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Fleur Grey
Senior Specialist Credit
Retail Banking and Payments Financial Services
Australian Securities and Investments Commission

By email: responsible.lending@asic.gov.au

Dear Ms Grey

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

We are responding to ASIC's invitation to comment on Consultation Paper 309: Update to RG209: Credit Licencing: Responsible Lending Conduct ('**CP309'**).

Macquarie Group Limited ("**Macquarie**") has reviewed the proposals as they apply to our home loan, credit card, auto loan products and strata improvement loans.

ASIC's Regulatory Guide 209: Credit licensing: Responsible lending conduct ('**RG209'**) is a key component of the compliance framework for lending and we thank ASIC for the opportunity to provide a submission in relation to their proposed amendments.

If you have any questions, please don't hesitate to contact me on +61 28237 3575 or by email at drew.hall@macquarie.com.

Yours sincerely

Drew Hall

Head of Banking Product
Banking and Financial Services
Macquarie Group Limited

Thank you for the opportunity to provide ASIC with feedback on their proposed changes to RG209. Changes to RG209 will have a significant impact to consumers seeking credit, the banking industry and the Australian economy. In forming a response Macquarie has considered various options to ensure we deliver good consumer outcomes and maintain prudent lending standards, whilst having regard to efficiency, competition and innovation.

Principal Views

Macquarie's principal views are:

a) The current litigation between ASIC and Westpac addresses some of the same issues raised by the consultation paper. With the *amicus curiae* in that case expressing views that differ markedly from the positions submitted by both parties, it is clear that a different interpretation of the existing law to that reflected in RG 209 and CP309 could be expressed by the Court. We strongly favour introducing the updated regulatory guide only with the benefit of the Court's decision. This will avoid the risk of error in the regulatory guide, and of having two phases of industry change with respect to a single and unchanged regulatory regime. We would also welcome the opportunity to make further submissions if appropriate after the Court has made its decision.

b) We think it would be valuable for both consumers and industry that ASIC provides more detailed practical guidance in RG209. This assists in establishing regulatory certainty and reduces the risk of different credit providers adopting materially different lending standards, thereby reducing the risk of regulatory arbitrage and so is beneficial on competition grounds;

c) The Explanatory Memorandum to the National Consumer Credit Protection (NCCP) Bill (EM) states that verification is not required to go beyond steps that a prudent lender would undertake. This reflects the legislation which states that lenders need take 'reasonable steps', not *all steps*, and only to the extent needed to avoid likely 'substantial hardship'. We expand on these points further in part 2 below.

   As such:

   1. the full verification of all living expenses is not needed in the vast majority of lending assessments under the current legislative framework. This is because verification of living expenses is either:

      i. not a 'reasonable step' because it does not produce reliable or accessible information[1] and therefore imposes excessive measures on the consumer and credit provider without any material benefit to the consumer or the credit provider; or

      ii. not a necessary step to ensure that the loan is not unsuitable given the discretionary nature of expenses. In saying this, there are circumstances when verification may be a prudent step to help confirm serviceability, for example, if the credit provider is on notice of discrepancies in the loan application;

   2. different assessment processes can be adopted for different loan products and different consumers and it would be helpful if the regulatory guidance can give more detailed views on these differences;

d) The law imposes an obligation on borrowers to not make false or misleading representations when applying for a loan (NCC section 154 and paragraphs 3.77 to 3.79 of the Explanatory Memorandum). This provision has a role to play when determining what 'reasonable steps' a lender needs to take when making further inquiries and undertaking verification. It is also relevant when assessing liability in disputes where a borrower has submitted misleading

[1] see paragraph 64 of opinion of *amicus curiae*

information. ASIC guidance should include when this provision would apply to the information a borrower represents to the lender resulting in the need to not make further inquiries or verification.

2) Responsible lending and the current statutory obligation

Responsible lending obligations under section 130 of the NCCP Act require the credit licensee to take 3 key steps in relation to a consumer's financial situation:

(a) to make *reasonable inquiries* about a consumer's financial situation;

(b) to take *reasonable steps to verify* the consumer's financial situation; and

(c) to make an assessment about whether the credit contract is *not unsuitable* for the consumer (based on the inquiries and information obtained in the first 2 steps).

A contract will be unsuitable for a consumer if, at the time of the assessment, it is *likely* that the consumer will be unable to comply with the consumer's financial obligations under the contract or could only comply with *substantial hardship*. There is a presumption of substantial hardship if the consumer could only comply by selling their principal place of residence.

Guidance is obtained from the EM, which states that the purpose of undertaking inquiries about a consumer's financial situation is to obtain a *reasonable understanding* of the consumer's ability to make repayments under the loan. The legislative purpose is not to require a licensee to know exactly what the consumer's financial position is – rather, as set out in para 3.140 of the EM, it is to have the licensee gather and verify sufficiently reliable information for the licensee to have a *reasonable understanding* of the consumer's ability to afford the loan.

In relation to verification, the standard to be applied is that of a *reasonable and prudent lender in the circumstances*. Para 3.147 of the EM states that the licensee "*must make such efforts to verify the [financial] information provided by the consumer as would normally be undertaken by a reasonable and prudent lender in those circumstances. Credit providers are not expected to take action going beyond prudent business practice in verifying the information that they receive*."

When considering the verification of a consumer's living expenses, Macquarie's experience does not support that this is a relevant or useful measure for protecting the consumer from experiencing substantial hardship. Our review of early term delinquencies (arrears within the first 6 months from origination) in home loans do not align to the understatement or underestimation of living expenses. In our experience 90% of hardship applications for Macquarie home loans stem from life events such as medical or illness, reduction of income and loss of employment. Hardship events are not easy to predict and are often of a material and ongoing nature. The remaining 10% of instances do not involve the understatement or underestimation of non-discretionary living expenses.

We have found there is no correlation between the number of applications disclosing living expenses below the HEM benchmark and the level of arrears in our home loan portfolio over time. In our view the current practice of using the higher of consumer's declared living expenses and the income adjusted HEM is acting as an appropriate safety net and reasonable basis for consumers who underestimate their expenses, to be able to afford their loan without suffering substantial hardship.

Another important consideration of these expenses being variable is that consumers can adjust their lifestyle and their level of such expenses if needed to avoid substantial hardship. Or at least, this outcome can arise in the absence of a material adverse life event. As mentioned, this is reflected in our arrears experience in our home loans portfolio.

The collection and calculation of accurate living expenses is a difficult exercise for consumers. Consumers often misunderstand expense inquiries and experience frustration when looking to calculate them. This reflects the fact that living expenses are variable and discretionary given that many of them involve personal preferences which change particularly once a home is acquired. It is because consumers can and do regularly adjust their living expenses in their everyday living that they find the collection and calculation if of these expenses difficult. Verification of and then further enquiry of living expenses may lead to many consumers choosing not to refinance their loans to get a better deal due to the time and effort involved leading to worse outcomes for consumers and reduced competition.

Our responses in **Appendix 1** are framed within the requirements of the current law, as we understand them and have set out above in part 2. Similarly, we submit that it is important that the regulatory guide pay due regard to this interpretation and the limits of the extent of the obligations placed on credit providers in light of the purpose of the legislative regime.

Appendix 1

B1 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.

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?

Yes, guidance on particular inquiries and verification steps would be useful.

Macquarie believes this guidance will be useful to provide consumers with a clear understanding of the pathways to credit.

For credit providers, this will help ensure consistency across the industry and reduce the risk of credit providers competing, whether intentionally or inadvertently, by virtue of different interpretations of legislative requirements.

B1Q2 If there are particular examples of industry practice that you consider should be reflected in any guidance, please provide details of those practices.

ASIC should include the following examples of industry practice and scenarios in the revised RG209:

- Practical application of responsible lending laws and guidance in relation to different products, covering home loans, credit cards, asset finance, personal loans and strata corporations. We note that CP309 and RG209 guidance focuses on lending to individuals and that responsible lending obligations also apply specifically to strata corporations for which different considerations apply.

- Ability to extend loans to consumers where income is not their sole means of meeting their financial obligations. For example, high net worth clients with varied financial resources which create additional means of managing hardship events.

- The obligations of all parties to be honest and not misleading in the credit transaction and the credit provider's ability to accept certain information from consumers including where verification is limited. This is articulated in NCC s154 and EM 3.17.

  For example, a credit provider should be able to rely on a third-party introducer in relaying the outcomes of a credit provider's further inquiry on their consumer's application.

  Particularly where these will be subsequently validated by the consumer independently. This supports efficiency and the credit assistance provider's role in the lending process.

- The use of unpacked living expenses has gradually been adopted by mortgage lenders, however variances between lenders still exist. ASIC should standardise the unpacked living expense categories applicable to different products.

- There is an opportunity for ASIC to play a role in the setting of the use of HEM benchmark parameters. We recommend that the guidance be updated to include:
  - setting the benchmark, implementation of the most up to date and applicable versions, clarification of attributes to be included and how to apply across different household compositions. E.g. sole borrower vs joint borrowers; and
  - what threshold comparative to HEM would require a credit provider to make further inquiries and verifications.

- Where there is a sole borrower applying for a credit product and that borrower has shared household expenses and / or liabilities. Further guidance should be provided on how a credit provider should treat those shared obligations in the serviceability assessment.

- ASIC should give guidance to an appropriate interest rate buffer when assessing serviceability of debt to eliminate misalignment between ADI's and non ADI's.

B1Q3 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.

We consider that it is reasonable to undertake fewer inquiries and verification steps in particular scenarios. These include:

- **High net worth clients** – consumers that have high levels of excess surplus capacity evident on initial verification. In Macquarie's experience, further inquiry and verification does not materially alter the assessment in these cases.

- **Existing Customers** – Credit providers can make use of existing information and therefore can undertake fewer inquiries.

We also consider this question in relation to requirements and objectives in C4Q1.

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.

Macquarie's view is that there should be a core level of inquiry and verifications steps required for individual consumers on all products, with further inquiries and verifications completed when certain risk indicators are evident.

The level of further inquiry and verification will be defined by risk indicators and an assessment of the risk of loss to the consumer. For example, a product with a repayment liability which represents a smaller proportion of the consumer's income, would warrant a different level of further inquiry than product which represents a higher portion of their income.

Our responses to B1Q4 and B1Q5 are set out with this in mind.

In our view the core **inquiries** that should be made are:

- Income required for servicing.
- Unpacked living expenses.
- Liabilities, and where relevant interest rates and loan structure details (e.g. existing mortgage I/O terms and credit card limits).
- Accommodation costs (e.g. Rent, board etc).
- Assets
- Personal circumstances (e.g. marital status, dependants, age).
- Any foreseeable changes and the consumer's plan to manage these.

Examples of risk indicators that may warrant **further inquiry** include:

- Conflicting information against the client's profile (e.g. dependants declared does not align with a core verification document provided).
- Disputed information on supplied evidence (e.g. inconsistent YTD income figures on a payslip).
- Declared living expenses are not plausible (e.g. living expenses are significantly below the nominated benchmark).
- Negative credit bureau information.

Further inquiry may be undertaken in a number of ways, including discussions with the consumer or their third-party broker.

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.

In our view, credit providers would need to undertake the following core **verification** steps:

- Income required for servicing.
- Liabilities as ascertained through comprehensive credit reporting (CCR).
- For secured lending - Assets acquired under or securing the proposed credit contract (e.g. property securing a mortgage).

We believe that these items should be verified in all circumstances as they are fundamental to a consumer's financial situation, reliable documents can be obtained to verify this information and it is readily available and easily understood by consumers.

Examples of risk indicators that may warrant **further verification** include:

- Application is outside a defined assessment ratio e.g. High Repayment to Income (RTI) ratio.
- After making further inquiry living expenses are still not plausible.
- Where the accommodations costs declared are not plausible.

Aspects of the consumer's financial situation that we believe do not need to be verified in ***all*** circumstances are:

<u>Living expenses</u>

We do not believe that the intent of the legislation is for credit providers to verify living expenses (both fixed and discretionary) in **all** circumstances. As noted in the EM "…c*redit providers are not expected to take action going beyond prudent business practice in verifying the information that they receive".*

We believe full verification of living expenses in all circumstances is disproportionate to the limited link between understated living expenses (noting that the industry now uses the higher of income-adjusted HEM and disclosed living expenses) and a higher risk of substantial hardship. It is also unduly intrusive in most cases.

Further, there is no reliable way to verify a consumer's ongoing expenses with complete accuracy and we do not believe that taking steps which do not result in reliable information should be regarded as a 'reasonable step' that must be taken in *all* circumstances under the law.

Consumers often ‘spend the money they have’ on discretionary items prior to engaging in credit. Macquarie does not believe that verifying a consumer’s historic spending habits is useful given consumers often adjust their spending and lifestyle to cater to their new debt obligations. Additionally, mortgage lenders buffer interest rates and haircut income resulting in the amount of disposable income actually available to consumers being higher than the serviceability assessment shows.

<u>Any foreseeable changes</u>

Where possible, credit providers should take reasonable steps to verify proposed changes to financial circumstances, however we do not believe a credit provider is able to reliably verify *all* proposed changes to financial circumstances and proposed management plans at the time of application. For example, Parental leave may be verifiable through employer issued documentation, whereas proposed plans to downsize in the medium term is subject to many variables, making it unreasonable to verify.

<u>Personal circumstances</u>

It is very difficult to reliably verify the number, age or type of dependants. As such, we do not think it reasonable that such items are verified. Noting that if the credit provider is on reasonable notice that the disclosed number may not be correct, the credit provider may need to make further inquiries. On the other hand, this is an easy item for the borrower to state reliably and credit providers should be allowed to assume that the consumer will comply with the statutory obligation to not provide misleading information.

The separation of these aspects above reflects the difference between parameters that are likely to cause substantial hardship and those that are not.

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?

If ASIC’s proposed updates outlined in CP309 are implemented in their current form, Macquarie foresees the likely effects on consumers to include:

- Increased application processing time and cost of credit will impact consumers individually and the Australian market more broadly.
- Continued anxiety and frustration from consumers in relation to living expense analysis may deter consumers from seeking credit.
- Reduction in credit products available in the market due to some credit providers not being able to deliver a commercially viable product.
- Certain consumer segments may be disadvantaged where the regulations assume information is readily available. For example, New Australians or Indigenous Australians with limited historical expense information or CCR data.
- Risk of consumers staging behaviours according to defined steps and criteria from ASIC to obtain unsuitable credit, which could lead to substantial hardship.
- Reduced competition as barriers to refinance are increased limiting consumers from seeking to get a better deal.

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.

ASIC's proposed updates outlined in CP309 are likely to affect business costs in the following ways:

- Increased operating costs - due to the increased time to train staff, originate credit and monitor compliance with particular inquiry and verification steps. As an example, Macquarie noted a significant increase in the origination processing time where bank statements were manually reviewed.

- Credit providers are likely to require system development to enable more efficient inquiry and verification.

B1Q8 In your view, what would be the effect (either positive or negative) on competition between licensees? Please provide details.

ASIC's proposed updates outlined in CP309 are likely to affect competition in the following ways:

- An increase in operating costs may make some products less commercially viable for licensees, which could result in a withdrawal of products and reduction of competition in the market.
- Proposed verification steps will favour larger banks with readily available client information. This may see consumers default to their primary bank for convenience rather than seeking better offers from
- The proposed guidance favours technology solutions which may disadvantage some credit providers with less sophisticated systems and more limited resources at their disposal.
- The proposed inquiries would require many consumers to seek assistance to understand credit requirements and manage their application. This may limit direct digital credit providers' ability to engage with this segment of consumers and discourage further innovation in this area.
- Some proposed verification methods (e.g. CCR) will be limited to credit providers and therefore preclude credit assistance providers such as third party brokers from accessing this information. This may have an impact on competition, as consumers may favour using direct lender solutions rather than third party brokers.

ASIC should consider aspects of the lending assessment which have an impact on competition outside of inquiry and verification steps, such as the treatment of interest rate floors between APRA and non-APRA regulated entities. We are concerned that non-APRA regulated lenders are not applying the 7.25% interest rate floor or are considering ceasing to do so.

Enabling differences may result in consumers obtaining higher levels of credit that do not have consideration for future interest rate changes, leading to a higher risk of detriment if interest rates do increase.

C1 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 are readily available in common circumstances; and

(b) clearly state that views on what are 'reasonable steps' will change over time, as different forms or sources of verifying information become available.

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?

Following on from our response in B1Q5, we believe that the following types of information are appropriate and readily available forms of core verification:

Item	**Types of information**
Income	Payslips
	Income tax returns / notice of assessment
	Centrelink statements
	Financials / BAS statements
	Investor portfolio reports
Liabilities	Comprehensive Credit Report
Assets (security to the loan)	Property valuation
	Asset tax invoice

In addition to these, ASIC should include in its guidance:

- A credit provider's ability to simultaneously inquire and verify information through information obtained from comprehensive credit reporting.

- Information types appropriate for Strata Corporations. Macquarie welcomes the opportunity to discuss these with ASIC.

C1Q2 Do you consider that the examples included in Appendix 1 are appropriate? Why or why not?

In terms of Appendix 1, our feedback is as follows:

Table	**Feedback**
Table 1 - Income	Macquarie considers the sources of information listed by ASIC in appendix 1 to be appropriate except for the use of bank statements in most cases. Bank statement are not the most appropriate way to verify income. We see them being used a supplementary document in a small number of circumstances. Payslips provide credit providers with more robust information that is not available on a bank statement including overtime, commissions and year to date income figures. The other documents listed in appendix 1 are appropriate because they are readily available for *individual* consumers, easy for the consumer to understand the reason for collection, contain reliable information and are available to all types of licensees.
Table 2 - Existing debits/liabilities	Credit reports are appropriate for all credit providers to use. Comprehensive Credit Reporting will provide credit providers with reliable information about a consumer's existing debts and liabilities.
Table 3 - Fixed living expenses	These examples are not appropriate forms of verification. Refer to B1Q5 (living expenses).
Table 4 - Variable living expenses	
Table 5 - Overall financial situation	As noted above and in B1Q5 bank statements do not provide a reliable or effective means for credit providers to verify a consumer's overall financial situation.

Appendix 1 should differentiate what is reasonable for a credit provider to obtain compared to a credit assistance provider.

C1Q3 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.

Macquarie is supportive of the value of data aggregation services in the credit assessment process and of continued innovation in this area. Some additional consideration should be included to acknowledge the following:

- **ePayments Code conflict** – The guidance should include ASIC's views on the use of these services, taking into consideration the current conflict with the ePayments code and ADI's terms and conditions for banking accounts and the sharing of account details and passwords.

- **Interpretation of data** – where transactions are non-specific or defined in different categories between services (e.g. cash out at an ATM in a specific location) this could lead to further intrusive questioning or unfair assumptions of expenditure. ASIC should articulate the expected treatment of all transactions and their categories.

- **Use of summary data** – where a summary of a consumer's financial profile is provided by a data aggregation service, ASIC's guidance should confirm, that subject to there being no risk indicators in the summary, credit providers do not need to have regard to the line by line information that the summary is based on.

The tools and technology available to establish transaction data are in the early stages of significant change. The Australian Government has committed to implementing Open Banking reforms that will require major banks to make data available (with a consumer's authorisation) on credit and debit card, deposit and transaction accounts and mortgages no later than February 2020. Data on all products recommended by the Review will be available by 1 July 2020. All remaining banks will be required to implement Open Banking with a 12-month delay on timelines compared to the major banks.

Macquarie Group has been at the forefront of Open Banking and believes that the Open Banking initiatives will provide significant opportunities for efficiently accessing transaction data of prospective borrowers where necessary, and for the development and evolution of systems to analyse transaction data. However, an effective and efficient use of Open Banking is in our view still many years away.

The implementation of Open Banking is relevant to the practical effect of an increase in the extent to which lenders must verify expenses by reference to transaction data statements.

At present, the burden of locating and providing bank statements falls on a consumer unless all of their accounts are held with the proposed lender. The desirability of avoiding this burden is likely to increase the relative attraction of borrowing from one of the major banks, which more consumers will bank with and which are more likely to hold all of a consumer's accounts.

Open Banking ought to help level the playing field between major retail banks and others by reducing the significance of this point of difference, however this presumes the consumer is willing to share their data and they accurately disclosure all their banking relationships.

Macquarie submits that any change to responsible lending obligations that increases the extent to which lenders must have regard to bank statements should be synchronised with the implementation of Open Banking and the development and evolution of systems to analyse transaction data made accessible by Open Banking.

This ought to make it easier for both borrowers and lenders to deal with the verification of expenses and minimise any adverse effect on competition.

Further, in making any change, due regard should be had to both the difficulty of verifying expenses by reference to bank statements and the potential inconclusiveness of the process.

Some factors of relevance in considering those issues include[2]:

(b) The amount of data to be collected and analysed would be considerable – there are currently:

- approximately 37 million debit card accounts and 16 million credit and charge card accounts in Australia (implying an average of about 2.65 accounts per person or 5.3 accounts for a couple).

- approximately 240 million credit card and 568 million debit card transactions per month in Australia (implying an average of 485 transactions per person per annum or 970 transactions for a couple per annum).

(b) The transactions recorded may not provide a complete or conclusive view of the expenses incurred by the consumer[3] as:

- The consumer may not provide access to all accounts held by them.

- The transactions will not reveal how any cash withdrawals are spent. Where a withdrawal is in cash (there are approximately 50 million withdrawals valued at over $11 billion per month in Australia at ATMs alone) there will be no meaningful information about how the cash was spent.

- Interpreting or deciphering what particular entries relate to is difficult and time consuming.

- It will often not be possible to assign particular transactions to categories that reflect the distinction between necessities and discretionary expenditure, for example a credit card purchase at a department store could be for food staples, clothing or whitegoods.

(c) Unless the lender is to rely on the consumer's assurance that the account statements provided record all the consumer's expenses, it will also be necessary to reconcile the expenditure with the consumer's opening and closing balances and income. The difficulty of doing that will be compounded in many circumstances, for example where a couple with separate bank accounts and incomes are applying jointly for a loan, or where a person is applying for a loan when they hold a joint account with their partner.

As noted above many expenses are discretionary and subject to change limiting the value of verification.

[2] Reserve Bank of Australia Payments Statistics (https://www.rba.gov.au/payments-and-infrastructure/resources/payments-data.html) accessed 25 October 2018.
[3] Assuming there are approximately 20 million Australians over the age of 15

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**
- **(b) including an 'if not, why not?' approach**

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?

Yes, this type of guidance would be useful as it will ensure consistency of approach across the industry.

ASIC will need to include guidance on appropriate 'if not, why not' examples to ensure consistency in approach is maintained.

C2Q2 Would an 'if not, why not' approach encourage improvements to current verification practices? Why or why not?

Yes, however there is level of subjectivity to an 'if not, why not' approach. Without appropriate guidance, some credit providers may continue to use the 'why not' approach to maintain current processes.

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)?

This question is answered in B1Q6 where Macquarie outlines the effect specific steps of verification would have on consumers.

C2Q4 What additional business costs would be involved in this approach?

This question is answered in B1Q7 where Macquarie outlines the increased costs involved with the proposed approach.

C2Q5 In your view, what would be the effect (either positive or negative) on competition between licensees? Please provide details.

This question is answered in B1Q8 where Macquarie outlines the effect on industry competition.

C3 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:

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**

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.**

C3Q1 Do you consider that the proposed clarification of guidance about use of benchmarks would be useful? Why or why not?

Macquarie considers the proposed guidance would be useful and will incorporate the guidance from REP445 in relation to income adjusted benchmarks into the new RG209. Given Macquarie already applies income and demographic based variables to benchmarks we do not consider this will require further buffering.

ASIC should be explicit where benchmarks used for plausibility could be relied upon in an assessment. Furthermore, ASIC should provide guidance on:

- Setting the benchmark, implementation of the most up to date and applicable versions, clarification of attributes to be included and how to apply across different household compositions. E.g. sole borrower vs joint borrowers.
- What threshold comparative to HEM would require a credit provider to make further inquiries and verifications.

This will eliminate the wide range of differences in HEM usage between credit providers and ensure a prudent standard for assessing consumer applications.

Credit providers use the HEM benchmark in serviceability assessments, in circumstances where a consumer may have understated or underestimated their living expenses. The circumstances in which the HEM benchmark is used by credit providers is consistent with the obligation to conduct an assessment to ensure that a consumer is not likely to experience substantial hardship.

HEM is built from Household Expenditure Survey data conducted by the ABS and is indexed to income, marital status and number of dependents. The Melbourne Institute paper notes that HEM is an inclusive measure and allows for median spending on non-discretionary items and a level of discretionary spending. The HEM benchmark therefore identifies a realistic base level of spending for consumers based on their income and family composition.

Macquarie recognises that a reasonable proportion of consumers can and do spend in a 'low budget' manner. ASIC should include where this is acceptable in their updated guidance.

C3Q2 Please provide information on what buffer amounts you currently apply, or would otherwise consider to be reasonable.

Macquarie currently applies the following buffer concepts to consumer living expenses:

- **Welfare floor on HEM tables** – where income levels are below the welfare level of income then the HEM figure used for comparison with declared living expenses is derived from the income adjusted HEM at the welfare level. Effectively, this floor replaces any lower HEM value.

- **Cash surplus buffer** – built to represent unexpected costs and can range from $0 to $180 per month depending on consumer circumstance and product. Some exclusions apply where the consumer has demonstrated they have capacity to absorb unexpected costs, e.g. savings or cash surplus

- **Rental/Boarding cost floor** – a minimum cost for board or rental expense, ranging from $250 to $650 per month depending on customer circumstance and product is applied to ensure consideration is given to a required living cost. This applies even in circumstances where the consumer is not currently paying board – e.g. living with parents.

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)?

This question is answered in B1Q6 where Macquarie outlines the effect specific steps of inquiry and verification would have on consumers.

Where ASIC does not recognise a consumer's ability to live in a 'low budget' manner, this may disadvantage the consumer by applying higher expenses and reducing their ability to borrow.

C3Q4 What additional business costs would be involved in this approach?

This question is answered in B1Q7 where Macquarie outlines the increased costs involved with the proposed approach.

C4 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).

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?

Whilst additional guidance on the consumer's requirements and objectives would be beneficial, we suggest that the proposed guidance should be reconsidered to cater for different products.

Home Loans

We believe that the implementation of the Combined Industry Forum (CIF) Broker Interview Guide (BIG) across the home loan industry would be sufficient to address a consumer's requirements and objectives for Home Loan products.

Credit Cards & Auto Loans

We believe that the same level of inquiry is not required for Credit Cards and Auto Loans. Many inquiries required under the BIG could lead to decision fatigue and consumers adding features that cost more, that they do not understand or that they think are more likely to lead to an approval. These behavioural biases have been described in ASIC's Report 470 about the sale of add on insurance.

We suggest that where a consumer has chosen the basic features of these products, no further inquiries are required. Where a consumer chooses a product or feature with additional cost or risk (e.g. balloon repayments or a high annual fee credit card), a credit provider could provide additional information about these costs and risks and confirm the consumer wishes to proceed with the product and / or feature.

We recognise this approach may encourage some consumers to apply for lower risk / lower cost products as a 'path of least resistance'. We do not, however, consider that this creates a material risk of consumer detriment.

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)?

This question is answered in B1Q6, where Macquarie outlines the increased costs involved with the proposed approach.

In addition, where requirements and objectives are not scaled by product as proposed above we consider there is a risk of consumers choosing features which they do not understand or think they are more likely to lead to an approval. This would result in an unsuitable product being given to the consumer.

C4Q3 What additional business costs would be involved in this approach?

This question is answered in B1Q7, where Macquarie outlines the increased costs involved with the proposed approach.

D1 We propose to include new guidance in RG 209 on the areas where the responsible lending obligations do not apply.

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.

- Where Macquarie receives an application with multiple loan purposes and the predominant purpose is regulated by the NCCP Act, it will apply responsible lending obligations to all facilities in that application. This results in portions of the application being subjected to responsible lending criteria which would not have applied had they been applied for separately.

  For example, where a consumer wishes to use their current home loan and obtain an equity release to purchase a smaller business asset.

- In our Business Banking division, individuals may apply for a business purpose loan (e.g. purchase a commercial asset) and seek a redrawable facility or a line of credit to fulfil this contract. Macquarie collects a business purpose declaration and supporting evidence from the consumer to support their application. This would support the loan not being included in RL regime as at the time of assessment, they did not meet the NCCP threshold.

  However, given the consumer may redraw funds and use them for personal use, which may result in the loan being used predominantly for domestic use for an individual, Macquarie treats these redrawable business loans as regulated by the NCCP, even though at origination they would be out of scope. Macquarie seeks clarity from ASIC on the treatment of these loans to ensure appropriate flexibility is available in servicing small business clients

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.

No, there are no forms of small business lending where we are unsure if responsible lending obligations apply.

D2 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

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

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?

Yes, specific guidance about loan fraud and the impact on responsible lending would be useful. We believe the guidance would ensure consistency across the industry and assist in reducing the risk of consumers entering unsuitable credit contracts as a result of fraud.

Specific examples of loan fraud would help clarify the differences between disclosure oversights and genuine fraud. For example, falsified identity or income verification documents compared to common rounding errors on living expenses or liabilities.

ASIC should reconsider the use of high arrears rates of loans introduced by certain brokers as an indicator of fraud, as in our experience this is not a sole indicator of a fraudulent application.

We have included additional triggers in D2Q2 which ASIC should consider for this purpose.

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.

We consider the following risk factors to be useful in relation to identifying application fraud:

- Over reliance on HEM and / or consistent over representation of similar expense figures across applications or living expense categories.
- Templated responses to free text fields such as product features or requirements and objectives.
- Anomalies in disclosure when compared to consumers of a similar profile in the credit provider's portfolio (e.g. age, marital status).

Not all risk factors should be considered as an automatic trigger to obtain further verification information from consumers. We also consider it important for credit providers to be able to identify risk indicators and to conduct investigations on an intermediary's processes and determine whether the information was genuine.

When a credit provider has completed an investigation and still has concerns about the validity of the information provided additional verification steps could include:

- conducting employment references;
- obtaining additional payslips and / or tax returns; or
- collecting credit references.

We would also encourage ASIC to provide guidance on what remedial steps may need to be taken if a credit provider identifies fraud perpetrated by the person who assisted the consumer to apply for a loan. Both in instances where the consumer was involved in the fraud and where they were not.

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)?

Benefits

Consumers will benefit if intermediaries and staff of credit providers engaging in fraudulent activities are identified quickly and removed from the industry.

Risks

There is a risk that some indicators may cause assessment bias and disadvantage consumers dealing with a particular broker. Further risks exist to consumers if credit staff or brokers are able to move between aggregators or credit providers without a robust way to highlight fraudulent or potential fraudulent behaviour to new employers.

Costs

This question is answered in B1Q6, where Macquarie outlines the increased costs involved with the proposed approach.

D2Q4 What additional business costs would be involved in this approach?

This question is answered in B1Q7 where Macquarie outlines the increased costs involved with the proposed approach.

D3 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**
>
> **(b) this information should instead trigger the licensee to make more inquiries to enable them 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.**

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?

Yes, we think that guidance on the topic of hardship indicators would be useful. It will be important to distinguish between hardship indicators and arrears information.

We believe hardship indicators should generally lead to further inquiry and ASIC's guidance would assist credit providers in not refusing further credit. However, for arrears indicators Macquarie may still refuse applications for further credit products where it does not present a good consumer outcome.

ASIC should provide guidance on which RHI indicators it considers would generally result in a credit contract being unsuitable. This has previously been provided by way of prescribed regulations for Small Amount Credit Contracts.

ASIC should also provide additional guidance on how credit providers should approach Consumer Credit Liability Information (CCLI) as credit providers are likely to use CCLI to verify a consumer's liabilities.

Macquarie would welcome further guidance on:

- **Under disclosure**: ASIC should allow for tolerances in under disclosure, when comparing the comprehensive credit report with the consumer's declared liabilities, without the need for further inquiry if the consumer is still able to service the loan using the higher amount; and
- **Simultaneous inquiry and verification of liabilities**: This should include that simultaneous inquiry and verification is consistent with a credit provider's responsible lending obligations.

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)?

Consumers are likely to have a better understanding of how late repayments and under disclosure have an impact on their ability to obtain credit, resulting in consumers taking more control of their financial lives.

D3Q3 What additional business costs would be involved in this approach?

This question is answered in B1Q7 where Macquarie outlines the increased costs involved with the proposed approach.

D4 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.

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?

Yes, this type of guidance would be useful for licensees if the guidance is expanded to consider products other than interest only home loans (as contemplated in REP493).

This guidance should be technology neutral and recognise that many application forms, 'fact finds', 'needs analysis' and assessment notes and documents are online and collected and updated throughout the assessment process.

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.

We consider these practices to be generally appropriate for licensees if the obligations remain scalable based on product and customer profile.

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)?

This guidance will assist credit providers in ensuring they are meeting ASIC's expectations in relation to record keeping. Depending on the finalised scope there may be increased costs and time to access credit if credit providers need to significantly change their processes and / or hire more staff.

D4Q4 What additional business costs would be involved in this approach?

This question is answered in B1Q7 where Macquarie outlines the increased costs involved with the proposed approach.

D5 We propose to provide additional guidance in RG 209 on what information we think should be included in a written assessment.

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?

Yes, this guidance would be useful to credit providers.

Whilst we consider this guidance would be useful to avoid uncertainty in relation to a licensee's obligations we have concerns with including information the licensee has decided it cannot rely on. Providing this information to consumers could divulge sensitive commercial decision-making information such as the licensee's serviceability models and thresholds. This in turn may encourage consumers to provide information in future credit applications which is in line with these buffers or floors, even if the consumer's actual expenditure is higher.

We would suggest that this item be removed from the example in Appendix 2.

If ASIC feels it is necessary to have this information in the assessment, we think further and specific guidance is needed about the extent this part of the written assessment applies. For example, if a consumer has been a customer for 20 years, do we need to advise them that we have only used the last year worth of transaction data as opposed to 20 years.

We would expect that ASIC guidance should only apply to credit contracts entered into after the guidance is released. This will allow for the appropriate system changes and training to be completed.

D5Q2 Please provide any comments on the example set out in Appendix 2.

In addition to the points we have raised in D5Q1, we have comments on the below items in Appendix 2:

Dependants	The type and age of dependants does not change the outcome of the assessment or expense treatment when using living expense benchmarks. We do not think this information is reasonably needed for all applications.
Requirements & Objectives	Please see our response to C4Q1 on the level of information in this example as it comes to requirements and objectives

RG209 should be clear that the form of Appendix 2 relates only to the requests made by consumer for copies of their written assessment and does not apply to the assessment made by credit providers at the time of approving the loan. We see minimal value in credit providers undertaking significant development of systems to report information in the form of Appendix 2 outside of requests received from consumers e.g. "type of verification document"

D5Q3 What are the benefits, risks and costs for consumers in this approach (including any effect on access to and cost of credit for consumers)?

Benefits
Consumers will obtain the same form of written assessment from any credit provider that they request this document from.

Risks
We are concerned that the level of information in the example is not collected for all products. Any new guidance ASIC includes in the updated version of RG209 should not apply to credit contracts entered into prior to the update.

D5Q4 What additional business costs would be involved in this approach?

This question is answered in B1Q7 where Macquarie outlines the increased costs involved with the proposed approach.