industry practice[2]. In practice this means that provisions of the Code may be applied across the industry by FOS – and banks that are not formally signatories adopt at least some of the higher standard practices of the Code as a matter of practicality.

3.2. Content of the Code

The Code provides protections to customers who are individuals (individual customers) or small businesses and their guarantors.

Code provisions address bank accounts, bank transfers, loans, credit cards, terms and conditions, account statements, financial difficulty, debt collection, dispute resolution and related matters. All of these matters are subject to other legal requirements that have continued to evolve since the Code was first conceived.

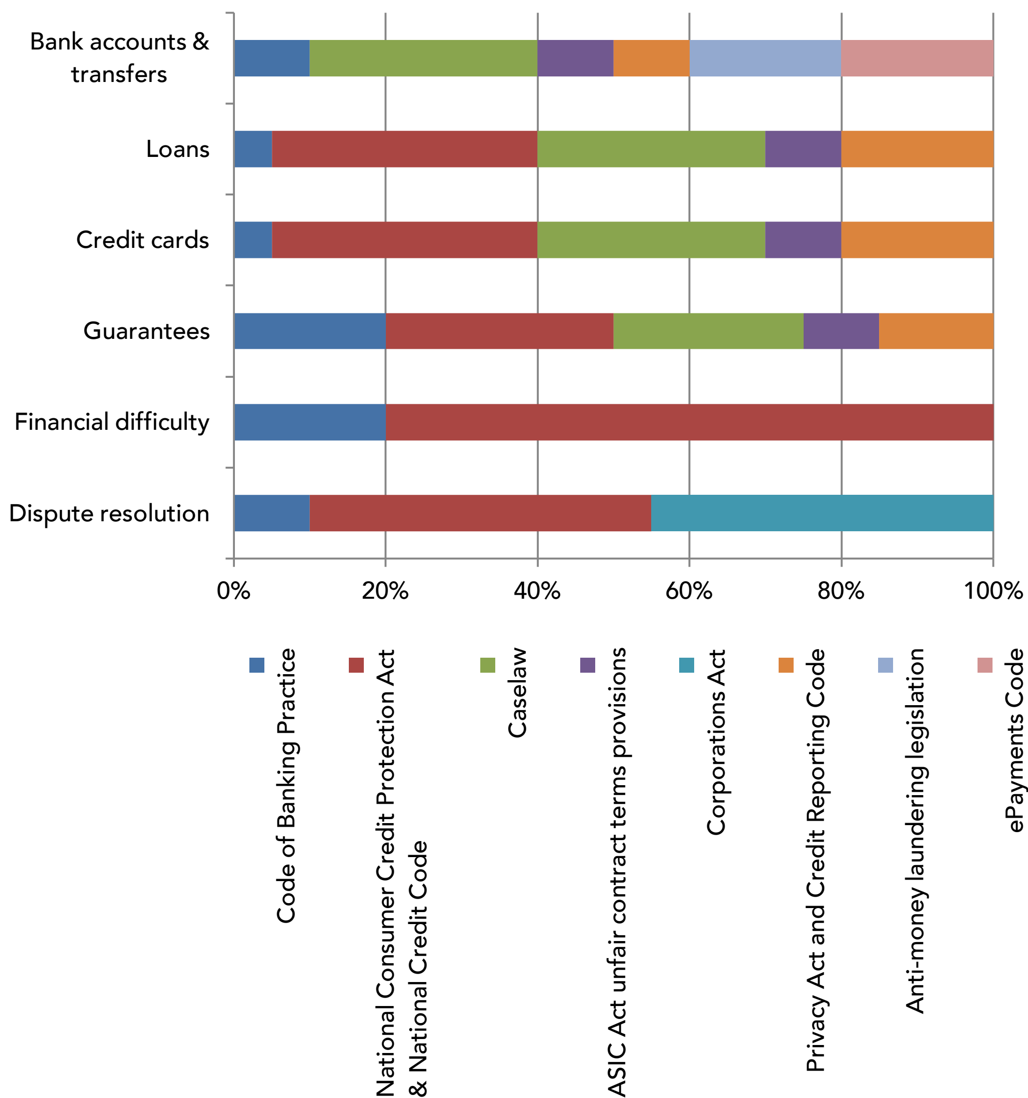
This is quite a complicated 'tapestry' of obligations, and quite indigestible as a table or lengthy list, so I have attempted to provide a graphical representation of the relative practical impact that the current Code provisions have on common banking services compared with other sources of obligations.

Taking the first example in the chart in Figure 1. below (bank accounts and transfers), signatory banks' key regulatory obligations include, in addition to the Code, three major Acts of Parliament, case law, and two other legally binding Codes. My estimation is that the relative impact of the Code on this group of services is around 10% of the total. In other words, of all the obligations that banks must currently meet for bank accounts and transfers, the Code only makes up about one in ten.

[2] The FOS Approach to the 2013 Code of Banking Practice, http://www.fos.org.au/publications/our-approach/

It is clear from this representation that the Code is just one of many elements and it is important not to overstate its current impact. For readers of the Code, it means that the task of understanding the Code is complicated by the need to understand related legal obligations. For banks, this representation graphically supports their contention that as a matter of practicality, business procedures, training and compliance documentation must be built around products or common processes and integrate all the obligations that apply. A staff member must know how to write a loan correctly, not necessarily which requirements come from the Code and which originate from (say) case law.

Figure 1. Relative significance of requirements imposed on banks from different sources



Source: Independent Reviewer estimate

The Code also establishes a body, the Code Compliance Monitoring Committee (CCMC), to monitor compliance by banks with the Code. Attached to the Code is the CCMC Mandate that sets out the committee's functions, responsibilities, composition, staffing, compliance monitoring processes and sanctioning powers.

3.3. Position of the Code

A part of this tapestry of obligations, the Code operates at a number of levels:

1. There are some Code provisions that impose broad principle-level obligations.

   In particular, clause 3.2 obliges signatory banks to act fairly and reasonably towards customers in a consistent and ethical manner.

2. There are some provisions of the Code that have largely been overtaken by case law and legislation designed to protect consumers. As a result, those provisions, although expressed as applying to all Code customers (individuals and small businesses), now have importance principally for a relatively small subset of Code customers not already covered by the law.

   For example, clause 27 of the Code (Provision of credit) imposes responsible lending obligations on signatory banks. Clause 27 is expressed as applying to loans to all Code customers. However, the National Consumer Credit Protection Act 2009 (NCCP Act) imposes a more detailed responsible lending regime for consumer credit regulated by the National Credit Code (consumer credit). This regime applies to the vast majority of loans to individual customers but does not apply to loans for business purposes. The result is that arguably clause 27 adds nothing for consumer loans but continues to have importance for loans to individuals that are not regulated by the National Credit Code and for loans for business purposes.

3. There are some provisions where the Code summarises and adds to legislative and case law obligations.

   For example, most of the requirements in clause 31 (Guarantees) duplicate obligations in the National Credit Code. Those duplicated provisions add nothing by way of protection for a guarantor of consumer credit regulated by the National Credit Code, but a guarantor of a small business loan gains protections that may not otherwise apply.

   Clause 31 does not, however, simply duplicate National Credit Code obligations. It also adds some additional requirements that benefit all Code customers, for example, some requirements as to the information that must be provided to guarantors.

4. There are some Code obligations that are entirely independent of legislation or case law requirements and so create protections that would not otherwise apply.

   For example, clause 21 obliges signatory banks to promptly fulfil a Code customer's request to cancel a direct debit arrangement.

Clause 41 of the Code specifies that signatory banks are bound by the Code in respect of any banking service and guarantee. Clause 12.3 provides:

> *"Any written terms and conditions will include a statement to the effect that the relevant provisions of this Code apply to the banking service but need not set out those provisions."*

As a result, "relevant provisions" of the Code become part of the contract with the Code customer. The Courts have confirmed this. In a recent case, the Victorian Court of Appeal held that clause 25 (Provision of credit) was a "relevant provision" and so incorporated into the terms of a guarantee[3].

[3] Doggett v Commonwealth Bank of Australia [2015] VSCA 351

4. CONTEXT FOR THE CODE REVIEW

It would be impossible to approach this Review in isolation from the current context – one in which a series of scandals and failures have called into question the banking industry's bona fides, competence and fairness. The banks have been criticised heavily by the community, by media commentators, by government committees, by regulators and the courts.

Calls for a Royal Commission into the sector have been resisted by the industry[4], by some commentators and by the Commonwealth government. The package of reforms initiated by the industry (Better Banking) including this Review have generally been welcomed by stakeholders, however it has been criticised by some as too little, too late and as simply an attempt to avoid a 'tougher' process.

I have encountered these critical views multiple times during the course of my consultations, although to their credit, most critics of the process I am conducting were still willing to contribute their perspectives and ideas to the Review – and to wish me well in my endeavour.

I mention this in particular, because whether supportive or critics of this process, almost all I spoke to, including many within the industry, expressed the strong view that the recommendations of this Review would have to be significant or 'transformational' in nature to overcome scepticism in the community towards the banking industry. While I have not agreed with all submissions put to me, I have been influenced by these views. It seems to me to be the worst of outcomes for the signatory banks to go to great effort and cost to produce a better, voluntarily strengthened Code – only to have it howled down.

4.1. Industry share of Code signatory banks

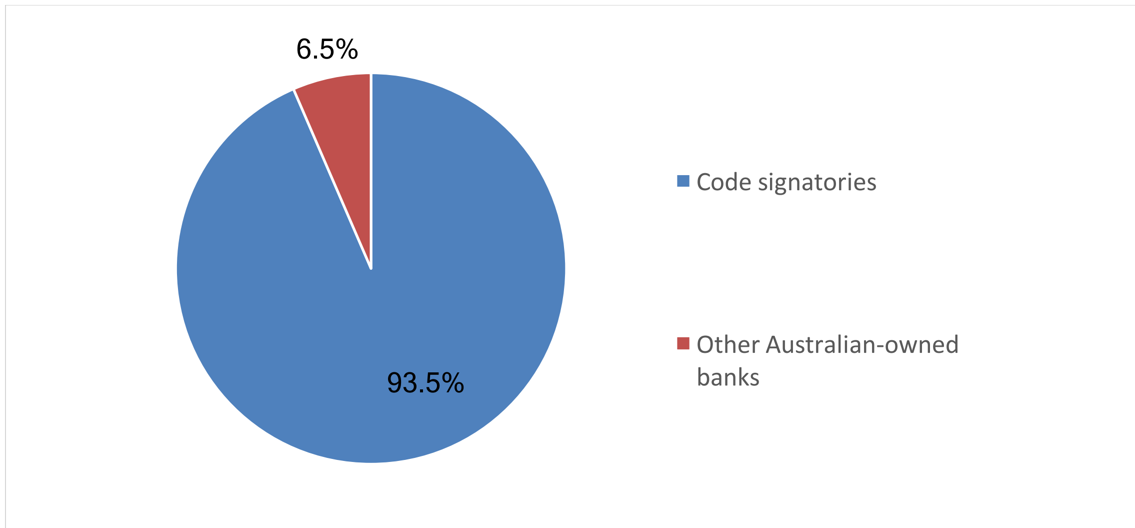
As at 20 December 2016, there were 31 Australian owned banks, 7 foreign subsidiary banks and 45 branches of foreign banks operating in Australia[5]. As discussed, 13 banks are signatories to the Code, and they are very dominant both in deposit taking and lending as the following figures show. (For both foreign-owned banks and foreign bank branches, their share of household banking deposits is less than 0.1% and so does not appear in the chart below.)

Note that some member banks probably do not have any banking services that would fall under the Code and some of the newer member banks are former mutuals that are subscribers to the Customer Owned Banking Association ("COBA") Code.

[4] http://www.betterbanking.net.au/delivering-change-now/

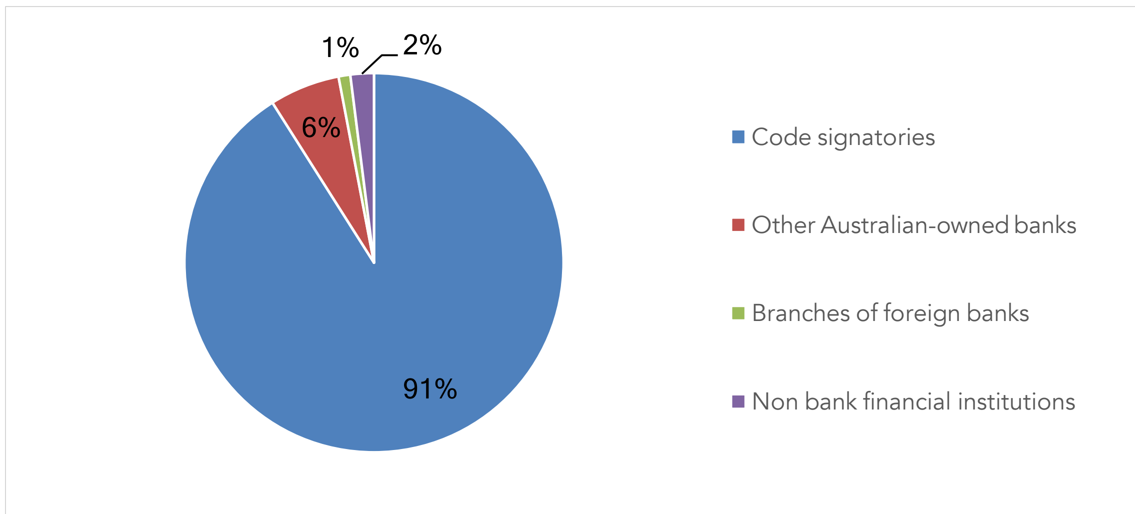
[5] http://www.apra.gov.au/adi/Pages/adilist.aspx

Figure 2. – Share of banking deposits



Source: APRA monthly banking statistics, September 2016 (released 31 October 2016)

Figure 3. – Share of bank lending to households



Source: APRA monthly banking statistics, September 2016 (released 31 October 2016)

4.2. Societal importance of banks

I do not propose to attempt to add to arguments made by many commentators about the key role that banks play in the nation's economy, in its financial infrastructure and in enabling a complex society to function. The fact of this Review and the other parts of the Better Banking initiatives is evidence enough that the community expects – and the industry recognises – that banks have a responsibility beyond maximising profitability for shareholders.

I think from my discussions with stakeholders, that the community expectation is sufficiently clear. Banks, like any commercial organisation, should be free, indeed should be encouraged, to make profit – but that this profit should not come from exploiting what people see as the banks' privileged position and significant market power, unfairly or unreasonably.

I also see this as more than a one-way dynamic. Banks are a significant, but nonetheless dependent part of a complex financial eco-system and I think that banks themselves work best when their customers have trust and confidence in them.

4.3. Customer satisfaction

It is important to acknowledge that while there are many reports of 'banks having lost the trust of the community', this is not the full picture. Banks do enjoy high levels of customer satisfaction – at least amongst the majority of their own customers.

> *"Customer satisfaction with the big four banks remains close to historically high levels and has remained around the 80% mark for the last two years although it has shown some weakness over the last 12 months (down 1.4% points). The satisfaction of home-loan customers (77.8%) remains below that of other customers (80.7%) and has not yet recovered to where it was in September (80.1%) prior to the home-loan rate increases announced in October. This below-average satisfaction performance for home-loan customers is proving to be a drag on overall customer satisfaction. The drop in the cash rate at the start of May should boost satisfaction among borrowers but has the potential to impact negatively on depositors."*

Source: Roy Morgan research June 2016

It is also true that the banks have done some excellent work in key areas of customer protection. I have seen innovative programs by banks enhancing financial difficulty assistance, improving collections processes, addressing vulnerable customers' access to banking services – which have been producing very promising results and which are a credit to the banks involved.

Yet there have been vocal criticisms of banks by customers, particularly during the period since the Global Financial Crisis (GFC). Even with an 80% satisfaction rating, there remains one in five customers who are less than satisfied. That is a very large number of people. It is not difficult to see how an impression of a general loss of trust can emerge.

4.4. Trust issues

The key factors influencing this reported level of mistrust that were expressed to me included:

- For small business and farmers - cycles of 'easy credit' followed by periods of tightening loan conditions and restricted access to credit, when banks are perceived to be focused on reducing the risk in their loan book, (for example by unilaterally changing the terms of loans, calling in loans early, etc.) leaving customers facing high risks, or exposed to loss of trading finance, loss of assets and business failure.

- Very high interest rates, in particular on credit cards, that appear to be completely out of sync with the cost of capital and the apparent failure by banks to reduce these in line with cash rate reductions.

- Terms and conditions that are unexpected or counter-intuitive, seen as unfair or 'tricky'.

- Fees, particularly late payment and other types of 'hidden' default or exception fees continue to be a source of criticism.

- Poor loan establishment processes (often 'on-the-spot', with multiple documents for signing simultaneously) where customers do not get time or enough information to assess their position properly.

- Poorly explained cross-selling particularly of consumer credit insurance.

- Poor practices in related non-banking businesses, in particular, financial planning advice and life insurance sales and claims practices. It is clear from submissions to my review that it makes no difference to the perception of untrustworthiness that these are non-bank services. The image of the banks' corporate citizenship and ethical reputation extends far beyond core banking services - to all their activities.

Of particular importance to this review of the Code is not only that the original conduct quoted was seen as quite contrary to the spirit of the Code and public assurances by banks – but also, that the banks' response to the exposure of this poor conduct was perceived as wholly inadequate. Some of this dissatisfaction was expressed quite crudely as a demand that 'heads must roll', but for most, it was expressed as evidence of a broader failure of accountability.

While it is not my place to put the banks on trial, if I am to provide advice that goes to the question of trust, it seems to me essential that there is an understanding of what is not trusted. From the public commentary, from other inquiries, from submissions and from my interviews and consultations, I found that the mistrust is expressed in a few repeating themes:

1. **Not doing what was promised** – most often these are compliance problems or system failures or misunderstandings or inadequate staff training. Most stakeholders recognise some of these are inevitable in any very large organisation. The mistrust arises when these problems persist or the bank is not seen to take their occurrence seriously. The problem is often the perceived attitude rather than the breach.

2. **Being 'tricky'** – stakeholders raise the use of lengthy qualification of promises, overly complex or excessively lengthy Terms & Conditions, unfair contract terms including terms that allow the bank to unilaterally vary the contract, 'hidden' fees that customers only become aware of when something goes wrong, application of interest or fees in an unexpected or counter-intuitive way, and the use of euphemistic corporate language to describe less pleasant aspects of banking.
3. **Being 'secretive'** – many see the banks' unwillingness to share information as untrustworthy. Examples can include refusal to share a valuation or forensic accounting report about a business, claiming information is commercial-in-confidence when challenged by a customer or government committees, and an over-sensitivity to how information might be unfairly used 'against the banks'.
4. **High-handedness** – mentioned to me are contract terms that allow the bank to unilaterally vary the contract, repeated re-writing of terms and conditions, products and services that are designed to transfer as much risk as possible onto customers, and bank-centric language.
5. **Sweeping problems under the rug** – this includes not disclosing problems or scandals until forced to, a sense that admission of error or wrong-doing is 'through gritted teeth', poor treatment of whistle blowers, being too quick to declare that 'all problems are behind us' or that the problem was a few 'bad apples', a sense that staff are not held responsible for problems, and that those at fault are not disciplined.

4.5. Are the criticisms 'fair'?

While industry leadership has publicly accepted that banks have a 'trust issue' which they must respond to, I have seen considerable frustration amongst bank staff about this mistrust. Bank staff I spoke to do not see banks as untrustworthy. Many feel that banks are highly scrutinised and heavily regulated – and subject to unreasonable expectations and unfair criticism.

Some of the banking practices that attract criticism from outside the industry (eg. one-sided contract terms, refusing to share independent reports, apparently disproportionate fees) are seen by many within the banking industry as normal commercial behaviour – no different to practices used by thousands of other large Australian businesses. When statistics are available, they often tell a story of very small, sometimes miniscule percentages of problems occurring amongst vast numbers of satisfactory transactions carried out by banks. Where clear misconduct is discovered, staff feel that although these are exceptions, the whole industry is unfairly tarred with the same brush. Criticism from politicians and journalists in particular, is seen by many staff as highly unfair, opportunistic 'bank-bashing'.

In my view there is no doubt that this staff perspective has some truth. Banks are highly regulated. Problem transactions and practices are a minor fraction of the whole of banking services provided. However, this is not the time to be conducting a long debate about 'fairness'. In my view, this will only reinforce the perception that the community has of the banks 'not listening'.

I am also guilty of being unfair to bank staff in this Report, in that I have chosen not to spend pages explaining the banks' position on every matter. This is not to be one-sided, but because I judge that it would be unhelpful and in many cases would play to community prejudices. I have taken the view that it is my job to focus on the changes that should be made to the Code so that it better meets reasonable community expectations and to help the industry re-establish the trust that it needs.

4.6. Bank 'blind spots'

In the same way that I identified common threads to the mistrust reported to me, I also identified some repeating 'blind spots' – unconscious thinking and behaviours from within the banking industry that feed directly into the common threads of mistrust discussed above. This is not to say that these behaviours are always the case. Rather, they occur often enough to influence opinion. To illustrate:

1. **Rationality** – A natural characteristic of the banking industry is to be highly rational and numbers-driven. Where banks don't sufficiently recognise that the 'outside world' is not necessarily rational and numbers-driven, mistrust problems can be magnified. One particular aspect of this is a tendency to dismiss statistically small problems.

   Being able to say that something 'hardly ever happens' is no response at all to those to whom it has happened. This contributes to a perception of sweeping problems under the rug and not taking 'small' issues seriously, and where the problem persists, feeds into a sense of not keeping promises. An example discussed in this Report is the cancellation of direct debit arrangements.

2. **Risk focus** – Banks are risk-focused businesses. Amongst other things, they take commercial risk to make profit, they design products and services to match customers' risk/reward preferences, they are subject to competitive risk, exposed to economic risk, currency risk, political/regulatory and compliance risk.

   Because of the scale of banks, there many hundreds of staff whose jobs are focused on <u>minimising</u> risk to the bank (as opposed, I would argue, to <u>managing</u> risk). This workforce is essential to the bank and the economy, however its role is often seen as shifting as much risk as possible from the bank to the customer. This plays out most obviously in extensive use of caveats and qualifications, overly complex or excessively lengthy Terms & Conditions (the 'fine-print') or retaining 'catch-all reserve' powers to protect the bank in the event of a changed risk environment and so on.

   It is not difficult to see how these characteristics and behaviours contribute directly to external mistrust dimensions of high-handedness or 'trickiness'.

3. **Corporate language** – Bank staff live and operate in some of the largest corporate entities in Australia. Inevitably these organisations develop their own language and terminology – and as inevitably forget that this is not the language of most customers. This use of 'corporate' language, and in particular the tendency to use euphemisms and 'sugar-coating' was put to me repeatedly as evidence of untrustworthiness. (This perception of 'spin' is not exclusive to banks, but I think it is viewed with greater suspicion when it comes from very large institutions that are 'supposed to be trustworthy').

4. **Immersion in banking –** In a similar way to being immersed in corporate language, bank staff can become so immersed in banking that they no longer appreciate that the community generally has very low knowledge of money and the complexities of banking. Again, I see this exacerbating some of the impressions of mistrust.

5. **Secrecy** – two factors stand out to me as bank behaviours that play into this community perception of excessive secrecy. The first is commercial-in-confidence concerns over competitive advantage. From comments put to me, I think that this is viewed with scepticism principally because from the outside, banks are not perceived to be in 'real' competition. The big banks in particular, are seen as having emerged from the GFC without any meaningful competition from smaller players and often indistinguishable from each other.

   The second factor is incompatible data across industry. Despite their great similarities, banks operate using different structures, different data systems and internal definitions and it is extremely difficult to obtain comparable data.

   There is a clear community expectation that the industry should be much more transparent, however, this wish is frustrated because of this incompatible data. The most obvious example in this space is the different definitions of a complaint used by the industry – a bugbear for consumer advocates and regulators for decades.

   The inability of the industry to answer what seem to be obvious questions about industry trends and to provide comparable data is widely viewed with scepticism. The industry is seen as living and breathing numbers/data and having enormous information technology capability, yet it cannot deal with data incompatibility issues. In my view, this directly fuels this common thread of mistrust over secrecy.

   There is also some resentment from within banks at the expectation that they must, 'for the common good', share a level of business information that is not expected of (say) BHP Billiton or Apple. I think this resentment is visible – at least in some of the bank's responses to Parliamentary inquiries, which again does not help the overall impression.

I saw evidence of the conduct and problems that are complained about, but I do not think that these are a function of intent, greed or negligence. I met dozens and dozens of bank staff clearly committed and working hard to do the right thing by customers. I have no doubt that they are representative of thousands of their colleagues. I have examined the statistics. I have seen examples of procedures that specify sound processes and good customer service. Banks apologise, fix problems and pay compensation to thousands of customers every year.

I think that most of the problems that customers and stakeholders see are primarily a function of the sheer scale of the organisations and of the volumes of transactions involved, of the 'silos' that inevitably produce jobs with narrowly focused responsibilities, of narrowly cast performance measures and incentives and from time to time - of a defensive culture that contributes to greater mistrust than needs be.

If banks are feeling unfairly treated and that they have been set an unreasonably high bar, they must accept that to some extent they are victims of their own success. Higher expectations of them are in part a function of their scale, profitability and dominance in the financial services sector in Australia – and all things considered, a good problem to have.

4.7. Criticisms of the Code

Unsurprisingly, I encountered a range of criticisms of the current Code – some more informed than others. Many are dealt with in specific chapters, however a brief summary includes:

4.7.1. Complex and inaccessible

A common area of criticism from both regular users and first-time readers of the current Code is clarity and language. Variously, users report that they find:

- The structure hard to follow.
- It is not clear who the audience is.
- The language to be excessively legalistic.
- Referencing concepts that are not commonly understood, nor are they explained – notably the "prudent and diligent banker" or "prudential obligations".
- Additional clauses have simply been added on to existing provisions.

4.7.2. Caveats and Exclusions

Readers complain of far too many caveats and exclusions – they say that there often appear to be more words qualifying the promise and protecting the interests of banks than protecting customers.

Gaps in the Code's coverage were cited by many contributors, notably of course for small business customers[6].

[6] Eg CPA Australia Ltd submission of 25 August 2016

4.7.3. Insufficient support for vulnerable customers

Although many acknowledged the existing provisions in the Code for vulnerable customers, I received further examples of problems confronted by a wide range of customers with vulnerabilities or special needs. These groups included those in financial difficulty but also elders, residents from remote communities, indigenous Australians, those with disabilities, prisoners and those affected by domestic violence.

4.7.4. Lack of 'teeth'

Many contributors bemoaned the Code as 'weak' and pointed to the absence of sufficient sanctioning powers, of the 'invisibility' of the CCMC, of the failure to 'report banks to ASIC' and so on. I note that some of these comments applied to the whole of the regulatory framework, with criticisms also made of the Australian Securities and Investments Commission (ASIC) and other government regulators. At an individual level, many customers who had reported a suspected breach to the CCMC were appalled to discover that even if the CCMC found a breach, there was no 'real' consequence.

Many stakeholders simply rejected the concept of self-regulation and would not accept that anything other than legislation and government regulation could be effective.

4.7.5. Worth fixing

I accept these criticisms; however it must be said in the Code's defence, and more particularly in the defence of those involved in developing it, that the document was conceived and most of it drafted many years ago. Consumer representatives have told me that at various points in its history they have seen the Code as a breakthrough document with significant and lasting impact.

Significant effort has clearly been expended over the years in drafting, reviewing, consulting and achieving agreement. That effort and the periodic review cycle has served the industry and customers well through several versions.

That the Code is seen to have flaws today is no surprise. I see this as part of the cycle of continuous improvement that a self-regulatory framework should deliver. Of course, we all think we can do a better job today and this is an excellent opportunity to do just that.

5. REVIEW APPROACH

The following summarises the key approaches that I have applied to my thinking in this Review.

1. Covering the issues

I have done my best to make this Report comprehensive. Given the criticism by some that this Review was an inadequate response to community concerns, it was my judgment that I had to err on the side of inclusion of issues rather than exclusion. All contributions from industry, stakeholders and bank customers has been taken into consideration in my thinking and analysis, however practicality means that the Report does not exhaustively include a response to every thought put to me by stakeholders and the industry.

2. Reflecting the context

Although the external environment has been something of a moving feast, I have done my best to conduct the review in a way that is connected to the wider debate. In particular, the Review has considered the 'trust' dimension of an issue raised with me, not just the technical/operational/legal considerations. In other words, I have applied my own judgement about whether a suggested change will meet community/stakeholder expectations. Of course, this is ultimately a call for the signatory banks to make, however I have taken the view that there is little point obtaining submissions and having the benefit of confidential discussions if the full dimension of this input is not reflected in my recommendations.

3. Explaining the background

It became evident quickly that stakeholders did not always fully understand aspects of banking practice and how the Code operates. In many cases, neither did I. It seemed to me that in the spirit of creating trust, it was important to ensure that in these areas, the Report was careful to start from an understanding of the underlying facts. This has added to the length of the report and will no doubt be unnecessary text for those with deep knowledge of banking.

4. As long as is necessary

Some of the length of this report comes from my view that on balance it is better to err on the side of a full explanation than to risk misunderstanding in the pursuit of brevity. The issues are complex, and require a nuanced understanding and a sound basis for choosing when to make recommendations. The audience for a discussion will often not have a banking or self-regulatory background.

5. Assuming a complete re-write

Very early in the process, it became clear that the Code could not meet stakeholder expectations simply by being edited and by additions. A complete re-draft is necessary in my view including of Code clauses that are not specifically discussed in my Report. For convenience, I have sometimes expressed my Recommendation in terms of changes to an existing clause, but my expectation is of course that the numbering will change.

As redrafting is to be a task for someone else, it has meant that Recommendations are generally not written with specific wording included. There are also many more recommendations by number than would be needed if I were directly drafting proposed wording.

To address the risk that readers will not be able to visualise what I have in mind, I have done my best to illustrate how I see the new Code looking, hopefully without straying too much into the drafters' territory nor limiting good ideas that they will no doubt bring to the task.

6. Cost of change

Clearly there is a balance to be struck in terms of what is fair and reasonable for profit-making institutions that occupy a critical but privileged position in our society. Much has been made of the fact that millions of Australian citizens have a stake in the banks, not just as customers, but also as shareholders (especially through superannuation investments) – and successful, profitable banks are clearly in their interests as shareholders.

I understand that banks are not a 'magic pudding' – able to endlessly fund customer protections and benefits without passing on the impact. A measure designed to protect or benefit customers may well have a cost – although I suspect that when assessed broadly, many will also produce benefits for banks.

Any such cost may potentially be to the loss of shareholders through diminished profit – or in other words a transfer of benefit from the shareholder to the customer. Alternatively, the banks may recover any lost profit through higher interest rates, fees and charges elsewhere – a burden that may fall fairly or unfairly. It is also the case that this is not a zero-sum exercise. Banks may choose to exit some business lines completely or to create new business lines. I am in no position to predict accurately the net impact of a change – and from my enquiries, often, neither is the industry.

I have taken the view that where a measure will involve some cost or inconvenience to banks – this is not of itself a reason to reject the measure. However, where information is available to me, I must take this into account in considering whether the costs of a suggested change may be disproportionate to the potential benefits.

7. Customer choice

One challenge in considering different aspects of customer protection is to consider where there are trade-offs between provisions that would limit the ability of some customers to 'get into trouble' and where that limit if applied universally, would remove choice of products or services for other customers.

An example is reduced interest balance transfers of credit card balances – a service that no doubt encourages some customers to avoid confronting their mounting debt problem and increases their potential indebtedness – but on the other hand is of considerable benefit to customers who are able to responsibly take advantage of these offers.

These tensions exist along a spectrum of benefit and potential mischief. In a few examples, the choice is pretty clear, but often there are no easy answers to these tensions. To the extent possible, I have tried to take into account the interests of all customers and looked for ways to target recommended protections and prohibitions as best as possible and to preserve choice and access to products as much as is possible.

6. THE NEW CODE

It is important to understanding specific recommendations that stakeholders have a shared understanding of what the new Code will look like (its purpose, audience, structure, language). In my experience, the areas of disagreement can be much reduced if stakeholders are approaching the change with a common mental model of how each piece is intended to fit together.

I have taken the view that the new Code:

1. Represents the voluntary undertakings that signatory banks make to the community – intended to recognise the special place that banks have in the community and the economy;

2. Acknowledges the standards of integrity that the community expects from banks;

3. Recognises that signatory banks are prepared to hold themselves to higher and broader standards than imposed by the law; and

4. Represents the commitment of signatory banks to continuous improvement and spread of good practice (not merely meeting static minimums).

I have set out my basis for this in more detail below.

6.1. Scope of the Code

The Code currently applies to banking services provided in Australia. "Banking services" are defined as any financial service or product provided by the signatory bank. This includes a signatory bank's services in distributing another entity's financial services or products – but does not include the other entity's service or product.

As with any Review like this one, there are a range of views as to what the Code should cover. One view put to me was that a simple-to-understand Code should cover all signatory banks' services, including other financial services provided by banking groups, such as financial planning, funds management, superannuation products or life insurance.

While there is no question in my mind that customers expect that the high level in-principle commitments (eg. fairness and reasonableness) would apply to any product or service provided by a bank signatory to this Code, I did not think it was practical to entertain such a broad scope. There are other industry codes that apply to those other products and services covering banks as well as non-banks that are part of those sectors. To the extent that a voluntary code possesses a unique power, it arises from the sense of ownership and common purpose that it can engender in signatories.

Equally, I took the view that there should be no narrowing of the concept of "banking services" to restrict the scope of the Code. Some banks argued that the current definition of "banking services" incorporates non-traditional banking business such as commercial asset finance and wealth management products that were not intended to be captured and that this puts signatory banks at a competitive disadvantage – especially to the non-bank providers. An example of this concern might be small business equipment financing, where if signatory banks had (say) disclosure requirements that a non-bank competitor did not have, these might prevent the bank (but not its non-bank competitor) from being able to 'sign the customer up on the spot'.

While I understand the practical concern, I think the industry needs to take a strategic perspective as a priority. First, I think that the current very broad Code definition that covers all 'banking services' is a strength. It is one of the few elements of the Code that is in plain, unqualified language. As discussed later in my Report, I think that exceptions and carve outs generally complicate the Code and diminish the strength of the promises made by the Code.

Second, I think that the introduction of new exceptions and carve outs at this time can only act against the banks' aim of strengthening community trust and confidence, potentially undermining the effect of other enhancements to the Code. Finally, one of the key drivers for this review is improved protection of small business by the Code and I think it is legitimate for small business to expect that specialised products such as commercial asset finance marketed to small business by a signatory bank will meet the same standards as for other products. It would be poor timing I think, to now begin to introduce product carve-outs for small business.

6.2. Different audiences

It became evident during the Review process that stakeholders' expectations of how the Code should be written varied considerably and were becoming increasingly incompatible. For example, calls for greater detail, prescription and legal precision are at odds with the objective of clearer, plain speaking, customer-friendliness. Calls for much broader inclusion of more products or more classes of customer, inevitably bring the need for further definition and explanation and are likely at odds with calls for simplicity and clarity. Calls for a more comprehensive, regulator-approved Code can be at odds with calls for a greater emphasis on flexibility and a values-based approach.

It is clear that different groups have different ways of using the Code and differing needs. To illustrate:

- The purpose of the Code is to better serve Code customers, and while comparatively few individual customers and small businesses will have a problem with their bank and turn to the Code, it must be written in simple clear language aimed at them. They should be able to make sense of it and understand both the principles and the intent of the protections offered.

- Senior bank staff need the principles that shape the Code for high-level guidance and the precision of specific prescription to set policy and business rules and design systems and training, but also to understand where there is flexibility in implementation.

- Bank customer service and complaints staff need specific Code obligations to be spelled out in sufficient detail to enable them to advise customers and make day-to-day decisions.

- Consumer advocates need to be able to advise consumers about their rights and to be able to understand and challenge banks on matters in disagreement.

- External dispute resolution scheme (EDR scheme) staff need to be able to interpret the Code with certainty.

In my view, this drives towards a Code that is capable of operating at different levels – with each level able to better deliver what particular groups of stakeholders are seeking. This is a more complex, nuanced approach and I understand that this complexity can be difficult to accept in an environment where stakeholders are looking for 'black-letter' action and may view some aspects of a layered design as 'soft'.

In my view, re-establishing the Code in a layered, adaptable design is important, not just for effectiveness and efficiency reasons but for this improved ability to meet the different needs and trust of multiple stakeholders.

6.3. What is possible

In the sections below I will make the arguments that:

1. Re-structuring the Code into layers aimed for its different audiences will assist with clarity;
2. Some of the qualification and 'fine-print' in the current version can be eliminated by taking a genuine risk management approach (as opposed to risk aversion);
3. Some of the feared risks can be dealt with by being honest about what is achievable and what may go wrong;
4. The Code can be simplified by using referenced 'outboard' guidance – that can allow for different bank operations and business models and practices;
5. A sense of trust would be much assisted by using the warmer language of a trusted relationship – rather than the language of compulsion and exceptions and exclusions; and
6. Using plain speaking language in the Code is essential.

6.4. Design Approach for a new Code

From my close involvement with the Code over the past few months, it is my view that the Code should be re-drafted completely (of course, while retaining the intent of current working provisions). The aim here is to modernise its structure and language, to enable it to better meet the needs of different audiences and to improve its flexibility and continuous improvement. I suggest that the following principles or design guides should steer development of a new Code.

1. Principles-driven

In my view, good design of an industry code should build from principles – every provision should flow from the objectives or outcomes that are being sought. Process prescription, of course has its place; however, it must accommodate variation in practice (ie. between big and small signatories, between different business models, between different technology platforms or communication channels). It must also allow for evolution and innovation over time.

2. Accessible structure and language

The Code should be written in a way that makes the document as accessible as possible. The ability to pursue this principle is limited by the Code's technical nature, its framing by detailed legislation and by the nature of banks as very large organisations that need to be highly process specific in their operations. Given this, it is important that the Code uses plain language and techniques like brief summaries or margin notes to aid a quickly scanning or non-expert reader.

3. Avoid duplication

The Code should avoid duplicating legislation – accepting however, that to meet the goal of clarity and plain-speaking, some explanatory text and signposting to legislation can be appropriate so that Code provisions are understood in the context of applicable legislation.

4. Implementation detail in Industry Guidelines

Detail of how obligations will be met should, to the extent practicable, be set out in supporting guidelines rather than in the Code itself – in the same way that regulations can provide the detail absent in statute law. This can only be done in a way that maintains stakeholder confidence in the core obligations – ie. the guidelines must be seen as implementation assistance, and cannot be seen as 'watering down' the provision.

5. Room for flexibility in implementation

Whilst the Code sets good industry practice, it should allow room for banks to choose how they achieve (or exceed) that standard and where appropriate, how they differentiate themselves in the market. In the current environment, this must not be misunderstood as freedom to lower or avoid standards.

6. Cost-awareness

The Code should not mandate measures that carry substantial costs for the banking system unless the measures are likely to achieve well-defined and targeted policy aims. (I choose the term 'cost-awareness' as opposed to cost-effectiveness deliberately.)

7. Target obligations

To the extent practical and appropriate, new protective measures in the Code should be targeted to areas where there is evidence of current problems, rather than trying to apply to all theoretically possible scenarios. They should also be targeted to groups who are most vulnerable, for whom the asymmetry of knowledge and power is the greatest, rather than necessarily applying across the board to all customers.

8. Maintain customer choice

As a general principle, the Code should not unreasonably or unfairly limit customers' choice.

9. Encourage innovation and continuous improvement

A modern Code should encourage signatory banks to innovate and develop services and processes and must allow for continuous adaptation and improvement of itself.

6.5. An architecture

To best deal with these diverse demands of the Code, I suggest the following overall design or architecture for the new Code.

Preamble

Purpose & spirit

About the Code

1. **Preamble –** a brief section which incorporates:

    a. **Purpose** – a high level introduction to the Code that captures the purpose and intended spirit of the promises by banks to the community.

    b. **About the Code** - reference the voluntary commitment of signatory banks to the Code, how the Code adds to legislative obligations that signatory banks must meet and that Code obligations form part of the terms and conditions for Code customers.

2. **Principles** – akin to the current Key Commitments. These are key promises by signatory banks - eg. how banks will inform customers, how banks will 'speak', responsibility in lending, how contracts will be fair and reasonable, etc. These principles will guide how specific obligations will be shaped. I have suggested around 8 of these in Chapter 6.7 below.

Principles

Fair & reasonable

Information

Responsible lending

Fair Contracts

Etc.

3. **Obligations** – these are the specific promises that the signatory banks make – the area where practitioners both inside and outside signatory banks are guided in specific conduct.

   To minimise duplication, obligations should be structured by product or service topic rather than divided into sections applicable to different Code customer group. To enhance navigation within the detail of the obligations, this part of the Code should be divided into subsections with an executive summary at the start of each.

   Also the Code should include an attachment that is designed specifically for small businesses and summarises the protections afforded to them by the Code with appropriate cross referencing.

Obligations

Section heading

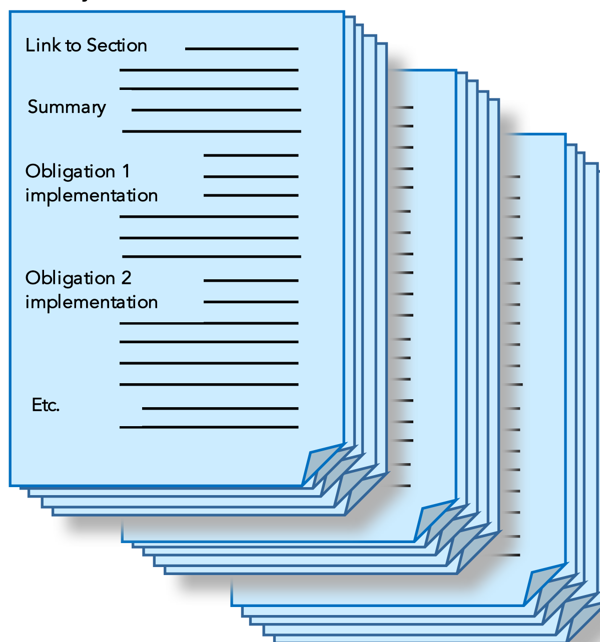
Summary

Obligation 1

Obligation 2

Refer to Law or Guideline

4. **Industry Guidelines** – sitting outside the Code, these are the lengthy, detailed documents that provide guidance on how principles and obligations can be implemented. Typically, they allow for different size operations and provide descriptions of multiple ways of doing things that would meet the obligations. These can be developed and updated outside the formal Code change and approval processes. Although they are less prescriptive, the fact that EDR schemes are able to reference them as good practice gives them considerable weight while retaining some flexibility.



An example currently existing are the Guidelines developed by the ABA in the areas of financial difficulty and protecting vulnerable customers from potential financial abuse.

I encountered different views about the effectiveness of the current development process used for Industry Guidelines – I mention this because, if this suggested Code structure is to be accepted by regulators and consumer advocates, there will need to be a credible, accepted process for consulting with stakeholders in the development of these Industry Guidelines. I address this in Chapter 22 Next Steps.

I think that the Code should be structured into Chapters much like those in this report – dealing with like issues together. I have included as Attachment 5 an outline of the new Code as I envisage it, with cross-references to existing Code clauses to show how they will fit in, and with an appended brief guide for small business.

6.6. Suggested Preamble

This should be a high level introduction to the Code that captures the purpose and intended spirit of the promises made by banks to the community. It should mention:

- the Code obligations form part of the contract with Code customers;
- its interaction with other sources of obligation from the law or other codes;

- its overall structure and elements including the relationship with Industry Guidelines;
- the important role of the CCMC in monitoring and community assurance; and
- the intention to continuously improve the Code's operation.

6.7. Suggested Code Principles

While it is for industry and the drafters to settle the ultimate content, by way of illustration, I have suggested below 8 matters which I think would be useful Principles to be committed to in the new Code.

1. Focus on Customers

This should include references to respect for the customer, and earning the customer's trust.

2. Fair and reasonable, ethical

This should include references to treating customers ethically, fairly and straightforwardly – ie. avoiding processes, Terms and Conditions, fees and charges, etc. that are not what people would intuitively expect or understand and may perceive as trickiness or untrustworthiness, in particular in sales practices.

3. Speak clearly and plainly

Should commit to plain-speaking, and no surprises for the customer.

4. Transparent to customers and the community

Should reference open and robust monitoring of Code compliance – and provision of information to customers and the broader community.

5. Responsible in lending

Should be simple statement of commitment to a responsible approach.

6. Support for financial inclusion and special needs

Should be a statement that accommodates a range of aspects (avoid lists).

7. Assistance with financial difficulty

Should use 'warm' language, express commitment to assistance, and clarity of information.

8. Open, fair treatment of complaints

Should reference the importance of customer expressions of dissatisfaction, and a commitment to respond.

6.8. Obligations language

Enhanced accessibility also requires the language of the Code obligations to be different. Plainer, less qualified language is needed. Also, the tone needs to be warmer. To illustrate, the current Code's section 37 is set out in the table below – with a suggested re-drafting alongside it. The policy issues inherent in the redraft are discussed in Chapter 8.11.

Current Code	Suggested re-draft	Comments
37. Internal dispute resolution	Complaints	
37.1. We will have an internal process for handling disputes with you which is free and accessible.	We will try and resolve your complaint on the spot or as soon as practicable.	*Plainer and warmer language that reframes current clause 37.3(f) as a positive commitment (rather than as an exclusion)*
37.2. If you are: (a) an individual, and not a small business; or,	If you are not satisfied, we will provide ready access to a separate disputes resolution process within the bank at no charge. That process will meet the standards set by the regulator, ASIC (provide link).	*Commitment to apply ASIC standards to all complaints by Code customers – not just complaints that are legislatively required to be handled in accordance with those standards*
(b) a small business to which any relevant internal complaints handling standard or guideline which ASIC publishes for application to Australian financial services and credit licensees ("Approved Standard") applies, our internal process will meet the standards set out in the Approved Standard (for example, as at the date of the publication of this Code, Regulatory Guide 165).		
37.3. If clause 37.2 does not apply to you, then, clauses 37.3(a) to 37.3(g) apply to you. (a) We will notify you of the name and contact number of	We will keep you informed about the process including the name and contact details of the person handling your complaint, and the results of our investigation.	*As this provision is one that is particularly important for a customer, the essential information needs to be complete in the Code and in plain*

the person who is investigating your dispute; (b) Within 21 days of becoming aware of a dispute, we will: (i) complete the investigation and inform you of the outcome of the investigation; or (ii) inform you of our need for more time to complete our investigation. (c) Unless there are exceptional circumstances, we will complete our investigation within 45 days of receipt of the dispute. (d) If we are unable to resolve a dispute within 45 days, we will: i. inform you of the reasons for the delay; ii. provide you with monthly updates on progress with the dispute; and iii. specify a date when a decision can reasonably be expected, unless we are waiting for a response from you which we have told you we require. (e) If the rules of an external dispute resolution scheme of which we are a member, provide that a matter may be referred to it if a decision is not made within a specified time period, then we will inform you, no more than 5 business days after the expiry of that time period, that a dispute may be lodged with the scheme.	We will do our best to complete the investigation and advise you within 21 days. Sometimes an investigation takes longer than this. If we have not given you our decision within 45 days, we will explain the delay, when we expect to give you a decision and that you are entitled to take your dispute to an independent dispute resolution service outside the bank, free of charge. After that, we will provide monthly updates on progress. You are also entitled to take your dispute to an independent dispute resolution service outside the bank, free of charge, if you are not satisfied with our decision.	*language.* *Note that duplication here with clause 39.2(b) will need to be resolved as part of the redraft process.*

(f) Our dispute resolution process is available for all complaints other than those that are resolved to your satisfaction at the time they are drawn to our attention.		
(g) We will provide you with the above information in writing unless it has been mutually agreed that it can be given verbally.		*Unnecessary to essential explanation – set out in the detail of RG.165*

Recommendation 1

The new Code should:

a) Be re-drafted in a modern structure and style.

b) Be drafted in layers that address the differing needs of its multiple audiences – ie. Preamble, Principles, Obligations and Industry Guidelines.

c) Cover all banking services offered to retail and small business customers.

d) Use plain, accessible language and a warmer tone as part of making the document more customer-focused and accessible.

e) Be as straightforward as possible with the minimum of qualification and 'fine-print'.

f) Avoid duplicating the law.

g) Put complex implementation detail in Industry Guidelines.

h) Include an accompanying Guide to the relevant parts of the Code for small business customers.

7. CULTURE

The operation of any code of conduct should not only be reflected in 'hard' dimensions of an organisation's operation (eg. business rules, procedures, compliance requirements, complaints-handling procedures etc.) but also in the 'soft' dimensions of internal culture, staff behaviour, the interplay with performance measures and incentives, escalation, flexibility and so forth.

While there is a separate review, led by Stephen Sedgwick AO, that is looking at the particular issue of remuneration and incentives, many stakeholders raised broader questions of culture with me in the context of the effectiveness of the Code. Matters included the quality of staff training, the position of the Code in the hierarchy of compliance obligations, the extent to which staff are able to apply the principles of the Code 'beyond' the prescriptive rules of day-to-day process, whether general principles are of any utility in a process and rule-driven bank environment and whether the attitude to whistleblowing is reflective of the Code principles.

To be blunt, many stakeholders believe that the 'problem with banks' is one of internal culture and they are sceptical about whether the banks are capable of managing change to their cultures. They argue that no system of voluntary rules (eg. the Code) will have genuine impact unless it can be seen to be credibly addressing internal culture.

7.1. Opportunities

I deal with this issue first amongst the dozen or so key areas, because these 'soft' factors are pervasive elements of each of the issues I will discuss later in the report.

It is not my role to advise signatory banks on how to manage their operations, people or culture. I think it is my role to understand what impact the Code currently has within the operations of these large, complex organisations and to make recommendations that might strengthen the influence of the Code on a bank's operational culture. Some discussion of these issues within this report may also help stakeholders to calibrate their expectations of what is possible to achieve through a voluntary code of conduct.

I have no delusions as to the Code's place in the internal world of banking. As one of our interviewees put it:

> *". . . the Code is not in the top 5 considerations in day-to-day decision-making within the bank, it is more like 50th . . . "*

Source: former banking senior executive

This relative importance is not of itself a problem. As discussed in Chapter 3.2, the Code is but one of many sources of obligations (a 'tapestry') for the banks to work within. However, I think that for signatory banks to genuinely demonstrate the sentiments expressed by the banking industry on the ABA website ("we hear you, we are delivering change now"), the changes that flow from the Better Banking program, including to the Code, must be reflected within the bank – in a way that is 'real' and evident to bank staff.

I am optimistic, that in a time of great pressure on the industry, a 'new' Code represents an opportunity for signatory banks. Even with the least fanfare, a new Code will have an impact for a time - if only for the task of implementation. New provisions will need to be put into systems, procedures and scripts. Changes will need to be communicated to staff. Some staff will need training on new processes and business rules.

Signatory banks can take advantage of this initial impact. They can choose to use the results of this and other Better Banking initiatives as a positive catalyst for change. I see two dimensions where the new Code should be able to have some impact on values and culture.

1. Hardwiring

Like all white-collar, large organisations, banks rely on business rules, policy, procedures, systems, scripts, authority delegations, training and an array of compliance controls designed to make an organisation of tens of thousands of staff deliver service in a consistent, quality way.

I see these as the 'hardwired' elements that impact bank conduct and are the obvious ways in which Code provisions are embedded in bank policy, systems and process. These are areas in which the banks have great experience and expertise in developing and implementing – and I expect will happen in a business-as-usual manner.

The opportunity that exists in the Better Banking and new Code implementation process is for leadership (at all levels) within the bank to deliver messages of commitment and support for the thrust of the changes.

2. Flexibility, escalation and workarounds

Of course, no matter how much effort goes into design and testing, there are no business rules, systems or procedures that are fool-proof nor that can fully anticipate every scenario or circumstance that a customer might be in. This is not only a source of some customer dissatisfaction ("computer says 'no' . . [7]") but also a source of frustration for bank staff who may be placed in a position of insisting on procedures and rules that are aggravating the customer.

In these circumstances, staff must be able to deal with a matter in a sensible way – typically by 'going around' the standard process in some way. This might be approving some transaction that does not meet the strict business rule, expediting an application, by waiving a fee and so on. This requires recognising when the standard process is going to produce the wrong outcome, knowing when and how best to exercise discretion or at least when to escalate the issue to a higher level where discretion can be exercised.

This a problematic area for large scale operations such as banks. On the one hand, every effort is put into ensuring that staff know what procedures are and that they adhere to them. Great effort is also put into simplifying the systems that staff use – so that complexity is removed and the system produces the 'answer'. Neither of which especially encourage flexible, customer-oriented decision-making.

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[7] From TV comedy "Little Britain" – impenetrable bureaucratic inflexibility

I am aware that some banks have culture and customer service programs designed to complement hardwired systems and to encourage some greater flexibility. I am also aware that hundreds of managers, customer service and internal complaints staff are kept busy dealing with and fixing thousands of these issues for customers with quite some success. That said, improvement is always possible.

A well-drafted Code could make a difference here. The statements of principle in such a Code could form the basis of guidance and training for staff in recognising where an exception from the usual answer is called for and in designing delegations and authorities that make this easier.

I do not see that the Code's framing of these principles needs to be a straightjacket for signatory banks, limiting their ability to drive customer service internally, consistent with the bank's culture and values. There would be no problem with a bank using its own internal principles, provided that they were consistent with the promises made by all signatory banks through the Code.

7.1.1. The moral compass

I have had a number of discussions with stakeholders and with bank staff around the idea that the way to impact culture is to have a 'higher authority' or an independent moral compass that acts to empower bank staff to weigh up what they are being expected to do against the question of 'what is right'.

The Banking and Financial Oath[8] is an example of this approach and after something of a slow start, I understand it is now achieving quite some support amongst staff and the leadership of Australian banks. I understand that some banks, including internationally, have developed their own versions of a personal commitment for their staff. The oath is an example of approaching the moral compass as a personal commitment by an individual.

A different pathway to the moral compass is the commitment by a group. I understand there are people within the industry looking at the concept of a 'banking profession' with explicit standards and values. This is much as doctors or lawyers are expected to have an allegiance to a set of professional values that are common to their profession and 'above' the organisation they work for.

[8] *"Trust is the foundation of my profession. I will serve all interests in good faith. I will compete with honour. I will pursue my ends with ethical restraint. I will help create a sustainable future. I will help create a more just society. I will speak out against wrongdoing and support others who do the same. I will accept responsibility for my actions. In these and all other matters; My word is my bond."* The Banking and Finance Oath. See also www.bfo.org .

These seem to me to be excellent initiatives and I was impressed by the emerging support for them. I would encourage banks to support them in a way that aligns with their own leadership style and values. I do not think however, that there should be an expectation that there is any single solution that will transform how banking is done. To put the conversation of 'doing the right thing' at every decision point in a large bank, will require the long-term effect of many different approaches. The oath is a powerful personal commitment – by its nature, some will adopt, some will not. A banking 'profession' will reach some professional staff but I think it will take some time before it will appeal to active members of other professions within banks – such as lawyers, accountants, IT or HR professionals. This is a long-term commitment.

7.1.2. What is measured

From my observations and discussions with staff and former executives, the most important dimension that drives behaviour in a bank is the same as any other large organisation – it is what management pays attention to – and in particular, middle managers. It is the way messages from the top are interpreted and passed down and the information that is communicated upwards by this layer of managers that speaks the loudest about 'real' culture and values.

There are ways in which hardwired aspects such as Key Performance Indicators, performance management agreements, job descriptions, monetary incentives and formal reward and recognition can reflect desired values and culture and may be imposed over the whole organisation.

I am convinced that there is no more powerful influence than the tone set by day-to-day operational interactions (eg. Q&A, results of escalated queries, meeting agendas, what gets discussed from performance reports, who gets included in discussions, what your boss worries about, who gets promoted, who gets fired, how genuine or cynical are the conversations about values and ethics, etc).

The adoption of a Code that incorporates a series of high-level principles linked to specific obligations – along with evident substantive change to consumer protections and a noticeable shift to a more plain-speaking style provides another opportunity to impact aspects of bank culture. In particular, I see that the linking of principles with concrete, substantive provisions is a powerful way of internally illustrating that 'we are delivering change now'.

Recommendation 2

The advent of the new Code should be used as an opportunity to reinforce values and culture settings within signatory banks, and to demonstrate genuine listening, commitment and change.

7.2. Training

A number of stakeholders raised the issue of staff training with me in submissions and discussions. Many thought that evidence of persisting problems must be evidence of inadequate training. Some of the anecdotal evidence offered up by consumer case-workers also suggested instances where bank staff were unaware of the law or Code provisions.

There is an existing Code obligation under Clause 9 (b) for staff to "have an adequate knowledge of the provisions of this Code and its application to banking services". While I fully understand why stakeholders would call for signatory banks to commit to more regular Code-specific training, I am conscious that this is easier said than done – and that it may not actually be effective. Bank staff are already under great pressure to be fully across an ever-expanding range of compliance requirements – and if the recommendations of this report are accepted, there will be further expansion!

I also understand that staff procedures and training are not organised around the specific source of an obligation. Staff are not generally trained in a piece of the law or the Code separately – rather they will receive training that covers all that they need to know in order to fulfil certain services – see Chapter 3.2. This holistic approach to compliance requirements becomes even more practically necessary as the Code increasingly weaves in between and overlays provisions sourced from legislation.

While I am not persuaded that a requirement to train staff in the Code itself would necessarily be of any assistance, I do think that the 'person in the street' would expect that the banks are reviewing their internal enquiry, customer service and complaints data to identify where there are persisting issues – and are improving procedures or providing remedial training where this is necessary. I understand that there are some existing 'continuous improvement learning loops' already built in to some bank systems and that this is unlikely to be a great impost.

Recommendation 3

The Code should oblige signatory banks to have in place processes and systems to identify persisting issues that may indicate that revised procedures, system changes or some additional or reinforcing training is required to achieve compliance with Code obligations – and to deliver that continuous improvement as appropriate. A wide range of inputs should be used to identify issues including supervisory systems, customer surveys, complaints data, information provided by consumer representatives and other customer representative groups, regulator reports, CCMC analysis and so on.

7.2.1. Promotion of the Code

The Code currently includes obligations to promote the Code.

> *"10. We will require the ABA to*

(a) Promote this Code; and

(b) Clearly make public:

i. which banks subscribe to this Code; and

ii how you can get a copy of this Code".

11. We will

(a) display, at our branches, a copy of this Code in a readily visible manner;

(b) make this Code available on request;

(c) publish this Code on our website; and

(d) send this Code to you by electronic communication or mail on request.

A number of stakeholders argued for greater promotion of the Code, with some specific requests for links on websites and the like – which I understand. While I certainly support the banks providing links to the Code on websites, because of the Code's role within a larger framework of obligations, I am reluctant to make highly specific recommendations around its promotion as it might be seen as claiming a profile that is disproportionate to its impact, or 'crowding out' references to other forms of protection that may well be more important for customers. I am also inclined to think that the current requirements in clause 11 that signatory banks display the Code in branches is no longer apposite in this digital age.

As discussed above, I think the implementation of the new Code is an opportunity to both impact staff internally and to deliver the key message externally – consistent with "we hear you, we are delivering change now". I make two modest recommendations regarding the promotion of the Code.

Recommendation 4

(a) Signatory banks' websites should provide an easily navigable, clear link to the Code, with links from the obvious places such as customer service and complaints information. They should no longer be required to display the Code at branches.

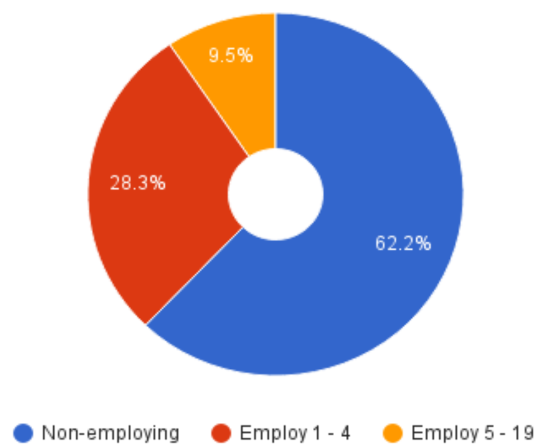
(b) In order to maximise the message of change to customers, signatory banks should look at ways of coordinating publicity and messaging about the implementation of the new Code.

8. SMALL BUSINESS

8.1. Introduction

Small businesses play a pivotal role in Australian society. There are 2 million actively trading businesses in Australia with fewer than 20 employees. Together they employ 4.8 million people, over 40% of the workforce.

Figure 4. Small business employment Australia



Source: Australian Treasury's Small Business Data Card, September 2012
http://www.treasury.gov.au/ PublicationsAndMedia/Publications/2012/sml-bus-data

Bank lending practices to small businesses have been the subject of complaints that have been considered in a number of Parliamentary inquiries.

The November 2012 Senate Economics References Committee report *The post-GFC banking sector* referred to the "significant imbalance in negotiating power" between small business and large financial institutions and the difficulties confronted by "small business owners . . . [busily] focused on the day-to-day operations of their business"[9], words echoed in the subsequent Parliamentary Joint Committee *Impairment of Customer Loans Report*, May 2016[10]. The Senate Economics References Committee called upon the ABA to develop a code of practice specifically relating to lending to small businesses[11]. The Committee saw this as a key mechanism to enhance banks' disclosure and processes to better meet small business borrowers' needs. Similarly the Parliamentary Joint Committee recommended that the ABA add to the Code to address small business issues[12].

Following on from these inquiries, on 31 August 2016 the Minister for Small Business tasked the Australian Small Business and Family Enterprise Ombudsman with an inquiry into the adequacy of the law and practices governing financial lending to small businesses[13]. The Australian Small Business and Family Enterprise Ombudsman's report was publicly released on 3 February 2017 (Ombudsman's Report).

As in these reports, the small business issues raised with me by organisations representing small business focused on lending practices. In addition to considering the proposals put directly to me in submissions on behalf of small businesses, I see my task as recommending what changes should be made to the Code to address the issues put forward in the two Parliamentary Inquiry Reports and the Ombudsman's Report.

This Chapter addresses small business specific issues. In subsequent chapters, I address issues that apply also to individual customers. For the assistance of small business, Attachment 4 sets out the key recommendations in my Report that impact small business and cross-references these to the Ombudsman's Report.

8.2. Small business borrowing

I have not been able to obtain an accurate picture of the extent of lending by signatory banks to small business as there is no publicly available data. Because signatory banks use different monetary thresholds to categorise small business loans, their data cannot simply be aggregated. Moreover, small businesses are often funded through personal lending (a loan secured by a home mortgage) which further complicates the picture.

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[9] Senate Economics References Committee report *The post-GFC banking sector* Executive summary p. xxiii

[10] Senate Economics References Committee report *The post-GFC banking sector* Executive summary p. ix

[11] Senate Economics References Committee report *The post-GFC banking sector* Rec 9.1

[12] Parliamentary Joint Committee *Impairment of Customer Loans* Rec 2

[13] Media Release by the Hon Michael McCormack MP dated 31 August 2016, *Inquiry into small business lending practices*

With those caveats, industry provided me with the estimate that, as at the end of March 2015, signatory banks had about 700,000 small business loans on their books. The next table collates the information about the business lending portfolios of three banks, provided by them to the Standing Committee on Economics in the course of its public hearings in late 2016.

Figure 5. - Small business lending by Commonwealth Bank, Westpac and National Australia Bank

$m	2013	2014	2015
CBA: business loans of up to $1 million			
Total value of loans	14,417	18,164	17,752
Value of loans in default - residentially secured		51	67
Value of loans in default - not residentially secured	194	171	173
Value of loans written off	36	40	60
Westpac: business loans of up to $1 million			
Total value of loans	13,593	13,583	14,566
Value of loans in default - residentially secured	24	37	30
Value of loans in default - not residentially secured	213	213	207
Value of loans written off	40	133	68
NAB: business loans of up to $25 million			
Total value of loans	55,200	55,200	59,200
Value of loans in default		971	657
Value of loans written off	339	207	76
Fully secured		69%	70%
Partly secured		26%	25%
Unsecured		5%	5%

Source: http://www.aph.gov.au/Parliamentary_Business/Committees/House/Economics/Four_Major_Banks_Review/Documents

Some banks deal with small businesses as customers of the retail division. Where this is the case, the small business benefits from retail division processes designed to meet legislative and Code requirements for individual customers, not all of which are mandatory for small business customers. From the bank's perspective, however, a uniform process approach for retail customers (business and individual customers) simplifies the bank's processes.

Typically, the retail division of a bank will have a threshold that caps the amount that the division is able to lend to a customer. This threshold varies from bank to bank as the data in Figure 5 illustrates. If a business borrows an amount that is greater than the bank's small business threshold, the business may be dealt with under bank processes that are quite different from those of the retail division.

8.3. How should small business be defined?

Clause 42 of the Code defines a "small business" as a business having less than 20 full time equivalent employees, or 100 employees in the case of a manufacturer. If, however, the banking service is a financial product or service regulated under Chapter 7 of the *Corporations Act*, the Code only applies to a 'retail client' within the meaning of the Corporations Act. This affects an adjustment of the definition for the purposes of deposit products, but not for lending products.

The underpinning rationale of the Code definition of "small business" is that a business with a limited number of employees is unsophisticated and does not have ready access to specialist resources such as legal and financial advice.

Whilst I heard no criticism of the rationale that unsophisticated businesses should have the benefit of the Code, the wording of the "small business" definition has been criticised. It may be that a company, with extensive assets and very large and complex credit facilities, will have few employees and so be categorised as a small business for the purposes of the Code. This can be the case where the company is part of a large corporate group. On the other hand, a farming enterprise with large numbers of seasonal workers may for at least some of the year fall outside the definition of "small business". It has been argued that neither result is consistent with the rationale for the Code's application to small business.

Providing further momentum for this debate, the FOS is currently revisiting its small business jurisdiction. Like the Code, FOS's Terms of Reference currently utilises a less than 20 full time equivalent employee test (or 100 employees for a manufacturer) – with a discretion to exclude the complaint if the applicant is not a retail client. Unlike the Code, however, FOS's Terms of Reference include carve outs that exclude first, a member of a large corporate group[14] and second, a borrower of more than $2 million[15]. To enhance small business access to external dispute resolution, FOS is now proposing to change its Terms of Reference to allow access to a borrower of up to $10 million and to enable FOS to make an award of up to $2 million. It consulted with stakeholders about this proposal last year, but has not yet announced what changes it has decided to make..

8.3.1. Stakeholder submissions

Stakeholder submissions to my review of the Code reflected very different perspectives as to how 'small business' should be defined in the Code.

- The Australian Small Business and Family Enterprise Ombudsman's submission to my Review was that the test should be broadened to a business with less than 100 full time equivalent employees, consistent with one of the parameters of its own jurisdiction[16]. Her report released 3 February 2017 recommended a range of protections for small business loans below $5 million.

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[14] Clause 5.1p)

[15] Clause 5.1r)

[16] Australian Small Business and Family Enterprise Ombudsman Act sec 5

- The Tasmanian Small Business Council supported the current less than 20 full time equivalent employee definition and noted that the definition is consistent with Australian Bureau of Statistics' small business definition[17].

- The ABA in conjunction with its member banks proposed both to FOS and my Review that the less than 20 full time equivalent employee test (or 100 in the case of a manufacturer) should include exclusions - for borrowers of at least $3 million, for businesses with annual turnover of at least $5 million and for companies in a corporate group with a total credit exposure of at least $3 million to $5 million.

8.3.2. Discussion

Like any number of commentators, I am concerned about the plethora of 'small business' definitions[18] that currently apply. Whilst I recognise that for different contexts, different definitions can make sense, the inconsistency is confusing for small business.

I also recognise the complexity for signatory banks that results if the definition relies upon benchmarks that vary year to year or even within a year, such as turnover and number of employees. In the case of credit, signatory banks' preference is to rely upon the credit facility size as the salient benchmark although this does not solve the question for non-credit banking services.

Balancing all of these issues, my recommendation is that the Code definition of "small business" should be broadened to extend to a business that employs less than 100 full time equivalent employees (in the case of a business that is part of a group of companies, the calculation should include all employees of the group of companies). This would better accommodate businesses such as farming enterprises that increase their workforce on a seasonal basis (whilst seasonal workers in the past have often been regarded as independent contractors there is increasing awareness of the breadth of the employment concept). Australian Bureau of Statistics analysis suggests that this would expand the small business net from 97% of actively trading businesses in Australia to about 98% of all actively trading businesses[19].

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[17] www.aph.gov.au *Definitions and data sources for small business in Australia: a quick guide,* 1 December 2015

[18] For example, Australian Securities and Investments Commission Act 2001 sec 12BF which uses an employment test (fewer than 20 persons) and a contract payment price test ($300,000 upfront payment price under the contract or alternatively $1 million upfront payment price for a contract with duration of over 12 months).

[19] Australian Bureau of Statistics, *81650.0 – Counts of Australian Businesses, including Entries and Exits,* June 2015, released 26 February 2016, www.abs.gov.au/ausstats/abs@nsf/mf/mf/81650. The ABS defines "actively trading businesses" as businesses that are actively remitting GST.

In the case of the Code provisions relating to credit, I think that it is appropriate to apply a credit facility limit. Consistent with the Ombudsman Report recommendations, the Code provisions relating to loans should apply only to a small business credit facility of less than $5 million. A $5 million threshold is consistent with my view expressed in another context that a credit facility above that amount often takes on a heightened level of complexity[20]. In the interests of simplicity and a broad reach for the Code, I think that the credit facility limit threshold should be applied per credit facility, rather than on the basis of aggregating all credit facilities provided to that borrower.

The effect of this would be that the Code provisions relating to responsible lending, credit contracts, financial difficulty, joint debtors, guarantees and debt collection would only apply to a small business facility below $5 million. For financial products or services regulated by the Corporations Act 2001, I think that alignment with the Corporations Act "retail client" test remains appropriate.

Recommendation 5

a) The Code definition of "small business" (other than for the purposes of financial products or services regulated by the Corporations Act 2001) should be amended to mean a business that employs fewer than 100 full time equivalent employees or, in the case of a business that is part of a group of companies, the group employs fewer than 100 full time equivalent employees.

b) The provisions of the Code that relate to credit should apply to a small business credit facility only if it is below $5 million.

8.4. Applications for credit for a business purpose

8.4.1. Introduction

The Parliamentary Joint Committee *Impairment of Customer Loans Report*, May 2016, expressed concern about the responsibility of some lending to small business. The Committee noted that NCCP Act responsible lending obligations do not apply to loans for business purposes. The Committee thought that further regulation was required. To ensure that "protections do not impede business that are well informed, have a strong business case and are prepared to back themselves in taking on a venture", there should be an exclusion for a borrower that has sought independent advice as to their capacity to manage extra debt and has signed a terms summary front sheet to the loan contract[21].

In response to the Committee's concerns, I have considered whether changes should be made to clause 27 of the Code titled 'Provision of credit'. That clause provides:

[20] 2013 Independent Review of Financial Ombudsman Service, Report to the Board, p.65 www.fos.org.au

[21] Parliamentary Joint Committee *Impairment of Customer Loans Report*, May 2016, p.30

> *"Before we offer, give you or increase an existing credit facility, we will exercise the care and skill of a diligent and prudent banker in selecting and applying our credit assessment methods and forming our opinion about your ability to repay the credit facility".*

This clause has been enforced by the Courts, most recently in *Doggett v Commonwealth Bank of Australia* [2015] VSCA 351 where the Victorian Court of Appeal found that the bank had not taken sufficient care in assessing the debtor's ability to repay the loan. This breach would have adversely affected the bank's ability to recover the debt, but for other matters set out in the judgment.

8.4.2. Stakeholder views

In discussions with small business representatives, I heard criticism that the banks' processes, where a small business applies for credit, can be opaque and difficult for the small business applicant to navigate. I did not hear criticism about irresponsible lending. In fact, concern was expressed to me by small business representatives that, if the Code is amended to import NCCP Act responsible lending-type requirements for small business, there could be undesirable consequences, that this could restrict small business access to credit. This could particularly be the case for a new business, without an established profit record, where access to credit depends, at least in part, upon reliance by the bank on security or guarantee arrangements.

Signatory banks told me that, to meet their prudential obligations, banks must consider the risks of lending to a small business, including the small business borrower's ability to repay credit. Not all credit applications are approved. To grant credit, the bank needs to be satisfied that there is a strong business case for the project or investment.

8.4.3. Discussion

Concern about irresponsible lending is, of course, driven by concern that small business credit has higher impaired rates than consumer credit. To understand this, I sought data about small business loans where there are repayment issues. There is no publicly available data, but indicative data provided by 8 signatory banks provides some comfort that the vast majority of small businesses are successfully servicing the credit provided by their signatory bank. According to this data, as at the end of March 2015:

- Less than 1.5% of loans to small business (farming enterprises and other enterprises) were in work out (where the bank is working with the borrower to address repayment problems);

- Less than 0.5% of loans to small business (farming enterprises and other enterprises) were subject to loss provision as impaired loans (typically a loan is classified as impaired where the loan is 90 days overdue)[22];

- Less than 0.02% of loans to small business (farming enterprises and other enterprises) were in recovery action (where loan foreclosure has occurred); and

- Farming enterprises were up to twice as likely to be in work out, impaired or recovery, as compared with non-farming small business loans.

This leads me to the question of whether the Code is currently encouraging signatory banks to strike the right balance between lending based on proven cash flow and access to credit considerations that takes into account the availability of security for the credit.

In my consultations with small business, I was told that, in the interests of facilitating commerce, banks need to provide their small business customers with some flexibility. I agree that at times it will be appropriate for a bank when making its credit assessment to rely on the customer's security for the credit. The NCCP Act responsible lending provisions would restrict flexibility in a way that I think would be undesirable. I am not recommending that the Code mandate this for small business customers.

Instead I think that current clause 27 of the Code should be improved. Whilst I understand that the Code's 'diligent and prudent banker' obligation carries weight in the Courts when considering a dispute, it seems to me that the clause is obscurely worded and would not readily convey to a small business what the bank's promise is. In Chapter 9, I recommend the modernising of clause 27 to make it clearer and more meaningful for individual customers and small business customers alike.

In addition, I think that the Code should commit banks to provide more assistance to small business applicants with the credit process. To assist small business, the ABA with CPA Australia has developed an online resource www.financingyoursmallbusiness.com.au. This website includes pages dealing with the following:

- Before applying for a loan: What type of finance is needed, how the banks assess an application, using an adviser, understanding bank speak, and top tips;

- Applying for a loan: common mistakes that can jeopardise a loan application, checklist, and top tips; and

- After obtaining a loan: managing the relationship with the lender, and switching banks.

[22] See also Joint Parliamentary Committee, *Impaired Customer Loans Report,* p.11 reference to ABA information that for the year ending March 2015 less than 1% of business and agribusiness customers had impaired loans and a tenth of 1% were in recovery action.

This is clearly a valuable resource for small businesses that are referred to this site. However, this site is not a substitute for assistance that is tailored to a small business's specific situation. To address this need, CPA Australia has proposed that the Code adopt the approach taken in codes of conduct for small business lending in Canada, the United Kingdom and Ireland[23]. Those codes incorporate the following commitments:

- to explain the requirements needed to obtain bank credit;
- to notify the small business applicant of additional information requirements where the lending decision cannot be made and provide an estimate as to how long it will take before a credit decision will be made; and
- to require banks to explain to small business customers the main reason for a refusal to lend and the requirements to enable the bank to reconsider the application.

I agree that obligations of this type would strengthen the Code's promises to small business. It would be consistent with my proposed Principle 1 Focus on customers. I accept, of course, that in providing guidance to small business applicants for finance, banks would need to be clear about the limits of their guidance and that, for example, guidance as to the information that a bank requires does not constitute conditional approval of an application for credit. I think that with clear communication, this can be navigated.

Recommendation 6

A new clause should be included in the Code applying to a credit facility below $5 million that is provided for a small business purpose. The clause should oblige banks to explain:

a) the requirements needed to obtain bank credit;

b) additional information requirements where the lending decision cannot be made and how long a lending decision is likely to take; and

c) where possible, the main reason for a refusal to lend and the requirements to enable the bank to reconsider the application.

8.5. Small business credit contracts

The Parliamentary Joint Committee *Impairment of Customer Loans Report*, May 2016 also expressed concern that small business borrowers often do not understand the terms of their long and complex loan contracts. The Committee recommended better disclosure of key loan terms including default clauses and that the Australian Small Business and Family Enterprise Ombudsman lead and coordinate reform in this area[24]. Consistent with this, the Ombudsman's Report recommends two reforms applicable to small business loans below $5 million:

[23] Canada - *Model Code of Conduct for Bank Relations with Small and Medium-sized Businesses*, United Kingdom - *A Statement of Principles – Banks and micro-enterprises – working together*, Ireland - *Code of conduct for business lending to Small and Medium Enterprises*

[24] Recommendation 4

"banks must provide a one-page summary of the clauses and covenants that may trigger default or other detrimental outcomes for [small business] borrowers"[25]; *and*

"banks must [each] put in place a new small business standard form contract that is short and written in plain English"[26].

The Code does not include obligations about the content or format of credit contracts, other than the general obligation in clause 3.1(d) "to provide information to you [the customer] in plain language".

In the case of consumer credit, the National Credit Code has very prescriptive obligations both in relation to pre-contractual disclosure and in relation to disclosure of interest rates and fees in the credit contract[27]. These obligations do not apply to credit disclosed to be for business purposes. (Of course, many small businesses use consumer credit products to fund their businesses and for them, these observations do not apply.) Credit for business purposes is now, however, encompassed by unfair contract term legislation that formerly was only applicable to individual consumers. Contract size limits apply - the credit facility must not be in excess of $1 million (or $300,000 if the credit facility is for less than 12 months)[28].

8.5.1. Discussion

During my consultations, some signatory banks said that small business credit contracts could be presented in a way that highlights key terms and conditions more accessibly. I agree that this would lift bank standards for small business customers. I recommend that the Code oblige signatory banks to provide small business credit customers with a pre-contractual disclosure statement that sets out the key terms and conditions. This could be provided either in advance, or at the same time, that the small business customer is provided with the credit contract for signing. The aim of the disclosure statement would be to present key information to the borrower in a much more accessible way which could include the presentation of some information diagrammatically.

Recommendation 7

A new clause should be included in the Code that obliges signatory banks to provide a written pre-contractual summary statement before providing a credit facility for a small business purpose, below $5 million. The key terms and conditions must be summarised in an accessible way, for example, a table format that includes:

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[25] Recommendation 6

[26] Recommendation 7

[27] National Credit Code sec 16 and 17. The National Credit Code applies to credit to a natural person or a strata corporation that is for personal, domestic or household purposes or to purchase, renovate or improve residential property for investment purposes: sec 5.

[28] Australian Securities and Investments Commission Act 2001 Part 2 Division 2 Subdivision BA took effect for small business on 12 November 2016.

a) the credit period,

b) repayment obligation,

c) applicable interest rates or how these are calculated (specifying the current rate),

d) fees and charges (flat fee where possible or otherwise how calculated),

e) events of default and any increased costs associated with default, again with specification of what the current rate is where a formula applies, and

f) the signatory bank's entitlement to change terms and conditions and the notice of change that will be given.

I also support the Ombudsman's Report recommendation that each bank develop a new small business standard form contract, for loans below $5 million, that is short and written in plain English. To my mind, existing clause 3.1(d) of the Code establishes a general principle that supports this initiative which makes it unnecessary for the Code to explicitly require signatory banks to work with the Ombudsman on this once-off initiative.

8.6. Variation to credit contracts

The Parliamentary Joint Committee *Impairment of Customer Loans Report*, May 2016, also focused on banks' powers under loan contracts to unilaterally vary the terms of the loan and to do so without providing the small business enough time to re-finance, should the business so wish.

To address this issue, the Ombudsman's Report recommends:

> *"A minimum 30 business day notice period to all changes to general restriction clauses and covenants (except for fraud and criminal actions) be added to give borrowers more time to respond and react to a potential breach of conditions."*[29]

[29] Australian Small Business and Family Enterprise Ombudsman, *Small Business Loans Inquiry Report*, 12 December 2016, Rec 4

8.6.1. Discussion

On 12 November 2016, the unfair contract terms requirements in Australian Securities and Investments Commission Act 2001 Part 2 Division 2 Subdivision BA took effect for small business. The impact of this has not yet been tested, however it is expected that the legislation will place a substantial brake on banks including in small business standard form contracts, a broad power to unilaterally vary a contract in a way that materially adversely affects the small business[30].

The unfair contract terms requirements are not, however, mandatory for a small business credit contract in excess of $1 million, or $300,000 if the credit facility is for less than 12 months[31] (although I understand that some signatory banks are voluntarily applying the unfair contract term principles to small business contracts where a larger amount of credit is provided). So, the possibility for at least some small business credit contracts of a unilateral contract change remains – and the issue as to what period of notice by the bank is appropriate in these circumstances.

Clause 20.4 currently provides:

> *"If:*
>
> *(a) you are a small business with a banking service being a credit facility; and*
>
> *(b) we make a variation (other than a variation referred to in clause 20.1 or 20.2) to only the terms and conditions of your credit facility (and not to the terms and conditions of the credit facilities of other small business customers), and we reasonably consider the variation will be materially adverse to you, we will give you a reasonable period of notice (not less than 10 business days) in writing of that variation, unless we consider a shorter notice period is necessary for us to avoid or reduce an increase in the credit risk to us."*

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[30] Sec 12BH gives examples of unfair terms. Para (d) specifies that a term that permits one party only to vary the terms of the contract may be unfair.

[31] Australian Securities and Investments Commission Act 2001 Sec 12BF(4)

It seems to me that 10 business days is manifestly inadequate for a variation that is particular to and materially adverse for a small business customer. This would frequently not be enough time for a small business customer to re-finance should this become an imperative in light of the materially adverse variation. The current Code timeframe is much shorter than the 6 month time period recommended in the Joint Parliamentary Committee *Impairment of Customer Loans Report*[32]. It is also shorter than the 20 days' notice that generally applies to consumer credit[33], yet a consumer credit facility re-financing would often be less complex and quicker to arrange than a small business credit facility re-financing. In my view, a 30 business day time period, as recommended in the Ombudsman's Report, would be much fairer (as per my proposed Principle 2 Fair and reasonable, ethical behaviour) in the context of a clause 20.4 materially adverse variation.

Clause 20.4 raises another issue. It currently contains a very broad proviso that permits a shorter notice period where the bank considers this "*is necessary for us to avoid or reduce an increase in the credit risk to us*". While banks advise that this is rarely used, this is a qualification that almost nullifies the provision, a practice that I have noted commonly gives rise to stakeholder complaints. I understand that there are scenarios where the bank considers that a secured asset is at risk or there is a loss of goodwill from the customer and so speedy action is required, however the exception is far too broad as currently framed. I think that the only exception that should apply is where the credit facility is in default.

Recommendation 8

Clause 20.4 of the Code should be amended to require 30 business days (rather than 10 business days) where a bank exercises the power to unilaterally vary a particular small business's credit contract in a way that is materially adverse if the credit facility is below $5 million.

Instead of the current carve out where the signatory bank considers this is necessary to avoid or reduce an increase in the credit risk, the only carve out should be where the small business is in default under the credit contract.

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[32] Rec 2b.

[33] National Credit Code section 68

8.7. Rollover of credit facilities

Banks' end of loan procedures were another point of major focus in the Parliamentary Joint Committee *Impairment of Customer Loans Report.* The Committee received evidence about borrowers being taken by surprise at their bank's decision not to roll over a term loan upon expiry. The Committee accepted that this did not normally occur. But to ensure time for a small business customer to arrange alternative finance, the Committee recommended that dialogue is commenced with the borrower at least 6 months prior to the expiry of a term loan; and where a monetary default has not occurred – a minimum of 3 months' notice of a decision not to roll over the loan, even if this requires an extension of the loan beyond the expiry date[34].

Consistent with this, the Ombudsman's Report recommends:

> *"For [small business] loans below $5 million, banks must provide borrowers with decisions on roll over at least 90 business days before loans mature, so borrowers can organise alternative financing. A longer period of time should be given for rural properties and complex businesses that would take longer to sell or refinance"[35].*

8.7.1. Discussion

In my consultation with them, signatory banks generally agreed that the Code should commit banks to provide a non-defaulting small business customer with end of loan notice. The suggestion by banks was 3 months' notice of a decision not to extend the loan, with whatever extension to the loan period is necessary to achieve this notice period.

This seemed reasonable to me, however small business representatives suggested that 3 months may not be sufficient time to organise alternative finance. The longer 90 business day timeframe recommended in the Ombudsman's Report seems to reasonably provide this additional time.

In my consultations with signatory banks, there was also discussion about the types of credit facilities to which this notice should apply. I would encourage as broad an ambit as possible and can see no reason why this would not apply to a small business overdraft. On the other hand, I understand that it may not be appropriate for the notice requirement to apply to (say) an operating lease, where the loan term is intrinsically tied to the useful life of the asset. This issue requires more detailed investigation by signatory banks, which should be picked up in the drafting stage. Needless to say, the objective should be to apply the principle as consistently as possible across small business finance and with the least number of caveats or qualifiers.

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[34] Rec 2

[35] Australian Small Business and Family Enterprise Ombudsman, *Small Business Loans Inquiry Report*, 12 December 2016, Rec 5

Recommendation 9

The Code should be amended to require a signatory bank to provide a small business customer, that is not in default under a term credit facility below $5 million, with 90 business days' notice of a decision by the bank not to extend the loan for a further term.

The ABA should consult with signatory banks about whether any types of term credit facilities should be excluded or subject to a varied rule, but with the aim for the notice requirement to apply as consistently as possible.

8.8. Small business financial difficulty

Clause 28 of the Code is a long clause setting out the assistance that a signatory bank will provide to a customer in financial difficulty. This clause applies both to small business and to customers that also have the benefit of the National Credit Code financial hardship requirements.

It seems to me that the references to the National Credit Code and some of the language in clause 28 gives the clause an appearance of focus on individual customers to the exclusion of small business customers. As a result, it may not be readily apparent to a small business customer what assistance signatory banks are committing to provide them as a customer in financial difficulty.

The clause needs to be rewritten as several clauses with some obligations applying to both small business and individual customers (the obligations currently found in clauses 28.4, 28.5, 28.6, 28.8, 28.10 and 28.11) and other clause 28 obligations redrafted so as to be particular to small business and individual customers respectively. For small business customers, a more targeted form of clause 28.2 would in my view, be more meaningful. Here I suggest the language used in the United Kingdom's *The Lending Code*:

> *"A subscriber will support a rescue plan if it believes it will succeed. If the subscriber does not believe that the rescue plan will succeed, they should explain the reasons why and help the customer and their advisers to consider other options."*[36]

In addition, the clause needs to build in relevant protections that apply to consumer credit, in particular, restrictions on signatory banks instituting or continuing with enforcement action. The details of this, for example, whether restrictions should apply where a receiver has been appointed before the signatory bank, will need to be resolved at the drafting stage.

Recommendation 10

Clause 28 of the Code should be rewritten to separate out more clearly the commitments that signatory banks are making to assist a customer with a small business credit facility

[36] *The Lending Code*, revised 28 September 2015, para 257

below $5 million in financial difficulty. In redrafting the clause, regard should be had to the language used in the United Kingdom's ***The Lending Code***. The provision should build in relevant protections that apply to consumer credit, including restrictions on signatory banks instituting or continuing with enforcement action.

8.9. Small business default notice

The Joint Parliamentary Committee's *Impairment of Customer Loans Report* included discussion of evidence provided about banks' default notice practices. This discussion was framed by concern that a bank should provide its small business customers with adequate time to address the situation.

The Committee was provided with evidence by one bank that: *"the average length of time that a borrower's loan remains in financial difficulty is over 12-18 months for non-farm gate loans and around 12-24 months for farm gate loans"*[37]. The Committee refrained from making a recommendation as to the period of default notice, accepting that a bank generally works with a small business customer for some time before a default notice is served.

8.9.1. Discussion

Unlike credit provided to an individual that is regulated by the National Credit Code, there is currently no statutory or Code requirement as to what period of default notice must be provided to a small business borrower before a credit provider may proceed to enforce its rights under the credit contract. Common law requires, however, a demand that gives "time for the borrower to arrange repayment by getting the money from a convenient place"[38].

To further lift standards for small business customers with a credit facility below $5 million, I recommend that the Code require banks to provide 30 days' notice before beginning enforcement proceedings against a small business customer in default under a credit contract. By fixing a timeframe, the Code would provide greater transparency to small business customers as to what the rules are. A 30 day timeframe would be the same period of notice as that mandated under legislation for consumer credit[39] and so provides equal treatment to small business.

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[37] Joint Parliamentary Committee, *Impairment of Customer Loans*, p.25

[38] Allens Banking & Finance Update, August 2001 referring to *Bunbury Foods Pty Ltd v National Bank of Australia Ltd* (1984) 153 CLR 491: "This does not mean time to arrange re-finance or a new bank loan but time to advise a bank or financier of the need for funds to make a payment and transfer funds to make this possible."

[39] National Credit Code sec 88 requires 30 days notice to be given to a consumer borrower in default.

As for consumer credit, it would be appropriate for the Code to include an exception for where the bank reasonably believes that urgent action is necessary to recover the debt or avoid loss in value of the security for the credit. For example, action in less than 30 days might be necessary if the bank wants to appoint a receiver and the small business customer is contemplating appointment of a voluntary administrator. Urgent action might be required if the customer cannot be located or the assets of the business or the security have a short term life and/or are deteriorating in value.

Recommendation 11

The Code should be amended to require a signatory bank to provide a customer, in default under a small business credit facility below $5 million, with 30 days' notice before beginning enforcement proceedings. An exception should apply where the bank reasonably believes that more urgent action is necessary to recover the debt or avoid loss in value of the security for the credit.

8.10. Bank appointment of receivers

The Joint Parliamentary Committee's *Impairment of Customer Loans Report* addressed conflict of interest issues where a bank appoints a firm as receiver that has previously acted as investigating accountant. The Committee recommended that in these circumstances the small business borrower should have an opportunity to request that an alternative firm is appointed as receiver[40].

As part of her small business loans inquiry, the Australian Small Business and Family Enterprise Ombudsman undertook further investigation of this issue. Her report recommended:

> *"Banks must implement procedures to reduce the perceived conflict of interest of investigating accountants subsequently appointed as receivers. This can be achieved through a competitive process to source potential receivers and by instigating a policy of not appointing a receiver who has been the investigating accountant to the business."*[41]

8.10.1. Discussion

I understand that there may be efficiencies in using the same firm as both investigating accountant and then receiver and in some remote areas, there may not be many firms to choose from. I have also considered the statistical evidence provided by one bank to the Joint Parliamentary Committee that shows that the appointment of an investigating accountant does not inevitably lead to the appointment of a receiver.

[40] Rec 9a.

[41] Australian Small Business and Family Enterprise Ombudsman, *Small Business Loans Inquiry Report*, 12 December 2016, Rec 10

While it seems to be a pretty infrequent occurrence, there can nevertheless be a clear appearance of conflict where an investigating accountant is subsequently appointed as receiver and it is important for signatory banks to be seen to be above board and clearly taking steps that are cognisant of conflict issues.

To address this, I think that the Code should require signatory banks to have a policy in place that requires potential conflict of interest issues to be taken into account in the process of appointing investigating accountants and receivers. This would be consistent with the spirit of banks' Corporations Act 2001 section 912A(1)(aa) obligation to have adequate arrangements to manage their own conflicts of interest and also with my proposed Code Principle 2 - Fair and reasonable, ethical behaviour.

Recommendation 12

The Code should be amended to require a signatory bank to have in place adequate arrangements to address potential conflicts of interest issues pertaining to proposed appointments of investigating accountants and receivers.

8.11. Small business dispute resolution

Part F of the Code encompasses dispute resolution.

Clause 37 obliges signatory banks to have a free and accessible internal dispute resolution process. In the case of some disputes brought by small business customers, the dispute resolution process must meet the standards made by ASIC under legislative provisions and set out in Regulatory Guide 165 (ASIC standards). In the case of a dispute about small business credit, the dispute is outside the parameters of legislation and instead the Code requirements in clause 37.3 apply. The ASIC standards and the clause 37.3 requirements are similar in their essentials, but the ASIC standards are more detailed.

Clause 38 obliges signatory banks to belong to an external dispute resolution scheme. As a result, if a small business customer's dispute with a bank is not resolved within the bank's internal processes, the small business borrower is able to take its complaint to EDR, unless an exclusion in the EDR scheme's Terms of Reference renders the dispute outside of scope.

In its submission to the Code Review, the ABA has suggested simplification of the Code's dispute resolution provisions. More fundamentally, other submissions have expressed concerns about the unavailability to small business of external dispute resolution because of exclusions in EDR scheme Terms of Reference.

In this section, I address dispute resolution issues that relate to small business. Other dispute resolution issues with ramifications for all Code customers are discussed in Chapter 19.

8.11.1. Internal dispute resolution

As mentioned earlier in my Report, a signatory bank often chooses to deal with a small business as a customer of the bank's retail division. Where this is the case and the small business makes a credit-related complaint, the signatory bank may handle the complaint utilising processes and procedures that meet the ASIC standards – over and above the less detailed requirements set out in clause 37 of the Code. The ASIC standards and clause 37 requirements are highly congruent and it may be that from bank's perspective, a uniform process for retail customers (business and individual customers) is a simplification.

I understand that it would, therefore, be largely consistent with current practice if the Code were simplified by requiring all complaints to be handled in a way that meets ASIC standards. Of importance for this Chapter of my Report, this would mean that all small business complaints (not just those encompassed by ASIC Regulatory Guide 165[42]) would have to be handled in a way that meets the ASIC standards.

Whilst this would not require much, if any, change in practice for the banks, it would be an appropriate strengthening of the commitments that the Code makes for small business. In Chapter 6.8, I have provided a suggested redraft of current clause 37 that effects this recommendation.

Recommendation 13

The Code should be amended to oblige signatory banks to provide all Code customers that have a banking services dispute with access to internal dispute resolution processes that meet the standards set out by the Australian Securities and Investments Commission in Regulatory Guide 165.

8.11.2. External dispute resolution

The Joint Parliamentary Committee's *Impaired Customer Loans Report* expressed concern about small business, including farming enterprises, access to external dispute resolution for loan disputes. This has led to three reviews.

1. As previously referred to, FOS is reviewing its small business jurisdiction in consultation with ASIC[43].

[42] Note that Corporations Act 2001 section 912B has the result that the ASIC standards only apply to a financial services licensee where providing a financial service. Although a bank is a financial services licensee, the provision of credit is not a financial service. Accordingly the ASIC standards do not apply to a dispute about a bank's provision of credit. Where the ASIC standards do not apply, currently Code clause 37.3 sets the requirements for the internal dispute resolution process.

[43] FOS, *Expansion of FOS's Small Business Jurisdiction*, Consultation Paper, August 2016

2. There is a Review of external dispute resolution and complaints schemes by a Panel chaired by Professor Ramsay (terms of reference dated 8 August 2016) (Ramsay Review). This is also considering the adequacy of small business access[44]. The Review Panel's Interim Report, issued in December 2016, includes a draft recommendation that small business should have access to financial services external dispute resolution for higher value disputes than is currently available[45].

3. The Australian Small Business and Family Enterprise Ombudsman was also tasked to address external dispute resolution as part of her small business loan review. Her report recommended access to external dispute resolution for a small business credit facility of up to $5 million[46], with capacity by the scheme to deal with disputes with third parties appointed by the bank such as valuers, investigating accountants and receivers[47]. In addition, she recommended a nationally consistent approach to farm debt mediation[48].

These reviews are very important. In my consultations, I heard concerns, in particular, that farmers are being channelled by banks into state-based farm debt mediation schemes that do not offer the same quality of dispute resolution available through EDR (eg. there is no independent investigation, there are often no binding powers, etc). My expectation is that the various reviews referred to above will progress resolution of the problem. However, there are two enhancements to the Code that I think would assist here.

First, the Code should include a new obligation on signatory banks, when informing Code customers of mediation options, to also provide information about their entitlement to access the bank's internal and then external dispute resolution process. This is all the more important given that tight timeframes for accessing mediation often apply. For example, the Queensland Farm Debt Mediation Scheme Protocols give farmers 21 days from notice of intention to take enforcement action to request mediation.

Second, the Code should oblige signatory banks to consent to their EDR scheme having jurisdiction to decide a dispute with a Code customer that has been the subject to mediation but has failed to reach an agreed settlement. Where there is no settlement, the dispute is unresolved and so access to the EDR scheme should be available.

Recommendation 14

The Code should include the following new obligations on signatory banks:

a) when informing Code customers of mediation options, signatory banks must also

[44] http://kmo.ministers.treasury.gov.au/media-release/072-2016/

[45] *Review of the financial system external dispute resolution and complaints framework*, draft recommendation 3

[46] Australian Small Business and Family Enterprise Ombudsman, *Small Business Loans Inquiry Report*, 12 December 2016, Rec 11

[47] Australian Small Business and Family Enterprise Ombudsman, *Small Business Loans Inquiry Report*, 12 December 2016, Rec 13

[48] Australian Small Business and Family Enterprise Ombudsman, *Small Business Loans Inquiry Report*, 12 December 2016, Rec 14

provide information about the customer's entitlement to access the bank's internal and then external dispute resolution process;

b) signatory banks must consent to their external dispute resolution scheme having jurisdiction to decide a dispute with a Code customer that has been the subject of mediation but has failed to settle.

9. RESPONSIBLE LENDING

In response to submissions to the Code Review, this Chapter considers the prominence given in the Code to responsible lending and whether current clause 27 should be redrafted either to convey the bank's commitment more clearly or to enhance the legislative process requirements. A couple of issues in relation to reverse mortgages are also covered.

The previous Chapter of my report deals with issues specific to the provision of credit for the purposes of a small business. The following Chapter addresses the related issue of credit card lending which was a particular focus of many stakeholders in their submissions and discussions with me.

9.1. Code and legislative provisions

Clause 27 of the Code imposes the obligation on banks to lend responsibly. It provides:

> *"Before we offer, give you or increase an existing credit facility, we will exercise the care and skill of a diligent and prudent banker in selecting and applying our credit assessment methods and forming our opinion about your ability to repay the credit facility".*

In 2010, the NCCP Act commenced. The Act applies to credit provided to an individual or strata corporation that is for personal, domestic or household purposes or to purchase, renovate or improve residential property for investment purposes. As previously noted, the Act does not apply to credit for business purposes.

To comply with the Act's detailed responsible lending regime for consumer credit, a bank must make reasonable inquiries about a consumer's credit requirements and objectives. The bank must also make reasonable inquiries and take reasonable steps to verify the consumer's financial situation. The bank must then make an assessment of the product in light of the information about the consumer: the credit contract must be assessed as unsuitable for the consumer if the consumer will be unable to comply with the financial obligations under the credit contract (or could only comply with substantial hardship) or if the credit contract will not meet the consumer's requirements or objectives. This assessment is referred to as a 'not unsuitable assessment'.

9.2. Prominence of Code responsible lending commitments

There has for many years been a view that the Code does not give sufficient prominence to the banks' commitment to lend responsibly. In her December, 2008 Final Report, the last Independent Reviewer of the Code recommended that a new key commitment is incorporated in the Code:

> *"We will be responsible lenders in approving credit, offering credit limit increases, supporting customers facing financial difficulty; and promoting responsible use of credit."*

This recommendation was not accepted by the ABA. The same issue was raised in submissions to my Review.

9.2.1. Discussion

It seems inarguable to me that responsible lending is a key issue that should be given prominence in the Code. Under my recommended architecture discussed in Chapter 6.5, the Principles would be the place for this. In my example Principles, a commitment to a responsible approach to lending is Principle 5.

Recommendation 15

The Code should give prominence to the banks' commitment to lend responsibly by including this in Principles that appear at the front of the Code.

9.3. Clause 27

9.3.1. Stakeholder views

A number of submissions suggested that current clause 27 is obscurely drafted and does not clearly convey its intent. It was suggested that it should be renamed "Responsible lending" rather than "Provision of credit". One submission proposed that the Code could take guidance from the Customer Owned Banking Code of Practice that applies to Australian credit unions, mutual building societies and mutual banks. That code includes the following:

> *"6.1. We will always act as a responsible lender and will comply with responsible lending laws.*
>
> *6.2. We will base our lending decisions, including decisions to extend existing credit facilities, on a careful and prudent assessment of your financial position and requirements and objectives as indicated to us. We will periodically review our credit assessment procedures and criteria for the products we issue.*
>
> *6.3. We will generally only lend amounts to you that we believe, on the information available to us, you can reasonably afford to repay. However, different criteria will apply in the case of some products, such as bridging finance arrangements and reverse mortgage loans (if we offer these).*
>
> *6.4. We expect you to provide honest and accurate information to us when applying for a loan or the extension of a credit facility. We will also take reasonable steps to verify your financial situation.*

> *6.5. We will promote the responsible use of credit to our customers using a range of approaches."*

The Joint Consumer Submission (which was made on behalf of 16 consumer representative organisations) proposed that clause 27 should be bolstered by obliging banks to comply strictly with ASIC Regulatory Guide 209 *Credit licensing: Responsible lending conduct* [49]. It also proposed that the clause is expanded to require a clear process to ensure credit is not unsuitable, detailed information is requested about the borrower, the financial situation of the borrower is verified and the credit meets the needs and objectives of the borrower[50].

Additionally, the ABA proposed that clause 27 is amended to clarify that a guarantor is entitled to rely upon clause 27 and to expect the bank to take care in its credit assessment of the customer whose debt is being guaranteed.

9.3.2. Discussion

In Chapter 3.3, I have referred to the Courts' willingness to hold banks to account where they find the diligent and prudent banker credit assessment obligation has been breached. Clearly the clause as drafted is currently legally effective. As mentioned elsewhere, the weakness is that the current clause 27 wording does not readily convey to a borrower what the banks' promise is. To that extent, it compares unfavourably with clause 6 of the Customer Owned Banking Code of Practice. My recommendation is that clause 27 should be renamed "A responsible approach to lending" and modernised to use plain language that is much more accessible for Code customers.

Recommendation 16

The Code should rename current clause 27 as "A responsible approach to lending" and redraft it to use clearer, more modern language. The new clause should oblige banks:

a) to review the applicant's financial information, situation and requirements carefully and prudently and consider the application on its merits; and

b) in general, only lend amounts that the bank believes the applicant can reasonably afford to repay.

Further I agree with the ABA that it would be useful if the Code clearly states that a guarantor is entitled to rely upon clause 27 and to expect the signatory bank to take care in its credit assessment of the customer whose debt is being guaranteed. This would be consistent with *Doggett v Commonwealth of Australia* (2015) VSCA 351[51].

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[49] Rec 24b.

[50] Rec 24c.

[51] In that case, the Court of Appeal held clause 27 was a "relevant provision" for the purposes of the guarantee the subject of the case (clause 31.3 of the Code requires a guarantee to include a statement

Recommendation 17

The Code should make explicit that the obligation in current clause 27 is owed to a guarantor not just the borrowing customer.

I do not, however, support the extension of clause 27 to traverse and expand upon the responsible lending process requirements in the NCCP Act as proposed in the Joint Consumer Submission. First, my Code Design Approach aim is to avoid duplication of legislation unless this is essential to consumer understanding. To the extent that proposed wording goes beyond the legislation (particularly the Joint Consumer Submission suggestion that the banks request "detailed" financial information), it seems to me that the extension is subtle and is likely to lead to arguments about maladministration. Given that the NCCP Act prescriptive legislative regime for responsible lending was carefully worked out by government with input from all stakeholders, I hesitate to recommend a subtle re-working of this via the Code unless there is a clear benefit.

Nor do I think that it is appropriate for the Code to oblige strict compliance with ASIC guidance (Regulatory Guide 209) about responsible lending. As ASIC indicates in its guidance, the NCCP Act responsible lending obligations to make "reasonable inquiries" and take "reasonable steps" are "scalable", that is, what is required depends on the circumstances[52]. Regulatory Guide 209 is intended by ASIC to be guidance – not to be entrenched into a customer contract by the Code.

9.4. Transparency of responsible lending process

9.4.1. Stakeholder views

During consultations with stakeholders, there was discussion about making signatory banks' responsible lending processes more transparent to their customers. One submission suggested that, where credit is sourced for a customer by a broker, the bank should be obliged to inform the customer that the broker is the customer's representative and the customer should carefully check all information submitted to the bank by the customer. I was advised however, that customers often do not see information submitted by a broker on their behalf and so are not in a position to check the information. To address this issue, the Joint Consumer submission suggested that the bank should be required to provide this information to the customer for checking.

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that "relevant provisions of the Code apply") and so the bank's clause 27 obligation was owed to the guarantor, not just the borrowing customer.

[52] ASIC Regulatory Guide 209 p.11

When these issues were discussed with signatory banks, I was told by one bank that its practice is to 'play back' to a consumer credit applicant the financial information that the bank is relying upon in making its 'not unsuitable' assessment. The bank noted, however, that this is not necessarily the financial information that is submitted at the time of application, that the bank's inquiry and verification process may lead to some adjustment of the original information.

To avoid creation of yet another disclosure standard, it seems to me that the best way for signatory banks to 'play back' information to a consumer credit customer is for the bank to provide the customer with the bank's already obligatory 'not unsuitable' assessment. The legislation requires this document to be provided free of charge on request[53]. I understand from signatory banks that few requests are currently received, quite possibly because few consumer customers are aware of this document and their right to request it. The advantage of the 'not unsuitable' assessment is that the figures in this assessment of are at the end of the chain – after the customer's input, the broker's input and any further input from the bank itself.

From the examples of 'not unsuitable' assessments that were provided to me, it would seem that typically this document is very brief. In my consultations, I heard suggestions that a more fulsome document should be provided to consumers, including details of the verified income and expense calculations, along with a warning that the document should be checked before the credit contract is signed. These proposals highlight a dilemma inherent in disclosure as a tool to protect consumers – basic information may not reveal enough, too much information is unlikely to be read.

Signatory banks have indicated that significant process change and operational cost would be incurred in producing and providing the 'not unsuitable' assessment to all consumers – even in its current minimalist form. Signatory banks are concerned that this would further slow the lending process and note the marketing emphasis placed by non-bank short term lenders on their ability to provide credit quickly.

Given these concerns, I am not proposing that the Code require the 'play back' information to incorporate more detail than that necessary to meet legislative requirements. Some signatory banks may choose to provide more detail and even to initiate a discussion with consumer customers about the figures before the signing of the credit contract. Some consumer customers may initiate such a discussion themselves. In either case, this could potentially reduce lending on the basis of incorrect information (including because inaccurate information is provided by the customer's broker) and give the customer a chance to re-think affordability.

Recommendation 18

The Code should be amended to include a new provision that obliges signatory banks to provide an applicant for consumer credit with the bank's 'not unsuitable assessment' prepared in accordance with National Consumer Credit Protection Act 2009 Part 3-2. This document should be provided free of charge, and as a matter of course, prior to the customer signing the credit contract.

[53] National Consumer Credit Protection Act 2009 sec 132

9.5. Reverse mortgages

9.5.1. Submissions

In its submission to the Code Review, FOS suggested that the Code should include reverse mortgage protections similar to those in the Customer Owned Banking Code of Practice. FOS stated that this would harmonise standards in the financial services sector[54].

The Customer Owned Banking Code of Practice provides:

> *"8.1. We are committed to responsible lending practices in relation to reverse mortgage loans (if we issue, introduce or arrange these products).*
>
> *8.2. As an issuer, introducer or arranger of reverse mortgage loans, we will:*
>
> - *comply with all applicable National Credit Act requirements regardless of the purpose for which the loan proceeds are used*
> - *strongly encourage you to discuss a reverse mortgage loan with family members and Centrelink (so that you understand any impact on Centrelink entitlements)*
> - *strongly encourage you to seek financial advice from an independent qualified financial adviser, and to consider seeking independent legal advice (we may require this)*
> - *ensure the reverse mortgage loan:*
> - *limits your repayment obligations to the market value of the property (or lesser amount if owed), except in the circumstances permitted by the National Credit Act; and*
> - *allows you to discharge your obligations under the loan at any time*
> - *comply, where they apply, with National Credit Act restrictions and requirements in relation to enforcement proceedings."*

[54] p. 11 - 12

9.5.2. Discussion

The National Credit Code extensively regulates reverse mortgages that are entered into for personal, domestic or household purposes, but not for other purposes. For a credit union or other financial institution that has subscribed to the Customer Owned Banking Code of Practice, the effect is that National Credit Code rules apply to all reverse mortgages extended to that institution's individual or small business customers. The Customer Owned Banking Code of Practice also introduces two new protections for all reverse mortgages to which the code applies: the requirement to caution the customer to seek financial and legal advice and the customer's right to early discharge of the loan.

I recommend that the Code is amended to incorporate similar protections so as to keep pace with the standards set by credit unions, mutual building societies and customer owned banks. Whilst the reverse mortgage market is currently quite small, there have been some suggestions that as baby boomers retire there may be more interest in this product, making the amendments worth doing now.

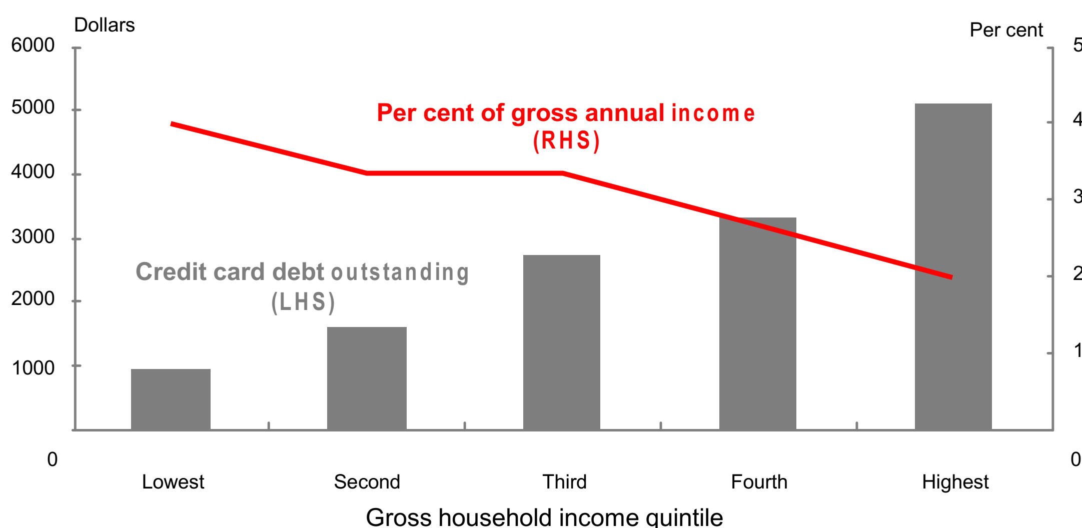
Recommendation 19
The Code should be amended to include protections for reverse mortgage customers that match those set out in clause 8 of the Customer Owned Banking Code of Practice.

10. CREDIT CARD LENDING

10.1. Introduction

Whilst credit cards are highly advantageous for some customers, there is increasing concern that some customers are encountering problematic credit card debt. A recent study in the United Kingdom by the Financial Conduct Authority found that this was the case for 24% of credit card holders[55]. In Australia, there is a falling percentage of credit card debt that accrues interest (down from 70% in 2011 to 66% in 2016)[56]. According to the ABA Fact Sheet *Credit Card Use in* Australia, credit card interest accrued in relation to an average amount of $1,971 in 2015, was 6% lower than in the previous year. This is a positive indication, but statistics as to the average credit card debt burden for lowest quintile householders remain troubling.

Figure 6. - Credit card debt by household income quintile, 2013-14



Source: Australian Government, The Treasury ***Credit cards: improving consumer outcomes and enhancing*** competition, May 2016, quoting ABS Catalogue Number 6523.0

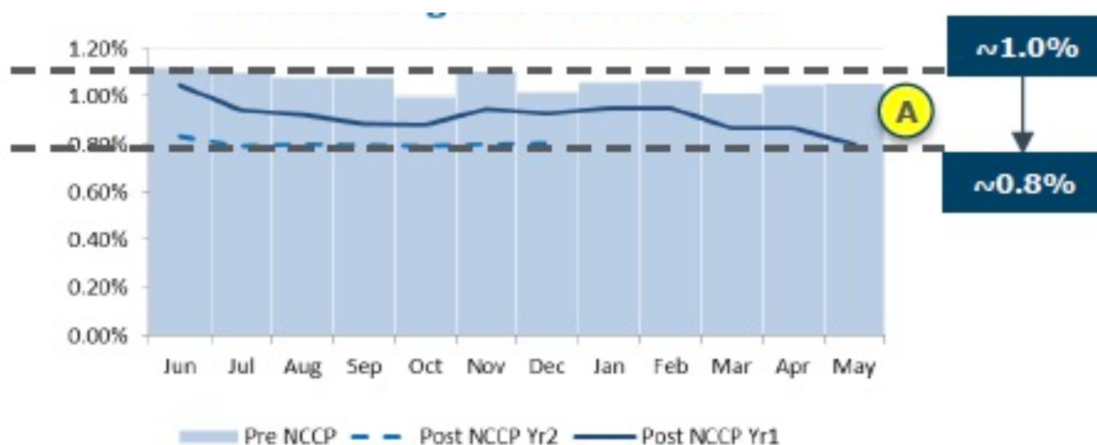
This shows that the burden of servicing debt associated with credit card balances most impacts households in the lowest income quintile. This further diminishes those households already limited discretionary income.

[55] UK Financial Conduct Authority *Final findings report MS14/6.3*, July 2016

[56] Australian Government the Treasury, *Credit cards: improving consumer outcomes and enhancing competition*, May 2016, p.4

In 2011, a range of credit card reforms were enacted by government[57]. These included card provider disclosure obligations, restrictions on credit card credit limit offer practices and payment application requirements. Although I understand that there is some disagreement as to the impact of the 2011 reforms, one of the major banks has provided me with analysis that suggests that for customers making minimum monthly payments only (those of greatest concern) since the implementation of these reforms, interest charges as a percentage of credit card balances have reduced by about 20%. While some of this may be the effect of the new payment hierarchy (applying payments to highest interest rates first), the data suggests some change in customer behaviour. Consumer advocates also provided anecdotal evidence that the 2011 reforms have encouraged consumers to understand the importance of reining in their debt.

Figure 7. - Interest charges as a % of Credit Card balances for customers making minimum repayments



Source: Information provided by a signatory bank, November 2016

Following a Senate Economics References Committee Inquiry[58], the Australian Treasury in May 2016 proposed further credit card reforms to improve consumer outcomes and enhance competition. For some of these reforms, Treasury has indicated that draft legislation will be developed in the near term (Phase 1 reforms). Other possible reforms will be considered by government after the completion of consumer behavioural testing (Phase 2 reforms). For both Phase 1 and any Phase 2 reforms that are decided upon by government, it is likely to be at least 18 months before draft legislation is available. Competing priorities for Treasury and drafting resources and for Parliamentary time could mean that legislation will not be introduced into Parliament during the life of this Parliament.

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[57] National Consumer Credit Protection Act 2009 Part 3-2B and Regulations pursuant to that Part

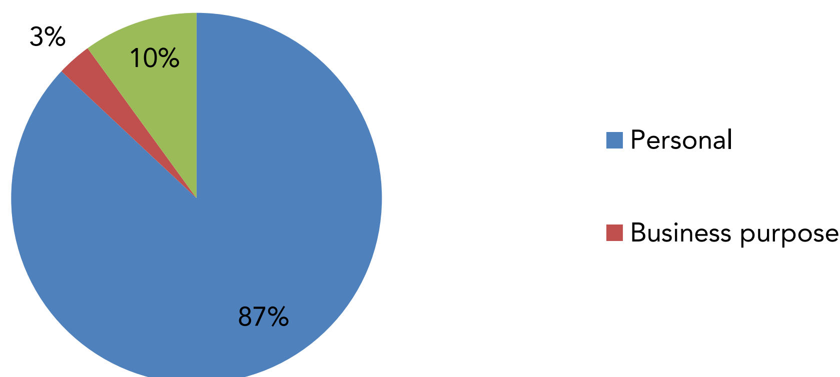
[58] Senate Economics References Committee Report, *Interest rates and informed choice in the Australian credit card market*, December 2015

In view of this, some of the submissions to the Code Review by consumer representative organisations urged that the Code should, as a best practice measure, commit signatory banks to credit card reforms, including those canvassed in the May 2016 Treasury Consultation Paper. Likewise, Treasury representatives have expressed their support for industry voluntarily adopting some of their proposed reforms. On the other hand, some industry submissions to the Code Review thought that the credit card reforms should be left to government so that the reforms apply to all card issuers, and not just to signatory banks.

10.2. Credit card market

As at April 2015, there were about 16 million credit cards on issue and these were being used for 179.5 million transactions on average each month. As at September 2016, there was an estimated $50 billion aggregate balance on credit cards in Australia.

Figure 8. - Credit card usage (number of transactions) in Australia



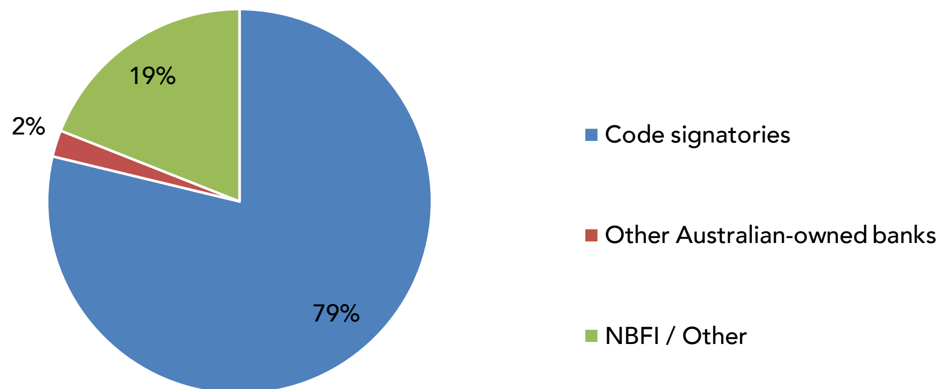
Source: ABA data provided in December 2016

Credit cards are relied upon heavily by individual consumers as a source of unsecured credit, constituting 68% of applications made by them for unsecured credit. Credit cards represent just under half small business unsecured credit applications[59]. There are estimated to be about 200 credit card products on the market with signatory banks having a market share of about 88% of the credit cards on issue and about 81% of balances outstanding[60].

[59] Information provided by Code Compliance and Monitoring Committee arising out of Own Motion Inquiry, Provision of Credit Report, January 2017

[60] Senate Economics References Committee, *Interest rates and informed choice in the Australian credit card market*, December 2015, p.10 quoting information provided to the Inquiry by the ABA

Figure 9. - Credit card balances outstanding by category of institution (September 2016)

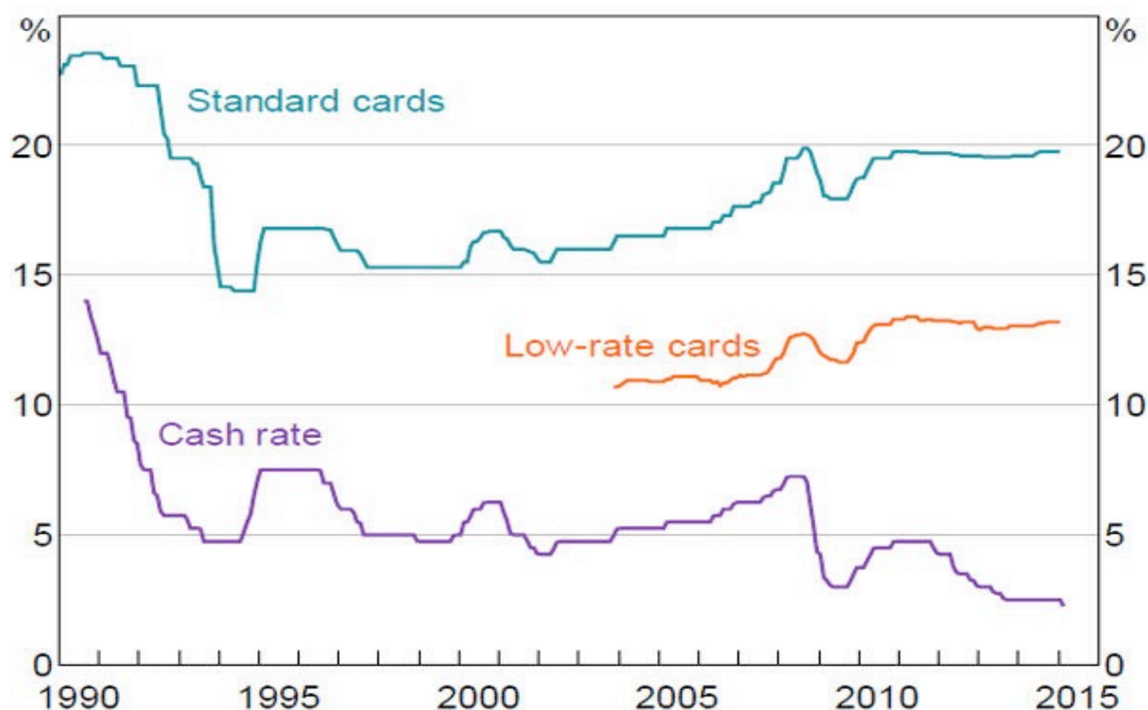


Source: APRA monthly banking statistics September 2016 and ABA data as to non-bank share of credit card market

Intense competition has seen discounted balance transfer offers and a focus on rewards program, in effect increasing the cross-subsidy between credit card customers. Despite this competition, the headline interest rate on 'standard' credit cards has remained near 20%, and the headline interest rate on 'low-rate' cards has remained at around 13% since 2011. (Of course, this data masks the considerable diversity in rates offered by banks, with some cards having interest rates below 10%.) By way of comparison, the Reserve Bank of Australia cash rate was almost 5% in 2011 and has been falling steadily to the December 2016 rate of 1.5%[61].

[61] http://www.rba.gov.au/statistics/cash-rate/

Figure 10. - Credit card interest rates and the cash rate



Source: Reserve Bank of Australia data (2015)

This is not to suggest that the gap between the cash rate and the card rate represents the actual interest return for banks. Interest free periods and promotional interest rates on balance transfers reduce that return. Industry has provided me with data that suggests that interest earned as a percentage of balances outstanding on 'standard' cards is actually more like 13%.

10.3. A role for the Code

A threshold issue for my consideration of credit cards was whether it was something that could fairly be dealt with in the Code. During consultations, many signatory banks expressed the firm view that credit card reforms should apply to all credit card issuers and that it would introduce an 'uneven playing field' if the Code brought forward these reforms for signatory banks alone.

I understand that non-bank and non-signatory competitors may be able to win some market share from signatory banks, with a revenue cost to Code-subscribing banks. The industry were unable to provide any historical data that might indicate the extent of this projected customer 'flight'. What evidence I could find suggested that bank customers tend not to be very mobile and are inclined to stay with their existing provider – even where it would be financially sensible to switch. Nonetheless, I accept this is a risk.

The banking industry expressed concern that different rules for signatory banks and other credit card issuers would add to customer confusion in an already complex credit card landscape. Another concern expressed was that the new requirements would drive the customers who can least afford it to lower standard providers who may offer lesser consumer protections (for example, less generous financial difficulty assistance) or offers more credit at higher fees and interest rate charges. Perversely, protection standards may well actually drop for them. I accept that this may occur for some customers, but of course this must be balanced against the improvements in protection that would occur for customers of signatory banks – currently the vast majority.

It seems to me that the evidence of consumer detriment that flows from excessive credit card debt is indisputable. Where available credit makes payment simple and consumers do not see the money they are spending, research shows that consumers will spend more[62]. Studies suggest that at least some consumers rely on their credit card issuer's approval of a credit card as a signal as to what they can afford[63]. It is also abundantly clear that many stakeholders view credit cards as a priority area for improvement in consumer protection and have a strong expectation that this Review will produce meaningful change.

On my assessment of the risks of proceeding with greater protection in the Code compared to the risks of doing nothing while waiting for government reform, I am recommending that the Code be used to lead the way and bring forward reform in this area.

10.4. Assessment of customer's ability to service a credit card

In response to concerns about the "credit card debt trap"[64], there has been questioning as to whether the credit limits that are set by credit card providers are consistent with responsible lending practices. This has uncovered an ambiguity in the way responsible lending obligations apply to the assessment of a customer's ability to meet credit card payment obligations.

The Treasury Consultation Paper, *Credit cards: improving consumer outcomes and enhancing competition,* May 2016 states:

> *"While credit providers are still required to ensure the consumer is able to meet their financial obligations without substantial hardship, many card issuers test affordability of a credit limit based on a consumer's ability to meet only the minimum prepayment amount, sometimes with a small buffer.*

[62] Sunstein C, 'Apple Pay Could Make You Poorer' *Bloomberg View*, 10 September 2014 cited in a literature review undertaken by ASIC in September 2015

[62] Rec 25a.

[63] Cheema and Soman *The Effect of Credit on Spending Decisions: The Role of the Credit Limit and Credibility* (2002) Marketing Science 21(1) cited in a literature review undertaken by ASIC in September 2015

[64] Senate Economics References Committee *Interest rates and informed choice in the Australian credit card market*, December 2015 p. 55

> *This then sets an upper bound on the credit limit that the issuer is able to offer the consumer. The length of the repayment period and cumulative interest charges associated with only making the minimum repayments may not be considered when assessing whether a card is 'not unsuitable'."*[65]

To address this ambiguity and inconsistency of practice, Treasury is proposing the amendment of the NCCP Act to state that a credit card will be unsuitable if a consumer cannot afford to repay the full credit limit within a reasonable period. This is a Phase 1 requirement and so has the government's support. Treasury has asked for submissions as to how a 'reasonable period' should be defined in the legislation.

The Joint Consumer Submission to the Code Review proposed that the Code should introduce this reform and should require signatory banks to assess customers' ability to pay the credit limit over a 3 year period[66]. As discussed in Chapter 10.3, the banking industry position has been that reform in this area should be done by government, citing concerns over confusion for consumers, maintaining higher standards of customer protection and the need for a level playing field.

10.4.1. Discussion

Consistent with my proposed Principle 5 Responsible approach in lending, I think that the Code should include an obligation on signatory banks to assess the consumer's capacity to pay the full amount of the card credit limit – not just the consumer's ability to meet minimum monthly repayments. Suffice to say here that this change could assist some consumers to rein in burdensome levels of credit card debt.

Whilst some consumers may go elsewhere to obtain their credit as a result, I do not think that this is a justification for signatory banks to put aside the principles of responsible lending and participate in lower standards. I discuss at Chapter 10.3 the competition issues more fully.

Consistent with my position that access to credit issues dictate a more flexible lending approach for small business, I am not proposing that this should also be the case where a credit card is issued to a small business. In any event, as Figure 8 shows, there are relatively few credit cards issued for business only purposes.

I have given thought to whether a proposed Code provision should mandate a period of time that should be used as the repayment period. I have decided against a fixed time period and am recommending the language of "a reasonable period".

---

[65] Australian Government the Treasury, *Credit cards: improving consumer outcomes and enhancing competition*, May 2016, p.12

[66] Rec 25a.

First, this approach is consistent with my view discussed in Chapter 6.4 that a code of conduct should to the extent practicable, operate at a principles-level rather than impose detailed prescription. Second, I do not have sound evidence to determine which fixed time period should apply. The "reasonable period" requirement establishes the principle but still preserves some flexibility for signatory banks to accommodate different consumers' needs and situations. It also provides some recognition of the "level playing field" argument.

The language of "reasonable period" is also consistent with the United Kingdom Consumer Credit Sourcebook approach. Its accompanying guidance refers to the relevance, when determining what is a reasonable period, of the typical time period for repayment for a fixed-sum unsecured personal loan of the card limit amount – but this is guidance rather than prescription. If, in fact, the Code is in time overtaken by legislation, it would be possible to omit the Code provision at that time.

Recommendation 20

The Code should be amended to include a new obligation that applies to signatory banks when undertaking a 'not unsuitable' assessment in relation to a consumer credit card (new credit card or credit increase). The bank should assess the consumer's capacity to pay the full amount of the card credit limit in a reasonable time period.

10.5. Amount of initial credit card limit

10.5.1. Introduction

National Consumer Credit Protection Regulation 28JA requires a credit card issuer to make reasonable inquiries about the maximum credit limit that a consumer requires. The Regulation does not expressly prevent the card issuer from offering the consumer a higher amount, although I understand that some signatory banks interpret its intersection with responsible lending requirements as having this result.

The Joint Consumer Submission suggested that the Code should provide that the maximum credit limit must not be greater than that applied for by the customer or greater than the price of the goods purchased in a linked credit transaction[67]. (The latter is in circumstances where goods or services are paid for by applying for a credit card – assisted by the merchant. Defined as a 'tied continuing credit contract' under the National Credit Code).

10.5.2. Discussion

According to the ABA Fact Sheet *Credit Card Use in* Australia, the average credit card limit was the same in 2015 as it was five years ago. This may be a positive indicator, but that depends upon other factors including the distribution of the average and whether the average number of credit cards per customer has increased.

[67] Rec 25d. and e.

I think that it would address any current ambiguity in the law and be good practice if the Code required signatory banks to refrain from offering Code customers a credit limit that is greater than their stated credit need. To my mind, this would be respectful of the customer's decision to set the level of debt they are comfortable with and it would be giving primacy to the customer's decision, rather than the bank's marketing and sales interests. It would, therefore, be consistent with my proposed Code Principle 1 Focus on customers. For some customers, this would also help them to manage their spending and would be consistent with my proposed Code Principle 5 Responsible in lending.

I recommend that the Code include a new provision obliging signatory banks to ensure that the credit limit for a credit card issued to a Code customer is no greater than the amount applied for. If a signatory bank issues a credit card for a tied continuing credit contract (as defined in the National Credit Code), the amount of credit applied for by the Code customer should be not greater than the cost of the goods – which I see as the identical principle. I have been told by industry that signatory banks do not enter into contracts of this type and by consumer advocates that they do. It seems the path of least harm to prohibit them.

In my view this should apply to all Code customers including the relatively few credit cards that are issued specifically for the purpose of a small business. It seems to me that the logic of respecting a customer's decision about their credit needs applies equally to a small business.

Recommendation 21

The Code should be amended to include a new obligation that prohibits signatory banks from providing a customer with a credit card credit limit that is more than that applied for by the customer or more than the cost of goods purchased in a linked credit transaction.

10.6. Credit card credit limit increase offers

10.6.1. Introduction

As a result of legislative change in 2011, a credit provider is only allowed to make a written credit card limit increase offer to a consumer if the consumer has previously given their express consent to such an invitation and the credit provider has a record of this consent[68].

The Treasury Consultation Paper, Credit cards: improving consumer outcomes and enhancing competition, May 2016 states:

> *"The Government is aware that some card issuers circumvent the spirit of the legislation by making unsolicited offers by other means, such as over the phone or via online banking portals. Consumers are also often unaware that they have granted their prior consent to receiving unsolicited offers, because of the way in which consent is sought at the time of applying for a credit card."*

[68] National Consumer Credit Protection Act 2009 Part 3-2B

To address this, Treasury is proposing a complete prohibition on credit card issuers making credit card credit limit offers, including the removal of card issuers' ability to seek prior consent to an offer. This is a Phase 1 requirement and so has the government's support.

The Joint Consumer Submission urged the Code to implement this reform for all Code customers[69]. However, most signatory banks felt that this reform should be left to government so that reform applies to all credit card issuers. They also argued that the rules changed with the 2011 reforms and a further rule change via the Code (which would only apply to signatory banks) would be confusing for signatory bank customers.

10.6.2. Discussion

In assessing this issue, I have looked closely at data provided by some signatory banks that they argue shows that customers with a bank-initiated credit limit increase pose no more risk of credit default, than customers who have self-initiated a credit limit increase. It is interesting data but not conclusive, as I would expect that customers under financial pressure are quite likely to be disproportionately represented amongst customers who have self-initiated a credit limit increase. A comparison with that group does not necessarily disprove the concern that bank-initiated credit limit increases are adding to the financial pressure on at least some of those who accept those offers.

The data provided to me also suggests that at least some signatory banks make credit limit increase offers to customers categorised by the bank as posing a high credit risk. Granted that high risk customers are considerably less likely to receive a credit limit increase offer than low risk and mid-level risk customers, however, on one view any bank-initiated credit limit increase offers to that group could be a concern.

This prompted some discussion with industry about whether a restriction on credit card limit increase offers should only apply to customers at risk of over-indebtedness. My concern here is about how this could be framed in a way that would provide meaningful protection without becoming overly prescriptive.

In the end, I did not find any sound reason to depart from the view arrived at by Treasury in its review. As in the previous discussion, I think that it would be respectful for signatory banks to leave it to Code customers to initiate a credit card credit limit increase if they should so wish. I agree with Treasury that an 'opt in' mechanism at the time of application for a card is not a particularly effective mechanism for testing whether the customer wants to receive bank marketing of credit card limit offers. I am also aware that bank marketing of credit card limit offers is known to use psychological and behavioural concepts to make their offers tempting[70]. In my view, it would be better practice if credit card credit limit increases cease to be the domain of bank marketing, but rather are entirely responsive to customer requests.

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[69] Rec 25b.

[70] Harrison, P and Massi, M *Congratulations you are pre-approved! An analysis of credit limit upselling letters*, commissioned by Consumer Action Law Centre and cited in in a literature review undertaken by ASIC in September 2015

I recommend that the Code should bring forward the Treasury proposal so that a higher credit card limit is only able to be offered in response to a specific request by a Code customer (and for the reasons in the previous section I propose that this apply to small business customers not just to individual consumers). This would mean that a Code customer 'opt in' to credit card limit increase offers would no longer be sufficient to warrant an offer of a higher limit.

Of course, my recommended change to the Code would not prevent a bank from providing a new credit customer with information about how to apply for a credit card credit limit increase should they so wish at a later date. Nor would it prevent a bank employee from responding to a question from a customer about whether a credit limit increase is possible or how to apply for one.

It has been put to me that such a ban would be unfair to those customers who have already 'opted in' to bank credit card credit limit increases, and are expecting them to continue. Again, it would be open to each bank to undertake a final round of credit card credit limit increases for those customers, together with an explanation of the new requirements, before the new Code provision came into effect.

Recommendation 22

The Code should be amended to include a new obligation that prohibits banks from offering a credit card credit limit increase to a Code customer, other than in response to a customer-initiated specific request for a higher credit limit. The drafting should make it clear that the requirement for a customer-initiated specific request is not met by the customer 'opting in' to the bank making credit limit increase offers to the customer.

10.7. Charging of interest on unpaid credit card balance

10.7.1. Introduction

The Treasury Consultation Paper, Credit cards: improving consumer outcomes and enhancing competition, May 2016 states:

> *"The calculation of interest charges on credit cards is complex and varies across card issuers. The most common contractual arrangement is that when the statement balance is not paid in full, interest is charged (in the next statement) on every purchase in that month from the date that the purchase was recorded to the date when repayments are made. Two aspects of this arrangement are likely to be poorly understood by consumers or perceived as unfair:*
>
> - *in the first statement where interest charges appear (that is, the statement following the one where the balance was not repaid in full), interest is charged not only for that statement period, but also the previous one…; and*

- *for the balance from the previous statement period, interest is charged on the total balance – rather than the unpaid balance – up to the date that the repayment for that statement period was made; in other words, interest-free days are lost for all purchases in that period, and not just those that were unpaid by the due date."*[71]

To address this, the Treasury is proposing that interest is only able to be charged by credit card issuers, from the end of the statement period, on the amount outstanding at the end of that date. (This change will not, of course, directly impact customers who pay off their credit card balances in full each month.) I am advised that this is consistent with the US Truth in Lending Act (Regulation Z)[72]. This is a requirement of Phase 1 of the Treasury proposed reforms and has the Government's support.

10.7.2. Discussion

The following examples set out the three possible ways in which interest is charged on a credit card balance where part payment is made, as Treasury observes, the most common being Method A.

Figure 11. – Method A – Waiver fully withdrawn (Interest charged on full account balance where full payment is not made)

Interest at 20%		Amount	Balance
1 Oct	Purchase A	-1,000.00	-1,000.00
15 Oct	Purchase B	-2,000.00	-3,000.00
1 Nov	Statement issued with interest waived		-3,000.00
20 Nov	Part payment on due date	2,000.00	-1,000.00
1 Dec	Statement issued charging interest that accrued for both October purchases at 20% cumulative for period up to 1 Dec)	-86.13	-1,086.13

Figure 12. – Method B – Waiver partly withdrawn (Interest charged on unpaid portion of the account balance where full payment is not made)

Interest at 20%		Amount	Balance
1 Oct	Purchase A	-1,000.00	-1,000.00
15 Oct	Purchase B	-2,000.00	-3,000.00

[71] The Treasury Consultation Paper, *Credit cards: improving consumer outcomes and enhancing competition*, May 2016, p.9

[72] The Treasury Consultation Paper, *Credit cards: improving consumer outcomes and enhancing competition*, May 2016, p.18

1 Nov	Statement issued with interest waived		-3,000.00
20 Nov	Part payment on due date	2,000.00	-1,000.00
1 Dec	Statement issued charging interest on $1,000 at 20% cumulative for 47 days from 15 Oct to 1 Dec)	-26.08	-1,026.08

Figure 13. – Method C – Waiver honoured (No reinstatement of interest for previous period where full payment is not made)

Interest at 20%		Amount	Balance
1 Oct	Purchase A	-1,000.00	-1,000.00
15 Oct	Purchase B	-2,000.00	-3,000.00
1 Nov	Statement issued with interest waived		-3,000.00
20 Nov	Part payment on due date	2,000.00	-1,000.00
1 Dec	Statement issued charging interest on $1,000 at 20% cumulative for 30 days from 1 Nov to 1 Dec)	-16.57	-1,016.57

Of course, interest charges are imposed for two reasons: first, to compensate the banks for the financing costs of funding the customer's purchases (with merchant fees also contributing to this cost) and secondly, to mitigate the credit default risk cost. Given the unsecured nature of credit card lending, the credit default risk cost might be regarded as the more significant cost for banks. This is what is said to justify charging on the basis set out in Method A.

Whilst I understand the imperative for signatory banks to manage their credit default risk and that an incentive to pay on time (the conditional waiver of the customer's accrued interest) is an important way of doing this, the methods of charging interest set out in Methods A and B have an appearance of backdating that cannot help but attract arguments of unfairness. In the court of public opinion, Method A is particularly exposed to criticism for failing to honour the waiver on the portion of the account balance that is paid on time and for failing to distinguish between a customer who pays virtually all of the balance outstanding (imagine $2,999.00 out of a balance of $3,000) and a customer who pays only the specified minimum amount (say $60.00 out of a balance of $3,000).

In my view, few customers would be aware that this was happening at all, let alone understand the reasoning behind it. In my view, there are issues of substantive fairness (the application of interest charges) and of perceived fairness (is the approach easily understood and intuitively fair to the customer) be dealt with.

Method A is in my view unacceptable and must be prohibited. It is substantively unfair in applying interest and (if understood) would be perceived by customers as just plain 'tricky'.

Method B I see as substantively fair in its application of interest (only the unpaid portion attracts the full interest rate). However as noted above, for many customers who may not understand how the concept of a conditional waiver is being applied, it will still appear to be retrospectively removing a promised interest-free period. It seems to me that this Method will require a companion education piece.

Method C is, I think, substantively unfair to the bank as the customer is able to claim the interest-free period without making the repayment that justifies the waiver. However, it unlikely to upset the customers' perception of fairness (the banks are held to the interest charges as quoted on the previous month's statement).

My conclusion is that the Code should prohibit charging under Method A. Charging in accordance with Method B should be assumed. This seems to me to be the fairest treatment of the interest for both parties. (I note that consumer representatives have not proposed that Method C be mandated, however it would be open to a bank to choose to do so.)

The problem that remains under Method B is that many customers will not understand the concept of a 'conditional waiver' – and may well continue to see this approach as unfair or dishonest. Credit card account statements should be required to specify the amount of the interest charges that are being waived, explain that the waiver is conditional upon payment on time and that interest charges will be added to future statements for any portion of the monthly balance unpaid at the due date. For interested customers at least, this would help address the current lack of understanding referred to in the Treasury paper.

Recommendation 23

The Code should be amended to include:

a) a prohibition on signatory banks charging Code customers interest on the portion of their credit card balance that is paid off by the due date; and

b) an obligation on signatory banks to specify on a statement the amount of the interest charges that are being conditionally waived, explain that the waiver only applies if the payment is made on time and that interest charges will be reinstated and added to future statements for any portion of the monthly balance not paid on time.

10.8. Pre- July 2012 credit card contracts

Since 1 July 2012, credit providers have been required by law to apply credit card payments against amounts to which the highest interest rate applies (cash advances) before reducing the amount outstanding where a lower interest rate applies (credit card purchases)[73]. But this reform only applied to credit card contracts entered into from 1 July 2012[74].

[73] National Consumer Credit Protection Act 2009 Part 3-2B Division 6

[74] National Consumer Credit Protection Amendment (Hone Loans and Credit Cards) Act 2011 Schedule 1 sub item 2(2)

Whereas some banks have gone 'beyond the law' and treat pre-1 July 2012 credit cards similarly, other banks have not done this. It was put to me that the Code should mandate this requirement for all credit cards issued by signatory banks, regardless of when the credit contract originated.

10.8.1. Discussion

The legislative payment application rules for post-1 July 2012 credit cards were motivated by fairness considerations. I think that it is confusing and somewhat unfair for Code customers to have different payment application rules for credit cards first issued before 1 July 2012. This is another area of banking practice where few consumers would understand how it actually works – and that it works against their interests. I am also conscious that this practice will not quickly disappear, given that customer loyalty (or inertia) means that large numbers of pre-1 July 2012 credit card contracts are likely to continue in existence. Note that replacement cards (issued after date expiry) remain part of the original contract.

Using the Code to voluntarily remove poorly understood practices that disadvantage customers is exactly the kind of change that will build trust for signatory banks. In my view, it would be consistent with the spirt of the Code to give the current law a broader application and apply them to pre-1 July 2012 credit cards. While there may be an interest revenue impact for banks, the systems to support the current law and all cards issued since mid-2012 are already in place.

Recommendation 24

The Code should be amended to include a new obligation that signatory banks apply Code customer credit card payments so that higher interest debts are discharged first – applying to all cards.

10.9. Introductory offers

10.9.1. Introduction

The Treasury Consultation Paper, *Credit cards: improving consumer outcomes and enhancing competition*, May 2016 refers to the increase in popularity of zero or low-interest introductory balance transfer offers.

> *"[These] may compound the problem of over-borrowing and under-repaying. By pushing the possibility of incurring interest into the future, some consumers may use such offers to extend their indebtedness or avoid repaying debt. Consumers are likely to pay less attention to interest costs that may occur a year or more in the future"*[75].

[75] The Treasury Consultation Paper, *Credit cards: improving consumer outcomes and enhancing competition*, May 2016, p.15

Citing information provided by Australian banks, the Treasury Paper indicates that between 30% to 60% of consumers do not pay off their transferred balance in full by the end of the introductory period[76].

To address this, Treasury is proposing that credit card issuers provide consumers with timely electronic notifications regarding the expiry of the introductory period. This is a Phase 2 recommendation and so is to be the subject of consumer testing. Treasury representatives have, however, indicated to me that they think it would be appropriate for the Code to address this issue.

The Joint Consumer Submission would like the Code to ban introductory balance transfer offers. Failing that, the Submission proposes that introductory offer periods should not be less than 12 months, that the new bank should require the consumer to close the previous account and that the new bank should provide regular disclosure of the monthly payment required to pay off the transferred balance and timely electronic notification of the expiry of the introductory offer period[77].

10.9.2. Discussion

I do not think that the Code should prohibit signatory banks from offering a credit card balance transfer with low or no interest applying for an introductory period, or for the Code to discourage these offers by stipulating a minimum period during which the favourable interest charges apply. While I understand that this is a marketing/sales technique aimed at attracting those card customers who are most profitable to the bank (customers who have a history of carrying credit card debt for longer periods of time), these offers can also be highly advantageous for Code customers, including some who are trying to fight their way out of debt. This goes to my Code Design Approach of maintaining choice for consumers where possible.

I accept the concern however, that with the passage of time Code customers may lose track of when their introductory period expires. It would clearly assist customers if the signatory bank provides a reminder of the expiry date. In my discussions with signatory banks, I found general agreement that a notification obligation would enhance the service signatory banks provide their customers. It seems to me that an electronic notification – SMS or email – would generally be appropriate. I see no need for the Code to mandate the communication channel: signatory banks should be able to determine what is likely to be the most effective communication channel to use. One signatory bank suggested that the notification should be provided 30 days prior to expiry. I agree that this timeframe is contemporaneous enough with the expiry date to be meaningful, whilst giving the customer reasonable time to arrange alternative finance should this be required.

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[76] The Treasury Consultation Paper, *Credit cards: improving consumer outcomes and enhancing competition*, May 2016, p.15

[77] Rec 26

I am not persuaded that the Code should impose additional prescription and require regular notifications by signatory banks to their customer during the introductory offer period. It is not clear to me from the research that regular disclosure to consumers of the type proposed in the Joint Consumer Submission would be effective, given strongly ingrained behavioural biases that can impede sound financial decision making[78].

While I understand the objective, I was also not persuaded by the Joint Consumer Submission proposal that a signatory bank should require a customer to close their previous credit card if transferring the balance from a credit card issued by another provider. The pre-existing contract is one between the customer and the 'previous' card provider and it is difficult to see how a signatory bank (the 'second' provider) could enforce any advice to customers to close the previous credit card.

In some cases, I imagine that it may also be in the best interests of the customer to maintain the 'previous' card. The balance transfer offer may be capped and may not clear the 'previous' balance. The customer may have a financially sound reason to increase their credit card limit in aggregate rather than on just one card. It may also be in the best interests of a customer to maintain the previous card in order to optimise the use of each card's features. Consistent with the discussion at Chapter 5, I am reluctant to limit customer choice here.

My recommendation is that the Code include a new provision requiring signatory banks to provide Code customers with notice at least 30 days prior to expiry of an introductory offer period. For the reasons discussed in earlier sections, I am proposing that this should apply where a credit card is issued to a small business, not just to credit cards issued to individuals.

Recommendation 25

The Code should be amended to include a new obligation that signatory banks provide their Code customers with notice (in the form preferred by the customer) at least 30 days prior to expiry of an introductory offer period during which no or low interest accrues on all or a portion of the account balance.

10.10. Card cancellation or reduction of credit limit

The Treasury Consultation Paper, *Credit cards: improving consumer outcomes and enhancing competition*, May 2016 refers to the lack of online options to cancel a credit card or reduce a credit limit on a credit card, necessitating a process that "[c]onsumer feedback indicates …can be unnecessarily onerous"[79].

[78] A literature review undertaken by ASIC in September 2015 discusses the impact of optimism, present bias and inertia bias.

[79] The Treasury Consultation Paper, *Credit cards: improving consumer outcomes and enhancing competition*, May 2016, p.19

"Consumers wishing to cancel an existing card are generally required to do so by visiting a bank branch or by calling a consumer service representative. During this process they may be encouraged to keep their card open, sometimes through attractive offers. A potential outcome is that consumers seeking to switch may keep their old card active when obtaining a new card, resulting in an increase in their total available credit (which may induce higher spending than otherwise)."[80]

To address this, the Treasury is proposing to require card issuers to provide consumers with the option to cancel their credit card, or reduce their credit limit, via simple electronic means. Again this is a Phase 1 requirement and so has the Government's support.

Similarly the Joint Consumer Submission proposed that the Code should commit banks to providing simple options for customers to cancel credit cards including online, by e-mail and in writing (in addition to in person or by telephone)[81].

10.10.1. Current online functionality

Discussions with the signatory banks confirmed that online functionality to request a change to the credit card limit is not necessarily accompanied by online functionality to cancel a credit card. Technological developments are, of course, costly and have competitive ramifications. Nevertheless, banks are rapidly and actively expanding their technological support for products and services electronic and I found general agreement from the signatory banks that customers should also have an easily accessible electronic means to cancel or reduce the credit limit of a credit card.

Recommendation 26

The Code should be amended to include a new obligation that wherever there is functionality (electronic or otherwise) for a customer to alter a credit card limit, this must (equally and as prominently) include the ability to reduce the credit limit or to cancel a Code customer's credit card.

10.10.2. Information to be provided by bank

The Joint Consumer Submission noted that banks reserve the right to cancel a credit card at any time. The Submission proposed that if the bank decides to cancel the customer's card, the bank should:

- notify their customer in writing;
- explain the reasons for the cancellation;

[80] The Treasury Consultation Paper, *Credit cards: improving consumer outcomes and enhancing competition*, May 2016, p.9

[81] Joint Consumer Submission Rec 23a.

- provide a list of active recurring payment arrangements and instructions detailing how to cancel these, so that the customer can make alternative arrangements; and
- provide contact details should the customer wish to complain[82].

If the customer exercises the right to cancel a card, the bank should similarly be required to give the customer a list of currently active recurring payment arrangements and instructions about how to cancel these.

My understanding is that signatory banks notify Code customers in writing if the bank exercises its right to cancel the customer's credit card. Terms and conditions do not, however, typically require reasons to be given – and it seems to me that it would be respectful to the customer to provide an explanation where possible. I accept that there will be situations where reasons will not be able to be given (for example, where the customer is suspected of engaging in money laundering and banks have a legislative obligation not to 'tip off' a customer about suspicions of this kind).

Currently, banks do not have sufficient visibility of recurring credit card payment arrangements to be able to provide customers with a listing of these. I appreciate that it would be useful for customers if signatory banks could produce this information. In Chapter 15.2, I discuss this issue.

It would also be appropriate for the bank to provide information about how the customer may make a complaint if they so wish. This would be consistent with my proposed Principle 8 that emphasises openness to customer expressions of dissatisfaction. The Code should include new obligations to entrench these practices.

Recommendation 27

The Code should be amended to include a new obligation that requires a signatory bank to notify a Code customer in writing if the bank exercises its right to cancel the customer's credit card. The notification should, where possible, include an explanation of the reasons for the cancellation and provide contact details should the customer wish to complain.

[82] Joint Consumer Submission Rec 23b.

10.11. Other issues

10.11.1. Introduction

The Treasury Consultation Paper, *Credit cards: improving consumer outcomes and enhancing competition*, May 2016, and submissions to the Code Review by consumer representative organisations canvas a range of other possible reforms in relation to credit card lending. For example, the Joint Consumer Submission proposes that the Code should prescribe a minimum monthly repayment formula that would require higher customer repayments than signatory banks currently stipulate (typically about 2.5% of the total balance outstanding is all that is currently required to be repaid). Other proposals are that signatory banks should provide additional disclosure to their customer about credit card costs and the availability of alternative products.

10.11.2. Discussion

In assessing these proposals, I have taken into account recent reform initiatives in the United Kingdom and America. I have also been assisted by an ASIC literature survey (September 2015) analysing the results of research into the effectiveness of regulatory measures that aim to assist consumers with credit card debt management. The literature survey casts doubts on the effectiveness of minimum payment requirements and information disclosure in overcoming deeply engrained behavioural biases that profoundly affect some consumers' credit card spending and repayment practices.

My conclusion is that currently the evidence base is not sufficiently strong to support other proposed reforms. Of course, this may change once Treasury behavioural testing results are available. Treasury has encouraged industry to work with it to improve credit card outcomes for Code customers, which I understand is being supported by signatory banks.

11. CREDIT CONTRACTS AND BORROWER DEFAULT

This Chapter addresses issues pertaining to credit contracts that were raised in Parliamentary Inquiries in the context of loans to small business, but that apply equally to customers who are individuals. It also addresses other credit contract-related issues that were raised in submissions to my Review.

So far as small business borrowers are concerned, consistent with Chapter 8.3, this Chapter's recommendations only apply to a credit facility that is below $5 million.

11.1. Credit contract events of default

The Parliamentary Joint Committee *Impairment of Customer Loans Report*, May 2016, expressed concern that non-monetary default clauses in small business loan contracts can be unfair[83]. These clauses give the bank the power to demand repayment of the loan, even where the customer has met all payment obligations. Because of the asymmetry in power, small business customers are not in a position to negotiate these. The Committee recommended that the Code explicitly include protections relating to non-monetary defaults and that the Australian Small Business and Family Enterprise Ombudsman lead and coordinate reform in this area[84]. Consistent with this, the Ombudsman's Report recommends:

> *"For all loans below $5 million, where a small business has complied with loan payment requirements and has acted lawfully, the bank must not default a loan for any reason. Any conditions must be removed where banks can unilaterally:*
>
> - *value existing security assets during the life of the loan*
> - *invoke financial covenants or catch-all 'material adverse change' clauses"*[85].

11.1.1. Discussion

To explore this issue, I sought data from industry to ascertain the extent to which small business loans are placed in default because of breach of a loan to valuation ratio. Indicative data only was available. This suggested that, at least in current economic conditions, there are almost no loans where default is triggered solely by a breach of a loan to valuation ratio.

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[83] *Impairment of Customer Loans Report*, p. 20

[84] Recommendation 2c. and 4

[85] Australian Small Business and Family Enterprise Ombudsman, *Small Business Loans Inquiry Report*, 12 December 2016, Rec 3

Further, one bank stated in its evidence to the Joint Parliamentary Committee that it does not use non-monetary default clauses of any type to enforce repayment of small business loan. Nevertheless, the bank asserted that non-monetary default clauses were useful, "*serv[ing] as an 'early warning sign' that a customer may be experiencing difficulty meeting their obligations, or that they may do so in the near future*"[86].

I accept that there is a place in credit contracts for triggers of heightened borrower risk, such as loan to valuation ratios and material adverse change clauses. A breach of these clauses may justify consequences such as additional reporting or a higher interest rate. But I think that the community legitimately expects that a signatory bank will not rely upon these types of clauses to enforce a credit facility against a Code customer (whether an individual or a small business customer) if the customer is meeting their payment obligations.

I also accept that, even where the customer is meeting their payment obligations, there will be some limited circumstances in which enforcement of the loan should be permitted, such as an insolvency event or the customer having obtained the credit through fraudulent means or otherwise acting unlawfully. Again the drafting stage provides an opportunity for detailed consideration of this, but on the basis that there should be as few caveats or qualifiers as possible. The Australian Small Business and Family Enterprise Ombudsman should be consulted during this process.

Recommendation 28

The Code should be amended to prohibit a signatory bank from enforcing a credit facility against:

a) a customer who is an individual; or

b) a small business customer where the credit facility is below $5 million,

if the customer has complied with loan payment requirements and has acted lawfully.

The ABA should consult with stakeholders including the Australian Small Business and Family Enterprise Ombudsman about any exceptions, for example, to permit enforcement of a small business credit facility where an insolvency event has occurred.

[86] *Impairment of Customer Loans Report*, p. 19

11.2. Valuations and investigating accountant's reports

The Joint Parliamentary Committee's *Impaired Customer Loans Report* dwelt upon loan security revaluation practices. The Report referred to small business borrowers not having a chance to view and challenge the appropriateness of the valuation. To address this, the Report recommended that, where a bank obtains a revaluation of a small business customer's security, the bank should provide the customer with its instructions to the valuer and the valuation[87]. (The Committee also made recommendations aimed at valuer practices that are outside the scope of my Review of the Code.) Similarly, where a bank engages an investigating accountant to examine and report on a small business borrower's financial situation, the Committee thought this should occur in a transparent manner[88].

The Australian Small Business and Family Enterprise Ombudsman in her small business loans report recommends:

> *"All banks must provide borrowers with a choice of valuer, a full copy of the instructions given to the valuer and a full copy of the valuation report."*[89]
>
> *"Every borrower must receive an identical copy of the instructions given to the investigating accountant by the bank and the final report provided by the investigative accountant to the bank."*[90]

11.2.1. Discussion

I support Code customers' involvement in the choice of expert where the customer is expected to pay for the expert's report. For example, the signatory bank could provide the customer with a choice of two or three experts that the bank considers has the requisite expertise.

I also support a transparency regime whereby the Code customer is provided with both the signatory bank's instructions to the expert and the expert's report in response to those instructions. In my consultations with signatory banks, they indicated support for this where the customer bears the cost of obtaining the bank's expert advice and where the customer is not in default.

However, I consider that the principle of transparency should not be limited to these situations. A transparent process is important to provide the customer with opportunity to challenge any mistakes or faulty assumptions that underpin the valuation or assessment. At the very least, it enables the customer to have a better understanding of the signatory bank's position where, for example, the bank asserts that the customer's security is insufficient or the business is not viable.

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[87] Rec 2c. and 5di.

[88] Rec 5d.ii

[89] Australian Small Business and Family Enterprise Ombudsman, *Small Business Loans Inquiry Report*, 12 December 2016, Rec 8

[90] Australian Small Business and Family Enterprise Ombudsman, *Small Business Loans Inquiry Report*, 12 December 2016, Rec 9

Some signatory banks have expressed concern that transparency is only possible where the expert consents to the report being made available to the customer. Granted that the expert's consent is required, but the bank is in a position to require the expert to give their consent as a condition of engaging the expert – and should do so.

Transparency should not, however, be required where the bank undertakes internal analysis by bank staff. As I understand, internal analysis does not trigger consequences under a credit facility in the way that may be the case for an external opinion and so is much less critical for the customer.

Lastly, there is the issue of how the Code should entrench a fairer, more transparent approach by signatory banks engaging valuers and investigating accountants. Consistent with my Code design approach described in Chapter 6.4, I think that the Code should operate at a principles-level and require signatory banks' processes for managing expert valuations and investigating accountants' opinions to be fair and transparent. This should be supported by an Industry Guideline that traverses in more detail the various matters I have discussed above. As discussed at Chapter 6.5, the Guideline should be developed in close consultation with interested stakeholders.

Recommendation 29

a) The Code should be amended to require signatory banks processes in relation to expert valuations and investigating accountants' reports to be fair and transparent. In the case of small business, this obligation should apply to a credit facility below $5 million.

b) Signatory banks should develop an Industry Guideline that sets out in some detail fairness and transparency issues. Interested stakeholders including the Australian Small Business and Family Enterprise Ombudsman should be closely involved in the development of the Guideline.

11.3. Late payment credit reporting

Since March 2014, it has been possible for banks to tell credit reporting bodies, such as Veda, if an individual customer makes a payment that is more than 14 days late (adverse repayment history information)[91]. This information can then be included by the credit reporting body in the individual's credit report, so that other credit providers can take this information into account when considering whether to provide credit to that individual.

The Privacy Act 1988 requires credit providers to notify their customers that information about them may be provided to credit reporting bodies. But customers do not have to be told each time adverse repayment history information is provided about them to a credit reporting body.

[91] Privacy (Credit Reporting) Code 2014 para 8.1

The Joint Consumer Submission proposes that signatory banks should disclose on customers' regular statements any reporting of adverse repayment history information[92]. The banking industry position is that there would be systems impediments. Moreover if this is to be required, this is more properly for the Privacy Act 1988 and the Privacy (Credit Reporting) Code and should apply to all credit providers not just to signatory banks.

11.3.1. Discussion

I think that there would be advantages both to signatory banks and to individual customers if signatory banks were transparent about their reporting of adverse repayment history information. For banks, this would assist them to educate their customers about the credit reporting process and would encourage on-time repayment. For customers, timely notification would provide them with an opportunity to change their behaviour and thereby protect their credit rating.

I have thought about whether this reform should be part of the new Code or whether instead it should be picked up as part of the review of the Privacy (Credit Reporting) Code, due to occur this year. I am attracted to signatory banks leading by example on this issue. After all, banks are key generators of late repayment history information and are well positioned to make timely disclosure to their customers via customers' regular bank statements.

I recommend a new obligation in the Code, although I accept that this should be at a principles-level. This is an increasingly important issue for individual customers and consumer advocates. As customer awareness of credit reporting improves, this will increase pressure on banks to explain and justify the benefits of credit reporting and to be transparent about their reporting processes. Given the complexities of the industry's construction of reporting of repayment history information and the use of numeric codes to indicate how late a repayment is, an Industry Guideline would assist to ensure that consistent and comprehensible information is provided to individual customers by signatory banks.

As for a number of other recommendations that I am making, it will clearly be necessary for signatory banks to have time to make system changes before the new Code obligation comes into effect.

Recommendation 30

a) The Code should be amended to require signatory banks to disclose in individual customers' bank statements if the bank reported adverse repayment history information to a credit reporting body in connection with the customer's account during the period of the statement.

b) The ABA and signatory banks should develop an Industry Guideline to assist banks to provide disclosure in a way that is consistent and comprehensible for customers. Proposed wording should be consumer tested.

[92] Joint Consumer Submission Rec 18

11.4. Garnishing practices

The Department of Human Services has a Code of Operation (the DHS Code) that applies to the recovery of debts that arise from customers' overdrawn accounts where no repayment arrangement already exists. The DHS Code states.

> *"The aim of this Code is to ensure that recipients of income support payments and DVA [Department of Veteran Affairs] payments have sufficient income to maintain adequate food and shelter."*[93]

The DHS Code establishes a default position that a customer should be able to retain at least 90% of their Australian Government payments in any fortnightly period.

The DHS Code is voluntary but has been endorsed by the ABA on behalf of its member banks. Consistent with this, the ABA's website states that banks are bound to comply with the DHS Code[94]. Currently the Code only addresses one aspect of the DHS Code - account combination[95].

In its submission to my Review, the CCMC stated that it has been made aware of removal of funds by signatory banks from Centrelink customer accounts via garnishee orders (an order by a court enabling a creditor to receive automatic payments from a debtor's bank account) that do not comply with the DHS Code. On that basis, the CCMC proposed that the Code should explicitly oblige signatory banks to comply with the DHS Code.

11.4.1. Discussion

I think that the Code commitment that signatory banks will comply with the DHS Code should be broadened and not just to limited to account combination. This would I think place signatory banks in a more secure position to resist a garnishee order that would offend the DHS Code. I agree with the CCMC proposal and note that this would bring the Code up to the standard of the Customer Owned Banking Code of Practice which provides:

> *"26.5. We will comply with any applicable requirements of the Code of Operation: Recovery of Debts from Department of Human Services Income Support Payments or Department of Veterans' Affairs Payments (both when enforcing indebtedness owed to us and, to the extent the law permits, when facilitating enforcement by a third party judgment creditor).*

[93] https://www.humanservices.gov.au/corporate/publications-and-resources/code-operation

[94] http://www.bankers.asn.au/Consumers/Industry-Standards

[95] Code clause 19.1

Recommendation 31

The Code should be amended to include an obligation on signatory banks to comply with the Department of Human Services' Code of Operation – and to make this clear to customers and creditors.

11.5. Debt collection and assignments of debts

11.5.1. Introduction

Clause 32 of the Code already includes substantial protections in relation to debt collection and assignments of debt:

- It commits signatory banks and their collection agents to complying with ASIC's Debt Collection Guidelines[96].
- Signatory banks are only able to sell a debt to a buyer that agrees to comply with ASIC's Debt Collection Guidelines.
- Signatory banks are not able to assign a debt while actively considering either financial difficulty assistance under the Code or a hardship variation under the National Credit Code.

The Joint Consumer Submission makes a number of proposals to strengthen consumer protections in this area.

11.5.2. Notice of assignment

The Joint Consumer Submission proposed that the Code should require a signatory bank that is assigning a debt to notify the customer of the name of the debt buyer, their contact details and the amount currently outstanding[97]. The aim is to ensure that a Code customer, who receives a payment demand from a debt buyer, understands that their debt is now owed to the debt buyer.

[96] Regulatory Guide 96

[97] Joint Consumer Submission Rec 17c.

I agree that it would be confusing for a Code customer to receive a payment demand from a debt buyer without having been notified of the assignment of the debt. As I understand, current practice is that signatory banks prepare a notice of assignment – but some bank divisions allow this to be sent to the customer on the letterhead of the debt buyer where this is permitted under State legislation[98]. I agree that this can be confusing for the customer who may receive contact from a firm they have never heard of.

Better practice would be for the notice of assignment to be on the letterhead of the assigning signatory bank. (This does not require the bank itself to actually send the notice, rather it requires the notice to bear the bank's letterhead.) This would not apply where the bank transfers the liability off its books, for example as part of a securitisation program, but continues to be responsible for customer contact.

Recommendation 32

The Code should be amended to include an obligation on a signatory bank, where a Code customer's debt has been assigned and the bank will not be the future contact with the customer about their debt, to arrange for a written notice advising of the change to be sent to the customer on the bank's letterhead. The notice should set out details of the debt including the amount currently owing and the name and contact details of the purchaser of the debt.

11.5.3. Debt assignment contracts

The Joint Consumer Submission also proposes that signatory banks should place additional parameters around debt buyers' debt recovery practices[99]. As noted earlier, the Code already restricts banks from selling a debt to a buyer that has not agreed to comply with ASIC's Debt Collection Guidelines. This is a valuable protection for Code customers because, as the Guidelines expressly acknowledge, the Guidelines do not otherwise have legal force[100].

However, this does not address all issues with debt buyer conduct. I recognise that some debt buyers operate very responsibly and take advantage of the opportunity afforded by purchasing debts at a discount to face value to reach an accommodation with the debtor on mutually satisfactory terms. I received a detailed submission from Credit Corp Group Limited outlining how this can work to a consumer's advantage.

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[98] ASIC Regulatory Guide 96 para 11(m) notes that some (but not all) state-based property legislation prescribes that the assignor must give express notice of the assignment to a debtor in writing.

[99] Joint Consumer Submission Rec 17d. and e.

[100] Regulatory Guide p.3

However, I am aware that not all debt buyers behave in the same way and some are quick to institute legal action. Of course, for signatory banks, the risk is that their reputation will be tarnished if a debt buyer that the bank partners with is unwilling to spend any time negotiating with debtors. Code customers are unlikely to distinguish between the signatory bank and the debt buyer – and any attempt by the signatory bank to distance themselves from the conduct of the debt buyer risks being perceived as ''tricky'.

I am aware that at least some signatory banks closely monitor their debt buyers' collections activity. I was provided with information about one bank's program which includes regular attestations by debt buyers, a review by the bank of debt buyers' complaint registers and quarterly reviews of 5 randomly selected accounts (notes and call recordings) to assess compliance with legislation, ASIC's Debt Collection Guidelines, the Code and the bank's values. This seems a quality approach, consistent with the idea of respect for the customer.

Consistent with my recommended Code design approach in Chapter 6.4, I think that the Code should operate at a principles-level and require signatory banks to develop processes to monitor compliance by debt buyers with legislation, ASIC's Debt Collection Guidelines and the Code Principles. This could be supported by an Industry Guideline to assist in shaping a robust monitoring program and expectations as to reasonable debt buyer conduct. This Guideline should be scalable to allow for differing models and volumes of debt assignment.

Recommendation 33

a) The Code should be amended to require signatory banks to develop processes to monitor compliance by their debt assignees with legislation, ASIC's Debt Collection Guidelines and the Code Principles.

b) The ABA and signatory banks should develop a scalable Industry Guideline to shape expectations as to reasonable conduct by debt assignees and a robust monitoring program for them.

11.6. Other issues

Whilst I have not attempted in this Report to respond to every proposal for Code reform that was made in submissions to my Review, I did want to address a couple of credit contract-related proposals that were put to me. First, the proposal that where a signatory bank unilaterally varies the credit contract of an individual customer, the Code should oblige the bank to provide a lengthier notice period than that provided for under the National Credit Code[101]. Secondly, that where a signatory bank decides not to rollover a loan upon the expiry of its term, that the individual customer should be provided with a lengthy notice period if the customer was not in default under the expired loan[102].

[101] Joint Consumer Submission Rec 14b.

[102] Joint Consumer Submission Rec 14a.

Submissions referenced the Parliamentary Joint Committee *Impairment of Customer Loans Report,* May 2016. That report's focus was small business and commercial loans and the Committee heard evidence about situations in which inadequate notification adversely affected farmers and businesses. The Committee was cognisant that small business and commercial loan refinancing can take a longer period of time than refinancing of household loans. I agree with the concerns expressed by the Joint Parliamentary Committee and have made recommendations in Chapters 8.6 and 8.7 about notice periods for small business.

I did not receive evidence of any specific harm that is currently occurring due to banks' end of loan practices or loan contract variation notification periods for consumers. The argument that individual customers should be provided with parity with small business in relation to these issues, I did not find sufficiently persuasive. It seems to me that small business re-financing is intrinsically more complex and generally riskier and requires more time than consumer credit re-financing, which is the justification for the special notification protections. I do note that some banks may find it procedurally simpler to apply the same provisions across all Code customers.

12. JOINT ACCOUNT HOLDERS

Whilst joint accounts are convenient and work well for many Code customers, they can raise difficult issues. There can be misuse of the account by one joint account holder to the detriment of the other account holder. This is particularly the case where the relationship between the joint account holders breaks down.

The ABA Industry Guideline *Financial abuse and family and domestic violence policies*, November 2016 states at page 5:

> *"Significant issues can arise when joint accounts and joint liabilities are involved as these finances can be used as another avenue to intimidate or control individuals."*

Clause 29 (Joint debtors) and clause 30 (Joint accounts and subsidiary cards) of the Code provide some protections for account holders. Consumer representatives state that they are nevertheless continuing to see situations of joint account abuse and so they submit that additional protections are needed.

This Chapter considers the key issues raised in relationship to joint accounts. Reference should also be made to Chapter 8.8 in relation to co-debtor financial difficulty assistance.

12.1. Co-debtor benefit

Clause 29.1 of the Code provides:

> *"We will not accept you as a co-debtor under a credit facility where it is clear, on the facts known to us, that you will not receive a benefit under the facility."*

The Joint Consumer Submission was concerned about co-debtor arrangements where very minimal benefit is received by one of the co-debtors. The Submission proposed a tightening of the co-debtor benefit test to ensure that the Code's guarantee protections are not circumvented by the signatory bank signing up a guarantor as a co-debtor[103]. Legal Aid NSW's submission expressed particular concern about a co-debtor arrangement to finance an asset acquired in the name of one only of the co-debtors. The submission recommended that the Code is amended to require "demonstration" that a co-debtor will receive a "substantial benefit" under the credit facility[104].

[103] Joint Consumer Submission Rec 30

[104] Legal Aid NSW Submission Rec 20

12.1.1. Discussion

In the typical situation of a joint and several credit facility, each co-debtor is liable to repay the entire amount of the facility. Yet a co-debtor does not have the benefit of the protections the Code provides to guarantors (information requirements, procedures that must be followed when the guarantee is signed, enforcement-related protections, etc.). This is because the co-debtor is assumed to share in the benefits of the credit. On the other hand, there is a recognition that a guarantor might not derive much benefit from the guaranteed facility and may be motivated solely by, for example, familial considerations, and so warrant greater protections.

This schema breaks down where a co-debtor's interest in a credit facility is limited to that which typically motivates a person to become a guarantor – in other words where the person takes on co-debtor obligations when their own interests would be best served by being a guarantor. This could occur where the primary debtor does not have sufficient income to support a responsible lending 'not unsuitable' assessment as required under the NCCP Act in order for the bank to be able to lend. I was told by signatory banks that parents are often very willing to be signed as a co-debtor in order to assist their sons or daughters to buy a home.

It seems to me, however, that it would not be appropriate for a signatory bank to effectively remove a third party's guarantor protections in order to side-step responsible lending requirements. To do so opens the door to abuse situations of the kind described in the Joint Consumer Submission. It seems to me that if family members have the financial capacity to assist, then there are other ways to do so – without placing themselves in the high-risk position of a co-debtor.

I recommend that the Code is amended to require a co-debtor to derive a "substantial benefit" from the credit facility. A substantial benefit would be more than just a familial interest in supporting the acquisition of the asset. In the case of a residential property loan, it would be more than just residing at the financed property in the capacity of family member (given that many family members live together rent-free[105]). As stated by FOS in *FOS Approach to 2013 Code of Banking Practice* para 2.6:

> *"We consider that to be treated as a co-debtor, a person must receive a substantial benefit from the loan, for example owning a fair share of a property that has been purchased with the loan. We consider that just being able to live in or use a property that has been purchased with the loan funds is not a sufficient benefit on its own to indicate that a consumer should be treated as a co-debtor. If a consumer is not receiving a benefit from the loan funds, then they may be asked to provide a guarantee for the debtor who would receive a benefit."*

[105] http://www.smh.com.au/money/planning/boomers-go-bust-over-kids-20110910-1k2rs.html

I think that the Code should also be amended to place some obligation on signatory banks to make enquiries as to whether a co-debtor is receiving a substantial benefit from the credit facility. It would be appropriate for a signatory bank to make enquiries where, for example, the co-debtor is not on the title of an asset being financed. In my view, clause 29.1 could serve to discourage the signatory bank from enquiring whether a co-debtor benefits from a credit facility. This is because the clause 29.1 restriction applies "where it is clear, on the facts known to us [the signatory bank]" that the co-debtor does not receive a benefit. The result of this formulation is that if the signatory bank makes no enquiry, it will not be in possession of knowledge that may prevent the bank from signing the person as a co-debtor.

Recommendation 34

Clause 29 of the Code should be redrafted to require a co-debtor to receive a "substantial benefit" under the credit facility and a signatory bank to make reasonable enquiries to ensure that this is the case (thereby reversing the position currently achieved by the words "it is clear, on the facts known to us"). In the case of a credit facility for the purpose of a small business, the clause 29 obligation should only apply to a credit facility below $5 million.

I think that clause 29 should also specify the consequences that flow where a signatory bank accepts as a co-debtor a person who does not have a substantial interest in the credit facility. I set out in Chapter 13.6 my view that, where a signatory bank fails to comply with pre-execution guarantee requirements, the guarantee should be unenforceable.

Similarly, I think that the Code should make it clear that a credit facility is unenforceable against a co-debtor where the signatory bank should have known that the co-debtor was not receiving a substantial benefit under the credit facility. This recognises the harm that can result from mischaracterising as a co-debtor and would be consistent with the strong wording currently used in clause 29.1 of the Code "we will not accept you as a co-debtor under a credit facility where…".

Recommendation 35

Clause 29 of the Code should specify that a credit facility is unenforceable against a person who is accepted as a co-debtor but who, the signatory bank should have known, was not receiving a substantial benefit under the credit facility. In the case of a credit facility for the purpose of a small business, the clause 29 obligation should only apply to a credit facility below $5 million.

12.2. Joint accounts

12.2.1. Introduction

Clause 30.1 of the Code obliges signatory banks to provide information to customers opening a joint account. General descriptive information must be provided by the signatory bank to the customers: about how funds may be withdrawn, how instructions can be varied and liability for debts incurred on the joint account.

The Joint Consumer Submission argued that issues arise in joint accounts that are not addressed by disclosure. The Submission gave the example of a joint account holder who became jointly liable for her ex-husband's overdraft withdrawal from the account which took place after the bank had refused her request to close the then-nil balance account (the account instruction enabled the account to be operated by the husband as sole signatory). Particular concern was expressed by consumer representatives about joint account abuse as part of situations of domestic violence.[106]

12.2.2. Discussion

The ABA's recently released Industry Guideline *Financial Abuse and Family and Domestic Violence*, November 2016 commits to working with customers to manage joint accounts.

> *"To manage joint accounts banks will:*
>
> - *Accept verbal instructions to amend the operating instruction to 'two to operate' or place a hold on the account in circumstances where one party is concerned about joint funds or credit. Note, the bank is required to notify the other account holder of a change in operating instruction.*
> - *Require the authorisation of both parties to subsequently amend the operating instructions to 'either to operate' or remove the hold.*
> - *Advise their customer to seek independent legal or financial advice in relation to the options available to them."*

I think that the Code should enshrine the first of these commitments so as to give maximum visibility to the options that this affords joint account holders. It would also assist if the Code provision made footnote reference to the ABA's Industry Guideline for readers who need further explanation. I understand that most signatory banks already have procedures that mirror the Guideline.

Recommendation 36

Clause 30 of the Code should include a new provision committing signatory banks to act upon instructions from a joint account holder either:

[106] Joint Consumer Submission Recs 32 and 33

- to amend the account operating instructions to "two to operate"; or
- to place a hold on the account.

A footnote to the provision should refer to the ABA Industry Guideline ***Financial Abuse and Family and Domestic Violence***, November 2016 for more explanation.

13. GUARANTORS

A large number of issues relating to guarantees were raised with me. This Chapter focuses on the issues where I consider that meaningful Code amendments are possible. This Chapter should be read together with Chapter 14.9 of this Report which discusses guarantor financial difficulty assistance.

13.1. Current protections

While assuming the responsibility of being a guarantor has no doubt been of great assistance to many borrowing customers, guarantors themselves can be in a position of particular vulnerability: their own financial security can be undermined by a transaction from which they might gain little or no benefit. The ABA Industry Guideline *Protecting vulnerable customers from potential financial abuse* recognises that pressure, for example, on a family member to become a guarantor can be a form of financial abuse[107].

To protect guarantors, the Courts have invoked their equitable jurisdiction[108]. The National Credit Code[109] also provides a range of significant protections for a guarantor of consumer credit (generally credit provided to an individual for personal, domestic or household purposes or in connection with a residential investment property). The amount secured by a guarantee cannot exceed the sum of the debtor's liabilities under the credit contract and reasonable enforcement expenses. The credit provider must provide a guarantor with warnings and information about the nature and risks of guarantee, including that the guarantor should get legal and financial advice. The credit provider must also provide the guarantor with a copy of the credit contract. There are process restrictions that apply to the enforcement of a guarantee.

For signatory banks, the guarantee-related obligations in clause 31 of the Code also apply. To a large extent, the requirements in clause 31 codify case law and overlap with National Credit Code requirements. The result is that, where the National Credit Code also applies, the Code's additional protections are relatively modest, with the key additional protections being additional information requirements and, for a guarantor who has not been legally advised, one day to consider the information.

For guarantors of a small business credit facility, clause 31 of the Code distinguishes between commercial asset financing guarantors, sole director guarantors and trustee guarantors on the one hand and other small business guarantors on the other hand as shown in Figure 14.

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[107] ABA Industry Guideline *Protecting vulnerable customers from potential financial abuse*, December 2014, p. 2

[108] For example, Garcia v National Australia Bank (1998) 194 CLR 395

[109] National Credit Code Part 3 Division 2 and sec 90

Figure 14. – Small business guarantor protections under Code clause 31

Code provision	Requirements	Applicability to commercial asset financing guarantors, sole director guarantors and trustee guarantors	Applicability to other small business guarantors
31.2	Guarantee must be limited to a specific amount plus associated liabilities or the value of specified security at time of recovery	Yes	Yes
31.3	Guarantee must include a statement that the relevant provisions of the Code apply to the Guarantee but need not set out those provisions.	Yes	Yes
31.4 (a)	Prominent notice to be given by signatory bank that you should get legal and financial advice, you can refuse to enter into the Guarantee, there are financial risks involved, there is a right to limit liability in accordance with the Code and as allowed by law and information can be requested about the transaction or facility to be guaranteed	Yes	Yes
31.4 (b) & (c)	Obligation on signatory bank to provide information about: • any notice of demand made on the debtor • any dishonour on any facility within previous 2 years • any excess or overdrawing of $100 or more on any facility by the debtor within previous 6 months • whether any existing debtor facility will be cancelled, or the facility to be guaranteed will not be provided, if the Guarantee is not provided	No	Yes
31.4 (d)	Obligation on signatory bank to provide following documents: • credit contract together with a list of any related security contracts (or copy if requested) • final letter of offer to the debtor and details of any conditions in an earlier version of that letter of offer that were satisfied before the final letter of offer was	No	Yes – but in the case of a director guarantor (not being a sole director guarantor) not if the guarantor has elected to opt out of this

	issued • debtor credit report from a credit reporting agency • any current credit-related insurance contract • any debtor financial accounts or statement of financial position within the previous 2 years • statements of account for the guaranteed facility for the period of a disclosed notice of demand or dishonour • any unsatisfied notice of demand in relation to the guaranteed facility within the previous 2 years		obligation, after being told of the right to receive these documents and that they are important
31.4 (e)	Obligation on signatory bank to provide other information that is reasonably requested, other than internal opinions	No	Yes
31.5	Signatory bank to provide guarantor with 1 day to consider provided information (unless independent legal advice has been obtained)	No	Yes – but in the case of a director guarantor (not being a sole director guarantor) not if the guarantor has elected to opt out of this obligation, after being told of the right to receive these documents and that they are important
31.6	Signatory bank must not arrange the signing of the guarantee through the debtor – and must arrange signing in the absence of debtor	No	Yes
31.7	Guarantor may ask for further copies of clause 31.4(d) documents – to be provided by signatory bank within 14 days (or 30 days if more than 1 year later)	No	Yes
31.8	Warning notice substantially in the form of National Credit Code Form 8 to appear directly above place of signature	Yes	Yes
31.9	Guarantor may limit the amount of the guarantee to not less than the amount of	Yes	Yes

	debtor's liability under contract (couple of exceptions apply)		
31.10	Guarantor may extinguish liability by paying debtor's liability or lesser amount under guarantee	Yes	Yes
31.11	Guarantor may withdraw before credit first provided or if the credit contract is materially different from the credit contract as originally provided to the guarantor	Yes	Yes
31.12	Third party mortgage unenforceable in relation to a future credit contract or guarantee, unless the mortgagor has been provided with a copy of the future credit contract or guarantee and the signatory bank has obtained the mortgagor's written acceptance	Yes	Yes
31.13	Guarantee is unenforceable in relation to a future credit contract unless the signatory bank has provided the guarantor with a copy of the future credit contract and obtained the guarantor's written acceptance (unless at or before the guarantor signed the guarantee, the signatory bank provided the guarantor with a notice that a future credit contract could be covered by the guarantee)	Yes	Yes

13.2. Complexity

The ABA considers that clause 31 provides important protections for guarantors that go beyond the reach of legislation, however it has suggested that the clause should be redrafted to address its complexity and length.

I agree. For guarantees of consumer credit, clause 31 largely duplicates legislative requirements and it is not easy to see what the extra Code protections are. For guarantees of small business credit, clause 31 requires close reading to ascertain which provisions apply and in what circumstances. My view is that clause 31 would be clearer if the different categories of guarantors were separately addressed.

For guarantors of credit provided to individuals other than sole traders, a clause committing signatory banks to comply with National Credit Code guarantor protections and then setting out the additional protections afforded by the Code would make the clause much shorter. For a guarantee regulated by the National Credit Code, this would avoid duplicating the law.

In the relatively rare instance of a guarantee of individual non-business credit that is not regulated by the National Credit Code, this approach would effectively import the National Credit Code provisions into the Code – rather than summarising them as currently occurs.

The result would be that clause 31.14 (a provision that only applies where the principal debtor is an individual) would no longer be needed. This would resolve an inconsistency between it and National Credit Code section 90. As seen in Figure 15, clause 31.14 purports to permit a signatory bank to enforce a guarantee against a guarantor of a non-business individual customer where the debtor has not provided security or has provided inadequate security – something not permitted under section 90 of the National Credit Code.

Figure 15. – When a judgement against a guarantor must be enforced

Clause 31.14 of Code	National Credit Code sec 90
Enforcement is not possible unless: (a) a judgment against the debtor has been unsatisfied for 30 days after demand; (b) the debtor cannot reasonably be located; (c) the debtor is insolvent; (d) a court, tribunal or other body has relieved the signatory bank from the obligation to proceed first against the debtor; (e) the guarantor has provided security but the debtor has not; or (f) the debtor's security has been enforced or is reasonably expected to be insufficient.	Enforcement is not possible unless: (a) a judgment against the debtor has been unsatisfied for 30 days after demand; (b) the court has relieved the credit provider from the obligation to obtain judgment against the debtor on the ground that recovery from the debt is unlikely; (c) the credit provider has made reasonable attempts to locate the debtor without success; or (d) the debtor is insolvent.

Separate clauses could address the two substantial categories of guarantors of credit provided to small business. This would better address the complications apparent from Figure 14. As well as a restructuring of the provision in this way, clause 31 would greatly benefit from a plain English redraft.

Recommendation 37

Clause 31 of the Code should be should be redrafted to deal separately with:

- guarantors of credit to an individual other than a sole trader; and
- guarantors of a credit facility below $5 million provided for a small business purpose.

13.3. Pre-guarantee disclosure

Consumer representatives proposed that signatory banks provide guarantors with additional disclosure. One proposal was the provision of the signatory bank's assessment in accordance with the NCCP Act that the credit facility is "not unsuitable" for the debtor[110]. Also that guarantors should have a longer minimum period to consider information provided to them than currently applies[111].

13.3.1. "Not unsuitable" assessment

As recently confirmed by the Courts[112], a signatory bank's responsible lending obligation under the Code is owed to a guarantor as much as to the debtor and I think that it would assist a guarantor to see the signatory bank's assessment that credit is "not unsuitable" for the debtor, where an assessment of this type is required by the NCCP Act. This information could help a conscientious guarantor to perceive much more clearly the risk that they are incurring and would also be a more open approach that should assist in building trust.

This should be a minimal impost for the signatory bank given my recommendation that the "not unsuitable" assessment should be provided to all consumer borrowers. Of course, the debtor's permission would be required in order to share this document with the guarantor, however this could be made a condition of the credit facility.

Recommendation 38
A signatory bank should be obliged to provide a guarantor with the signatory bank's assessment that credit is "not unsuitable" for the debtor, where the signatory bank is required by National Consumer Credit Protection Act 2009 to prepare this.

13.3.2. Time to consider information

Under clause 31.5(b) of the Code, a guarantor who has not obtained independent legal advice, cannot be signed under a guarantee until at least the day after they were provided with the Code-required information by the signatory bank. The purpose is to give the guarantor time to consider the information and whether to seek independent advice.

In my consultations with industry, I was told that Code customers are often impatient with the delay that this causes. There was opposition to a lengthier period of time for the guarantor on the basis that this could result in borrowers not meeting settlement timeframes and facing penalty fees or missing out on settlement opportunities.

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[110] Joint Consumer Submission Rec 35

[111] Legal Aid NSW Rec 7

[112] Doggett v Commonwealth of Australia (2015) VSCA 351

I accept that a longer timeframe for guarantors could result in some debtors incurring inconvenience and greater pressure on signatory banks to prepare credit facility and guarantor documentation more quickly. Nevertheless I think that one day is not enough time for guarantors considering the complexity and risks of a guarantee and the often limited knowledge of a guarantor. A minimum period of 3 days would be more realistic. Whilst less than the 7 days proposed by Legal Aid NSW[113], it seems to me that 3 days provides an appropriate balance between protection of the guarantor and the timeliness of the provision of credit process.

Clause 31.16(e) of the Code presently allows director guarantors to waive the deferral period. The rationale presumably is that the director and corporate borrower are in substance the same person. But this fails to protect passive directors who may be subject to undue influence by the principal director – and I understand from FOS that they see a number of such situations. Whilst I am aware that timing can be sensitive for small business, I think that protective considerations outweigh the inconvenience for some of a 3 day delay – which can in any event be reduced by obtaining independent legal advice.

Recommendation 39

The Code should be amended to prohibit signatory banks from signing a guarantor, who has not been legally advised, until at least the third day after the provision of all required information to the guarantor.

This provision should also apply to a guarantor of a small business credit facility below $5 million with an exception at the election of a sole director guarantor, a trustee guarantor or a commercial asset financing guarantor.

13.4. Disclosure during the period of the guarantee

13.4.1. Introduction

FOS proposed that the Code should require signatory banks to provide guarantors with better information where a guarantee is extended to cover a new credit contract[114]. During consultations, it was also suggested that a signatory bank should be obliged to inform a guarantor if a debtor encounters payment difficulties.

13.4.2. Financial information about the debtor

The Code currently requires extensive debtor financial information to be provided by the signatory bank to the guarantor before signing the guarantee. Where an existing guarantee is extended to cover a new credit contract, the Code requires the new contract to be provided to the guarantor, however not any updated financial information. This is a clear gap in keeping the guarantor appraised of the financial risk they are undertaking. By way of comparison,

[113] Legal Aid NSW Rec 13

[114] FOS Submission p. 12

clause 12.12 of the Customer Owned Banking Code of Practice requires the provision in these circumstances of:

> *"any updated information available to us on the financial position of the borrower, being information that a careful and prudent guarantor may wish to consider before allowing a guarantee to be extended".*

The Code should be amended to incorporate a similar disclosure requirement. An exception should, however, apply for a sole director guarantor, a trustee guarantor or a commercial asset financing guarantor. These categories of exception would be consistent with the categories of exception for debtor financial information provided pre-guarantee. As is currently the case under clause 31.13, an exception should also apply where the new guaranteed amount is within the limit previously agreed by the guarantor and the original notice provided to the guarantor included a prominent statement that the guarantee can encompass future credit.

Recommendation 40

Before an existing guarantee is extended to cover a new credit contract, the Code should require the signatory bank to provide the guarantor with any relevant updated information available to the signatory bank as to the current financial situation of the debtor.

This provision should only apply to a guarantor of a small business credit facility below $5 million with an exception for a sole director guarantor who has chosen not to receive this information, a trustee guarantor or a commercial asset financing guarantor.

13.4.3. Information about debtor payment difficulty

The Code does not currently require a signatory bank to provide any information to the guarantor where the debtor is encountering payment difficulty. The first they may know of this difficulty could be a notice of default served on the guarantor.

Consistent with the idea of keeping a guarantor appraised of the risk they are exposed to, it would be fair to provide some form of alert. Early notice would also give the guarantor an opportunity to discuss the matter with the debtor and see what can be done to right the situation.

I do not suggest that a signatory bank should have to alert a guarantor to any failure by a debtor to make payment on time. A payment can be inadvertently missed and that one missed payment is not necessarily an indication that the debtor is encountering payment difficulty. A 2 month period of continuing default would, however, be of concern.

Equally, a change to the contract on the basis of financial hardship would be of concern. Under the National Credit Code, a financial hardship change is triggered by the debtor telling the credit provider that they are unable to meet their obligations under the credit contract. It seems to me that a guarantor should be entitled to be told this.

I recognise that signatory banks would need to have the permission of the debtor to provide this information to the guarantor, but again this can be made a condition of the credit facility.

Recommendation 41

The Code should include a new provision obliging signatory banks to inform a guarantor where the debtor has been in continuing default for more than 2 months or where the debtor's credit contract has been changed because the debtor has encountered financial hardship.

This provision should only apply to a guarantor of a small business credit facility below $5 million.

13.5. Guarantee procedures

Consumer representatives proposed a number of amendments to the guarantee signing process. One proposal was that signatory banks should have more responsibility for considering guarantors' financial situation and should not enter into a guarantee with a person who receives a Centrelink payment[115]. Another proposal aimed to further encourage guarantors to seek independent advice.

13.5.1. Assessment of guarantor's financial position

I understand the concern about guarantors who lose their home as a result of guaranteeing credit from which they may derive no benefit. I also understand that there is an apparent consistency with responsible lending principles for a signatory bank to undertake an assessment of whether a guarantee has the potential to cause substantial hardship for the guarantor.

On the other hand, a guarantor is not responsible for making regular repayments, so the responsible lending assessment methodology does not translate well to a guarantee context. Also, guarantees play an important role in facilitating access to credit and so there could be some borrowers, particularly small business borrowers, who would be adversely affected if signatory banks begin taking a more restrictive, risk averse approach to the guarantor security they will accept. I am conscious of my design approach that the Code should not unreasonably impinge on customer choice.

I am also aware that there are limits to the extent to which frontline bank staff can be expected to be expert in diagnosing every possible danger or risk to a guarantor. It is not my intention that the new Code provision represent a promise that abuse will not occur, nor that the signatory bank can be held accountable for every misfortune that may befall a guarantor. Rather it is my intention that the signatory bank will take all reasonable care when considering the circumstances of a proposed guarantee – and that they will only be held accountable for taking reasonable care.

[115] Legal Aid NSW Rec 16

My view is that the priority here is to do what is practicable to protect the vulnerable and to avoid exacerbating any financial abuse and signatory banks' responsibility to consider the impact of a guarantee on the guarantor should be confined to this. Signatory banks should be alert to signs that the provision of a guarantee could constitute a form of financial abuse and not accept a guarantee as security for credit where their enquiries support this suspicion.

ABA Industry Guidelines *Protecting vulnerable customers from potential financial abuse* (last updated December 2014) and *Financial abuse and family and domestic violence policies* (issued November 2016) touch upon the potential for guarantees to constitute a form of financial abuse. In consultation with consumer representatives, further guidance should be developed to assist signatory banks to identify when a proposed guarantee should be viewed as financial abuse and so when it is appropriate for the bank to exercise its discretion not to accept the proposed security for credit.

Recommendation 42

In consultation with consumer representatives, signatory banks should enhance Industry Guidelines to assist bank staff to identify when a guarantee should be viewed as financial abuse and accordingly when the signatory bank should exercise its discretion not to accept a guarantee as security for credit.

The guidance should cover the factors that might be suggestive of financial abuse and what further steps a signatory bank should take in response, including enquiries about the guarantor's financial position to assess the extent of hardship that would result if the guarantee is enforced by the signatory bank.

13.5.2. Independent legal and financial advice

I have also considered whether the Code should require signatory banks to do more to encourage guarantors to obtain independent legal and financial advice and in particular, Legal Aid NSW's proposal that the Code should oblige signatory banks to obtain a guarantor signed acknowledgement that independent advice has been obtained or that the right to obtain advice has been waived[116].

1. Clause 31.4 of the Code requires a "prominent" notice that the guarantor should seek independent legal and financial advice on the effect of the guarantee.

   In *National Australia Bank Ltd v Rose*, the guarantor successfully defended a claim by the signatory bank under the guarantee on the basis of non-compliance with this provision[117]. This requirement, therefore, already has 'teeth'.

2. Clause 31.8 of the Code requires a boxed notice, marked "Important", to appear directly above the place of signature by the guarantor stating that the guarantor should obtain independent legal advice and should also consider obtaining independent financial advice (National Credit Code Form 8 requirements imported into the Code by clause 31.8 of the Code for the benefit of all guarantors of Code customers).

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[116] Legal Aid NSW Rec 14

[117] National Australia Bank Ltd v Rose [2016] VSCA 169

In the end, I was not persuaded that the signing of an additional document waiving the right to advice would sufficiently add to the Code protections.

13.6. Guarantee enforcement

The Joint Consumer Submission expressed concern that a signatory bank is able to proceed to enforce security provided by a guarantor, rather than having to first enforce security provided by the debtor. The argument was made that as the debtor is primarily liable and has obtained the benefit of the credit, it seems unfair to enforce against the guarantor ahead of the debtor.

Neither clause 31.14 nor section 90 of the National Credit Code affect this position. In fact, clause 31.14 specifically contemplates that a signatory bank can enforce security provided by a guarantor if the signatory bank reasonably expects that the proceeds of enforcing debtor security will not be sufficient to meet the liability.

I think that there is a reasonable community expectation that a signatory bank would have recourse to security provided by an individual customer borrower before it would have recourse to the guarantor's security. To do otherwise is counter-intuitive, would be seen as 'tricky' and should be avoided. This is particularly the case where the signatory bank could be seen to be taking the 'easiest' option (not the necessary option) in selling up the guarantor and leaving them to attempt to recover from the debtor.

I recognise that in some circumstances this could slow the signatory bank's security realisation process and that where the sale of both the debtor's and the guarantor's asset is required that there will be higher enforcement costs than if just one asset was sold. I also recognise that, where the debtor's security is not significantly less than the amount owing, it may be a poor outcome for both the debtor's security and the guarantor's security to be sold. However, in this situation, the guarantor may find another way to preserve their secured asset, especially critical assets such as the family home. Also, a new Code provision should not prevent the debtor and guarantor agreeing to ask the signatory bank to sell the guarantor's security without first selling the debtor's security. Of course, a signatory bank would need in these circumstances to be satisfied that the guarantor has given genuine consent and that issues of financial abuse do not arise.

A significant benefit of my recommended approach is the shift away from the guarantor of the burden of taking recovery action (to the extent possible) against the debtor. It seems entirely appropriate to shift this burden, given that it was the signatory bank that made the assessment of the debtor's credit worthiness and chose to lend to the debtor and the bank is much better equipped than the guarantor to carry out this recovery action.

Different considerations apply to small business credit. As in my discussion of responsible lending in Chapter 8.4, the credit assessment process, time-sensitivity and extent of reliance upon security can be quite different for small business lending and more commonly, the guarantor derives benefit from the credit facility. I am not proposing that this protection should be extended to guarantors of credit for a small business purpose.

Recommendation 43

The Code should be amended to require signatory banks to have recourse to security provided by an individual customer borrower, before the signatory bank has recourse to the guarantor's security, unless the guarantor and individual customer borrower agree otherwise.

13.7. Non-compliance with guarantor requirements

The Code does not currently specify the consequences where a signatory bank fails to provide a guarantor the protections due to the guarantor under the Code. In the absence of this, there can be difficult arguments about whether or not the guarantor would have entered into the guarantee, if the signatory bank had in fact complied with Code obligations.

FOS has proposed in its submission that it would be best practice if non-compliance with the guarantor requirements renders the guarantee unenforceable. It argues that this outcome would be consistent with the strong wording used in clause 31 "we will include a statement", "we will do the following things", "we will not ask you to sign", "we will ensure that a warning notice …appears" etc. This result would also recognise the very significant detriment that can impact a guarantor if the clause 31 protections are not afforded. This is in fact how FOS interprets the Code where FOS decides a dispute about a guarantee of credit provided to a Code customer. The banking industry position is that normal legal principles should determine the ramifications of non-compliance with the Code.

13.7.1. Discussion

As noted earlier, clause 31 does not currently add much to the National Credit Code protections provided to a guarantor of an individual debtor. It would strengthen the Code substantially if the consequence of a pre-execution contravention was that the guarantee was unenforceable (a result that would not necessarily apply for a breach of National Credit Code requirements).

I think that this would be consistent with a plain-speaking, less qualified approach to the Code that I have argued would help to build customer trust. The alternative message could be interpreted as: 'We said that we would provide important information to you as a guarantor. We failed to do this, but we think this doesn't matter because we don't think that you would have read or relied upon the information'.

Recommendation 44

The Code should specify that a guarantee is unenforceable if the signatory bank fails to comply with the pre-execution requirements. Similarly non-compliance with a post execution requirement means that the guarantee is unenforceable in relation to debt or costs that accrue after that time.

13.8. EDR scheme jurisdiction

The two Australian EDR schemes open to signatory banks both have Terms of Reference that restrict the scheme's jurisdiction both by reference to the size of the claim (currently a maximum of $500,000) and the quantum of the award they can make (currently capped at $309,000). The scheme can only exceed its monetary limit if the financial services provider gives its consent. Typically this does not occur.

As previously noted, FOS is in the process of consulting with stakeholders about changing its Terms of Reference to give it power to consider higher value claims and to make larger awards in small business disputes. I understand that this is likely to lead to an amendment of FOS's Terms of Reference this year. The Credit and Investments Ombudsman is reported as indicating that it will amend its monetary jurisdiction to adopt the same or substantially similar monetary thresholds to that of FOS[118].

As also previously noted, the Ramsay Review is considering the adequacy of financial services external dispute resolution claim and award limits generally. The Interim Report issued in December 2016 includes a draft recommendation that higher limits should apply[119] and seeks submissions about what these should be. Part of the rationale for higher limits is that housing cost increases have pushed many mortgages and guarantees on home loans beyond the schemes' jurisdiction[120].

13.8.1. Discussion

I accept arguments put to me that the current EDR scheme claim and award monetary limits are inadequate in the case of a dispute with a guarantor of a home loan. Typically, a debtor with a dispute with the bank over a home loan is not raising a dispute over the whole amount of the mortgage (it might be over interest or fees, etc.) which means that the EDR scheme jurisdiction limits are not an issue for debtors as often as might be imagined. Because a dispute about a guarantee has the potential to make the guarantee unenforceable, the full amount of the guarantee will often be in issue. In today's market, a dispute about a guarantee to secure a home loan will very often involve more than $309,000 and so will be outside the EDR scheme's jurisdiction. These are not unusual sums and certainly not indicative that the guarantor is sophisticated or will have the resources or confidence to litigate in court.

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[118] *Review of the financial system external dispute resolution and complaints framework, Interim Report*, 6 December 2016, p.111

[119] *Review of the financial system external dispute resolution and complaints framework*, draft recommendation 2

[120] *Review of the financial system external dispute resolution and complaints framework*, p.104 and 105

It is likely that the Ramsay Review will make recommendations to resolve this problem. But it will take time for the Ramsay Review recommendations to be implemented. As an interim measure, it would be possible, as the Joint Consumer Submission proposed, for the Code to oblige signatory banks to consent to their EDR scheme deciding a dispute about a guarantee for a specified amount being more than the scheme's monetary limit[121]. In discussions with me, consumer representatives suggested that this should be the case where the guarantee limits liability to $1 million.

This conforms with the Ramsay Review Interim Report reference to the ABA view that a claim and award limit of $1 million is appropriate for consumer and small business claims alike[122]. My concern is that, given housing costs, $1 million may be seen as barely enough by much of the public. Arguably a higher threshold would be seen as more realistic. I recommend that the ABA and signatory banks should decide upon a threshold, taking into account the average housing costs in capital cities and FOS's small business monetary limit, once that limit is announced.

Recommendation 45

The ABA and signatory banks should agree a monetary limit up to which signatory banks must consent to their EDR scheme having jurisdiction to decide a claim about a guarantee to secure a home loan to an individual customer (if the EDR scheme's terms of reference would otherwise bring the dispute within the scheme's jurisdiction). The monetary limit should be at least $1 million and should be determined taking into account the average housing costs in Australian capital cities and FOS's small business monetary limit once that limit is announced. The Code should be amended to include this commitment.

[121] Joint Consumer Submission Rec 39

[122] *Review of the financial system external dispute resolution and complaints framework*, p.104

14. FINANCIAL DIFFICULTY

Financial difficulty issues were a key focus in submissions to the Code Review. There were views that the Code should clarify what is meant by financial difficulty assistance and give more prominence to financial difficulty in the Code. A number of submissions suggested that signatory banks should better publicise the availability of this assistance. A repeated theme was that signatory banks should be more proactive in identifying customers at risk of financial difficulty. Issues were also raised as to the type of assistance provided by signatory banks in response to customer financial difficulty. Where financial assistance has been agreed but is not confirmed in writing to the customer, the potential for miscommunication was of concern. This Chapter addresses those issues, with a focus on individual customers.

Financial difficulty issues are also touched upon in other Chapters of my Report. Chapter 8.8 addresses small business financial difficulty assistance. Chapter 20.10 recommends better financial difficulty assistance public reporting.

14.1. Background

Financial difficulty assistance is a key part of banks' social compact. Signatory banks recognise that their customers from time to time experience circumstances that place them under financial pressure. As stated in the ABA's Industry Guideline, "[signatory] banks want to help their customers during times of financial difficulty"[123].

The National Credit Code sets out in some detail the processes that apply where an individual tells their credit provider that they are unable to meet their financial obligations under a consumer contract. The credit provider has to consider whether a change to the contract would restore the customer's financial situation[124]. This is referred to as a hardship change.

In addition to their National Credit Code obligations, signatory banks also have an obligation under clause 28.2 of the Code to assist with financial difficulty. This applies to small business customers, not just to individual customers.

> *"28.2. With your agreement and cooperation, we will try to help you overcome your financial difficulties with any credit facility you have with us . We could, for example, work with you to develop a repayment plan."*

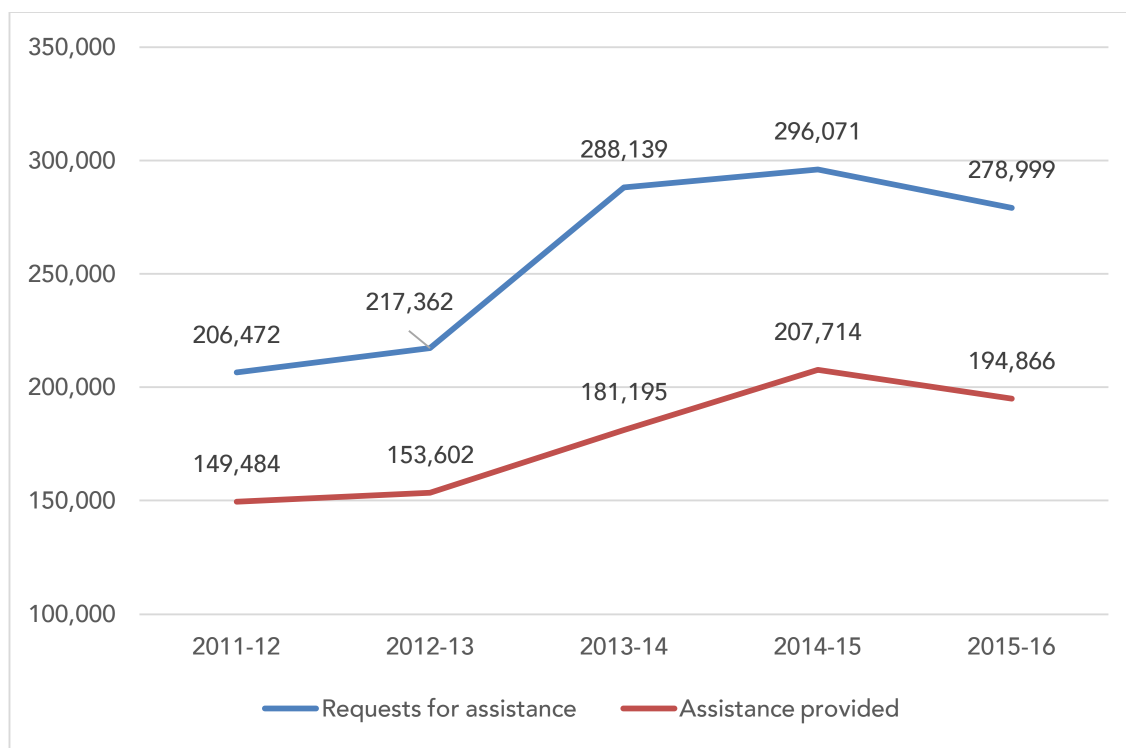
Figure 16. below demonstrates the significant numbers of requests for financial difficulty assistance and that about 70% of requests are granted[125].

[123] ABA Industry Guideline, *Promoting understanding about banks' financial hardship programs*, updated November 2016, p.1

[124] National Credit Code sec 72

[125] Code Compliance Monitoring Committee, *Financial Difficulty Own Motion* Inquiry, November 2015 p.36

Figure 16. – Signatory bank financial difficulty requests 2011 - 2016



Source: CCMC, ***CCMC 2015-16 Annual Report***

14.2. Prominence of financial difficulty assistance

Given the importance of financial difficulty assistance, it is perhaps not surprising that there were suggestions that the Code should give more prominence to this issue. This harks back to the recommendation of the previous Independent Reviewer of the Code that a new key commitment make reference to "supporting customers facing financial difficulty"[126]. This recommendation was not implemented at that time, however I see the proposed new Code as an opportunity to include this. Under my recommended architecture discussed in Chapter 6.7, the Principles would be the place for this. In the example Principles, a commitment to assistance with financial difficulty is Principle 7.

Recommendation 46

The Code should give prominence to signatory banks' commitment to support customers facing financial difficulty by including this in Principles that appear at the front of the Code.

[126] McClelland, J *The Code of Banking Practice Final Report*, December 2008, Rec 1

14.3. Defining financial difficulty

In its submission to the Code Review, the CCMC noted the absence of a definition of "financial difficulty" and suggested a definition along the following lines.

> *"The CCMC considers that financial difficulty means that a customer is willing but unable to meet their obligations under a credit facility. This may be due to a change in circumstances such as illness, unemployment, an increase in living expenses or other cause.*
>
> *It may require assistance such as a variation to a customer's repayment obligations but is unlikely to include overlooked or late payments, in the absence of evidence that the consumer is unlikely to be able to pay."*[127]

The CCMC's language is similar to the language that the National Credit Code uses. That code contemplates a credit provider changing a consumer credit contract for a debtor who "considers that he or she is or will be unable to meet his or her obligations". A relevant factor is whether the credit provider believes that "there is a reasonable cause for the debtor's inability to meet his or her obligations".

In comparison, the ABA in its Industry Guideline[128] identifies three categories of financial difficulty as shown in Figure 17 below.

[127] CCMC Guidance Note 13 *Financial difficulty* paragraphs 2 and 3

[128] ABA Industry Guideline *Promoting understanding about banks' financial hardship programs*, updated November 2016,p. 2

Figure 17. – Categories of financial difficulty

Late payment assistance	**When restoring a customer's financial situation is possible**	**When restoring a customer's financial situation is unlikely***
Customer requires help from their bank to overcome a short term payment difficulty. For example, a customer would like to make their repayment at a later date, or they have accidentally missed a payment and would like the late payment fee waived. Banks have the discretion to provide relief to their customers, such as offering a payment arrangement or deferral (known as a 'promise to pay' arrangement). Banks can also agree to refund or waive late payment or default fees. Formal financial hardship assistance is unlikely to be required in these circumstances.	Banks' financial hardship arrangements focus on situations where a customer can recover their financial position if appropriate assistance and agreed arrangements are put in place. Arrangements can be: **Short term** Examples include moving to interest-only or reduced payments for an agreed period of time. **Longer term** Examples include extending the loan's term so repayments are lower for the life of the contract. Longer-term arrangements would generally require a change to the conditions of the existing credit contract and a new repayment plan.	Due to a permanent change in their financial situation, the customer's capacity to recover and meet repayments in a reasonable amount of time is unlikely. Even if the conditions of the existing credit contract were changed, the customer would not be able to satisfy their repayment obligations in the long term or restore their financial position. It may not be possible or appropriate for the bank to offer payment arrangements under their hardship program. However, even in these circumstances, banks can offer support and advice but the existing contract would generally not continue. Options may include agreeing on an alternative arrangement, plan or contract; refinancing; selling the property; or pursuing bankruptcy or insolvency arrangements.

During the course of their relationship with their bank, a customer may move in and out and between these situations:

- Repeated requests for late payment assistance may lead to a need for formal hardship assistance.
- If a customer cannot restore their existing financial position, they may sell their assets and refinance with the same bank.

* In certain circumstances a customer may be able and willing to repay even if conditions do change permanently.

Dealing with longer-term hardship is an inherently difficult and challenging issue for the community. The banking industry is committed to working with stakeholders to explore ways it can assist.

Source: ABA Industry Guideline Promoting understanding about banks' financial hardship programs, November 2016, p.2

Signatory banks have told me that they interpret "financial difficulty assistance" as encompassing more than just financial hardship contract variations. For example, a customer may be able generally to meet their financial commitments, but may have inadvertently failed to make a payment in a particular month. The signatory bank may agree to waive rights in relation to the late payment (for example, late payment fees). The signatory bank may make this concession (sometimes referred to as an indulgence) in a single phone discussion with the customer. Signatory banks may also provide assistance to a customer whose financial position cannot be restored by a change to their contract on the basis of financial hardship.

14.3.1. Discussion

I support a broader ambit to the concept of "financial difficulty" than the legislative "financial hardship". This is consistent with the conception of the Code as going beyond minimum legal standards and encourages greater innovation in prevention or early remediation strategies.

It appears, however, that current practices do not make it clear when financial difficulty assistance is being provided under the Code to a consumer customer and when financial hardship assistance is being provided under the National Credit Code. Yet clarity is important because different consequences may flow depending upon the nature of the assistance.

To address this, I think that the Code needs to explain the concept of financial difficulty and, for consumer customers, the extent of overlap with the legislative financial hardship requirements. A diagrammatic presentation along the lines of the ABA Industry Guideline would be helpful. I am, however, concerned about the description in the ABA Industry Guideline diagram of late payment assistance – a concern that has also been expressed by consumer representatives and by FOS. It seems to me that the explanatory language incorporates situations that are actually encompassed by the legislative concept of financial hardship. Accordingly I recommend that this is revisited by signatory banks.

Recommendation 47

The Code should explain the concept of financial difficulty and, for consumer customers, the extent of overlap with the legislative financial hardship requirements. A diagrammatic presentation of the categories of financial difficulty, with examples, along the lines of the ABA Industry Guideline ***Promoting understanding about banks' financial hardship programs*** would be helpful. The description in the ABA Industry Guideline diagram of late payment assistance should, however, be revisited to ensure that it does not encompass situations that are properly within the legislative concept of financial hardship.

14.4. Proactivity by signatory banks

In written submissions to the Code Review and in consultations with me, consumer representatives urged that the Code should place more onus on signatory banks to proactively contact customers and offer assistance[129]. This proactive contact from the bank could begin as an inquiry about whether the customer is aware of the availability of other products that may be more suitable, for example, a lower cost bank account or credit product. The opportunity could then be taken to introduce the availability of financial difficulty assistance.

The Joint Consumer Submission also proposed that banks should proactively work with any customer who is identified as experiencing financial difficulty and develop a plan with the customer[130]. Another proposal was that banks proactively identify customers who are eligible for a debt waiver[131].

[129] Joint Consumer Submission Rec 10b., 16b.

[130] Joint Consumer Submission Rec 10a.

[131] Joint Consumer Submission Rec 16b.

Similarly Treasury has proposed that credit providers should be required to proactively contact credit card customers who are persistently making small repayments and so may benefit from alternative credit arrangements (for example, transferring to a lower interest rate credit card or a personal loan) or alternative payment options (for example, higher repayments to reduce the amount outstanding)[132].

> *"In these cases, one option is for card providers to identify these consumers and contact to offer 'solutions'. The Government is aware that a number of card issuers already have similar policies in place but is concerned that this practice is not widespread and may be triggered too late in the life of the debt. Under this proposal, card issuers would be required to contact consumers well before they reach the point of imminent default."*[133]

14.4.1. Discussion

I think that signatory banks would greatly enhance the service they provide if they establish 'early warning' systems for individual customers under debt pressure. This would be a best practice initiative that would have the potential to transform signatory banks' financial difficulty assistance for some customers by identifying and addressing debt issues before they become overwhelming.

Of course, it would not be realistic to expect signatory banks to identify all Code customers who are starting to become burdened by debt. Because businesses naturally have cash flow peaks and troughs, I think it would not be practical to encompass them in an 'early warning' system. For individual customers, I think that the most that the Code could require is that signatory banks establish systems and processes that aim to identify and contact those at high risk of future financial difficulty. Along the lines of the UK Lending Code, the Code could include a non-exclusive list of factors to be taken into account for the purposes of determining individuals at risk, for example:

- the customer repeatedly exceeding the credit facility credit limit;
- multiple requests by the customer to increase their credit facility credit limits;
- high or increasing numbers of default charges being incurred by the customer;
- regular returned items or refused authorisations in respect of point of sale or ATM transactions;
- high interest rate payments on the customer's credit card relative to the credit card balance; and

[132] Australian Government The Treasury *Credit cards: improving consumer outcomes and enhancing* competition, May 2016, Rec 9

[133] Australian Government The Treasury *Credit cards: improving consumer outcomes and enhancing* competition, May 2016, p.24.

- deteriorating credit rating for the customer as identified by a credit reporting body[134].

Having identified an at-risk individual, the next step would be for the signatory bank to contact the customer to discuss their banking options and to introduce the possibility of financial difficulty assistance. The ABA Industry Guideline *Promoting understanding about banks' financial hardship programs* provides some useful guidance for the purpose of proactive contact with a customer in response to behaviours that could be a sign of financial difficulty[135]. Clearly, to be successful, proactive contact of this type needs to be undertaken sensitively by the signatory bank. From my discussions with signatory banks, it is clear that some banks are building the staff skills to facilitate these types of conversations. So, it can be done.

Finally, I note that, whilst the primary reason for this type of intervention is to assist individual customers, it may be that signatory banks will find early intervention results in some reduction in impaired loans, so that there are also commercial benefits associated with this approach. I understand that this is the emerging experience of one signatory bank.

Recommendation 48

The Code should include a new clause that obliges signatory banks to establish systems and processes to identify and contact individual customers at high risk of future financial difficulty and to try and assist those customers. The clause could include a non-exclusive list of factors that could be taken into account for the purposes of determining customer risk, for example:

- the customer repeatedly exceeding the credit facility credit limit;
- multiple requests by the customer to increase their credit facility credit limits;
- high or increasing numbers of default charges being incurred by the customer;
- regular returned items or refused authorisations in respect of point of sale or ATM transactions;
- frequent use of cash advance facility;
- failure to reduce outstanding balance over time; and
- a customer known to have a significantly deteriorating credit rating as identified by a credit reporting body.

[134] See UK The Lending Code para 183

[135] ABA Industry Guideline, *Promoting understanding about banks' financial hardship programs*, November 2016 p. 14

14.5. Financial difficulty assistance process

Good communication between the signatory bank and Code customers is critical for financial difficulty assistance to be effective. The customer needs to tell the signatory bank at an early stage about the financial difficulties they are experiencing. Bank staff need to take the time to listen to the customer and to do so without judging the customer.

In submissions to the Code Review, a couple of proposals were made that were directed at enhancing the financial difficulty assistance process.

14.5.1. Early communication by customers of financial difficulty

Clause 28.5 seeks to encourage Code customers to tell their signatory bank if they are experiencing financial difficulties in meeting repayment obligations.

The Joint Consumer Submission[136] expressed the view that the language in clause 28.5 should be encouraging, rather than the language of obligation – eg. "you should make contact with us as soon as possible". The Submission also proposed that the Code include a commitment by signatory banks to consider a customer's situation "sympathetically and positively", language that is used in the United Kingdom code[137].

I discuss at Chapter 6.8 the importance of the Code language using a warm tone. It is particularly important that a positive tone is set for communications between the signatory bank and the customer about financial difficulty issues. To my mind, the current language could readily be improved[138].

Recommendation 49
Clause 28 of the Code should be rewritten using language that is simpler and warmer in tone. For example, clause 28.5 could "encourage" customers to "let us know" about financial difficulty. Signatory banks should commit to considering cases of financial difficulty "sympathetically and positively".

14.5.2. Using intermediaries to deal with the bank

The Joint Consumer Submission proposed that banks should encourage customers to seek help with their financial difficulties, but warn them against using debt management firms[139].

[136] Joint Consumer Submission p.40

[137] The Lending Code para 178

[138] See also Customer Owned Banking Code of Practice para 24.1 reference to working "constructively" with the customer.

[139] Joint Consumer Submission Rec 12i. and j.

Currently the Code obliges signatory banks to recommend independent advice, for example from a financial counsellor, only if the customer is contemplating seeking early release of superannuation benefits[140]. The ABA Industry Guideline is broader and envisages that, in appropriate cases, signatory banks will refer customers in financial difficulty to financial counsellors[141]. Some signatory banks have partnerships with financial counselling organisations to facilitate this[142].

My recommendation is that the Code reflect the ABA Industry Guideline and include a simple statement that in appropriate cases signatory banks will refer Code customers in financial difficulty to financial counselling organisations. This can replace existing clause 28.9(b).

Whilst I understand the concerns expressed about predatory practices by some debt management firms, it seems to me that this is a matter for the government to address through regulation. I don't think that I should be recommending that signatory banks should be obliged to cast aspersions on debt management firms.

Recommendation 50

In place of existing clause 28.9(b), the Code should include a simple statement that in appropriate cases signatory banks will refer Code customers in financial difficulty to financial counselling organisations.

14.6. Nature and consequences of assistance

Currently clause 28 says little about the types of financial difficulty assistance that signatory banks may provide. There is reference in clause 28.2 to the possibility of a repayment plan. Other subclauses simply refer to "options available to assist" the customer.

The Joint Consumer Submission made a number of proposals that would increase the specificity of the Code as to the nature and consequences of financial difficulty assistance including:

1. Requiring banks to give more consideration to customer affordability when agreeing a payment plan with the customer[143];
2. That the Code explicitly refer to the possibility of debt waiver[144]
3. That the Code commit signatory banks not to report adverse information on a customer's credit report (including adverse repayment history information) where financial difficulty assistance has been provided[145]; and

[140] Code clause 28.9

[141] ABA Industry Guideline *Promoting understanding about banks' financial hardship programs,* November 2016,p. 4, 7, 11, 13 and 14

[142] www.kildonan.org.au/media-and-publications/news/nab-change-the-world

[143] Rec 19

[144] Rec 16

4. That the Code commit signatory banks to afford some leniency if a customer has a minor non-compliance with an agreed payment plan[146].

Note that the discussion in this section does not apply to a small business – instead see discussion at Chapter 8.8.

14.6.1. Discussion

I think that the options and design considerations for financial difficulty assistance require a nuanced discussion that refers to the variety of circumstances that can arise. This requires detailed discussion that I see as inappropriate for a code. In my view, an industry guideline is a much better vehicle to do this – and in fact, the ABA Industry Guideline *Promoting understanding about banks' financial hardship programs* sets out in some detail examples of the assistance that banks may provide, including debt waiver.

This Guideline, developed by the ABA and signatory banks (including some consultation with consumer representatives), is a good initiative and has evolved over time with the most recent version issued in November 2016. It would be further enhanced by including more guidance about how to restructure repayments so that arrangements are sustainable and sufficiently take into account affordability considerations. It could also address what a customer should do if they find that they cannot comply strictly with an agreed financial difficulty assistance arrangement. A Code footnote reference to the Guideline could also help individual customers to find out about the Guideline and so to better understand the types of assistance that may be available.

Recommendation 51

The ABA and signatory banks should continue to regularly review ABA Industry Guideline ***Promoting understanding about banks' financial hardship programs.*** The next version of the Guideline could usefully address the importance of signatory banks ensuring that restructured arrangements are sustainable and sufficiently take account of affordability for the customer.

It would also be useful to address what a customer should do if they find that they cannot comply strictly with an agreed financial difficulty assistance arrangement. When developing the next iteration of the Guideline, the ABA and signatory banks should work closely with consumer advocates.

In addition to further development of the ABA Industry Guideline, there are two amendments that I think should be made to the Code to enhance the quality of financial difficulty assistance by signatory banks.

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[145] Rec 12d.

[146] Rec 12e.

I think clause 28 should expressly contemplate longer term financial difficulties. I recognise that the Industry Guideline already refers to longer term financial difficulty assistance. But this issue is of such importance that I think the Code should also address this. Here I note the comments in the CCMC Inquiry Report *Financial Difficulty:*

> *"While a three-month moratorium may be appropriate in many cases, it should not be a 'default' option and should only be offered where there is a likelihood that a customer will recover their position or when it is part of a longer-term offering."*

The CCMC recommended that signatory banks should:

> *"ensure that any assistance offered to customers is appropriate to their circumstances and that a longer-term offering is considered where it is evident that a short term solution will not contribute to the customer overcoming their financial difficulty*[147]*.*

A specific reference to longer term financial difficulty would also bring the Code into line with the Customer Owned Banking Code of Practice which provides:

> *"we will have procedures in place to ensure we:*
> *….*
>
> *• consider longer term as well as short-term financial issues when they are relevant.*
>
> *If you are experiencing longer term difficulties, we will try to develop an appropriate solution with you to allow you to meet your obligations*[148]*.*

Recommendation 52

Clause 28.2 of the Code should be amended to contemplate assistance by a signatory bank to help a Code customer to overcome short term or longer term (but nevertheless finite) financial difficulties with a credit facility provided by the signatory bank.

[147] CCMC Inquiry Report Financial Difficulty, November 2015, Rec 9

[148] Para 24.2

The second change that I am recommending is that clause 28 should include a new provision that a signatory bank may in its discretion decide to waive a small unsecured debt if the bank is provided with evidence that the person is in long term financial hardship and the circumstances warrant a compassionate approach[149]. Assistance of this type is contemplated in the Industry Guideline *Promoting understanding about banks' financial hardship programs*[150], but it is of sufficient importance that I think it should be included in the Code. The provision would need to be clear that debt waiver is at the discretion of the signatory bank.

Recommendation 53

Clause 28 of the Code should be amended to include a new provision that a signatory bank may, at its discretion, decide to waive a small unsecured debt if the bank is provided with evidence that the person is in long term financial hardship and the circumstances warrant a compassionate approach.

I do not, however, support the proposal that the Code restrict a signatory bank from charging default fees while considering whether to provide assistance for financial difficulty. A waiver of default fees may, of course, be an aspect of the signatory bank's financial difficulty assistance if assistance is granted. However, fee waiver should not be an entitlement that automatically follows from asking the bank for assistance. Assistance may not be warranted and there is some potential for 'gaming' here.

Nor am I recommending that the Code include restrictions on signatory banks' ability to report adverse repayment history information where a financial difficulty arrangement is in force[151]. There are issues here about the interplay between the Code financial difficulty provisions and the National Consumer Credit financial hardship provisions that I think need addressing first – given that, as I understand, a legislative financial hardship contract change restructures the payment obligation and means that there is no late payment and so reporting should not occur.

Second, as has been recognised recently by the Productivity Commission[152], there is a public good in accurate comprehensive credit reporting so I am reluctant to intervene here. Third, if reporting restrictions are thought to be appropriate, these would be better located in the Privacy (Credit Reporting) Code 2014 (due to be reviewed next year).

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[149] See United Kingdom The Lending Code para 214 for a similar approach

[150] Industry Guideline *Promoting understanding about banks' financial hardship programs*, March 2015, p.10

[151] Under the Privacy Act 1988, a payment would have to be at least 14 days overdue to be reported as late.

[152] Productivity Commission 2016, *Data Availability and Use*

14.7. Co-debtor financial difficulty assistance

The Joint Consumer Submission reported that many consumers encountered difficulties when seeking financial difficulty assistance for joint debts where their relationship with their co-debtor had broken down. This was because the bank required input from the consumer's ex-partner[153]. The Submission proposed that it should be made clear in the Code that either co-debtor can seek financial hardship assistance and the signatory bank can make a variation with one debtor only[154].

14.7.1. Discussion

There now appears to be a consensus of views that the National Credit Code financial hardship provisions enable a credit provider to vary a credit contract on the basis of financial hardship at the request of a co-debtor, even if the other co-debtor does not agree to the change. This is FOS's guidance as to how the National Credit Code should be interpreted[155] and the ABA's recently released Industry Guideline *Financial Abuse and Family and Domestic Violence*, November 2016 also proceeds on this basis.

> *"To manage joint liabilities/debt banks will:*
>
> *Accept a financial hardship request from a joint borrower without the consent of the other co-borrower.*
>
> *In circumstances where there is a joint loan and parties are jointly and severally liable, the bank will, wherever possible, obtain the consent of all parties to any variation of the loan. Banks, however, acknowledge that this may not be reasonable in all circumstances. A bank can, therefore, decide to settle a claim for the whole or part of the debt against one co-borrower (i.e. the borrower impacted by family and domestic violence). This can have the effect of severing or apportioning the loan so the co-borrower pays only a portion (including no payment if appropriate) of the debt in return for a release from the whole of the debt. Provision of these arrangements will be assessed on a case-by-case basis."*[156]

The Guideline makes a commitment that signatory banks will not require the borrower to contact or obtain information or the consent of the other co-borrower. There is also a commitment to "fast track hardship requests where family and domestic violence has been disclosed as an issue, recognising that in some cases the statutory timeframe for responding to a hardship request (21 days) may create additional stress and safety concerns for their customer"[157].

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[153] Joint Consumer Submission p.88

[154] Joint Consumer Submission Rec 31

[155] *The FOS Approach to Financial Difficulty series – Dealing with common issues* p.2

[156] ABA Industry Guideline *Financial Abuse and Family and Domestic Violence*, November 2016, p.5

[157] ABA Industry Guideline *Financial Abuse and Family and Domestic Violence*, November 2016, p.6

It seems to me that the ABA's Industry Guideline deals well with this difficult issue. The Guideline establishes clear general principles, but also acknowledges that arrangements need to be assessed on a case-by-case basis.

Given the importance of this issue, I think that the Code should make reference to this issue. There is now an increasing awareness that financial factors play a very significant role in domestic abuse and also that domestic abuse is devastatingly prevalent in our community. Consumer representative submissions urged the Code to acknowledge this[158]. The ABA Industry Guideline should also be footnoted to assist readers to locate the more detailed explanation of signatory banks' approach to the issue that the Guideline offers.

Recommendation 54

Clause 28 of the Code should acknowledge that financial difficulty assistance may be sought by a co-debtor, in the absence of agreement from the other co-debtor, and that signatory banks will try to assist particularly in situations of financial abuse or family violence. The clause should have a footnote referring to the ABA Industry Guideline ***Financial Abuse and Family and Domestic Violence***, November 2016 for more explanation.

14.8. Confirmation of assistance

Clause 28.8 of the Code provides:

> *"We will inform you in writing of our decision whether or not to provide you with any assistance if you are in financial difficulty with a credit facility you have with us and the reasons for our decision. If we agree to provide you with assistance, we will confirm in writing the main details of the arrangements."*

Similarly, the National Credit Code requires a credit provider to respond in writing to a hardship notice[159]. ASIC has, however, provided an exemption from the obligation to confirm in writing a simple arrangement, that is, an agreement that defers or reduces the debtor's obligations for a period of not more than 90 days[160].

[158] Eg Legal Aid NSW Rec 21

[159] National Credit Code sec 72

[160] ASIC Class Order [CO]14/41]

Consumer representatives report that, where financial difficulty arrangements are not confirmed in writing, their consumer clients are sometimes unsure about what the bank has agreed to. For example, they are often unsure whether, at the end of the period of assistance, normal payments resume and the credit facility term is extended or alternatively a lump sum payment or increased periodic payments are required. In discussions with me, they proposed that signatory banks should provide written confirmation where an arrangement applies for a period of 30 days or more or if the debtor requests written confirmation. The Joint Consumer Submission also proposed that clause 28.8 of the Code should be more prescriptive as to contents of a clause 28.8 notice and should require the notice to include the details of the repayments required, what will happen at the end of the arrangement and any adverse consequences for the customer in accepting the arrangement, such as whether the account will be listed as in default or as overdue on the customer's credit report, whether default interest rates or fees will apply and whether the customer's credit card will be cancelled[161].

14.8.1. Discussion

The ABA Industry Guidelines *Promoting understanding about banks' financial hardship programs* provides guidance about confirmation of financial difficulty assistance. It states:

> *"banks will provide their customer with the main details of an arrangement or agreement put in place to deal with the categories of financial difficulty (page 2 of this industry guideline, including financial hardship):*
>
> - *verbally or in-writing if the arrangement or agreement is for a period less than 30 days (a customer can request the notice to be in-writing); and*
> - *in-writing where the arrangement or agreement is for a period of more than 30 days."*
>
> *Importantly, banks should ensure their customers understand what is required of them, especially when a new arrangement is put in place to assist them through the period of financial hardship. The main details might cover:*
>
> - *amount of outstanding debt;*
> - *key aspects of the arrangement (such as an alternative arrangement or repayment plan);*
> - *details of whether the arrangement will affect the credit contract or outstanding debt;*
> - *whether interest is affected and, if so, how interest (existing and accrued) will be managed;*
> - *the duration of the arrangement;*
> - *whether, and at what point, the arrangement will be reviewed; and*

[161] Joint Consumer Submission Rec 12f.

> • *the customer's obligations under the arrangement (so they do not inadvertently default at the end of the arrangement)."*[162]

Consistent with the ABA Industry Guideline, clause 28.8 should be amended to require a signatory bank to provide written confirmation of financial difficulty assistance, either if the customer requests this or if the assistance will span a period of 30 days or more. The clause should also identify the contents of the notice to be given. In particular, in the interests of fully and fairly informing the customer, it is important that the customer is informed of any adverse consequences of a financial difficulty assistance arrangement including adverse credit reporting. If this occurs, future disputes are likely to be minimised.

Recommendation 55

Clause 28.8 of the Code should be amended to require a signatory bank to provide written notification of financial difficulty assistance that it has agreed to provide this to an individual customer if:

- the customer so requests; or
- the assistance will span a period of 30 days or more.

The notice should include the details of the repayments required, what will happen at the end of the arrangement and any adverse consequences for the customer in accepting the arrangement, such as, whether the account will be listed as overdue on the customer's credit report, whether default interest rates or fees will apply and whether the customer's credit card will be cancelled.

This provision should also apply where financial difficulty assistance is provided to a small business in respect of a credit facility below $5 million.

14.9. Guarantor financial difficulty

Clause 28 does not expressly apply to a guarantor of a Code customer. This is because clause 28.1 provides: "This clause 28 applies to a credit facility you have with us. Clause 42 defines "you" to mean the individual or small business that is the signatory bank's customer.

FOS has proposed that the Code should be amended to contemplate financial difficulty assistance for guarantors. This is consistent with FOS's approach where it decides a dispute between a signatory bank and a guarantor. In *The FOS Approach to Financial Difficulty series – Dealing with common issues*, FOS states at para 2.4:

> *"We consider that it is good industry practice to give genuine consideration to a guarantor's financial difficulty; however, the options available to a guarantor will*

[162] ABA Industry Guideline, *Promoting understanding about banks' financial hardship programs,* November 2016, p.10

> *be different to those of a borrower. The options available may include a short-term repayment arrangement or a reasonable time for the guarantor to either refinance the debt with a third party or undertake the sale of assets."*

14.9.1. Discussion

I think that the Code should extend the ambit of signatory banks' financial difficulty assistance obligation to guarantors of Code customers who are in debt to the signatory bank because the bank has made a demand under the guarantee. I see no reason to confine the compassion that underpins financial difficulty assistance to the bank/ customer relationship. While they may not be customers of the signatory bank in their own right, guarantors are often part of the customer's family and a sensible customer relationship approach would be extended to them. As discussed earlier in my report, financial difficulty obligations are a recognition that this assistance is a key part of the banks' social compact which I see as applying equally to guarantors.

The Code should be amended to achieve this and in addition, the ABA and signatory banks, working with consumer representatives, should develop industry guidance as to the options for assistance.

Recommendation 56

The Code should be amended to introduce a financial difficulty assistance regime for guarantors of guarantors of Code customers who are in debt to a signatory bank because the bank has made a demand under the guarantee. The ABA and signatory banks, working with consumer representatives, should develop industry guidance as to the options for assistance.

14.10. Publicising financial difficulty assistance

Clause 28.10 currently commits signatory banks to publicising their financial difficulty processes.

> *"We will make information about our processes for dealing with customers in financial difficulty with a credit facility available on our website (including relevant contact numbers). We will inform you at your request about how to find this information on our website and we will make this information available in another format if you tell us you do not have access to our website."*

There is further detail in the ABA Industry Guideline, Promoting understanding about banks' financial hardship programs:

> *"Banks should ensure information on their websites is suitable, prominent, easily identifiable, and accessible (consistent with the agreed industry standard on website disclosure). For example, banks will provide a 'button' on their*

homepage which links directly to information about the bank's financial hardship program and hardship assistance. The button will be permanently on the homepage. Banks will also provide a FAQs section with information about the types of arrangements that may be available, the hardship process (including assessment of a hardship notice), and what happens when an application is accepted or declined.

Banks acknowledge it is important that customers also have access to information about their hardship programs and practices via other banking channels. Banks will:

- *Make information presented on the website available in hard copy upon request.*
- *provide branch displays (consistent with the agreed industry standard on branch disclosure).*
- *Provide a brochure consistent with the agreed industry standard, including information to raise awareness about the availability of hardship assistance and details about the bank's dedicated financial hardship team.*
- *Promote the availability of information about financial hardship and money management, including providing links to the ABA's 'DoingItTough' website, the Financial Counselling Australia's website, including its "Debt Self Help" tool, and ASIC's MoneySmart website.*

In determining when and how to make this information available, banks should identify relevant branches and other locations as well as other factors (i.e. prominence, times, etc).

To ensure customers can talk to staff members who can help them, banks will make the dedicated financial hardship team available during normal business hours (Monday to Friday). At other times, banks may make other bank staff available to deal with customer queries or alternative processes. For example, some branches may be open outside normal business hours, or call centre staff could direct customers to the bank's website where a hardship notice can be made online, or a message/call back service could refer the query to the dedicated financial hardship team for response during business hours."[163]

The Joint Consumer Submission proposed that clause 28.10 should be expanded upon by requiring branches to have posters and brochures to publicise financial difficulty processes, bank statements and bills to make reference to financial difficulty relief and bank financial difficulty contact details to be published on the signatory bank's EDR scheme website.

[163] ABA Industry Guideline, *Promoting understanding about banks' financial hardship programs*, November 2016, p.16

14.10.1. Discussion

There is legitimate concern that Code customers, if not represented by a financial counsellor or consumer lawyer, may not be aware that financial difficulty assistance is available from their bank. For those customers, signatory banks play a vital role in bringing their financial difficulty processes to the attention of customers.

I am aware that signatory banks promote the availability of financial difficulty assistance using a variety of channels in addition to their website. The CCMC Inquiry Report, *Financial* Difficulty, refers to bank information that promotion takes place via product brochures, account statements, default notices and collections letters, in branches, through call centres and via SMS notifications to customers affected by natural disasters[164].

During my review, I heard of other excellent initiatives by signatory banks, including a signatory bank that undertook a major promotion of its financial difficulty processes in a regional centre that is affected by substantial uncertainty about the fate of a major employer.

Equally, I am aware that the CCMC Inquiry Report found that more could be done to publicise financial difficulty processes. In particular:

> *"While the ABA industry guideline states that the provision of such materials within branches is good practice, only three [out of 44] branches [visited by the CCMC for the purposes of its inquiry] … had posters and 17 branches overall had brochures."*[165]

Given the importance of signatory banks publicising their financial difficulty processes, I think that the Code should incorporate some of the commitments in the ABA Industry Guideline and the practices outlined by banks to the CCMC in the course of its inquiry.

I am not persuaded that signatory banks' EDR scheme website should be required to have financial hardship contact details. Third party website information carries the risk that it will not be updated as changes occur, which would diminish rather than improve accessibility.

Recommendation 57

Clause 28.10 of the Code should be extended to incorporate the additional commitments:

- information about the availability of financial difficulty assistance should be "prominently" displayed on each signatory bank's website and a search for the words "hardship" and "financial difficulty" must find the relevant information;
- each branch should display a poster and brochures about the availability of financial difficulty assistance and how to inquire about this; and
- account statements, default notices and collections letters should advise that financial difficulty assistance is available and how to inquire about this.

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[164] CCMC Inquiry Report *Financial Difficulty*, November 2015, Table 3, p.15-16

[165] CCMC Inquiry Report *Financial Difficulty*, November 2015 p.17

15. TERMS AND CONDITIONS, DIRECT DEBITS AND CHARGEBACKS

15.1. Banking Service terms and Conditions

Clause 3.1(d) of the Code provides:

> *"We will provide information to you in plain language".*

Yet banking service terms and conditions continue to be long and complex, written in legal language. As a number of stakeholders commented, this means that they are inaccessible to all but the most diligent or skilled readers. To address this, there have been proposals that the Code should commit to terms and conditions being in plain English and that they include an executive summary[166].

I agree that banking service terms and conditions are very difficult to read. It seems to me that the risk focus that I discuss earlier in my Report has been at the cost of a customer focus that the Code's plain language commitment is intended to achieve.

I am not, however, persuaded that a new Code obligation, such as an obligation to begin terms and conditions with an executive summary, is the answer. Inflexible drafting 'rules' can have perverse results, eg. an executive summary would further lengthen terms and conditions and may do nothing to ensure that the full terms and conditions are comprehensible.

Rather, it seems to me that a continuous improvement approach is more likely to deliver 'real-world' results. I think that a way to do this is for the existing clause 3.1(d) of the Code to be given more operation. At the moment, it is a commitment that the Code places outside the scope of the CCMC's monitoring and enforcement powers[167]. The rewritten Code should include clause 3.1(d) as an obligation that, like other obligations, the CCMC is able to monitor and enforce (see Chapter 6.5 where I propose a new architecture for the Code). This would permit the CCMC to undertake an own motion inquiry to compare signatory banks' terms and conditions and to work with signatory banks to identify and implement best practice techniques to enhance readability.

Recommendation 58

The redrafted Code should include clause 3.1(d) as an obligation that is capable of being monitored and enforced by the CCMC.

[166] Joint Consumer Submission Rec 7

[167] Code clause 36(b)(iii)

15.2. Cancellation of payment arrangements

Since 2003, the Code has included a requirement that signatory banks must carry out a customer's instructions to cancel a savings or transaction account direct debit arrangement. Clause 21 currently provides:

> *"21.1 We will take and promptly process your:*
>
> *a) instruction to cancel a direct debit request relevant to a banking service we provide to you; and*
>
> *b) complaint that a direct debit was unauthorised or otherwise irregular.*
>
> *21.2 We will not direct or suggest that you should first raise any such request or complaint directly with the debit user (but we may suggest that you also contact the debit user).*
>
> *21.3 Clause 21.1 does not apply to a payment service relating to a credit card account (see clause 22)."*

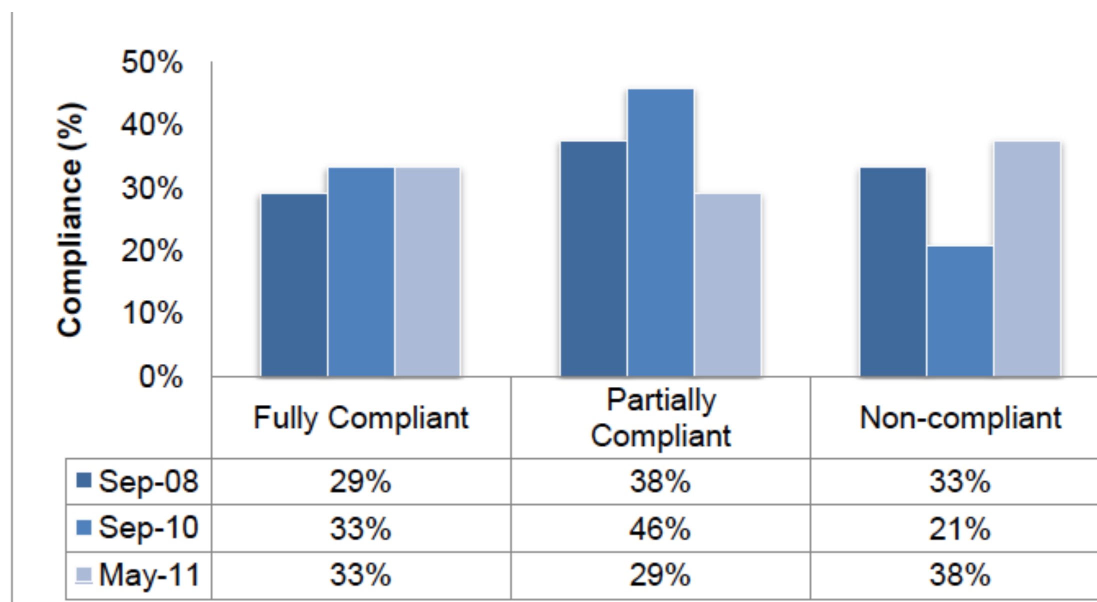
Where a recurring payment arrangement has been set up for a Mastercard or Visa credit or debit card, signatory banks do not organise cancellations of these on behalf of their customers. Instead the customer must tell the merchant to cancel the arrangement. If the merchant fails to do this and makes an unauthorised charge to the card, the customer has to notify their bank that the charge is disputed and the bank is required by clause 22 of the Code to claim the amount back on behalf of the customer (referred to as a chargeback).

In my consultations, I was told by the Financial Counselling Association that financial counsellors continue to find that banks direct their customers to the merchant to cancel savings and transaction account direct debit arrangements (not just Mastercard or Visa card recurring payment arrangements). There were also assertions that signatory banks impose shorter timeframes for a chargeback claim than is available to them under the card schemes and that this unnecessarily disadvantages their customers.

15.2.1. Direct debit cancellations

The CCMC undertook 'shadow shopping' exercises in September 2008, September 2010 and May 2011 to test whether signatory bank staff understood that they are obliged by the Code to act upon a customer's instructions to cancel a direct debit arrangement. The CCMC found a disappointing lack of understanding – and moreover little improvement over this period.

Figure 18. - Compliance with Code direct debit cancellation obligations



Source: CCMC Direct Debits Inquiry Follow Up Report May 2012 p.5

A failure to act upon a customer's direct debit cancellation instruction exposes the customer to more than just inconvenience. There is a risk of fraud (that the customer's account will be depleted by unauthorised transactions) and of unfairly incurring bank fees (that unauthorised transactions will cause the account to be overdrawn, incurring fees for the customer) and of exacerbating financial difficulty. As stated by the CCMC:

> *"The ability for customers to cancel direct debits at their bank is a powerful safeguard for customers especially for those who are in financial difficulty. Failure for banks to accept or act on notice of a direct debit cancellation request may cause members who are already in financial trouble to be further impacted when exception and penalty fees are imposed on the account."*[168]

To test financial counsellors' assertion that direct debit cancellation requests continue to be a source of difficulty, I sought data as to the number of direct debit stop transactions and the number of complaints about direct debit stops. This data is of course only indicative because direct debit complaints are not all necessarily about the failure to promptly cancel a direct debit arrangement and because not every non-compliance ends in a customer complaint.

[168] *Direct Debits Inquiry Follow Up Report*, May 2012, p.5

Figure 19.: Ratio of direct debit complaints to direct debit cancellations

	Average monthly number of direct debit complaints	Average monthly number of direct debit cancellations	Ratio of direct debit complaints to cancellations
Bank 1	9.5	1,123	1: 118
Bank 2	3.2	240	1:75

Source: ABA December 2016

The other data I have looked at is the clause 21 breach data that is self-reported by signatory banks to the CCMC - shown in the next chart.

Figure 20. – Signatory banks' self-reported breaches of clause 21 of Code

Self-reported breaches	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16
Direct debit breaches	16	13	53	59	92	136
Total breaches	2,541	5,794	9,415	3,969	6,577	7,987
Direct debit breaches as % of total breaches	0.6%	0.2%	0.6%	1.5%	1.4%	1.7%

Source: CCMC Annual Report 2015/16

To understand the instructions being provided by signatory banks to their staff, I sought example direct debit stop request procedures. The provided example procedures clearly specified that the signatory bank is obliged to act on a customer's request to stop a direct debit arrangement. If these procedures are representative of those of other signatory banks, I can only assume that the instances of non-compliance are because of inadequate staff training by signatory banks.

Exercising my mind is the question of what to recommend to address this long-standing problem. The Joint Consumer Submission has proposed wording changes to clause 21: replacing "promptly" with "immediately" and removing the reference in clause 21.2 to the possibility of the signatory bank suggesting to the customer that they also contact the merchant.

I am not persuaded that the problem is with the wording of clause 21. Rather it seems to me that the problem is one of compliance with clause 21 as the CCMC found in both 2008 and 2012. It is, however, apparent that the CCMC's recommendations for enhanced staff training and monitoring have led to little change.

So, it seems that the problem may be small in number of instances, but has persisted for years, the problem can have significant consequences for customers, signatory banks have been alerted to the issue multiple times, they have had standing recommendations from the CCMC and as far as I can establish, the instructions to bank staff are clear. What to recommend?

One approach that has not been tried is the Joint Consumer Submission proposal that the Code should specify a cash penalty for where a signatory bank fails to comply with clause 21. Tempting as it is to try this approach, as discussed later in my Report, I think that a cash penalty regime does not sit well with a best practice voluntary Code.

Rather I think that this is something that needs to be internally addressed by signatory bank management, and of course, it is not my role to delve into this. I have, however, been asked by industry to consider the merits of the Code requiring signatory banks to have a Customer Advocate (see Chapter 19.2) and it seems to me that this is an issue where the signatory banks' new Customer Advocates could demonstrate their ability to have influence over bank priorities.

No doubt they will need some mix of analysis and monitoring of internal complaints data, access to training packages, profile raising activities, shadow-shopping and other research tools, the ability to sufficiently prioritise this issue on the agendas of busy line executives, some compensation for disappointed customers and some mechanism for the consequences of the problem to be felt within management. While I understand that Customer Advocates' roles are new, it seems to me that this is a perfect (small scale) test with the distinct advantage that it will be keenly observed by external stakeholders.

This exercise could also be used as a test run of the new proposed role for the CCMC, with signatory banks reporting regularly to the CCMC to ensure that there is public visibility of the efforts to improve performance in this area.

Recommendation 59

Signatory banks' Customer Advocates should be tasked with championing better customer service in relation to direct debit cancellation requests. They should work with internal management to achieve this, using all the resources and tools that they will need to be effective in their roles over the long term.

Signatory banks' Customer Advocates should report regularly to the CCMC as to the steps the signatory bank is taking to enhance compliance by staff with customer direct debit cancellation requests and the impact those steps are having.

The CCMC should publicly report on signatory banks' progress in improving compliance with direct debit cancellation requests, including by releasing signatory banks' data on an anonymised basis, together with the CCMC's trend analysis and assessment of the adequacy of signatory banks' efforts.

15.2.2. Direct debit cancellation fees

In its 2014-15 Annual Report, the CCMC reported the steps it had taken to discourage signatory banks from charging a fee for cancelling a direct debit arrangement and that only one bank was persisting in doing this[169]. I understand from the ABA that there are now no signatory banks that charge a fee for cancelling a direct debit arrangement. I welcome this voluntary practice by the banks. The need from time to time to cancel a direct debit arrangement is a necessary cost of the automation of the payment system which has brought great efficiencies for banks. It is I think, fair that banks bear these costs without recovering specifically for associated costs.

15.2.3. Cancellation of recurring payment arrangements (credit card)

The Joint Consumer Submission stated that credit card recurring payment arrangements are increasingly common and are encouraged by banks through the establishment of loyalty schemes[170]. Further customers often establish these arrangements unaware that their bank will not assist them with cancellation should the need arise.

Industry has told me that there are technology and system limitations that prevent signatory banks from cancelling a recurring payment arrangement through a credit card. In the case of the Visa card scheme, I understand that the scheme platform does not currently include facility for a bank to cancel a recurring payment arrangement. In the case of the Mastercard scheme, I understand that banks can establish a facility that enables them to cancel at least some recurring payment arrangements, but that there is a cost payable by the bank to Mastercard and as a consequence few, if any, signatory banks currently have taken up this facility.

I think that this situation is quite unsatisfactory from the point of view of customers. If a customer is in dispute with a merchant who refuses to cease deduction, the customer is in an invidious position if the customer is unable to instruct their bank to stop a recurring payment arrangement. The customer's only recourse is to respond to each payment put through by the merchant and instruct their bank to exercise their chargeback rights – or alternatively cancel their card (something I understand can be difficult to achieve where recurring payments are charged)..

Signatory banks earn interchange fees for each purchase under a credit card recurring payment arrangement. Failure by signatory banks to assist with cancellation of credit card recurring payment arrangements has a somewhat regrettable appearance of willingly paying the cost of establishing recurring payments but protecting the bank's income stream by not supporting cancellation. I think that it is reasonable for the public to expect that part of the cost of obtaining recurring payments fees is the cost of enabling customers to switch them off.

Signatory banks should discuss this issue with card scheme companies and work towards implementing a solution over a reasonable timeframe. Whilst, I accept that there will be costs incurred by signatory banks as a result, I think that these costs should not be passed on as an additional visible impost to customers. Rather these costs should be factored into interchange fees and seen as a cost of the convenience for merchants of recurring payment arrangements.

[169] CCMC 2014-15 Annual Report p.13

[170] Joint Consumer Submission p.64

Again, to give public visibility to this initiative, I think that the industry should keep the CCMC appraised about progress in relation to this and the CCMC should be responsible for publicly reporting about this project.

Recommendation 60

Signatory banks should work with card scheme companies to build functionality and processes to enable signatory banks to carry out customer requests to cancel card recurring payment arrangements. The aim should be to put this in place within two years. The CCMC should be kept appraised of progress in relation to this and should report about this in its Annual Reports. Once the required functionality and processes are in place, signatory banks should undertake to carry out their customers' recurring payment arrangements cancellation requests free of charge.

15.3. Credit card chargebacks

Amongst this collection of issues raised with me are credit card chargebacks, where a customer is able, in some circumstances and under the rules of the credit card scheme, to claim back a disputed credit card transaction.

Clause 22 of the Code states:

> *"22.1 If you have disputed a card transaction with us within the required timeframe, we will, in relation to a credit card or, where relevant, a debit card transaction (including an unauthorised payment debited to your card account pursuant to a recurring payment arrangement):*
>
> *a) claim a chargeback right, where one exists, for the most appropriate reason; and*
>
> *b) not accept a refusal of a chargeback by a merchant's financial institution unless it is consistent with the relevant card scheme rules.*
>
> *22.2. We will make available general information about chargebacks on our website or by electronic communication to you and we will notify you of the availability of this information on or with the relevant card statement of account at least once every 12 months."*

Australian Consumer Law regulators established a National Credit Card Chargebacks Project[171] to improve regulators understanding of the way chargebacks work. The purpose of the project was to enable regulators to assist consumers in disputes with traders. I have been provided with a summary of the high level findings of the Project. These include that:

[171] www.consumerlaw.gov.au/the-australian-consumer-law/acl-national-projects/

- consumers have limited understanding of their chargeback rights and are not getting the full benefit of their chargeback rights;
- there is a degree of inconsistency in the way that banks and their staff are presenting information about chargeback; and
- timeframes for consumers to exercise chargeback rights are often unclear and varied without communicating these changes to consumers.

15.3.1. Discussion

I think clause 22 needs a re-write in plain language that strips away the current legalistic language. As part of this, the clause should state that signatory banks cannot impose a shorter timeframe for making a chargeback claim than that available under the credit card scheme rules (currently, as I understand, 3 months). (I have been told that signatory banks do not in any event impose a shorter timeframe than under card scheme rules, so if the Code made this requirement, there would be no systems or other practical issues for signatory banks.)

Also, it is clear from the findings of the National Credit Card Chargebacks Project that signatory banks need to do more to build customer awareness of the chargeback process. This can be partly addressed through a principles-level obligation in the Code, for example, that signatory banks must provide clear and prominent information to card holders about what they should do about unauthorised card transactions, both at the time of issue of a card and at regular intervals thereafter.

I think that more is likely to be required to address an issue that is clearly of substantial concern to regulators. For example, an ABA advertising campaign may be necessary. To the extent that individual action by signatory banks may be appropriate, an Industry Guideline may be required. I recommend that the ABA and signatory banks should develop and implement a plan of response to address those aspects of the findings within their purview. The CCMC should be kept informed about progress and publicly report about this work.

Recommendation 61

a) Clause 22.1 of the Code should be amended to prevent signatory banks from imposing a shorter timeframe for making a chargeback claim than that available under the credit card scheme rules.

b) Clause 22.2 of the Code should be amended to require signatory banks to provide clear and prominent information to card holders about what they should do about unauthorised card transactions. This information should be provided both at the time of issue of a card and at regular intervals thereafter.

c) The ABA and signatory banks should develop and implement a plan of action to make Code customers more aware of their chargeback rights and to better help them to access those rights. The CCMC should be kept informed about progress and publicly report about this work.

16. FEES

Bank fees have been under the spotlight in successive Parliamentary and Government Inquiries[172] and were raised again in submissions to my Review. I have, however, been reluctant to engage in a broad ranging consideration of bank fees. There are a few reasons for this. Signatory banks must, of course, fund their operations and fees are a legitimate part of this. It is neither my role, nor do I have the expertise, to assess the fairness of fees and how well competitive forces are operating so far as bank fees are concerned.

Other bodies have been entrusted this role. The Government has decided that the Productivity Commission should periodically review financial sector competition[173]. In addition, the House of Representatives Standing Committee on Economics has recommended that the Australian Competition and Consumer Commission or proposed Australian Council for Competition Policy monitor competition in the banking sector more closely, including to "improve[e].. the sector's accountability for its conduct and the pricing of interest rates and fees"[174].

I have, therefore, confined my consideration about fees to three issues:

1. whether there are weaknesses in the approach to disclosure of banking service transaction fees that are contributing to public lack of trust in signatory banks;
2. whether the Code is keeping up with best practice in relation to default fees, recognising that these are not susceptible to competitive pressures through disclosure; and
3. whether, consistent with signatory banks' preparedness to reduce transaction account fees for disadvantaged members of the community, there are other fees where there is a case for some fee relief for those members of the community.

Reference should also be made to Chapter 15.2 for my recommendation that the Code should prohibit signatory banks from charging a fee for cancelling a direct debit arrangement and to Chapter 18 for my recommendation that the Code should require fee relief for customers who receive post mailed account statements and who do not have a home internet connection.

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[172] Senate Economics References Committee Inquiry, *Access of Small Business to Finance*, June 2010, the Financial System Inquiry, November 2014, the Senate Economics References Committee Inquiry, *Interest rates and informed choice in the Australian credit card* market, December 2015, the Parliamentary Joint Committee on Corporations and Financial Services Inquiry, *Impairment of Customer Loans*, May 2016 and most recently the House of Representatives Standing Committee on Economics, *Review of the Four Major Banks First Report*, November 2016

[173] Australian Government, Attachment: Government response to Financial System Inquiry Recommendations,<http://www.treasury.gov.au/PublicationsAndMedia/Publications/2015/Govtresponse-to-the-FSI

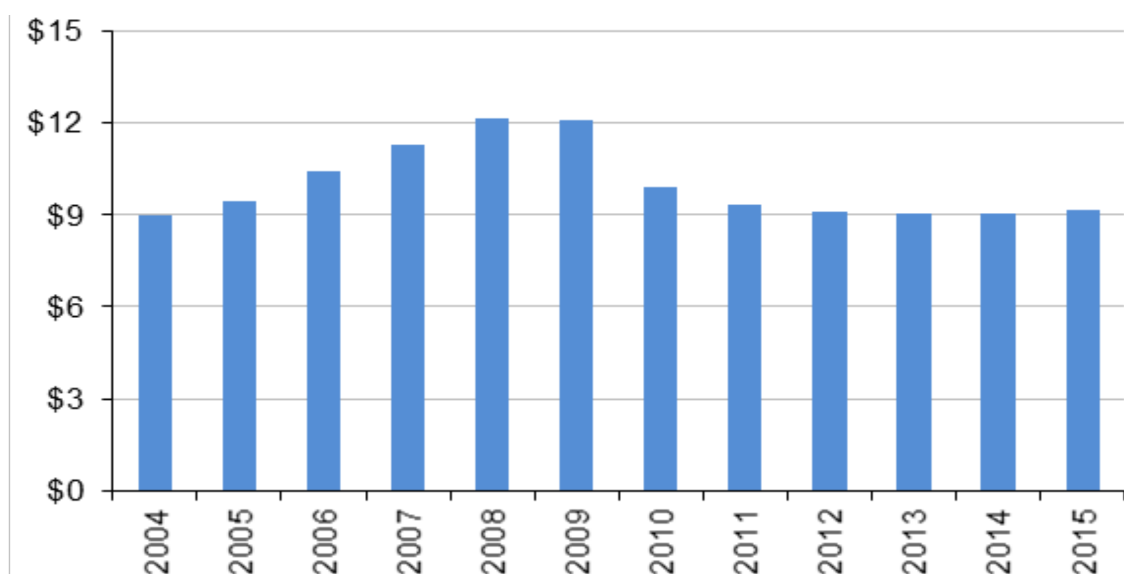
[174] House of Representatives Standing Committee on Economics, Review of the Four Major Banks First Report, November 2016, Recommendation 3

16.1. Background

The Joint Consumer Submission pointed to Reserve Bank of Australia analysis that bank fees grew in 2014 at a faster rate than the consumer price index, with credit card fee growth of 5.9% particularly highlighted[175]. The Reserve Bank of Australia analysis concluded, however, that the growth in fees in 2014 was primarily driven by volume rather than increases in unit fees[176]. In 2015, domestic banking fee income grew by 3.5% "reflecting moderate increases in fees paid by both households and businesses, driven by a combination of volume growth and increases in some unit fees"[177].

The ABA has provided me with analysis that over the last 5 years that the amount of bank fees paid on average by households has been steady at around $9.00 per week.

Figure 21. - Average weekly bank fees paid by households



Source: ABA November 2016

The following tables use Reserve Bank of Australia data to show the aggregate banking product fees of various types.

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[175] Wilkins, Banking Fees in Australia, Bulletin, June Quarter 2015http://www.rba.gov.au/publications/bulletin/2015/jun/pdf/bu-0615-5.pdf

[176] Wilkins, *Banking Fees in Australia,* Bulletin, June Quarter 2015 *p.39* "In 2014, domestic banking fee income grew by 2.8 per cent, to around $12 billion. This reflected moderate increases in fees paid by both households and businesses, largely driven by volume growth rather than increases in unit fees."

[177] Wilkins, *Banking Fees in Australia, Bulletin, June Quarter 2016* p.43 http://www.rba.gov.au/publications/bulletin/2016/jun/6.html

Figure 22. - Fees from household products

Type of fee	2015 $m	%
Transaction accounts		
Account Servicing	$299	29%
Transaction	$271	26%
Exception fees	$332	32%
Other fee	$132	13%
Total	$1,034	100%
Housing loans		
Account Servicing	$956	77%
Transaction	$43	3%
Exception fees	$32	3%
Other fee	$219	17%
Total	$1,250	100%
Personal Loans		
Account Servicing	$299	80%
Transaction	$8	2%
Exception fees	$19	5%
Other fees	$50	13%
Total	$376	100%
Credit Cards		
Account Servicing	$648	43%
Transaction	$159	11%
Exception fees	$212	14%
Other	$484	46%
Total	$1,503	100%

Source: ABA November 2016 – numbers from 15 banks surveyed

Figure 23. - Fees from small business products

Type of fee	2015 $m	%
Deposit Accounts		
Account Servicing	$240	59%
Transaction	$111	28%
Exception fees	$36	9%
Other	$16	4%
Total	$404	100%
Loans		
Account Servicing	$1,173	85%
Transaction	$58	4%
Exception fees	$37	3%
Other	$105	7%
Total	$1,373	100%

Source: ABA November 2016 – numbers from 15 banks surveyed

16.2. Banking service transaction fees

16.2.1. Introduction

The Joint Consumer Submission noted that banks are responding to internet and phone banking by providing innovative services that assist customers to manage their finances. Whilst this was welcomed, the Submission expressed concern that fees are not always as transparent to customers as is desirable. The Joint Consumer Submission gave the example of a dishonour alert service where the following information is provided at the time of the customer opting in to the service.

> *"This alert notifies you when an account has been overdrawn by a cheque, direct entry or periodical payment. Upon receipt of a dishonour alert you may wish to reverse this by depositing funds into your account accordingly by 1:30PM, that day. You will be charged an honour fee to have the dishonour reversed.*
>
> *Note: We, and all of the third parties we rely upon to provide the Alerts Service are not liable or responsible for any failure or delay in transmitting information to you or any error or failure in such information. We are not liable to you or responsible for losses arising from any industrial action, or any cause beyond our reasonable control including (but not limited to) any equipment or electronic or mechanical failure or malfunction, the failure of your Electronic Equipment to receive information, or telecommunications breakdowns. We are not liable to you if you suffer loss due to an Alert not being received accurately or at all. If you fail to ensure the security of your Electronic Equipment, or if you fail to notify us of a change in your email or SMS details, we have no liability to you in respect of any loss or damage that may occur after transmission of any Alert by us. You acknowledge that we are not responsible for any loss or damage caused to your data, software, computer, Electronic Equipment or other equipment caused by your use of the Alerts Service."*[178]

Aside from the unfortunate ratio of 'promise words' to ' qualification words', the issues here are that the amount of the honour fee is not specified at the time of the customer opting in to the service, nor is there a reference to where the amount of the fee might be found, and when the service is utilised there is no reminder that an honour fee applies.

16.2.2. Discussion

The Code requires some fees to be disclosed in a contemporaneous way. However, clause 18.1 requires an application fee to be disclosed in advance of a customer becoming liable to pay it. Also clause 17 requires advance disclosure of fees for bank cheques and certain other services. It provides:

> *"Where we charge you for the provision of a bank cheque, an inter-bank transfer or like service, we will disclose the fee or charge to you when the service is*

[178] Joint Consumer Submission p. 59 - 60

> *provided, or at any other time on request, except where the relevant banking service is regulated by Chapter 7 of the Corporations Act 2001."*

Similarly the ePayments Code requires ATM fees to be disclosed before the ATM user completes the transaction – and must allow the user to cancel the transaction at no cost after receiving that disclosure[179].

I think that it would be appropriate to update clause 17 of the Code to encompass modern day banking services transaction fees. The general principle should be that the amount of the fee is disclosed (or, where the fee is referrable to the size of the transaction, the method of calculation should be disclosed) and this should occur immediately prior to each transaction that results in the fee being incurred (as is the case for ATM transactions). To do otherwise is to invite customer criticisms that the signatory bank is deliberately hiding the fee in a way that is ''tricky' and which relies upon the customer to question the bank about the quantum of the fee or to check their statement carefully to detect the fee.

Given that there are a complex range of fees that are currently utilised, as part of the Code redrafting process, industry will need to work with the drafters to identify the fees that properly fall within the ambit of this recommendation.

Recommendation 62

Clause 17 should be redrafted to apply more generally to banking service transaction fees. The general principle should be that the amount of the fee is disclosed (or, where the fee is referrable to the size of the transaction, the method of calculation of the fee) each time that the customer is invited to use the banking service.

16.3. Default fees

Default fees (sometimes called exception fees) include dishonour fees, late payment fees and over limit fees. As can be seen from Figure 21, default fees represent about a third of fees levied on household transaction accounts and about a seventh of the fees levied on household credit cards. Because loan fees are typically much higher than account fees, default fees represent a lower proportion of loan fees, both for households and small business.

The Parliamentary Joint Committee on Corporations and Financial Services' *Impairment of Customer Loans Report* referred to submissions made to the Committee about excessive loan default fees [180]. The Inquiry recommended that default fees and interest should be contained to the increased cost incurred by the bank as a result of the impairment of the loan[181].

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[179] ePayments Code cl 6

[180] Parliamentary Joint Committee on Corporations and Financial Services Inquiry, *Impairment of Customer Loans*, May 2016, p.21

[181] Parliamentary Joint Committee on Corporations and Financial Services Inquiry, *Impairment of Customer Loans*, May 2016, Recommendation 1c.

Similarly, the Joint Consumer Submission to my Review expressed concern about default fees, arguing that competitive pressures do not moderate default fees and that they are levied in a regressive way, with the burden falling most heavily on those who are least able to afford them. The Submission proposed that the Code should:

> *"a. examine their fee structures to address the extent to which any of their fees are regressive;*
>
> *b. limit the charging of fees for breaches of terms and conditions or default to the maximum of the direct costs incurred as a result of the breach".*[182]

The recent decision of *Paciocco v Australia and New Zealand Banking Group Ltd*[183] potentially creates a different impetus. That case held that it is not unconscionable for banks to set late payment fees taking into account a broad range of considerations including the direct operational costs incurred by the bank in relation to late payments, the costs of loss provisioning and increases in regulatory capital and even the bank's profit making aspirations.

16.3.1. Discussion

I accept that the *Paciocco* decision provides the court's assurance that it is not illegal for banks to charge fees taking into account a very broad range of considerations. In a program of reform based on restoring trust between signatory banks and customers, it would seem to me, however, that legality is not the main issue. A proportion of customers think that the default fees being charged by banks are unfair, because they are often unexpected or counter-intuitive and because the amount being charged seems intuitively disproportionate to the service or the customer's 'offence'.

It seems to me that there is quite some sensitivity to fees, and in particular to default fees and a strong community expectation that a new Code will address this question – and I cannot see how the industry could not make some gesture in this space.

I have looked to the example of other codes of practice. Paragraph 5.2 of the Customer Owned Banking Code of Practice provides:

> *"We will make sure any exception fees we charge (including credit card late payment fees, account overdrawn or dishonour fees, direct debit dishonour fees, cheque dishonour fees, and ATM failed transaction fees) are reasonable having regard to our costs. Our costs include charges imposed by our service providers, where applicable."*

This formulation does not distinguish direct and indirect costs and customer owned banks of course, do not have the same obligation to return a profit to shareholders, however it seems to me that signatory banks need at minimum, to include a similar commitment to be seen to be meeting best practice and addressing the issue.

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[182] Joint Consumer Submission Rec 20b.

[183] [2016] HCA 28

I am reluctant to go further than this and support the Joint Consumer Submission's formulation that default fees should reflect only "direct costs". First, the economic and costing arguments around what is or is not 'in' for the purpose of establishing costs are complex and beyond my expertise. Second, I think these are matters of judgement and likely open to endless argument. Finally, I am loathe to recommend including detail prescription about this in the Code.

I note however that a formulation similar to the Customer Owned Banking Code of Practice would mean that default fees could not include a direct contribution to profits. I also understand that 'applying a margin' is an entirely common business practice. I understand that to apply restrictions in only one class of fees might simply be offset elsewhere. I understand that the actual effect may be more symbolic than real. Nevertheless, I think that this would be seen as a trust-building concession by stakeholders. It is difficult to see how any lesser formulation would be taken as a positive.

Recommendation 63

The Code should include a new provision that obliges a signatory bank to set default fees that are reasonable having regard to the signatory bank's costs. A broad definition of default fees should be included in the Code to give this provision a wide reach.

16.4. Fee relief

Signatory banks often recognise that there are situations where some members of the community are under a particular disadvantage that warrants fee relief. For example, most signatory banks are involved in an initiative with the Australian Government launched in December 2012 to provide fee-free ATM services to those in remote communities[184].

In a similar vein, the Joint Consumer Submission argued that there are circumstances in which signatory banks should waive fees for the provision of documents. Clause 13.7 of Code currently provides:

> *"We may charge you a reasonable fee for providing you with a copy of a document under this Code."*

The Joint Consumer Submission noted reports of charges of as much as $7.00 to provide a document. The Submission argued that this is unreasonable and that banks should develop a list of circumstances in which a charge for the provision of statements or documents will not be made, including where documents or computer access has been lost due to family violence or natural disaster and where the customer has a Centrelink benefit as the main source of income.

[184] http://banking.treasury.gov.au/content/atms.asp

16.4.1. Discussion

I understand from signatory banks that they frequently waive document fees in deserving circumstances. I think that it would be appropriate for the Code to acknowledge this.

My view is that any waiver of fees should (as now) be at the discretion of a signatory bank, rather than by right in specific circumstances. I do not favour a list of examples of where a waiver of document fees may be appropriate. This is likely to become out of date and a list of examples can serve to narrow a provision even where inclusive language is used.

Recommendation 64

Clause 13.7 of the Code should be amended by adding in the words "but we will waive our right to a fee where we think your circumstances warrant this".

17. SALES PRACTICES INCLUDING INSURANCE CROSS SELLING

There has been world-wide concern about mis-selling by banks. United States authorities have reached settlements of more than $50 billion from banks in connection with their mis-selling of residential mortgage-backed securities pre-GFC [185]. Wells Fargo was in the spotlight last year in relation to its sales practices. In the United Kingdom, it is estimated that nearly £25 billion has been paid to consumers since 2011 as compensation for payment protection insurance mis-selling, largely by banks[186].

In Australia, the industry have responded to community concern about bank sales practices by establishing an independent review by Stephen Sedgwick AO of product sales commission and product based payments and other incentives. The aim is to ascertain how these might motivate retail bank staff to focus on their own financial interests, rather than those of their customers and what changes should be made in bank-to-staff practices. This review is due to report in late March 2017 and will address implementation issues. Given competition and other issues, it is not clear at this stage what the implementation mechanism will be for the review's recommendations.

With this context, I consider in this Chapter bank staff-to-customer practices and what changes to the Code should be made in relation to these to promote responsible sales practices.

17.1. Current requirements in relation to cross-selling

Although the Code applies to the distribution by banks of other financial institutions' products[187], the Code does not have any provisions that are specific to this activity. However the general commitment in clause 3.2 of the Code is relevant:

> *"We will act fairly and reasonably towards you in a consistent and ethical manner. In doing so we will consider your conduct, our conduct and the contract between us."*

There are legislative protections that apply, at least in relation to the selling of insurance by a provider of consumer credit[188]. The National Credit Code provides that a credit provider must not require the consumer to take out consumer credit insurance or, in the case of other types of insurance, specify which insurer the consumer must use. Other protections include a cap on commission paid to a distributor of consumer credit insurance.

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[185] Financial Times,29 September 2016, *US seeks pre-election settlement of bank mis-selling claims*, US Department of Justice Media Releases 17 and 18 January 2017

[186] The Guardian, 2 August 2016, Treanor, J: *PPI claims – all you need to know about the mis-selling scandal*,

[187] See Code sec 43 definition of "banking services"

[188] National Credit Code Part 8

17.2. Stakeholders’ proposals

The Joint Consumer Submission proposed that the Code should include commitments that arise from the Independent Review of Product Sales Commission and Product Based Payments. In addition, the Code should institute suitability requirements for all sales within banks and a mandatory delay between the sale of a primary product (for example a loan product) and an add-on product (for example consumer credit insurance). Other proposals included the prohibition of sales of add-on products via an opt-out mechanism[189].

Legal Aid NSW’s submission proposed that the Code should include an obligation that marketing and advertising is undertaken in an appropriate and responsible way including the prohibition or restriction of high pressure sales techniques including cold calling[190]. In addition, the Code should require bank staff who sell add-on insurance with any credit product to have qualifications to provide financial advice and be obliged to advice a customer about the suitability of insurance[191].

17.3. High pressure sales techniques

In 2011, ASIC issued a report detailing significant problems with the way in which consumer credit insurance was being sold to consumers by authorised deposit-taking institutions, including “pressure tactics and harassment being used to induce consumers to purchase [the insurance]”[192]. ASIC’s report expressed concern about:

1. staff persisting with an insurance sales pitch to a consumer who has clearly indicated they do not wish to purchase the product;
2. the practice of keeping consumers ‘captive’ until after the insurance sales pitch has been completed;
3. using the insurance cooling-off period as a selling point;
4. highlighting the risks of not having insurance if the consumer became sick or unemployed, without providing information about other alternatives such as financial hardship variations; and
5. deliberately masking the cost of the insurance in the loan repayment.

I share ASIC’s concern about these practices which are neither consistent with the Code’s current commitment to fair, reasonable and ethical behaviour nor the new Principles that I propose for the redrafted Code (see Chapter 6.7).

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[189] Joint Consumer Submission Rec 28

[190] Legal Aid NSW Rec 27

[191] Legal Aid NSW Rec 28

[192] ASIC Report 256 *Consumer credit insurance: A review of sales practices by authorised deposit-taking* institutions, October 2011, Part C

The Code should be amended to include a new obligation that signatory banks must ensure that their staff and authorised representatives, when promoting or selling financial services or products to Code customers, do this in a fair and ethical manner, without engaging in pressure sales techniques. This wording would build upon the language used in existing clause 3.2 of the Code. The principle of fair and ethical selling should apply to sales of all financial services and products. For this reason, I am not proposing that the provision should be limited to sales of insurance, even though the sales issues have arisen most visibly in that domain.

Recommendation 65

The Code should require signatory banks to ensure that their staff and authorised representatives, when promoting or selling financial services or products to Code customers, do this in a fair and ethical manner, without engaging in pressure sales techniques.

17.4. Customer consent

In its 2011 report about consumer credit insurance sales practices, ASIC also expressed concern about consumers being sold insurance without their knowledge or consent[193]. ASIC's review focused on telephone sales and found scripting that used ambiguous language and failed to clearly seek the consumer's consent to acquire the insurance product.

In the case of online sales of consumer credit insurance in conjunction with, for example, credit cards, it is not clear to me whether or to what extent signatory banks' representatives currently use an opt-out mechanism to sell the add-on insurance (an opt-out mechanism is a default mechanism that pre-selects a purchase and has to be overridden by the customer to avoid the sale). It is, however, clear that if this occurs, it is not good practice. As stated by the UK Financial Conduct Authority:

> *"opt-out selling results in consumers purchasing products that they would not otherwise have bought and may not need. …opt-out selling of add-ons undermines competition because consumers are unable to make effective purchasing decisions and exploits consumer biases."*[194]

[193] ASIC Report 256 *Consumer credit insurance: A review of sales practices by authorised deposit-taking institutions*, October 2011, Part C

[194] Financial Conduct Authority, *General Insurance Add-ons Market Study – Proposed Remedies: Banning opt-out selling across financial services and supporting informed decision-making for add-on buyers*, March 2015, Consultation Paper CP15/13

With effect from 1 April 2016, the Financial Conduct Authority has introduced a requirement that a customer's active consent must be obtained where an optional additional product is sold in conjunction with a regulated financial services primary product[195]. This applies to commercial customers as well as individual customers.

I recommend that the Code include a provision that signatory banks must be able to evidence their customer's explicit consent to the acquisition from or through them of a financial service or product. This should be drafted in such a way as to prohibit the use of an opt-out mechanism for an add-on sale and to make it clear that an ambiguous telephone sale script would not constitute evidence of explicit consent. The provision would apply to a sale of insurance as an add-on to a primary product – a situation that is perhaps particularly prone to raise issues of consent – but would not be restricted to that situation given that the principle of customer consent applies to all sales.

Recommendation 66

The Code should prohibit a signatory bank from charging a Code customer for the acquisition of a financial product or service from or through the signatory bank unless the signatory bank is able to evidence that the customer's explicit consent was obtained at the time of the acquisition.

17.5. Consumer credit insurance

In its 2011 report, ASIC set out its analysis from a 13 month study of consumer credit insurance sales practices by 15 authorised deposit taking institutions. ASIC noted that authorised deposit taking institutions are not the only distributors of consumer credit insurance but that most complaints to ASIC related to this distribution channel[196]. Like ASIC, I have not been able to find publicly available information about the market share of the various distribution channels for consumer credit insurance.

[195] United Kingdom Conduct of Business sourcebook 2.5

[196] ASIC Report 256 *Consumer credit insurance: A review of sales practices by authorised deposit-taking institutions*, October 2011, p.14

ASIC's report noted that consumer credit insurance is not often actively sought out by consumers[197]. Yet there is a high conversion rate for the product (nearly 20% of consumers who had taken out home loans, personal loans or credit cards from 15 authorised deposit taking institutions during the period of ASIC's research project)[198]. This was despite the industry high rate of declinatures for consumer credit insurance (13% in 2010 as compared with 2% for all personal general insurance claims) and the relatively low ratio of benefits to premiums (34% in 2010)[199]. ASIC found that, during its 13 month review period, 13.8% of consumer credit insurance policies were cancelled for reasons other than closure of the loan. In light of this data, ASIC attributed the high conversion rate to the sales practices of the authorised deposit taking institutions. ASIC made ten recommendations to reform those sales practices. In a follow up report, ASIC stated that the 15 authorised deposit taking institutions involved in ASIC's review had agreed to adopt and implement the recommendations set out in Report 256 to improve CCI sales practices[200].

I sought information to test whether the conversion rate for consumer credit insurance has declined since the time of ASIC's report. I posited that if the conversion rate has declined significantly this may suggest that sales practices have moderated in response to ASIC's recommendations. Unfortunately the industry was not able to provide data to test whether this was the case.

What I do have is the preliminary work of the Independent Reviewer of Retail Banking Remuneration which clearly demonstrates that banks are continuing to set targets and incentivise their staff to cross-sell consumer credit insurance. In an Issues Paper dated 17 January 2017, the Reviewer stated:

> *"Such targets seem to carry particular risks of inappropriate outcomes, especially for products that are discretionary add-ons to the primary product such as insurance products sold in conjunction with a line of credit or a mortgage. An example is the sale of credit insurance to a credit card holder who was ineligible ever to make a successful claim on the policy as set out in the Consumer Action Law Centre submission. A number of banks employ cross-sales targets or measures to encourage customer-facing staff to have conversations intended to assist customers identify and meet their needs for financial services (and thus identify sales opportunities for the bank).*
>
> *I have tentatively concluded that cross-sales targets, especially those that are used as a gateway to access rewards otherwise available to a Seller (or a modifier*

[197] ASIC Report 256 *Consumer credit insurance: A review of sales practices by authorised deposit-taking institutions*, October 2011, p.5

[198] ASIC Report 256 *Consumer credit insurance: A review of sales practices by authorised deposit-taking institutions*, October 2011, p.6

[199] ASIC Report 256 *Consumer credit insurance: A review of sales practices by authorised deposit-taking institutions*, October 2011, p.5

[200] ASIC Report *Consumer credit insurance policies: Consumers' claims experiences* 361 p.8

> *to increase the reward otherwise available), significantly increase the risk of mis-selling."*[201]

Whilst I recognise that signatory banks are not the only distributors of CCI, I think that it is entirely consistent with the Code's best practice mantra for signatory banks to provide leadership and commit to reformed sales practices. This may encourage customer owned banks and other distributors of CCI to follow their lead, but I do not think that discussions with other industry bodies and participants should slow Code momentum in this important area. I recommend that the Code should be amended to include the following specific requirements that build upon ASIC's recommendations.

1. Consumer credit insurance must not be promoted to an individual customer where the signatory bank's representative should have been aware that the individual is not suited to the policy[202].

   This would not prevent the sale of insurance to the customer on a 'no advice' or 'general advice only' basis – a signatory bank would not be required to undertake a full assessment of the suitability of the insurance policy for the customer. But equally, where a signatory bank's credit application process reveals matters that mean that a customer is unsuited for consumer credit insurance (for example, ineligibility to claim on all components of the policy being sold to the consumer), the signatory bank would not be able to ignore this.

2. Consumers should be provided with prominent, timely and sufficient disclosure to enable them to make an informed decision as to whether to purchase the product[203].

3. Signatory banks should ensure that their consumer credit insurance sales processes are tailored appropriately to meet the needs of customers, including those not familiar with consumer credit insurance[204].

4. An individual customer's application for consumer credit insurance must not be completed earlier than the day after information is provided to the customer about consumer credit insurance. This would give the customer a little time to consider the features of consumer credit insurance and whether the insurance is suitable for their needs. Moreover the sale may only be completed if the customer contacts the signatory bank to proceed with the application – a signatory bank representative would not be allowed to follow up the customer to see if the customer wants to proceed.

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[201] Stephen Sedgwick, *Retail Remuneration Review Issues Paper*, 17 January 2-17 p.45 - 46

[202] See ASIC Report 492 *A market that is failing consumers: The sale of add-on insurance through card* dealers, September 2016, para 185

[203] See ASIC Report 361 *Consumer credit insurance policies: Consumers' claims experiences*, July 2013, Table 1 p.9

[204] See ASIC Report 361 *Consumer credit insurance policies: Consumers' claims experiences*, July 2013, Table 1 p.9

My deferral period recommendation borrows from the United Kingdom obligations for sales of Guaranteed Asset Protection insurance (insurance cover offered as a supplement to car insurance) introduced to address the "structural point-of-sale advantage" associated with an add-on mechanism that "has a clear impact on consumer behaviour and often affects consumers' decision-making, weakening engagement"[205].

In my view, this is equally true for consumer credit insurance. Like Guaranteed Asset Protection insurance, consumer credit insurance is sold to customers whose interest and focus is the main product they are acquiring (for consumer credit insurance, this is the home mortgage, car loan or credit card), with the result that minimal attention is often given to the merits and costs of the add-on (the consumer credit protection insurance).

Stakeholders expressed very different views to me about a deferral period. The Joint Consumer Submission suggested a 14 day deferral period, with a requirement that the customer must initiate the completion of the sale[206]. On the other hand, signatory banks were generally opposed to any deferral period and noted that most customers want to complete their needs in one visit to a bank branch or in a single phone or online transaction.

In the United Kingdom, a three day deferral period applies, with the option of a one day deferral where the customer initiates completion of the sale. I think that, provided that the customer is the one who must initiate the completion of the sale, a one day deferral period is sufficient to break the momentum of the sales pitch. A short deferral period would also cause less inconvenience for customers with time constraints, for whom a deferral period may create a risk that they will have a period when they are uninsured.

Recommendation 67

The Code should include a new provision that applies to signatory bank distribution of consumer credit insurance. This should specify:

a) A signatory bank's representative must not promote consumer credit insurance to an individual customer where the signatory bank's representative should have been aware that the individual is not suited to the policy.

b) A signatory bank must provide an individual customer with prominent, timely and sufficient information to make an informed decision as to whether or not to purchase the product.

c) Signatory banks should ensure that their consumer credit insurance sales processes are tailored appropriately to meet the needs of a wide range of customers, including those not familiar with consumer credit insurance.

d) A signatory bank must not complete an individual customer's application for consumer credit insurance earlier than the day after information is provided to the

[205] Financial Conduct Authority *Guaranteed Asset Protection insurance: competition remedy*, June 2015, PS15/13 p.6

[206] Joint Consumer Submission Recs 28c. and d.

customer about consumer credit insurance. Moreover the sale may only be completed if the customer contacts the signatory bank to proceed with the application – a signatory bank representative must not follow up the customer to see if the customer wants to proceed.

17.6. Lenders mortgage insurance

17.6.1. Introduction

In Australia, banks typically require a home loan customer to pay for lenders mortgage insurance if the customer is borrowing more than 80% of the value of the mortgaged property. The customer bears the cost of the upfront premium. Under some but not all policies, a portion of the premium is repaid if the loan is repaid within the first year or two. The lenders mortgage insurance market is dominated by two independent insurers. In addition, a number of banks have a related insurer that provides 'captive' lenders mortgage insurance, that is, to the related bank but not to other lenders.

The media and other commentators have raised two concerns in relation to lenders mortgage insurance. First, customers frequently do not understand that the insurance cover is for the bank and not for the customer and that, if the bank claims on the insurance because the customer cannot repay the loan, the insurer can take action to recover from the customer the amount that it has paid the bank under the insurance policy.[207] Secondly, fairness issues have been raised in relation to the costs passed on by banks to their customers.

17.6.2. Discussion

I understand that some signatory banks provide information to customers about lenders mortgage insurance, where this insurance is a condition of a home loan. Sometimes this is done as a stand-alone document. Sometimes this information is incorporated in the loan contract. I consider that a stand-alone fact sheet would be best practice to highlight the information and be the most effective way to educate customers about this product.

The Insurance Council of Australia has a fact sheet explaining Lenders Mortgage Insurance. This states that lenders mortgage insurance covers the lender but not the borrower, but does not explain that, if the insurer makes a payment to the lender under the policy, the insurer can sue the borrower for this amount or bankrupt the borrower.

[207] http://www.abc.net.au/news/2016-09-15/mortgage-insurance-providers-forcing-borrowers-to-bankruptcy/7848746

Rather than use the Insurance Council of Australia fact sheet, I recommend that the ABA and signatory banks develop their own fact sheet that must be provided to customers who are required to obtain lenders mortgage insurance as a condition of their home loan. This should clearly explain that if the signatory bank makes a claim on the insurance, the insurer is able to pursue the customer for this amount. The fact sheet should be capable of tailoring by signatory banks to specify what, if any, entitlement to premium refund would apply under the signatory bank proposed lenders mortgage insurance policy, if the loan is repaid early, for example by refinancing the loan. Consumer testing of the fact sheet would assist to ensure that it meets the needs of borrowers.

Recommendation 68

The ABA and signatory banks should develop a fact sheet that explains lenders mortgage insurance to home loan borrowers. The Code should require this to be provided to a Code customer who is required by a signatory bank, as a condition of their home loan, to obtain lenders mortgage insurance.

The Joint Consumer Submission also proposed that signatory banks should only pass on to a Code customer the actual cost to the signatory bank of lenders mortgage insurance, net of any rebate or commission paid to the signatory bank[208]. In addition, the signatory bank should pass on to a Code customer any rebate of premium that the signatory bank receives if the customer repays or refinances their home loan[209]. I am not aware of whether or to what extent current practices differ from this, however in my consultations with signatory banks, I found general agreement that both proposals are fair.

Industry advises that if the Code required this, it could be viewed as anti-competitive. My recommendation is therefore framed in the alternative – either the Code should implement as requirements or the Code should impose a disclosure regime. This would then permit industry to obtain legal advice to determine whether the first option – my preferred option – would be viable, either with or without authorisation by the Australian Competition and Consumer Commission.

Recommendation 69

The Code should either:

a) restrict signatory banks from charging a home loan customer for lenders mortgage insurance more than the actual cost incurred by the signatory bank net of any discount or commission paid by the insurer to the signatory bank and require a signatory bank to pass on to a home loan customer any rebate of premium that the signatory bank receives if the customer repays or refinances their loan; or

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[208] Joint Consumer Submission Rec 29a.

[209] Joint Consumer Submission Rec 29b.

b) impose a disclosure regime whereby signatory banks disclose to their customers any discount, commission or rebate obtained by the bank at the inception of the policy and at the time of cancellation of the policy.

18. CUSTOMERS WITH SPECIAL NEEDS

Signatory banks recognise that there are customer groups who face particular barriers in accessing banking services.

There are a number of clauses of the Code that respond to the special needs of particular customer groups. The Code is, however, only part of the picture. Other important initiatives are the ABA's Position on Financial Inclusion, Industry Standards on Accessibility of Electronic Banking (currently under review), Indigenous Statement of Commitment and Guiding Principles of Accessible Authentication.

18.1. Key commitments

Clause 7 of the Code is headed "Customers with special needs". It provides:

> *"We recognise the needs of older persons and customers with a disability to have access to transaction services, so we will take reasonable measures to enhance their access to those services."*

Clause 8 of the Code addresses special needs of customers in remote indigenous communities. The clause includes a number of obligations to meet those communities' needs including that signatory banks make information about relevant banking services available in an accessible manner and that they provide information about no or low standard fee accounts upon request. Clause 8 also obliges signatory banks to assist these customers with identification requirements to meet obligations under Anti-Money Laundering and Counter-Terrorism Financial Act 2006.

Clauses 7 and 8 are located in Part C of the Code which sets out signatory banks' key commitments. A number of submissions to my Review proposed that there should be recognition of the special needs of other customer groups[210]. Submissions also proposed the broadening of clause 8 to apply more generally to indigenous Australians (ie. not necessarily in remote communities). In addition, there was a view that the Code should link to Industry Guidelines: these were seen as important in setting out in more detail what signatory banks should do to meet the needs of different customer groups[211].

[210] Joint Consumer Submission Rec 40, Legal Aid NSW Rec 13, Legal Aid Qld, CCMC Submission p.13

[211] Vision Australia Submission p.2, Legal Aid Queensland p.4

18.1.1. Discussion

In Chapter 6.5 of my Report, I have recommended that the Code is rewritten to include Principles that set out the key promises by signatory banks and that frame the specific obligations in the Code. As proposed by the ABA[212], I think that the Principles should include a commitment to financial inclusion and recognition of the special needs of some customer groups – this is my proposed Principle 6.

It is important that there are specific obligations that give substance to this Principle. I think that the Code should oblige signatory banks to design and make available their banking services in a way that is inclusive and has regard to the needs of customers, taking into account factors and circumstances including work status, age, gender, geographic distance, language, indigenous status, health and disability and experience of trauma, abuse or disadvantage including a natural disaster, family violence or socio-economic disadvantage.

This wording includes all the groups that stakeholders have identified to me as facing barriers to access to the banking system (but of course the drafters could include further examples of relevant factors and circumstances if they felt this appropriate). But this is not intended to be a closed group: it may be that new groups are identified in the future.

ABA Industry Guidelines, such as its Indigenous Statement of Commitment – August 2015 and Position on Financial Inclusion – October 2016, can and should continue to provide a further level of detail.

Recommendation 70

As one of the Principles set out at the front of the Code, there should be a commitment by signatory banks to financial inclusion and recognition of the special needs of some customer groups.

To implement this Principle, the Code should oblige signatory banks to design and make available their banking services in a way that is inclusive and has regard to the needs of customers taking into account factors and circumstances including work status, age, gender, geographic distance, language, indigenous status, health and disability and experience of trauma, abuse or disadvantage including a natural disaster, family violence or socio-economic disadvantage.

The ABA and signatory banks should continue to develop Industry Guidelines to give further depth and specificity to this obligation.

[212] ABA Submission p.15

Similarly, clause 8 should become a series of obligations that are framed by the general Principle on financial inclusion. There were several submissions that clause 8 should be broadened to apply to indigenous Australians generally, not just those in remote communities[213]. Also that the clause should require more proactive assistance by signatory banks[214].

I agree. Further than that, I think the clause requires a complete rewrite to make the obligations on signatory banks more meaningful and clearer. To illustrate the problems of the current drafting, let me focus on clause 8(b):

> *"If you are a member of a remote indigenous community, we will take reasonable steps to:*
>
> *....*
>
> *(b) at your request, provide you with details of accounts which may be suitable to your needs, including in a remote location. This information may include details of our accounts which attract no or low standard fees and charges;"*

The words "at your request", "may be suitable", "may include" qualify these paragraphs to such an extent that signatory banks appear to be committed to very little. This diminishes rather than enhances the standing of the Code and the signatory banks. As discussed in Chapter 6.8, I recommend that the redrafted Code use plainer, less qualified language. By way of example, it would be much meaningful if the clause stated plainly "when you visit a branch to open an account, we will provide you with information about accounts that attract no or low standard fees and charges if it is likely that you will be eligible for an account of this type".

Recommendation 71

Redrafted clause 8 should apply to all indigenous Australians, not just those in remote communities. It should use clear and direct language to create meaningful obligations, thereby providing substance to the Principle of financial inclusion.

18.2. Customers with disability

Australians with disability can have particular problems accessing banking services and managing their financial affairs. This customer group includes more than 353,800 Australians currently living with dementia, a number that is expected to grow to nearly 900,000 people by 2050[215].

The Australian Law Reform Commission's report 124 "Equality, Capacity and Disability in Commonwealth, August 2014 recognised the importance of:

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[213] Joint Consumer Submission Rec 41, Legal Aid NSW Rec 3 and CCMC Submission p.10

[214] Legal Aid NSW Recs 5 and 9

[215] Capacity Australia Submission p.2

> *"ensuring people with disability have an equal right to make decisions for themselves"…[and] respecting people's dignity, autonomy and independence, while supporting them to make their own decisions, where such support is needed".*

The Commission recommended that the ABA should encourage banks to recognise supported decision-making.

> *"The Australian Bankers' Association should encourage banks to recognise supported decision-making. To this end, the ABA should issue guidelines, reflecting the National Decision-Making Principles and recognising that:*
>
> *(a) customers should be presumed to have the ability to make decisions about access to banking services;*
>
> *(b) customers may be capable of making and communicating decisions concerning banking services, where they have access to necessary support;*
>
> *(c) customers are entitled to support in making and communicating decisions; and*
>
> *(d) banks should recognise supporters and respond to their requests, consistent with other legal duties."[216]*

18.2.1. Discussion

This is clearly an important issue for many Australians and their families. During the course of my Review, I heard about banking difficulties experienced by cognitively impaired bank customers and by family members endeavouring to support them. At the same time, there is increasing awareness that customers with disability are highly susceptible to financial abuse – and an expectation that banks will play a role in identifying and addressing this.

As proposed by the Australian Law Reform Commission, I think that the Code should include a new obligation on signatory banks to develop policies and procedures that recognise that customers should be presumed to have the ability to make decisions about banking services and to accommodate this entitlement including with support. Signatory banks should develop an Industry Guideline to assist, linked to the ABA's existing guidance on financial abuse.

[216] Australian Law Reform Commission's report 124 "Equality, Capacity and Disability in Commonwealth, August 2014 Rec 6-5

Recommendation 72

The Code should include a new provision headed "Customers with disability" obliging signatory banks to develop policies and procedures recognising:

a) that customers should be presumed to have the ability to make decisions about access to banking services;

b) that customers may be capable of making and communicating decisions concerning banking services, where they have access to necessary support;

c) that customers are entitled to support in making and communicating decisions; and

d) signatory banks should recognise supporters and respond to their requests, consistent with other legal duties.

18.3. Entitlement to a no or low cost bank account

The ABA's Affordable Banking website lists 11 banks, including the major four banks, which offer a transaction account that is fee-free to eligible customers (a basic bank account). The website states:

> *"Generally, to qualify for a basic bank account, a customer will need to hold a Pensioner Concession Card, Health Care Card or Commonwealth Seniors Health Card. If a bank requires a customer to hold a Concession Card or Health Care Card, they will typically require that income support or family assistance payments social security benefits be paid into this account."*

Basic bank accounts are, therefore, reasonably available. However, a bank operating in Australia is not obliged by law to accept a person as a customer. This creates a potential problem given that, in today's society, a bank account is a fundamental necessity. As stated by the European Commission in a memo dated 8 May 2013:

> *"Citizens without a payment account are excluded from important aspects of life in their country. They may encounter substantial difficulties with receiving their salary or social security payments. They cannot transfer money or execute transactions other than cash based ones and are excluded from any type of online transaction or purchase, which can be cheaper. As a result, they often face higher costs and larger risks as they can only use cash."*[217]

[217] European Commission Memo, *Proposal for a Directive on Payment Accounts – Frequently Asked Questions*, 8 May 2013

The Joint Consumer Submission referred to the inability of some Australians, especially indigenous, remotely located and aged Australians, to obtain a bank account because the person's local bank refuses their application or closes existing accounts. Sometimes it is the customer's behaviour that results in this action being taken. But the submission stated that sometimes it is because the account is not profitable for the bank[218]. The submission suggested that a bank account of last resort regime should apply[219].

18.3.1. Discussion

The Affordable Banking website is tangible evidence that the ABA and its member banks understand that the banking sector has a societal (if not legal) obligation to provide access to a basic account, whatever a person's financial situation. But banks must also, of course, meet their legal obligations including to provide their staff with a safe working environment.

In the United Kingdom, the Payment Accounts Regulations 2015 finds a balance between these various imperatives. These Regulations oblige a designated credit union to offer a payment account with basic features to any consumer legally resident in the European Union (whether or not they have a fixed address) who does not hold a payment account. The only permitted exceptions to this obligation are where the opening of the account would be unlawful (for example, because contrary to anti-money laundering requirements) or where the consumer's conduct amounts to an offence under legislation (for example, threatening or abusive behaviour).

Similarly, I think that the Code should only permit a signatory bank, that offers a basic account, to refuse an application by an eligible person for an account in the circumstances stipulated in the United Kingdom Regulations. Note I am not, however, recommending that all signatory banks should be compelled by the Code to offer a basic account. Given that the largest signatory banks voluntarily offer a basic account, it seems that there is no need for the Code to stipulate this. Further I note that consumer representatives have not proposed that more providers are needed.

Recommendation 73

The Code should specify that if a signatory banks offers a fee-free transaction account to eligible customers (a basic bank account), the signatory bank may only refuse to allow an eligible person to open an account of this type if:

a) the opening of the account would be unlawful; or

b) the person has conducted themselves in dealings with the signatory bank in a way that amounts to an offence under legislation (whether or not the person has been charged with committing an offence).

[218] Joint Consumer Submission p.101

[219] Joint Consumer Submission Rec 42

18.4. Account suitability for low income or disadvantaged customers

Clause 16 deals with no or low fee accounts for low income earners and disadvantaged persons. It includes the following provisions:

> *"16.2. If you tell us that:*
>
> *(a) you are a low income earner or a disadvantaged person (regardless of whether you are an existing or prospective customer); or*
>
> *(b) you would like factual information about accounts which attract no or low standard fees and charges,*
>
> *we will provide you with factual information about any of our accounts which may be suitable to your needs. That information may include details of our accounts which attract no or low standard fees and charges.*
>
> *16.3. If in the course of speaking with you, in relation to your accounts, we become aware that you may be the holder of a Commonwealth Seniors Health Card, Health Care Card or Pensioner Concession Card (regardless of whether you are an existing or prospective customer), we will provide you with factual information about our accounts which attract no or low standard fees and charges.*
>
> *16.4. Please note that we will not assess continuously whether you may be a low income earner or a disadvantaged person, but we encourage you to let us know at any time if this is the case.*
>
> *16.5. We will make information publicly available about accounts which attract low or no standard fees and charges on our website and through other means."*

The concern that has been expressed here is that these provisions rely upon a consumer to self-identify as a person eligible for a basic bank account. But an eligible person may not be aware that basic bank accounts exist. This is particularly the case given that some bank websites do not readily navigate to information about basic bank account. For example, one large bank's website has a list of products that includes bank accounts – but the navigation from this does not refer to the basic bank account.

By way of comparison, I am told that Clause 3.1 of the former UK Banking Code provided:

> *"[the bank] will assess whether your needs are suited to a basic bank account (if we offer one) and if they are we will offer you this product".*

A couple of submissions to the Code Review called for signatory banks to be subject to a similar obligation to this.[220]

18.4.1. Discussion

This is an issue that has been the subject of discussion for some years. The last independent Reviewer of the Code recommended that the Code include the following wording:

> *"if, in the course of dealing with you, we become aware that you are in receipt of Centrelink or like benefits, or assess that your needs are suited to an account which attracts no or low fees and charges, we will provide you with factual information about these accounts".*[221]

It seems to me that the time has come for the Code to address this matter. It would be quite easy for an account application form (both branch version and online version) to include information about the bank's basic bank account, if the signatory bank offers one, and then ask some targeted questions to test the eligibility of an applicant for an account of this type.

Recommendation 74

The Code should oblige signatory banks that offer a basic bank account to include in their bank account application forms:

- Information about the basic bank account; and
- targeted questions to test the eligibility of an applicant for an account of this type,

so that the signatory bank can offer a basic bank account to the applicant if eligible for this product.

Of course, an account holder's circumstances may change. They may not have been eligible for a basic bank account at the time of opening an account but may thereafter. Ideally signatory banks would have systems and processes whereby they could scan for customers who are likely to be eligible for basic bank account, and proactively offer that option. I tested the feasibility of this with the industry and was advised that signatory banks are unable to identify Centrelink payments that are made and could not use this as a way of detecting likely eligibility.

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[220] Joint Consumer Submission p.28 and Rec 10, Legal Aid NSW Rec 29

[221] McClelland, J *The Code of Banking Practice Final Report*, December 2008, Rec 35

I have, however, earlier recommended that signatory banks establish systems and processes to identify and contact individual customers at high risk of future financial difficulty to offer assistance, including by providing information about products that may be more suitable for them – see Chapter 14.4. Many of these customers would also have transaction accounts and the opportunity could be taken to provide information about a basic bank account where appropriate.

In addition, I think that the ABA and signatory banks should establish a project to work with Centrelink to see what can be done to identify Centrelink recipients who would be eligible for and would benefit from a basic bank account. I realise that this will not be easy and that there would be implications for inter-operability between government and banking systems. This would, however, enable signatory banks to enhance the services they provide for disadvantaged customers, As I earlier suggested in relation to another medium term project, the CCMC should be kept appraised of progress in relation to this initiative and, to provide visibility to the public of signatory banks' efforts, could report in its annual reports about efforts to improve capability and hence performance in this area. I have not, however, made a specific recommendation in relation to this because to do so may be perceived as going beyond my proper scope..

Recommendation 75

The Code should oblige a signatory bank that offers a basic bank account to use situations when they are in contact with individual customers:

- at high risk of future financial difficulty; or
- in financial difficulty,

to make those customers aware of the option of transferring to a basic bank account.

Finally, clause 16 needs to be redrafted to remove repetition and overcome the defects earlier discussed in relation to clause 8. At the moment, some subclauses are highly qualified: "[we] may include details of our accounts which attract no or low standard fees" and "if in the course of speaking with you, in relation to your accounts, we become aware…". Other subclauses focus on the negative "we will not assess continuously whether you may be a low income earner". I also recommend a stronger obligation to publicise the availability of basic bank accounts.

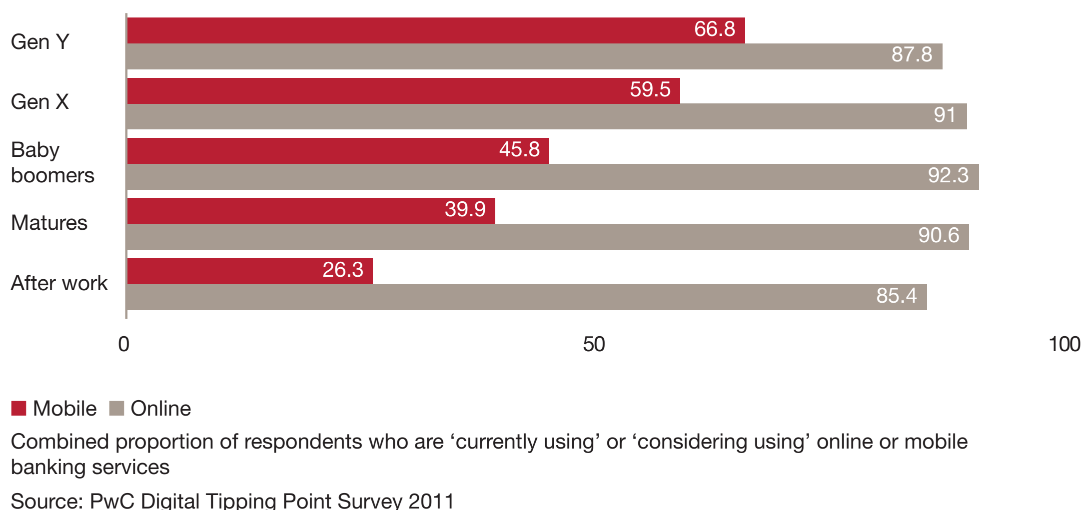
Recommendation 76

Clause 16 of the Code should be redrafted to remove repetition and to create meaningful obligations using clear and direct language. The obligation to publicise the availability of basic bank accounts should be strengthened, for example, the information should be "prominently" displayed on the bank's website and website navigation should reliably lead to the relevant information.

18.5. Electronic communications

Banking has been revolutionised by digital technologies, with younger customers embracing online and mobile services in numbers that dwarf the level of on-line usage by older generations. See Figure 24 below.

Figure 24. - Proportion of PwC 2011 survey recipients (sample size almost 3,000) currently using or considering using online or mobile banking



Mobile Online

Combined proportion of respondents who are 'currently using' or 'considering using' online or mobile banking services

Source: PwC Digital Tipping Point Survey 2011

Recognising the needs of people with disability, the ABA has an Industry Standard on Internet Banking (currently under review) that sets standards for "the design, deployment and operation [of internet banking]". This, however, presupposes internet access. An Australian Bureau of Statistics study of internet use[222] found that, whereas 99% of 15 to 17 year olds are internet users, only 51% of those at least 65 years old are internet users. Wealth is also a factor in internet use, with 97% of households in the highest income quintile and only 67% of households in the lowest income quintile being internet users.

The result is that the households in the lowest income quintile can be excluded from products that require an email address. In addition, they are more likely to incur fees charged by banks for branch transactions and paper statements. The Joint Consumer Submission expressed the view:

> *"Charging a fee on those on the wrong side of the digital divide is disproportionate and only exacerbates financial hardship. They are in a sense being penalised for being poor."*[223]

Several submissions argued that the Code should address this problem[224].

[222] http://www.abs.gov.au/ausstats/abs@.nsf/mf/8146.0

[223] Joint Consumer Submission p.78

It is, of course, more efficient for banks to communicate with customers electronically than by posted mail. Recognising this, signatory banks typically do not charge for emailed account statements, but often do charge for posted account statements. This is an incentive for customers to 'save the forests' and to promote efficiency, however a side effect is to penalise those who cannot afford or do not otherwise have access to a home internet connection. I think that it would be consistent with signatory banks' commitment to financial inclusion and customers with special needs if signatory banks waive these fees for customers who do not have a home internet connection.

Recommendation 77

The Code should require a signatory bank, that charges a fee where a customer elects to receive post mailed account statements rather than emailed statements, to waive those fees for a customer who does not have a home internet connection.

[224] Joint Consumer Submission Rec 27, ,Legal Aid NSW Rec 31

19. COMPLAINTS HANDLING

Clauses 37 and 38 of the Code impose obligations in relation to a signatory bank's internal dispute resolution process and external dispute resolution process. Clause 39 of the Code obliges signatory banks to publicise the availability of both processes.

Earlier Chapters of my Report address aspects of these provisions.

1. Chapter 6.8 proposes an illustrative redraft of Clause 37 as part of the discussion of Code structure and language.
2. Chapter 8.11 notes that small business loan complaints are not encompassed by the ASIC standards and so small business would benefit if the Code is amended to require signatory banks to undertake internal dispute resolution of any Code customer complaint in a way that meets the ASIC standards. The Chapter argues the appropriateness of this as an uplift in the commitment that the Code makes for small business.
3. Chapter 8.11 also touches upon small business, including farming enterprises, access to external dispute resolution for financial services disputes. The Chapter notes that there are other reviews underway at the moment inquiring into the adequacy of access to external dispute resolution and that my expectation is that these will resolve the access problems that have been identified. The Chapter also addresses the issue of information about external dispute resolution options – an issue that arises in particular for small business.

This Chapter deals with two other issues that have been raised with me in relation to the complaints handling provisions of the Code.

19.1. Definitional issues

The Code uses the terms "complaint" and "dispute". Neither of these terms is, however, referenced to the international complaints handling standard's broad definition of complaint, encompassing any expression of dissatisfaction. A couple of submissions to my Review proposed that alignment with the complaints handling standard would be appropriate.

19.1.1. Discussion

As previously noted, I am recommending that signatory banks should be required by the Code to provide any Code customer, who is not satisfied with the outcome of their complaint, with ready access to an internal dispute resolution process that meets the standards set by ASIC. I cast this language to conform with the international complaints handling standard. Note also that the ASIC standards require the adoption of the definition of "complaint" in the international complaints handling standard[225].

[225] Regulatory Guide 165.78

The ASIC standards recognise that there is a significant administrative burden in capturing and maintaining records of all minor expressions of dissatisfaction. Accordingly, ASIC permits a bank to refrain from registering a complaint that is resolved to the customer's complete satisfaction within 5 business days of the receipt of the complaint[226]. As I understand, most signatory banks take advantage of this, but not all do. The result is that signatory banks' differing approaches increase the difficulty of cross sector comparison. It has been suggested to me that a uniform approach to complaints recording would increase the utility of the complaints data that is collected by the CCMC.

I am not recommending that the Code mandate a uniform approach to complaint recording. First, the banks' own definitions are often built around internal structures, processes, business rules, performance measures and reporting, values and cultural settings – many of which are deeply embedded. Second, the exercise would be costly – and would require some independent validation if it was to be trusted. Third, it would take the Code to a degree of intrusion in how a bank chooses to run its business that in my view, would not be justified by the benefit.

It is, however, important that complaints data and meaningful analysis of this data is available to the public. In Chapter 20.10, I discuss how I think the CCMC can achieve this, whilst continuing to allow signatory banks the freedom to decide whether or not they record expressions of dissatisfaction that are fully resolved within 5 business days.

19.2. Customer Advocate

On 30 September 2016, the ABA announced that banks had agreed to appoint dedicated internal customer advocates[227]. The ABA Guiding Principles - Customer Advocate state that the purpose of a Customer Advocate is:

> *"to make it easier for customers when things go wrong by helping to facilitate fair complaint outcomes and minimise the likelihood of future problems".*

The Guiding Principles explicitly refrain from prescribing a 'one size fits all' approach and recognise that banks may design the role differently, taking into account their specific needs, current arrangements and aspirations and customer and community expectations[228]. The Principles require, however, the function to be effectively resourced to carry out the role and to have regular access to the Chief Executive Officer, other members of the senior executive and/ or the Board[229].

The ABA's submission to my Review proposed that the Code is amended to entrench the requirement for signatory banks to have a Customer Advocate[230].

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[226] Regulatory Guide 165.80

[227]http://www.bankers.asn.au/media/media-releases/media-release-2016

[228] ABA Guiding Principles – Customer Advocate para 1.2 and 1.3

[229] ABA Guiding Principles – Customer Advocate para 2.2

[230] ABA Submission p.8

19.2.1. Discussion

I agree that a requirement for each signatory bank to appoint a Customer Advocate should be contained in a Code provision. I am conscious that this is a bank initiative – in my consultations, I heard no clamouring by stakeholders for this – and I agree with the ABA's Guiding Principles that signatory banks must have some freedom to design and manage the role in a way that fits their circumstances.

That said, from a Reviewer's perspective, it is important that the Customer Advocate is seen by stakeholders as a credible role that is capable of having genuine impact in the bank. Factors that would influence this would include:

1. Consistent with the ABA's Guiding Principles, the Code should require the function to be effectively resourced to carry out the role and to have regular access to the Chief Executive Officer, other members of the senior executive and/ or the Board. This I see as eminently scalable and readily applied to a range of configurations.

2. To ensure an independent perspective is brought to bear, ideally, each signatory bank should recruit their Customer Advocate from outside the banking sector (although they may well have had previous banking experience). I recognise that this may be more difficult to achieve in a smaller bank environment where the function might have to be supported by part-time or shared resources.

3. The Code should also specify at least a high level articulation of the broad purpose or nature of the role. As a starting point, I would think that the role should include reference to:

    - enhancing the customer responsiveness and effectiveness of internal dispute resolution;

    - assisting the signatory bank to identify and address systemic issues that become apparent as a consequence of complaints;

    - liaising with external stakeholders including small business and consumer representatives, the signatory bank's external dispute resolution scheme and the CCMC to identify opportunities for the signatory bank to address issues that impede Code customers' experience of the signatory bank; and

    - providing a customer "voice" within the signatory bank.

The role could include an opportunity to be involved in specific complaints – either as a point of escalation or to provide advice to the complaints team or support to the Code customer during the internal dispute resolution process. Where this is the case, the Customer Advocate's involvement must not delay the resolution of disputes. This is clear from ASIC Regulatory Guide 165.121 and reinforced by the ABA Customer Advocate Guiding Principles which state:

> *"Any engagement with a Customer Advocate should not put customers in a worse position by lengthening, replacing or substituting internal complaints handling processes".*[231]

Most importantly, however, I think that Customer Advocates should work to address systemic issues. By way of example, I have discussed in Chapter 15.2 the role that the Customer Advocate could play in relation to Code customer requests to cancel direct debit arrangements.

I am aware that some ABA member banks, that are not currently signatory banks, may become a signatory to the new Code and am concerned that, for smaller banks, or ones with a very different service offering or customer-base, a Customer Advocate model that would well suit a major bank may be less applicable. I am also aware that even the major banks are evolving varying conceptions of the Customer Advocate role. I think it is a difficult role and industry should be prepared to keep it under evaluation. It is not my place to make specific recommendations on how banks manage themselves internally, so I have focused on external credibility in my recommendation.

Recommendation 78

The Code should be the vehicle for the industry decision that signatory banks should appoint a Customer Advocate. While there will need to be flexibility in how the function is implemented, for external credibility any specification in the Code should include:

a) a commitment to an independent perspective – ideally by appointing from outside the banking sector (although they may have previous banking experience);

b) a commitment to proper resourcing and effective reporting lines that maintain effective separation;

c) a high level articulation of the role of the Customer Advocate that includes:

- enhancing the overall customer-responsiveness and effectiveness of internal dispute resolution;
- assisting the signatory bank to identify and address systemic issues that become apparent as a consequence of complaints;
- liaising with external stakeholders including small business and consumer representatives, the signatory bank's external dispute resolution scheme and the CCMC to improve customer experience; and
- providing a customer "voice" within the signatory bank.

[231] ABA Customer Advocate Guiding Principles para 2.4

20. CODE MONITORING AND COMPLIANCE

20.1. Background

The Code is monitored for compliance by the Code Compliance Monitoring Committee ("CCMC"), a committee of 3 people who are supported by a small staff. The rules governing its approach are currently in clause 36 of the Code (obligations on the banks regarding Code monitoring) and in the CCMC Mandate (setting out what the CCMC is meant and permitted to do).

During my review, I heard much criticism of the powers and scope of this compliance monitoring function. These go to an inadequate profile, inadequate resourcing, limits to the CCMC's powers to investigate, a lack of available sanctions, inadequate public reporting and a lack of coordination with external disputes resolution schemes and with regulators. Some saw the CCMC to be deliberately designed to be as small in impact as possible.

Most feedback from industry was quite positive about the CCMC, however I did hear a few criticisms from industry of the opposite – of CCMC pursuing trivial matters already acknowledged by banks, overstepping its remit, of 'fishing' for issues and of failing to understand 'how banking really works'.

A feature of the criticisms, whether they come from consumers, politicians, other stakeholders or signatory banks is a confusion of views as to the CCMC's role and the place of the Code in the regulatory framework. It seems to me that the only way to make sense of the various criticisms is to begin by forming my own view as to its proper role going forward, taking into account the changes to the Code that I am recommending. From there, I can weigh up the ideas put to me and make any recommendations for change.

A linked question is whether to recommend that the Code of Banking Practice is submitted to ASIC for approval under Corporations Act section 1101A – as proposed by a number of non-industry stakeholders and generally opposed by industry. I think that question can also only be properly considered once a clear view of the Code's role is established. I turn to this question in the following chapter.

I have separately been asked to conduct an Independent Review of the CCMC. With respect to role, remit and powers, the issues for both Reviews are the same, however for the CCMC Review, I am also reviewing the effectiveness of its operations within the constraints of its current mandate. I will separately publish a Report about the CCMC which will in substance repeat this section of the Code Review – and go on to evaluate CCMC's current operations in greater detail.

20.2. Current CCMC operations

The CCMC is operated on behalf of the ABA by FOS employed-staff. These staff are part of FOS's independent Code Compliance and Monitoring team which has around a dozen staff who are also responsible for monitoring other industry Codes. The Committee itself is made up of an independent Chairperson, a banking industry representative and a consumer representative. These three act as a 'panel' – so that monitoring and investigative work is done by a small number of staff, but the decisions and reports are considered and signed off by the Committee, except to the extent that the Committee has formally delegated powers to staff.

In practice, the CCMC has several channels for 'monitoring compliance' with the Code.

1. It requires all signatory banks to lodge an Annual Compliance Statement setting out information about their risk and compliance framework, policies and procedures to address Code obligations, financial difficulty assistance, types and numbers of breaches recorded and any remedial action taken, etc;
2. It conducts individual investigations of allegations of Code breaches made by any person;
3. It can receive a referral from the ABA, asking it to investigate a matter (although this has never happened); and
4. It conducts 'own motion inquiries' ("OMI"), (one per year for the last two years), into a matter of its choosing, which involves asking banks to provide information on the subject matter chosen – and producing a report with recommendations for the banks. A risk-based approach is used for selecting and targeting the OMI – and the Annual Compliance Statement is typically used to collect information on implementation of any previous OMI recommendations.

The CCMC also produces an Annual Report in which it sets out its work for the year, including the individual investigations and a summary of its own motion inquiry, and provides some de-identified data about banks compliance with the Code.

20.3. Stakeholder criticisms

Non-industry stakeholders see the CCMC's configuration as 'limited'. Specific feedback included:

- The CCMC is seen as low profile to the point of invisibility. The Committee's name does not include the word 'bank'.
- There was criticism of the limitation of one year to bring an alleged breach to the CCMC as far too restrictive.
- The CCMC's powers are seen as toothless. Most consumers who bring an allegation of a breach are shocked to discover that there is no penalty or consequence for the bank if an investigation does find a breach. As a result, many stakeholders view the CCMC individual breach investigations as adding little value.

- Criticism that the CCMC Mandate specifically restricts the CCMC's ability to investigate non-compliance with Clauses 3 and 4 (key commitments and compliance with laws).
- Criticism of the CCMC's 'failure' to name banks more often in its reporting.
- CCMC reporting also came in for criticism because of lack of comparability of bank data.
- The CCMC is at times criticised for lack of deep expertise in some aspects of banking.
- For the last two years, CCMC has conducted a single OMI per annum – this was widely seen as manifestly inadequate.
- Some stakeholders called for much more cooperation between CCMC and ASIC and between CCMC and FOS.

Overwhelmingly, these are not criticisms of the CCMC's performance, nor of banks cooperation with the CCMC – they are of the Code itself, of the CCMC mandate and of current resourcing.

In parallel to this Review, I have been conducting a more detailed review of the effectiveness of the CCMC's function. That task will be completed shortly after this Code Report, however to ensure that my comments in this section are not misinterpreted, in summary the CCMC Review report will say that I found the CCMC's operation to be professional and well-run within the limitations it faces.

20.4. Current Role of CCMC

Code customers (both individuals and small businesses) are quite unclear about the CCMC's role. Despite the CCMC being careful on its website to position its role as being about Code breaches and, for example, using the language of 'report' as distinct from 'complaint', many Code customers assume that the CCMC is simply another dispute resolution mechanism such as FOS or a regulatory body like ASIC. While it is true that some who bring issues to CCMC are in a state of high anxiety and in no mood to listen, there is clearly an expectation gap that needs to be addressed.

More closely engaged stakeholders' expectations of the CCMC role also varied, with some demanding regulator-like powers and behaviour and others arguing for an approach based on 'ownership' from industry and a focus on openness and goodwill.

The CCMC's current activity shows something of a contradiction as to its focus. Its processes and profile seem to be pitched to a strong emphasis on individual breaches of the Code (heavily prescribed investigation processes for individual breaches and scant mention of how own motion inquiries might be conducted or intelligence gathering might occur).

Yet investigation of individual breaches is the part of the CCMC's function that least satisfies external stakeholders. That is because even where a breach is established, the Code customer invariably leaves dissatisfied and the bank simply accepts the one-off breach as one of many that it has likely found itself. In general, it is only when the individual investigation unearths a more systemic issue that genuine value is added.

CCMC own motion inquiries enjoy a better level of satisfaction – both within banks and amongst external stakeholders - although external stakeholders think that the CCMC could usefully do more of these than has been the recent practice. The inquiries are sometimes also criticised for a lack of depth of expertise.

The CCMC's public reporting is seen as a positive – but it too has been criticised for its limitations (incompatible statistics, not enough enquiry to deepen the analysis, little trend information, too 'soft' on banks, an absence of use of both IDR and EDR complaints information, etc).

20.5. Future role for the CCMC

I have concluded that while a prescriptive, regulatory style of operation will need to be some part of its operations, this is not where the CCMC can add the most value. With the development of a great deal of law in this space, and the increased powers and resourcing granted to ASIC, the CCMC is likely to disappoint if it is being compared with 'hard' government regulatory standards and enforcement.

My preference is for the CCMC to evolve away from the idea of being a quasi-regulator towards being more of a mechanism for community assurance through active monitoring and promoting higher standards and continuous improvement of banking practice. A role of this nature fits 'alongside' regulation, with the focus being the commitments in the Code that clearly go 'beyond the law' and so that are not the realm of government regulation. (If recommendations in other Chapters of my Report are accepted, the Code will more extensively go 'beyond the law' giving the CCMC a clearer scope.)

I think that the most important word in the description of the CCMC is 'monitoring'. The Code is a promise to the community – and the CCMC function should be focused on providing assurance to the community that the Code is working. It is difficult to avoid the conclusion that at least some part of the loss of trust in banks is that the mechanism for monitoring the Code has not been sufficiently visible nor provided a robust level of assurance.

Continuing that line of reasoning, I see the greatest CCMC value coming from activities that – directly or indirectly – provide assurance to the community and are likely to raise standards of conduct and compliance across the industry:

1. Prioritising investigative/analytical effort on gathering evidence of **systemic non-compliance (**common problems, complaint and reported breach trends, etc).
2. **Transparency** – providing industry and the community with investigative, statistical and analytical information demonstrating the level of compliance with the Code and identifying any trends and potential problem areas.

3. Supporting **continuous improvement** of banking practice by providing feedback as to the effectiveness of the implementation of the Code, including the operation of Industry Guidelines, identifying and promoting **good practice** conduct and compliance, identifying areas for new or strengthened Code provisions or Industry Guidelines, and reporting about longer term Code-related projects to provide assurance to the community about progress.

It is important that stakeholders are clear that while the CCMC welcomes reports of suspected breaches of the Code from individual consumers, it has no role in obtaining redress and will only investigate an individual report where there is value that can be applied across the broader population and across industry.

For the CCMC to be able to credibly deliver on the responsibilities above, it has to be trusted and that means being appropriately visible and possessing sufficiently credible powers, albeit focused on system improvement and better customer outcomes rather than 'punishment'.

Recommendation 79

The Code and the CCMC Mandate should be redrafted to make it clear that the primary focus of the CCMC should be its monitoring and public assurance – with the areas of greatest value-adding activity being:

a) Taking a risk-based approach to prioritise investigative effort on systemic non-compliance (common problems, complaint and reported breach trends, etc);

b) Transparency – providing industry and community with information demonstrating compliance with the Code and identifying trends and potential problem areas; and

c) Supporting continuous improvement of banking practice by providing feedback on implementation, identifying and promoting good practice conduct and compliance, and identifying areas for new and strengthened Code provisions or industry guidelines.

In my view, a focus on the above areas of value-add provides a basis to recommend some specific improvements – some directly related and some that go to visibility and trust. These are discussed below.

20.6. Greater visibility

I do not see a high public profile for the CCMC function as particularly essential to its successful day-to-day operation. There are a tiny number of people who would have need for day-to-day familiarity with the CCMC. For most consumers and small businesses, at a practical level, it is sufficient that the CCMC can be found if needed.

However, the current 'presence' of the CCMC is clearly inadequate in stakeholder's eyes, and I do see some short-term lifting of its profile as needed – in particular in relation to its strengthened remit to monitor a more robust Code and a greater focus on systemic Code

effectiveness as discussed above. Such publicity would be a demonstration of the industry's commitment to being held accountable for its promises to the community.

I recommend that profile-raising effort in the medium to long term be focused on points of advocacy, such as industry associations, consumer advocates and other lobby organisations. The purpose here is not to 'fish for individual breaches', but to provide assurance that the Code is being monitored and that the CCMC is being active in its role.

In the short term, I propose some modest steps. First, the ABA announcements of its response to this Report and of the new Code should give some weight to the strengthening of Code monitoring. Second, the monitoring function must have a new name – one that mentions the word 'bank'. I have recommended elsewhere that the Code itself should be renamed the "Banking Code"- for similar reasons. The Code monitoring function should similarly have a plain-speaking, straightforward name that makes it clear what it does. I suggest "Banking Code Monitoring Panel".

Third, the function's Mandate must make it clear that the CCMC function has a responsibility for promoting transparency and trust around the Code – therefore it will have more of a role in communicating to the public about the effectiveness of the Code than currently is the case – and it follows, something of a greater profile.

Fourth, for the avoidance of doubt, the Code should embed a responsibility on the CCMC to publish such information about the effectiveness of and compliance with the Code, including inquiry reports, statistical data, determinations and case studies that would meet its role to enhance trust and transparency.

Recommendation 80

Promotion of awareness of the CCMC should be focused on points of advocacy, such as industry associations, consumer advocates and other lobby organisations. The purpose here is to provide assurance that the Code is being monitored and that the CCMC is being active in its role.

Recommendation 81

The CCMC should be renamed the "Banking Code Monitoring Panel".

Recommendation 82

The CCMC Mandate should explicitly recognise the CCMC role in promoting transparency and trust in signatory banks' compliance with the Code and embed a responsibility for publishing information about the effectiveness of and compliance with the Code, including statistics, results of inquiries, Investigation outcomes and case studies as appropriate.

20.7. Strengthening collection of compliance information

As the key proposed role of the CCMC function is monitoring – the function should have and be seen to have an ability to collect information from wherever it is reasonably available including sources that would be intuitively expected by stakeholders. The language around this should be inclusive and positive – not limiting or negatively framed.

I agree with most stakeholders, that for credibility, these sources must be seen as more robust and open than the current channels represent. The CCMC should be informed by regular, quality information sourced from:

- The Annual Compliance Statement;
- Code customers – 'reporting' suspected breaches and from selected individual investigations of alleged breaches;
- Own motion inquiries;
- Publicly available information including, for example, Parliamentary Inquiries and media reports;
- The banks internal disputes resolution processes and the bank internal Customer Advocates (see also discussion at Chapter 20.10 on sharing data);
- The banks' own systemic conduct and Code compliance review processes, including the banks' identification of compliance patterns and trends (internally and across the industry) and their plans for responding to these and prioritising them for attention;
- The banks' external disputes resolution services (currently FOS); and
- From consumer representative and other stakeholder organisations.

Note that CCMC should not be passive in the area of Code customer complaints. For example, it is a common perception that small business and rural business customers under-report in complaints and breaches statistics. Anecdotally, this is partly through ignorance of CCMC's existence and partly because typical small business problems require resolution in much tighter timeframes than many retail consumer issues (once the business cannot pay its suppliers, it is effectively finished and most owners move on). I would expect to see the CCMC function taking some steps to actively seek information regarding alleged breaches of the Code from groups that may not be reporting at a reasonably representative level.

Similarly, the CCMC should be looking to systematising input from consumer representative organisations. Currently, these organisations generally report areas of concern through consultative forums and much of that input will be anecdotal. Although the numbers involved are comparatively small, any ability to substantiate with data will strengthen the CCMC's ability to act on issues raised.

I also support the suggestion that consumer advocacy groups or other reputable stakeholder organisations should be able to refer a matter they believe to be serious or systemic to the CCMC. They are in a unique position to identify Code customer banking issues that are repeatedly occurring, and it would seem sensible and consistent with the remit of the CCMC to welcome their insights.

This is along the lines of the 'super-complaint' that registered consumer representative groups are able to lodge in the UK. I think that the regime that applies in the UK is somewhat different, with a system in place for government registration to ensure that a consumer group is a credible, bona fide organisation. I do not think that the working model that the CCMC 'must investigate or explain why not' is the right one for this Code. I do think that the Code should explain all organisational referrals in the same way, drawing no distinction between referrals from stakeholder organisations – and that there should be an obligation to communicate back to the referring organisation as to the outcome of the referral.

Banks have been criticised, in some cases unfairly, for avoiding public disclosure of breaches and of withholding information about breaches of the Code – until the last minute or until the matter is 'forced into the open'. The new Code should minimise the opportunity for this to be a point of criticism. I am recommending quarterly reporting to the CCMC of all Code breaches. I do not think this will be an especially material change, but it is consistent with the promise of transparency and a better look than being accused of 'withholding' information from the CCMC for up to 12 months. While I understand that many of the signatory banks have very manual processes for reporting Code breaches, this change should not increase overall reporting workload.

Recommendation 83

The Code should oblige signatory banks to be proactive in providing information to the CCMC including arranging regular engagement with their internal disputes resolution area and internal Customer Advocate.

Recommendation 84

The Code and the CCMC Mandate should explicitly set out its role and responsibility to proactively gather relevant information about the effectiveness of and compliance with the Code – including from sources external to the banks such as bank customers, Australian Small Business Ombudsman, consumer advocacy groups, financial counsellor networks, Legal Aid organisations, community legal centres, consumer affairs departments and other government regulators.

Recommendation 85

The Code and CCMC Mandate should make it clear that referrals from external dispute resolution schemes, the ABA, regulators, consumer or other stakeholder organisations will similarly be fed into CCMC priority setting, but will not necessarily be automatically investigated, however in each case, the CCMC will provide a written explanation of the reasons for any decision not to pursue a referred matter.

Recommendation 86

The Code should oblige signatory banks to report breach information as required by the CCMC on a quarterly basis.

20.7.1. Access to IDR data

Greater transparency in relation to signatory banks internal disputes resolution (IDR) information was called for by many groups of stakeholders. I understand why this is a sensitive area for banks, both in terms of overall public perceptions and in terms of competitive comparisons.

I do think that there are opportunities for improved use of this internal data by CCMC in its monitoring role. For example, CCMC could receive copies of internal management reports on complaint numbers and trends. This could be part of the relationship between the banks' new internal Customer Advocates and the CCMC.

Another example might be for an OMI request to be for signatory banks, on a project basis, to collect additional information about a specific type of complaint – cancellation of direct debits comes to mind.

I think there are a number of excellent opportunities for sensible collaboration in this space, however they depend on a changed remit, powers and capability for the CCMC and the confidence in the relationship between CCMC and the banks to develop.

20.7.2. Access to EDR data

Stakeholders are also asking for CCMC to have greater access to EDR (currently FOS) information and for EDR to be more proactive in referring matters to CCMC. Much of this feedback included a level of surprise that this was not already the case.

I think that the logic is clear, and in principle I am supportive, however I recognise that there are some practical issues that must be considered.

1. Data limitations

Having some first-hand knowledge of EDR complaints data, it is unlikely that this is the mine of information often assumed. All EDR schemes that I am aware of are under considerable workload and time pressure – and understandably, they have a focus on resolving complaints, not on creating a database of precisely classified complaints information. If a complaint can be resolved by reference to the law or banks' internal processes or simply by negotiation, the question of whether the matter could be a potential breach of the Code may never come up.

Where there is a mention of a Code or Industry Guideline within a case record, it may well be no more than a passing reference to a provision within the Code and by no means a definitive finding of a breach. Even where a matter progresses to an Ombudsman's determination, whether the detail of the matter included a potential brush with the Code may not be recorded.

This is not a failing of EDR processes. This reflects the different purpose of the organisations and my view is that it would be a mistake to unduly distract EDR schemes from their core purpose of resolving consumer complaints. Of course, this does not mean that EDR information will be of no use to CCMC, rather that learning from the data will not be straightforward.

2. Improving EDR data

I am sceptical that requiring EDR staff to record instances of potential Code breaches would be successful in building a mineable database of potential Code breach information. Unless EDR were being specifically resourced to look at this aspect of every complaint, this could quickly become a matter of ticking a box, with the risk of becoming perfunctory and producing unhelpful 'garbage data'.

3. Improving referrals

I have also given some thought to the idea that EDR staff – perhaps the most senior, should be required to more actively refer potential Code breaches to CCMC. I think this plan suffers from the same problems as trying to force data recording. It is not 'core business' for EDR staff who are under significant workload pressure. I think this would be an irritation and struggle to be sustainably effective.

A better basis for referrals in my view is for the systemic issues team within an EDR scheme to have an explicit responsibility to review its own work for evidence of Code Breaches and to pass this on to the CCMC. The systemic issues staff are already thinking about the range of issues that impact on matters of greater impact and are much better placed to form a view about whether provisions of the Code may have been breached. This would also ensure that EDR referrals are already focused on issues of a systemic nature, consistent with the focus I recommend for the future CCMC (see discussion at Chapter 20.8). This would involve far fewer people and be much lower cost and it is much easier for the managers and staff of two small teams with some commonality to sustain good working relationships over time.

Recommendation 87

CCMC should work towards an agreement with signatory banks' EDR schemes to establish an explicit responsibility for the scheme's Systemic Issues Team to refer to the CCMC any Code compliance issues the team identifies through its own work.

The arrangements should be set out in writing between the EDR scheme and CCMC.

4. Safeguards

The second major consideration is protecting the data of individuals on EDR databases. A number of important safeguards are needed. There would need to be controls for consumer privacy consents, there would need to be a system for authorising CCMC staff and authorised contractors for access, policies to control which data could be accessed, systems of audit trails and so forth – as there are for current EDR staff.

Only CCMC staff and authorised contractors should have direct access to EDR data – ensuring that the Panel members are above any accusation of browsing or misusing information. EDR database administrators must have the right to audit and control CCMC use as they would any other access. The EDR scheme would need to budget for any associated costs. Any requests from CCMC for support or special assistance with reports or the like would have to be agreed by the scheme and explicitly funded by the CCMC.

All of these provisions should be the subject of protocols between the EDR scheme and the CCMC rather than attempt to cover them within the Code.

Recommendation 88

The CCMC and signatory banks' EDR schemes should develop protocols for appropriate exchange of information and access to relevant EDR data, subject to safeguards that include:

a) Explicit consent from EDR scheme complainants;

b) Restricting access only to CCMC staff and authorised contractors;

c) CCMC staff subject to the same audit and security controls as EDR staff; and

d) EDR costs are met.

The arrangements should be set out in writing between the EDR scheme and CCMC.

20.8. Focusing effort on systemic level issues

As part of focusing the CCMC function's effort on more value-adding activity, there must also be some reduction in effort on low value-adding activity. From my enquiries, it is clear that many individual investigations add very little value and often disappoint consumers - see comments under Chapters 20.3, 20.4 and 20.5. I do not suggest that no value can come from an individual consumer or small business operator bringing an allegation of a Code breach to the CCMC. The allegations or reports have value of themselves and the CCMC have made it quite clear to us that investigations of some of these do add considerable value and should be continued.

It is sensible for the CCMC function to be able to target its efforts at those investigations that will add the most. That will mean that some allegations will not be investigated, as the CCMC has the discretion to do now[232]. A risk-based approach is the reality of modern compliance and regulatory activity.

While the CCMC has been careful in its public communication, some further re-casting of individual consumer and small business 'reports' to the CCMC would be helpful. To reduce any expectation of a full-blown investigation for all allegations of breaches, members of the public should be encouraged to 'report' to the CCMC – with the clear understanding that the CCMC will take on board that information and use it as part of its monitoring activity and risk-based targeting. An investigation may proceed – but in most cases, it will not. Note that the CCMC should refer any individual or small business to EDR if they have not already been there.

The balance to this approach is an overt increase in the effort going into other forms of information collection and own-motion inquiries. The CCMC Panel should develop a two or three year business plan (updated as needed) that addresses the issues that are highest risk to public trust in the Code and in signatory banks. In the interests of public confidence, it should explain the risk assessment used to arrive at its priorities and as appropriate where referrals have come from.

That forward thinking will better enable banks to prepare for, collect and provide specific information in the Annual Compliance Statement or for a planned OMI. It will also assist the CCMC to continue to develop the range of different formats for OMIs that suit the subject matter of the inquiry. These currently include broad-based inquiries, 'deep dives', follow-up to previous inquiries, etc.

Banks mentioned to us the need for forward planning to be able to ensure that they can meet CCMC information requests and to assist with OMIs. I expect banks to be very supportive in this endeavour as they say that they obtain considerable value from the internal reporting/feedback that CCMC is able to provide them.

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[232] Code Compliance Monitoring Committee Mandate para 6.3

While there may be some concern about potential confusion between 'systemic investigation' in the EDR context and 'systemic focus' in the CCMC context, there is a clear difference in my view. While both are looking at patterns, trends, or issues 'affecting multiple customers' – EDR is looking at specific examples of loss and redress for consumers – CCMC is not. It is looking for compliance with the Code, and supporting continuous improvement through feeding back non-compliance issues identified and good practice to the signatory banks.

Recommendation 89

The CCMC should adopt a risk-based approach to focus its effort, including:

a) selecting which individual or small business reports of suspected breaches are formally investigated;

b) where an individual or small business reports a suspected breach to CCMC and has not been to EDR, CCMC should refer them to the appropriate scheme; and

c) selecting which referrals from other organisations it makes the subject of an own-motion-inquiry.

Recommendation 90

The Code, CCMC Mandate and CCMC communications material should adopt language that echoes the risk-based approach to be taken by the CCMC, including:

a) that individuals that take their matter to CCMC are "reporting a suspected breach";

b) that there should be clear information that CCMC will use this 'report' information to inform its risk assessments – but will only investigate selected individual matters; and

c) that referrals from EDR, the ABA, regulators or consumer organisations will similarly be fed into CCMC priority setting, but will not necessarily be automatically investigated.

Recommendation 91

The Code, CCMC Mandate and CCMC communications material should adopt language that emphasises the difference between EDR and Code monitoring, including:

a) language in the Code, Mandate and public information should eliminate reference to 'determinations' and any other EDR-like terms;

b) reduce the degree of detail and specificity regarding investigations in the Code, allowing the CCMC to tailor the process used to the matter at hand.

20.8.1. Timeframe for investigation

The current CCMC Mandate lists a number of matters that are outside the CCMC's scope to investigate. It also provides that if the matter has not been brought to the CCMC within one year of the individual or organisation becoming aware of the alleged breach, it is excluded from scope (unless the matter was brought to the EDR scheme within that 1 year timeframe).

The ABA recommended that this period be increased to two years after the event. Others suggested that the timeframes should align with the EDR period of limitations (FOS' Terms of Reference allows for up to 6 years).

While I can see the practicality and simplicity of alignment, the CCMC should be focused on monitoring current effectiveness and on continuous improvement of process. It would be a waste in my view, for energy to be spent on determining breaches and improving processes that were up to 6 years old and almost certainly no longer current. I think the ABA suggestion of two years strikes a reasonable balance.

Recommendation 92

The CCMC should be empowered to investigate breaches of the Code for up to two years after the individual or organisation reporting the suspected breach became aware of the events in question or reported the matter to a relevant EDR organisation.

20.8.2. Limits to investigation and breach powers

Another issue under this head raised by a number of my correspondents was criticism of Clause 36 (b) which limits the CCMC's powers to monitor, investigate or report on breaches of Clauses 3 and 4 in isolation from any other detail breach under other clauses.

As I understand the background, this limitation was inserted as a result of the last Independent Review and the intention here was to avoid duplication and confusion about the CCMC's role. I deduce that there was concern about 'fishing expedition' investigations that might be framed very broadly, a finding of a breach where there was no specific evidence to rely on and duplicative CCMC investigations of alleged breaches of the law (Clause 4).

I agree that it would be inappropriate for the CCMC to undertake an investigation into compliance by signatory banks with the law. It is ASIC that is responsible for compliance with the law, not the CCMC. Equally it would be inappropriate for the CCMC to monitor compliance with a high level statement of principle where there are no specific Code obligations that give substance to the principle.

The problem is that Clause 3, as currently drafted, includes some high level statements of principle, but also some provisions that are more accurately categorised as obligations that the CCMC should be monitoring. For example, I consider that the CCMC should have jurisdiction to monitor the clarity and comprehensibility of bank signatory documents provided to Code customers (Clause 3.1(d)).

My proposed Code architecture (see Chapter 6.5) aims to address the issue of the CCMC's jurisdiction in the following ways:

- Reference to compliance with laws would be in the Preamble – and so outside the CCMC's monitoring jurisdiction.
- The CCMC would not be able to monitor compliance with the Principles in isolation from specific obligations.
- The CCMC would be able to monitor compliance with all obligations and would interpret and apply these in light of the Principles. In other words, the Principles would point to the spirit and intent of specific obligations.

The CCMC's Mandate should also be redrafted. Consistent with my recommendations for the redrafting of the Code, the Mandate should be redrafted so as to be more positive and less cluttered with qualifiers. For example, Section C of the Mandate on Investigations opens with three paragraphs on what the CCMC can do, followed by seven paragraphs on what it cannot do. This approach diminishes the value of what is quite a significant collection of promises from signatory banks – in an attempt to mitigate against what I think are often quite remote risks.

Recommendation 93

The CCMC mandate should be redrafted along the lines recommended for the Code, in plain language and with a minimum of qualifiers and caveats.

20.9. Strengthening resourcing and skills

20.9.1. Resourcing

My recommendations will result in some need for increased resourcing for the CCMC, but this should not be by prescription or mandated in the Code itself. It should simply be a matter of negotiation between the future CCMC Panel and the ABA (and FOS as the service provider) – in light of identified priorities and a business plan.

Perhaps of greater significance in terms of costs may be the outcome of discussions/negotiations between CCMC and signatory banks – and CCMC and FOS in terms of routine information sharing to meet recommendations under Chapter 20.7 above. I think that any such costs are likely to be systems-driven and beyond my ability to estimate.

20.9.2. The Panel

From my interviews and from submissions, there are two ways in which the Panel's skills and experience could be strengthened in stakeholders' eyes – broadening the perspectives and increasing its standing.

1. Broaden perspectives

Under this head, I have in mind to explicitly include some small business and possibly agribusiness skills and experience, which would be an excellent signal to stakeholders and go some way to improving these sector's understanding of the Code and the CCMC.

In an ideal world, I would have Panel members (currently Committee members) selected on a skills and experience mix basis rather than on the current representative basis. A tripartite selection panel made up of a representative from the ABA, consumer advocacy groups and the EDR scheme would select a group that between them, brings together the best mix of skills available and that ensures the relevant perspectives, including small business, are present.

I think it is likely too much to ask of this round of reform for constituent groups to surrender their right to appoint 'one of their own'. I think the simpler thing to do is to add another member to the future Panel with relevant small business and/or agribusiness skills and experience. Of course, like all appointees, this member would also have to have sound understanding of the environment, of self-regulation and of customer issues in banking.

The process for appointing this new additional member will need to be a little different to the methods for the existing members in order to involve the intended constituency groups – small business and agribusiness - otherwise the intended boost to those groups' confidence in the Panel may not eventuate. I suggest a hybrid method in the recommendation below.

2. Standing

It is also important to ensure that members of the Panel have a sufficiently senior profile amongst their constituents and the community. This profile is in part a function of how recently members were actively involved in their respective sectors and how senior they were or are perceived to be. This would equally apply to the Independent Chair and their perceived standing in the community.

These are unfair criteria in many ways, because knowledge of the Code and the CCMC operation can only be acquired through experience on the Panel. Unfair or not, the standing of a self-regulatory panel is often a function of who is a member, not necessarily what they can bring to the task. I am not suggesting any change to the current members - they have strong knowledge of the function and are in a very good position to advise on and manage any change – however standing is a factor that should be taken into account in future appointments.

Recommendation 94

The CCMC Panel should have a fourth member with small business and/or agribusiness skills and experience along with other relevant skills.

a) This member should be appointed by the Chief Ombudsman of FOS and a consumer advocate member of the FOS Board, consulting with representative organisations from the small business and farming sectors.

b) The Panel should have the option of sitting with 3 or 4 members depending on the matter being considered, however the Independent Chair of CCMC should have an additional casting vote to ensure against deadlock in a 4 person Panel.

A further dimension to the notion of 'standing' is the level within the bank at which the CCMC interacts. The banks have suggested that an annual meeting between the CCMC Panel members and the CEO of the major signatory banks would be a way of demonstrating that the work of the CCMC was being taken seriously. I agree, although I would prefer to see this as a commitment of the CEO rather than a compliance issue.

20.9.3. Staffing

Without any criticism of current staff skills, the CCMC permanent staffing should explicitly recognise the need for data analysis skills – both for systemic investigations and for transparency reporting.

Also, while it is clear that the CCMC function requires a small permanent staffing (for support of the Panel, for collecting ACS data, for handling consumer enquiries, for liaison with banks, for individual investigations, etc), its expertise should be added to as needed for specific investigations on a project basis (eg. skills in audit, banking services and processes, specific product lines, etc).

In this way, the depth of skills for a specific (say) own motion inquiry can be strengthened in a highly targeted way – without building a larger permanent staffing.

Recommendation 95

The CCMC permanent staff mix should explicitly include strong data analytics skills.

Recommendation 96

The CCMC resourcing should allow for the ability to temporarily hire in specialist expertise for specific investigations or projects.

20.10. Sharing more data publicly

A number of stakeholders raised with me the idea that the banking industry should be more transparent and make more data about its operations available to the public and to researchers. This was a theme picked up in a number of other recent reports, including by Parliamentary Committees, the Productivity Commission and ASIC.

While it is clear that this would be seen as a positive step by the community, I accept that these are sensitive issues for signatory banks. The notion of greater transparency raises the risk for industry that data might be used 'against' signatory banks, or that commercial-in-confidence information might be leaked. There may also be some resentment that signatory banks are being held to a higher standard of accountability than (say) very large corporations such as mining companies, insurers or automobile manufacturers. While many in the community view banking as a utility or essential service akin to gas or water, not all within the sector necessarily accept this.

Another significant problem with transparency is that the banks' data is frequently not comparable – being based on internal distinctions that vary from bank to bank. Obtaining meaningful data about numbers of complaints or numbers of small business loans are two cases in point. Every bank's data is different.

I think it is a mistake to use these reasons to avoid sharing more information about the industry. First, it risks looking 'secretive'. Second, it cuts off an opportunity for banks to educate the public about the industry. As discussed elsewhere in this report, I have found that the numbers tell a story that is generally very positive to the banking industry. For the most part, the horror stories that excite the attention of the media or politicians and bring the industry into disrepute are the exception to thousands or even millions of unremarkable and successful transactions. It is only the numbers that tell that story.

I think that banks that are signatories to the Code have a significant opportunity to lead in this space and take a step towards greater transparency. I think this is an initiative that will go a long way to re-establishing the kind of trust that the banking industry is seeking.

A way of doing this that provides for some protection against misuse and an opportunity to translate incompatible data would be to give the CCMC the responsibility of providing a greater range of information to the public. Rather than each bank attempting to either force all of its own data into one standard format (an enormous task) for the purposes of reporting – the CCMC could take on the role of understanding the differences between each banks internal data – and reporting at a level of equivalence. To borrow a term from the world of information technology – it could become the 'middleware' to progressively be able to make more of the banks' data transparently available.

Complaints data can be used to illustrate the approach I am recommending. In Chapter 19.1, I set out my reasons for my view that the Code should not mandate a uniform approach to complaint recording.

Instead I think that the CCMC, as a trusted and independent body, with the explicit role of monitoring, should analyse complaints data and to do the 'translation work' for the community and provide some assurance as to the figures equivalence. I think this would be more likely to generate cooperation from industry than looking to government regulators to progressively force consistency. There would be practical limitations to this approach. For one thing, translated equivalent data would not be reliable enough for 'league table' comparisons and could not be used to criticise one bank over another. But equivalent data could be used to build up a picture of key issues for a signatory bank – eg. complaint growth trends for particular products. It could be used to make generalised observations – for example, the cohort of banks that have a particular approach to (say) cross-selling or debt collection have lower related complaints figures than the cohort who don't.

Financial difficulty data is also an area of great interest to stakeholders. At the moment, the CCMC publishes in its Annual Reports aggregate data about the number of requests for financial difficulty assistance and the number of requests that were granted. But no insights are provided as to the different practices of signatory banks and, for example, the implications for debt recovery action by banks. A deeper analysis would be of great value to stakeholders generally.

I recognise that it might take a period of years to build up sufficiently useful data. I imagine that as part of the CCMC's business planning, some priorities would be set in relation to developing equivalent data and a work plan agreed and resourced. No doubt there would be much to be learned and some difficult issues to be resolved along the way.

Recommendation 97

The CCMC should be explicitly tasked with progressively working with industry to develop the ability to publicly report on relevant signatory bank data and statistics, including acting as the trusted 'translator' of disparate bank information, producing equivalent information to enable broader reporting.

20.11. Powers and sanctions

Throughout this report, I have emphasised my view that this voluntary Code should be focused on continuous improvement and public confidence. It is in this latter objective that calls have come from non-industry stakeholders for a more robust set of consequences or sanctions to be applied by the CCMC.

I have approached this issue with some caution. A voluntary Code is not government regulation. This Code must strike a balance between measures that strengthen credibility and public trust and continuing to have high levels of cooperation and openness from its signatory banks.

For completeness and credibility, it is, however, my view that any package of improvements that signatory banks put to the community arising from this Review must include some toughening of the compliance monitoring of the Code and the consequences for non-compliance.

In my view, a sensible, reasonably credible package would include:

1. The ability for CCMC to require rectification or implementation of recommendations in its own motion reports within a reasonable period of time determined by the CCMC after consultation with the bank.

2. The ability for the CCMC to require corrective advertising and/or publication of information relating to the breach.

3. The ability for the CCMC to specify that an independent compliance audit of the signatory bank's remediation be conducted at the bank's expense and provided to the CCMC.

4. Suspension or termination of status as a signatory to the Code.

I expect that there would be little or no cost to the CCMC and with the expected continuation of a cooperative approach, it would be rare that any of these would have to be imposed on a signatory bank.

I have not accepted all submissions put to me regarding sanctions. For example, I do not think it is correct for a breach to cause expulsion from the ABA – not all ABA members are signatories to the Code and there is sufficient variation in the scale and business models of member banks to persuade me that this is reasonable. I am advised that some member banks would not offer any services covered by the Code.

I also do not think that a framework of fines is appropriate to a voluntary Code (nor can I imagine an amount for a Code breach fine that would not be viewed as derisory in the context of organisations where revenues are measured in tens of billions of dollars).

Recommendation 98

The Code should strengthen the powers of CCMC, including the ability to:

a) require rectification or implementation of CCMC recommendations from own motion inquiries within a reasonable period of time (to be specified by the CCMC after consultation with the signatory bank);

b) require corrective advertising and/or publication of information;

c) require an independent compliance audit of the signatory bank's remediation actions; and

d) suspend or terminate status as a signatory to the Code.

20.11.1. Compensatory gestures

An interesting proposal put to me was that signatory banks should offer a small compensatory financial gesture where a straightforward provision of the Code is not met. An example offered was for non-timely cancellation or failure to cancel a recurring payment. This it was argued, would be a moral equivalent to exception fees and penalties applied to customers for (say) late payments and be only fair in the circumstances. An example pointed to from another setting was small customer service payments commonly made in the telecommunications space.

At first blush, the idea has some merit. There is much resentment from customers about what is perceived as a double-standard in the relationship between them and their bank. I am sure that this would be something of a minor embarrassment that signatory banks would seek to avoid and no doubt for some customers, there would be some satisfaction on receipt. I also have no doubt that it would likely obtain some media attention on release of the industry response to this Report.

I think however, that there are some practical issues. Which breaches would attract compensatory payments? If not all breaches attracted compensation gestures, what would be the policy basis for the 'ins and outs'? How much should the payment be? (For some straightforward late service items there might be an equivalent late payment bank fee that could be used to justify the amount, but for others, it would not be so easy.) If there should be a range of payment amounts relating to the seriousness of the breach, in what circumstances would payments not apply? How would such an initiative sit with the philosophy of external dispute resolution where compensation is provided for financial loss, but usually not otherwise? Would an initiative of this kind further confuse the role of the CCMC vis a viz EDR.

I struggled to come up with practical responses to these issues and I am sceptical that the ABA could frame a system that would be accepted by all signatory banks. Even if a coherent policy for all of this could be found, I am also concerned any payment made would be seen as derisory at least as often as it was seen as fair. Finally, (however minor the amounts might be) this would take the Code into the conceptual area of compensation – the territory of IDR and EDR – and potentially setup an expectation by individuals alleging a breach that CCMC would investigate and enforce the compensatory gesture.

While there may be circumstances in which it would make sense for a signatory bank to voluntarily offer a goodwill payment where the bank has failed to comply with Code obligations (see discussion on direct debit cancellations at Chapter15.2), I am not persuaded that I have a reasonable basis to propose a compensation regime as part of the Code.

21. ASIC APPROVAL OF CODE

The question of whether the ABA should apply to ASIC for approval of the Code under Corporations Act section 1101A has received quite some attention with strong arguments put to me both for and against this.

Whilst not doing justice to the full arguments, the arguments for ASIC approval centred around robustness with stakeholders seeing the process as a toughening of standards, creating a stronger linkage to the regulatory system and promoting more of a compliance/enforcement orientation.

For those against, the concern is that the Code would move from being a voluntary promise by the banks to the community to taking on more of a regulatory flavour and becoming 'just another compliance obligation' which would be something to meet as a minimum standard.

21.1.1. RG 183 Key criteria for code approval

In order for the Code to be approved by ASIC, the Code must meet the legislative criteria as expanded upon in ASIC Regulatory Guide RG.183 (see Figure 24 below).

Figure 25. - ASIC Regulatory Guide 183 Table 1 Key criteria for code approval

Criteria	Reference
Freestanding and written in plain language	RG 183.55 & RG 183.129
Body of rules (not single issue, unless Section E of this guide applies)	RG 183.19 & RG 183.24
Consultative process for code development	RG 183.49–RG 183.54
Meets general statutory criteria for code approval	RG 183.28–RG 183.41
Code content addresses stakeholder issues	RG 183.55–RG 183.62
Effective and independent code administration	RG 183.76–RG 183.81
Enforceable against subscribers	RG 183.25–RG 183.27
Compliance is monitored and enforced	RG 183.79–RG 183.81
Appropriate remedies and sanctions	RG 183.68–RG 183.73
Code is adequately promoted	RG 183.78–RG 183.80
Mandatory three-year review of code	RG 183.82–RG 183.84

Source: ASIC Regulatory Guide 183.12

Although it is a matter for ASIC, on my read of the Guide, it seems that the current Code would meet most - but perhaps not all of the criteria. Many of the recommendations made in this Review would bring the Code closer to compliance with RG. 183, however there remains a conceptual difference between the Code as I see it in the future and the RG.183 vision. This difference is minor but centres around the 'harder edged' enforcement features such as reporting to ASIC, sanctions such as fines and compensation for loss.

This minor mismatch is completely understandable. ASIC's Regulatory Guide was developed some time ago, albeit last revised in March 2013, and is designed to accommodate a range of different codes. I do not see the difference as so significant that it would threaten the concept of a voluntary code, nor do I have any sense that the industry would consider ASIC approval to be a deal-breaker. The concepts of a voluntary, aspirational industry code can co-exist with regulatory approval.

I also consider that ASIC approval is something of an essential element to community acceptance of a re-packaged Code, albeit I think that many have an unrealistic expectation of what ASIC would actually do once the Code was approved. Perhaps the telling quote I received in my consultations was:

> *". . and why wouldn't the banks want the Code to be approved by ASIC?"*

No matter the merits, in the court of public opinion, a response based on subtle philosophical/conceptual differences is unlikely to be convincing. Worst of all, it sounds 'tricky. Whereas, I think that willingly volunteering to have the Code approved by ASIC would have a very different sound.

Recommendation 99

Once it has been re-drafted, the Code should be submitted to ASIC for approval under Corporations Act section 1101A and Regulatory Guide 183.

22. NEXT STEPS

While the next steps following this Report are, of course for the ABA to determine, some stakeholders have asked that from the perspective of the Reviewer, I set out any observations I have for the next steps.

22.1. Steps

The key steps that I see will be needed to complete the Review include:

1. Initial consideration of the Report
2. Publishing the Report
3. ABA response
4. Considering other reviews and recommendations and integrating into the ABA response
5. Drafting the new Code
6. Consulting on the draft new Code and transitional issues
7. Finalising the Code – likely for submission to ASIC for approval
8. Once approved, implementation including undertaking any necessary transitional work
9. Development of supporting Industry Guidelines where required

22.2. Implementation risks

From my observations during the Review, the main risks that I see in the steps following acceptance of this Report are briefly discussed below along with a few observations on risk mitigation.

1. Risk management

Much of what I have recommended depends on the ability of signatory banks to make high level judgements about balancing reputation and profit, short and long term interests, the interests of customers and those of shareholders and so on. In short, risk management as opposed to risk minimisation.

I have considered it a very positive indicator to see the interest and involvement of very senior bank executives in the discussions I have had during the Code review. I think it is critical that senior bank executives, those with genuine responsibility for true risk management, are closely involved in the settling of the new Code.

2. Risk of delay

Even with the best will, significant time will be required to move from an agreed response by banks, through drafting, consultation amongst signatory banks, consultation with stakeholders, finalising an Approval Draft and submitting it to ASIC (which will need time for its own processes). To some extent, this is unavoidable, but exposes signatory banks to easy criticism of appearing to be 'dragging their feet'.

To add to this, there are other reviews, some not yet complete, that must be taken into account before the industry will be able to have a full picture – including the recently released Australian Small Business and Family Enterprise Ombudsman inquiry into small business loans, the Sedgwick Review of compensation, the FOS process for reviewing its small business jurisdiction and the Ramsay Review of the external disputes resolution system.

I see the involvement of senior banking executives as discussed in 1. above as vital to minimising the risk of delay affecting implementation. It is also important for the banking industry to maintain open communication and transparency as to the process of implementation – a vital part of retaining maximum stakeholder trust and goodwill.

3. Risk of dilution

Another key risk I see (a self-interested perspective, I grant) is 'creeping dilution'. In their initial response, signatory banks may or may not commit to a principle set out in one of my recommendations – that is their decision. If an overly risk-averse approach is taken, the effluxion of both time and repeated 'refinement' may result in the end position being seen by stakeholders as having been progressively watered down, through carve-outs or qualifications or even abandoning an originally positive commitment, the cost in terms of trust will be significant.

This is a particular risk if the new draft Code must be repeatedly cycled through banks' risk and compliance experts in attempts to reach agreement – and, as will be natural over time, drops below the focus of the most senior bank executives (see Risk 1 above).

4. Risk of stakeholder acceptance of new structure

A further risk is stakeholder acceptance of Industry Guidelines. I have recommended that a number of new Code obligations should be drafted at a higher level, with supporting detail in Industry Guidelines. I have heard criticisms that previous processes had not provided enough opportunity for dialogue with non-bank stakeholders about their concerns. To reduce the risk that this Code design approach may be resisted by non-bank stakeholders, it will be important to develop the new Industry Guidelines in an open and inclusive way.

In my view, if the standing of the Industry Guideline is diminished, it will result in a push for more prescription within the Code provisions themselves – a bad outcome, I think.

5. Risk of same-old, same-old

For the revised Code to emerge as evidence of 'we hear you, we are delivering changing now' – it is my view that the development of both the new Code and supporting Industry Guidelines should be by a process that is markedly different to the 'usual'. The process itself should confirm that 'we are delivering changing now'. To my mind this should include trust-inspiring indicators such as plain-speaking, being prepared to absorb some risks and rapid decision-making.

I encourage the industry to think 'outside the usual square' in approaching the tasks ahead.

ATTACHMENT 1 – REVIEW TERMS OF REFERENCE

Source: http://www.cobpreview.cameronralph.com.au/TOR.htm

Independent Review of the Code of Banking Practice Terms of Reference

The Code of Banking Practice (the Code) is the banking industry's code of conduct which sets standards of good banking practice for banks to follow when dealing with their individual and small business customers and their guarantors. The latest version for the Code is known as the Code of Banking Practice (2013).

The Code provides for a review of the Code every five years or earlier if the member banks of the Australian Bankers' Association (ABA) request the ABA to do so. As part of the industry initiatives announced on 21 April 2016, the ABA's member banks have requested the ABA to commission an independent review of the Code and to complete this review by 31 December 20161. The ABA commissions this Code review on 7 July 2016.

Objectives

The banking industry recognises that customers and the wider community expect banks to make sure they have the right culture, the right practices, and the right behaviours.

The Code review will make sure the offer of banking products and services is done in a way that further lifts standards, accessibility and transparency across banking and bolsters the existing strength of the regulatory framework.

Banks are committed to improving their practices and continuing to meet customer needs and community expectations. We want to make sure our Code of Banking Practice is effective in enhancing banks' capacity to serve consumer interests and to building trust and confidence in banks.

To achieve this, the independent review will:

- Consider the effectiveness of the Code and identify the relevance and operation of the Code and changes which have occurred in the legal and regulatory environment, including self-regulation, and changes anticipated in banking services
- Understand and collate views about banking practices to ensure the Code continues to set standards for good banking practices building on banks' legal obligations and other relevant industry codes, standards and guidelines and reflecting consumer needs and behaviour and community expectations
- Make recommendations on how the banking industry can strengthen the operation of the Code and promote informed and effective relationships between banks and their individual and small business customers
- Give attention to the initiatives contained in the industry announcement on 21 April 2016 and other recent initiatives and the extent to which these commitments should be contained in the Code, and

- Ensure banks and consumers are clear about their rights and responsibilities and that the Code articulates the standards of behaviour expected of banks, including promotion of the Code.

Scope

The review will cover all provisions of the Code and any additional matters considered relevant to be included in the Code. The Code reviewer will give specific attention to assessing and considering:

a. Purpose and role of the Code in setting the standards for good banking practices and the benefits that the Code provides to banks and their individual and small business customers.
b. Structure of the Code and clarity in communicating the standards for good banking practices to banks and their individual and small business customers.
c. The extent to which the Code demonstrates banks' commitment to putting their individual and small business customers first.
d. The effectiveness of the key commitments of banks and whether these commitments meet consumer and community expectations to:
    i. Promote better informed decisions about banking services.
    ii. Provide information about the rights and obligations of banks and their individual and small business customers in relation to banking services, including raising awareness of the legal and regulatory frameworks governing banks.
    iii. Act fairly and reasonably towards individual and small business customers in a consistent and ethical manner.
    iv. Comply with all relevant laws and regulations relating to banking services.
    v. Take reasonable measures to provide relevant information and enhance accessibility for people in remote Indigenous communities, older persons and customers with a disability.
    vi. Provide hardship assistance to individual and small business customers experiencing financial difficulties.
    vii. Resolve complaints and disputes between banks and their individual and small business customers.
    viii. Provide appropriate staff training, including on discharging their functions, providing banking services and knowledge of the Code.
    ix. Promote the existence of the Code.
e. The role and mandate of the Code Compliance Monitoring Committee (CCMC), the appropriateness of the differences between the CCMC mandate and clause 36 of the Code, and incentives for compliance by banks with the Code.
f. The operation of the Branch Closure Protocol, taking into account the recent review and changes made to ensure the effective operation of the Protocol.

In addition, the Code reviewer will have regard to the following:

g. Definitions, including practical definitions of banking services and small business.
h. Recognition of the needs of communities in remote, rural and regional areas.

i. Dealing with the particular needs of agricultural small businesses with respect to banking services.
j. Direct debits and recurring payments made using a debit or credit card.
k. Notice provided by banks with regards to any changes with a banking service.
l. Guarantees provided by a person for the purpose of securing finance or a facility for another individual or small business customer and joint debts.
m. Laws and regulations covering banking services to individual and small business customers and the extent to which new legal obligations to act in the client's best interest and responsible lending principles are addressed or require any amendment to the Code.
n. Treatment of disclosures and communications between banks and their individual and small business customers about products, services, and the costs of these products and services and the evolving technological developments in banking services and electronic communications, including the provision of bank statements to customers.
o. Sales and distribution and advertising and marketing practices of banks.
p. The extent the Code covers the practices and qualifications of intermediaries and others banks use in the course of providing banking services.
q. Commitments to accessibility and financial inclusion, including account suitability and basic bank accounts, financial literacy and the implications of technology developments on banking services.
r. The desirability for the Code to provide for banks to develop standards for communicating and dealing with vulnerable customers including older persons, customers with a disability and Indigenous customers.
s. The desirability of the Code to include minimum standards for working with small business customers in financial distress. For example, customer communication; notice period for enforcement actions; on request by the customer, disclosing independent valuation reports of its small business customer obtained by the bank and paid for by their customer; and ethical standards of receivers/ managers (particularly for rural properties with livestock).
t. The desirability of the Code to set a reasonable compliance timeframe for a small business customer to comply with a bank's notice of demand and circumstances in which a minimum timeframe should not apply having regard to the provisions of clause 28 of the Code for the bank to work with the customer to try and help their customer overcome its financial difficulties with its credit facility.
u. The desirability of the Code to include minimum standards for the offer of credit cards, and specifically whether minimum repayment requirements or alternatives should be prescribed.

In addition, the Code reviewer is asked to consider whether the Code ought to comply, and whether it does comply with, ASIC's Regulatory Guide 183: Approval of financial sector codes of conduct [RG 183]2.

Clause 14.3 of the CCMC mandate requires the CCMC to arrange a periodic review of its activities to coincide with a review of the Code. The Code reviewer is also asked to conduct a review of the activities of the CCMC concurrently with this review. This separate and independent review is given under instructions from the CCMC. More information about this review can be found at www.ccmcreview.cameronralph.com.au.

Independent Reviewer

The ABA has appointed Mr Phil Khoury, Managing Director, Cameron Ralph Pty Ltd, an independent person with relevant qualifications and experience to conduct this review.

In commissioning this Code review and identifying the Terms of Reference, the ABA has sought the views of the ABA's Consumer Stakeholder Forum and a number of other stakeholders.

Consultation

The Code reviewer will conduct the review publicly in consultation with:

i. consumer and small business organisations
ii. financial services industry representatives
iii. Finance Sector Union and employees of banks
iv. relevant regulatory bodies
v. member banks, and
vi. other interested stakeholders.

Submissions

Submissions to the review are invited on any of the matters covered by the Terms of Reference.

The Code reviewer prefers submissions to be provided in Microsoft Word (docx) files or in PDF format. Submissions should be lodged by email to the Code reviewer at this address: Email: banking.code.review@cameronralph.com.au

Final report

Mr Phil Khoury will assess submissions received on the Terms of Reference and feedback provided and prepare a report. A draft report will be used to facilitate further consultations.

A final report will be published with findings and options about changes to improve the operation and performance of the Code. The findings and options presented by the report will take into account the submissions of all interested parties but will be determined and framed according to the independent judgement of the Code reviewer.

The findings and options will be those of the Code reviewer. The ABA and its member banks will need to consider the report and determine their response and any next steps. The banks are committed to meaningful change that is supported by independent advice and a transparent and public process, and they will have regard to the findings and options identified by the report in determining and implementing appropriate changes to the Code, consistent with their obligations including under the competition law.

Timing

The independent review is to be conducted in a timely, transparent and accountable manner. A final report will be published by the end of December 2016.

The implementation of the independent review final report's recommendations will require assessment by the banking industry and changes to be determined. Commencement and transitional arrangements for the new Code will reflect the nature of the changes made.

The banking industry is committed to ensuring that the time taken in responding to the recommendations, making any changes to the Code, and implementing the changes by banks is completed in as timely a fashion as possible.

Independence

The ABA will appoint the Code reviewer. While the banking industry will fund the review, the banking industry will not have any influence over the findings and options identified by the Code reviewer beyond our input as a participant in the review, and the Code reviewer and secretariat will act independently and not in the interests of, or on behalf of, the ABA or its members.

Mr Ian McPhee, the independent expert appointed by the ABA to oversee the progress of the commitments announced by the banking industry, will monitor the process, progress and findings of the review.

Confidentiality

It will be assumed that submissions are not confidential. Submissions may be published on the Code review website established for this review at www.cobpreview.cameronralph.com.au and be publicly available.

If a submitter wants their submission, or any part of it, to be treated as "confidential" please indicate this clearly.

The Code reviewer reserves the right to not publish submissions or other material received by the Code reviewer in the course of this review that is offensive, potentially defamatory, or clearly falling outside the scope of the review.

Footnotes:

1.http://www.bankers.asn.au/media/media-releases/media-release-2016/banks-act-to-strengthen-community-trust

2. http://download.asic.gov.au/media/1241015/rg183-published-1-march-2013.pdf

ATTACHMENT 2 – SIGNATORY BANKS

Banks that have adopted Code of Banking Practice

Source: (last updated 31 January 2014) which gives attribution to ASIC's website reporting as at 13 August 2003

Bank	Code of Banking Practice 2013	Modified Code of Banking Practice 2004	Revised Code of Banking Practice 2003	Code of Banking Practice 1993*
Adelaide Bank Limited (a division of Bendigo and Adelaide Bank as of 1 December 2008)	1 February 2014	4 April 2005	12 August 2003	✔
AMP Bank Limited	1 February 2014	10 December 2010		✔
Arab Bank Australia Limited				✔
Australia and New Zealand Banking Group	1 February 2014	16 August 2004	15 August 2003	✔
Bank of Melbourne (a division of Westpac Banking Corporation as of 25 July 2011, see Westpac Bank)				
Bank of Queensland Limited	1 February 2014	6 December 2004	7 October 2003	✔
Bank of Western Australia (a division of Commonwealth Bank as of 1 October 2012, see Commonwealth Bank)		1 April 2005	7 September 2006: Full adoption 19 January 2004: Conditional adoption	✔
BankSA (a division of Westpac Bank as of 1 March 2010, see Westpac Bank)		1 June 2004	12 August 2003	✔
Bank of Sydney	10 February 2014	1 January 2012		
Bendigo Bank (a division of Bendigo and Adelaide Bank as of 1 December 2008)	1 February 2014	1 July 2005		

Citigroup Pty Limited	1 February 2014	14 October 2004	5 April 2004	✔
Commonwealth Bank of Australia	1 February 2014	22 July 2004	12 August 2003	✔
HSBC Bank Australia Limited	31 January 2014	5 July 2004	10 May 2004	✔
ING Bank (Australia) Limited	1 February 2014	15 June 2004	3 November 2003	✔
Macquarie Bank Limited				✔
National Australia Bank Limited	1 February 2014	31 May 2004	29 August 2003	✔
Rabobank Australia Limited	1 February 2014	22 September 2008		✔
St George Bank Limited (a division of Westpac as of 1 March 2010, see Westpac Bank)		1 June 2004	12 August 2003	✔
Suncorp Metway Limited	1 December 2013	30 June 2004		✔
Westpac Banking Corporation	1 February 2014	1 June 2004		✔

ATTACHMENT 3 - DEFINED TERMS

Defined term	Explanation
ABA	Australian Bankers' Association – industry association that developed the Code
adverse repayment history information	Information provided to a credit reporting body by a signatory bank to the effect that an individual customer has made a repayment that is more than 14 days late
ASIC	Australian Securities and Investments Commission – regulator of banks' dealings with consumers
ASIC standards	ASIC's standards and requirements for the internal resolution of complaints by banks (as well as other financial industry participants). These standards and requirements are made by ASIC in accordance with legislative powers given to it.
Better Banking initiatives	The package of reforms initiated by the ABA industry including my Review
Code	Code of Banking Practice
Code customers	Individual customers and small business customers of a signatory bank
consumer credit	Credit provided to an individual that is regulated by the National Credit Code set out in Schedule 1 to the NCCP Act
DHS Code	Department of Human Services Code of Operation addressing the recovery of debts from Department of Human Services income support payments or Department of Veterans' Affairs payments
EDR scheme	A dispute resolution scheme that is independent of signatory banks (such as that operated by FOS) that has the power to resolve complaints by Code customers about signatory bank decisions

FOS	Financial Ombudsman Service – the external dispute resolution service of which all signatory bank banks are currently a member
GFC	Global Financial Crisis of 2007 to 2008
Individual customers	Customers of signatory banks who are natural persons – this excludes companies
NCCP Act	National Consumer Credit Protection Act 2009
Ombudsman Report	*Small Business Loans Inquiry Report* by Australian Small Business and Family Enterprise Ombudsman dated 12 December 2016 and publicly released on 3 February 2017
Ramsay Review	Review of external dispute resolution and complaints scheme by a Panel chaired by Professor Ramsay - terms of reference dated 8 August 2016
signatory banks	Banks that are members of the ABA and have chosen to become a signatory to the Code and thereby to become bound by the Code.

ATTACHMENT 4 - SMALL BUSINESS RECOMMENDATIONS

List of key recommendations that impact small business

Report ref.	Rec No.	Recommendation	Ombudsman Report Rec No.
Chapter 6	1.	The Code should be substantially revised and should: a) Be re-drafted in a modern structure and style b) Be drafted in layers that address the differing needs of its multiple audiences – ie. Preamble, Principles, Obligations and Industry Guidelines c) Cover all banking services offered to retail and small business customers d) Use plain, accessible language and a warmer tone as part of making the document more customer-focused and accessible e) Be as straightforward as possible with the minimum of qualification and 'fine-print' (including by absorbing some risks) f) Avoid duplicating the law g) Put complex implementation detail in Industry Guidelines Include an accompanying Guide to the relevant parts of the Code for Small Business	2
Chapter 8.3	5.	a) The Code definition of "small business" (other than for the purposes of financial products or services regulated by the Corporations Act 2001) should be amended to mean a business that employs fewer than 100 full time equivalent employees or, in the case of a business that is part of a group of companies, the group employs fewer than 100 full time equivalent employees. b) The provisions of the Code that relate to credit should apply to a small business credit facility only if below $5 million.	N/a
Chapter 8.4	6.	A new clause should be included in the Code applying to a	N/a

<table>
<tr><td></td><td></td><td>credit facility below $5 million that is provided for a small business purpose. The clause should oblige banks to explain:
a) the requirements needed to obtain bank credit;
b) additional information requirements where the lending decision cannot be made and how long a lending decision is likely to take; and
c) where possible, the main reason for a refusal to lend and the requirements to enable the bank to reconsider the application.</td><td></td></tr>
<tr><td>Chapter 8.5</td><td>7.</td><td>A new clause should be included in the Code that obliges signatory banks to provide a written pre-contractual summary statement before providing a credit facility for a small business purpose, below $5 million. The key terms and conditions must be summarised in an accessible way, for example, a table format. The types of matters that should be included in the summary are:
a) the loan period,
b) repayment obligation,
c) applicable interest rates or how these are calculated with specification of what rate is at that time,
d) fees and charges (flat fee where possible or otherwise how calculated),
e) events of default and any increased costs associated with default again with specification of what rate is at that time where a formula applies, and
f) the signatory bank's entitlement to change terms and conditions and the notice of change that will be given.</td><td>6</td></tr>
<tr><td>Chapter 8.6</td><td>8.</td><td>Clause 20.4 of the Code should be amended to require 30 business days (rather than 10 business days) where a bank exercises the power to unilaterally vary a particular small business's credit contract in a way that is materially adverse if the credit facility is below $5 million.

Instead of the current carve out where the signatory bank considers this is necessary to avoid or reduce the increase in credit risk, the only carve out should be where the small business is in default under the credit contract.</td><td>4</td></tr>
<tr><td>Chapter 8.7</td><td>9.</td><td>The Code should be amended to require a signatory bank to provide a small business customer, that is not in default under a term credit facility below $5 million, with 90</td><td>5</td></tr>
</table>

		business days' notice of a decision by the bank not to extend the loan for a further term. The ABA should consult with signatory banks about whether any types of term credit facilities should be excluded or subject to a varied rule, but with the aim for the notice requirement to apply as consistently as possible.	
Chapter 8.8	10.	Clause 28 of the Code should be rewritten to separate out more clearly the commitments that signatory banks are making to assist a customer, with a small business credit facility $5 million, in financial difficulty. In redrafting the clause, regard should be had to the language used in the United Kingdom's ***The Lending Code***. The provision should build in relevant protections that apply to consumer credit, including restrictions on signatory banks instituting or continuing with enforcement action.	N/a
Chapter 8.9	11.	The Code should be amended to require a signatory bank to provide a customer, in default under a small business credit facility below $5 million, with 30 days' notice before beginning enforcement proceedings. An exception should apply where the bank reasonably believes that more urgent action is necessary to recover the debt or avoid loss in value of the security for the credit.	N/a
Chapter 8.10	12.	The Code should be amended to require a signatory bank to have in place adequate arrangements to address potential conflicts of interest issues pertaining to proposed appointments of investigating accountants and receivers.	10
Chapter 8.11	13.	The Code should be amended to oblige signatory banks to provide all Code customers that have a banking services dispute with access to internal dispute resolution processes that meet the standards set out by the Australian Securities and Investments Commission in Regulatory Guide 165.	N/a
Chapter 8.11	14.	The Code should include the following new obligations on signatory banks: a) when informing Code customers of mediation options, signatory banks must also provide information about the customer's entitlement to access the bank's internal and then external dispute resolution process; b) signatory banks must consent to their external dispute resolution scheme having jurisdiction to decide a dispute with a Code customer that has been the subject of mediation but has failed to settle.	11

Chapter 9.3	16.	The Code should rename current clause 27 as "A responsible approach to lending" and redraft it to use clearer, more modern language. The new clause should oblige banks: a) to review the applicant's financial information, situation and requirements carefully and prudently and consider the application on its merits; and b) in general, only lend amounts that the bank believes the applicant can reasonably afford to repay.	N/a
Chapter 11.1	28.	The Code should be amended to prohibit a signatory bank from enforcing a credit facility against: a) a customer who is an individual; or b) a small business customer where the credit facility is below $5 million, if the customer has complied with loan payment requirements and has acted lawfully. The ABA should consult with stakeholders including the Australian Small Business and Family Enterprise Ombudsman about any exceptions, for example, to permit enforcement of a small business credit facility where an insolvency event has occurred.	3
Chapter 11.2	29.	a) The Code should be amended to require signatory banks processes in relation to expert valuations and investigating accountants' reports to be fair and transparent. In the case of small business, this obligation should apply to a credit facility below $5 million. b) Signatory banks should develop an Industry Guideline that sets out in some detail fairness and transparency issues. Interested stakeholders including the Australian Small Business and Family Enterprise Ombudsman should be closely involved in the development of the Guideline.	8, 9
Chapter 19.2	78	The Code should be the vehicle for the industry decision that signatory banks should appoint a Customer Advocate. While there will need to be flexibility in how the function is implemented, for external credibility any specification in the Code should include: a) a commitment to an independent perspective – ideally by appointing from outside the banking sector	12

(although they may have previous banking experience);

b) a commitment to proper resourcing and effective reporting lines that maintain effective separation;

c) a high level articulation of the role of the Customer Advocate that includes:

- enhancing the overall customer-responsiveness and effectiveness of internal dispute resolution;
- assisting the signatory bank to identify and address systemic issues that become apparent as a consequence of complaints;
- liaising with external stakeholders including small business and consumer representatives, the signatory bank's external dispute resolution scheme and the CCMC to improve customer experience; and

providing a customer "voice" within the signatory bank.

Chapter 20.9	93.	The CCMC Panel should have a fourth member with small business and/or agribusiness skills and experience along with other relevant skills. a) This member should be appointed by the Chief Ombudsman of FOS and a consumer advocate member of the FOS Board, consulting with representative organisations from the small business and farming sectors. b) The Panel should have the option of sitting with 3 or 4 members depending on the matter being considered, however the Independent Chair of CCMC should have an additional casting vote to ensure against deadlock in a 4 person Panel.	N/a

ATTACHMENT 5 – PROPOSED CODE OUTLINE

The table below illustrates a suggested outline for the new Code, cross-referencing the discussion in this Report and, where applicable, the relevant provisions in the current Code.

Heading	Description/ issue	Report reference	In current Code
Preamble	High level introduction to Code	Chapter 6.6	Cl 3.1, 4, 5, 24
Principles	Key promises by banks	Chapter 6.7	Cl 3.2, 7
Specific obligations			
Credit generally	A responsible approach to lending	Chapter 9.3, 10.4	Cl 27
	Joint debt	Chapter 12.1	Cl 29
	"Not unsuitable" assessment document	Chapter 9.4	N/a
	Lenders mortgage insurance	Chapter 17.6	N/a
	Foreign currency loans	N/a	Cl 23.2
	Credit contract events of default	Chapter 11.1	N/a
	Home loans – insurance reminder	N/a	Cl 12.6
	Valuers	Chapter 11.2	N/a
	Disclosure of late payment credit reporting	Chapter 11.3	N/a
Business purpose loans (below the specified monetary threshold)	Applying for a loan	Chapter 11.3	N/a
	Pre-contract disclosure	Chapter 8.5	N/a
	Variation of loan contract	Chapter 0	Cl 20.4
	End of loan procedures	Chapter 8.7	N/a
	Default notices	Chapter 8.9	N/a
	Investigating accountants	Chapter 11.2	N/a
	Appointment of receivers	Chapter 8.10	N/a
Credit cards	Credit limits	Chapter 10.5,10.6	N/a
	Introductory offers	Chapter 10.9	N/a
	Charging of interest	Chapter 10.7	N/a
	Application of payments	Chapter 10.8	N/a

Heading	Description/ issue	Report reference	In current Code
	Card cancellation or reduction of limit	Chapter 10.10	N/a
Reverse mortgages	Disclosure to customer	Chapter 9.5	N/a
	Entitlement to discharge loan at any time	Chapter 9.5	N/a
Guarantees	Guarantee of individual customer other than sole trader	Chapter 13.2,13.3	Cl 31
	Guarantee of small business credit facility below the specified monetary threshold	Chapter 13.2	Cl 31
	Signing process	Chapter 13.3	Cl 31
	Disclosure during the guarantee period	Chapter 13.4	N/a
	Extension of guarantee to new credit facility	Chapter 13.4	Cl 31.13
	Guarantee enforcement	Chapter 13.6	Cl 31.14
	Non-compliance with guarantor requirements	Chapter 13.7	N/a
Financial difficulty	What is financial difficulty assistance	Chapter 14.3	Cl 28.2
	Publicising financial difficulty assistance	Chapter 14.10	Cl 28.10
	Bank proactivity	Chapter 14.4	Cl 28.5
	Customer proactivity	Chapter 14.5	Cl 28.4
	Financial counsellor referrals	Chapter 14.5	Cl 28.9
	Joint debtor financial difficulty	Chapter 14.7	N/a
	Guarantor financial difficulty	Chapter 14.9	N/a
	Small business financial difficulty	Chapter 8.8	N/a
	Bank process of considering financial difficulty assistance	N/a	Cl 28.6
	Types of assistance	Chapter 14.6	N/a
	Confirmation of assistance	Chapter 14.8	Cl 28.8
	Consequences for customer	Chapter 14.6	Cl 19.2
Borrower default	Garnishing of accounts	Chapter 11.4	N/a
	Debt collection	Chapter 11.5	Cl 32
	Assignment of debts	Chapter 11.5	Cl 32
Accounts generally	Account information	N/a	Cl 15
	Maintaining account security	N/a	Cl 25
	Combination of accounts	N/a	Cl 18.3, 19

Heading	Description/ issue	Report reference	In current Code
	Joint accounts	Chapter 12.2	Cl 30.1
	Subsidiary credit or debit cards	N/a	Cl 30.2, 30.3
	Account statements	N/a	Cl 26
	Closure of accounts in credit	N/a	Cl 33
Other banking services	Foreign exchange services	N/a	Cl 23
	Direct debit cancellation process	Chapter 15.2	Cl 21
	Recurring payment cancellation process	Chapter 15.2	N/a
	Chargebacks	Chapter 15.3	Cl 12.5, 22
Fees and interest rates	Cost of credit disclosure for purposes of comparison rate preparation	N/a	Cl 14
	Application fees	N/a	Cl 18.1
	Lenders mortgage insurance costs	Chapter 17.6	N/a
	Disclosure of fees and interest rates in terms and conditions	N/a	Cl 12.4
	Transaction fees	Chapter 16.2	Cl 17
	Default fees	Chapter 16.3	N/a
	Document fees	Chapter 16.4,18.5	Cl 13.7
	Changes to fees or interest	N/a	Cl 20
Cross selling	Sales conduct	Chapter 17.3	N/a
	Customer consent	Chapter 17.4	N/a
	Consumer credit insurance	Chapter 17.5	N/a
Customers with special needs	Banking services to be financially inclusive	Chapter 18.1	N/a
	Indigenous Australians	Chapter 18.1	Cl 8
	Customers with disability	Chapter 18.2	N/a
	No or low fee bank account	Chapter 18.3,18.4	Cl 16
Bank documents and information	Code provisions incorporated	N/a	Cl 12.3
	Clear and easy to read documents	Chapter 15.1	Cl 3.1(d) , 12.2
	Disclosures in bank documents	N/a	Cl 12.4
	How terms and conditions will be provided	N/a	Cl 12.1, 12.2
	Responding clearly to requests for information	N/a	Cl 3.1, 13, 15, 18.2
	Provision of documents on request	N/a	Cl 12.1, 13, 35
	Changes to terms and conditions	Chapter 0	Cl 20

Heading	Description/ issue	Report reference	In current Code
Dispute resolution	Internal dispute resolution	Chapter 8.11	Cl 37, 39
	External dispute resolution	Chapter 8.11,	Cl 38, 39
	Customer Advocate	Chapter 19.2	N/a
Bank employees	Training	Chapter 7.2	Cl 9, 28.11
	Whistle blowing	N/a	N/a
General	Promotion of Code	Chapter 7.2	Cl 10, 11
	Stakeholder consultation	N/a	Cl 3.1, 6.3
	Review of Code	N/a	Cl 6
	Code monitoring	Chapter 20	Cl 36
	Transitional provisions	Chapter 22	Cl 2, 41
Definitions	Definitions	N/a	Cl 42
Appendix	Guide to the Code for small business customers	Chapter 6.5	N/a

ATTACHMENT 6 – LIST OF RECOMMENDATIONS

No.	Recommendation
The New Code	
1	The Code should be substantially revised and should: a) Be re-drafted in a modern structure and style. b) Be drafted in layers that address the differing needs of its multiple audiences – ie. Preamble, Principles, Obligations and Industry Guidelines. c) Cover all banking services offered to retail and small business customers. d) Use plain, accessible language and a warmer tone as part of making the document more customer-focused and accessible. e) Be as straightforward as possible with the minimum of qualification and 'fine-print'. f) Avoid duplicating the law. g) Put complex implementation detail in Industry Guidelines. h) Include an accompanying Guide to the relevant parts of the Code for Small Business.
2	The advent of the new Code should be used by signatory banks as an opportunity demonstrate and reinforce internal values and culture settings.
3	The Code should oblige signatory banks to have in place systems to identify persisting issues from enquiries, customer service and internal complaints information that may indicate that revised procedures, system changes or some additional or reinforcing training is required – and to deliver that continuous improvement as appropriate.
4	Signatory banks' websites should provide an easily navigable, clear link to the Code, with links from the obvious places such as customer service and complaints information. In order to maximise the message of change to customers, signatory banks should look at ways of coordinating publicity and messaging about the implementation of the new Code.

Small Business

5

a) The Code definition of "small business" (other than for the purposes of financial products or services regulated by the Corporations Act 2001) should be amended to mean a business that employs fewer than 100 full time equivalent employees or, in the case of a business that is part of a group of companies, the group employs fewer than 100 full time equivalent employees.

b) The provisions of the Code that relate to credit should apply to a small business credit facility only if it is below $5 million.

6

A new clause should be included in the Code applying to a credit facility, below $5 million, that is provided for a small business purpose. The clause should oblige banks to explain:

a) the requirements needed to obtain bank credit;

b) additional information requirements where the lending decision cannot be made and how long a lending decision is likely to take; and

c) where possible, the main reason for a refusal to lend and the requirements to enable the bank to reconsider the application.

7

A new clause should be included in the Code that obliges signatory banks to provide a written pre-contractual summary statement before providing a credit facility for a small business purpose, below $5 million. The key terms and conditions must be summarised in an accessible way, for example, a table format that includes:

a) the credit period,

b) repayment obligation,

c) applicable interest rates or how these are calculated (specifying the current rate),

d) fees and charges (flat fee where possible or otherwise how calculated),

e) events of default and any increased costs associated with default, again with specification of what the current rate is where a formula applies, and

the signatory bank's entitlement to change terms and conditions and the notice of change that will be given.

8

Clause 20.4 of the Code should be amended to require 30 business days (rather than 10 business days) where a bank exercises the power to unilaterally vary a particular small business's credit contract in a way that is materially adverse if the credit facility is below $5 million.

Instead of the current carve out where the signatory bank considers this is necessary to avoid or reduce the increase in credit risk, the only carve out should be where the small business is in default under the credit contract.

9	The Code should be amended to require a signatory bank to provide a small business customer, that is not in default under a term credit facility below $5 million, with 90 business days' notice of a decision by the bank not to extend the loan for a further term. The ABA should consult with signatory banks about whether any types of term credit facilities should be excluded or subject to a varied rule, but with the aim for the notice requirement to apply as consistently as possible.
10	Clause 28 of the Code should be rewritten to separate out more clearly the commitments that signatory banks are making to assist a customer with a small business credit facility below the specified monetary threshold, that is in financial difficulty. In redrafting the clause, regard should be had to the language used in the United Kingdom's ***The Lending Code***. The provision should build in relevant protections that apply to consumer credit, including restrictions on signatory banks instituting or continuing with enforcement action.
11	The Code should be amended to require a signatory bank to provide a customer, in default under a small business credit facility below $5 million, with 30 days' notice before beginning enforcement proceedings. An exception should apply where the bank reasonably believes that more urgent action is necessary to recover the debt or avoid loss in value of the security for the credit.
12	The Code should be amended to require a signatory bank to have in place adequate arrangements to address potential conflicts of interest issues pertaining to proposed appointments of investigating accountants and receivers.
13	The Code should be amended to oblige signatory banks to provide all Code customers that have a banking services dispute with access to internal dispute resolution processes that meet the standards set out by the Australian Securities and Investments Commission in Regulatory Guide 165.
14	The Code should include the following new obligations on signatory banks: a) when informing Code customers of mediation options, signatory banks must also provide information about the customer's entitlement to access the bank's internal and then external dispute resolution process; b) signatory banks must consent to their external dispute resolution scheme having jurisdiction to decide a dispute with a Code customer that has been the subject of mediation but has failed to settle.
Responsible Lending	
15	The Code should give prominence to the banks' commitment to lend responsibly by including this in Principles that appear at the front of the Code.

16	The Code should rename current clause 27 as "A responsible approach to lending" and redraft it to use clearer, more modern language. The new clause should oblige banks: a) to review the applicant's financial information, situation and requirements carefully and prudently and consider the application on its merits; and b) in general, only lend amounts that the bank believes the applicant can reasonably afford to repay.
17	The Code should make explicit that the obligation in current clause 27 is owed to a guarantor not just the borrowing customer.
18	The Code should be amended to include a new provision that obliges signatory banks to provide an applicant for consumer credit with the bank's 'not unsuitable assessment' prepared in accordance with National Consumer Credit Protection Act 2009 Part 3-2. This document should be provided free of charge, and as a matter of course, prior to the customer signing the credit contract.
19	The Code should be amended to include protections for reverse mortgage customers that match those set out in clause 8 of the Customer Owned Banking Code of Practice.
Credit Card Lending	
20	The Code should be amended to include a new obligation that applies to signatory banks when undertaking a 'not unsuitable' assessment in relation to a consumer credit card (new credit card or credit increase). The bank should assess the consumer's capacity to pay the full amount of the card credit limit in a reasonable time period.
21	The Code should be amended to include a new obligation that prohibits signatory banks from providing a customer with a credit card credit limit that is more than that applied for by the customer or more than the cost of goods purchased in a linked credit transaction.
22	The Code should be amended to include a new obligation that prohibits banks from offering a credit card credit limit increase to a Code customer, other than in response to a customer-initiated specific request for a higher credit limit. The drafting should make it clear that the requirement for a customer-initiated specific request is not met by the customer 'opting in' to the bank making credit limit increase offers to the customer.

23	The Code should be amended to include: a) a prohibition on signatory banks charging Code customers interest on the portion of their credit card balance that is paid off by the due date; and b) an obligation on signatory banks to specify on a statement the amount of the interest charges that are being conditionally waived, explain that the waiver only applies if the payment is made on time and that interest charges will be reinstated and added to future statements for any portion of the monthly balance not paid on time.
24	The Code should be amended to include a new obligation that signatory banks apply Code customer credit card payments so that higher interest debts are discharged first – applying to all cards.
25	The Code should be amended to include a new obligation that signatory banks provide their Code customers with notice (in the form preferred by the customer) at least 30 days prior to expiry of an introductory offer period during which no or low interest accrues on all or a portion of the account balance.
26	The Code should be amended to include a new obligation that wherever there is functionality (electronic or otherwise) for a customer to alter a credit card limit, this must (equally and as prominently) include the ability to reduce the credit limit or to cancel a Code customer's credit card.
27	The Code should be amended to include a new obligation that requires a signatory bank to notify a Code customer in writing if the bank exercises its right to cancel the customer's credit card. The notification should, where possible, include an explanation of the reasons for the cancellation and provide contact details should the customer wish to complain.
Credit Contracts and Borrower Default	
28	The Code should be amended to prohibit a signatory bank from enforcing a credit facility against: a) a customer who is an individual; or b) a small business customer where the credit facility is below $5 million, if the customer has complied with loan payment requirements and has acted lawfully. The ABA should consult with stakeholders including the Australian Small Business and Family Enterprise Ombudsman about any exceptions, for example, to permit enforcement of a small business credit facility where an insolvency event has occurred.

29	a) The Code should be amended to require signatory banks processes in relation to expert valuations and investigating accountants' reports to be fair and transparent. In the case of small business, this obligation should apply to a credit facility below $5 million. b) Signatory banks should develop an Industry Guideline that sets out in some detail fairness and transparency issues. Interested stakeholders including the Australian Small Business and Family Enterprise Ombudsman should be closely involved in the development of the Guideline.
30	a) The Code should be amended to require signatory banks to disclose in individual customers' bank statements if the bank reported adverse repayment history information to a credit reporting body in connection with the customer's account during the period of the statement. b) The ABA and signatory banks should develop an Industry Guideline to assist banks to provide disclosure in a way that is consistent and comprehensible for customers. Proposed wording should be consumer tested.
31	The Code should be amended to include an obligation on signatory banks to comply with the Department of Human Services' Code of Operation – and to make this clear to customers and creditors.
32	The Code should be amended to include an obligation on a signatory bank, where a Code customer's debt has been assigned and the bank will not be the future contact with the customer about their debt, to arrange for a written notice advising of the change to be sent to the customer on the bank's letterhead. The notice should set out details of the debt including the amount currently owing and the name and contact details of the purchaser of the debt.
33	a) The Code should be amended to require signatory banks to develop processes to monitor compliance by their debt assignees with legislation, ASIC's Debt Collection Guidelines and the Code Principles. b) The ABA and signatory banks should develop a scalable Industry Guideline to shape expectations as to reasonable conduct by debt assignees and a robust monitoring program for them.
Joint Account Holders	
34	Clause 29 of the Code should be redrafted to require a co-debtor to receive a "substantial benefit" under the credit facility and a signatory bank to make reasonable enquiries to ensure that this is the case (thereby reversing the position currently achieved by the words "it is clear, on the facts known to us"). In the case of a credit facility for the purpose of a small business, the clause 29 obligation should only apply to a credit facility below $5 million.

35	Clause 29 of the Code should specify that a credit facility is unenforceable against a person who is accepted as a co-debtor but who, the signatory bank should have known, was not receiving a substantial benefit under the credit facility. In the case of a credit facility for the purpose of a small business, the clause 29 obligation should only apply to a credit facility below $5 million.
36	Clause 30 of the Code should include a new provision committing signatory banks to act upon instructions from a joint account holder either: • to amend the account operating instructions to "two to operate"; or • to place a hold on the account. A footnote to the provision should refer to the ABA Industry Guideline ***Financial Abuse and Family and Domestic Violence***, November 2016 for more explanation.
Guarantors	
37	Clause 31 of the Code should be should be redrafted to deal separately with: • guarantors of credit to an individual other than a sole trader; and • guarantors of a credit facility below the specified monetary threshold provided for a small business purpose.
38	A signatory bank should be obliged to provide a guarantor with the signatory bank's assessment that credit is "not unsuitable" for the debtor, where the signatory bank is required by National Consumer Credit Protection Act 2009 to prepare this.
39	The Code should be amended to prohibit signatory banks from signing a guarantor, who has not been legally advised, until at least the third day after the provision of all required information to the guarantor. This provision should also apply to a guarantor of a small business credit facility below $5 million with an exception at the election of a sole director guarantor, a trustee guarantor or a commercial asset financing guarantor.
40	Before an existing guarantee is extended to cover a new credit contract, the Code should require the signatory bank to provide the guarantor with any relevant updated information available to the signatory bank as to the current financial situation of the debtor. This provision should only apply to a guarantor of a small business credit facility below $5 million with an exception for a sole director guarantor who has chosen not to receive this information, a trustee guarantor or a commercial asset financing guarantor.

41	The Code should include a new provision obliging signatory banks to inform a guarantor where the debtor has been in continuing default for more than 2 months or where the debtor's credit contract has been changed because the debtor has encountered financial hardship. This provision should only apply to a guarantor of a small business credit facility below $5 million.
42	In consultation with consumer representatives, signatory banks should enhance Industry Guidelines to assist bank staff to identify when a guarantee should be viewed as financial abuse and accordingly when the signatory bank should exercise its discretion not to accept a guarantee as security for credit. The guidance should cover the factors that might be suggestive of financial abuse and what further steps a signatory bank should take in response, including enquiries about the guarantor's financial position to assess the extent of hardship that would result if the guarantee is enforced by the signatory bank.
43	The Code should be amended to require signatory banks to have recourse to security provided by an individual customer borrower, before the signatory bank has recourse to the guarantor's security, unless the guarantor and individual customer borrower agree otherwise.
44	The Code should specify that a guarantee is unenforceable if the signatory bank fails to comply with the pre-execution requirements. Similarly non-compliance with a post execution requirement means that the guarantee is unenforceable in relation to debt or costs that accrue after that time.
45	The ABA and signatory banks should agree a monetary limit up to which signatory banks must consent to their EDR scheme having jurisdiction to decide a claim about a guarantee to secure a home loan to an individual customer (if the EDR scheme's terms of reference would otherwise bring the dispute within the scheme's jurisdiction). The monetary limit should be at least $1 million and should be determined taking into account the average housing costs in Australian capital cities and FOS's small business monetary limit once that limit is announced. The Code should be amended to include this commitment.
Financial Difficulty	
46	The Code should give prominence to signatory banks' commitment to support customers facing financial difficulty by including this in Principles that appear at the front of the Code.

47	The Code should explain the concept of financial difficulty and, for consumer customers, the extent of overlap with the legislative financial hardship requirements. A diagrammatic presentation of the categories of financial difficulty, with examples, along the lines of the ABA Industry Guideline ***Promoting understanding about banks' financial hardship programs*** would be helpful. The description in the ABA Industry Guideline diagram of late payment assistance should, however, be revisited to ensure that it does not encompass situations that are properly within the legislative concept of financial hardship.
48	The Code should include a new clause that obliges signatory banks to establish systems and processes to identify and contact individual customers at high risk of future financial difficulty and to try and assist those customers. The clause could include a non-exclusive list of factors that could be taken into account for the purposes of determining customer risk, for example: • the customer repeatedly exceeding the credit facility credit limit; • multiple requests by the customer to increase their credit facility credit limits; • high or increasing numbers of default charges being incurred by the customer; • regular returned items or refused authorisations in respect of point of sale or ATM transactions; • frequent use of cash advance facility; • failure to reduce outstanding balance over time; and • a customer known to have a significantly deteriorating credit rating as identified by a credit reporting body.
49	Clause 28 of the Code should be rewritten using language that is simpler and warmer in tone. For example, clause 28.5 could "encourage" customers to "let us know" about financial difficulty. Signatory banks should commit to considering cases of financial difficulty "sympathetically and positively".
50	In place of existing clause 28.9(b), the Code should include a simple statement that in appropriate cases signatory banks will refer Code customers in financial difficulty to financial counselling organisations.

51	The ABA and signatory banks should continue to regularly review ABA Industry Guideline ***Promoting understanding about banks' financial hardship programs.*** The next version of the Guideline could usefully address the importance of signatory banks ensuring that restructured arrangements are sustainable and sufficiently take account of affordability for the customer. It would also be useful to address what a customer should do if they find that they cannot comply strictly with an agreed financial difficulty assistance arrangement. When developing the next iteration of the Guideline, the ABA and signatory banks should work closely with consumer advocates.
52	Clause 28.2 of the Code should be amended to contemplate assistance by a signatory bank to help a Code customer to overcome short term or longer term (but nevertheless finite) financial difficulties with a credit facility provided by the signatory bank.
53	Clause 28 of the Code should be amended to include a new provision that a signatory bank may, at its discretion, decide to waive a small unsecured debt if the bank is provided with evidence that the person is in long term financial hardship and the circumstances warrant a compassionate approach.
54	Clause 28 of the Code should acknowledge that financial difficulty assistance may be sought by a co-debtor, in the absence of agreement from the other co-debtor, and that signatory banks will try to assist particularly in situations of financial abuse or family violence. The clause should have a footnote referring to the ABA Industry Guideline ***Financial Abuse and Family and Domestic Violence***, November 2016 for more explanation.
55	Clause 28.8 of the Code should be amended to require a signatory bank to provide written notification of financial difficulty assistance that it has agreed to provide this to an individual customer if: • the customer so requests; or • the assistance will span a period of 30 days or more. The notice should include the details of the repayments required, what will happen at the end of the arrangement and any adverse consequences for the customer in accepting the arrangement, such as, whether the account will be listed as overdue on the customer's credit report, whether default interest rates or fees will apply and whether the customer's credit card will be cancelled. This provision should also apply where financial difficulty assistance is provided to a small business in respect of a credit facility of below $5 million.

56	The Code should be amended to introduce a financial difficulty assistance regime for guarantors of Code customers who are in debt to a signatory bank because the bank has made a demand under the guarantee. The ABA and signatory banks, working with consumer representatives, should develop industry guidance detailing the options for assistance.
57	Clause 28.10 of the Code should be extended to incorporate the additional commitments: • information about the availability of financial difficulty assistance should be "prominently" displayed on each signatory bank's website and a search for the words "hardship" and "financial difficulty" must find the relevant information; • each branch should display a poster and brochures about the availability of financial difficulty assistance and how to inquire about this; and • account statements, default notices and collections letters should advise that financial difficulty assistance is available and how to inquire about this.
Terms and Conditions, Direct Debits and Chargebacks	
58	The redrafted Code should include clause 3.1(d) as an obligation that is capable of being monitored and enforced by the CCMC.
59	Signatory banks' Customer Advocates should be tasked with championing better customer service in relation to direct debit cancellation requests. They should work with internal management to achieve this, using all the resources and tools that they will need to be effective in their roles over the long term. Signatory banks' Customer Advocates should report regularly to the CCMC as to the steps the signatory bank is taking to enhance compliance by staff with customer direct debit cancellation requests and the impact those steps are having. The CCMC should publicly report on signatory banks' progress in improving compliance with direct debit cancellation requests, including by releasing signatory banks' data on an anonymised basis, together with the CCMC's trend analysis and assessment of the adequacy of signatory banks' efforts.
60	Signatory banks should work with card scheme companies to build functionality and processes to enable signatory banks to carry out customer requests to cancel recurring card payment arrangements. The aim should be to put this in place within two years. The CCMC should be kept appraised of progress in relation to this and should report about this in its Annual Reports. Once the required functionality and processes are in place, signatory banks should undertake to carry out their customers' recurring payment arrangements cancellation requests free of charge.

61	a) Clause 22.1 of the Code should be amended to prevent signatory banks from imposing a shorter timeframe for making a chargeback claim than that available under the credit card scheme rules. b) Clause 22.2 of the Code should be amended to require signatory banks to provide clear and prominent information to card holders about what they should do about unauthorised card transactions. This information should be provided both at the time of issue of a card and at regular intervals thereafter. c) The ABA and signatory banks should develop and implement a plan of action to make Code customers more aware of their chargeback rights and to better help them to access those rights. The CCMC should be kept informed about progress and publicly report about this work.
Fees	
62	Clause 17 should be redrafted to apply more generally to banking service transaction fees. The general principle should be that the amount of the fee is disclosed (or, where the fee is referrable to the size of the transaction, the method of calculation of the fee) each time that the customer is invited to use the banking service.
63	The Code should include a new provision that obliges a signatory bank to set default fees that are reasonable having regard to the signatory bank's costs. A broad definition of default fees should be included in the Code to give this provision a wide reach.
64	Clause 13.7 of the Code should be amended by adding in the words "but we will waive our right to a fee where we think your circumstances warrant this".
Sales practices including insurance cross-selling	
65	The Code should require signatory banks to ensure that their staff and authorised representatives, when promoting or selling financial services or products to Code customers, do this in a fair and ethical manner, without engaging in pressure sales techniques.
66	The Code should prohibit a signatory bank from charging a Code customer for the acquisition of a financial product or service from or through the signatory bank unless the signatory bank is able to evidence that the customer's explicit consent was obtained at the time of the acquisition.

67 The Code should include a new provision that applies to signatory bank distribution of consumer credit insurance. This should specify:

a) A signatory bank's representative must not promote consumer credit insurance to an individual customer where the signatory bank's representative should have been aware that the individual is not suited to the policy.

b) A signatory bank must provide an individual customer with prominent, timely and sufficient information to make an informed decision as to whether or not to purchase the product.

c) Signatory banks should ensure that their consumer credit insurance sales processes are tailored appropriately to meet the needs of a wide range of customers, including those not familiar with consumer credit insurance.

A signatory bank must not complete an individual customer's application for consumer credit insurance earlier than the day after information is provided to the customer about consumer credit insurance. Moreover the sale may only be completed if the customer contacts the signatory bank to proceed with the application – a signatory bank representative must not follow up the customer to see if the customer wants to proceed.

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68 The ABA and signatory banks should develop a fact sheet that explains lenders mortgage insurance to home loan borrowers. The Code should require this to be provided to a Code customer who is required by a signatory bank, as a condition of their home loan, to obtain lenders mortgage insurance.

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69 The Code should either:

a) restrict signatory banks from charging a home loan customer for lenders mortgage insurance more than the actual cost incurred by the signatory bank net of any discount or commission paid by the insurer to the signatory bank and require a signatory bank to pass on to a home loan customer any rebate of premium that the signatory bank receives if the customer repays or refinances their loan; or

b) impose a disclosure regime whereby signatory banks disclose to their customers any discount, commission or rebate obtained by the bank at the inception of the policy and at the time of cancellation of the policy.

Customers With Special Needs

70	As one of the Principles set out at the front of the Code, there should be a commitment by signatory banks to financial inclusion and recognition of the special needs of some customer groups. To implement this Principle, the Code should oblige signatory banks to design and make available their banking services in a way that is inclusive and has regard to the needs of customers taking into account factors and circumstances including work status, age, gender, geographic distance, language, indigenous status, health and disability and experience of trauma, abuse or disadvantage including a natural disaster, family violence or socio-economic disadvantage. The ABA and signatory banks should continue to develop Industry Guidelines to give further depth and specificity to this obligation.
71	Redrafted clause 8 should apply to all indigenous Australians, not just those in remote communities. It should use clear and direct language to create meaningful obligations, thereby providing substance to the Principle of financial inclusion.
72	The Code should include a new provision headed "Customers with disability" obliging signatory banks to develop policies and procedures recognising: a) that customers should be presumed to have the ability to make decisions about access to banking services; b) that customers may be capable of making and communicating decisions concerning banking services, where they have access to necessary support; c) that customers are entitled to support in making and communicating decisions; and d) signatory banks should recognise supporters and respond to their requests, consistent with other legal duties.
73	The Code should specify that if a signatory banks offers a fee-free transaction account to eligible customers (a basic bank account), the signatory bank may only refuse to allow an eligible person to open an account of this type if: a) the opening of the account would be unlawful; or b) the person has conducted themselves in dealings with the signatory bank in a way that amounts to an offence under legislation (whether or not the person has been charged with committing an offence).

74	The Code should oblige signatory banks that offer a basic bank account to include in their bank account application forms: • Information about the basic bank account; and • targeted questions to test the eligibility of an applicant for an account of this type, so that the signatory bank can offer a basic bank account to the applicant if eligible for this product.
75	The Code should oblige a signatory bank that offers a basic bank account to take the opportunity of contact with individual customers: • at high risk of future financial difficulty; or • in financial difficulty, to make those customers aware of the option of transferring to a basic bank account.
76	Clause 16 of the Code should be redrafted to remove repetition and to create meaningful obligations using clear and direct language. The obligation to publicise the availability of basic bank accounts should be strengthened, for example, the information should be "prominently" displayed on the bank's website and website navigation should reliably lead to the relevant information.
77	The Code should require a signatory bank, that charges a fee where a customer elects to receive post mailed account statements rather than emailed statements, to waive those fees for a customer who does not have a home internet connection.

Complaints Handling

78 Any new obligation on signatory banks to appoint a Customer Advocate should be included in the new Code. While there will need to be flexibility in how the positions are implemented, for external credibility any specification in the Code should include:

a) a commitment to an independent perspective – ideally by appointing from outside the banking sector (although they may have previous banking experience);

b) a commitment to proper resourcing and effective reporting lines that maintain effective separation;

c) a high level articulation of the role of the Customer Advocate that includes:

- enhancing the overall customer-responsiveness and effectiveness of internal dispute resolution;
- assisting the signatory bank to identify and address systemic issues that become apparent as a consequence of complaints;
- liaising with external stakeholders including customer advocates, the signatory bank's external dispute resolution scheme and the CCMC to improve customer experience; and
- providing a customer "voice" within the signatory bank.

Code Monitoring and Compliance

79 The Code and the CCMC Mandate should be redrafted to make it clear that the primary focus of the CCMC should be its monitoring and public assurance – with the areas of greatest value-adding activity being:

a) Taking a risk-based approach to prioritise investigative effort on systemic non-compliance (common problems, complaint and reported breach trends, etc);

b) Transparency – providing industry and community with information demonstrating compliance with the Code and identifying trends and potential problem areas; and

c) Supporting continuous improvement of banking practice by providing feedback on implementation, identifying and promoting good practice conduct and compliance, and identifying areas for new and strengthened Code provisions or industry guidelines.

80 Promotion of awareness of the CCMC should be focused on points of advocacy, such as industry associations, consumer advocates and other lobby organisations. The purpose here is to provide assurance that the Code is being monitored and that the CCMC is being active in its role.

81	The CCMC should be renamed the "Banking Code Monitoring Panel".
82	The CCMC Mandate should explicitly recognise the CCMC role in promoting transparency and trust in signatory banks' compliance with the Code and embed a responsibility for publishing information about the effectiveness of and compliance with the Code, including statistics, results of inquiries, determinations and case studies as appropriate.
83	The Code should oblige signatory banks to be proactive in providing information to the CCMC including arranging regular engagement with their internal disputes resolution area and internal Customer Advocate.
84	The Code and the CCMC Mandate should explicitly set out its role and responsibility to proactively gather relevant information about the effectiveness of and compliance with the Code – including from sources external to the banks such as bank customers, Australian Small Business Ombudsman, consumer advocacy groups, financial counsellor networks, Legal Aid organisations, community legal centres, consumer affairs departments and other government regulators.
85	The Code and CCMC Mandate should make it clear that referrals from external dispute resolution schemes, the ABA, regulators, consumer or other stakeholder organisations will similarly be fed into CCMC priority setting, but will not necessarily be automatically investigated, however in each case, the CCMC will provide a written explanation of the reasons for any decision not to pursue a referred matter.
86	The Code should oblige signatory banks to report breach information as required by the CCMC on a quarterly basis.
87	CCMC should work towards an agreement with signatory banks' EDR schemes to establish an explicit responsibility for the scheme's Systemic Issues Team to refer to the CCMC any Code compliance issues the team identifies through its own work. The arrangements should be set out in writing between the EDR scheme and CCMC.

88	The CCMC and signatory banks' EDR schemes should develop protocols for appropriate exchange of information and access to relevant EDR data, subject to safeguards that include: a) Explicit consent from EDR scheme complainants; b) Restricting access only to CCMC staff and authorised contractors; c) CCMC staff subject to the same audit and security controls as EDR staff; and d) EDR costs are met. The arrangements should be set out in writing between the EDR scheme and CCMC.
89	The CCMC should adopt a risk-based approach to focus its effort, including: a) selecting which individual or small business reports of suspected breaches are formally investigated; b) where an individual or small business reports a suspected breach to CCMC and has not been to EDR, CCMC should refer them to the appropriate scheme; and c) selecting which referrals from other organisations it makes the subject of an own-motion-inquiry.
90	The Code, CCMC Mandate and CCMC communications material should adopt language that echoes the risk-based approach to be taken by the CCMC, including: a) that individuals that take their matter to CCMC are "reporting a suspected breach"; b) that there should be clear information that CCMC will use this 'report' information to inform its risk assessments – but will only investigate selected individual matters; and c) that referrals from EDR, the ABA, regulators or consumer organisations will similarly be fed into CCMC priority setting, but will not necessarily be automatically investigated.
91	The Code, CCMC Mandate and CCMC communications material should adopt language that emphasises the difference between EDR and Code monitoring, including: a) language in the Code, Mandate and public information should eliminate reference to 'determinations' and any other EDR-like terms; b) reduce the degree of detail and specificity regarding investigations in the Code, allowing the CCMC to tailor the process used to the matter at hand.

92	The CCMC should be empowered to investigate breaches of the Code for up to two years after the individual or organisation reporting the suspected breach became aware of the events in question or reported the matter to a relevant EDR organisation.
93	The CCMC mandate should be redrafted along the lines recommended for the Code, in plain language and with a minimum of qualifiers and caveats.
94	The CCMC Panel should have a fourth member with small business and/or agribusiness skills and experience along with other relevant skills. a) This member should be appointed by the Chief Ombudsman of FOS and a consumer advocate member of the FOS Board, consulting with representative organisations from the small business and farming sectors. b) The Panel should have the option of sitting with 3 or 4 members depending on the matter being considered, however the Independent Chair of CCMC should have an additional casting vote to ensure against deadlock in a 4 person Panel.
95	The CCMC permanent staff mix should explicitly include strong data analytics skills.
96	The CCMC resourcing should allow for the ability to temporarily hire in specialist expertise for specific investigations or projects.
97	The CCMC should be explicitly tasked with progressively working with industry to develop the ability to publicly report on relevant signatory bank data and statistics, including acting as the trusted 'translator' of disparate bank information, producing equivalent information to enable broader reporting.
98	The Code should strengthen the powers of CCMC, including the ability to: a) require rectification or implementation of CCMC recommendations from own motion inquiries within a reasonable period of time (to be specified by the CCMC after consultation with the signatory bank); b) require corrective advertising and/or publication of information; c) require an independent compliance audit of the signatory bank's remediation actions; and d) suspend or terminate status as a signatory to the Code.
ASIC Approval of Code	
99	Once it has been re-drafted, the Code should be submitted to ASIC for approval under Corporations Act section 1101A and Regulatory Guide 183.