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Dr Richard Grant
Acting Committee Secretary
Senate Economics Legislation Committee
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Parliament House
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Dear Dr Grant,

Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011 (First Enhancements Bill)

The Australian Bankers' Association (ABA) is pleased to have the opportunity to provide comments to the Committee on this First Enhancements Bill.

The ABA has provided the same submission to the Parliamentary Joint Committee on Corporations and Financial Services earlier this week in anticipation of Joint Committee hearings on 24 October. The ABA will be participating in the hearings.

The ABA is the peak national body representing banks (other than mutuals) that are authorised by the Australian Prudential Regulation Authority to carry on banking business in Australia. The ABA's membership of 23 banks comprises the four major banks, former regional banks that now operate nationally and foreign banks that are represented and carry on banking business in Australia as Australian banks.

1. Introductory comments

1.1 General context

The ABA believes that the First Enhancements Bill should be considered in the context of the Government's other consumer credit reforms.

The Government's and the Council of Australian Governments' (COAG) credit regulatory reform program has been, and continues to be, comprehensive and time consuming for industry. The reforms are moving at a pace at odds with the significant regulatory burdens they impose on industry. In the ABA's view, the fast-tracked pace of the reform program fail to take sufficient account of industry's need to implement these reforms in orderly and workable timeframes.

The First Enhancements Bill is the first of two enhancements bills proposed to be legislated over the next 12 months. In fact, the First Enhancements Bill follows the National Consumer Credit Protection Amendment (Home Loans and Credit Cards) Act 2011 (Home Loans and Credit Cards Act) that was enacted on 4 July 2011 and amends the National Consumer Credit Protection Act 2009 (NCCP Act) The second enhancements bill is being prepared for introduction and passage in 2012. Consultation on this Bill is expected to commence in November 2011. This Bill is likely to cover reforms in relation to the following topics: extending the NCCP Act to products that are currently unregulated (home reversion schemes, exempt leases, solicitor lending and peer-to-peer lending), avoidance issues and what is expected to be a substantial overhaul of the existing consumer credit pre-contractual disclosure regime.

Further, if any need for regulation is identified by the Government and COAG in respect of lending to small businesses and lending for investment purposes, Treasury has advised these reforms will also be introduced through this second enhancements bill.

An illustrative chronology of key stages of the credit regulatory program so far is provided in Appendix 1.

Added to this reform activity are the following other reforms that are in train or soon to be in train:

- Financial Claims Scheme Feb 2012
- Personal Property Securities Feb-July 2012
- Account Switching July 2012
- Future of Financial Advice legislation July 2012

and will overlap with the implementation timetable for the credit reform program and impact on our members' ability to make the required changes for systems upgrades, processes, documentation and staff training.

1.2 Commencement timing

Relevantly, the provisions in the Schedules of the First Enhancements Bill, Schedule 1 -financial hardship, enforcement proceedings, conduct remedies and prohibited representations; Schedule 2 - reverse mortgages and Schedule 3 - small amount credit contracts are to commence on 1 July 2012.

On the same date, 1 July 2012, the credit cards provisions (and regulations) of the Home Loans and Credit Cards Act will commence. The home loans provisions

(and regulations) of the Home Loans and Credit Cards Act will commence on 1 January 2012.

In all, there are 3 substantial pieces of credit regulation requiring industry implementation over the next 7 months[1].

In setting the commencement timing for these reforms, little account appears to have been taken by the Government of industry's need to plan its resourcing and IT systems modifications and implement necessary compliance frameworks. For example, banks set periodical "windows" where they are able to open up their IT systems for making normal business changes and changes necessitated by regulatory requirements. Documentary, procedural and staff training changes are critical for banks to ensure their compliance frameworks are adequate.

These are changes that have to be made in a planned and orderly way and not just by the "flick of a switch" to ensure change risk is minimised. Management of change risk includes not only IT systems changes but also all relevant processes, documents and staff training to avoid risk to both the bank and its customers.

The ABA requests the Committee to note these timing and implementation concerns. If as a result the Committee is disposed to consider a need for the Government to reconsider the commencement dates for both the First Enhancements Bill and the Home Loans and Credit Cards Act in its report this would be welcome.

2. Substantive legislative changes

2.1 Part 1 – Protection of debtor in cases of hardship

2.1.1 Preliminary ABA Comment

At the outset, the ABA considers that its members have set commendable standards for helping their customers who fall into financial difficulty with their credit commitments, particularly those customers who have home loans. Member banks can provide thousands of examples where customers have benefited from their banks' financial hardship arrangements.

A critical component in reaching these types of arrangements is to ensure that the customer is not worse off in the longer term through a variation in the terms of their contract, for example, where any equity available to the customer in the asset, provided as security, is significantly eroded over time and this could have been avoided by earlier realisation of the asset.

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[1] Banks implement IT systems "freeze" periods from December to mid-January to ensure that systems are able to serve this traditionally high customer transactions period and to provide for seasonal staff and consultants" leave arrangements

2.1.2 Key changes

The Bill proposes a number of substantive changes to the current law as it applies to varying a credit contract on the grounds of hardship under the National Credit Code ('NCC'). These changes and the practical implications of the proposed amendments for the credit provider and the customer are outlined below.

Section 72

Section 72(1) of the Bill proposes that if a debtor considers they will be unable to meet their obligations under their credit contract, the debtor may give the credit provider a 'hardship notice' orally or in writing.

The ABA notes the following changes to the current provisions of the NCC:

1. The removal of the need for the debtor to apply for a hardship variation on specified grounds[2].

2. No requirement for a debtor to make a formal hardship application to the credit provider. Rather, a debtor states (orally or in writing) their inability to meet their credit obligations under the contract. This statement will constitute a 'hardship notice' for the purposes of the law, upon receipt of which the credit provider's obligations, and the formal hardship process, are triggered. No form of notice is proposed to be prescribed for the debtor's notice.

3. No requirement on the debtor to provide details of their hardship

4. No requirement on the debtor to demonstrate to the credit provider that they could reasonably expect to discharge their obligations if the contract were changed[3].

5. The requirement for the debtor to seek to change the terms of the contract in a manner prescribed in section 72(2) has been removed. The customer therefore does not need to ask for any specific remedy[4]. By removing the reference to the limited specific changes a debtor is able to seek, it should not follow that the credit provider should be obliged to accept any of the debtor's proposed changes. The credit provider must retain the ultimate discretion.

   Furthermore, it is not clear in the Bill whether the debtor can seek a decrease in the Annual Percentage Rate (APR), despite section 72(2) of

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[2] Section 72(1) of the current NCC specified: illness, unemployment or another reasonable cause.

[3] Section 72(1) of the current NCC.

[4] Section 72(2) prescribed a debtor to seek to change the contract in three ways (without changing the Annual Percentage Rate): Extending the period of the contract and reducing the amount of each payment due under the contract; Postponing dates on which payments are due for a specific period or extending the period of the contract and postponing the dates on which payments are due for a specified period

the current law providing that the APR cannot be changed.[5] The ABA believes it is necessary for the Bill to provide certainty that customers can seek to change the terms of the contract *but without a change being made to the APR or rates.*

ABA Comments

The Bill intends to reduce the barriers on debtors seeking to change their contract on the grounds of hardship by removing the requirement for a formal application to be made to the credit provider. This requirement has been replaced by an obligation on the credit provider to formally respond to the debtor as a result of an exceptionally broad trigger of a 'hardship notice' by the debtor i.e. the debtor stating an inability to meet their obligations.

While the ABA recognises the purported intent upon which the amendments are based the inclusion of such a broad trigger could lead to impractical and suboptimal outcomes for both the customer and credit provider.

Under the Bill, there are many situations in which a statement (oral or written) made by a customer could constitute a hardship notification. Upon notification the credit provider must assume without further enquiry that the customer actually is in a situation of hardship and commence a formal process of written notifications and negotiations within prescribed time limits.

It is important to note that under the currently drafted Bill many scenarios would constitute a 'hardship notification' and trigger a formal process, despite a customer not being in a situation of genuine hardship nor requiring a formal process to solve their issue. For example, a customer may advise the credit provider of their inability to meet one of their credit card repayments on the due date or make their monthly home loan repayment on time but will do so in two weeks' time and could request an extension of time to make the repayment. Under the current law, such a notification could be solved immediately through an agreed arrangement between the credit provider and customer without a formal process being needed.

Notwithstanding the flexibility of the current law, the Bill proposes that such a notification would trigger the formal hardship process, thereby increasing the number of hardship notifications received by credit providers and an associated increase in the resourcing requirements of credit providers. A credit provider would have to issue a section 72(2)(a) notice agreeing to negotiate and then a section 73 notice setting out a change to the contract if it is agreed to. This would delay the commencement of the arrangement to the detriment of the customer.

In these situations this prescriptive process would be completely unnecessary and confusing for the customer. Yet the bank's failure to follow procedure and provide the notice would leave the bank liable to a strict liability criminal penalty.

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[5] The only indication in the Bill that the Annual percentage Rate cannot be amended is in section 74(2) which provides that the court can order a change "*but not so as to reduce the amount ultimately payable by the debtor to the credit provider under the contract".*

The ABA strongly submits that the Bill should allow current flexible business practice to continue in relation to the resolution of customer's requests and readily agreed arrangements with credit providers, without automatically triggering the formal process outlined in the Bill.

The ABA also submits that the broad trigger of the 'hardship notice' be refined to ensure that the hardship resources of credit providers continue to be used efficiently to deal with customers who are facing a genuine hardship situation and enable staff to assess their situation, rather than resources being used in a formal prescribed process for customers in situations that do not require or suit such a response.

Finally, the removal of the requirement in section 72(1) on the customer to *reasonably expect to discharge the debtor's obligations if the contract were changed* is extremely problematic. For example, the obligation to issue a notice under section 72(2) could arise from outbound calls from collections staff to a debtor who is in arrears. If the debtor indicated they could not pay the arrears immediately, the credit provider would have to issue a section 72(2) notice stating whether they agree to negotiate, even if the debtor indicates they have no intention or no ability to make repayments. The ABA emphasises the need for *a reasonable expectation on the part of the customer to discharge the debtor's obligations if the contract were changed* as a legislative pre-condition to the credit provider dealing with the debtor's hardship notification.

Section 72(2)

Section 72(2) provides that within 21 days of receiving the hardship notice, the credit provider must notify the debtor whether the lender is prepared to negotiate. If they are prepared to negotiate they will issue the debtor a section 72(2)(a) written notice to the customer. If they are not prepared to negotiate, the credit provider will issue a section 72(2)(b) written notice which must provide the reasons for not agreeing, the name of its EDR scheme, and the debtor's rights under the scheme.

At this stage of the proposed process a decision on a change to a contract on the grounds of hardship is not required; a credit provider is only required to provide a statement of whether the credit provider is prepared to negotiate with the debtor. This notice will be prescribed by the regulations.

Conversely, under the current law credit providers have 21 days from the receipt of a customer's hardship application to provide a debtor with a written notice stating whether or not they agree to the change. The Bill therefore proposes an additional step and additional written correspondence with a customer.

ABA Comments

The ABA interprets the requirement as 21 days to decide if the credit provider will negotiate and then 21 days to agree to a change or give notice that the credit provider is not prepared to negotiate further. If there is a difference of opinion as to what is expected, there needs to be clarification in the Bill.

Significantly, the ABA notes that under the Bill the credit provider must make a decision on whether to negotiate or not in the absence irrespective of having any information from the debtor. Any decision whether to negotiate should be based on relevant information from the debtor and knowledge of the debtor's circumstances. The ABA strongly submits that there would be better outcomes for both customers and credit providers if the Bill places a legal obligation on the debtor to provide information reasonably required by the credit provider to assess the 'hardship notification' and that time for the purposes of any notice requirement will not commence to run until this information is received.

While there is nothing in the Bill to prevent a credit provider from requesting information from the debtor to assess their hardship notice, the Bill does not impose a legal requirement on the customer to provide that information to the credit provider. In practice, a credit provider needs relevant information to assess a customer's situation of hardship and make the relevant decisions; firstly whether to negotiate a change to the contract and secondly whether to change the contract. We note that section 89A assumes that reasons for the hardship notice are given to the credit provider, and therefore the Bill should enshrine a requirement on the debtor to provide relevant information.

In practice, if a credit provider does not receive relevant information from a customer to assess their hardship notice, the credit provider will send a s72(2)(b) notice stating the credit provider does not agree to negotiate a change to the contract. This is not only a poor outcome for the customer but may also result in an increased number of complaints going to the Financial Ombudsman Service (FOS).

A positive obligation on a debtor to provide information 'reasonably required' by the credit provider to assess a hardship notice is a necessary legislative provision. The credit provider should be able to request information from the debtor about possible changes to the credit contract and whether the debtor reasonably expects to be able to discharge their obligations under the contract if it is changed accordingly.

This would help ensure that less hardship notifications are rejected on the basis of insufficient information and enhance the ability of credit providers to provide tailored solutions relevant to each individual's hardship needs on a case-by-case basis. We outline this recommendation in further detail in section 2.1.8 of this submission.

2.1.3 Section 74

In line with the current law, if a credit provider does not change the credit contract at the customer's request, the debtor may apply to the court to change the terms of the credit contract (but not so as to reduce the amount ultimately payable).However, because the Bill proposes to repeal section 72(2) of the Code (prescribing the manner in which a contract could be changed) the Court may vary a credit contract and make such other orders as it sees fit, including ordering an extension of the term, which is an option not available under the current law. We note that the amount payable will increase if more interest is incurred and expect that this would be taken into account under Court orders.

2.1.4 Section 89(A)

Section 89A provides that the credit provider must not begin enforcement proceedings if:

- the credit provider gives a s88 default notice; and
- either before or after giving the notice the debtor gives a hardship notice under s72; and
- in the 4 months before the day the current hardship notice is given, the debtor either hasn't given another hardship notice or had given a notice but the credit provider reasonably believes that the basis of the current notice is materially different from the previous notice, unless:
- The credit provider has responded to the notice stating that the credit provider does not agree to negotiate a change (s 72(2)(b) notice) and a further period of 14 days has elapsed.

ABA Comments

Section 89A(1) is unduly complex. The current drafting is unclear as to whether a credit provider could continue proceedings if the basis for the current notice is not materially different from the previous notice and whether a section 72(2) notice is still required despite the notice not being materially different. The ABA recommends that a credit provider should not be required to formally respond with a written notification to a hardship notice if the basis for the current hardship notice is not materially different from the previous notice and that proceedings should be allowed to continue in this situation.

Under section 89A(2) if a hardship notice is given to a lender prior to, or after, issuing a section 88 default notice[6], the lender must not begin enforcement proceedings until 14 days after providing a written notice stating that the lender is not willing to negotiate i.e. a section 72(2)(b) notice. There is no equivalent provision to this in the current law. The proposed provision would require

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[6] A credit provider must still allow at least 30 days from the S88 notice for the default to be remedied.

amendments to be made to credit providers' collections procedures in order to allow for a mandatory time period between a hardship notice, a credit provider's response and commencement of enforcement. Such changes would be made more difficult by the ability of a customer to make a hardship notice under section 72(1) on such broad terms, either orally or in writing.

In practice, even if it is clear the debtor cannot remedy the default as they are unable to make a payment, or the debtor is not agreeable to the credit provider's proposal, the credit provider would be required to issue a section 72(2)(b) notice stating they are not willing to negotiate and then wait a further 14 days before beginning enforcement proceedings. It is noted that the note to section 89A(2) of the Bill contemplates that the period of 14 days and the mandatory period of 30 days under the section 88 default notice may overlap and run concurrently. The ABA suggests that if the credit provider has determined that the debtor cannot perform the obligations under the credit contract the 14 days period should not apply.

2.1.5 Section 94

Under the current law, Section 94 of the NCC provides for a debtor to request a negotiation to postpone enforcement proceedings. Conversely, the Bill appears to impose an obligation on a credit provider to take both written and oral requests from the debtor to postpone enforcement proceedings, actions taken under those proceedings or the operation of any acceleration clause.

Enforcement proceedings cannot begin unless the credit provider has provided the debtor with a notice within 21 days agreeing to, or rejecting the request and a further period of 14 days from the day the notice is given. This will impact realisations staff as they will need to ensure written notifications are completed before the 21 day maximum response period in an effort to reduce delays.

ABA Comments

It appears a customer can delay enforcement proceedings by up to a total of 35 days, simply by stating they cannot meet their obligations under the credit contract, even if they are not in a situation of genuine hardship. If this provision is retained, it is necessary for the Bill to clarify that a customer can only delay the enforcement proceedings once on this ground. This will ensure that an abuse of process does not take place on the part of the customer.

2.1.6 Recommended changes to Part 1

The ABA suggests the addition of new provisions into Part 1 of the Enhancements Bill which would lead to more practical and beneficial outcomes for the customer, and decrease the prospect of an undue resource burden on credit provider's hardship teams.

The process map in section 2.1.9 outlines the recommended changes below:

1. It is necessary to ensure flexibility to allow banks to work with debtor's to provide a solution tailored to their individual needs on a case-by-case basis.

In some cases, problems can be solved immediately when the debtor notifies the credit provider of their inability to meet their obligations under their credit contract without requiring formal hardship assistance. For example, a customer's temporary inability to meet a credit card repayment on the due date. Under the current law, a notification from the customer does not necessarily have to be treated as a hardship arrangement requiring a formal response – many first interactions can be solved with standard collections arrangements without varying the contract. There is a need to maintain flexibility for credit providers to use these options without triggering the formal assessment and response process under the financial hardship provisions of the Bill. This flexibility should be enshrined within the law. Without an amendment to the Bill, the broad trigger of a 'hardship notice' will substantially increase consumer correspondence and credit provider resourcing requirements without providing a consumer benefit.

It is essential for the law to enable both an informal and formal hardship process to remain, to ensure that the credit provider may provide an adequate, proportionate and relevant solution to the debtor. The law should clearly delineate between these two processes so it is clear to both the customer and credit provider when a request for formal hardship arrangements is made, triggering the Bill's requirements of written notifications and decision making on the part of the credit provider in relation to negotiations and a variation to the credit contract. For this reason:

a) a credit provider should be permitted to establish a process that facilitates working to reach agreement with a debtor on the debtor's circumstances. This may mean that a debtor's request for hardship variation under section 72 may be required to be in writing to the credit provider, particularly as the requirement on the part of the credit provider to respond in writing carries a criminal penalty if this is not done; and

b) while placing excessive barriers between debtors and the ability to seek a hardship variation should be avoided, it would be clearer if the proposed 'hardship notice' is complemented by a requirement for the debtor to indicate specifically to the credit provider that the debtor is in 'financial difficulty' rather than an 'inability to meet their obligations'. This would be a clearer and more useful trigger.

2. The addition of a positive obligation on a debtor to provide information 'reasonably required' by the credit provider to assess a debtor's hardship notice, within a prescribed timeframe e.g. 14 days, as a precondition to the credit provider dealing with the debtor's 'hardship notice'[7].

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[7] A credit provider would need to make a request for this information from the debtor within a specified period.

This positive obligation is particularly important given the proposed removal of section 72(2) in the current law which required one of three temporary reasons for a hardship application. The removal of this section could result in customers applying for hardship in a wider range of situations, but also applying for hardship when hardship variation is not appropriate.

In order to assess a customer's hardship situation and develop a tailored solution, credit providers need two relevant pieces of information: firstly, an understanding of why a debtor cannot meet their obligations (to assess whether the debtor's situation is temporary or permanent as contract variation may not be suitable if a situation is permanent) and secondly, what obligations a debtor is able to meet (to ensure something could reasonably be achieved by a hardship arrangement).

As the *Australian Securities and Investments Commission's* (ASIC) *Infosheet 105* states:

> *It is important that credit providers respond quickly and appropriately to requests for assistance by borrowers experiencing financial difficulties. It is equally important, however, that credit providers properly understand the nature and impact of those difficulties, and are in a position to assess whether it is reasonable to expect that the borrower will be able to meet revised obligations if the terms of the contract are varied as requested.*

3. Credit provider's receipt of reasonably required information from the debtor would trigger the s72(2) 21 day time limit for written response of credit provider's decision whether to negotiate or not.

Obligation to respond in any formal way would only commence upon receipt of that information. This proposal is in line with ASIC's *Infosheet 105*[8]:

> *ASIC considers that the 21-day period commences after the borrower makes an application with sufficient information to allow the credit provider to make a final decision… Until that information is provided, ASIC's view is that an application for the purposes of s72(3) has not been made, and so the 21 days will not have commenced*[9]*.*

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[8] http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Dealing_with_consumers_and_credit.pdf/$file/Dealing_with_consumers_and_credit.pdf

[9] "Where a request for a variation is made without sufficient information, the credit provider will need to identify what further information is required to make a final decision and advise the borrower as soon as practicable. A request for further information should be limited to information that is genuinely needed to allow a final decision to be made, and any such request should not have the effect of unreasonably or unnecessarily delaying the process."

Once the information is provided by the debtor, if the credit provider agrees to negotiate they will issue a s72(2)(a) notice to the customer. If they do not agree to negotiate they will issue a s72(2)(b) notice to the customer, in line with the provisions included in the Bill.

4. The inclusion of a *"reasonable expectation on the part of the customer to discharge the debtor's obligations if the contract were changed"* as a legislative pre-condition to the credit provider dealing with the debtor's 'hardship notice'.

It is essential that a debtor demonstrates a capacity and willingness to meet obligations under a varied contract. This principle is contained in the current NCC and in the *Code of Banking Practice*[10]*.* The ABA strongly suggests that this obligation, as contained in section 72(1) of the NCC, is retained in the Bill. This is particularly important as it is assumed that ASIC would still expect a credit provider to satisfy itself that the debtor could meet the revised obligations under the credit contract (as quoted in recommendation 2).

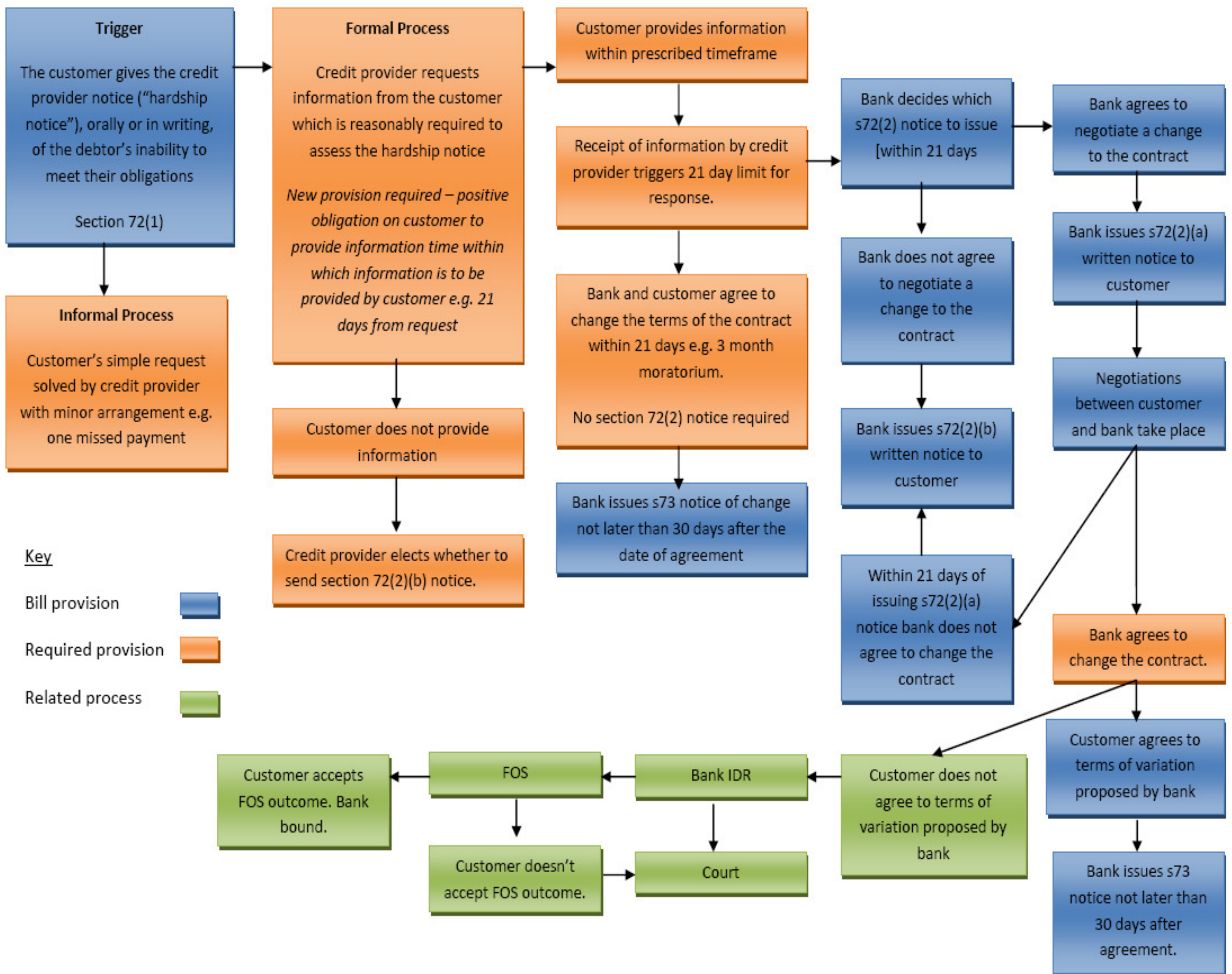
5. The Bill should not prevent the credit provider and customer agreeing to an arrangement within the 21 day limit for a section 72(2) response by the credit provider.

If this occurs a section 72(2) notice (outlining the credit provider's decision to negotiate or not) should not be required. However, if a bank agrees to change the terms of the contract within the 21 day time limit, the credit provider would need to issue a section 73 notice of change to the contract not later than 30 days after the date of the agreement (in line with the current section 73 requirements).

This will maintain flexibility and ensure appropriate solutions are tailored to the customer's needs on a case-by-case basis, while reducing the resourcing burdens on credit providers.

[10] Clause 25.2 of the Code states, "With your agreement we will try to help you overcome your financial difficulties with any credit facility you have with us".

2.1.7 Suggested changes to section 72 – Process map



2.2 Part 3 – Representations about eligibility to enter credit contracts, consumer leases etc. Without assessing unsuitability

In the consultations on this Bill the ABA raised the concern that the wording of proposed subsection 128(aa) of the NCCP Act the ABA made the observation about banks being able to provide to a customer the basis on which the bank may be prepared to indicate to the customer that the customer would be free to bid for a property at a forthcoming auction. The proposed amendment to the NCCP Act would require the customer to submit to the bank's full responsible lending assessment of the customer irrespective of whether the customer's bid proved to be successful.

There are broader concerns with the Part 3 changes, preventing representations to consumers that they are eligible to enter into or increase the limit of a credit contract without making a suitability assessment.

The ABA believes that this is already a requirement in the ASIC Act preventing misleading and deceptive conduct in financial services.

The ABA understands the policy objective of these provisions as prohibiting credit providers to use terms such as "Congratulations, you are pre-approved" but these terms will have to be qualified because a bank is subject to the responsible lending obligations in the NCCP Act which include the provision of certain information by the consumer and for the bank to verify this.

The Explanatory Memorandum states:

> *"2.58 The effect of these amendments is to prohibit credit providers from making representations to consumers that they are eligible to enter into a contract, or have their credit limit increased irrespective of, for example, their personal circumstances or credit history. These types of representations can encourage a consumer to apply for credit because of the certainty their application will be accepted, but where the resulting terms on which the credit is provided may be more onerous than those offered by other credit providers.*
>
> *2.59 As a result of the amendments the credit provider can represent to the consumer they are eligible to enter into the contract (or have the credit limit increased) once an assessment has been made. This representation can only be made for the same period of time following an assessment that the credit provider is able to rely on the assessment in order to enter into the credit contract or increase its limit (that is, for a period of 90 days or such other period as may be prescribed in the regulations)."*

The ABA submits that the policy intent expressed in paragraph 2.59 of the Explanatory Memorandum is not explicit in the drafting of the proposed amendment and should be amended accordingly.

2.3 Schedule 2 – Reverse Mortgages

2.3.1 Part 1 – Definitions

An amendment is necessary to the definition of a "reverse mortgage" in item 2 of Schedule 2 that is to be inserted as section 13A of the NCC. In proposed subsection 13A(2) the ABA submits that the words in bold in the following passage should replace the words to "**less than the maximum amount**" as follows:

"…without the debtor being obliged to reduce that liability to **the maximum amount or less** …"

Otherwise, for facilities such as overdrafts and lines of credit that are not reverse mortgages the definition would capture these facilities where a bank may normally require that a customer's debt be reduced to the maximum amount of credit and not to an amount less than that maximum.

This amendment would not appear to affect the policy objective for the regulation of reverse mortgages.

Secondly, under section 133DB(1) of the Enhancements Bill, licensees must use "a website approved by ASIC" to generate projections made in accordance with the regulations and to show them to consumers in person.

It is not clear whether "a website approved by ASIC" is a website that will be developed by ASIC or one that must be developed by each licensee. If it is the latter then any requirement to build a website will result in licensees incurring considerable cost in relation to such a build and may delay our ability to comply with the new reverse mortgage obligations.

Thirdly, subsection 18C(1) provides that the regulations may regulate or prohibit the entry by a credit provider into a credit contract for a reverse mortgage if the debtor has not obtained legal advice about the contract or reverse mortgage.

Banks' experiences with a mandatory requirement for customers to obtain independent legal advice prior to entering into a contract (for example a guarantee or a reverse mortgage) has been met with some resistance by both customers, due to the added cost for the advice, and by legal practitioners, who are concerned that the advice sought may include financial advice that they are neither qualified nor insured to provide.

3. Schedule 3 – Small amount credit contracts

In the Minster's second reading speech on introduction of the Bill he said

> *"Australians who use payday loans are usually unable to access other cheaper forms of credit. As a result they face two risks"*

The Minister went on to describe the two risks as the excessively high cost of credit for consumers who cannot shop around and the risk of a debt spiral where existing loans are extended or rolled into new loans.

The definition in item 1 of Schedule 3 of the Bill sets out the criteria for what will constitute a "small amount credit contract" and excludes from the definition a credit provider that is an authorised deposit taking institution (ADI).

There is the clear policy intention for this Bill to apply to only what are collectively described as payday lenders. The Government has identified market failures by this group of credit providers that it proposes to address by this legislation. If follows that the proposed regulation should not be extended ADIs.

4. Schedule 4 – Caps of costs etc. for credit contracts

The ABA disagrees with the principle of regulatory intervention to control pricing of financial services which the provisions of this Schedule 4 propose to do in this case by capping interest together with fees and charges.

The proposed regulation extends to persons providing credit assistance who suggest or assist a consumer to apply for a particular credit contract if the "cost rate" (as defined) exceeds 48%.

The proposed model for calculation of the "cost rate" is based on a model legislated under the Credit (Commonwealth Powers) Act 2010 (NSW) upon which there was no prior consultation with the credit industry. Subsequent representations to the New South Wales government were to no avail.

The concerns that the ABA expressed then appear to be applicable to proposed subsection 32B(3). However, the ABA welcomes the proposed exemption in section 32A(4) that section 32A will not apply to an ADI that is the credit provider.

Provided that exemption is retained in the legislation it is unnecessary for the ABA to pursue the matter of the proposed "cost rate" model. Supporting reasons for an ADI exemption expressed by the ABA previously are outlined below for the information of the Committee:

(1) A fee or charge payable by a debtor will be included in the calculation whether it is paid under the credit contract or otherwise as set out in circumstances in (3) (b) (i) and (ii), despite a credit provider potentially being unaware of the payment.

(2) A credit provider would have to establish systems to detect any payments made, and the time they are made, to third parties in order to make the relevant calculation to ensure the cap is not exceeded.

(3) Ordinarily credit providers do not have access to information about fees charged by or paid to third parties *unrelated* to the credit contract even though the credit provider introduced the third party to the customer. For example, a customer may ask their bank to suggest a financial planner to assist with advice about an investment property loan but the credit

provider would not know the specifics of what the planner will charge the borrower for the financial planning service. If the financial planning services continue as an ongoing service what further third party fees would have to be included in the recalibration of the credit cost amount.

(4) Third party service providers, for example insurers to whom the customer is referred or roadside assistance and maintenance providers (related to car loan packaging) would be captured in the credit cost calculation.

(5) In addition, there are difficulties in differentiating between an insurer to whom the bank has referred a customer, and debtor-sourced insurance that the bank simply finances for the customer.

(6) Further, loan originators have the option of charging consumers a direct origination fee, which is genuinely a payment to the originator and which the bank would often not know about.

(7) Possibly reward programs may be involved in the calculation depending on whether the credit provider is a linked credit provider with respect to the third party.

5. Conclusion

The ABA wishes to express its continued concern on the implementation pressures associated with the current consumer credit reforms, particularly given the scope, pace and timing of the reforms. These reforms should be viewed in the context of the remaining reforms to be released over the next 12 months. The ABA anticipates that the effectiveness and impacts of the Phase 1 credit reforms will be reviewed by the Government in the next 12 months.

We trust that our approach to the proposed changes to the financial hardship provisions in the NCC are viewed by the Committee as constructive and will ultimately deliver better outcomes for both consumers and banks. We look forward to attending the Committee hearing on 24 October and thank the Committee for the opportunity to participate by teleconference.

Yours sincerely

Ian Gilbert

APPENDIX 1

(1) In December 2009 the NCCP Act was enacted providing for the registration and licensing of credit providers and credit assistance providers, transfer, with some modifications, of the states and territories based Consumer Credit Code to the Commonwealth and renamed National Credit Code (NCC) and the observance of a legislated responsible lending regime for credit and credit assistance providers.

(2) On 1 January 2011 the responsible lending requirements of the NCCP Act commenced for banks, other authorised deposit taking institutions and registered finance companies.

(3) On 24 March the Bill for the Home Loans and Credit Cards Act was introduced into the Parliament and as noted above was passed on 4 July

(4) On 15 June 2011 the House of Representatives Standing Committee on Economics reported on its inquiry into the Home Loans and Credit Cards Bill. The Committee recommended that commencement of the home loans provisions (obligations on credit providers to provide home loan key facts sheets to consumers) should be deferred from 1 September 2011 to 1 January 2012 because there would be insufficient time of industry to prepare for compliance. The Committee noted its expectation that that there would be a 12 months period for finalisation of the credit cards regulations aspects of the Act and which would be developed in "the near future"

(5) On 1 January 2012 the home loans provisions (obligations on credit providers to provide home loan key facts sheets to consumers) of the Home Loans and Credit Cards Act will commence.

(6) To date detailed regulations to be made under Home Loans and Credit Cards Act that will be essential in driving bank's compliance and implementation projects are still not finalised. These regulations are not expected to be fully complete until November 2011.