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Mr Richard McMahon
Senior Manager
Deposit Takers, Credit and Insurers
Australian Securities and Investment Commission
GPO Box 9827
Sydney NSW 2001

Via email: creditcards@asic.gov.au

Dear Mr McMahon

CP303 – Credit Cards: Responsible lending assessments

Thank you for the opportunity to provide comment on CP303 – Credit Cards: Responsible lending assessments.

COBA is the industry association for Australia's customer-owned banking institutions – mutual banks, credit unions and mutual building societies. The customer owned banking sector comprises 74 ADIs with total assets of more than $110 billion, 4 million customers, and 10 per cent of household deposits.

Key Points

- COBA requests additional time (i.e. 6 months) for credit card providers to make these changes to allow for more orderly and efficient implementation
- COBA members opinions vary about the appropriateness of the single three-year period, particularly relating to the blanket application across all circumstances.
- Customer-owned banking institutions provide good-value credit card products, particularly focused in the low interest market
- Improving financial literacy can help reduce consumer harm and reduce the impact of the issues that this reform seeks to address

Customer-owned credit card products

While our sector offers a wide range of credit card products, the most common product provided by COBA members are low interest rate credit cards. These products are highly competitive in the market place with all CANSTAR's outstanding value (5-star) low rate credit cards coming from the customer-owned sector. Customer-owned institutions provide a further 17 of 24 CANSTAR's 4-star low rate credit card products.[1]

CANSTAR's website shows that there are around 40 credit cards from customer-owned banking institutions with a purchase rate of less than 13 per cent[2]. The vast majority of our

[1] CANSTAR 2018 Credit Cards Star Ratings https://www.canstar.com.au/wp-content/uploads/2018/04/Crystal-Reports-Credit-Cards-2018.pdf
[2] CANSTAR https://www.canstar.com.au/compare/low-interest-rate-credit-cards/

sector's credit cards are well below the interest rate used by ASIC in CP303 (22 per cent), with the lowest available interest rate at 8.99 per cent. In some cases, COBA members' credit cards have lower interest rates than their unsecured personal loan offering.

The difference between a low and high interest rate card can lead to a significant saving in the level of interest paid by consumers (see Table 1). ASIC's REP 580 highlights the aggregate potential saving noting that consumers revolving debt on a high interest rate card could have saved $621 million if they shifted to a low rate credit card (i.e. with a rate less than 13 per cent). Consumers could benefit from utilising lower rate cards, including those from the customer-owned banking sector.

Table 1: Total Interest Paid (as % of credit limit) over repayment period

	Interest Rate												
	10%	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%	21%	22%
3 Year Period	16%	18%	20%	21%	23%	25%	27%	28%	30%	32%	34%	36%	37%
4 Year Period	22%	24%	26%	29%	31%	34%	36%	39%	41%	44%	46%	49%	51%
5 Year Period	27%	30%	33%	37%	40%	43%	46%	49%	52%	56%	59%	62%	66%

Improving financial literacy

COBA believes that there are competitive products and genuine choice in the credit card market. While COBA supports the intent of this reform, COBA wants to stress the important role that financial literacy plays in reducing consumer harm. Better financial literacy can assist consumers to remain informed and empowered to act in their own interests.

COBA notes that this reform seeks to ensure that consumers are able to repay their credit limits in a reasonable period. However, while this reduces the potential harm in terms of the potential size of the debt, it does not address how consumers end up in a harmful situation.

COBA believes ASIC and other government agencies could do more to ensure that consumers are better informed about the diversity and range of offerings in the credit card market, potential credit card alternatives and the risks of high-rate cards.

Additional time to implement the prescribed period

COBA members have varying opinions about the appropriateness of the three-year period, particularly relating to the blanket application across all circumstances.

COBA agrees that a single period for all classes of credit card contracts, credit limit amounts, and interest rates would simplify the implementation process. However, some COBA members have noted that multiple periods may be appropriate for lower interest rate products[3], or for larger credit limits.

COBA notes that even if a single period is quickly prescribed the timeframe will be challenging given that these changes to systems and processes will need to be done within four months to meet the 1 January 2019 deadline (assuming the instrument is made by the end of August). COBA members have raised concerns about the practicalities of meeting this timeline given the overlap with the holiday period.

Given that the implementation date was known at the passage of the bill, COBA members believe that it would been greatly beneficial to have consulted on and made the instrument earlier this year to give the entire industry, particularly smaller credit card providers, a more reasonable implementation period.

[3] Noting that CP330 starts with the assumption of a 22% interest rate.

COBA notes that our members are subject to the cumulative cost burden of multiple simultaneous legislative and regulatory changes. These include the Banking Executive Accountability Regime, accounting standard changes, comprehensive credit reporting, and APRA's proposed information security standard. In aggregate, continual regulatory change imposes a disproportionate cost on smaller entities given their more limited resources.

In line with this, COBA requests additional time (i.e. 6 months) to implement these changes. COBA believes that a short extension is unlikely to have a material detriment on consumers while allowing industry more time to implement these measures. COBA notes that this extension would provide a more reasonable 9-month implementation time (inclusive of the holiday period) from the making of the instrument.

Future review of the prescribed period

COBA also notes that the proposed 3-year period is shorter than the various periods proposed by industry. Some COBA members believe that this could lead to certain types of consumers (such as lower income consumers) turning to less regulated lenders or less appropriate products.

COBA believes that ASIC should review the prescribed period in future, potentially in line with the 'follow-up' review outlined in REP 580.

Consistency with the two-year period

COBA strongly objects to ASIC prescribing a period of two years to align with the minimum repayment warning under reg 79B of the National Credit Protection Regulations 2010.

There is no reason as to why these periods need to align given that they are for different purposes (repaying a balance faster vs. repaying a credit limit within a reasonable period). This approach would restrict the availability of credit cards, consistent with the CP303's observation that the "two-year period would have a greater effect on access to credit card contracts".[4]

Required system and process changes

COBA members note that given the broad scope of these reforms they will require changes to multiple systems and processes.

As noted in ASIC's REP 580, credit providers currently assess credit cards based on the ability to make monthly repayments of a fixed percentage of the credit limit. These reforms shift this fixed percentage amount to an amount that varies, at minimum, with the interest rate charged on that card. While COBA agrees with this assumption, this subtle change will lead to system changes across the board as providers will now need to calculate repayments that vary with the interest rate on the underlying credit card product.

Broadly, the following system changes will be required:

- incorporate the revised serviceability methodology into origination calculators, often across multiple systems which now requires a different calculation for each product based on its interest rate (see below)
- collecting additional and record data on interest rate for other institutions cards (including how these will be collected from customers), and
- recording additional data and information for compliance purposes.

[4] COBA notes that the assessment repayment under a 2-year period is 55-70% higher than a 3% of credit limit repayment.

As with all system changes, these will need to go through system development, testing, assurance and deployment stages. Most COBA members rely on external system providers or third parties to make these system changes. This generally extends the time required to implement any necessary system changes given the commercial negotiations required.

A COBA member has also noted that they are currently using a legacy credit card origination system which means that more time is required to ensure that changes are implemented with the necessary due diligence and care. They note there are potential system workarounds but these options still require additional time for implementation and quality assurance.

COBA notes that the following processes will require changes (listed in order of increasing complexity):

1. Serviceability assessment when originating a credit card
2. Serviceability assessment when originating a credit card, involving the assessment of repayments on another credit card (whether it is from the originating institution, or another institution), and
3. Serviceability assessment when originating other credit products (i.e. home loans), involving the assessment of repayments on a credit card (whether it is from the originating institution, or another institution).

COBA members will need to develop new procedures and policies for staff to align with these system changes as well as develop and implement staff training in these new requirements. This will be complicated by the end of year holiday period and short implementation period. Moving the implementation period outside of the end of year holiday period will ensure that there are appropriate resources and support available if there are issues.

COBA also notes that providers may also need to put communication plans in place to help customers and staff understand the potential impacts that these changes have on a customer's borrowing capacity.

Further clarifications on assumptions

Assumptions 48-49: Inclusion of interest and fees

COBA agrees that repaying the credit limit within the prescribed period should include interest charges.

However, COBA asserts that credit providers should not be required to include fees within its assumptions on for credit assessment in these circumstances. COBA seeks clarification that ASIC agrees with this assertion.

Card issuers can charge a variety of fees under their credit contracts, which can vary depending on customer spend, product selection, and repayment behaviour. Including fees would substantially increase the complexity of credit assessments through the potential need to model behaviour (or at least common assumptions about behaviour) and an increase in data requirements.

Assumption 50: Use of highest rate under the credit card contract

ASIC notes that "it would be good practice for the assessment to assume interest is accruing at the highest rate that applies under the credit card contract." COBA notes that there would be a range of rates under a credit contract and not all are applicable to the primary purpose of a credit card.

In our view the highest rate should refer to the purchase rate rather than the cash advance rate for credit assessment purposes as this provides a better balance between assessing an applicant's ability to repay and ensuring reasonable access to credit. The purchase rate aligns with a credit card's primary purpose to enable purchases as a substitute for cash.

Assumption 51: Inclusion in other credit contracts such as home loans

COBA notes that this creates the reasonable expectation that providers will utilise the above assumptions for existing credit card contracts.

COBA seeks clarification about whether Assumption 51 extends to assessments for other credit contracts (such as home loans) where a consumer has an existing credit card contract. COBA notes that it will take longer to adapt systems to meet this requirement.

If this is the case, then COBA seeks clarification about ASIC's expectations for pipeline application management. It can often take several months for a home loan to be settled, however the customer is likely to receive a 'pre-approval' from their lender in the interim. COBA presumes that its members will be able to honour all 'pre-approvals' issued prior to 1 January 2019 (or any extended date) that have been credit assessed based on the legislative requirements at that time without a need to reassess the customers' ability to repay prior to settlement, which may occur or after 1 January 2019 (or any extended date).

Additional assumptions: use of a conservative proxy

Some COBA members have noted that it may be simpler and more efficient for their organisation to assess all other institutions' cards at a single conservative interest rate (i.e. the 22 per cent indicated in ASIC's CP303 which is equivalent to a 3.8% of credit limit monthly repayment) rather than calculate interest rate-specific repayments. COBA seeks clarification whether this approach is acceptable, that that this meets the requirement to repay the limit within a three-year period for the vast majority of credit cards.

Thank you for the opportunity to comment on this consultation paper. Please contact Mark Nguyen, Senior Policy Adviser on 02 8035 8443 if you have any further queries.

Yours sincerely

MICHAEL LAWRENCE
Chief Executive Officer