Australian Securities & Investments Commission

CONSULTATION PAPER 115

Responsible lending

September 2009

About this paper

This paper sets out ASIC's proposals for guidance about meeting the responsible lending obligations of Australian credit licensees in Chapter 3 of the National Consumer Credit Protection Bill 2009.

We are seeking the views of potential credit licensees and consumers on our proposals.

About ASIC regulatory documents

In administering legislation ASIC issues the following types of regulatory documents.

Consultation papers: seek feedback from stakeholders on matters ASIC is considering, such as proposed relief or proposed regulatory guidance.

Regulatory guides: give guidance to regulated entities by:

- explaining when and how ASIC will exercise specific powers under legislation (primarily the Corporations Act)
- explaining how ASIC interprets the law
- describing the principles underlying ASIC's approach
- giving practical guidance (e.g. describing the steps of a process such as applying for a licence or giving practical examples of how regulated entities may decide to meet their obligations).

Information sheets: provide concise guidance on a specific process or compliance issue or an overview of detailed guidance.

Reports: describe ASIC compliance or relief activity or the results of a research project.

Document history

This paper was issued on 2 September 2009 and is based on the National Consumer Credit Protection Bill as at 25 June 2009.

Disclaimer

The proposals, explanations and examples in this paper do not constitute legal advice. They are also at a preliminary stage only. Our conclusions and views may change as a result of the comments we receive or as other circumstances change.

Contents

The consultation process **4**

A Background to the proposals **6**
Regulation of consumer credit by the Commonwealth 6
The responsible lending obligations 7
Context of the responsible lending obligations 10
Objectives of the responsible lending obligations 10
Our general approach to administering the responsible lending obligations 11

B Proposed guidance about reasonable inquiries **12**
Making reasonable inquiries 12
Verification of information provided by the consumer 17

C Assessment of unsuitability **21**
Forming a view that the credit contract is not unsuitable 21
Determining the consumer's financial situation, capacity to repay and substantial hardship 23
Fitness for purpose: Determining the consumer's requirements and objectives in relation to the credit contract 29
Switching and refinancing 33

D Guidance about written assessment that credit contract is not unsuitable **34**

E Regulatory and financial impact **36**

Key terms **37**

List of proposals and questions **38**

The consultation process

You are invited to comment on the proposals in this paper, which are only an indication of the approach we may take and are not our final policy.

As well as responding to the specific proposals and questions, we also ask you to describe any alternative approaches you think would achieve our objectives.

We are keen to fully understand and assess the financial and other impacts of our proposals and any alternative approaches. Therefore, we ask you to comment on:

- the likely compliance costs;
- the likely effect on competition; and
- other impacts, costs and benefits.

Where possible, we are seeking both quantitative and qualitative information.

We are also keen to hear from you on any other issues you consider important.

Your comments will help us develop our policy on the responsible lending obligations in Chapter 3 of the National Consumer Credit Protection Bill 2009 (National Credit Bill). In particular, any information about compliance costs, impacts on competition and other impacts, costs and benefits will be taken into account if we prepare a Business Cost Calculator Report and/or a Regulation Impact Statement: see Section E, 'Regulatory and financial impact'.

Making a submission

We will not treat your submission as confidential unless you specifically request that we treat the whole or part of it (such as any financial information) as confidential.

Comments should be sent by 28 October 2009 to:

Sophie Waller
Senior Lawyer
Strategic Policy
Australian Securities and Investments Commission
GPO Box 9827
Melbourne VIC 3001
facsimile: (03) 9280 3306
email: policy.submissions@asic.gov.au

What will happen next?

Stage 1	2 September 2009	ASIC consultation paper released
Stage 2	30 September 2009	Comments due on the consultation paper
	28 October 2009	Date extended for comments due on the consultation paper
	October and November 2009	Drafting of regulatory guide
Stage 3	December 2009	Regulatory guide released

A Background to the proposals

Key points

Credit licensees must comply with the responsible lending conduct obligations in Ch 3 of the National Credit Bill.

While credit licensees must decide how they will meet the responsible lending obligations, we propose to provide guidance about our expectations for compliance.

This section of the paper sets out some background information in relation to our proposals

Regulation of consumer credit by the Commonwealth

1 The Council of Australian Governments (COAG) agreed on 3 July 2008 that the Commonwealth would assume responsibility for the regulation of consumer credit. The Australian Government introduced the National Consumer Credit Protection Bill 2009 (National Credit Bill) into Parliament on 25 June 2009. The national regulation of consumer credit aims to boost consumer protection and raise standards in the credit industry.

2 Regulation of consumer credit in the new regime will be the responsibility of ASIC. A key component of the new credit regime is that businesses who provide credit services or who are engaged in other 'credit activities' will be required to be licensed and meet a range of obligations, including the responsible lending obligations.

3 This consultation paper is based on the National Credit Bill. We will consider all submissions to this consultation paper before reaching a final view on whether our suggested approach is the most appropriate solution. Our final position will be published in a regulatory guide later this year and will be based on the final legislation as passed by the Australian Parliament.

Note: The Corporations Act will be amended to include a responsible lending obligation in relation to margin loans under the Corporations Legislation Amendment (Financial Services Modernisation) Bill 2009. This paper does not deal with the responsible lending provisions in relation to margin lending.

The responsible lending obligations

4 The National Credit Bill introduces responsible lending obligations for Australian credit licensees (credit licensees). These obligations will apply to both credit providers (i.e. lenders, such as banks, credit unions and finance companies) and credit assistance providers (e.g. mortgage or finance brokers).

Note: On 14 August 2009, the Hon Chris Bowen, Minister for Financial Services, Superannuation and Corporate Law, announced changes to the commencement timetable for the responsible lending provisions. The responsible lending obligations for brokers and some lenders will now apply from 1 January 2010 (instead of 1 January 2011, as previously proposed). For the remaining lenders (i.e. authorised deposit-taking institutions (ADIs) and registered finance corporations), the obligations will apply from 1 January 2011. For more information, see Media Release No. 009 at http://mfsscl.treasurer.gov.au/listdocs.aspx?doctype=0&PageID=003&min=ceba

5 Among other things, this means that before a credit licensee suggests, assists with, or provides a new credit contract or lease, to a consumer, the credit licensee must:

(a) make reasonable inquiries of the consumer about their financial situation and their requirements and objectives in relation to the credit contract; and

(b) based on these inquiries, form a view as to whether the contract is unsuitable for the consumer.

6 In addition, the responsible lending obligations also apply where a credit licensee:

(a) increases the limit on an existing credit contract, suggests that a consumer increase the limit or assists the consumer to increase the limit; or

(b) suggests to a consumer that they remain in an existing contract or consumer lease.

Note: Unless otherwise mentioned, future references to a ‘contract’ or ‘credit contract’ also include a reference to a lease.

7 The key concept is that credit licensees must not enter into a credit contract with a consumer, suggest a credit contract to a consumer or assist a consumer to apply for a credit contract if the credit contract is unsuitable for the consumer. Table 1 summarises the general Ch 3 obligations for credit licensees.

Table 1: Summary of key responsible lending obligations

What the licensee must do		Brief overview of obligation
1	Conduct reasonable inquiries about the consumer	The licensee must, before making the assessment (or preliminary assessment) of whether the credit contract is unsuitable: • make reasonable inquiries about the consumer's financial situation; • make reasonable inquiries about the consumer's requirements and objectives; • take reasonable steps to verify the consumer's financial situation; and • take any steps prescribed by the regulations to verify any matter prescribed by the regulations: cls 117, 130, 140 and 153.
2	Based on these views, make an assessment (or a preliminary assessment if providing credit assistance) about whether the contract is unsuitable for the consumer	The contract will be unsuitable if, at the time of the assessment, it is likely that: • the consumer will be unable to comply with their financial obligations under the contract, or could only comply with substantial hardship; • the contract will not meet the consumer's requirements or objectives; or • the regulations prescribe circumstances in which a credit contract is unsuitable: cls 118(2), 119(2), 131(1), 141(2), 142(2) and 154(2).
3	Give the consumer the assessment or preliminary assessment (where requested)	If the consumer requests a copy of the assessment from the licensee, the licensee must give the consumer a written copy of the assessment: cls 120, 132, 143 and 155.

Documents that licensees must provide to consumers

8 In addition to the responsible lending obligations discussed above, Ch 3 also requires licensees to provide certain documents to consumers at particular stages of the credit process. Table 2 summarises these documentation requirements. Section D outlines our proposed guidance on the obligation to provide a consumer with a copy of the assessment that a credit contract is not unsuitable.

Table 2: Summary of the Ch 3 obligations relating to documents

Document	Who obligation applies to	Brief overview of obligation
Credit guide	Credit providers, credit assistance providers and credit representatives must give a credit guide to the consumer	**Credit assistance providers** must give a credit guide to the consumer as soon as practicable after it becomes apparent to the credit assistance provider that they are likely to provide credit assistance to the consumer: cls 113(1), 136. **Credit providers** must give a credit guide to the consumer as soon as practicable after it becomes apparent to the credit provider that the consumer is likely to enter into a credit contract with them: cls 126(1), 149. **Credit representatives** must give a credit guide to the consumer at the same time that they give the consumer the credit guide of the licensee they represent: cl 158.
Quote for providing credit assistance	Credit assistance providers	**Credit assistance providers** must not provide credit assistance to a consumer unless they have given the consumer a quote and the consumer has signed and dated the quote (or otherwise indicated their acceptance of the quote): cls 114(1), 137.
Credit or lease proposal disclosure document	Credit assistance providers	**Credit assistance providers** must, at the same time as providing credit assistance to the consumer, provide the consumer with a credit or lease proposal disclosure document: cls 121, 144
Written preliminary assessment or final assessment that a credit contract is not unsuitable	Credit providers and credit assistance providers	If requested: • **credit assistance providers** must give the consumer a copy of the preliminary assessment; and • **credit providers** must give the consumer a copy of the final assessment. For further information see Section D.

Context of the responsible lending obligations

9 The vast majority of loans are made responsibly. Many providers are already required to lend responsibly. These requirements may come from a variety of sources such as legal duties, contractual obligations and industry codes.

Note: For example, the Financial Ombudsman Service (FOS) provides guidance on its approach to lending responsibly, such as the FOS Bulletins 45 (March 2005), 50 (June 2006) and 58 (June 2008). FOS has previously indicated that it may take into account failure to follow its guidelines in determining whether maladministration has occurred.

10 However, the National Credit Bill has introduced responsible lending obligations to reinforce industry good practice and because of community concern about some cases of inappropriate lending in recent years.

11 Instances of irresponsible lending have arisen due to different factors, including the growth in distribution through intermediaries, inadequate safeguards for vulnerable and remote borrowers (by both mainstream and fringe lenders), and also the growth in non-conforming loans such as ‘low-doc’ loans.

Note: See, for example:

- REP 109 *All we have is this house: Consumer experiences with reverse mortgages* (November 2007);
- REP 119 *Protecting wealth in the family home: An examination of refinancing in response to mortgage stress* (March 2008); and
- Treasury Green Paper, *Financial services and credit reform: Improving, simplifying and standardising financial services and credit regulation* (June 2008).

12 To address the issue of irresponsible lending practices, the responsible lending obligations in Ch 3 of the National Credit Bill set out the standards of conduct expected of credit licensees when they enter into a credit contract with a consumer, suggest a credit contract to a consumer or assist a consumer to apply for a credit contract.

13 Those credit licensees who are already lending responsibly will not have to significantly change their business practices to meet these new obligations. The key message for credit licensees is that the new obligations turn what is now good practice into a statutory requirement (which will therefore also be enforceable).

Objectives of the responsible lending obligations

14 The key responsible lending obligation is that licensees must ensure that they do not provide a credit contract or lease to a consumer (or suggest, or assist a consumer to enter into, a credit contract or lease) that is unsuitable for the

consumer. According to the Explanatory Memorandum to the National Credit Bill, the responsible lending provisions are intended to:

(a) introduce standards of conduct to encourage prudent lending and leasing, and impose sanctions in relation to irresponsible lending and leasing (see paragraph 3.15); and

(b) curtail undesirable market practices, particularly where intermediaries are involved in lending (see paragraphs 3.9–3.10).

15 ASIC will administer the responsible lending obligations to reduce the risk of consumers being offered loans that they cannot afford to repay or that are otherwise clearly unsuitable for them. We have formulated the proposals in this paper in light of this objective.

Our general approach to administering the responsible lending obligations

16 We will provide guidance about our expectations for compliance with the responsible lending obligations, including guidance about the kind of conduct we will expect from licensees. As this is a new statutory obligation, we are consulting on our proposed guidance and seeking industry and consumer feedback. We will discuss our proposed guidance with industry and consumer representatives before it is finalised and released.

17 We will administer the responsible lending obligations in light of other obligations that apply to credit licensees, including the general conduct obligations they are required to meet under cl 47 of the National Credit Bill, the consumer protection provisions in the *Australian Securities and Investment Commission Act 2001* (Part 2, Div 2) and other relevant credit legislation.

B Proposed guidance about reasonable inquiries

Key points

In order to determine whether a credit contract is unsuitable, the legislation requires credit licensees to make reasonable inquiries about the consumer's financial situation, and their requirements and objectives in relation to the credit contract.

We propose to provide guidance on our expectations about making 'reasonable inquiries'.

Making reasonable inquiries

18 The key responsible lending obligation for licensees is to ensure that they do not enter into a credit contract with a consumer, suggest a credit contract to a consumer or assist a consumer to apply for a credit contract if the credit contract is unsuitable for the consumer.

19 In order to determine whether a credit contract is unsuitable, the legislation states that credit licensees must make reasonable inquiries about the consumer. This means that licensees must:

(a) make reasonable inquiries about the consumer's requirements and objectives in relation to the credit contract;

(b) make reasonable inquiries about the consumer's financial situation (i.e. to determine whether they can repay the loan); and

(c) take steps to verify the consumer's financial situation.

Note: See cls 117, 130, 140 and 153.

Scalability of the reasonable inquiries obligation

20 We think that the obligation to make reasonable inquiries is scalable—that is, what a credit licensee needs to do to meet these obligations will vary depending on the circumstances. 'Scalable' means that the obligation varies depending on the circumstances, including the potential impact on the consumer of entering into an unsuitable credit contract, the complexity of the credit contract and the objectives and financial literacy of the client.

21 In administering the law on the reasonable inquiries obligation, we will take into account all the circumstances when determining whether the licensee has satisfied the obligation to make reasonable inquiries. This would include, for example, the nature of the services offered by the credit licensees. We have set out some relevant factors in relation to the concept of scalability in

Table 3. We have also set out some examples to illustrate this: see Examples 1 and 2.

Table 3: Factors relevant to the scalability of the reasonable inquiries obligation

Relevant factor	Effect on reasonable inquiries obligation
Potential impact on the consumer of entering into unsuitable credit contract	More extensive consumer inquiries are likely to be necessary where the potential negative impact on the consumer is likely to be relatively serious if the credit contract is unsuitable
Complexity of the credit contract	Less extensive inquiries are likely to be necessary where the credit contract has relatively simple terms that the consumer can easily understand
Objectives and financial literacy of the consumer	The reasonable inquiries obligation will involve attempting to resolve and clarify the consumer's objectives where the consumer: • has limited financial understanding or knowledge; • has conflicting objectives; • is confused about their objectives (or has difficulty articulating them); or • there is an apparent mismatch between the consumer's objectives and the product being considered by the consumer.

Note 1: This is not intended to be an exhaustive list of potentially relevant factors.

Note 2: As well as being relevant to the scalability of inquiries, these factors are also relevant to determining the appropriate mode of inquiry—that is, whether the inquiries should be made one-on-one with the consumer (either face-to-face or by phone) or whether it is sufficient to make inquiries of the consumer via questions on the application form.

Example 1: Scalability of reasonable inquiries

Generally, for a more basic credit contract, such as a small personal loan (i.e. one that is small relative to the person's capacity to repay), we expect that credit licensees would need to make less detailed inquiries than for a $500,000 mortgage (where this amount is a significant amount that is approaching the limit of a person's capacity to repay without substantial hardship). We would expect credit licensees to have specific processes in place for making reasonable inquiries that are appropriate for each of these situations.

Example 2: Inadequate inquiries

A consumer may approach a lender after entering into a contract to sell their residence and buy another property. The lender should carefully advise the consumer of the funding implications of the transactions and what, if any, shortfall will arise after transfer of the existing loan to the new property. If the lender discovers an error in the funding information provided to the consumer, the lender should not simply lend the shortfall where this will put the consumer in a situation of being unable to service the loan. To do so would be to compound the earlier mistake.

Proposal

B1 We propose to provide guidance (along the lines of paragraphs 20–21, Table 3 and Examples 1 and 2) that the obligation to make reasonable inquiries is scalable—that is, what a credit licensee needs to do to meet this obligation will vary depending on the circumstances.

Your feedback

B1Q1 Do you agree with our proposed approach to guidance about the reasonable inquiries obligation being scalable?

B1Q2 Is there any further guidance we should give? Please provide as much specific information as possible, as this will assist us to provide guidance that is of greater use to credit licensees.

What inquiries should licensees make?

22 We expect credit licensees to decide what inquiries they need to make in order to meet their responsible lending obligations for a given transaction. However, in administering the law, when considering whether a licensee has conducted reasonable inquiries, we would look at whether the licensee has made inquiries about the kinds of issues listed in paragraphs 23–24.

Reasonable inquiries about the consumer’s financial situation

23 Reasonable inquiries about the consumer’s financial situation could include inquiries about:

(a) the consumer’s current amount and source of income or benefits (this would include the nature of their employment, e.g. full-time, part-time or casual);

(b) the extent of the consumer’s fixed expenses (such as rent, repayment of existing debts, child support and recurring expenses such as insurance);

(c) the consumer’s variable expenses (and drivers of variable expenses such as dependants and any particular or unusual circumstances);

(d) the extent to which the existing credit contracts are to be repaid from the credit advanced;

(e) the consumer’s credit history;

(f) the maximum amount to be repaid under the credit contract (including fees);

(g) the consumer’s circumstances, including their age (particularly where they may be a minor) and number of dependants;

(h) the consumer’s assets (including nature and value); and

(i) geographical factors, such as remoteness, which may require consideration of specific issues (such as potentially higher living costs compared to urban areas).

Reasonable inquiries about the consumer’s requirements and objectives

24 Reasonable inquiries about the consumer’s requirements and objectives could include inquiries about:

(a) the amount of credit needed or the maximum amount of credit sought;

(b) the timeframe for which the credit is required;

(c) the purpose for which the credit is sought and the benefit to the consumer (e.g. how the consumer plans to use the money); and

(d) whether the consumer seeks particular product features or flexibility, and understands the costs of these features and any additional risks.

Proposal

B2 We propose to provide guidance that we expect credit licensees to decide what inquiries they need to make in order to meet the reasonable inquiries obligation for a given transaction. However, when considering whether a credit licensee has conducted reasonable inquiries, we propose looking at whether the licensee has made inquiries about the kinds of issues listed in paragraphs 23–24.

Your feedback

B2Q1 Do you agree with our proposed approach to guidance about making reasonable inquiries?

B2Q2 In your view, are the obligations about making reasonable inquiries consistent with current good business practice?

B2Q3 Is there any further guidance we should give? Please provide as much specific information as possible, as this will assist us to provide guidance that is of greater use to you.

Processes to ensure that reasonable inquiries are made

25 We expect credit licensees to have processes in place to ensure that they make reasonable inquiries about the consumer. If a licensee does not have appropriate processes in place, it will be difficult for them to demonstrate that they are meeting their responsible lending obligations.

26 Many credit providers already have product-specific processes in place to assess new consumers for different credit products. For example, we understand that it is already good industry practice to make more detailed inquiries in relation to offering a home loan compared with the inquiries made for a small personal loan.

Processes that are appropriate to the licensee's business model and the type of credit activity they are undertaking

27 In addition, we expect that the supervision and compliance processes a credit licensee puts in place will depend on their business model and the credit activities that they undertake. For example, if a licensee has employees who are located in a number of different locations, the licensee will need to have specific measures in place to ensure that employees are adequately supervised. This could include measures such as ensuring that compliance staff are located in offices at various geographical locations, rather than only having compliance staff at head office.

> Note: The guidance we are proposing to provide in relation to meeting the general conduct obligations of credit licensees is also relevant to the measures credit licensees will need to take to ensure their processes are adequate: see Consultation Paper 110 *General conduct obligations of credit licensees* (CP 110).

28 We expect that if a credit licensee's business includes refinancing activities, the licensee will need to have specific processes in place to ensure that their employees are adequately supervised and trained to undertake these activities. For example, we expect that when considering whether to offer credit as part of a refinancing transaction, the provider would make careful inquiries about the consumer's existing credit arrangements before forming a view about whether the new credit is unsuitable. See a further discussion of switching and refinancing issues at paragraph 66.

Proposal

B3 We propose to issue guidance (along the lines of paragraphs 25–28) that we expect credit licensees to have processes in place to ensure they make inquiries that are reasonable in the circumstances of each transaction.

Your feedback

B3Q1 Do you agree with our proposed approach to guidance about the processes we expect credit licensees to have in place to ensure they make reasonable inquiries?

B3Q2 To what degree do you anticipate that you will need to implement new processes (or change your current processes) to comply with the responsible lending obligation to make reasonable inquiries?

B3Q3 Is there any further guidance we should give? Please provide as much specific information as possible, as this will assist us to provide guidance that is of greater use to you.

Verification of information provided by the consumer

29 A licensee is obliged to take reasonable steps to verify the consumer's financial situation. Generally, this will require some positive steps to verify the information provided by the consumer: see Table 4. Depending on the circumstances, reasonable steps may involve:

(a) accessing the consumer's credit report;

(b) asking for a copy of payslips, tax returns, bank statements or Centrelink statements;

(c) with the consumer's permission, making inquiries with their employer or accountant;

(d) making other or further inquiries (e.g. making inquiries of other lenders), particularly where the information or documents provided do not accord with other information provided; and

(e) requesting to sight the original documents, not only the photocopies.

Note: We understand it is standard lending practice to verify the nature of the business activities and financial situation of self-employed applicants by contacting the consumer's accountant and documenting the results of the inquiry. It would not generally be sufficient to merely check the registration of an ABN, because whether or not an ABN is registered gives no information about the nature of the business or its income, assets or liabilities.

30 For example, we think that it would not constitute reasonable verification of information if a credit licensee were to offer a 'no-doc' home loan (i.e. without considering any documentary evidence of income etc.) to a consumer with a regular income, such as a PAYG employee or someone dependent on government benefits for their income. We would expect that in this situation, the credit licensee would need to undertake the kinds of inquiries set out in paragraph 29.

31 We recognise that in certain circumstances, a credit licensee would be able to verify a consumer's financial situation without receiving information from the consumer. For example, a bank could look at the consumer's regular deposited salary and the timing of credit card payments, and payment of other expenses. However, we would expect the licensee to take care relying on such information, which may not reflect the consumer's entire financial position due to, for example, credit cards with other financial institutions.

Table 4: Examples of types of evidence to verify a consumer's financial situation

	Types of evidence
For PAYG employees	Payroll receipts/payslips Confirmation of employment with the employer (with the consumer's consent)
For self-employed consumers	Income tax returns A statement from the person's accountant Business Activity Statements
For all consumers	Credit report Information/reports from other lenders Bank account or credit card records (e.g. expenses can be verified by examining bank statements over a period of time).

Note: This is not intended to be an exhaustive list of types of evidence that could be used to verify information provided by a consumer.

32 We believe that in certain situations, the credit licensee may be expected to conduct more than one round of inquiries. This may arise when information produced by the consumer may be anomalous and inconsistent with other information. For example, the licensee may believe that an application involving a full-time student with a $6000 per month income should warrant further verification. This may be due to inadvertence rather than fraud on behalf of the consumer.

33 Credit licensees may also need to verify that the information they are relying on is up-to-date. This is particularly so when relying on information in a preliminary assessment: see paragraphs 34–35.

Example 3: Inadequate verification

Reliance on old payslips may not be enough to satisfy the obligation to verify information, particularly where the proposed loan is at the limits of affordability for the consumer based on the information provided as to income. Contact with the consumer's employer could reveal that the consumer is a casual employee, on probation, or no longer employed with that employer.

Proposal

B4 We propose to issue guidance (along the lines of paragraphs 29–33 and Example 3) that the obligation to take reasonable steps to verify the consumer's financial situation will require the licensee to take some positive steps to verify the information provided by the consumer.

Your feedback

B4Q1 Do you agree with the guidance we are proposing to give in relation to verification of information?

B4Q2 How consistent are the obligations about verification of information with current good business practice?

B4Q3 What changes will you need to make in your business to ensure that you meet the obligation to verify information?

B4Q4 Is there any other guidance you think it would be useful for us to give?

Taking into account information in the preliminary assessment

34 For customer convenience, in some circumstances the National Credit Bill allows credit providers to take into account information provided in a preliminary assessment by another credit licensee without further verifying the information: cls 130(3) and 153(3).

35 Credit licensees are, however, still bound by the reasonable inquiries obligation, as well as the general obligations such as to act efficiently, honestly and fairly. We expect that reasonable and prudent credit licensees will have processes in place to ensure the reliability of any information collected by third parties. This could include a combination of approaches such as:

(a) conducting ‘spot checks’ on some of the information by re-verifying it themselves;

(b) ensuring they only rely on preliminary assessments from intermediaries that have robust compliance arrangements; and

(c) ensuring that any incentives offered to intermediaries encourage, rather than discourage, appropriate information collection practices.

Proposal

B5 We propose to issue guidance (along the lines of paragraphs 34–35) about credit licensees relying on information provided in an intermediary's preliminary assessment.

Your feedback

B5Q1 Do you agree with the guidance we are proposing to give in relation to relying on information provided in an intermediary's preliminary assessment?

B5Q2 Is there any other guidance you think it would be useful for us to give?

C Assessment of unsuitability

Key points

A credit licensee must positively form a view that a loan is not unsuitable before they enter into a credit contract with a consumer, suggest a credit contract to a consumer or assist a consumer to apply for a credit contract. This view must be recorded in writing (which may be electronic).

We expect that credit licensees will base this assessment on the reasonable inquiries they have made about the consumer: see Section B.

There are two main issues for credit licensees to consider in determining that a credit contract is not unsuitable:

- capacity to repay; and
- fitness for purpose.

Forming a view that the credit contract is not unsuitable

36 As discussed in Section B, the responsible lending obligations, require credit licensees to:

(a) make reasonable inquiries about the consumer's requirements and objectives in relation to the credit (i.e. to determine whether the credit contract is fit for purpose);

(b) make reasonable inquiries about the consumer's financial situation (i.e. to determine whether they can repay the loan);

(c) take steps to verify the consumer's financial situation; and

(d) make an assessment that the credit contact is not unsuitable for the consumer.

Note: See cls 115, 116, 117, 128, 129, 130, 140 and 153.

37 In addition, credit licensees must assess a credit contract as unsuitable where:

(a) the consumer will be unable to comply with the their financial obligations under the contract, or could only comply with substantial hardship; or

(b) the contract will not meet the consumer's requirements or objectives.

Note: See cls 118, 119, 131, 141, 142 and 154.

38 The responsible lending obligations also provide that, credit licensees must not:

(a) provide credit assistance to a consumer by suggesting that the consumer remain in, enter into or increase the limit on, an unsuitable credit contract (see cls 123, 124);

(b) provide credit assistance to a consumer by suggesting that a consumer apply for, or remain in, an unsuitable consumer lease (see cls 146, 147);

(c) enter into a credit contract or increase the limit on a credit contract that will be unsuitable for the consumer (see cl 133); or

(d) enter into a consumer lease that will be unsuitable for the consumer (see cl 156).

39 Further, if requested, a credit licensee must provide to the consumer a copy of the assessment that the credit is not unsuitable for the consumer: see cls 120, 132, 143 and 155. In practice, this means that the licensee must record the assessment in a form that allows them to provide a copy promptly to the consumer.

40 Together, these provisions of the National Credit Bill mean that a credit licensee must take active steps in order to form a view that a loan is not unsuitable before they enter into a credit contract with a consumer, suggest a credit contract to a consumer or assist a consumer to apply for a credit contract. The credit licensee's view must be recorded in writing (which may be in electronic form, such as email): see Section D.

Note: If a preliminary assessment has been made, and certain conditions are met, then the credit licensee is not required to take reasonable steps to verify information contained in the preliminary assessment: see cls 130(3) and 153(3).

41 We expect that credit licensees will base their assessment on the reasonable inquiries they have made about the consumer (plus any other relevant information they have).

Proposal

C1 We propose to issue guidance that a credit licensee must form a view that a credit contract is 'not unsuitable' before they enter into a credit contract with a consumer, suggest a credit contract to a consumer or assist a consumer to apply for a credit contract, and this view must be based on the reasonable inquiries they have made about the consumer (and any other relevant information they have about the consumer).

Your feedback

C1Q1 Do you agree with our proposed approach to guidance?

C1Q2 What changes will you need to make in your business to ensure that you meet the obligation to form a view that a credit contract is not unsuitable for the consumer?

C1Q3 Is there any further guidance we should give? Please provide as much specific information as possible, as this will assist us to provide guidance that is of greater use to you.

Determining the consumer's financial situation, capacity to repay and substantial hardship

42 Determining the consumer's financial situation (i.e. the capacity to repay test) is part of a licensee's overall obligation to avoid placing a consumer in a credit contract that is unsuitable for them.

43 Having completed reasonable inquiries (as per Section B), a licensee must assess whether the credit contract is unsuitable, which includes whether the consumer has the capacity to make repayments (as well as whether the credit contract is fit for the consumer's purpose: see paragraphs 59–62).

44 Under the capacity to repay test, a credit contract (or an increase to a credit limit) is unsuitable if, at the time of the assessment, it will be likely that the consumer will:

(a) be unable to comply with their financial obligations under the contract (e.g. to make repayments); or

(b) only be able to comply with the contract with substantial hardship.

Note: See cls 118(2)(a), 119(2)(a), 131(2)(a), 141(2)(a), 142(2)(a) and 154(2)(a).

45 The assessment of unsuitability on the grounds that the consumer will be unable to comply with the financial obligations under the credit contract takes into account information reasonably believed, or which ought reasonably to be believed, by the licensee, and also any additional information the licensee would have reasonably believed had they made reasonable inquiries or verification: see cls 118(4), 119(4), 131(4), 141(4), 142(4) and 154(4).

What the credit licensee should take into account in determining capacity to repay

46 We expect that licensees will base the assessment of capacity to repay on the reasonable inquiries they have made about the consumer's financial situation.

47 In addition, the Explanatory Memorandum states that the purpose for undertaking reasonable inquiries about the consumer's financial situation is to ascertain a reasonable understanding of the consumer's ability to meet all the repayments, fees, charges and transaction costs of complying with the proposed credit contract: see paragraph 3.69. We would expect the licensee to take into account these types of issues when assessing whether the consumer will be able to repay the credit contract.

Example 4: Capacity to repay and taking into account all costs

A consumer goes to the website of a credit assistance provider to make an application to refinance a loan. When the credit assistance provider assesses the consumer's application, they will need to take into account all of the costs of changing credit contracts when assessing the consumer's ability to meet the obligations of the new credit contract over its entire term. This would include any fees for using the credit assistance provider's services.

Processes to ensure that capacity to repay is assessed

48 We expect credit licensees to have processes in place to assess whether a consumer has the capacity to repay the credit contract without substantial hardship. If a licensee does not have appropriate processes in place, it will be difficult for them to demonstrate that they are meeting their responsible lending obligations.

Meeting repayment obligations from income, not assets

49 Generally, consumers should be able to meet a credit contract's obligations from income rather than equity in an asset. However, there may be circumstances where this may not be a reasonable position (e.g. bridging loans and reverse mortgages).

Note: We expect lenders to take particular care when assessing capacity to repay for products like reverse mortgages and bridging loans. We expect lenders to follow industry best practice here, such as the SEQUAL Code of Conduct.

50 Under the National Credit Bill, it is presumed that if a consumer will only be able to comply with their financial obligations under the credit contract by selling their principal place of residence, then the consumer could only comply with those obligations with substantial hardship, unless the contrary is established: see cls 118(3), 131(3), 142(3) and 156(3). The effect of this is that where a consumer establishes that they could only meet the repayments by selling their home, then the onus is on the credit assistance provider to establish that the credit contract was not unsuitable.

Proposal

C2 We propose to issue guidance about determining the consumer's financial situation and capacity to repay, including that:

(a) licensees should take into account all costs associated with the credit contract when determining capacity to repay;

(b) licensees should have appropriate processes in place for assessing whether a consumer will be able repay a credit contract without substantial hardship; and

(c) generally, consumers should be able to meet the credit contract's obligations from income rather than equity in an asset.

Your feedback

C2Q1 Do you agree with our proposed approach to guidance about determining the consumer's financial situation and capacity to repay?

C2Q2 Are the obligations about the capacity to repay consistent with current good business practice?

C2Q3 What changes will you need to make in your business to ensure that you meet the obligation to assess whether a consumer has the capacity to repay a credit contract?

C2Q4 Is there any further guidance we should give? Please provide as much specific information as possible, as this will assist us to provide guidance that is of greater use to you.

Substantial hardship

51 ‘Substantial hardship’ is not defined in the National Credit Bill. We do not propose to give any definitive formulation of what substantial hardship means. The law about the meaning of ‘substantial hardship’ will develop and become clearer as cases come before the courts and judgments are handed down.

Note 1: Case law and other legislation provide some guidance on the interpretation of ‘hardship’ in different contexts. For example, in the superannuation context, one of the tests for whether a person is in ‘severe financial hardship’ is that ‘the person is unable to meet reasonable and immediate family living expenses’: reg 6.01(5)(a)(ii), Superannuation Industry (Supervision) Regulations 1994.

Note 2: Although we are not aware of any judicial consideration of the meaning of substantial hardship in relation to the UCCC, courts have considered the meaning of ‘substantial hardship’ in various contexts, including the following:

– The expressions ‘undue hardship’ or ‘substantial hardship’ must be taken to be used in their ordinary grammatical meaning. Neither expression lends itself to precise quantification: *Re Wilson and Minister for Territories* (1985) 7 ALD 225 at 228; *McMahon v The Treasurer* [1995] ACT AAT 120 at [19].

– ‘Substantial hardship’ is hardship of considerable degree: *Re Wilson and Minister for Territories* (1985) 7 ALD 225 at 228. What degree of hardship is required all depends on the circumstances of the case: *McMahon v The Treasurer* [1995] ACT AAT 120 at [20]; *Noble v Vorreiter* (by L J Hooker Unley) [2003] SARTT 15.

- ‘Hardship’ by itself is something severe which is hard to endure: *Liberian Shipping Corporation v A King & Sons Ltd* (‘The Pegasus’) [1967] 2 QB 86 at 98.
- An inability to meet ‘some of the necessities of life’ would amount to ‘undue hardship’ in some cases. But in others the availability of significant discretionary expenditure should be taken into account in assessing whether undue hardship would exist: *McMahon v The Treasurer* [1995] ACT AAT 120 at [21].

52 We think that determining whether repaying a credit contract will cause substantial hardship to a consumer will relate to a number of factors.

53 In administering the law, we will take the following factors into account when considering whether a transaction is likely to result in substantial hardship:

(a) the money the consumer is likely to have left after their living expenses have been deducted from their after-tax income;

(b) how consistent and reliable the consumer’s income is (and the size of the loan relative to their income level);

(c) whether the consumer’s expenses are likely to be significantly higher than average (e.g. because they live in a remote area);

(d) the consumer’s other debt repayment obligations and similar commitments (e.g. child support);

(e) how much of a buffer there is between the consumer’s disposable income and the repayments (e.g. how vulnerable they are to an increase in interest rates; the impact once any ‘honeymoon rates’ end etc.); and

(f) whether the consumer is likely to have to sell their assets, such as a car or primary residence (see paragraph 50), to repay the loan.

Note: This is not intended to be an exhaustive list of potentially relevant factors. In determining whether a situation involves substantial hardship, the presence (or absence) of any one or more of the listed factors is not conclusive.

54 In addition, credit licensees may wish to take into account any other conversations that they have had with the consumer about how the loan will impact on the consumer’s living standards. For example, a consumer may be willing to make reasonable changes to their lifestyle to enable them to afford the loan without substantial hardship (such as cutting back on non-essential expenses).

Processes for determining substantial hardship

55 We expect licensees to develop appropriate systems and processes to identify whether a proposed credit contract is likely to cause substantial hardship to a consumer. Different licensees are likely to take different approaches, depending on the nature of their business and their range of customers.

56 Some possible benchmarks that licensees may wish to consider include that a consumer would be assumed to be exposed to substantial hardship if their disposable income is:

(a) below a level where they do not have funds to meet their basic needs and those of their dependants;

(b) below a particular objective poverty indicator, such as the Henderson Poverty Line; or

(c) below the maximum applicable level of government benefits for a person in the financial and family situation of the consumer.

57 Most lenders already have detailed processes to assess whether the consumer will be able to repay a loan. These include processes for calculating what funds a person needs to pay for basic living expenses in order to determine how much they can borrow (i.e. at what level a consumer can make repayments).

Proposal

C3 We propose to issue guidance (along the lines of paragraphs 51–57) about factors ASIC will take into account when considering whether a particular situation involves substantial hardship.

Your feedback

C3Q1 Do you agree with our proposed approach to guidance about substantial hardship?

C3Q2 Is our proposed guidance in relation to substantial hardship consistent with current good business practice?

C3Q3 What changes will you need to make in your business to ensure that you are able to determine whether a credit contract will cause a consumer to experience substantial hardship?

C3Q4 Is there any further guidance we should give? Please provide as much specific information as possible, as this will assist us to provide guidance that is of greater use to you.

Examples in relation to capacity to repay and substantial hardship

58 Some examples to illustrate our guidance on capacity to repay and substantial hardship are set out below.

Example 5: Regular family expenses

In assessing whether a credit contract will cause a consumer to experience substantial hardship, a licensee might set a reasonable standard level of funds representing a minimum level of family living expenses required to meet the consumer's (and their dependants') basic needs, which would need to be left over out of a consumer's income, having deducted the ongoing repayments under the credit contract (and all other repayments and regular other financial commitments of the consumer). Below this level, the licensee would, as a policy, not consider the consumer to have the capacity to repay the loan without substantial hardship, regardless of their circumstances.

Example 6: Temporary period without income

A consumer wishes to enhance their chances of a promotion in the future by undertaking tertiary study on a vocational course with direct relevance to their chosen job. The consumer seeks credit to pay for the course. Their employer has given assurances that the consumer will be able to take their job back at the end of the course, if they do not obtain a higher paid one within the firm on the basis of the new qualification.

However, for the duration of the course the consumer will only be able to meet their repayments under the proposed credit contract by making serious cutbacks on their expenditure. The consumer has indicated they are willing to incur this short-term hardship for the purpose of improving their long-term prospects, and they have a realistic plan for economising so that they can still meet their minimum loan repayments.

In this case, the licensee may conclude that the consumer would have the capacity to repay without substantial hardship, even if most other individuals (with a different purpose for the loan funds) would not.

Example 7: Refinancing

Where a consumer cannot currently comply with their existing financial obligations under a credit contract (or only with substantial hardship), a licensee can refinance the consumer's debts if, after refinancing, they will be able to comply with the resulting credit contract without substantial hardship. In such circumstances, the level at which substantial hardship is assessed may well be different from a situation where the consumer was not previously having serious repayment difficulties.

Example 8: Reverse mortgages

An elderly couple may seek to improve their lifestyle (without selling their property and renting) by entering into a reverse mortgage. This will allow them to receive a payment as a lump sum or as an income stream over a specified period of time. A licensee should ensure that the method of payment (i.e. lump sum or income stream) is fit for the consumers' purpose and the terms of the contract should be suitable for the consumers (e.g. the length of the income stream should exceed the life expectancy of the consumers if the consumers do not wish to vacate their home before they die).

Because of the nature of a reverse mortgage (being an unusual type of home loan), we would expect the licensee to take extra care to ensure the consumer fully understands the key features of the reverse mortgage product. Generally, we would expect the licensee to ensure that the consumer is unlikely to end up in a negative equity situation (i.e. where the amount owing exceeds the loan value), as otherwise the consumer is unlikely to have the capacity to repay the loan.

Example 9: Casual employees

A consumer receives their first fortnightly pay cheque as a casual employee, and applies for a credit card. The consumer is told by the bank officer to multiply their salary by 26 to calculate their annual income. This is not an appropriate method to determine income because the consumer's employment is on a casual basis and their salary fluctuates considerably from fortnight to fortnight. The resulting calculation based on the bank officer's instructions will not accurately reflect the consumer's annual income and capacity to repay the loan.

Fitness for purpose: Determining the consumer's requirements and objectives in relation to the credit contract

59 The fitness for purpose test is part of a licensee's overall obligation to avoid placing a consumer in a credit contract that is unsuitable for them. Having completed reasonable inquiries (as per Section B), a licensee must assess whether the credit contract is unsuitable, which includes whether it is fit for the consumer's purpose (as well as whether the consumer has the capacity to make repayments, as discussed earlier in this section).

60 A credit contract is unsuitable if it 'will not meet the consumer's requirements and objectives' (the 'fitness for purpose' test): see cls 118(2)(b), s119(2)(b), 131(2)(b), 141(2)(b), 142(2)(b) and 154(2)(b). This is an objective test looking at the extent to which the credit contract is likely to meet the consumer's requirements and objectives.

61 If none of the credit contracts that a licensee provides (or provides services about) is fit for purpose (i.e. they are all unsuitable) for a given consumer, then the licensee must not enter into a credit contract with a consumer, suggest a credit contract to a consumer or assist a consumer to apply for a credit contract.

62 The assessment of unsuitability on the grounds that the credit contract will not meet the consumer's requirements and objectives ('unfitness for purpose') takes into account information reasonably believed, or which ought reasonably to be believed, by the licensee, and also any additional information the licensee would have reasonably believed had they made reasonable inquiries or verification: see cls 118(4), 119(4),131(4),141(4), 142(4) and 154(4). If the licensee is unsure of the consumer's objectives and needs, this should be resolved through the reasonable inquiries process.

Meeting the consumer's requirements and objectives

63 The Explanatory Memorandum to the National Credit Bill states that the minimum required of licensees in order to meet the obligation to make reasonable inquiries about the consumer's requirements and objectives will be to understand the purpose for which the credit is sought and determine if the type, length, rate, terms, special conditions, charges and other aspects of the proposed credit contract meet this purpose or put forward credit contracts that do match the consumer's purpose: see paragraph 3.68.

64 We think that whether a credit contract meets a consumer's requirements and objectives will vary depending on the circumstances, but some examples of factors that licensees could take into account include:

(a) the nature of the credit requested by the consumer, and the consumer's objectives in obtaining credit (based on inquiries made of the consumer);

(b) if the loan is to purchase a specific item, the term of the loan relative to the likely useful life of the asset;

(c) the express or implied purpose for which the consumer is seeking credit (e.g. to buy a home or car) and the degree of urgency;

(d) the amount of credit the consumer needs (e.g. to make a particular purchase);

(e) the interest rate and fees applying to the credit contract;

(f) the complexity of the credit contract, and whether a more basic product could meet the consumer's needs;

(g) the nature of the service being offered by the licensee;

(h) whether the consumer will need to finance a large final payment under the contract; and

(i) in relation to switching, the extent to which switching to the new credit contract will benefit the consumer.

Note: This is not intended to be an exhaustive list of potentially relevant factors. In determining whether a contract is fit for purpose, the presence (or absence) of any one or more of the listed factors is not conclusive.

65 Following are some examples to illustrate our proposed guidance on fitness for purpose.

Example 10: In-store finance or credit card

A consumer seeking to purchase a $1000 television at a department store may elect to do so using finance provided in-store. However, it would not be appropriate for the ultimate lender to automatically provide a credit card facility with a credit limit significantly exceeding the amount of credit the consumer needs to finance the purchase.

Example 11: Product range

A lender should not enter into a reverse mortgage with a healthy employed 60-year-old who wishes to obtain the finance to purchase a car, even if equity release products are the only credit contract that the lender provides. The limited range of products that the lender provides in practice does not absolve the lender of the responsibility to ensure that the credit product that is offered is fit for purpose.

Example 12: Key features for the customer

If a prospective borrower indicates that the ability to refinance their home loan is a key requirement, a credit contract that has high exit fees or other break costs would not be fit for the consumer's purpose.

Example 13: Short-term finance

A consumer contacts a mortgage broker by phone because she is having short-term difficulties in meeting bills, pending the maturing of a term deposit. The mortgage broker should not suggest a loan secured by the equity in the consumer's house. The costs involved in establishing this type of loan would not be warranted if the consumer's financial difficulty is clearly short term. A mortgage broker that was acting in an efficient, honest and fair manner would suggest that the consumer investigate the penalties associated with early access to the term deposit.

Example 14: Balloon payments

Some products involve a large 'balloon' payment at the end of the loan term. While a consumer may be able to manage the regular repayments under the loan, whether the product is suitable for them also depends on whether they will be able to make the final, much larger, payment. We would expect the licensee to satisfy itself that the consumer understands and has the capacity to cover the final repayment before offering this type of product to the consumer.

Proposal

C4 We propose to issue guidance about determining the requirements and objectives of the consumer in relation to the credit contract, including that:

(a) whether a credit contract meets a consumer's requirements and objectives will vary depending on the circumstances;

(b) we expect licensees to have appropriate processes in place for assessing whether a credit contract will meet the consumer’s requirements and objectives; and

(c) generally, a credit contract will be unsuitable unless it fits the purpose for which the consumer is seeking credit and any particular requirements expressed by the consumer.

Your feedback

C4Q1 Do you agree with our proposed approach to guidance about determining the consumer's requirements and objectives?

C4Q2 Is the obligation to determine a consumer's requirements and objectives consistent with current good business practice?

C4Q3 What changes will you need to make in your business to ensure that you meet this obligation?

C4Q4 Is there any further guidance we should give? Please provide as much specific information as possible, as this will assist us to provide guidance that is of greater use to you.

C5 We propose to issue guidance (along the lines of paragraphs 63–64) about factors ASIC will take into account when considering whether a particular credit transaction is fit for purpose.

Your feedback

C5Q1 Do you agree with our proposed approach to guidance about determining whether a particular credit transaction is fit for purpose?

C5Q2 Is our proposed guidance consistent with current good business practice?

C5Q3 Is there any further guidance we should give? Please provide as much specific information as possible, as this will assist us to provide guidance that is of greater use to you.

Switching and refinancing

66 We expect that licensees will undertake additional analysis when engaging in switching and refinancing activities. This would include consideration of whether entering the new credit contract or option:

(a) would result in overall cost savings to the consumer that are likely to override any loss of benefits; or

(b) where there may be a minimal net benefit in cost savings, but the new credit contract is a better fit for the consumer's stated purpose (e.g. because of greater flexibility or particular tailored features like a redraw facility on a mortgage).

67 The determination of whether there are overall cost savings to the consumer should take into account all the circumstances, including the cost of the replacement (i.e. making the switch) and all associated fees and other charges. There are usually transaction costs associated with refinancing, including any fees for using a credit assistance provider's services.

Proposal

C6 We propose to issue guidance that where the consumer is replacing one credit contract with another (or switching between repayment or interest options within a credit contract), the new credit contract or option will generally not meet the consumer's requirements and objectives if the licensee knew (or ought reasonably to have known) that the overall benefits likely to result from the new credit contract (or option) would be lower than under the old credit contract (or option).

Your feedback

C6Q1 Do you agree with the proposed guidance? Why or why not?

D Guidance about written assessment that credit contract is not unsuitable

Key points

Under the legislation, a licensee must, if requested, provide the consumer with a copy of the assessment that the credit contract is not unsuitable.

We propose to provide guidance about our expectations in relation to the form of this document.

Proposal

D1 We propose to issue some brief guidance about our expectations for the form and content of both the preliminary and final written assessment that a credit contract is not unsuitable. The information we expect would be provided in this document includes:

(a) a summary of what the consumer told the licensee in relation to their financial situation, requirements and objectives;

(b) a statement that the licensee has based the assessment on the information provided by the consumer; and

(c) a statement that the licensee has assessed a particular credit contract as not unsuitable for the consumer.

Your feedback

D1Q1 Do you agree that this is the type of information that should be included in a written assessment?

D1Q2 What changes will you need to make in your business to ensure that you are able to meet this obligation?

D1Q3 Do you think any additional information should be included in the written assessment?

Rationale

68 Under the National Credit Bill, a licensee must, if requested, provide to the consumer a copy of the assessment that the credit contract is not unsuitable for the consumer: see cls 120, 132, 143 and 155. In practice this means the licensee must keep a record of the assessment in a form that allows them to provide it promptly to a consumer.

69 We expect that this written assessment will be concise and easy for consumers to understand.

70 We consider that a degree of standardisation of content along the lines we propose will:

(a) assist consumers in understanding that the unsuitability or otherwise of the credit contract has been assessed, and the result of that assessment;

(b) ensure that the consumer has the opportunity to check the factual basis on which the licensee has made the assessment (as stated by the licensee in the written assessment), so that if it is inaccurate they can raise the matter with the licensee; and

(c) assist the licensee in demonstrating compliance with the responsible lending obligations.

71 We do not expect lenders to disclose the commercially sensitive lending criteria on which their credit decisions are based. Only the information that specifically relates to the statutory concepts of ‘fitness for purpose’, ‘capacity to repay’ and ‘reasonable inquiries’ should appear in the written assessment.

72 In addition, there is no obligation for lenders to disclose the reasons for rejecting a credit application. The licensee is not required to give the consumer a copy of the assessment if:

(a) the licensee is a credit provider (i.e. a lender) and the transaction does not go ahead; or

(b) the licensee is a credit assistance provider and it does not provide credit assistance to the consumer.

E Regulatory and financial impact

73 In developing the proposals in this paper, we have carefully considered their regulatory and financial impact. On the information currently available to us we think they will strike an appropriate balance between:

(a) ensuring that credit licensees comply with the responsible lending obligations in Ch 3 of the National Credit Bill; and

(b) not causing credit licensees to incur unreasonable costs in complying with the responsible lending obligations.

74 Before settling on a final policy, we will comply with the requirements of the Office of Best Practice Regulation (OBPR) by:

(a) considering all feasible options;

(b) if regulatory options are under consideration, undertaking a preliminary assessment of the impacts of the options on business and individuals or the economy;

(c) if our proposed option has more than low impact on business and individuals or the economy, consulting with OBPR to determine the appropriate level of regulatory analysis; and

(d) conducting the appropriate level of regulatory analysis—that is, by completing a Business Cost Calculator report (BCC report) and/or a Regulation Impact Statement (RIS).

75 All BCC reports and RISs are submitted to the OBPR for approval before we make any final decision. Without an approved BCC Report and/or RIS, ASIC is unable to give relief or make any other form of regulation, including issuing a regulatory guide that contains regulation.

76 To ensure that we are in a position to properly complete any required BCC report or RIS, we ask you to provide us with as much information as you can about:

(a) the likely compliance costs;

(b) the likely effect on competition; and

(c) other impacts, costs and benefits,

of our proposals or any alternative approaches: see ‘The consultation process’, p. 4.

Key terms

Term	Meaning in this document
ASIC	Australian Securities and Investments Commission
COAG	Council of Australian Governments
consumer	A prospective borrower
credit licence	An Australian credit licence under cl 35 of the National Credit Bill that authorises a licensee to engage in particular credit activities
credit licensee	A person who will be required to hold an Australian credit licence
lender	credit provider
National Credit Bill	National Consumer Credit Protection Bill 2009, tabled in Parliament on 25 June 2009
SEQUAL Code of Conduct	Senior Australian's Equity Release Association of Lenders Code of Conduct
UCCC	Uniform Consumer Credit Code

List of proposals and questions

Proposal		Your feedback	
B1	We propose to provide guidance (along the lines of paragraphs 20–21, Table 3 and Examples 1 and 2) that the obligation to make reasonable inquiries is scalable—that is, what a credit licensee needs to do to meet this obligation will vary depending on the circumstances.	B1Q1	Do you agree with our proposed approach to guidance about the reasonable inquiries obligation being scalable?
		B1Q2	Is there any further guidance we should give? Please provide as much specific information as possible, as this will assist us to provide guidance that is of greater use to credit licensees.
B2	We propose to provide guidance that we expect credit licensees to decide what inquiries they need to make in order to meet the reasonable inquiries obligation for a given transaction. However, when considering whether a credit licensee has conducted reasonable inquiries, we propose looking at whether the licensee has made inquiries about the kinds of issues listed in paragraphs 23–24.	B2Q1	Do you agree with our proposed approach to guidance about making reasonable inquiries?
		B2Q2	In your view, are the obligations about making reasonable inquiries consistent with current good business practice?
		B2Q3	Is there any further guidance we should give? Please provide as much specific information as possible, as this will assist us to provide guidance that is of greater use to you.
B3	We propose to issue guidance (along the lines of paragraphs 25–28) that we expect credit licensees to have processes in place to ensure they make inquiries that are reasonable in the circumstances of each transaction.	B3Q1	Do you agree with our proposed approach to guidance about the processes we expect credit licensees to have in place to ensure they make reasonable inquiries?
		B3Q2	To what degree do you anticipate that you will need to implement new processes (or change your current processes) to comply with the responsible lending obligation to make reasonable inquiries?
		B3Q3	Is there any further guidance we should give? Please provide as much specific information as possible, as this will assist us to provide guidance that is of greater use to you.

Proposal		Your feedback	
B4	We propose to issue guidance (along the lines of paragraphs 29–33 and Example 3) that the obligation to take reasonable steps to verify the consumer's financial situation will require the licensee to take some positive steps to verify the information provided by the consumer.	B4Q1	Do you agree with the guidance we are proposing to give in relation to verification of information?
		B4Q2	How consistent are the obligations about verification of information with current good business practice?
		B4Q3	What changes will you need to make in your business to ensure that you meet the obligation to verify information?
		B4Q4	Is there any other guidance you think it would be useful for us to give?
B5	We propose to issue guidance (along the lines of paragraphs 34–35) about credit licensees relying on information provided in an intermediary's preliminary assessment.	B5Q1	Do you agree with the guidance we are proposing to give in relation to relying on information provided in an intermediary's preliminary assessment?
		B5Q2	Is there any other guidance you think it would be useful for us to give?
C1	We propose to issue guidance that a credit licensee must form a view that a credit contract is 'not unsuitable' before they enter into a credit contract with a consumer, suggest a credit contract to a consumer or assist a consumer to apply for a credit contract, and this view must be based on the reasonable inquiries they have made about the consumer (and any other relevant information they have about the consumer).	C1Q1	Do you agree with our proposed approach to guidance?
		C1Q2	What changes will you need to make in your business to ensure that you meet the obligation to form a view that a credit contract is not unsuitable for the consumer?
		C1Q3	Is there any further guidance we should give? Please provide as much specific information as possible, as this will assist us to provide guidance that is of greater use to you.
C2	We propose to issue guidance about determining the consumer's financial situation and capacity to repay, including that:	C2Q1	Do you agree with our proposed approach to guidance about determining the consumer's financial situation and capacity to repay?
	(a) licensees should take into account all costs associated with the credit contract when determining capacity to repay;	C2Q2	Are the obligations about the capacity to repay consistent with current good business practice?
	(b) licensees should have appropriate processes in place for assessing whether a consumer will be able repay a credit contract without substantial hardship; and	C2Q3	What changes will you need to make in your business to ensure that you meet the obligation to assess whether a consumer has the capacity to repay a credit contract?
	(c) generally, consumers should be able to meet the credit contract's obligations from income rather than equity in an asset.	C2Q4	Is there any further guidance we should give? Please provide as much specific information as possible, as this will assist us to provide guidance that is of greater use to you.

Proposal	Your feedback
C3 We propose to issue guidance (along the lines of paragraphs 51–57) about factors ASIC will take into account when considering whether a particular situation involves substantial hardship.	C3Q1 Do you agree with our proposed approach to guidance about substantial hardship? C3Q2 Is our proposed guidance in relation to substantial hardship consistent with current good business practice? C3Q3 What changes will you need to make in your business to ensure that you are able to determine whether a credit contract will cause a consumer to experience substantial hardship? C3Q4 Is there any further guidance we should give? Please provide as much specific information as possible, as this will assist us to provide guidance that is of greater use to you.
C4 We propose to issue guidance about determining the requirements and objectives of the consumer in relation to the credit contract, including that: (a) whether a credit contract meets a consumer's requirements and objectives will vary depending on the circumstances; (b) we expect licensees to have appropriate processes in place for assessing whether a credit contract will meet the consumer's requirements and objectives; and (c) generally, a credit contract will be unsuitable unless it fits the purpose for which the consumer is seeking credit and any particular requirements expressed by the consumer.	C4Q1 Do you agree with our proposed approach to guidance about determining the consumer's requirements and objectives? C4Q2 Is the obligation to determine a consumer's requirements and objectives consistent with current good business practice? C4Q3 What changes will you need to make in your business to ensure that you meet this obligation? C4Q4 Is there any further guidance we should give? Please provide as much specific information as possible, as this will assist us to provide guidance that is of greater use to you.
C5 We propose to issue guidance (along the lines of paragraphs 63–64) about factors ASIC will take into account when considering whether a particular credit transaction is fit for purpose.	C5Q1 Do you agree with our proposed approach to guidance about determining whether a particular credit transaction is fit for purpose? C5Q2 Is our proposed guidance consistent with current good business practice? C5Q3 Is there any further guidance we should give? Please provide as much specific information as possible, as this will assist us to provide guidance that is of greater use to you.

Proposal		Your feedback	
C6	We propose to issue guidance that where the consumer is replacing one credit contract with another (or switching between repayment or interest options within a credit contract), the new credit contract or option will generally not meet the consumer's requirements and objectives if the licensee knew (or ought reasonably to have known) that the overall benefits likely to result from the new credit contract (or option) would be lower than under the old credit contract (or option).	C6Q1	Do you agree with the proposed guidance? Why or why not?
D1	We propose to issue some brief guidance about our expectations for the form and content of both the preliminary and final written assessment that a credit contract is not unsuitable. The information we expect would be provided in this document includes: (a) a summary of what the consumer told the licensee in relation to their financial situation, requirements and objectives; (b) a statement that the licensee has based the assessment on the information provided by the consumer; and (c) a statement that the licensee has assessed a particular credit contract as not unsuitable for the consumer.	D1Q1 D1Q2 D1Q3	Do you agree that this is the type of information that should be included in a written assessment? What changes will you need to make in your business to ensure that you are able to meet this obligation? Do you think any additional information should be included in the written assessment?