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Australian Securities and Investments Commission

By Email to: responsible.lending@asic.gov.au

Dear Ms. Grey,

Consultation on updates to RG 209 (Credit licensing: Responsible lending conduct)

Thank you for the opportunity to comment on the Australian Securities and Investments Commission's (ASIC) Consultation Paper 309 (CP 309) in relation to its proposed updates and changes to Regulatory Guide 209: Credit licensing: Responsible lending conduct (RG 209).

The Commonwealth Bank of Australia (CBA) supports the responsible lending regime. It serves a critical role in the financial system, primarily by ensuring customers can safely access credit and have transparency and consistency around how their applications for credit will be dealt with by credit providers.

CBA has recently taken steps to improve their approach to complying with regulatory and community expectations in relation to responsible lending. For example, CBA has enhanced its approach to inquiries and verification steps by introducing a mandatory expense breakdown for some credit products, updating the bank's serviceability calculators, increasing the number of expense fields in application forms, updating the bank's systems to better identify customers' liabilities with other financial institutions, and introducing written assessments to customers at the time of origination for some credit products.

CBA is supportive of ASIC's proposal to update its guidance to ensure that RG 209 is clear, practical, effective and consistently applied across the industry. CBA has contributed to a number of the submissions of industry bodies. This letter sets out CBA's specific perspectives on a number of the more critical issues raised in CP 309. CBA welcomes the opportunity to discuss these issues further, prior to the release of the updated guidance, and would also advocate for appropriate timeframes to allow industry to uplift and implement any changes to systems, processes and training that will be required to meet the new regulatory standards.

1. Additional guidance on reasonable steps to inquire and verify (proposal B1)

CBA is supportive of more prescriptive guidance regarding the steps ASIC considers 'reasonable' to inquire about, and verify a consumer's financial situation. Greater clarity and specificity ensures customers experience consistency in steps taken regarding their credit applications, levels the playing field and reduces ambiguity faced by regulated entities when seeking to meet responsible lending obligations.

In developing more specific guidance for industry, CBA encourages ASIC to consider two key factors when considering the required depth of inquiry and verification. First, the level of inquiry should be proportional to the potential customer detriment, which is based on factors such as loan size, assessed probability of default and customer experience in repaying debts of a similar type and size. This will minimise complexity, delays in processing, and burdens upon the customer through the application process when the likelihood of subsequent hardship is low. Second, the extent to which a customer's declarations of their financial situation deviates from expected ranges for their given characteristics should be a prompt for licensees to conduct deeper inquiry. That is, where a customers' stated living expenses are below expected levels when considering the income-scaled Household Expenditure Measure (HEM), further review and inquiry should be undertaken. Conversely, when customer stated living expenses are near or above the income-scaled HEM figure, there is limited need for additional further inquiry.

Other instances where there may be reduced expectations of deeper inquiry include high net-worth individuals where product suitability is assessed based on their total asset position, products held and business interests (i.e., noting that Private Banking customers are assigned dedicated relationship managers to oversee their personal and business finances holistically), and instances where customers are seeking to refinance or restructure their existing facilities within the same credit provider, rather than seeking additional credit (e.g., shifting to a lower interest rate loan with the same limit and term).[1]

CBA notes that customer behaviour post-obtaining a new loan can lead to moderation in their discretionary expenditure profile. This is common where first home buyers may choose to eat out less relative to their position when they were renting, or living with parents. Clarification from ASIC on the reasonableness of accepting credit applicants' proposals on reduced expenditure, and the level of inquiry and record keeping expected would be valuable. Guidance on this aspect would need to consider practical issues, namely, whether it is reasonable to allow an applicant to reduce their living expenses based on the information they have provided, and whether the licensee is expected to make value judgments on whether an applicant is likely, in fact, to actually reduce their expenses.

CBA recognises the limitations of verifying certain types of expenses as explored in the ABA's submission. Accordingly, in instances where a deeper level of inquiry is required, for example, where customer-declared expenses are below expected ranges based on their personal circumstances, CBA would welcome regulatory guidance that requires a strong level of inquiry for living expenses (e.g., obtaining a relatively granular break down of expenses by common categories), followed by further reasonable inquiries (e.g., appropriate follow-up questions to the customer and recording of answers). Consistent with this approach, CBA is investing in solutions to enhance the accuracy and granularity of customer declarations (e.g., digital spend tracking tools). CBA believes that this approach appropriately balances the need for due diligence on a licensee's part and the practical limitations of assessing a customer's future expenses.

[1] Note that the UK Financial Conduct Authority (FCA) is currently considering changes to its rules "to reduce regulatory barriers to consumers who are up-to-date with payments and not looking to borrow more switching to a more affordable mortgage". ASIC should consider findings from the FCA's consultation (CP19/14) in determining a safe level of inquiry and verification for existing customers which ensure that they are not deterred from restructuring their financial circumstances due to overly complex, lengthy processes.

2. Information to be used to verify a consumer's financial situation (proposal C1)

CBA agrees with ASIC's comments that certain developments such as open banking and comprehensive credit reporting (CCR) will enable licensees to "efficiently confirm the financial situation of a consumer" by "allowing simultaneous inquiry about and verification of some information"[2]. However, CBA would welcome ASIC's consideration of the following when updating RG 209, to ensure industry participants can easily transition to meet regulatory expectations and respond to technological developments:

- Guidance should continue to be technology-neutral and ensure that certain customer segments are not inadvertently limited by their choice in sharing information. Accordingly, ASIC should also consider the need to educate consumers on their rights and the benefits of sharing their data with regulated entities when applying for credit to supplement ongoing industry education efforts.
- Updated guidance should clearly set expectations on how licensees should reasonably access customer data for the purposes of inquiry and verification, whilst maintaining the customer's rights and expectations of privacy. CBA would welcome further clarity on how licensees can practically ensure that they only collect and use information that is required for the purposes of an assessment of affordability, and no other purpose. Clarity would also be valuable on how third-party liabilities and expenses (e.g., under joint accounts) may be verified whilst upholding the privacy rights of non-applicants.
- CBA has consistently expressed its concerns with tools that extract information from customers' online banking platforms[3]. CBA believes such services to be highly risky as they may invalidate privacy and data security protections by asking a customer to provide their banking log-on details, and using and storing the customer's data on third-party systems. CBA believes that the risks associated with such tools are often unknown or unclear to the customer, and as such, does not support the use of these services.

3. Reasonable verification steps and the 'if not, why not' approach (proposal C2)

CBA supports ASIC's proposals aimed at bringing greater clarity and guidance around 'reasonable steps' for verification. Whilst CBA is supportive of uplifting industry practices to require consideration of all relevant and accessible pieces of information about a customer's financial circumstances, CBA would encourage ASIC to consider the practical implications of complying with the 'if not, why not' proposal. CBA suggests ASIC develop guidance that expressly articulates:

- the level of inquiry that a licensee undertakes should be proportional to the potential customer detriment or extent to which customer-declared finances deviate from expected ranges or benchmark figures;
- a reasonable time period that licensees should look back to when examining a customer's financial circumstances;
- factors that ASIC considers 'reasonable' for a licensee choosing not to consider or use information that it had access to; and
- how licensees can verify information in certain complex circumstances (e.g., where an individual has applied for a loan and has a joint account with a non-applicant).

4. Clarification on industry use of benchmarks (proposal C3)

CBA supports ASIC's suggestion that whilst benchmarks should not be used as the sole method of positive confirmation of an applicant's income and expenses, they can be used as a tool to determine plausibility of the information provided by an applicant. CBA considers

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[2] CP 309 Proposal C1(b)

[3] CBA has expressed its concerns with such services through ongoing consultations and industry discussions with Government and regulators on the Consumer Data Right.

benchmarks, particularly HEM, to be a key determinant in whether deeper inquiry is warranted for a customer. This approach is consistent with recent commentary in the Royal Commission Final Report and the bank's intention to reduce its reliance on HEM as it improves its collection and assessment of customers' actual financial behaviours.

As such, CBA welcomes the proposal to clarify the role that benchmarks should play in the verification stage as this will standardise the use of benchmarks across industry players and allow customer transparency as to how their applications will be assessed. A consistent approach may also lead to an increase in consumer confidence in the suitability of the product they are applying for, as the assessment of their expenses will be based on information closest to their personal circumstances. As mentioned in proposal C3(iii), the need for standardisation across industry should also be extended to ASIC's expectations on licensees to regularly update their benchmark data. CBA believes that a review of benchmark figures every six months would be reasonable.

ASIC also suggests that additional steps be considered in relation to the use of benchmarks, including the use of a buffer. CBA encourages further consideration of the application and risks of introducing buffers, given some participants already apply buffers to their serviceability assessment practices (e.g., requirements in APG223 to add buffers of at least 20 per cent to most types of non-salary income such as rent and buffers applied to benchmark interest rates applied in the servicing assessment). A more appropriate approach could be to encourage licensees to lower their reliance on benchmarks (e.g., as a proportion of total credit applications received). Requiring licensees to apply a buffer may in fact, increase licensees' reliance on benchmarks, as they become a more conservative figure to rely on.

5. **Clarifying the scope of responsible lending obligations (proposal D1)**

CBA welcomes the proposed clarification that small business lending is outside the scope. Whilst the *National Consumer Credit Protection Act 2009* (NCCP Act) explicitly states that it extends to the provision of credit to individuals and strata corporations wholly or predominantly for personal, domestic or household purposes, or for investment in residential property, CBA notes that some small business customers are captured under the regime due to the nature of their operations and enterprise, thereby impacting their access to business credit. CBA has experienced a number of scenarios where there is not an objective measure to determine 'predominant purpose' or where, by definition, business customers are captured under the NCCP Act, thus impacting their ability to access credit. Common scenarios include:

- small business owner aiming to borrow funds to either purchase and/or refurbish a newsagency with joint residential premises attached above the shop, therefore the mixed commercial/residential use adds complexity and judgment whether it is predominantly business or not (noting that this scenario extends to a range of business operations);
- business sole trader undertaking property investment as a going concern business activity. Although falling below the $5 million threshold as per the NCCP Act, this does not always represent what is predominantly a business activity;
- purchasers of rural properties whose supplementary business income is commercial in nature and operated as a business for tax purposes, but is not their primary place of residence; and
- boarding house owner / purchaser where the loan purpose is residential investment yet is run on a going concern basis.

CBA requests guidance whether it is reasonable in these circumstances to rely upon the customer's declaration that the lending is predominantly for business purposes, thus acknowledging the loan will not fall within the scope of the NCCP Act. CBA is supportive of maintaining this distinction given the ABA's new Banking Code of Practice includes protections for small business customers. Any future guidance will avoid duplication or unnecessary complexity amongst these industry standards, and ensure customer confidence in the protections afforded to them by law and industry codes.

6. Record-keeping and written assessments (proposal D4 and D5)

CBA is supportive of ASIC's intent to uplift industry practices to drive conscious consideration of how a licensee is meeting their responsible lending obligations, and to provide customers with transparency on how their information has been used to arrive at decisions. CBA believes that customers' financial literacy and wellbeing can be enhanced by having access to clear, simple communications from financial services providers as to how they arrive at decisions, and what actions can be taken to align customers' circumstances with their needs and goals.

CBA encourages ASIC to set out the minimum aspects that it believes customers should have visibility of (e.g., facility purpose, amount sought, term, employment status, income, liabilities, and changes in personal circumstances that have been discussed which are likely to impact serviceability) but allow licensees to innovate on the format and manner in which assessments are developed in their respective systems and processes. Should ASIC include a prescriptive, comprehensive template similar to Appendix 2, CBA encourages conducting customer testing and research prior to releasing an updated RG 209, to ensure to the guidance aligns with customer needs and expectations of simple, short product and service disclosures.

CBA looks forward to further clarity on these core aspects of ASIC's responsible lending guidance. If you require further information in relation to any of the matters raised in this submission, please do not hesitate to contact myself or Mohini Tiwari on or at .

Yours sincerely

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