Australian Banking Association

07 August 2018

Australian Securities & Investments Commission
GPO Box 4000
Gippsland Mail Centre
Victoria 3841
By email creditcards@asic.gov.au

Dear Sir/Madam

Consultation Paper 303 – Credit Cards: Responsible lending assessments

The Australian Banking Association (**ABA**) welcomes the opportunity to comment on the Australian Securities & Investments Commission (**ASIC**) consultation paper 303 seeking feedback on the proposal for the prescribed period to be used when assessing whether a credit card contract or credit limit increase is unsuitable.

With the active participation of 24 member banks, the ABA provides analysis, advice and advocacy for the banking industry and contributes to the development of public policy on banking and other financial services. The ABA works with government, regulators and other stakeholders to improve public awareness and understanding of the industry's contribution to the economy and to ensure Australia's banking customers continue to benefit from a stable, competitive and accessible banking industry.

As we have noted in our previous submissions on improving consumer outcomes and enhancing competition in relation to credit cards, the vast majority of customers manage their credit cards and debt responsibly. The ABA acknowledges, however, that there is a small group of customers who experience financial stress.

The ABA strongly supports the implementation of workable and effective solutions to address the challenges faced by these customers. These need to be targeted to assist those customers suffering from financial hardship and complement the existing efforts of credit card providers in this area.

At the same time, care needs to be taken to ensure that any reforms are appropriate and do not risk increasing the price of credit, or unnecessarily restricting availability of credit for most credit card customers that use the revolving nature of the facility to smooth cash flows and take advantage of convenient payments and do not use it as a long-term credit facility.

The ABA holds a diverse membership consisting of major banks, smaller and regional banks as well as foreign banks. We note that on some aspects of the proposals outlined in the consultation paper, our members hold diverse views on policy settings and implications and these have been called out in the submission where relevant.

Implementation timeframe

The ABA is concerned that ASIC has not allowed sufficient time for industry to appropriately assess and develop the impact of this regulatory change on their products and IT systems as well as implement the necessary changes internally. The introduction of this change will require a significant investment of time and resources by the industry across many key areas, including:

- internal credit policies;
- product design and consumer information materials;
- compliance controls;

- core bank information and technology systems – change will be required across multiple systems, including decision engines for new credit capacity calculations;
- new procedures and policies for staff; and,
- staff training and education.

We strongly submit that ASIC's proposed compliance date of 1 January 2019 does not provide a realistic transition period for industry given the short timeframe facing industry following the release of a final instrument.

ABA members are also particularly concerned over this date given that many banks attempt to avoid making significant technology systems changes over the Christmas/New year holiday period due to the difficulty of coordinating development and testing at that time. Any change carries a potential higher risk to customers at this crucial time of the year when transaction processing is critical.

Case Study – ABA member bank

A regional bank has identified the major logistical challenges it will face in meeting the proposed compliance date of 1 January 2019.

Major changes will need to be made to 6 IT systems across the bank and these will need to be handled along with other key projects in its IT change queue. Like many in the industry, the bank puts a moratorium on IT work from 1 December through 31 January inclusive, meaning that these changes would have to be bundled in an already congested queue of prioritised work.

This insufficient timeframe imposes a significantly higher level of risk for the bank and its customers, as well as imposing a higher level of cost on implementation.

In February 2018, the UK's Financial Conduct Authority (**FCA**) released new rules and guidance on treatment of persistent credit card debt and earlier intervention. This required UK financial firms to make system changes and take other actions similar to some of those that would be required under ASIC's proposal. Following consultation with industry on required implementation, the FCA increased its compliance deadline with the new rules from three to six months.

Given the implementation challenges faced by industry, the ABA strongly recommends that ASIC does not implement a more stringent prescribed period until at least 1 July 2019.

Period for determining unsuitability in respect of credit card contracts

The ABA notes that ASIC proposes to prescribe a 'reasonable period' of three years for responsible lending assessments for new credit card contracts or credit limit increases and that this period would apply to all classes of credit card contracts.

In broad terms, the ABA supports the inclusion of a requirement for a credit card provider to conduct a responsible lending assessment of a consumer's ability to repay a credit limit within a 'reasonable period' for new credit card contracts or credit limit increases. We understand the intention of this reform is to prevent customers committing to an amount of credit that cannot be comfortably repaid, which would lead to an undesirably prolonged period of revolving credit.

However, the ABA notes that there is currently no industry consensus on what constitutes a 'reasonable period' or whether this should apply across all classes of credit cards.

'Reasonable period'

While ABA members support the inclusion of a requirement for a credit card provider to conduct a responsible lending assessment of a consumer's ability to repay a credit limit within a 'reasonable period', there are different views on what constitutes this period.

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Under clause 60 of the recently ASIC-approved ABA *Banking Code of Practice* (**Banking Code**), ABA members have committed to assessing a customer's ability to repay the amount of a new credit card or credit limit increase over a five-year period.[1] This will be binding on all banks with personal or small business customers wishing to be a member of the ABA.

Following the release of the consultation paper, some ABA members have indicated their support for a three-year repayment period in line with the ASIC proposal. There is a view that this is a reasonable period to assess a customer's ability to pay off a balance should the credit facility be fully drawn.

In an alternative view, other ABA members have expressed concern that the three-year period may be too restrictive and lead to some potential unintended consequences, including:

- limiting a customer's ability to smooth cash flows through responsible use of a flexible credit card facility;
- customers may seek access to alternative sources of credit, including non-mainstream credit products with less favourable interest rates and conditions, and
- exclude some customers from being able to access mainstream credit products and gaining the benefits of this flexible form of credit.

The consultation paper notes that the FCA requires credit card providers to consider a general consumer's ability to repay a credit limit within a "reasonable period" but does not provide a specific prescribed period. Instead, it provides guidance that credit providers "may have regard to the typical time required for repayment of an unsecured personal loan for that amount". The ABA notes that this period would often be for a term longer than three years.

Application across classes of credit card contracts

Under clause 60 of the Banking Code, the commitment by ABA members to assessing a customer's ability to repay the amount of a new credit card or credit limit increase over a five-year period will apply to all classes of credit card contracts. However, there are different views among ABA members on whether a shorter three-year period as proposed by ASIC should apply across all classes.

Some ABA members support the ASIC proposal for this to be imposed across all classes of credit card contracts as they believe it will reduce regulatory and operational complexity as well as being simpler to implement.

Other ABA members have expressed concerns about a three-year period applying across all credit cards as this blanket capture could potentially limit the accessibility of credit for some consumers (e.g., higher income-earning transactors who require higher limits and for whom there is no alternative product). It can be argued that this is not in line with the policy intent of the proposed changes, which is to address those consumers accumulating large debts.

There are a group of higher income consumers that seek out these types of credit cards for many reasons including as a means of managing cash flow, as well as taking advantage of other benefits such as interest free periods, frequent flyer points and complimentary insurances. Therefore, potentially limiting credit availability through this repayment period could have a real impact on these consumers who would not consider there to be comparable credit options available in the market.

Review period

Given the differing views on key aspects of these changes including the repayment period term and application across classes, the ABA recommends that ASIC conduct a review of its final instrument within two years. This would ensure that ASIC is able to review the operation of the changes in the context of their impact on consumers and as means of testing the market assumptions that has underlined its analysis.

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[1] Clause 60, *Banking Code of Practice,* approved by ASIC on 31 July 2018 with ABA members to implement by July 2019, available at: https://www.ausbanking.org.au/images/uploads/Banking_Code_of_Practice_2019_Web.pdf

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Fees and interest rates

The ABA seeks clarity on some of the key assumptions needed to be considered by credit providers in making responsible lending assessments under the proposal, including in relation to applicable fees and interest rates.

The consultation paper appears to provide no guidance on what assumptions should be made by credit providers in relation to fees charged to customers, such as late payment fees. In figure two, ASIC does not appear to have included any reference to fees as part of its calculation. Additionally, it is difficult for a credit provider to determine the exact level of fees that will be payable by a consumer over the course of the repayment period and generally these are not calculated as part of the overall credit card balance.

In terms of applicable interest rates, ASIC has indicated that it regards good practice for a credit provider to conduct an assessment assuming interest is accruing at the highest rate that applies under the credit card contract. The ABA notes that some credit providers do not currently calculate on this basis but on the average portfolio interest rate or a rate that would be representative of most of the portfolio. This is because only a small proportion of credit card balances are usually being charged the highest interest rate under the contract (e.g., cash withdrawals).

Switching ability

The ABA requests that ASIC consider how its proposal may impact on the ability of consumers to switch across different credit card products. This includes a consumer choosing to switch to a lower interest rate card product at the same credit provider or through a balance transfer for a card product at a competing credit provider.

As a credit provider will be required under this proposal to conduct the responsible lending assessment on the more restrictive three-year term period, some customers may be restricted from switching to a lower rate product, particularly in the context that there is no ability to compel the closing of the existing credit facility.

Yours faithfully

Justin Mining
Policy Director