Finance Industry Delegation
Australia

FINANCE INDUSTRY DELEGATION

Response to

ASIC

Consultation Paper 309
Update to RG 209: Credit licensing: Responsible lending conduct

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INTRODUCTION

This response is presented on behalf of the Finance Industry Delegation, a representative entity supported by 187 small, medium and large Australian Credit Licensees, both credit providers and lessors, across Australia, all of whom face an ever increasing and onerous burden of compliance regulation.

The opportunity to respond to Consultation Paper 309 is appreciated, because it provides an opportunity to avoid the impact of an unrealistic, one size fits all attempt to interpret the National Consumer Credit Protection Act 2009 and to avoid a potential effective failure to accept that the credit product spectrum is very wide.

Finance Industry Delegation supporters conduct their businesses in a very cost sensitive environment where any increase in compliance regulation is a critical cost impost. Without careful review, the attempt to impose standards far more suited to much larger, highly profitable loans (measured in dollar terms) would mean there would be a mass exodus from the industry sector, with the result that up to 1.75 million Australians will be denied commercial non-bank finance and leasing.

The Finance Industry Delegation respects ASIC's concern for clarity (mentioned 13 times in the Consultation Paper) and guidance (mentioned 119 times), but the prescriptive Regulatory Guide 209 regime that could emerge would provide an opportunity to effectively impose considerably greater regulation on the already overburdened sector. This imposition would also seriously threaten the essential need for flexibility of assessment criteria, according to the varying circumstances of the consumer’s credit or lease application.

The necessity to protect the public's right to access finance could emerge as an issue from the consultation process associated with the suggested approach in Consultation Paper 309.

The Finance Industry Delegation reminds ASIC that the non-ADI, small and medium amount lending sector and the lessors amongst its supporters, were not included in the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry’s Terms of Reference or official explanations of those Terms of Reference. Further, witnesses from those sectors were not called before the Commission. Consequently, a Commission report focussing on the banks cannot be automatically applied to those sectors in an attempt to create a one-size-fits-all ASIC regulatory regime.

Despite the disclaimer that appears at the front of every ASIC Regulatory Guide, indicating that it is <u>not</u> legal advice, it is the Delegation's view that this Disclaimer is somewhat overlooked by individual ASIC officers.

Further, the history of Consumer Advocate Legal Centre, Legal Aid, the majority of financial counsellors and the EDR schemes' reference to the pivotal RG 209, has been one of presuming that its content is effectively an extension of the Parliament's credit regulatory regime.

A challenge during the current consultation process could be to remind all stakeholders that it is the Commonwealth Parliament that sets the content of a regulatory regime. To ignore this fundamental is to precipitate future unnecessary Administrative Appeals Tribunal and Federal Court conflict.

Part A: Contextual Issues

There are a number of “contextual issues” that are of concern to the Finance Industry Delegation. With this in mind, we are pleased to note ASIC’s invitation on page 4 of Consultation Paper 309, “*to hear from you on any other issues you consider important*”. The Delegation considers that, while the specific answers provided in Part B of this response are important, the following will also make a contribution to ASIC’s stated intention that “*Your comments will help us develop our policy on responsible lending*”.

Concerning “What will happen next”

The opportunity for key stakeholders to speak to ASIC officers involved in the Regulatory Guide upgrading process at public hearings, in addition to providing written submissions, must not be overlooked. Since 2015, all reviews and inquiries impacting on some part of the Australian Credit Licence sector have been both inadequate and a sham.

The inclusive approach adopted by Treasury in regard to the NCCP Enhancements Bill, with the numerous Consultation Group meetings under the highly professional and constructive guidance and chairmanship of Mr Christian Mikula, in 2011 and 2012, should be the model adopted by ASIC on this occasion. Mr Mikula now works as a senior officer with ASIC.

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The inclusion of the 4 anticipated steps on page 5 of the Consultation Paper 309 is appreciated, but the Finance Industry Delegation is concerned that these be amended to include:

- Stage 3 - August-September 2019 - Response to submissions released, with ASIC responsible panel membership identified. Note, the opportunity for all stakeholders to read all the submissions should be considered critical to the necessary transparency that must be associated with the consultation process. There must not be any secret communications between ASIC and any particular stakeholder, or particular group of stakeholders. When ASIC conducts the appropriate all-stakeholder open forums or meetings, in order to promote a more effective and informed dialogue, those attending should be aware of the stated views of the other stakeholders <u>before</u> attending the forum or meeting.
- Stage 4 - September - October 2019 - Stakeholder consultation meetings, as occurred during the lead up to the current NCCP legislation - not closed meetings between one stakeholder, or a small group of stakeholders and the ASIC responsible panel. What is required is an open discussion forum where competing views can be aired and challenged by other stakeholders, with all participating or listening - i.e. not a secret dialogue between one stakeholder and the ASIC responsible panel.
- Stage 5 - December 2019 - release of draft Regulatory Guide 209, with invitation for further written submissions.
- Stage 6 - February 2020 - final version of Regulatory Guide 209 released.
- Stage 7 - March 2020 - ASIC conducted forums for Responsible Managers and Compliance Advisers in regard to the new Regulatory Guide.
- Stage 8 - July 2020 - commencement to allow the essential changes to application forms (including website reconstruction), assessment forms and the mandatory manuals, plus Responsible Manager and credit staff training required to accommodate the changes introduced into the Regulatory Guide.

The issue of "regulatory creep"

A fundamental foundation of the current consultation process must be to recognise what the Commonwealth Parliament has endorsed in the controlling Act, the National Consumer Credit Protection Act 2009 (NCCP) as the applicable regulatory regime in regard to the topics considered in CP 309.

It is useful to note how few and how simple the provisions are.

Section 130

"*Make reasonable inquiries about the consumer's requirements and objectives*".

"*Make reasonable inquiries about the consumer's financial situation*".

"*Take reasonable steps to verify the consumer's financial situation*".

Sections 118 and 131

"*The contract will be unsuitable... if it is likely that... the consumer will be unable to comply with the consumer's financial obligations*".

"*The contract will be unsuitable... if it is likely that... the consumer... could only comply with substantial hardship*".

"*It is likely that... the contract will not meet the consumer's requirements and objectives*".

(Concerning substantial hardship, Definitions) "*...if the consumer could only comply with the consumer's obligations under the contract by selling the consumer's principal place of residence*".

"*If the contract is a small amount credit contract... at the time of the assessment:*

(i) the consumer is a debtor under another small amount credit contract, and

(ii) the consumer is in default in payment of an amount under that other contract".

"*If the contract is a small amount credit contract... in the 90-day period before the time of the assessment, the consumer has been a debtor under two or more other small amount credit contracts*".

Section 120

"*Providing the consumer with a preliminary assessment*".

Section 132

"*Giving the consumer the assessment*".

"*…a written copy of the assessment*".

The proposals included in Consultation Paper 309 are not that simple.

"Reasonable"

Section 15AB of the Acts Interpretation Act 1901 (Cth) adopts the common law concept of determining that the meaning of words in an Act are those provided by "*the ordinary meaning conveyed by the text of the provision*" and with recognition of "*the desirability of persons being able to rely on the ordinary meaning conveyed by the text of the provision taking into account its context in the Act and the purpose or object underlying the Act*" and "*the need to avoid prolonging legal or other proceedings without compensatory advantage*".

What is "*reasonable*" has been determined at both common law and in statute to include:

- what a reasonable person would consider appropriate in all the relevant circumstances,
- in accordance with current community standards (including generally acceptable business standards),
- fair, proper and reasonably necessary, and
- adequate and sufficient.

See *Bankstown Foundry Pty Ltd v Braistina* (1986) 160 CLR 301, *McLelland v Symons* (1951) VLR 157, *Thorpe v south Australian National Football League* (1974) 10 SASR 17 and Part 11A, NSW Crimes Act.

The Finance Industry Delegation's concern is that, with the perceived shift to an ASIC prescribed series of tests, the opportunity for a lender or lessor, on a day to day basis continually dealing with all the circumstances and arguably exposed to contemporary community standards associated with the circumstances of lending and leasing, is to be deprived a role in the judgement as to what is reasonable - by an entity that has no experience in lending or leasing and no day to day contact with a broad cross section of the community.

If ASIC can identify any essential statutory power to support the creation of its Regulatory Guides, it becomes incumbent on ASIC to exercise that power reasonably and on reasonable grounds.

Assuming ASIC has the discretionary power to create Regulatory Guides and refer to them in its policing role, ASIC must avoid exercising that power in a manner whereby no reasonable decision-maker could have so exercised the power.

The Finance Industry Delegation contends that adopting a prescriptive approach to developing the content of the new Regulatory Guide 209, apparently based on the declarations in the current paragraphs RG 209.12 and RG 209.14, without the so far absent careful and precise clarification of the three vague and highly subjective terms in paragraph RG 209.12, is an abuse of power.

The subjective terms, "*prudent lending and leasing*", "*irresponsible lending and leasing*" and "*undesirable market practices*" are of concern. Absent a precise clarification, the inclusion of these three terms in the current Regulatory Guide 209 does not provide any objective standard of reasonableness, so that grounds for the recognition of facts, for coming to a decision concerning compliance, cannot be assessed as reasonable or unreasonable (See *George v Rockett* (1990) 170 CLR 104 and *Minister for Immigration and Citizenship v Li* (2013) 249 CLR 332).

Without the inclusion of precise clarification of the three vague and highly subjective terms, the issue of "Wednesbury unreasonableness" also emerges. The Finance Industry Delegation asserts that avoiding such precise clarification, in circumstances of possible expensive and traumatic ASIC audit and serious prosecution - with the subsequent business destroying legal costs and outcomes - opens the door to irrational, perverse, arbitrary, capricious and absurd decision making by ASIC (See *Associated Provincial Picture Houses v Wednesbury Corp* 1948] 1 KB 223, *Prasad v Minister for Immigration and Ethnic Affairs* (1985) 6 FCR 155, *Council of Civil Service Unions v Minister for the Civil Service* [1985] AC 374 and the Australian Administrative Decisions (Judicial Review) Act 1977, Sections 5 and 6).

The Finance Industry Delegation contends that ASIC faces an important challenge in regard to this very serious issue. In the new version of Regulatory Guide 209, either precise clarification of the three terms is included, or the terms must be omitted.

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The title "Regulatory Guide"

The concerns expressed in this response regarding the content of Consultation Paper 309 have also to be considered in the light of the expressions ASIC are already using in the current version (November 2014) of Regulatory Guide 209.

On the one hand, there is support for the notion of discretion and lender or lessor final decision in the content of their assessment policies.

Twice on the front page the document is referred to as a "*guide*".

On the following page, the "*Disclaimer*" reads - "*This guide does not constitute legal advice. We encourage you to seek your own professional advice to find out how the credit legislation and other applicable laws applies to you, as it is your responsibility to determine your obligations*".

This theme is continued in paragraph RG 209.8 which, in part, states "*...different business models, product types and differences in the services provided may mean different or additional steps are required to ensure compliance with the responsible lending obligations...*".

The theme is reinforced in paragraphs RG 209.19 to 209.22 and Table 3, which currently emphasise that the lender or lessor has the opportunity to consider scalability in regard to reasonable inquiries and verification "*depending on the circumstances*".

However, there is an apparent contradiction in paragraph RG 209.14, which provides a potential limitation to this implied Australian Credit Licensee discretion - "*This guide sets out our expectations for compliance with the responsible lending obligations, including the kind of conduct we will expect from you*".

The existing RG 209.14 continues with an inclusion that provides ASIC not only with a relatively objective test, but also 3 wide discretions or reference to discretions.

The paragraph commences with "*We will administer the responsible lending obligations to reduce the risk of consumers being offered credit contracts or consumer leases that they cannot afford to repay...*". This being the relatively objective test that simple arithmetic can help determine and which requires clarity as to what must be included in the calculations. This is achievable and has largely been achieved. The current Regulatory Guide 209 is reasonably clear and the Finance Industry Delegation is suggesting amendments in this response which will make it even clearer.

The Finance Industry Delegation has no issue with this test. It is fundamental to the consumer credit protection regime introduced by the National Consumer Credit Protection Act. It can be measured by examining the lenders and lessors' default rates and loan/lease write-off rates - actual, trends, and with industry comparison. Astute and effective compliance reviewers or auditors are already using this examination.

Unfortunately, as partly indicated earlier, the existing paragraph then continues, "*....or that are otherwise unsuitable for the consumer, and to promote the objectives set out in RG 209.12*" (RG 209.12 includes objectives "*encourage prudent lending and leasing*", "*impose sanctions in relation to irresponsible lending and leasing*" and "*curtail undesirable market practices*").

In other words, the industry sector is offered a reasonable certainty test - affordability - and then three platitudes in paragraph RG 209.12, presented as further tests that provide anything <u>but</u> certainty. If this phrase is to be continued to be used in the new version of Regulatory Guide 209 and ASIC plans to continue to use the phrase to justify its regulatory activities, then ASIC must clearly address these three tests. The problem for ASIC in accepting this challenge is that ASIC then strays into territory which it is <u>not</u> Constitutionally mandated to do - it creates regulation, it improperly creates "the law".

The Delegation notes that, in the box entitled "*About ASIC regulatory documents*" on page 2 of the Consultation Paper, in regard to regulatory guides, ASIC notes that these "*give guidance to regulated entities by:...* (dot point 2) *explaining how ASIC interprets the law*". It is critical to note that the wording does not present a message concerning ASIC "making" the law.

However, the Delegation is concerned about the implied contradiction to this message included at paragraph 93, under the subheading "*Regulatory and financial impact*" - "*Without an approved RIS, ASIC is unable to give relief or make any form of regulation, including issuing a regulatory guide that contains regulation*". The Delegation contends that the wording of paragraph 93 is totally inappropriate and expresses an ultra vires power being ascribed to ASIC.

It is the Finance Industry Delegation's view that the approach presented by ASIC in Consultation Paper 309 is focused on not providing any discretion for lenders and lessors and ignoring the

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actual and implied promises of the current first two pages and current RG 209.8, 209.19 and 209.22 content.

Significantly, there is no consideration of scalability. This focus appears to have its foundation provided by the current paragraph RG 209.14 and second part of paragraph RG 209.12 and seeks to demonstrate ASIC taking an illegitimate regulation creating role.

In regard to making reasonable inquiries, the current paragraph RG 209.18 expresses the responsibility on licensees as it should be - "*(b) make reasonable inquiries about the consumer's financial situation (i.e. to determine whether the consumer has the capacity to meet their payment obligations under the credit contract or consumer lease being considered)*". The Delegation contends that any addition of considering other possible undefined elements of "*suitability*" simply imports impossible levels of subjectivity for an ASIC investigator to exploit who might be seeking Key Performance Indicator (KPI) numbers and creates fundamental uncertainty for the industry sector.

The Administrative Appeals Tribunal could become a very busy place.

Federal Court ignored in two ways

The function of the Federal Court is ignored.

It is for this court to clarify what the legislation says or means, and therefore introduce certainty - not ASIC.

First there is the issue of ASIC's proposed new Regulatory Guide 209 misrepresenting the situation. ASIC could develop a list of (say) 29 criteria which would encourage the Australian Credit Licensee to assume that it covered the field. However, the Federal Court remains free to recognise only some of ASIC's criteria and to add others.

A move by ASIC to a rigid prescribed regime also defies the celebrated *ASIC v The Cash Store (in liquidation)* [2014] FCA 926 case, where Justice Davis was very clearly against recognising a "set in concrete" approach.

Included in her judgement were the following statements:

"*…a sufficient understanding of the person's income and expenditure*".

"*The extent to which additional information and further inquiries may be needed… will be a matter of degree in each particular case*".

The Finance Industry Delegation reminds ASIC of their self admitted role as "*administrators of the law*" and that the law that ASIC administers comes from the Commonwealth Parliament and the courts - just like the one presided over by Justice Davis - and there should never be an extra-Constitutional attempt, under the Australian Constitution, to add Regulatory Guides as a source of that law.

ASIC can never achieve ASIC Commissioner Sean Hughes' statement, included in the ASIC media release of 14 February 2019 concerning the consultation - "*ASIC wants to ensure its guidance provides industry with certainty…*".

Only far better drafted legislation, via now essential amendments to the National Consumer Credit Protection Act, and a series of Federal Court cases, can contribute to this objective.

ASIC's efforts should be directed to encouraging the Government to facilitate a considerable editing and updating of the National Consumer Credit Protection Act after a proper review - not like the sham 2015/16 Panel Review into SACCs and leases, or the 2018/19 Senate Economics Reference Committee disgrace - not in attempting a misguided and unconstitutional "solution" via a Regulatory Guide re-write.

To this end, the Delegation further reminds ASIC of an inclusion in the current Regulatory Guide 209 at paragraph RG 209.97. After ASIC rightfully refuses to give a definitive definition of "*substantial hardship*", in that paragraph ASIC states, "*The law about the meaning of 'substantial hardship' will develop and become clearer as cases come before the courts and judgements are handed down*".

Explanatory Memorandum <u>does not</u> demand a prescriptive approach

The Explanatory Memorandum provided in 2008 by the then Minister for Financial Services, Superannuation and Corporate Law, the Hon Chris Bowen, in paragraphs 3.69 and 3.139, and quoted in a Note to the current paragraph RG 209.95, does not demand absolutes.

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"*The purpose for undertaking reasonable inquiries about the consumer's financial situation is to ascertain a reasonable understanding of the consumer's ability to meet all the repayments, fees, charges and transaction costs of complying with the proposed credit contract*".

This is supplemented by earlier provisions that clearly recognise the Australian Credit Licensee as having flexibility or discretion.

In 2.105 - "*These obligations are principle-based and it is intended that licensees can be flexible in adopting practices that suit their organisation*".

In 2.107 - "*It is expressly provided that compliance with the obligations in paragraphs 47(1)(b), (g), (k) and (l) is to be determined according to the nature, scale and complexity of the credit activities engaged in by the licensee*".

In 2.108 - The reference to "*nature scale and complexity*" enable the licensee to tailor the way in which they comply with the obligations, taking into account factors such as:

- the types of credit activities in which the licensee engages;
- the diversity and structure of the licensee's operations (including the geographic spread of the operation and the extent to which the licensee out sources any of its functions);
- the volume and size of the transactions for which the licensee is responsible; and
- the number of people in the licensee's organisation.

The Explanatory Memorandum also addressed the issue of inquiries and what would be adequate. Again, the fundamental decision was left to the licensee at the coal face.

Paragraph 3.71 clearly prescribes that "*The significance* (and presumably extent) *of these inquiries will be dependent on circumstances*" of the particular loan or lease application and, as an example, used the difference between the expenses or cost impact of a mobile phone for a low income earner and a high net worth individual.

In this context it is important to note that Section 47(1)(k) of the National Consumer Credit Protection Act states, "(A licensee must) *...have adequate arrangements and systems to ensure compliance with its obligations under this section...*" and, as one of those obligations, the section includes "*(d) comply with the credit legislation*".

If ASIC now disagrees with a principle-based approach, change cannot be achieved by ASIC re-writing its Regulatory Guides. It is only the Australian Constitutional right of the Parliament to affect a non-principle based approach.

The one responsible ALP Minister and the 5 responsible Coalition Ministers, since Minister Bowen, have never sought to change this interpretation or this content of the National Consumer Credit Protection Act.

That means, in the drafting of the new version of Regulatory Guide 209, ASIC must recognise the intentions of the relevant Minister and the content of the credit legislation that provides for the licensee to tailor their assessment response (licensee flexibility) according to the nature, scale and complexity of their credit activities (three opportunities to underwrite the flexibility chosen) - to arrive at a reasonable understanding of the ability of the consumer to be able to repay their loan (not an absolute and infallible decision).

Again, the central issue is affordability, with the licensee determining the reasonable criteria for assessment. In a commercial context - if they don't get it right, they will face insolvency.

The "appropriate balance" - essential flexibility foregone

A consideration of page 33, "*E Regulatory and financial impact*" prompts two comments:

1. Paragraph 91(a), concerning ASIC's stated interest in "*helping licensees to understand what is required to comply with their responsible lending obligations*", considering the consultation paper as a whole - is potentially achieved with the prescriptive intentions revealed.
2. Paragraph 91(b), concerning "*ensuring licensees can continue to tailor their responsible lending processes in a way that is appropriate for their business and consumers*" is not achieved.

   Rather, if the ASIC proposals proceed as indicated in the Consultation Paper, this opportunity will be very, very substantially eroded. Any flexibility in the current regime will be replaced by a rigid ASIC compliance assessment checklist regime.

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ASIC's role

The Explanatory Memorandum distributed by Minister Chris Bowen in 2008 made it clear that ASIC does not have a regulation initiative role.

The reference to ASIC powers is always in terms of regulator and administrator, e.g. under the sub-heading "*Outline*" on page 3, "*the key components of the proposed national credit regime, which include:*

- *a comprehensive licensing regime... to be administered by the Australian Securities and Investments Commission (ASIC) as the sole regulator...*".

This description of ASIC's role is endorsed in the National Consumer Credit Protection Act, with the inclusion and content of Chapter 5, "*Administration*" and Chapter 6, "*Compliance and enforcement*" - both clearly ascribing a central role to ASIC, according to the title of the chapter. It is noted that there is no chapter entitled "Regulation", ascribing a creative role to ASIC associated with the activity indicated in the title.

Chapter 7 of the NCCP Act - Miscellaneous, Division 4 - Regulations, includes a reminder that it is the Minister (with the convention of reference to the Governor General) that initiates/makes regulations.

Section 329 of the NCCP Act states, "*The Governor General may make regulations prescribing matters*

(a) required or permitted by this Act to be prescribed; or

(b) necessary or convenient to be prescribed for carrying out or giving effect to this Act".

Schedule 1 (National Credit Code), Part 14, Division 4, provides an opportunity for ASIC to make a statutory instrument, but both Sections 214 and 215 limit this power to matters only authorised by the Code.

The Finance Industry Delegation notes that the statutory foundations for ASIC's Regulatory Guide 209 are not included the Code - but in the main body of the National Consumer Credit Protection Act - where such authorisation is also excluded.

For emphasis - neither the regulation creation power, nor the statutory instrument power, can be exploited by ASIC to create new regulation in regard to matters prescribed by the Act. Further, the ASIC Regulatory Guides are neither regulations under the Act, nor statutory instruments.

The content of the proposed new version of Regulatory Guide 209 must directly reflect what the Act prescribes and what the Minister declared in his Explanatory Memorandum, because Parliamentary approval is limited to those two documents and neither the Commonwealth Constitution, nor the Act, provides ASIC with the power to create regulations.

To do otherwise is to contradict a document published by ASIC in February 2010 - "*Regulation Impact Statement, ASIC implementation of the credit legislation: Responsible lending conduct*". Paragraph 7 of this document states, "*Regulation of consumer credit in the new regime will be the responsibility of ASIC. A key component of the new credit regime is that businesses that provide credit services... will be required to be licensed and meet a range of 'responsible lending obligations' set out in Ch 3 of the National Credit Act*".

Neither in this paragraph, nor in any other paragraph in this document, is there any mention of an ASIC Regulatory Guide being involved in presenting these *'responsible lending obligations'*. The Delegation also repeats its concern that ASIC has improperly assumed a power of "*regulation of consumer credit*", as expressed in this statement.

Significantly, under the subheading "*Problems*" at paragraph 31, the document states "*The Act imposes a high-level principle-Based obligation, but does not provide any specific guidance as to how the responsible lending obligations should be met*". This is followed by comment in paragraph 34, "*The lack of standards or guidance as to what assessment should be undertaken by credit licensees means that a variety of different and potentially inconsistent approaches could be undertaken across the industry in order to comply with the requirement*".

After comment on potential confusion and difficulty for consumers to adequately compare offerings, ASIC concluded with a statement in paragraph 36 that supports the Finance Industry Delegation's view that it is not for ASIC to address this perceived difficulty with its Regulatory Guide 209 - "*Government intervention to clarify the requirements under the law could address this potential problem*".

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Unfortunately, ASIC then contradicted this recommendation and proposed an Option 2 - assuming no proper Government intervention via the Parliamentary process, but for ASIC to provide *'indicative guidance to credit licensees on responsible lending obligations'*.

In paragraph 51, below the sub-heading "*Description of option*", ASIC clarified its position regarding offering indicative guidance, i.e. regulatory guides, as "*Under this option, we would not impose any set minimum requirements, but instead provide indicative guidance on our expectations about what credit licensees should do in order to comply with the responsible lending obligations under Ch 3 of the National Credit Act*".

The Finance Industry Delegation asserts that ASIC's Regulatory Guides do not work this way. Consumer advocate legal centres, Legal Aid offices, financial counsellors and individual ASIC officers consistently present that the requirements included in the Regulatory Guides are the minimum legal requirements and they are not *'guidance on …expectations'*, but the equivalent of regulations made by the Minister. Paragraphs 36 and 93, discussed above, have now to be revisited.

Concerning an overall issue

A review of the entire content of the Consultation Paper 309 could lead to a view that, fundamentally, its design is not prompted by any central or appropriate intention of promoting benefit for any stakeholder in the credit creation and receipt process. but rather to serve as a foundation for exploring the opportunity to be far more prescriptive in the content of Regulatory Guide 209, in order to facilitate an easier "tick the check box" approach to enforcement.

This in order to generate the ASIC KPI numbers necessary to satisfy re-elected political masters and offer a response to the criticisms received by ASIC during the conduct of the Royal Commission into Banking. In fairness to ASIC, the Finance Industry Delegation reserves its decision on this issue until the final version of the new Regulatory Guide 209 is published.

To this end, the Finance Industry Delegation is particularly concerned with an article appearing in the Law Society of NSW's "Monday Briefs" e-journal, dated 20 May 2019, which comments on a change of culture and a change in enforcement policy within ASIC.

Dealing with the Australian Financial Complaints Authority

On the presumption that ASIC considers that any amendments to Regulatory Guide 209 will add to certainty for all stakeholders, it will be beholden on ASIC, in its supervision and control of AFCA, to ensure that AFCA does not attempt to entrench and extend its "shadow regulatory" role with supplementary "Rules" that add to, or conflict with, the new Regulatory Guide 209.

At present lenders serve 2 regulatory masters - ASIC and AFCA - and the Finance Industry Delegation is not convinced that this was the intention of the Commonwealth Parliament.

PART B - List of proposals and questions - Finance Industry Delegation response to ASIC's questions

PROPOSAL B1 - identifying particular enquiries and verification steps

We are considering whether to identify particular inquiries and verification steps in RG 209 that we think would generally be reasonable to provide greater certainty to licensees about complying with their obligations.

General Comments:

The Finance Industry Delegation offers six general comments in response to ASIC's introductory statement.

1. Abandoning scalability

   The challenge is to avoid a simplistic, one size fits all, approach. Such an approach is fixated by process rigidity.

   This general tenure of the Consultation Paper 309 effectively means abandoning the scaleable approach and adopting a prescriptive approach. Yet ASIC has never comprehensively addressed this issue across the whole range of credit providers.

   Such an approach would also mean abandoning 2 other current paragraphs:

   RG 209.25 - "*This means that what amounts to a 'reasonable level of inquiries' and taking ' reasonable steps to verify' can differ, depending on the type of services and products you provide to consumers*".

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RG 209.39 - "*Your processes should be flexible and allow for additional inquiries to be made as needed*".

2. Imposed uniformity must be questioned

   Three questions have to be addressed:

   (a) Why demand exactly the same assessment processes for a loan of $200 for 4 weeks and a loan of $100,000 for 5 years?

   (b) How do you justify demanding the same time investment and labour on-costs for an unsecured loan that may gross $48 in permitted fees, and a loan that may gross approximately $145,000 in annual cost rate income?

   (c) The "Rationale" on page 9 includes mention of "*imposing minimum requirements*". How close do the proposals come to actually imposing not minimum - but maximum - possible requirements and totally abandoning any continuing opportunity for licensees to "*tailor their responsible lending processes*"?

3. Commercial realities ignored

   The thinking behind this approach continues to overlook the major commercial incentive for credit providers to take some care with their assessments - they lose money if they do not.

4. Suggestion as to what might be included vs. prescription - rigidity

   The Delegation's concern is this prescription builds in rigidity. What is listed becomes the de facto law. What is excluded, despite its utility for some or a particular credit provider, is considered invalid to include in the assessment process.

5. The ultimate most reliable tests of adequate inquiry and verification continue to be ignored

   The ultimate suitability/not suitable tests - the comparative default rates and the write-off rates continue to be ignored. The higher these are, the more likely the credit provider is <u>not</u> undertaking an appropriate level of assessment due diligence. The lower these are, the more successful and compliant the credit provider has been in undertaking the assessment process - regardless of what tactics and content have been adopted and the more compliant the credit provider is with the objectives of the National Consumer Credit Protection Act in regard to assessments. However, it should not be overlooked that defaults and write-offs will generally be higher with small amount credit contracts than larger loans, because of the largely different clientele and the fact that the consequences of a default or write-off, in the overall circumstances, is likely to be considerably less than if a consumer defaults on a much larger loan.

6. Concerning the proposed new basis of verifying information

   Paragraphs 20 to 23 refer to what ASIC considers reasonable steps in the verification of information and that they will "*change over time*". The Finance Industry Delegation has a number of concerns in this regard, including:

   (a) With ASIC's demand for credit providers to adopt new technology, this would mean credit providers facing greater compliance expense.

   (b) The encouragement of adoption may end up being predicated on ASIC expecting all available means of collection verification be used. This could introduce redundant steps, along with greater and unnecessary expense.

   (c) The danger that a new method will be presumed to automatically invalidate an old, successful method, especially if the new method simply adds functionality that is superfluous to the credit provider's needs.

B1Q1

Would it be useful for licensees if ASIC were to identify the inquiries and verification steps that we consider should be taken? Why or why not?

Answer:

A suggestion as to the range of steps that might be considered, not excluding others, is appropriate.

It presupposes a lending knowledge that ASIC does not have, to ascribe a role to ASIC of setting definitive, all inclusive, steps.

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Such a move imposes a rigidity of semi-permanence until the next review in (historically) 10 eventful years time, and an opportunity to find a credit provider non-compliant simply because a step that ASIC - with their lending inexperience - believe is warranted, is excluded from the credit provider's assessment menu.

The Delegation does not consider that identifying the inquiries and verification steps will necessarily offer "certainty" - as it is always subject to ASIC interpretation being different to credit providers' interpretation, because 'general' as supposed to 'very specific' words have to be largely adopted. This introduces the opportunity for subjectivity. The varying real life circumstances should outweigh the adverse issues associated with an unrealistic attempt to lock in a prescriptive approach. Such an approach demanding attention to steps that, in a particular case or particular class of cases, have been found to be unnecessary by the credit provider.

Finally, being prescriptive introduces the real danger of judging the credit provider on the list of steps - a simple yes/no exercise, regardless of the outcome of the assessment in terms of loan repayment performance - when the really important issue is what the result was of the credit provider's assessment. Also, not forgetting to ask - in the case of an adverse result - were there any other factors not revealed by the applicant and not easily otherwise discovered by the credit provider, or occurring after the assessment, that contributed to the adverse outcome?

B1Q2 - industry practice

If there are particular examples of industry practice that you consider should be reflected in any guidance, please provide details of those practices.

Answer:

As one of the range to consider, NOT mandatory prescription - third party bank statement analysis/reports.

B1Q3 - fewer steps

Are there any kinds of credit products, consumers or circumstances for which you consider it may be reasonable to undertake fewer inquiries and verification steps? Please identify the kinds of products, consumers and circumstances and particular features you think are relevant.

Answer:

In circumstances where the applicant/consumer has a long history of association with the credit provider and the credit provider has a substantial consumer file or history to which to refer.

This is barely mentioned in the current Regulatory Guide 209, but is a very significant point. These applicants resent the intrusion of yet another substantial assessment when they are already well known to the credit provider. This issue amplifies with the smaller the amount borrowed, the shorter the proposed loan term and the shorter the period between the last successfully repaid loan and the new application.

B1Q4

In your view, what aspects of the consumer's financial situation would a licensee need to inquire about in all circumstances? If you think some aspects of the consumer's financial situation do not need to be inquired about, please explain why.

Answer:

Inquiry in all circumstances - income and continuity of source.

Please note - continuity can be assessed from history, income documentation and a consideration of possible changes. It need not involve embarrassing contact with an applicant's employer, who is highly restricted in what they can tell anyway.

Aspects not necessarily needing inquiry are highly dependant on the individual consumer's circumstances and type and purpose of loan required.

That is why a suggested menu of assessment criteria - and not a prescriptive list - is very important.

B1Q5

In your view, what aspects of the consumer's financial situation would a licensee need to verify in all circumstances? If you think some aspects of the consumer's financial situation do not need to be verified, please explain why.

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Answer:

Verification in all the circumstances - income and continuity of source (as above, without embarrassing contact with the applicant's employer being mandated).

Aspects not necessary to include in the inquiry - again these are highly dependant on the individual consumer's circumstances and type and purpose of loan required.

Just as a prescriptive approach as to what to include is inappropriate, so is a prescriptive approach as to what not to include.

B1Q6

What would be the effect on consumers of ASIC identifying particular inquiries and verification steps? For example, what would be the effect on access to and cost of credit for consumers?

Answer:

Any expansion of expected steps means more staff time and a more expensive application process. Credit providers would be less enthusiastic about providing credit, for fear of being caught with a breach of the new and extended ASIC requirements.

While the cost of credit is price controlled under the National Credit Code, the result is no cost recovery opportunity for the proposed new impost. This means numerous credit providers will exit the market because it is no longer profitable under the new cost impost, there will be less competition and the possibility of less credit in the market being available for consumers.

In addition, the proposed impost will skew the supply of credit toward larger and longer loans that generate high gross profits for the same amount of assessment, i.e. a reduction in smaller amount loans being available - while encouraging greater consumer indebtedness, in a country that already has horrific household debt rates.

Further, in a market where consumers place much weight on fast approval times - the proposals for an increased menu of assessment criteria would blow out approval times in a way that would not be welcomed by the consumers.

Why should this matter to ASIC?

Should the re-elected Parliament proceed to pass any SACC lending and lease amendments Act, it will provide one more opportunity for the illegal lenders to move into the market and establish an even stronger presence than they have now. This will be particularly so after the hundreds of thousands of applications have flooded into the Good Shepherd organisation, which will continue to lack the capacity to assess such a volume, nor lend to the proportion of applications that would deserve approval, nor provide loans at the speed which consumers expect from the commercial sector.

B1Q7

What would be the effect on business costs of ASIC identifying particular inquiries and verification steps? Please provide details of the effect on compliance costs for the licensee, and any factors that are likely to affect the level of cost or cost savings.

Answer:

ASIC is proposing an expansion of the assessment requirements deemed acceptable.

That means:

- extra time taken with assessments by staff and supervising responsible managers; and
- the possibility of lenders, with staff and management already working at near or at full capacity, having to hire extra staff.

The Finance Industry Delegation conducted a survey of supporters in preparation for this response. In all cases, on average, the cost contribution (net of on-costs) can be measured at $6.13 for the extra ten minutes for credit assessors and $7.01 for the extra 10 minutes for responsible managers, to satisfy consideration of the extra "steps". For emphasis, that means the credit assessors' figure must be added to each loan and between 40 - 60% of the responsible managers´ figure must be added to each loan.

In addition, there will be:

- a minimum of 3 hours initial and refresher training involved per credit assessor and responsible manager, at $110.40 and $147.30 respectively for the 3 hours for wages; plus

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- the cost of an external trainer for the introductory session, at least $1,200; plus
- the cost of modifications to websites, checklists, application and assessment forms and manuals, averages $23,250 per Delegation supporter, with a range of $2,500 for a husband and wife business, to $100,000 for a multi-outlet and internet business. Businesses that were larger than 3 people presented figures of $16,000 or more. A major industry supplier, with substantial IT background, estimated that all of their many clients would have to invest $10,000 - $40,000. Significantly they estimated that the changes would take a minimum of four months and probably six months to introduce.

All of this cost increase without any opportunity to charge the consumer any more under the current price control regime. There will be no costs savings.

There will be little chance of increasing profitability due to lowering default and write-off rates, because each Delegation supporter already applies the critical assessment menu items and no material improvement is expected from adding to the number of items already used to enquire and verify.

In this context, it would be unwise for ASIC to continue to assume that access to consumer data created by new technologies will be as easy to access for non-bank, and particularly smaller lenders - as ASIC presumes in its Discussion Paper 309, e.g. at pages 12 and 14.

It must also be remembered that the licensee, in the absence of engaging a private detective to watch the consumer's spending habits for an extended period, or having any consumer capable of getting and keeping all their expenditure receipts, will always be considerably reliant on the honesty and accuracy of the consumer applicant.

B1Q8 - effect on competition

In your view, what would be the effect (either positive or negative) on competition between licensees? Please provide details.

Answer:

There will be no positive contribution. With the increased compliance costs involved, a number of marginally profitable credit providers will be forced out of the market. That means less competition by number of credit providers. The irony is that this approach by ASIC will reward two or three of the infamously non-compliant larger companies, with more market share.

On the assumption that ASIC effectively and uniformly enforces the new regime, all lenders will face similar compliance cost increases and no change in the competition mix, on the basis of cost savings, will materialise.

Also, chasing gross profitability with the same compliance costs for all loans, whether the loan is big or small, companies will be forced to move to offering larger and longer loans, further reducing competition in the small and medium loan sector.

PROPOSAL C1 - kinds of information

We propose to amend the current guidance in RG 209 on forms of verification to:

(a) clarify our guidance on kinds of information that could be used for verification of the consumer's financial situation, and provide a list of forms of verification that we consider is readily available in common circumstances; and

General comment:

The phrase "that could be used" is noted. If that implies a list from which the credit provider may select and a list that does not exclude other opportunities, the Delegation would approve for reasons outlined above. The Delegation would be most concerned if the approach was to impose a mandatory list, again for reasons discussed above.

Please do not leave it for ASIC "to consider" what is or is not readily available. Ready availability on the basis of both cost and access must not be presumed.

Please do not assume "common circumstances" - circumstances are considerably varied across the market. For example, Credit Corp can access information at very reduced cost because it simultaneously runs debt collection, credit repair and lending divisions while many small non-listed companies are pure lenders. Cash Converters and Nimble, with large company buying muscle can purchase bank statement analysis in quantity far cheaper than smaller companies. If ASIC fails to consider this issue - it will contradict the promises of the 3 major politic parties in the run up to the 2019 Federal Election to promote and safeguard small business.

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(b) *clearly state that views on what are 'reasonable steps' will change over time, as different forms or sources of verifying information become available. For example, developments in open banking and data aggregation services will assist licensees to efficiently confirm the financial situation of a consumer (including allowing simultaneous inquiry about and verification of some information).*

ASIC recognition that what are "*reasonable steps*" will change over time is critical.

That absolutely supports the Delegation's argument that any attempt by ASIC to list inquiries and verification criteria must be indicative - and not a rigid imposed list.

Further, at present it is most unwise to presume that "*open banking*" will provide material opportunities for enhanced assessment of non-bank loans. The complexities of consumer permission for access to information and the brutal bank protection of their market and dominant position makes this of marginal utility - if any.

Aggregation of information is much overrated. There is little to be gained by a small or medium amount lender that cannot already be achieved by a careful bank statement analysis by the credit assessor, with or without the supplement of a third party bank statement analysis report - particularly given the cost. ASIC must be careful not to be fooled by the "buzz word" users.

C1Q1

Please provide details of any particular types of information that you consider should be reflected in the guidance as being appropriate and readily available forms of verification?

Answer:

Already included on all credit providers' assessment menus:

- Centrelink income statements, and
- 90 days bank statements (all size loans), with possible supplementation from third party bank statement analysis reports.

A considerable number of Finance Industry Delegation supporters automatically include the following and, where others consider it is important to supplement bank statement information in regard to a particular consumer application, they include:

- pay slips,
- statements of employment,
- utility bills, and
- rent/mortgage documentation.

The issue is not increasing the list, but making sure every credit assessor pays careful attention to the information they already have generally available to consider.

Any other source of information for inquiry and verification, beyond the applicant interview, tends to be very peripheral and rarely of much use.

While fraud is an issue discussed later in this response, in the context of inquiries and verification, ASIC should not overlook the fact that electronic bank statements are now almost the only documentation that does not suffer the risk of unauthorised and dishonest tampering. Such is the level of falsifying pay slips, statements of employment and utility bills, that licensees are reporting constant fraudulent attempts by consumers.

C1Q2 - examples

Do you consider that the examples included in Appendix 1 are appropriate? Why or why not?

Answer:

They are a very mixed bag.

1. Confirmation of employment from an employer raises some applicant/consumer issues.

   This information is not necessarily "*readily available from the consumer*" and many consumers do not want to reveal their personal financial situation and decisions to their employer. This should only be considered as a possible option, subject to consumer approval, particularly as the basic information is also clearly available from the bank statements.

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2. Requests for recent income tax returns again must only be seen as an option, not a prerequisite. Many consumers seeking smaller loans consider such a request as an intrusion. In the market place it is considered appropriate for housing finance, but little else.

3. Any consideration of credit reports must recognise the anti-competitive nature of listing <u>all</u> enquiries for credit. This inhibits a borrower from undertaking a comparative analysis of what is on offer. Further, the age of dependants is not listed - something that can be critical to recognising actual costs.

   In addition, you already have the total unreliability of credit reports, due to the uncontrolled blackmail action of "credit repair" companies and consumer advocates - constantly using the cost of Australian Financial Complaints Authority investigations to force lenders to apply to take details off the consumer's file. The Finance Industry Delegation understands one senior ASIC officer was particularly concerned about this issue and sought information from the industry sector but, unfortunately, ASIC does not appears to have taken any action to address this issue.

   Also, a growing number of lenders are no longer providing information to credit reporting agencies due to the complexities of the Privacy Act-induced bad credit listing regime - a 6 month process to have an adverse listing completed is something exploited by many amoral borrowers.

   An issue of concern with the use of credit reporting agencies is that the number of enquiries made by a consumer are recorded and impact on the credit scores calculated for that consumer. This introduces a bias. The number of enquiries may simply reflect a consumer diligently comparing credit provider offerings for the one loan occasion and not multiple loan occasions, yet their credit score can then work against them.

4. It is nonsense to assume that, as a matter of course, other non-bank lenders are going to share information collected at their cost. This information is not readily available to the consumer or anyone else.

   While the inclusions under the subheading "*Living expenses - Sources of information*" are generally appropriate and identifiable, except for child care, the assumption that information concerning all categories "*is readily available*" is totally inaccurate. The average employed consumer, or consumers on a pension, do not keep financial documentation and are far from accurate as to the detail of their expenditure on living expenses.

   However, they can generally indicate, with some accuracy, what is left for discretionary expenditure after all their expenses are deducted from their income.

   To claim that "*Consumers are generally likely to maintain separate records of these kinds of expenses*" (fixed or recurring) is ludicrous. To claim "*some consumers may not maintain separate records of these kinds of expenses*" (variable) is also nonsense - "*some consumers may not*" should be replaced with "*almost <u>none</u> of the consumers maintains separate records of these kinds of expenses*".

5. In regard to the "*Overall financial situation*" and the listing of bank statements - this is an appropriate inclusion and the 90 day rule applicable to SACC lending could be extended in the new Regulatory Guide 209 to cover all borrowing. This would simply recognise an almost universal industry practice and create a level playing field. However, it is important to note that the prescription must be access to electronic bank statements, to avoid consumer's being fraudulent.

6. Mention of "*open banking*" as a possible improvement of obtaining information by credit providers in the non-bank sector, is to be overly optimistic and ASIC policy should not be based on any presumption that there will be any material benefit available for non-ADI lenders associated with the introduction of open banking.

7. Concerning data aggregation reports - those known to the writers and used by Finance Industry Delegation supporters are limited to analysing bank statements - not "*a broader range of accounts*". They are convenient and a double check mechanism, but can never totally replace the credit assessor undertaking a personal examination of bank statements.

   Any consideration of "new" and alternative sources of information must recognise the second part of the current paragraph RG 209.46 - *"...what amounts to reasonable verification will depend on the information and resources that you have access to and the facts and circumstances of each case*". In short, ASIC should not presume that all licensees have

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equal access to a particular source of information, nor that licensees all have the same resources.
To adopt such a presumption would be in conflict with all major political parties' support of small and medium business and would add further weight to the view that ASIC favours "*the big end of town*".

C1Q3 - data aggregation

Are there particular issues with using data aggregation services that you consider should be raised in our guidance? Please provide details of those issues, and information that you consider should be included in our guidance. For example, would it be useful to include specific guidance on matters the licensee could, or should, raise with the consumer before obtaining the consumer's consent to use this kind of service?

Answer:

To the extent that a bank statement is a data aggregation service, the Finance Industry Delegation considers there are no difficulties except the challenge of identifying when more than one bank account includes income deposits and expenditure withdrawals. This means often relying on consumer honesty to identify those accounts.

Further, to maximise effectiveness during the term of the loan, if a consumer is faced with financial difficulties that were not in existence at the time of the assessment, there should be the opportunity to refresh or revisit the consumer's electronic bank statement. This should be considered essential in the case of a hardship application.

However, other data aggregation services are of concern to the Delegation, including those that will be associated with open banking. ASIC should not presume that they have a utility for the SACC, MACC or smaller amount AOCC consumer. The consumer profile for such data aggregation services largely will not match most of the Delegation supporters' consumer sub-categories.

In addition, open banking data aggregation services are flagged to attract special licensing and demanding consumer consent procedures, which will be neither cost nor time effective in regard to the smaller loans that are primarily offered by the Finance Industry Delegation's supporters.

In short, data utility may be very marginally useful - if at all - to Delegation supporters and there is a concern that the data aggregation services will be looking at information to a particular point of time, which may not correlate with the data of the assessment.

PROPOSAL C2

We propose to expand our guidance on what are reasonable steps to verify the financial situation of a consumer by:

(a) more clearly stating that it is not sufficient merely to obtain verifying information but not have regard to it, or to use a source of information to verify only one aspect of the consumer's financial situation if it contains other (potentially inconsistent) information about other aspects of the consumer's financial situation; and

Comment:

This policy is already universally accepted by Finance Industry Delegation supporters and a clearer explanation in the Regulatory Guide is not an issue for the Delegation.

(b) including an 'if not, why not?' approach - that is, if a licensee decides not to obtain or refer to forms of verifying information that are readily available, they should be able to explain why it was not reasonable to obtain or refer to those forms of verification in the circumstances of the particular consumer involved.

Comment:

This suggestion fails to recognise that not seeking further verification may not be an issue of any concern:

1. Often the information from one source is so clear that no further verification is required.
2. In this response and with lenders generally, there is a critical fact needed to be recognised - what ASIC thinks is information that is readily available may not actually be available in the non-ADI lending world.

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3. This fails to recognise that the real test is the repayment performance overall of the lender's loan book. That means ASIC should make a comparative analysis of this performance and, if it is wanting compared to the industry sector as a whole, then it is appropriate to seek explanation from the lender as to why they did not consider a particular verification step as a policy, in the case of the individual loan under scrutiny.
4. To introduce a policy of written explanation being required - "*if not, why not*" - is to add another time constraint during the assessment process that makes lending even less profitable - encouraging an exit from the industry sector and substantially reduced competition, plus a push to larger and longer loans, as discussed above.
5. The aim must be to create a useful assessment report - not a long and involved document.
6. It is also important that the focus is on the outcome of the assessment and not the particular processes adopted by the lender or lessor to achieve this outcome. Given the general aim of the credit legislation regime, it would be inappropriate for an ASIC officer to attempt to impose a penalty on a lender or lessor, simply because that licensee did not use a verification method that ASIC has chosen to include in its preferred list.

C2Q1

Do you consider that the proposed clarification of guidance on reasonable verification steps would be useful? Are there any other aspects of our guidance on verification that you consider would be useful?

Answer:

No, for the reasons listed under the "Proposal C2", immediately above. The Finance Industry Delegation is particularly concerned that "guidance" be limited to a menu of possibilities, not a mandated, compulsory list.

C2Q2

Would an 'if not, why not' approach encourage improvements to current verification practices? Why or why not?

Answer:

No. It would encourage defensive tokenism.

For many lenders it would be easier to pretend that the credit assessor had gone through the motions verifying the information, than having to write a defence piece that would undoubtedly be very closely analysed and picked to pieces.

A "*why or why not*" request for a written explanation demands a lengthy and comprehensive explanation every time, in a business environment where the consumer is demanding a decision quickly and every minute spent writing the document is a contribution to labour costs that cannot be recovered in the price controlled environment.

The credit assessors will know that lawyers at ASIC, at AFCA and amongst the consumer advocates will be attempting a QC/SC-level analysis, knowing that the non-lawyer who wrote the explanation is not a trained wordsmith and has written it under a commercially driven and consumer driven time pressure.

It would significantly and easily increase ASIC KPI numbers, however it would impose an unconscionable burden on credit assessors. Delegation supporters are particularly concerned that they would be placed in a position where they would have to be prepared to continually justify their methodological decisions, in circumstances where the performance of the loan repayment clearly indicates that the assessment was successful and appropriate - but just did not use one or more of ASIC's preferred list of assessment criteria.

C2Q3

What are the benefits, risks and costs for consumers in this approach (including any effect on access to and cost of credit for consumers)?

Answer:

While there is no problem with the proposal to "*more clearly state*" a list of activities from which the credit provider can choose - the proposal to introduce an "*If not, why not*" regime will <u>not</u> provide any benefits to the consumer.

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1. The lender's key determinants associated with the verification will have already been employed and the decision as to the suitability of the application will have already been made.
2. The sham application of the other verification criteria, in order to avoid "*if not, why not*" scrutiny, will follow and be totally meaningless - except to avoid ASIC assessment scrutiny.
3. There will not be any cost for the consumer, because the price is already effectively fixed by the legislation for SACCs and MACCs. The price for AOCCs is likely to go up, because many lenders do not lend with an annual cost rate very near the 48% cap for these longer and larger loans - so there will be room to move annual cost rates up.

It is competition that will drive the cost of AOCCs. However, the extra time to employ the sham verification will increase compliance costs and increase the price for all lenders if they are to maintain their net profit levels. In other words, with extra costs there will be less of a margin between the lender's total costs and the 48% cap, on which to base competitive pricing.

C2Q4

What additional business costs would be involved in this approach?

Answer:

Cost of credit assessors and responsible managers' extra time required to be allocated to every loan application.

It is important to note that rejection rates for applications for Finance Industry Delegation supporters were revealed in the Delegation's survey. Excluding one very highly specialised lender with a very targeted marketing program, the average rejection rate was 67.71%, with a range between 50% and 87%. A number of the respondents indicated a difference in the rejection rates between small amount and medium amount loans of up to 5%.

Simply - if ASIC was to adopt this "*If not, why not*" model, every application would have increased labour costs - putting major pressure on the profitability of the much smaller number of loans approved, that have to carry these total costs.

Consumers can expect to see a drop off in the availability of small and medium loans, because the extra time costs required to employ every verification opportunity, even as a sham, or the time to write the explanation as to "*why not*" documents, cannot be expected to be recovered with the lower gross revenues for these loans - as opposed to attempting to lend only AOCCs, with the greater opportunity for cost recovery due to the bigger gross profits in dollar terms.

Other business costs

Other business costs that would be incurred with the adoption of the "*why not*" regime include assessment staff and responsible manager training, redesigning application and assessment forms, changes to IT procedures and a huge increase in the risk of being audited, which will demand more frequent and expensive voluntary compliance auditing.

C2Q5

In your view, what would be the effect (either positive or negative) on competition between licensees? Please provide details.

Answer:

Less competition, as lenders flee small and medium amount lending and move to the larger loans, to enjoy a chance to recover the extra staff costs associated with the regime discussed above.

More competition in the larger MACCs plus AOCCs market.

PROPOSAL C3 - Benchmarks

We propose to clarify our guidance in RG 209 on the use of benchmarks as follows:

(a) A benchmark figure does not provide any positive confirmation of what a particular consumer's income and expenses actually are. However, we consider that benchmarks can be a useful tool to help determine whether information provided by the consumer is plausible (i.e. whether it is more or less likely to be true and able to be relied upon).

(b) If a benchmark figure is used to test expense information, licensees should generally take the following kinds of steps:

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(i) ensure that the benchmark figure that is being used is a realistic figure, that is adjusted for variables such as different income ranges, dependants and geographic location, and that is not merely reflective of 'low budget' spending;

(ii) if the benchmark figure being referred to is more reflective of 'low budget' spending (such as the Household Expenditure Measure), apply a reasonable buffer amount that reflects the likelihood that many consumers would have a higher level of expenses; and

Comment:

All the above [sub-point (i) and (ii)] reflect the benchmarks policies currently adopted by most supporters of the Finance Industry Delegation, apart from those who have exercised their choice and refused to employ benchmarks in any capacity during the assessment.

In the Finance Industry Delegation's view, given all the difficulties associated with benchmarks, it would be unwise to consider anything in the new version of Regulatory Guide 209 that diminishes the content of the current paragraph RG 209.105 - "*Use of benchmarks is not a replacement for making inquiries about a particular consumer's current income and expenses, nor a replacement for an assessment based on that consumer's verified income and expenses*".

(iii) periodically review the expense figures being relied upon across the licensee's portfolio—if there is a high proportion of consumers recorded as having expenses that are at or near the benchmark figure, rather than demonstrating the kind of spread in expenses that is predicted by the methodology underlying the benchmark calculation, this may be an indication that the licensee's inquiries are not being effective to elicit accurate information about the consumer's expenses.

Answer:

This raises the issue of the capability of the lender's computer software, or any alternative method of "manual" review being necessary and whether or not an additional cost will result.

Extra cost will obviously discourage the use of benchmarks for general comparative analysis. It may also be unwise to assume that lenders will be prepared to undertake the research and allocate the time necessary to discover the spread of figures that is claimed to underlie benchmark calculations. It also introduces the research and analysis workload repeat factor, with some benchmarks being published every quarter.

Tertiary level research skills are not a prerequisite for an Australian Credit Licence and should not and cannot be presumed across the industry sector. It must be remembered that the imposition of onerous compliance methodology is in conflict with both major political parties' policies of reducing "red tape".

Question:

What does "periodically" actually mean? Attempts to address imprecision by introducing more or alterative imprecision are best avoided.

Concluding comment on benchmarks:

ASIC has made a substantial attempt to highlight the deficiencies associated with benchmarks in pages 15 to 22. There are more to add to this list. Consequently, the Finance Industry Delegation is of the view that the use of benchmarks should continue to be an option, not a mandatory requirement for compliant assessments.

C3Q1

Do you consider that the proposed clarification of guidance about use of benchmarks would be useful? Why or why not?

Answer:

Yes, with the exception of adopting the general audit concept and with the avoidance of imprecise terms, because it reflects what more compliant and better advised lenders are already doing and could introduce a more competitive, level playing field. Further, the use of a benchmark figure for comparative analysis with consumer provided figures, provides a useful position when dealing with the frequently inaccurate and inappropriate attacks (lacking a materially significant basis) from consumer advocates and their legal centres, some financial counsellors and AFCA.

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C3Q2 - buffer amounts

Please provide information on what buffer amounts you currently apply, or would otherwise consider to be reasonable.

Answer:

There are two methodologies adopted by Finance Industry Delegation supporters in regard to the buffer. These are adopted by the industry sector because there are now such narrow margins involved, particularly with SACC loans, that it is absolutely critical to make an accurate decision concerning affordability. It must be remembered that, if the assessment is inaccurate and the consumer defaults without repair, it can take the lender 8-12 successful loans thereafter to recover the money lost.

The first approach is to take net income, deduct all expenses and thereby calculate the balance of income that is discretionary and constitutes the buffer. The second approach is a two tier effort, where the licensee has a policy that includes a preliminary buffer, which is generally a percentage of total living expenses, as an expenditure included with all the other expenditure, and then, after the assessment calculation is considered, the discretionary income is a two tier buffer. Obviously, when making a responsible lending assessment, the two buffers should be added together.

The Delegation's survey revealed that the majority of Delegation supporters have adopted the two tier approach. The first tier buffer was found to be a minimum average of $32.50 per relevant person, per week. The two tier buffer was highly dependent on consumer circumstances, but generally exceeded $25.

One of the writers has had dealings with a very senior ASIC officer who suggested that a minimum of $25 per person, for those who were a contributor or beneficiary of income or living expenses in the household, would be appropriate.

C3Q3

What are the benefits, risks and costs for consumers in this approach (including any effect on access to and cost of credit for consumers)?

Answer:

The benefit to consumers is an additional test of affordability. The risks are:

(a) that some lenders will avoid or continue to avoid the use of benchmarks for comparative purposes, to give them a competitive edge over their more conservative or responsible rivals - and news of easier access to credit travels fast amongst many consumers;

(b) that consumers will preference the non-using lender, because non-use will speed up the approval process, compared to the competitors who are using benchmarks for comparative analysis; and

(c) that lenders will consider the new policy a further demand for a more conservative approach to lending approvals and the benchmark - rather than actual applicant consumer expenditure - will revert back to being the actual measure at the forefront of the lenders' minds.

It is relevant to note that, while benchmarks provide an obviously faster consumer assessment, they miss the significant nuances that emerge from individual consumer assessment.

C3Q4

What additional business costs would be involved in this approach?

Answer:

On the basis that the benchmarks will be accessed in addition to individual consumer assessments the following would apply:

1. Extra time in the assessment process to research the appropriate benchmark figure, leading to higher wage cost (depending on the sophistication of the lender's loan management software, this could be up to 5 minutes).
2. Loss of business to the competitors who do not use any reference to benchmarks (due to both speed of approval and the lack of the extra barrier to approval).

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3. Loan management software upgrades to reflect the requirement for the "*periodic review*" - in addition to the costs presented earlier in this response, if the benchmark proposal was to go ahead, the average cost of upgrading the loan management software to accommodate it was just over $34,500.
4. Management time to consider the results of these periodic reviews.

Including the extra time required to research, analyse and apply the appropriate benchmark in each loan assessment process, plus fulfil the other assessment tasks suggested in the Consultation Paper, Delegation supporters have estimated that it would take an average of 34.8 minutes longer, per assessment. That means, on average, each assessment would cost at least $21.34 more to undertake (just for the assessor alone). As one example of the impact of this extra cost - given the gross income from a $400 loan, for 4 weeks, is $96 and the extra wages for the credit assessor's time alone would be 22.23% of that gross income. Add to that the extra time for the responsible manager, plus the on-costs associated with the credit assessor and the general costs of running a business, per hour, it puts any further impost into perspective.

C4 - Report 493

We propose to update the current guidance in RG 209 on reasonable inquiries about the consumer's requirements and objectives to reflect the findings and guidance in Report 493 Review of interest-only home loans: Mortgage brokers' inquiries into consumers' requirements and objectives (REP 493).

General comment:

While every study undertaken by ASIC should have the potential to generate the possibility of general applicability, the application of Report 493 should be undertaken with consideration of the following:

1. It was a study involving a very specific form of credit for larger amounts of money than most lending to which the new Regulatory Guide 209 will apply.
2. It was a study concerning brokers' compliance behaviour, which involves different commercial and compliance dynamics to the lenders who will constitute the majority impacted by any changes to Regulatory Guide 209.

The Delegation is also concerned that the content of paragraphs 66 and 67 indicate that ASIC is expecting far too much from consumers. Delegation supporters report that almost all consumers think in very simple terms when it comes to the loan they request. Except for the tiny proportion of consumers who have a finance industry background, expecting a consumer to be able to annunciate specific features or conditions of a credit product, beyond the amount of money they are seeking, is taking a step too far.

As a number of supporters have reported, when lenders question consumers for detail, they can generally expect answers such as "*well what does everyone else go for?*", or "*well, what is available?*". Apart from the amount required, the only other possible, relatively precise information that interests consumers is how much they think they can afford to repay per income cycle.

Similarly, paragraph 88 indicates a further process that is asking too much of lenders and lessors. Delegation supporters are not convinced that "*a summary statement of the licensee's understanding of the consumer's requirements and objectives for confirmation of that understanding*" is any advance on simply noting the consumer's reasons for borrowing or leasing, in a few words.

C4Q1

Do you consider that the proposed clarification of guidance about understanding the consumer's requirements and objectives would be useful? Why or why not?

Answer:

Without detail as to what ASIC proposes to select from the "*findings and guidance*" in Report 493, we cannot respond to this question constructively.

However, to the extent that the "*fit for purpose*" loan suitability test continues, the Delegation is concerned that this test is far more appropriate for leases than loans, and the wording of the new Regulatory Guide 209 should reflect this.

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General concerns arising from the “*Rationale*” on pages 23 and 24 of Consultation Paper 309 are:

1. Applying Report 493 to anything governing assessment compliance for SACCs and MACCs, and at least smaller AOCCS, <u>must</u> recognise that the consumers extremely rarely have anything more than the basic requirements and objectives of obtaining what they suggest is the relevant loan amount for their perceived relevant purpose. Demanding further interrogation is a total waste of time, will be resented by consumers and will generate fake responses that are not properly considered or particularly relevant.

   To this end, one of the Delegation’s larger lending supporters conducted an experiment on their website to assist in the preparation of this response. They installed a drop down list providing 52 alternative answers to the question “How did you hear about us?”, which included all the possible sources previously indicated by the research sample, including the name of a lead generator. Conducted over two weeks, the experiment involved between 900 and 1,080 consumers per day, who had been referred by the lead generator. Significantly, in excess of 40% of the consumers who should have nominated the referrer, ignored that opportunity and made wild selections.

   In a further experiment, after the company had already asked and received information on the reasons for the loan, a test batch of 200 consumers, over three days, were again asked the reasons for their application. 45% of those consumers did not present the same reason twice. On the second occasion they simply randomly selected another purpose. The Delegation supporter assessed that the reason for this was an attempt to make a selection that the consumer felt gave them a better chance of being approved for a loan.

   Given these discrepancies, it may be appropriate to ask - does the loan purpose really matter?

   The Delegation notes that ASIC has recognised an important element that must not be overlooked in the context of considering the consumer’s requirements and objectives. This is found in the current paragraph RG 209.121 - “*Making an assessment that a credit contract or consumer lease meets a consumer’s requirements and objectives involves matching <u>the consumer’s stated requirements and objectives</u> (which you will understand from the <u>reasonable inquires process</u>...)*”.

   For emphasis, the licensee has to rely on what the consumer tells them and reasonable inquiries cannot imply interrogation.

2. Applying Report 493 must recognise that the choice of loans for a consumer after a SACC, MACC, or at least smaller AOCC, is not significantly based on cost - the National Credit Code regime has ensured virtual price fixing.

3. It must be asked - what is the compliance and assessment affordability use of seeking information beyond the high level description of purpose for loans?

   What the consumer perceives as being achieved, and what the consumer wishes to achieve with the purchase, is a consumer issue between the retailer and the consumer and not a credit issue.

   ASIC’s paragraph 62(a) on page 24 of the Consultation Paper places a retailer responsibility on the lender and/or implies that the average SACC, MACC or AOCC is a very complex contract with many adjustable features - when they are universally template documents with none of the adjustments that ASIC assumes are available.

4. Concerning conflicting requirements and objectives, as discussed in paragraph 67(f) - the writers, in their various capacities, have never experienced this occurring over the 18 years of association with the industry sector.

5. There is no need for a summary statement beyond the basic notation of the consumer’s requirements and objectives, as implied in paragraph 68 in page 24. To emphasise - the type of description (one only) in Appendix 1 to the Consultation Paper, with amendments as discussed later in this response, suffices for both purposes.

The Delegation recognises that it is different with leases, because it is appropriate that the transaction provides the right goods, in circumstances where the lessor is offering both the goods and the lease contract. This is because the lessor is involved in both a leasing and retailer transaction.

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C4Q2

What are the benefits, risks and costs for consumers in this approach (including any effect on access to and cost of credit for consumers)?

Answer:

See our answer to C4Q1 above

C4Q3

What additional business costs would be involved in this approach?

Answer:

See our answer to C4Q1 above.

PROPOSAL D1 - excluded lenders

We propose to include new guidance in RG 209 on the areas where the responsible lending obligations do not apply.

General comment:

Anything that discourages AFCA and the consumer advocates from their constant attempts to expand their power and reach, will be welcomed by those lenders and their compliance advisers who have to allocate time to remind them of their mandate and what lending is regulated by the NCCP Act.

D1Q1

Are there any forms of lending where the responsible lending obligations are being used by licensees in situations where the law does not require the responsible lending obligations in the National Credit Act to apply? Please describe the situations where this takes place.

Answer:

Small and medium business loans. Some choose to apply the obligations because of the definition of a personal loan in the National Credit Code that involves some investment purposes associated with real property, being more generally applied or misunderstood. Some out of lender choice to maintain consistency in their operations, because they also lend personal loans, and some because it suits their adopted business loan assessment policies.

D1Q2

Are there any forms of small business lending where licensees are unsure about whether the responsible lending obligations in the National Credit Act apply? Please describe the situations which give rise to this uncertainty.

Answer:

While not reported by Finance Industry Delegation supporters, the writers are aware of some non-supporter and poorly professionally advised confusion. Greater clarity as to when a personal loan becomes a business loan and vice versa, and in regard to the investment in property loans, recognised under the National Credit Code, may be of assistance. It could be useful for ASIC to check with AFCA on the types of non-personal loans and their circumstances that generate attempts to complain to AFCA.

PROPOSAL D2 - fraud

We propose to include new guidance in RG 209 on:

(a) the role of the responsible lending obligations, and in particular the obligation to take reasonable steps to verify information provided about the consumer's financial situation, in mitigating risks involved in loan fraud; and

General comment:

Given the total volume of loans lent, Finance Industry Delegation supporters report relatively few attempts at loan fraud, and these generally involve cases where the consumer misrepresents the purpose of the loan, actually spending the loan funds on a purpose not declared during the application process, and makes dishonest representations as to income.

A consideration of the content of paragraph 76 and 77 is of concern to Delegation supporters. It appears that ASIC's primary concern is to encourage lending to consumers and to be tolerant of situations of potential fraud. The reality is that indications of past fraud are rarely inaccurate. As

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a result, in the first instance it is unrealistic to expect that such indications are "*likely to raise doubt about the reliability of information*".

However, a relatively frequent issue is the involvement of credit repair companies, who accept their fee from the consumer, encourage further borrowing and then immediately seek to have their client involved in a Part IX agreement.

With the exception of overstatement of income, the type of fraud identified by ASIC on pages 26 and 27 is not relevant for SACC, MACC and most small AOCC loans that Delegation supporters are offering.

(b) risk factors that might indicate that additional verification steps should be taken.

General comment:

The major risk factor is the potential for dishonesty on the part of consumers and the associated encouragement by AFCA, consumer advocate legal organisations, Legal Aid and financial counsellors, who do not do due diligence and confirm the legitimacy of the consumer's complaint before taking the complaint further.

This problem is exacerbated by the constant media stories promoted by the consumer advocates, many of which are deliberate concoctions in an attempt to prove a point. The dishonest consumer reads, sees or hears stories about so called "vulnerable" borrowers and the "usurers", and sees an opportunity to obtain a free loan.

The Finance Industry Delegation is at a loss to suggest additional verification steps to solve this issue - except the creation of a national database that blacklists individuals from being able to successfully apply for a loan due to previous dishonesty and fraudulent behaviour, which can be accessed by credit providers.

D2Q1

Would specific guidance about loan fraud and the impact on responsible lending obligations of the licensee be useful? Would guidance encourage broader improvements in processes for identifying fraud and reduce the risk of consumers entering unsuitable credit contracts as a result of fraud? Why or why not?

Answer:

This is unlikely to be of much relevance to Finance Industry Delegation supporters, for the reasons noted above. The concern must not be directed at consumers entering unsuitable credit contracts, but consumers defrauding lenders and, in the process, generally walking away from repayment.

D2Q2

Please provide details of any risk factors that you consider it would be useful to identify, and additional verifying steps you consider to be reasonable in those circumstances.

Answer:

The risk factor of increasing consumer dishonesty and the growing number of consumers who know how "to play the system" is a reality.

Additional verification - access to a "black list" database (as mentioned above). This would supplement the current credit reporting system, which is unreliable due to:

- the time it takes to get an adverse listing included on the consumer's file;
- the lack of participation by many lenders; and
- the blackmailing of lenders by credit repair companies and consumer advocates, who use the costs associated with an AFCA complaint to force the lender to make the commercial decision simply to remove details that are correctly included on a consumer file - details that should remain available for all future lenders to discover on application.

D2Q3

What are the benefits, risks and costs for consumers in this approach (including any effect on access to and cost of credit for consumers)?

Answer:

The benefits would include more money being available to lend to honest consumers with the reduction in loan write-offs due to fraud, the elimination of many of the unscrupulous and

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unregulated credit repair companies, and a credit reporting system that many more lenders would support and use.

Another major benefit would be the saving in staff and management time plus a reduction in debt collection on-costs, due to fewer dealings with fraudulent consumers. There would not be any cost to consumers.

Please note: The Finance Industry Delegation and one international company have 2 different (competing) and tested models of this database available. It could be up and running within 3 months.

D2Q4

What additional business costs would be involved in this approach?

Answer:

The subscription costs to an effective new consumer database. For most lenders this cost would be easily covered by the reduction in costs due to consumer fraud.

PROPOSAL D3 - repayment history

We propose to include guidance in RG 209 to clarify how repayment history information may be used, including that:

(a) the occurrence of repayment difficulties on one product will not necessarily mean that a new credit product will in all cases be unsuitable for that consumer; and

General comment:

The Finance Industry Delegation has commissioned research over many years and the writers' experience with clients' compliance reviews consistently indicates that the words "not necessarily" should be very conservatively addressed.

The only general applicability is in regard to the issue of refinancing, where the financial obligations are significantly reduced and within the actual or new income and expenditure means of the consumer.

The Delegation notes that the current Regulatory Guide 209 recognises this opportunity for refinancing in the circumstances prescribed above. This is found in paragraph RG 209.118, Example 12, which recognises that refinancing could reduce the level of hardship.

However, where the difficulty faced by the consumer relates to the past, in the opinion of the Finance Industry Delegation, positive intervening and current changed circumstances should be considered. The content of paragraph 81 on page 29 in the Consultation Paper is helpful in this regard.

(b) The nearer to present time this information relates to should instead trigger the licensee to make more inquiries to enable it to understand those repayment difficulties, and the likelihood that the circumstances of the consumer leading to those difficulties will mean that the consumer would also be unable to meet financial obligations under the new product being considered.

Answer:

The majority of lenders are already undertaking these further enquiries. It must be remembered that lenders lose money if they are not effective in this task. The punishment involving larger numbers of loan write-offs is very potent.

Nevertheless, licensees will welcome opportunities to offer a loan or a lease in circumstances where there is an obvious and considerable change to the consumer's financial position and, to use Justice Davis' words in The Cash Store case, "it is reasonably likely" that the consumer will successfully fulfil their contractual obligations.

Please note: If the issue associated with repayment history involves comprehensive credit reporting, the Finance Industry Delegation is concerned to emphasise to ASIC that there is considerable disagreement as to the benefits and applicability of this concept to SACCs, MACCs and at least the smaller AOCCs. The issues of concern, on both sides of the debate, would demand an opportunity for considerable discussion time at an essential, all stakeholder, consultation meeting facilitated by ASIC as part of this consultation process.

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D3Q1

Would guidance about use of negative repayment history information and hardship indicators reduce the risk that credit providers consider it necessary to refuse applications for further credit products that may in fact be affordable for the consumer? Why or why not?

Answer:

Consumer advocate claims that consumers have a right to access credit, have to be balanced against the knowledge that the advocates are not the ones that lose their money if a loan goes bad.

Further, lenders are in business to lend according to their risk profile. No imposed guidance is required from ASIC, as a non-lender. This is an area for commercial decisions according to the lender's risk analysis and policies, in an environment where the lender has not forced the consumer to apply for a loan, and the lender's decision making should not be tampered with by the un-researched and unsubstantiated opinions of non-lenders.

The Finance Industry Delegation considers that evidence of negative repayment history stands on its own and it is up to the credit provider's consideration of later more favourable evidence, as to whether or not the latter outweighs the former in the assessment decision. It is the Delegation's view that no amount of 'guidance' will change a credit provider's careful approach to this assessment.

ASIC should not be optimistic that inclusion of guidance in the new Regulatory Guide 209 will increase assessment approval rates. It may be impractical for ASIC to consider that licensees will undertake the steps outlined in paragraph 81. These involve further assessment time and expense. Documenting the reasons why they have not proceeded with the application is contrary to the NCCP Act, where such a requirement is exclusively limited to where there has been a positive assessment. To expect otherwise is to contradict the Parliament's wishes.

D3Q2

What are the benefits, risks and costs for consumers in this approach (including any effect on access to and cost of credit for consumers)?

Answer:

The "benefit" is that a struggling consumer may get one more loan than they should have been given.

The major risk is the expansion of opportunity for consumers to enter a debt spiral.

The major cost will be a reduction in the number of credit providers and a lowering of competition, as credit providers face greater loan write-offs and further substantial reduction in gross and net profits. If this approach is supported by ASIC - then ASIC should participate in setting up a new lending outlet to service the consumers the policy seeks to serve, with diversion of the existing government grants to consumer advocate groups and entities - who support the philosophy of universal access to credit - to fund the new initiative.

D3Q3

What additional business costs would be involved in this approach?

Answer:

A substantial increase in loan write-offs. Unnecessary and inappropriate forced allocation of credit assessor and responsible manager time to undertake the assessments, and then the time spent attempting to chase up payments and money spent on debt collection.

Finance Industry Delegation supporters have indicated they would expect fewer loans and a lesser amount of credit to be available.

PROPOSAL D4 - maintaining records

We propose to include new guidance in RG 209 about maintaining records of the inquiries made and verification steps taken by the licensee, reflecting our findings and recommendations on good recording practices included in REP 493.

General comment:

If the new guidance revolves around the provisions in Appendix 1, in the suggested modified form, this would be welcomed by the Finance Industry Delegation (see later discussion on the content of Appendix 1 in this response).

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The Delegation emphasises that the record should be one document that incudes the enquiries and verification and the results of those enquiries and verification, and which can be used as the assessment when a consumer requests one.

This one document should not include file notes or prompting notes that relate to internal communications, or credit assessor reminders or check lists, or further issues the assessor considers should be explored.

In accordance with Note 2, dot point 1, in the current paragraph RG 209.7, these are the tools used to arrive at "*the basis of an assessment*", but are not the "*material*" that forms the basis of that assessment.

The Delegation notes the content of paragraph 85(c) on page 31 of Consultation Paper 309 and again counsels against a policy encouraging extended dialogue between the credit assessor and the consumer applicant on the requirements and objectives/purposes of a loan - but not a lease, where there is a retailer element to the transaction.

The Finance Industry Delegation is most concerned with any ASIC consideration that would open the door to rejected applicants seeking review and, more particularly, being encouraged to complain to AFCA and/or ASIC that they had been rejected. The history of such complaints is generally associated with highly irrational claims and constant harassment of both the credit provider and the external dispute resolution scheme. In essence, licensees should not be forced to do business with people with whom they don't want to do business. Again, such a policy has no support from the NCCP Act.

D4Q1

Do you consider that guidance on industry best practice for recording the inquiries and verification steps that have been undertaken would be useful for licensees? Why or why not?

Answer:

Yes. This introduces certainty and reduces the opportunity for unsupportable, frequently vexatious and/or unconscionable challenges by AFCA, consumer advocate legal centres, Legal Aid and financial counsellors.

D4Q2

Please provide any comments on the particular recording practices identified as 'best practice' by ASIC, and whether you consider those practices are generally appropriate for licensees.

Comment:

"*Best practice*" is one comprehensive template document not challenged, on the basis of whether or not it is concise (whatever that means).

D4Q3

What are the benefits, risks and costs for consumers in this approach (including any effect on access to and cost of credit for consumers)?

Answer:

The benefit is a comprehensive assessment report, if requested. The risk for the consumer is that the comprehensive nature of the template may reveal reasons for not accepting the consumer's application which may have remained undetected, or been overlooked, without the template to complete. There is no cost impact on the consumer.

D4Q4

What additional business costs would be involved in this approach?

Answer:

Extra staff time for assessment, for licensees who have not already adopted this practice.

PROPOSAL D5 - written assessment

We propose to provide additional guidance in RG 209 on what information we think should be included in a written assessment.

General comment:

The fundamental purpose of the assessment document must not be overlooked. It is both a checklist and a record of the licensee's assessment of the consumer's application.

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Lenders rarely receive requests for assessment reports, with the proportion being far less than 0.5% of licensees' transactions.

This proposal must recognise whether ASIC expects identical content in both the assessment documentation used by the lender to conclude their assessment decision, and the report the consumer is to be provided with if they request such.

Further, any nonsense instruction that the assessment (report) provided to consumers must be concise, must be abandoned to reflect what ASIC, AFCA, the consumer advocate legal centres and financial counsellors already expect to find.

In regard to the "*Rationale*" concerning the "*Content of a written assessment*" included on pages 31 and 32 of Consultation Paper 309, we provide the following comment:

1. Paragraph 88 contains the confusing assumption that the consumer can ask for a copy of the assessment before the loan is approved. The Delegation's reading of the Credit Act confirms that this is not the case - the consumer can only request a copy of the assessment if the loan is approved.
2. Paragraph 89(a)(iii) requires a credit assessor to summarise information provided by the consumer that was not used in the assessment, and to explain why. This is nonsense and implies that everything a consumer tells or provides a credit assessor deserves such attention. Irrelevant information is just that - irrelevant. What is relevant (only) is the information the credit assessor actually used to make their assessment.
3. Paragraph 89(a)(v) continues to encourage belief that a consumer can change their consumption/spending patterns to accommodate a new loan's financial obligations. As discussed elsewhere in this response, the Delegation considers any loan approval based on a consumer being expected to change their financial habits is most unsound, unless that approval involves a substantial explanation being noted, ideally with some evidence supporting the capability of the consumer to change their ways. It is not that the Delegation wants to discourage a consumer prepared to change their behaviour, it is a concern based on human psychology, avoiding supporters losing their money and preventing any unnecessary attacks by consumer advocates and their colleagues.
4. In paragraph 90, the Delegation notes ASIC's presumption that proposed legislation introduced into the Commonwealth Parliament earlier this year, will actually be reintroduced and passed in the coming parliamentary term. It may be unwise to assume this in the development of the proposed new regulatory guide.

D5Q1

Would it be useful for ASIC to provide an example of a written assessment to illustrate the level of information that we think should be included? Why or why not?

Answer:

Yes. Supporters of the Finance Industry Delegation would appreciate certainty, to ward off any unnecessary attacks by AFCA, the consumer advocate legal centres and financial counsellors, as to the adequacy of their assessment (reports).

An ASIC benchmark to assess the comprehensive application and assessment form template that continues to be recommended to the Delegation's supporters would be appreciated.

D5Q2

Please provide any comments on the example set out in Appendix 2.

Answer:

Given its surprising limitation in content, as opposed to the aggregated ASIC individual officer, CIO/FOS/AFCA, Consumer Action Legal Centre, Legal Aid and financial counsellor expectations that have emerged over the last 5 years, plus the many expectations that emerge from a variety of current ASIC Regulatory Guides and publications, the Finance Industry Delegation will be most interested to read the views of those entities and individuals.

In the Finance Industry Delegation's view, the current paragraph RG 209.146 provides an appropriate limitation on content of the assessment (report) - "*only information that specifically relates to the statutory concepts of 'requirements and objectives', 'capacity to repay' and 'reasonable inquiries' should appear in the written assessment*".

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It is hoped that this statement will be stressed and amplified in the new version of Regulatory Guide 209, because individual ASIC officers, consumer legal centres and FOS/CIO/AFCA have all encouraged, demanded and/or approved of considerably more content in recent years.

However, amplification should not inhibit the lender or lessor from adopting a more detailed approach if properly advised, because inclusion of this greater content has been a very significant determinant in a number of disputes familiar to the writers of this response.

Comments:

1. Objective: Purpose of obtaining credit.

   (a) The Finance Industry Delegation is very pleased to note the move away from the clumsy use of the terminology "*requirements and objectives*" and, additionally, "*purpose*". Most of the examples are a very useful and practical benchmark.

   (b) However, unless there are also post-purchase costs to be recognised in the loan amount, the need to include the "specific value" is unnecessary for loans (but not leases). It does not achieve any purpose. Credit assessors are broadly aware of the likely cost of an item and exact retail prices can vary between loan application and actual purchase, or between the intended retailer when the loan is applied for and the retailer offering a special deal when the funds are actually available.

   (c) Comment on quality is very subjective for most people and neither consumers, nor the credit assessor, should be presumed sufficiently technically knowledgeable to make a notation as to quality assessment. However, if a lessor is also the retailer of the leased product, then retailer comment on quality has validity.

2. Requirements: amount and term of credit requested.

   (a) Consumers approach an application for credit with an amount in mind. There is no issue of "maximum amount" until the credit assessor, due to the assessment undertaken, is forced to indicate a lower amount as being available than that for which the consumer originally applied.

   (b) Consumers do not apply for the loans lent by Finance Industry Delegation supporters with a clear view of the time frame they would prefer for repayment of the loan. That is far more an issue for home loans. They rely on the credit assessor to tell them.

3. Requirements: Particular features requested or not necessary

   (a) Delegation supporters do not have consumers applying with "*contract features*" in mind. The amount they want to borrow is the only feature of interest and most know that prices are effectively fixed by legislation for SACCS and MACCs and that the annual cost rate offered for AOCCs will be in accordance with the lender's own policies (up to the 48% cap). It should be noted that it is very rare for a consumer to attempt to negotiate on price.

   (b) Inclusion of a "*summary of any contract features the consumer has indicated are not wanted*" will generally elicit a "Not Applicable" notation or, for car loans, a list of "add-ons" such as special insurance, or tinted windows, etc. that are not being purchased by the consumer and are not to do with the actual credit contract, apart from impacting on the amount borrowed. We cannot see how an indication of personal preferences such as this is material to ASIC's ability to assess compliance with credit laws.

4. "*Financial position*"

   (a) Re. "*fixed or recurring expenses*" - the Delegation strongly recommends an expansion of "*debt commitments*" to include all loans, all leases, all "buy now, pay later" commitments and all payment plans. This is particularly critical for SACC and MACC applications, where the unbelievably unregulated "buy now, pay later" commitments are often a very serious financial burden for the consumer.

   (b) Re. "*Variable living expenses*" (non-discretionary) - there is a contradiction in the subheading and in the text. They are non-variable "*essential*" expenditures.

   The attempt to categorise according to variable living expenses - discretionary and non-discretionary - introduces problems of categorisation. The current paragraph RG 209.33 lists as "*discretionary*":

   - entertainment,
   - take-away food,

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- alcohol,
- tobacco and
- gambling.

Given that for many consumers these expenditure items are a way of life and not an ad hoc expenditure, they cannot always be considered discretionary. Such a categorisation problem introduces uncertainty.

Consideration as to what constitutes discretionary spending must also reflect the fact that, to date, the legislation and ASIC have declined to provide a definition of substantial hardship.

This situation has resulted in only one clear prescription being presented by ASIC in the current Regulatory Guide 209, which has a potential bearing on the relevance (or non-relevance) of discretionary expenditure in an assessment calculation.

In the Note to the current paragraph RG 209.97 there is mention of other legislation providing some guidance as to what substantial hardship might actually mean. Quoting the Superannuation Industry (Supervision) Regulations 1994 Regulation 6.01(5)(a)(ii), ASIC states - "*…one of the tests for whether a person is in 'severe financial hardship' is that 'the person is unable to meet reasonable and immediate family living expenses'…*".

It is possible that this definition would exclude the need for a licensee to recognise any discretionary expenditure in their suitability assessment, because such could be considered "unreasonable" expenditure not associated with immediate living expenses.

5. "*Assumptions dependant on consumer behaviour*"

   As indicated above, if recognised, these assumptions should be considered and discussed by the credit assessor. In this area - good intentions and consumer honesty, in regard to changing expenditure behaviour, should never be accepted as credible or realistic loan application assessment criteria, without great care.

   Because it cannot be guaranteed that a consumer would be successful in their well intentioned ambition to change their spending habits, considerable exploration of this issue during the assessment process must be expected.

   It cannot be assumed that the credit assessor has adequate training in psychology, or knowledge of the applicant consumer's track record in regard to such matters, to easily make an informed assessment as to whether or not any reduction offer was "realistically achievable". It would be most inappropriate to expect an assessment of changed consumer behaviour that was of such a high standard that it would imply an obligation on the part of the licensee to follow up with the consumer and ensure that the change had occurred.

6. "*Foreseeable changes to financial position*"

   (a) The Delegation welcomes ASIC's recognition that it must only be the consumer's assessment of foreseeability that can be involved.

   (b) The Delegation agrees with the continuing requirement to note post-purchase expenses associated with the purchase of a car with borrowed funds.

7. "*Financial support from a third party*"

   (a) The acceptable form of acknowledgement for a third party making a contribution to household income or expenses must be specified - as this is a very vexed area.

   (b) "*Details of the other person's financial position*" provides a practical challenge.

   They are not co-borrowers, they are not guarantors, they are rarely with the consumer at the bricks and mortar outlet making the application, and there is no way of knowing if they are in attendance when the consumer is applying online.

   Then there is the privacy issue of the credit assessor contacting them and revealing that another person has applied for a loan with some dependence on them to assist with repayment. ASIC must be on notice that two complete financial assessments are both impractical, and a significant negative cost issue for SACCs and most MACCs. In addition, there is often considerable negativity from the second party, who resents the intrusion of an attempt at a financial analysis by the credit assessor, in regard to someone else's loan.

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8. “*Information provided by the consumer that has not been relied upon*”

   Again, the Delegation is concerned about the possibility of being forced to include a range of useless information in the assessment report that is not relied on and being forced to explain why it was not instrumental in the assessment decision making process. The relevant information can only be the information actually used in the process. The NCCP Act demands “reasonable”, not “absolute”, inquiries and verification, in circumstances where having to explain the reason for not regarding information as relevant could create a battleground for the irate and irrational consumer to exploit.

D5Q3

What are the benefits, risks and costs for consumers in this approach.

Answer:

(a) Less chance of being given an unsuitable loan;

(b) the risk of being refused, when they may otherwise have been accepted with a less disciplined assessment; and

(c) there is no cost impact on the consumer, except where there is an opportunity to increase the annual cost rate of an AOCC, to cover costs associated with the extra impost.

D5Q4

What additional business costs would be involved in this approach?

Answer

None for most Finance Industry Delegation supporters, because they have application and assessment forms that already match - or exceed - the content included in the ASIC draft.

We thank you for your consideration of this response.

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