HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON ECONOMICS

REVIEW OF THE FOUR MAJOR BANKS

NAB

NAB44QW:

In the context of an exchange that occurred during the House of Representatives' Standing Committee on Economics' hearing with the Reserve Bank Governor and the Member for Mackellar on 14 August 2020:

> Mr FALINSKI: And I congratulate you for drawing attention to something that people have deliberately ignored for too long, but while we're on the point of bad regulations and unintended consequences, we, the federal parliament, introduced not long ago responsible lending obligations, which essentially have the principle that the lender is responsible for decisions that the borrower makes. Is it your evidence to this committee and to the parliament that that law is not having any impact on credit creation and lending to small business and to those enterprises that are taking a risk in starting new enterprises?
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> Mr Lowe: That's not my evidence. I think it is having an effect. Just to go back to the legislation the parliament passed, which at a very high level is eminently reasonable, it says that, when extending credit, the loan can't be unsuitable—who could argue with that?—and in making the loan you've got to take reasonable steps that the borrower can repay. Well, who could disagree with those two broad principles? I find it very hard to disagree with them. What has happened is that those principles have turned into hundreds of pages of guidance. Once the compliance people, the lawyers, the regulators and the media get involved, these high-level principles put in law get turned into a lot of guidance, because people don't want to offend these kinds of regulatory requirements.
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> Mr FALINSKI: Can I humbly put it to you that you're being very generous. Wasn't it the interpretation of the courts, until the recent ASIC v Westpac case, that what this actually did was put the obligations back on lenders to understand absolutely and completely the capacity of borrowers to service a loan? That's why it turned into hundreds of pages and, when this was tested before the courts, especially the lower courts, that's what they found. I guess that's why we say the principle makes sense but the unintended consequence was that it restricted lending in the Australian capital markets.
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> Mr Lowe: I agree with you. I think the principles in the legislation are sound, but I think the way we've translated those principles into reality needs looking at again. If we can't do that properly, maybe we need to look at the legislation. We can't have a world in which, if a borrower can't repay the loan, it's always the bank's fault. On a portfolio basis, we want banks to make some loans that actually go bad, because if a bank never makes a loan that goes bad it means it's not extending enough credit. The pendulum has probably swung a bit too far to blaming the bank if a loan goes bad, because the bank didn't understand the customer; if it had done proper due diligence—this is the mindset of some—the bank would never have made the loan. So some of the banks have had this mindset, 'Well, we can't make loans that go bad.' I would have to say, though, that in the past three or four months I've heard fewer concerns from the banks about the responsible lending laws. ASIC introduced new guidance. Institutions are gradually coming to grips with those.

Mr FALINSKI: That might be because, under the extraordinary powers we granted the Treasurer, he has given them relief from RLOs.

a) Can you advise whether the Governor of the Reserve Bank of Australia's views reflect that of your institution?

NAB takes its responsible lending obligations seriously and assesses all loan applications based on a range of measures to ensure customers can appropriately manage repayments.

RLOs are not the only consideration for NAB in relation to credit applications; there are additional requirements, such as prudential requirements and the Banking Code of Practice, which NAB must ensure loans comply with. These requirements impact the information NAB is required to obtain from a customer, the time taken to verify the information and the time taken to service a customer (not only during application stage).

The amalgamation of all requirements has resulted in protracted application processes and subsequent processing times. There are a number of overlapping regulation regimes, which causes complexity and uncertainty. Further clarity and consistency would help to ensure compliance with all requirements, without hampering the lending process.

b) Do you agree with the principles established in legislation on responsible lending obligations? If not, which principles and why?

Yes. Responsible lending principles aim to ensure consumers are protected in the extension of consumer credit.

c) Are there any principles in the legislation that you believe could be amended or replaced that would better enable the bank to provide credit?

Principles relating to the depth of enquiry and verification do increase the time taken and cost to extend credit, and do not always result in a corresponding increase in consumer protection. These could be amended.

Examples of this include:

- Requirements to enquire about and verify shared expenses with parties which are not involved in loan applications;
- The requirement to conduct in-depth verification of expenses; and
- The subsequent industry-applied standard that past expenditure behaviour is a key input into the affordability of a loan (noting ASIC has clarified that it is acceptable to consider discretionary expenses that a customer is willing to forego after the loan contract is entered into).

d) Do you agree with ASIC's guidance notes for the implementation of responsible lending obligations? If not, which sections do you disagree with, and why?

The subjective nature of responsible lending obligations allows for multiple interpretations of requirements. ASIC's updated RG209 guidance provides further clarity on responsible lending obligations and NAB believes the guidance is adequate in most cases. The additional examples in ASIC's updated regulatory guide on how responsible lending obligations are applied in practice have been well received.

NAB remains supportive of the concept of scalability in RG209. Scalability allows credit providers to tailor systems and processes to achieve appropriate customer outcomes. It also gives credit providers flexibility to innovate in relation to customer experience, whilst still meeting responsible lending obligations.

e) Are there any sections in ASIC's guidance notes for the implementation of responsible lending obligations that could be amended or replaced that would better enable the bank to provide credit?

NAB is comfortable with ASIC's guidance notes. NAB believes it has sufficient information to make the decisions required to continue to lend responsibly to customers.

There are instances where the requirements of APRA and ASIC do not align, which has the potential to erode efficiencies. An example of this is when a home loan customer switches from a principal and interest repayment basis to an interest only basis; ASIC guidance indicates variations to existing credit contracts should not trigger an assessment, however APRA's guidance in APG223 states that a serviceability assessment is required. In these circumstances, NAB therefore requires a customer to complete the same standard assessment that a new customer taking out a new loan would undertake.

f) Do you agree with APRA's guidance notes for the implementation of responsible lending obligations? If not, which sections do you disagree with, and why?

Broadly, NAB agrees with APRA's guidance as it promotes prudent lending. There are some discrepancies between the guidance provided by APRA and ASIC that have prevented NAB from implementing changes to its consumer lending process.

g) Are there any sections in APRA's guidance notes for the implementation of responsible lending obligations that could be amended or replaced that would better enable the bank to provide credit?

When comparing the obligations set by ASIC and APRA, examples of key differences include:

- ASIC has stated that scaled serviceability assessments based on a customer's risk of harm are acceptable, however APRA has not made such a determination. As a result, NAB has not implemented material changes to its processes.
- ASIC has stated that variations to existing loan contracts that do not result in a new contract or increased credit limit will not trigger responsible lending obligations (i.e. a subsequent assessment). However, APRA has stated that certain changes to existing loan contracts will require a further assessment. These include:
    - changes to existing loans from a principal and interest repayment structure to an interest only repayment structure; and
    - changes from a fixed rate to variable rate basis (or vice versa).
- As a result, minimal changes have been made to NAB's processes.

ASIC has indicated that asset based serviceability (i.e. accepting proceeds from the sale of assets) is an acceptable form of servicing, however this serviceability is not viewed as a standard repayment type under prudential guidance. NAB is therefore required to treat this as non-standard lending, which may require additional capital allocation or shading.

h) Have there been any unintended consequences resulting from the rulings of courts or tribunals that have applied strict interpretations of responsible lending obligations?

No.

i) Have there been any decisions of courts or tribunals, such as AFCA, that you have chosen to appeal? If so, please provide details.

No.

j) Have you removed any products as a result of responsible lending obligations?

Product removal decisions consider a range of inputs, of which the cost of compliance and consumer outcomes are key factors. Products, processes and credit policies continue to be developed, enhanced and rationalised.

k) Since 2008, what debt products have you removed from your product list as a result of responsible lending obligations?

Debt products have not been removed from NAB's product list as a direct result of responsible lending obligations.

Since 2008, NAB has removed low documentation (non-standard) home loans and interest only home loan products which trigger a balloon payment at the end of the interest only period from sale. These products would not satisfy responsible lending obligations.