REPORT 152

# Helping home borrowers in financial hardship

May 2009

## About this report

This report examines the processes and procedures lenders and brokers have in place to deal with borrowers experiencing difficulties in meeting the repayments on their mortgage.

In some cases, borrowers may benefit from temporary relief or assistance with their loan on the grounds of financial hardship. We looked at how financial hardship assistance is promoted, identified and determined by different lenders and brokers. Our findings show that practices are inconsistent and vary greatly among industry players.

This report sets out examples of good and poor practices. It aims to provide guidance to industry on how to improve practices when dealing with borrowers in these circumstances.

**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.

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- 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.

## Acknowledgement

We acknowledge those lenders and brokers who gave their time to complete our questionnaire and respond to our inquiries.

# Contents

# Executive summary

## About the project

The Australian Securities and Investments Commission (ASIC) undertook a project in conjunction with Consumer Affairs Victoria (CAV) to look at the practices and procedures of lenders and mortgage brokers when they are approached by borrowers who are experiencing difficulties making their mortgage repayments.

In mid-2008, we asked a representative sample of home lenders[1] and mortgage brokers[2] to complete a written questionnaire. This included gathering:

- information about their financial hardship processes and procedures, such as:
  - how financial hardship is identified, and
  - options available to borrowers for assistance, and
- quantitative data about hardship relief applications (lenders only).

We also consulted several financial counselling agencies that regularly deal with borrowers who are experiencing financial hardship and are seeking assistance or relief from their lender.

The project was limited to mortgages for the following reasons:

- A mortgage is likely to be a consumer's biggest debt and is secured over their most valuable asset, their home.
- In March 2008, ASIC released a report examining refinancing in response to mortgage stress.[3] The report focused on the fringe practice of equity stripping, but also looked at the broader issue of options for borrowers in financial difficulties. The report foreshadowed further work to be undertaken by ASIC, including working with industry to develop best practice.
- Industry commentators have reported an increasing number of consumers facing mortgage stress in recent years, a trend that is likely to continue in 2009.[4]

[1] This covered 15 lenders in total including 7 banks, 4 credit unions and friendly societies, and 4 non-banks.
[2] The mortgage broker questionnaire was compiled with the assistance of the MFAA and sent to 9 brokers and broker groups, all members of the MFAA.
[3] REP 119 *Protecting wealth in the family home—An examination of refinancing in response to mortgage stress*, March 2008, at www.asic.gov.au.
[4] Overall 900,000 households were experiencing some degree of mortgage stress in August 2008, a 5-fold increase from March 2007. This figure is largely attributed to a higher cost of living due to increased fuel prices and interest rates. In January 2009, the figure for mortgage stress fell 6% from December because of a fall in these costs but is predicted to rise

## The issue of financial hardship

Consumer laws give borrowers important rights for access to hardship relief, and industry codes of conduct include commitments about the ways in which signatory lenders should respond to borrowers experiencing financial hardship.

While access to relief or assistance on the grounds of financial hardship is an issue of ongoing relevance, current economic conditions suggest it is likely to become increasingly important.

Interest rate cuts in the second half of 2008 and early 2009 may offer relief to some borrowers.[5] However, further financial pressure is likely to continue for some homeowners due to the slowing of the economy.

Clearly some borrowers will face financial difficulties from which recovery, at least in the short term, will be difficult if not impossible. We recognise the challenges faced by industry in distinguishing between those cases where assistance will offer genuine relief and those where unpleasant decisions will need to be made.

For products where there is a long-term relationship between borrower and lender, however, a borrower's ability to meet repayment obligations is likely to change from time to time. This will not come as a surprise to a prudent lender. From that perspective, recognising and responding to such changes can be considered a standard rather than an exceptional part of a lender's role.

## Key findings and recommendations

In the course of the project, we identified good and poor practices around financial hardship. It was encouraging to see examples of practice going beyond minimum legislative requirements and code commitments.

However, many lenders and brokers fell short of minimum standards. This suggests some borrowers experiencing financial difficulties are not being provided with adequate assistance and information about the options available to them.

The key findings and recommendations from the project are summarised below.

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5% by July 2009 as a result of increasing unemployment rate. 'January 2009 Mortgage Stress-O-Meter', Fujitsu Consulting, 27 January 2009.

[5] www.rba.gov.au; interest rate cuts: 3 September 2008, 25 basis points; 8 October 2008, 100 basis points; 4 November 2008, 75 basis points; 3 December 2008, 100 basis points; 3 February 2009, 100 basis points.

### Table 1: Summary of key findings and recommendations on financial hardship

| Key finding | Background | Recommendation |
|---|---|---|
| **1. Information only provided at default**<br><br>Most lenders only provide borrowers with information about financial hardship when they have already begun to experience financial difficulties. | • 14 out of the 15 lenders surveyed stated that they provide borrowers with information about financial hardship when they have defaulted on their loan.<br>• Most borrowers receive very little information about financial hardship from lenders before defaulting. | Lenders should ensure that information about options and assistance in the event of financial hardship is accessible and available to *all* borrowers (not just those in default). |
| **2. Reliance on collection officers**<br><br>Lenders showed a heavy reliance on their collection officers to identify borrowers who are experiencing financial hardship. | • It was evident from all lenders' responses that their collection officers play a significant role in identifying borrowers experiencing financial hardship.<br>• This is of concern where lenders did not also demonstrate that they had adequate procedures for ensuring collection officers can and do effectively carry out this role. For example, one lender told us that their collection officers would only identify hardship if it was specifically raised by a borrower. | Lenders should implement and maintain procedures to ensure all staff responsible for identifying financial hardship effectively carry out that role. |
| **3. Additional assessment criteria used**<br><br>Some lenders have adopted policies that are inconsistent with the legal rights and remedies available to borrowers. | • Some lenders have policies that exclude hardship variations, based on criteria such as the age of the loan or the number of days past due.<br>• Introducing arbitrary criteria when assessing financial hardship applications may put borrowers at risk of losing their rights for assistance under legislation or industry standards. | Policies relating to financial hardship must at a minimum reflect and ensure consistency with legal rights and obligations available to borrowers. |
| **4. Bias towards short-term assistance**<br><br>Lenders prefer offering short-term assistance or relief rather than matching assistance to need. | • Based on the procedures we reviewed, lenders are likely to provide short-term payment moratoriums rather than other options that may require a more rigorous assessment process and more effort to implement.<br>• Responding to a financial hardship request by providing assistance quickly and easily, rather than providing assistance that actually meets the needs of the individual, may result in poor outcomes for both borrowers and lenders. | Lenders should adopt policies that are flexible, allowing tailored responses to particular needs and circumstances. |

| Key finding | Background | Recommendation |
| --- | --- | --- |
| **5. More information needed**<br><br>Information provided to borrowers throughout the financial hardship process often fails to help them understand their options and make informed choices. | • Many of the pro forma and template letters sent to borrowers during the hardship process could be improved with better and clearer information.<br>• Borrowers would benefit from being provided with information about their rights to request relief or assistance on the grounds of financial hardship and the options available to them to dispute a decision. | Lenders should provide borrowers with easy to understand written information about financial hardship, informing them of available options including their right to request a hardship variation. |
| **6. Early access to superannuation**<br><br>Most lenders' financial hardship processes include informing borrowers that they can access their superannuation early. | • 13 out of the 15 lenders surveyed told us that they would at some stage inform a borrower experiencing financial difficulties that they may be able to access their superannuation early.<br>• This is a concern where early access merely delays an inevitable foreclosure rather than resolving the problem.<br>• In some cases, borrowers obtaining early access to their superannuation still lose their home together with a portion of their superannuation. | Lenders should review their policies and procedures as they relate to informing borrowers about early access to superannuation. |
| **7. Mortgage brokers' role**<br><br>Mortgage brokers generally have a limited understanding of their role in responding to financial hardship, and practices within the industry vary considerably. | • Some mortgage brokers believe it is not their role to offer any assistance or advice to borrowers about the financial hardship options available to them. | Mortgage brokers should implement and maintain procedures to identify borrowers experiencing financial difficulties and inform them, where appropriate, about their right to request a hardship variation or, alternatively, refer them to their lender. |

# A The regulatory environment

**Key points**

In Australia, consumer credit is regulated under the Uniform Consumer Credit Code (UCCC), which is currently administered by the states and territories.

ASIC has a consumer protection role for credit, which will extend to regulation of all areas of credit when the UCCC is enacted into federal legislation.

Under the UCCC, borrowers can seek changes to their credit contract on the grounds of financial hardship.

Industry codes of practice also include standards for members relating to financial hardship.

## Legislation

The principle piece of legislation regulating consumer credit in Australia is the Uniform Consumer Credit Code (UCCC). The UCCC is administered by Australian states and territories, and in Victoria, CAV is the regulatory authority responsible for enforcing its compliance.

Since 11 March 2002, ASIC has had a consumer protection role for credit facilities under the *Australian Securities and Investments Commission Act 2001* (ASIC Act), which covers broad standards of conduct, including conduct that is unconscionable and misleading or deceptive.

On 2 October 2008, the Council of Australian Governments agreed that the Commonwealth would assume responsibility for all areas of credit. The initial phase of this process will see the UCCC enacted into federal legislation by mid-2009 and extended powers given to ASIC to regulate credit. For more information, see Section D.

## Financial hardship and the UCCC

Under the UCCC, borrowers can apply for changes to their credit contract on the grounds of hardship: see s66–68.[6] Section 66(1) provides that:

> A debtor who is unable reasonably, because of illness, unemployment or other reasonable cause, to meet the debtor's obligations under a credit

[6] For these provisions to apply, the maximum amount of credit that is or may be provided under the credit contract must be less than the amount prescribed by the regulations. This is a floating threshold, currently $320,320: see www.creditcode.gov.au. It is expected that this threshold will change to $500,000, *National Consumer Credit Protection Bill 2009.*

> contract and who reasonably expects to be able to discharge the debtor's obligations if the terms of the contract were changed in a manner set out in subsection (2) may apply to the credit provider for such a change.

The three options under s66(2) for changing the terms of the contract are:

- extending the period of the contract and reducing the amount of each payment due under the contract accordingly
- postponing during a specified period the dates on which payments are due under the contract, or
- extending the period of the contract and postponing during a specified period the dates on which payments are due under the contract.

If the credit provider does not change the contract in accordance with an application made by a borrower, the borrower may apply to a relevant court or tribunal to change the terms of the contract: s68.

## Industry standards

### The Code of Banking Practice

The Code of Banking Practice (Banking Code) is a voluntary code of conduct that sets out the banking industry's standards of good practice. Clause 25.2 of the Banking Code requires a bank to:

- help customers overcome their financial difficulties with a credit facility they have with the bank, and
- inform customers of the hardship variation provisions of the UCCC.

The Code Compliance Monitoring Committee (CCMC) ensures that banks that have adopted the Banking Code meet the standards of good practice set out in the Banking Code.

In March 2005 the CCMC conducted an inquiry into members compliance with cl 25.2 of the Banking Code. In addition, the CCMC's more recent inquiry into bank compliance with cl 29 (debt collection) extended to banks' responses to financial hardship. The reports from those inquiries provide useful guidance on best practice for all mortgage lenders.[7]

### The Mutuals Code of Practice

Abacus–Australian Mutuals (the Association of Building Societies and Credit Unions) has released a draft Code of Practice that will commence on

[7] The reports are available at www.codecompliance.org. Additional industry guidance is available from a variety of sources, including Banking and Finance Bulletins 46 and 53 of the Financial Ombudsman Service, available at www.fos.org.au.

1 July 2009. Clause 24 of the draft Code sets out a range of commitments in relation to financial hardship, including that members will:

- work constructively with and try to assist borrowers to overcome financial difficulties
- respond promptly to requests or applications for assistance, and
- consider longer-term as well as short-term financial issues when they are relevant.

The draft Code of Practice also provides for formal compliance monitoring processes.

The current Credit Union Code of Practice and Building Society Code of Practice do not refer to financial hardship.

## The MFAA Code of Practice

The Mortgage and Finance Association of Australia (MFAA) is a voluntary industry association for lenders and brokers. All brokers contacted for this project were members of the MFAA.

Table 2 sets out the obligations under the MFAA Code of Practice relating to financial hardship for lenders and brokers who are members. The MFAA Code of Practice does not provide for compliance monitoring.

**Table 2: Obligations under the MFAA Code of Practice**

| What lenders must do | What brokers must do |
|---|---|
| • Consider in good faith whether it is reasonably appropriate to vary the payment terms of a credit facility where a lender becomes aware of, or is advised by the borrower, that the borrower is or may be in financial difficulty.<br>• If it is appropriate, suggest that the borrower ask for a variation to the repayment terms.<br>• Consider in good faith and within reasonable time the borrower's request to vary the payment terms.<br>• In assessing the request, act reasonably and not require the borrower to apply for early release of superannuation or borrow from family, friends or other third parties.<br>• If the lender decides not to vary the payment terms, promptly inform the borrower in writing of the reasons for the decision and the borrower's right to complain to an ASIC-approved external dispute resolution scheme (EDR scheme). | • Consider in good faith whether it is reasonably appropriate to vary the payment terms of a credit facility where the broker becomes aware of, or is advised by the borrower, that the borrower is or may be in financial difficulty.<br>• If it is appropriate, suggest that the borrower asks the lender to vary the repayment terms.<br>• If the borrower informs the broker that they are unable to meet repayments, refer the borrower to the lender. |

# B What lenders are doing

**Key points**

In general, only when a borrower has defaulted on their loan do lenders take steps to inform them about their rights and options to apply for relief or assistance on the grounds of financial hardship.

Lenders rely heavily on collection officers to identify borrowers who are experiencing financial hardship, yet, in many cases, have minimal procedures in place for them to carry out this role.

Lenders do offer various types of assistance to borrowers (with some bias towards short-term over long-term assistance), but tend to take into account considerations beyond those set out in the UCCC.

Information provided to borrowers throughout the financial hardship process could be improved so it is more informative and useful for consumer decision-making.

Lenders take anywhere between a few days and 2 months to assess financial hardship applications, with some lenders reducing this time by taking applications over the phone.

## Defining financial hardship

As noted in Section A, the UCCC defines financial hardship as a reasonable inability to meet contractual obligations due to illness, unemployment or ‘other reasonable cause’, a concept that should be read widely.[8]

We reviewed lenders’ policies and procedures to see how they defined financial hardship. Most lenders have adopted their own definitions of financial hardship. For example:

> Hardship is defined as a customer who shows a willingness to pay their loan commitment but is unable to do so, for a short period, due to diminished or no cash flow/income as a result of unemployment, a natural disaster, illness or any other event that the authorised staff member considers hardship.

In contrast, one lender provides a much shorter definition:

> Financial hardship is when a customer wants to pay what they owe but is unable to do so.

[8] *Permanent Custodians Ltd v Carolyn Joy Upston* [2007] NSWSC 223 (16 March 2007). In that case, the court found that the borrower had suffered hardship as a result of a business failing. This was despite the fact that the borrower had voluntarily left her employment to investigate her business decline and despite the fact that she obtained employment shortly after the business was eventually sold.

The second example is significantly more flexible than the first, and arguably easier to apply in practice. Both refer to the borrower being willing but unable to pay, but the first example suggests that assistance might only be provided to borrowers who meet additional criteria, some of which are relatively vague and open to interpretation.

Some lenders do not appear to have a clearly stated definition of financial hardship. At least one lender appears to have more than one definition, including versions that are inconsistent and contradictory. For example, in contrast to its generally inclusive definitions, one version limits eligibility to borrowers 'unable to pay their commitments for a period exceeding three months'.

Defining eligibility for hardship assistance by reference to either a minimum or maximum time period was not uncommon, but does not appear to reflect the UCCC or other relevant standards.

It was also common to find lenders referring to financial hardship as being caused by a change in the borrower's financial circumstances, with examples including situations such as loss of employment, injury and divorce.

It is important in developing responses to hardship to recognise that even small changes, such as a small cut back in work hours or increasing interest rates may cause a borrower to experience financial hardship.

## Causes of financial hardship

The most common reasons lenders cited for a borrower requesting relief or assistance on the grounds of financial hardship were:

- unemployment
- reduction in income
- relationship breakdown
- illness.

Over-commitment was also cited as a common cause of financial hardship. It is important to distinguish between overcommitment as a result of subsequent additional indebtedness and overcommitment present at the time the borrower enters into the mortgage agreement.

The second raises a different set of issues, including about the decision to lend.[9] This report does not cover the appropriate responses to hardship arising as a result of over-commitment present at the time of the transaction.

[9] Under the UCCC, a court has the power to re-open a transaction if it considers that the contract, mortgage or guarantee was unjust. In determining whether a contract was unjust, the court has to consider a range of factors including whether the lender knew or should have known that the borrower could not afford repayments or not without substantial hardship: s70(2)(l).

## Information available to borrowers

### … before they experience financial difficulties

Ideally, lenders should provide borrowers with general information[10] about financial hardship before they experience financial difficulties. This might include information encouraging them to contact their lender as soon as they begin to or become aware of experiencing financial difficulties, and about their rights under the UCCC or other options to ask for relief or assistance on the grounds of financial hardship.

When we asked lenders if they provide borrowers with this type of general information, very few lenders responded that they did. On a positive note, however, some lenders were beginning to take steps in this direction. Examples were limited, but included detailed online information and brochures.

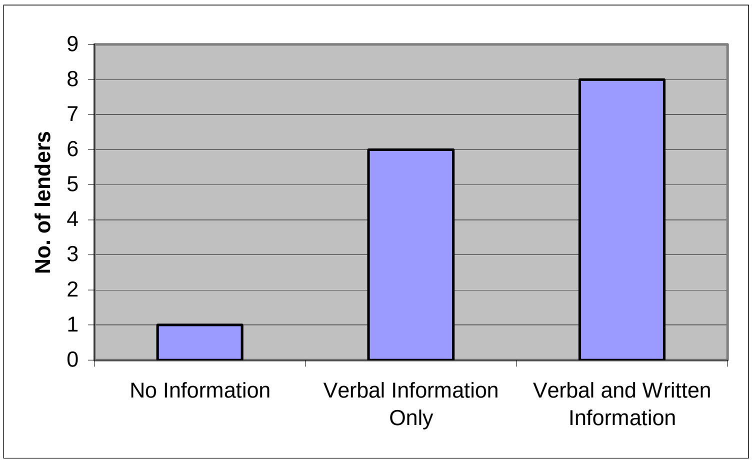
Also, some lenders inform borrowers about financial hardship assistance in correspondence notifying them of a change in interest rates.

### … when they have defaulted on their loan

With one exception, all lenders provide borrowers with information about relief or assistance on the grounds of financial hardship when they have defaulted on their loan. It was clear from the responses, however, that this does not mean this information is provided as a matter of course.

We asked those lenders how borrowers in default are informed about their options for relief or assistance on the grounds of financial hardship. All provide information verbally, with the majority also referring to these options in written correspondence, such as letters of arrears, default notices or collection letters: see Figure 2.

**Figure 1: How lenders provide financial hardship information to borrowers in default**




[10] We consider general information to be information that is widely accessible to customers *before* they are experiencing financial difficulties.

Of the 6 lenders relying solely on verbal communications, it was evident that information about relief or assistance is not routinely provided. For example, whether such information is provided may be 'dependent upon the context of the conversation'.

We also reviewed written correspondence setting out information about relief or assistance. In most cases the information was brief, often advising only of the availability of some form of accommodation rather than explaining what options might be available. For example:

> Please contact us if you are experiencing financial difficulties and cannot meet the current repayment structure. By contacting us, an alternative payment arrangement can be discussed.

In contrast, one lender also informs borrowers about their rights under the UCCC:

> We understand that financial circumstances can change due to illness, unemployment and other reasonable causes. We are willing to discuss any reasonable proposal for postponement of repayments, loan term extensions or reduced repayments. If your loan is regulated by the Consumer Credit Code, the hardship provisions of the Code, which provide for possible changes in regulated loan contracts on the grounds of hardship, could apply in your circumstances.

Some lenders said that some written correspondence refers to the following other sources of help:

- *Mortgage assistance schemes*: Some states and territories have schemes available to help borrowers who are having temporary difficulties in meeting their commitments after a change in their circumstances.
- *Seeking the assistance of a financial counsellor*: Financial counselling services help people who are in financial difficulty. They are available in every state and territory and provide a free, independent and confidential service.

Two lenders told us that they were reluctant to inform borrowers about hardship assistance in documentation such as default letters because they had trialled this and received too many calls that did not relate to genuine financial hardship cases. In response, one lender simply stopped providing this information. The other has continued to provide this information, deciding that even if a borrower was not eligible for hardship relief their enquiry could usually be dealt with elsewhere in their organisation.

## Accessing hardship teams

Anecdotal feedback from consumers and consumer advocates suggests that even where lenders have dedicated hardship teams, they are not always accessible, either directly or through internal processes.

Responding to this issue, the CCMC has stated its view that:

> banks should ensure there is an accessible and effective entry point for customers and their representatives, regardless of where that entry point is.[11]

We asked lenders if they have a dedicated toll-free telephone number for borrowers to call to deal with inquiries about or requests for relief or assistance on the grounds of financial hardship.

Seven lenders responded that they have a dedicated toll-free number in place to deal with financial hardship inquiries.

Of the 8 lenders who do not have in place a dedicated toll-free number, most told us that a borrower would have to call their general service area to inquire about financial hardship (for some lenders this number may be toll-free):

> Customers are offered a general enquiries 1300 number to access our call centre, where calls are screened and referred to Credit Management Officers who have initial responsibility for handling hardship applications.

## Dedicated toll-free numbers

For those lenders who have a dedicated toll-free number for financial hardship, the primary means for promoting the toll-free number are:

- on the lender's website
- in written correspondence, and
- verbally, usually by collections staff.

Where lenders told us they promote a toll-free number on their website, we reviewed their website. We found that in most cases toll-free numbers are not prominently promoted and in fact are often difficult to find. For example, in most cases, this number was found in pages on corporate social responsibility, rather than being included in information relating to customers, credit or home loans.

One lender includes its toll-free number in letters advising of an increase in interest rate. Most, however, wait until the borrower has defaulted, including the number in arrears or collections letters and/or in information accompanying a default notice. One lender limits reference to its toll-free number in written correspondence to letters that are 'provided once hardship is identified'.

While promoting access to hardship assistance is an important response to payment default, waiting for payment default to occur limits the opportunity for effective early intervention when problems arise. Limiting promotion of a dedicated number for borrowers experiencing financial hardship to those already identified as needing that assistance appears to offer little in terms of accessibility.

[11] CCMC, Inquiry into bank compliance with Clause 29 of the Code of Banking Practice, February 2008.

### General 'customer service' numbers

We asked lenders that have only their general customer service number for hardship inquiries how they promote the use of this number for inquiries on financial hardship.

The responses suggest there is little targeted promotion of general customer service numbers for the specific purpose of inquiring about or requesting relief or assistance on the grounds of financial hardship.

This suggests that the decision to have a dedicated number to deal with hardship issues is not just a decision about the means by which to provide access, but reflects a broader commitment to providing access.

When borrowers call a general customer service number with an inquiry or request that relates to financial hardship, they will generally be referred to a dedicated team. That referral may not, however, be direct or immediate. For example, in some cases:

- borrowers are transferred to another queue (where they are still likely to speak to someone on a very general level who will not be involved in any assessment or discussion about their actual inquiry), and
- borrowers are informed that a staff member will call them back.

## Identifying financial hardship

Lenders can actively seek to identify financial hardship before the borrower contacts them to inquire about or ask for help.

This is particularly important given that anecdotal evidence suggests borrowers are often unaware that assistance may be available, may be reluctant to seek assistance and/or be worried that telling their lender about financial difficulties may result in enforcement action.

We asked lenders if they have procedures in place for their staff to identify suitable cases for referral to relevant hardship processes.

### Early identification

A small number of lenders have taken steps to train staff to identify situations where a borrower may be experiencing financial hardship where this issue has not yet been raised. For example, one lender (through a pilot program) is assisting staff to identify 'triggers', such as a borrower advising that their home phone has been disconnected.

One lender also reported a more global approach to considering financial hardship, incorporating into their hardship processes a procedure to determine whether the borrower:

- has other credit products with their organisation, and
- needs help with their other credit products.

The more common response was that call centre staff have a role in fielding calls about hardship. There was, however, little reference to or evidence of staff training and guidelines to assist those staff in this aspect of their role.

Some lenders showed a heavy reliance on their collections staff to identify cases for hardship, with no reference to financial hardship being identified in any other way. These lenders tended to be the ones that did not make any attempt to inform borrowers about their hardship options in written correspondence, potentially compounding problems of access to available assistance.

### Identification of hardship after default

We asked lenders what processes they have in place for collection areas to identify suitable cases for referral to relevant hardship processes.

Some lenders have scripts or guidelines to assist collection staff to identify:

- what has caused the borrower's financial difficulties, and
- whether the borrower may be eligible for financial hardship assistance.

One lender stated that:

> It is our responsibility to identify the customer's need for financial assistance; we should not wait for them to ask for hardship.

Responses from other lenders suggested they have no formal processes in place to identify hardship. For example, one lender said that their collection officers would only make inquires about financial hardship if the borrower referred to financial hardship.

This approach to identifying financial hardship is consistent with observations made by the Banking and Financial Ombudsman,[12] which in a Bulletin issued in March 2007 noted that:

> In some cases it seemed that the bank member did not respond at all unless and until the words 'financial difficulty' or 'hardship' were used by the customer…[13]

More positively, some lenders had looked externally for assistance in developing processes and training staff to identify and respond to hardship, including working with and drawing on the experience of financial counselling

[12] Now the Banking and Financial Services division of the Financial Ombudsman Service.
[13] See FOS Banking and Finance Bulletin 53 March 2007, 'Customers in financial difficulties—Code of Banking Practice and UCCC Obligations'.

agencies. This more active engagement with these issues suggests a genuine commitment to enhancing access to relief or assistance for borrowers experiencing financial hardship.

## Consumer credit insurance

Many home lenders offer consumer credit insurance (CCI) to borrowers. CCI typically covers loan payments in the event of death, sickness, accident or unemployment, usually for a defined period. A borrower seeking to claim against a CCI policy will usually by definition be experiencing financial hardship resulting in payment default.

We asked lenders what processes they have in place to ascertain the progress of a borrower's CCI claim.

Some lenders told us that it is up to the borrower to notify them of the status of their claim:

> Ask borrower to contact insurance provider and request an update on status of claim.

Other lenders take a more active role and liaise directly with the insurer to establish the position of the claim:

> Initially, we contact [the insurer] to ensure that the claim is valid and that the original documents are all present. Then we continually contact the claims department in [the insurer] to assess the progress of the claim.

One lender goes a step further, establishing a direct connection with the progress of the claim:

> [We have] access to the insurer's system, and can determine the progress of a claim, or make telephone contact with the insurer.

We also asked lenders whether they defer repayments or enter into a hardship variation while a CCI claim is being assessed.

In most cases, an appropriate arrangement would be made, including:

- temporarily deferring repayments
- entering into hardship variation until the resolution of the claim, and
- suspending actions normally undertaken by staff to collect the debt.

In contrast, one lender's policy is that:

> Repayments are not deferred, however any late payment fees can be waived while the claim is pending. Dependent on the overdue position of loan, [the lender] may still issue legal notices, however no action will be taken against these until the outcome of the claim is known.

Even in the absence of an intention to take action, sending legal or default notices to a borrower who is making a CCI claim to cover default may be inappropriate and potentially misleading.

## Dealing with requests for assistance

After a borrower has asked for assistance or relief on the grounds of financial hardship, that request is likely to be:

- referred to a specialist area that deals with financial hardship applications, or
- handled within the collections team (this tended to be common for smaller lenders).

We asked lenders if they have procedures in place to ensure continuity of handling a borrower's financial hardship inquiry or request.

Twelve lenders said that each request for assistance is assigned to an individual staff member who will typically see it through from beginning to end:

> Once hardship has been identified, the dedicated hardship specialist handles the process from start to finish.

Some lenders also mentioned that where individual staff members are assigned to applications, they will usually provide the direct contact number of the officer responsible for the matter:

> Once an officer has first spoken with a customer, the customer is provided with that officer's direct telephone number. The majority of all related letters sent have the direct telephone number of the officer who handles the account.

Three lenders said that they do not have processes in place to ensure continuity. Their procedures included listing matters in a 'queue' where various staff members may undertake work on the request through the life of the matter.

### Requesting information

Most lenders will require a borrower to provide evidence of their financial hardship and expenditure. We asked lenders what information and documentation they generally require to assess a request for relief or assistance on the grounds of financial hardship.

The information commonly required to support a request for assistance includes:

- payslips or bank statements
- medical certificate
- Centrelink statements
- a statement of financial position, and/or
- a statement of income and expenditure.

Some lenders have taken steps to limit the amount of documentation they need to receive from borrowers in order to offer assistance. We found that some lenders have chosen to receive very limited or no documentation for hardship applications where:

- the application is for a short period of time (less than 3 months), and/or
- where the loan is not subject to lender's mortgage insurance.

Four lenders reported that they are beginning to accept financial hardship applications over the phone, and as part of that process require only a verbal statement of financial position and/or income and expenditure.

Those lenders reported positive experiences with phone assessment procedures, including that they:

- are quicker (one lender reported that the average time it takes them to process an application was cut from 2–3 weeks to 5 days), and
- provide more accurate information about the borrower's position.

## Assessing an application

We asked lenders what criteria they use to assess whether requests for relief or assistance on the grounds of financial hardship will be granted.

One lender applies a threshold test that excludes all requests other than those made in accordance with s66 of the UCCC.

In contrast, all other lenders told us that they would consider a request for assistance or relief on the grounds of financial hardship for regulated and unregulated loans:

> [We do] not treat regulated and unregulated loans differently for the purpose of hardship, and we rarely apply the Hardship Threshold.

At a general level, lenders assess an application for relief or assistance by reference to:

- the reason the borrower is seeking the assistance, and
- the borrower's ability to service the loan in the long run.

In practice, this means lenders seek to establish that there is a need to provide assistance and that the assistance provided will not merely delay an outcome that is in fact inevitable.

While the responses generally reflected flexibility in considering requests for assistance, some lenders introduced specific qualifying criteria that reflect a more rigid approach. For example, one lender will not provide hardship relief if the loan:

- was written less than 9 months before the request for relief, or
- is more than 60 days past due.

Other matters that might affect eligibility for hardship assistance include:

- the duration of the term of the loan
- the extent of equity in the property
- eligibility for early access of superannuation
- mortgage protection insurance cover, and
- lender's mortgage insurance.

For a discussion of early access of superannuation and the relevance of lender's mortgage insurance, see Section D.

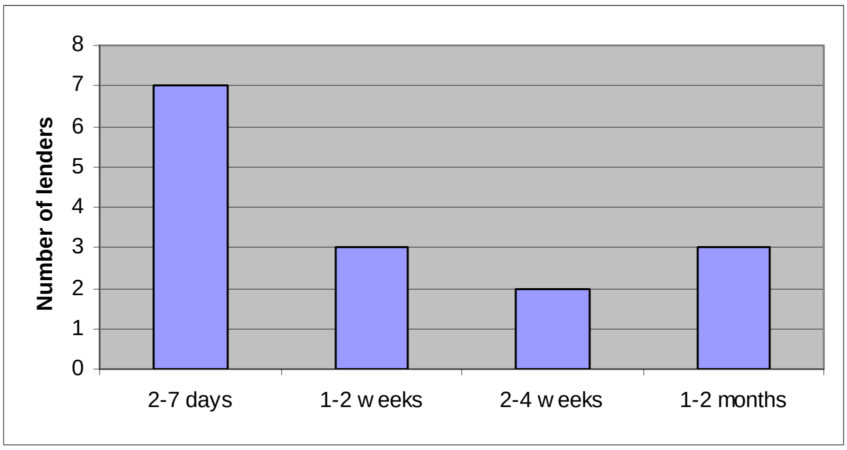
Consumer advocates have reported that some lenders will not help a borrower who has previously received assistance on the grounds of financial hardship. This is partially reflected in the policies of one lender, which state that a specific type of hardship relief can be provided only once within any 12-month period and no more than twice within any 5-year period.

Introducing additional qualifying (or disqualifying) criteria into the assessment of financial hardship applications risks arbitrarily or unreasonably limiting the availability of hardship assistance or relief to those who might benefit from it or be entitled to it. It is important to ensure that processes for assessing an application for relief or assistance are, at a minimum, consistent with the rights available to borrowers under the UCCC and relevant codes of conduct or other industry standards.

## Time taken to assess an application

We asked lenders the average length of time they take to finalise a request for relief or assistance on the grounds of financial hardship.[14] The average time taken to finalise a request for assistance varied greatly, ranging from 2 days to 2 months: see Figure 3.

**Figure 2: Time taken to assess financial hardship applications**




[14] By this we mean from the initial request for assistance to notifying the borrower.

It is difficult to account for such significant variation. Although dealing with applications by phone accounted for some of the quicker timeframes, lenders did report paper-based assessments being finalised within a week.

One lender which advised an average time of up to 2 months to finalise a request for assistance noted that the timeframe would be reduced significantly where borrowers provided all information required to make the assessment in a timely manner. While delays by borrowers in providing necessary information will of course delay the decision-making process, this average timeframe suggests the lender’s request for information may be exhaustive and possibly onerous.

An unreasonably prolonged assessment process can have significant negative consequences for borrowers. In circumstances where a borrower cannot make payments on their loan, arrears will be accruing while the financial hardship application is being assessed, potentially making it more difficult for the application to be accepted.

Some borrowers may also find a lengthy period of uncertainty upsetting, particularly as it is likely they will be trying to deal with other problems at the same time.

## Confirming an arrangement

We asked lenders how they document arrangements for providing relief or assistance on the grounds of financial hardship.

All but 2 lenders said the borrower would be informed in writing of the arrangement, whether by letter or, where relevant, through updated contractual documentation.

In some cases, borrowers may be required to sign an acknowledgment of the arrangement and return it to the lender.

Of those that said they would not in all cases confirm the arrangement in writing, one said the decision would be ‘communicated to the customer, most commonly in writing’, while the other said that a letter would be sent ‘if the assistance impacts upon the terms of the original agreement’.

We reviewed a sample of lenders’ template letters confirming assistance, from which it was clear that some lenders provide more information about the payment arrangements then others.

One letter, for example, explained that postponing payments resulted in additional cost as a result of the capitalisation of interest:

> Capitalisation of interest—We would like to draw your attention to the fact that this change to your repayments will involve capitalisation of the interest due. This means interest charged to your account under the original terms of your loan does not need to be paid on the agreed dates. However,

> the unpaid interest will continue to accrue to your account and further interest will be charged on that interest until either a sufficient lump sum payment is made or the loan is repaid.

Another letter confirmed the arrangement, but also included information about the UCCC process ensuring the borrower was aware that further options remained available:

> **Important information regarding financial difficulty:** You are entitled to apply for hardship assistance under the Consumer Credit Code. If you are not satisfied with our decision relating to your hardship application, you may apply directly to the relevant court or tribunal in your State or Territory to change the terms of your contract. Contact your Government Consumer Agency or get legal advice on how to do this. Financial counsellors may also be able to help you.

Some lenders made no effort to fully disclose to borrowers the nature of the repayment arrangement, including capitalisation of interest or their right to dispute the decision.

In the United Kingdom, it is mandatory for lenders to give adequate information and a reasonable time period for customers to consider the implications of any proposed arrangements.[15]

## Joint borrowers

Our review of lenders' policies found that where a loan involves more than one borrower, all borrowers must usually be a party to an agreement to provide relief or assistance on the grounds of financial hardship.

This is an issue that has been raised by consumer advocates such as financial counsellors, who have reported difficulties in obtaining financial hardship relief for a client who has separated from their partner (a co-borrower) and cannot afford to meet the repayments on their loan.

This issue is particularly relevant given that relationship breakdown was cited by lenders as one of the main causes of financial hardship.

## Refusing an application

Based on responses from lenders, the most common reasons for refusing financial hardship applications were:

- the borrower would be unable to meet the repayment terms of the loan contract (even if they were to be varied), and
- the borrower would be unable to meet their credit obligations in the long run.

[15] Financial Services Authority, *FSA Handbook*, MCOB 13.3.4, 'Dealing fairly with customers in arrears: policy and procedures'.

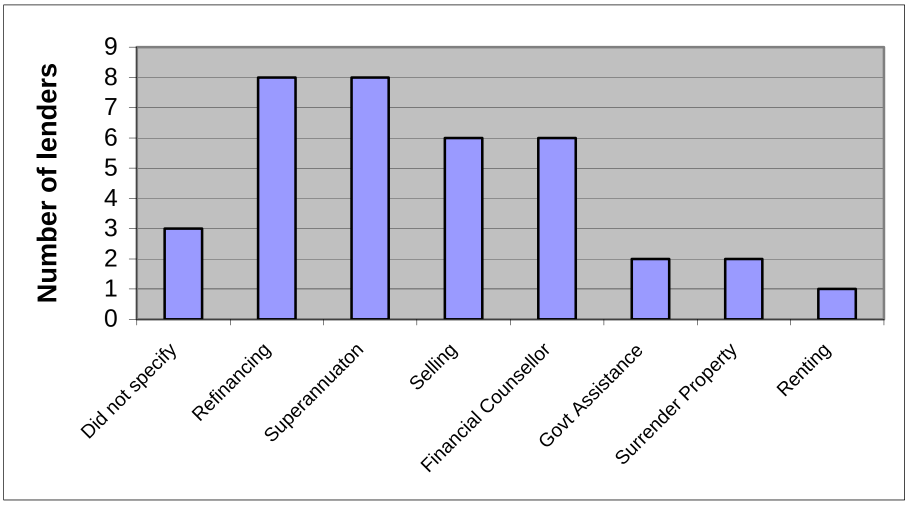
Some lenders also mentioned the following procedural reasons for not accepting a loan application:

- the documentation was not returned, and
- the mortgage insurer did not approve.

We asked lenders whether, if an application for assistance or relief is refused, they take steps to discuss the borrower's situation and options available to them. Most lenders inform borrowers that their application has been refused and discuss options available to them over the phone.

Figure 4 outlines the options different lenders will discuss, and shows that those most likely to be discussed include refinancing, early release of superannuation, selling and/or seeking the advice of a financial counsellor.

**Figure 3: Options discussed when assistance is refused**




In addition, letters we reviewed showed that some lenders also inform borrowers of their rights:

- under s66(2) of the UCCC to apply to the court to change the terms of the contract if the credit provider does not do so in accordance with an application made by the borrower (see s68), and/or
- to complain to a relevant EDR scheme, such as the Financial Ombudsman Service (FOS) or the Credit Ombudsman Service Ltd (COSL).

While refinancing might be an option to help some borrowers who are struggling to meet their payments on their current mortgage and can obtain a cheaper loan, ASIC's report examining refinancing by borrowers in response to financial difficulties showed that many pitfalls can occur in these circumstances.[16] For example, borrowers are likely to be charged higher then average fees, and in some cases where there are serious problems refinancing may only be a temporary solution.

For a discussion of early release of superannuation, see Section D.

### Treatment of debt after refusal

We asked lenders what happens after an application for relief or assistance on the grounds of financial hardship has been refused for an account in default.

All lenders said that the debt would be referred to the collections area (or, if already in a collections area, reactivated) and would be subject to normal collections processes.

Some lenders may take steps to help the borrower after their hardship application has been refused in this situation. Examples of such assistance include:

- if the borrower elects to place the property on the market they may be allowed additional time to sell the property themselves, avoiding a mortgagee sale, and
- a short period (2–4 weeks) of reduced payments may be granted for the borrower to seek independent financial advice.

## Types of assistance or relief available

We asked lenders what type of assistance they might provide to borrowers who are experiencing financial hardship. Most lenders said that they do not restrict assistance to the options provided under the UCCC, and offer a range of assistance beyond this: see Table 3.

However, when referring to changes or variations made to loan contracts under the UCCC, one lender stated in its policies and procedures that those changes and variations have 6-month limitations.

In fact, the UCCC does not refer to any specific time periods for assistance or relief.[17] It is important to ensure that rights to which consumers are entitled are properly reflected in policies and procedures.

[16] REP 119 *Protecting wealth in the family home—An examination of refinancing in response to mortgage stress*, March 2008, at www.asic.gov.au.
[17] See Section A of this report for a discussion of s66-68 of the UCCC.

**Table 3: Common types of hardship assistance or relief available from lenders**

| Type of assistance | Description |
|---|---|
| Capitalising, capping or re-ageing | Arrears are added to the loan balance and the loan term is extended. This option may be appropriate for borrowers who can currently meet the repayments on their loan but need help with current arrears. |
| Reduced repayments | This option involves reducing the amount of the borrower's monthly repayments, and may be appropriate where a borrower can afford to service some of their loan. |
| Moratorium | This option involves stopping all payments for a specified period, and may be appropriate where a borrower cannot meet any payments during hardship. |
| Payment holiday | If a borrower is ahead in payments on their home loan, they may be able to use this amount as a buffer to reduce current repayments. |
| Debt consolidation | This option involves aggregating multiple debts. |
| Mortgage assistance | Some states and territories have schemes to help borrowers who are having temporary difficulties meeting their commitments after a change in their circumstances |
| Financial counsellor | Financial counselling services help people who are in financial difficulty. They are available in every state and territory and provide a free, independent and confidential service. |
| Reduce spending | A borrower may be able to reduce non-essential spending. |

## Matching assistance to need

As Table 3 indicates, each of the options for assistance is designed to operate within a specific scenario and meet a specific need. For example, a payment moratorium may help someone entering into a period of reduced financial capacity but will not help someone who has come through such a period.

For that reason, the more options that a lender is prepared to consider, the more likely it is that a borrower's actual needs will be met. Equally important, however, is ensuring that available options are actually considered and discussed with a borrower.

One factor that seems to play a part in the options lenders discuss with borrowers is a bias towards short-term relief, rather than longer-term or less common types of assistance.

## Bias towards short-term assistance

A concern consistently raised by consumer advocates such as financial counsellors is that consumers seeking relief or assistance on the grounds of financial hardship are provided with short-term assistance, often a 3-month payment moratorium, rather than assistance that actually meet their needs.

The responses to our questionnaire and the policies and procedures that we reviewed suggest some lenders do prefer to respond to a request for assistance or relief by providing short-term relief, usually in the form of a payment moratorium.

In some cases, this approach was tied to attempts to streamline the process for obtaining assistance, particularly by those lenders dealing with requests for assistance over the phone.

The procedures that we reviewed showed that lenders are prepared to provide short-term assistance on the basis of a less rigorous assessment process. Considering longer-term assistance or less common forms of assistance may require:

- a greater level of inquiry, including collecting additional documentation
- greater effort to implement, and/or
- higher level sign off.

There is a danger, however, that responding to a request for assistance or relief by providing something that can be provided quickly and easily, rather than providing something that actually meets the needs of the individual seeking assistance, will result in poor outcomes for both borrowers and lenders.

A preference for short-term assistance also appears inconsistent with the most common causes of financial hardship, which include unemployment, relationship breakdown and illness. With respect to unemployment, for example, statistics show that the median duration of unemployment for persons who are looking for full-time work is 13 weeks.[18]

Problems created by providing short-term assistance to borrowers needing longer-term assistance may be exacerbated where the lender also has a policy of restricting the number of times that assistance will be provided, as a willingness to respond quickly to a request for assistance by providing short-term relief may operate as a bar to obtaining appropriate relief.

[18] Australian Bureau of Statistics, ‘Australian Labour Market Statistics’ 6105, July 2008.

# C What mortgage brokers are doing

**Key points**

Even though the MFAA Code of Practice imposes specific obligations on its members for dealing with borrowers in financial hardship, we found divergent views among mortgage brokers about their role in this regard.

While most mortgage brokers told us that they offer assistance to borrowers who may be in financial hardship, many appear to have little in the way of policies and procedures for doing so.

## Identifying financial hardship

We asked mortgage brokers how they determine or assess whether a borrower is in financial hardship.

One mortgage broker group expressed the view that mortgage brokers cannot engage in such conduct without holding an Australian financial services licence (AFS) licence, despite credit being excluded from the licensing regime: see the discussion later in this section.

Other mortgage brokers rely on borrowers self-identifying hardship and contacting them. However, it was evident from responses that this seldom happens because borrowers are more likely to contact their lender instead.

One mortgage broker encourages borrowers to make contact with them if they experience difficulty in meeting payment obligations, but reported that few borrowers do. This broker more commonly identifies hardship when trail commission payments cease as a result of the loan contract falling into arrears. When this happens the mortgage broker contacts the borrower to offer assistance.

An important aspect of identifying financial hardship is understanding what financial hardship means. None of the mortgage brokers surveyed had adopted a definition of financial hardship. Some brokers suggested they rely on general industry standards (although they did not specify what these standards were) or would assess each matter on a case-by-case basis.

## Helping borrowers in financial hardship

We asked mortgage brokers whether they offer assistance to borrowers who may be in financial hardship.

Most mortgage brokers told us that they do offer assistance to borrowers who may be in financial hardship. However, this was not necessarily consistent with responses to other questions, which suggested assistance offered may be very limited or restricted.

It was also evident that some brokers see refinancing as the first option when responding to financial hardship. Issues relating to refinancing and consolidation are discussed in more detail below.

## Understanding the borrower's financial position

We asked those mortgage brokers who do offer assistance to borrowers who may be in financial hardship whether they identify a borrower's:

- level of repayments on the home loan
- income
- level of debt on all liabilities and minimum monthly payment obligations for those liabilities
- living expenses, and/or
- ability to access superannuation on the grounds of financial hardship.

All mortgage brokers identify the level of repayments and existing income. Most will identify other debt obligations and some will identify living expenses. One mortgage broker would not make any further inquiries beyond the borrower's level of repayments and existing income.

Understanding a borrower's financial circumstances is crucial to determining what assistance might be possible and appropriate for a borrower experiencing financial difficulties. Inquiries that fall short of adequately establishing a borrower's financial circumstances are likely to undermine efforts to offer or provide appropriate assistance.

Some mortgage brokers will raise the option of early access to superannuation. For a discussion of early release of superannuation, see Section D of this report.

## Identifying the causes of financial hardship

We asked mortgage brokers if they identify the cause of a borrower's financial hardship, and whether it is likely to be short-term or continuing.

As one mortgage broker noted, understanding the cause and likely term of financial hardship is essential to assessing the needs of the borrower and the response required.

Not all mortgage brokers share that view. One broker explained that it does not examine whether borrowers are experiencing short-term or long term problems, but instead advises borrowers to discuss their problems with their current lender or a financial counsellor.

Suggesting that the borrower contact the lender and/or seek assistance from a financial counselling agency is likely to be helpful advice, but in the absence of any further engagement by a mortgage broker this cannot really be described as offering or providing assistance.

Understanding the cause of a borrower's financial hardship, and indeed their current financial situation, would also appear to be necessary precursors to compliance with the financial hardship provisions of the MFAA Code of Practice.

## Working with the borrower

For many borrowers experiencing financial hardship an appropriate response to their difficulty may involve a variation to their repayment obligations.

All mortgage brokers said that a variation on the grounds of financial hardship was an option that would be discussed with borrowers in financial hardship. However, there was inconsistency in the level of engagement by mortgage brokers in this process.

Some mortgage brokers will merely advise a borrower that this option may be available to them. Others will contact the lender to discuss this option or assist the borrower to do so.

We asked mortgage brokers whether, if a variation was being considered, they discuss the extent of payment reduction required.

One mortgage broker said that it does not, despite elsewhere responding that it does offer assistance to borrowers and will consider options such as a variation to the home loan.

All other mortgage brokers do discuss the extent of payment reduction required. Interestingly, a standard response was that while some early discussions can take place over the phone in most cases, where possible, some face-to-face discussion between borrower and mortgage broker is required.

We asked mortgage brokers whether they would discuss other options, including:

- selling the home
- encouraging borrowers to prepare a budget of recent expenses, or working with them to produce a budget
- reducing living expenses, and/or
- seeking assistance from a financial counselling or other agency.

While a number of mortgage brokers would discuss the option of selling the home, some suggested that this would only arise as a last resort and at least one indicated it was not an option that would be raised at all.

While selling the home may often be unpalatable for borrowers and a difficult option for a mortgage broker to raise, ruling it out altogether does not seem an appropriate response given that in some situations it may be the best or indeed only solution for a borrower in particularly difficult circumstances.

Responses about the other options were inconsistent, suggesting there is no standard industry approach to identifying ways in which assistance can be provided to borrowers experiencing financial hardship.

## Consolidating and refinancing a borrower's debt

ASIC's report on refinancing in response to mortgage stress[19] found that in some circumstances refinancing merely defers the inevitable loss of the home, and does so at considerable cost to the borrower. For that reason it is important that mortgage brokers (and lenders) only recommend refinancing when the transaction has appropriate long-term benefits for the borrower.

In many cases, a refinance may also be used to consolidate other debts into a single loan.

As one mortgage broker observed in its response to us, paying otherwise short-term debts over a long term, even at a lower rate of interest, is not normally the best option but might be offered as a last resort option.

We asked mortgage brokers in what circumstances they would suggest that a borrower consolidate their debts through a refinance.

Some mortgage brokers said that they will not consolidate debts, or only in limited circumstances.

Of those that said they would consolidate debts, some would only do so if the borrower was currently meeting all credit repayments. Others noted that they would encourage the borrower to:

- cancel credit cards or have limits reduced to manageable levels for emergency purposes only, and
- meet with the borrower at least annually to review their situation even when things are going well.

[19] REP 119 *Protecting wealth in the family home—An examination of refinancing in response to mortgage stress*, March 2008 at www.asic.gov.au.

The caution expressed by a number of mortgage brokers about consolidating is encouraging, but this is an area that may warrant further attention in the future.

Consolidating or refinancing in response to financial hardship should also be considered in the context of obligations imposed by the MFAA Code of Practice, which requires in the first instance that the option of a variation to the existing facility be considered in good faith and, where that option appears reasonably appropriate, referring the borrower to the lender.

## The mortgage brokers' role

Although the MFAA Code of Practice sets out certain obligations relating to financial hardship for brokers who are members (see Table 2 in Section B), it is clear that mortgage brokers have differing views about their role in relation to borrowers who are experiencing financial hardship. Some mortgage brokers provide genuine assistance to those borrowers, others offer limited assistance and some appear to provide no assistance at all.

Several reasons were cited as to why mortgage brokers could not provide assistance, or only limited assistance, to borrowers in financial hardship.

### Need for an AFS licence

One mortgage broker believes that its ability to offer assistance to borrowers in financial hardship is very much constrained by the fact that it does not hold an Australian financial services (AFS) licence.

The provision of financial services is regulated by the *Corporations Act 2001* (Corporations Act), which imposes a licensing regime on financial services providers. Credit, however, is specifically excluded from the regime.[20] Accordingly, the provision of credit or related services, including providing advice or assistance in relation to a credit product, is not an activity for which an AFS licence is required.

It is anticipated that the proposed Commonwealth credit laws will impose a licensing regime on credit providers and intermediaries. However, this should not limit the ability of a mortgage broker to provide assistance to borrowers in financial hardship, as both the general broking conduct and any assistance in relation to hardship is likely to fall within that regime.

[20] Section 765A(1)(h)(i).

### Financial hardship seen as lender's role

A number of mortgage brokers told us that identifying financial hardship is the responsibility of the lender.

Although the lender is the key decision maker when it comes to applications for financial hardship relief or assistance, this does not mean an intermediary such as a mortgage broker has no role to play.

Mortgage brokers can provide essential information and advice to borrowers at a time when understanding appropriate options and making the right decision is likely to be critically important.

The confusion about roles also highlights problems that can arise where intermediaries are involved in a transaction the primary parties to which are borrower and lender. It would appear evident that where multiple parties are involved, it is likely to be more difficult to ensure borrowers are given clear information about assistance or relief for financial hardship and the manner in which that assistance or relief can be accessed. This issue may warrant further inquiry.

# D Early release of superannuation

**Key points**

Superannuation is for people to access in their retirement. However, in limited circumstances, such as severe financial hardship, legislation allows for a person to access a portion of their benefit before retirement.

If a borrower has defaulted on their home loan, some lenders and mortgage brokers will provide information to the borrower about early access to superannuation.

In some cases, early access to superannuation may be no more than a temporary fix, and one that can come at a high cost to the borrower—they may lose their home and their superannuation.

We are also concerned that lenders and mortgage brokers may be providing unlicensed financial product advice.

## Legislation and industry standards

### SIS Act

The *Superannuation Industry (Supervision) Act 1993* (SIS Act) permits the early release of superannuation under 'specified compassionate grounds'.[21] One of the grounds for early release is to prevent a lender from selling the borrower's principal place of residence.

The Australian Prudential Regulation Authority (APRA) administers applications for the early release of superannuation under the SIS Act. However, although APRA must be satisfied that a person's application meets the specified grounds, the final decision lies with the trustee of the superannuation fund.

Superannuation funds can also release superannuation benefits early on the grounds of:

- permanent incapacity
- terminal illness
- severe financial hardship

[21] Superannuation Industry (Supervisions) Regulations (1994), reg 6.19A. Specified compassionate grounds include medical treatment for serious conditions that are not readily available through the public health system, transport for medical treatment, changes to a home or vehicle because of a severe disability, palliative care, funeral and burial expenses, or to prevent the forced sale of your home by your mortgagee.

- permanent departure from Australia, and
- preserved benefits balance of $200 or less.

To access funds on the grounds of severe financial hardship, a superannuation member would need to:[22]

- be in receipt of a Commonwealth income support payment, and have been so, continuously, for the last 26 weeks, and
- satisfy the trustee/retirement savings account (RSA) provider that they are unable to meet reasonable and immediate family living expenses.

Benefits released early by superannuation funds are limited to one payout of no more than $10,000 including tax during a 12-month period.[23]

### Industry codes and standards

The MFAA Code of Practice provides that members who are lenders must not require the borrower to apply for the early release of their superannuation when they are in financial hardship.

COSL (the Credit Ombudsman Service Ltd) has issued guidelines, which provide that the procedural aspects of s66 of the UCCC do not allow a lender to impose additional conditions on a borrower (e.g. requiring the early release of superannuation) before considering or agreeing to a request for a hardship variation).

In 2007, the Banking and Financial Services Ombudsman[24] raised concerns about members requiring customers to apply for early release of superannuation before accepting an application for assistance.[25]

## Procedures in place

### Lenders

We asked lenders whether they inform borrowers during the hardship process about their ability to access superannuation early. Only 2 lenders said that they would not inform borrowers of their ability to access superannuation early (unless a borrower raised this with them).

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[22] This is for persons under their preservation age—currently 55. Other conditions apply for persons who have reached preservation age: see reg 6.01(5) and Schedule 1 of the SIS Regulations.
[23] See footnote 22.
[24] Now the Banking and Financial Services division of the Financial Ombudsman Service.
[25] FOS Bulletin 53 March 2007, Customers in financial difficulties—Code of Banking Practice and UCCC Obligations.

We found that lenders may raise the option of early access to superannuation at various stages in the process of dealing with a request for relief or assistance on the grounds of financial hardship, including when:

- assessing an application for relief or assistance, or
- refusing an application for relief or assistance.

Only 4 lenders told us that they advise borrowers to seek advice or assistance from a financial counsellor if considering early access to superannuation.

One lender said that:

- staff are instructed not to consider the early release of superannuation as a standard assistance option that should be offered to borrowers, and
- collections staff are not permitted to use this option as a collections tool.

### Mortgage brokers

While some mortgage brokers will raise the option of early access to superannuation, others will not.

## Early access may not solve the problem

In many cases, if a borrower is experiencing significant financial difficulties, a lump sum payment may be only a temporary solution.

The worst-case scenario is that a borrower ends up losing their home *and* part of their superannuation. In fact, we found that this worst-case scenario is a real one for some borrowers.

We asked lenders how many accounts had been subject to an APRA-approved payment during the year 2007 and sought details of the performance of these accounts after the APRA-approved payment was received.[26] In all cases, the lenders who obtained this information reported to us that some accounts had gone back into default after the APRA-approved payment was made.

A breakdown provided by one lender showed that approximately 1 in 4 accounts returned to a non-performing status after receiving an APRA-approved payment: see Table 4.

[26] As this information was not readily stored on lenders' systems we only received a very limited number of responses to these questions.

**Table 4: Account status after APRA-approved payment**

| Status of account after payment | No. of accounts |
|---|---|
| Performing accounts | 146 |
| Accounts in default | 42 |
| Property in possession | 10 |
| Property sold and loss has been realised | 2 |
| **Total accounts subject to an APRA-approved payment in 2007** | **200** |

Table 4 shows that even if a borrower accesses their superannuation early this might not help them in the long run. There is a risk that the borrower might fall behind in payments again and their house could be repossessed by the lender or otherwise sold.

Table 4 also identifies 2 cases where borrowers' homes were sold and a loss was realised, indicating that each of those borrowers is likely to have lost any funds that were contributed to their mortgage, including superannuation.

It is clear that early access to superannuation may not be appropriate where there are underlying financial problems that a lump sum payment will not resolve.

This area is likely to warrant further work.

## Providing financial product advice

Since superannuation is a regulated financial product under the Corporations Act, a person who is providing financial product advice about superannuation needs to be licensed to provide financial product advice.[27]

In some cases, if lenders or mortgage brokers are informing borrowers about their ability to access superannuation, they may be providing unlicensed financial product advice. In particular, if they are taking into account a borrower's financial situation, such advice could constitute personal advice.

For more information about conduct that constitutes financial product advice, see ASIC's Regulatory Guide 36 *Licensing: Financial advice and dealing* (RG 36).

[27] Financial product advice means a recommendation or statement of opinion, or a report of either of those things, that is intended to influence a person or persons in making a decision in relation to a particular financial product.

# E Taking action

## What we will do

Currently ASIC has limited powers in relation to credit, covering broad standards of conduct, including:

- prohibitions on unconscionable conduct, and on conduct that is misleading or deceptive, and
- prohibitions on false and misleading representations.

It is expected that by mid-2009, the UCCC will be enacted as federal law and extended powers will be given to ASIC to regulate consumer credit.[28]

Further changes will be made to the national credit framework including:

- establishing a national licensing regime to require providers of consumer credit and credit-related brokering services and advice to obtain a licence from ASIC
- requiring licensees to observe a number of general conduct requirements including responsible lending practices, and
- requiring mandatory membership of an EDR scheme by all providers of consumer credit and credit-related brokering services and advice.

These changes, such as requiring licensees to observe a number of general conduct requirements, are likely to have a positive impact on how lenders deal and respond to borrowers experiencing financial hardship.

Within the scope of ASIC's current jurisdiction, with the assistance of CAV, we will:

- refine consumer education materials on the FIDO website about financial hardship and the options available to consumers
- work with industry to ensure that the poor practices identified in this report are improved upon
- work with EDR schemes to identify lenders and mortgage brokers whose hardship processes do not comply with the UCCC, and take appropriate action
- work with financial counsellors and consumer advocates to monitor lenders and mortgage brokers' conduct when dealing with consumers in financial hardship, and
- undertake further work on the issues identified in Section D of this report.

[28] 2 October 2008, Council of Australian Governments agreed that the Commonwealth would assume responsibility for all areas of credit. The Uniform Consumer Credit Code will be enacted into federal legislation by mid-2009.

## What lenders can do

| Suggested action(s) | Things to consider |
|---|---|
| **1. Give borrowers information early**<br><br>Provide *all* borrowers with information they can freely access about options available to them if they are experiencing, or begin to experience financial hardship. | • Can borrowers easily obtain information about financial hardship and the options that may be available to them on your website?<br>• Is information about financial hardship targeted to reach borrowers who are likely to be experiencing financial difficulties? For example, is it included in all correspondence sent to borrowers about overdue payments?<br>• Do you tell borrowers about their rights to request assistance or relief on the grounds of financial hardship under the UCCC?<br>• Is the information easy to understand? Is it written in a friendly manner that won't intimidate? |
| **2. Set up a contact number**<br><br>Set up a dedicated toll-free number for borrowers to make inquiries about financial hardship. Ensure staff are adequately trained to provide borrowers with options that may help them overcome their financial difficulties. | • Is the contact number for financial hardship promoted and easy to obtain by borrowers? Does the number have operating times that meets the needs of borrowers? Is the number adequately staffed to meet the needs of borrowers?<br>• Are staff adequately trained to discuss options with borrowers that are realistic and appropriate to the borrowers circumstances? Are the options clearly explained with implications?<br>• If the borrower needs further assistance, is the borrower given a dedicated point of contact with the lender? |
| **3. Check with borrowers who are in arrears**<br><br>Ensure that you have made reasonable inquiries with a borrower who is in arrears to ascertain whether they could meet their mortgage obligations if their repayment terms were varied. | • Before collection action begins, have you ensured that all reasonable efforts have been made to keep the borrower in their home?<br>• Have you discussed with the borrower a hardship variation? |
| **4. Look at other credit products**<br><br>Inform the borrower that they might be able to seek assistance for other credit products they have. | • Does the borrower have other credit products:<br>– with your organisation?<br>– with another financial institution? |
| **5. Simplify information requested**<br><br>Ensure that documentation you request to assess and determine an application for financial hardship is not overly burdensome. | • What documents do you currently need to obtain to assess an application for financial hardship? Can this be reduced?<br>• Can you take more information about the borrowers' financial situation over the phone?<br>• Can you alert the borrower earlier about the documents they are likely to need to produce? |

<table>
<tr><th>Suggested action(s)</th><th>Things to consider</th></tr>
<tr><td>6. Assess hardship variations promptly and fairly<br><br>Assess hardship variations based on the borrower's ability to service the loan in the long run.<br><br>Ensure that the length of time over which assistance is provided is practical.<br><br>Respond to and determine an application for a hardship variation without unnecessary delay.</td><td>• When determining an application for a financial hardship variation, are you considering factors that may unfairly disadvantaged the borrower, such as taking into consideration past applications the borrower has made for financial hardship?</td></tr>
<tr><td>8. Follow up with borrowers if you refuse a hardship variation<br><br>If you refuse a hardship variation, inform the borrower verbally and in writing about this decision.</td><td>• Have you explained to the borrower the reason(s) their hardship variation was refused?<br>• Is the borrower aware of their rights under s66(2) of the UCCC that they can apply to a state court or tribunal to change the terms of their loan?<br>• Is the borrower aware that they can access an ASIC-approved EDR scheme to complain about the decision?<br>• Do you have a checklist of appropriate options staff can discuss with borrowers that may assist them?</td></tr>
<tr><td>9. Keep consumer credit insurance in mind<br><br>Ensure that no collection action is taken on a loan where a CCI claim is pending.</td><td>• Have you asked the borrower whether they have a CCI policy?<br>• Does the borrower have a claim pending?</td></tr>
</table>

## What mortgage brokers can do

| Suggested action(s) | Things to consider |
|---|---|
| **1. Obtain borrower information**<br><br>Make all reasonable inquiries to obtain information about the borrower's financial situation. | • Is the borrower currently struggling to meet the repayments on their loan?<br>• Are the borrowers' financial difficulties temporary or ongoing?<br>• Have you inquired and assessed the borrowers' assets, liabilities, income and expenditure? |
| **2. Assess hardship options**<br><br>If the borrower is experiencing financial difficulties consider whether they would benefit from negotiating a payment arrangement with their lender or requesting a hardship variation. | • Have you discussed with the borrower:<br>– negotiating a payment arrangement with their lender (e.g. a repayment holiday)?<br>– their right to request a variation on the grounds of financial hardship, if they are eligible?<br>• Can you provide information and assistance to borrowers on these options and others, or encourage borrowers to contact sources that will provide them with free information and advice (e.g. the FIDO website, information from their lender or the advice of a financial counsellor)? |
| **3. Assess other options**<br><br>You can consider other options that may assist the borrower, including:<br>• refinancing, and<br>• selling their property. | *Refinancing:*<br>• Have you ensured that the borrower will be better off as a result of refinancing, and you have only recommend a loan that is appropriate with long-term benefits for the borrower?<br>• Have you made all necessary inquiries to ensure that the borrower can repay the loan?<br>• Have you disclosed all the costs of refinancing, and all fees and commissions in writing, so that the borrower can make an informed decision?<br><br>*Selling:*<br>• Have you compared the advantages and disadvantages of the borrower selling their home compared to a refinance?<br><br>*Remember:* Borrowers in financial stress need realistic information and advice. |

## What borrowers can do

| Steps to take | Things to consider |
|---|---|
| **1. Contact your lender**<br><br>If you are struggling to meet the repayments on your mortgage you should contact your lender and/or mortgage broker as soon as possible to discuss your situation. | • Are your financial problems temporary?<br>*If yes*:<br>– Discuss your situation with your lender and work out what you can realistically pay towards your loan now.<br>– Make sure you are honest.<br>– Remember, the sooner you act the easier it will be for your lender to try and help you.<br><br>*If no*:<br>– You will carefully need to consider whether you can afford to keep meeting the repayments on your mortgage.<br>– If you cannot successfully demonstrate to your lender that you will be able to pay your loan off in the long run, they are unlikely to negotiate a payment arrangement or accept a hardship variation from you.<br>– Act quickly and see if your lender can give you some time and flexibility in the short term for you to decide what to do.<br>• If you are unsure about whether you can afford to pay or not, contact a financial counsellor for help (see www.fido.gov.au). |
| **2. Ask for a hardship variation**<br><br>The law gives you the right to ask your lender to enter into a hardship variation to:<br>• extend your loan to reduce your repayments, and/or<br>• postpone your repayments for a period of time.<br><br>Note: A hardship variation gives you temporary relief. You still need to pay off your entire mortgage, but it will be stretched over a longer time period (and you will pay more interest in the long run). | • If your lender agrees to vary your loan, do you understand:<br>– what payments you need to make now?<br>– what payments you need to make when the variation period ends? (depending on the type of variation sometimes this will change)<br>– if your loan contract has been extended, what impact this will have on you?<br>• Is the hardship variation for a time period that will see you through your difficulties?<br>• A financial counsellor, community legal centre or solicitor may be able to help you ask for a hardship variation (see www.fido.gov.au).<br><br>*Remember:* You do not have to agree to a hardship variation if it is not on the terms you requested. You can dispute the decision (see step 4). |
| **3. Talk to other creditors**<br><br>Talk to all of your other creditors including credit cards, store cards and good and services. | • Again, the sooner you take action and discuss your financial problems with your creditors, the easier it will be to try and work out a solution.<br>• If the credit is covered by the UCCC, you can request a hardship variation for these products also. |
| **4. Complain if something goes wrong**<br><br>If your lender is a member of an external dispute resolution scheme approved by ASIC, then the service may be able to hear your complaint. | • If your loan is covered by the UCCC, has your lender agreed to vary your loan on the terms you requested?<br>• If your lender has refused your request, you can apply to a tribunal or court in your state for an order to change the terms of your loan. |

| Other options for borrowers | Some tips |
|---|---|
| **Budget**<br>If you begin to feel the pinch of meeting the repayments on your mortgage take some time to think about your income and expenses, and see if you can reduce your expenditure. | • You can use **FIDO's budget planner** to help you prepare a budget and manage your income.<br>• There is also lots of information and tips on budgeting and dealing with debts at **www.fido.gov.au**. |
| **Negotiate a better interest rate**<br>See if you can negotiate a better interest rate with your lender | • If you are making payments at your banks standard variable rate you may be able to get a discount. |
| **Refinance**<br>You might consider switching to another type of loan product or changing to a different lender because they have a cheaper loan. | • Although refinancing might look like a good idea, weigh your options up carefully before making a decision:<br>– If you are already in default or under financial stress, be realistic about whether you can afford repayments under a new refinancing arrangement.<br>– You may have to pay large fees to get out of your existing loan and pay mortgage insurance again.<br>• Go to **www.fido.gov.au** for more tips and a checklist on what to look out for when switching loans. |
| **Seek government assistance**<br>Find out if you are entitled to benefits or other government assistance | • Visit the **Centrelink website** to see if you are eligible for any entitlements. The site includes specific information for unemployed, self-employed, people in crisis (e.g. recently separated, divorced or bereaved, ill or injured).<br>• Some state governments offer short- term interest-free mortgage relief loans to cover temporary shortfalls. Contact your local state Department of Housing. |
| **Ask for help**<br>Financial counsellors can help people who are in financial difficulties. They provide a free, independent and confidential service to help you work out the best options for your situation.<br>ASIC and CAV also have information about credit and other financial issues. | • A full list of financial counsellors is at www.fido.gov.au.<br>• ASIC Infoline: 1300 300 630, website: www.fido.gov.au<br>• CAV's credit advice line: 1300 558 181, website: www.consumer.vic.gov.au |
| **Sell your property**<br>You could downsize or consider renting for a while. | • If you are really struggling to meet the repayments on your loan and you do not see your financial position considerably improving, it may be better to sell your property now then leave it till later when you have incurred more fees or perhaps gone through an expensive refinance.<br>• Also, if you leave things too late (which can happen very quickly) you will lose your ability to sell the property on your terms. |
| **Access your superannuation early**<br>Hardship provisions allow for early withdrawal of superannuation by people who are experiencing severe financial difficulty. | • This is a last resort option and you should think about it carefully. You may risk losing your house *and* your superannuation.<br>• Get the advice of a financial counsellor to help you decide what is best for you. |

# Key terms

| Term | Meaning in this document |
|---|---|
| AFS licence | Australian financial services licence |
| APRA | Australian Prudential Regulation Authority |
| ASIC | Australian Securities and Investments Commission |
| ASIC Act | *Australian Securities and Investments Commission Act 2001* and regulations made for the purposes of the Act |
| Banking Code | Code of Banking Practice |
| CAV | Consumer Affairs Victoria |
| CCI | Consumer credit insurance |
| CCMC | Code Compliance Monitoring Committee for the Banking Code |
| Corporations Act | *Corporations Act 2001* and regulations made for the purposes of the Act |
| COSL | Credit Ombudsman Service Ltd |
| EDR scheme | An ASIC-approved external dispute resolution scheme |
| financial hardship | Section 66(1) of the UCCC defines financial hardship as:<br>A debtor who is unable reasonably, because of illness, unemployment or other reasonable cause, to meet the debtor's obligations under a credit contract and who reasonably expects to be able to discharge the debtor's obligations if the terms of the contract were changed in a manner set out in subsection (2) may apply to the credit provider for such a change |
| financial product advice | A recommendation or statement of opinion, or a report of either of those things, that is intended to influence a person or persons in making a decision in relation to a particular financial product |
| FOS | Financial Ombudsman Service |
| MFAA | Mortgage and Finance Association of Australia |
| RSA | Retirement savings account |
| SIS Act | *Superannuation Industry (Supervision) Act 1993* |
| SIS Regulations | Superannuation Industry (Supervisions) Regulations (1994) |
| UCCC | Uniform Consumer Credit Code |

# Related information

### Headnotes

Financial hardship, financial difficulties, lenders, mortgage brokers, consumer protection

### Regulatory guides

RG 36 *Licensing: Financial advice and dealing*

### Legislation

*Australian Securities and Investment Commission Act 2001*

*Corporations Act 2001*

*Superannuation Industry (Supervision) Act 1993*

Superannuation Industry (Supervisions) Regulations (1994), Schedule 1, reg 6.01(5), 6.19A

Uniform Consumer Credit Code, s66–68, 66(1), 66(2), 68

### Cases

*Permanent Custodians Ltd v Carolyn Joy Upston* [2007] NSWSC 223 (16 March 2007)

### Reports

REP 119 *Protecting wealth in the family home—An examination of refinancing in response to mortgage stress*

 