



AUSTRALIAN BANKERS' ASSOCIATION INC.

Steven Münchenberg
Chief Executive Officer

Level 3, 56 Pitt Street
Sydney NSW 2000
Telephone: (02) 8298 0401
Facsimile: (02) 8298 0402

15 April 2010

Senator Mary Jo Fisher
Chair, Senate Standing Committee on
Environment, Communications and the Arts
PO Box 6100
Parliament House
CANBERRA ACT 2600
eca.sen@aph.gov.au

Dear Senator Fisher,

Green Loans Program

The Australian Bankers' Association (ABA) welcomes the opportunity to provide comments to the inquiry into the Green Loans Program. Our comments are restricted to those terms of reference with respect to financial institutions, including:

- the consultation and advice received from financial institutions regarding their participation;
- the basis on which the Government determined the amounts of the loan to be made available and Government subsidy; and
- the early reduction by the Government in the number of Green Loans to be offered, and subsequent discontinuation of the loans, including by financial institutions in advance of the Government's announced date of discontinuation.

1. Opening remarks

The ABA and our member banks support the Federal Government's climate change objective to reduce Australia's greenhouse gas emissions, adapt to climate change that cannot be avoided, and help shape a global solution. We believe that a comprehensive and multifaceted portfolio of policy responses is fundamental to changing the behaviour of governments, businesses and the community as a whole, which is critical to transitioning Australia to a future carbon constrained economy. In this context, we consider that 'Green Loans' could be useful in encouraging households to invest in environmentally sustainable home improvements.

Therefore, despite having an appreciation of the Federal Government's initial basis for announcing the 'Green Loans' program, we consider that problems with the program structure, product rules, administrative processes, legal uncertainties and national delivery and implementation timing resulted in only two banks and a number of credit unions being able to offer a 'Green Loan' product prior to the Government's announcement to discontinue the program.

Having said that, the ABA is disappointed with the Federal Government's announcement to change its environmental programs and redesign the 'Green Loans' program by discontinuing the loans component¹. We disagree with the Government's assertion that there is low interest and take up in 'Green Loan' products. While we do agree that additional resources were required to fulfill consumer demand in home assessments, adequate resources should also have been provided within the Department to deal with other program logistics, including addressing outstanding issues, implementing agreements with financial partners, and processing of loans (i.e. verification of assessment data).

The ABA is advised by the two member banks which became financial partners in the 'Green Loans' program that consumer demand exceeded initial expectations. Therefore, while only two banks offered 'Green Loan' products as part of the Government's program by the time the announcement was made to discontinue the program, we consider given the higher than expected consumer demand (even through difficult market conditions due to the global financial crisis and the availability of other Government incentives and initiatives), that interest and up take in 'Green Loan' products would have increased over time.

2. Specific comments

2.1 Consultation and advice received from financial institutions regarding their participation

The Federal Government announced the 'Green Loans' program as part of the 2008/09 Federal Budget. We understand that the program was designed to assist Australian families to install solar, water saving, and energy efficient products.

The ABA and member banks were subsequently provided with some information about the proposed program and implementation expectations as well as offered the opportunity to provide our comments on the proposed program, in particular the loan subsidy deed which would be used to put in place the arrangements between the Government and individual banks and other financial institutions.

The ABA notes that consultations conducted in late 2008 and early 2009 involved a number of discussions and correspondences between the Department of Environment, Water, Heritage and the Arts and the ABA and member banks in which we expressed concern with various elements of the proposed program. At the time, the ABA advised the Government that the policy, program structure and product design and rules should be:

- Reconsidered with a view to: (1) removing obstacles that hindered the ability for banks and other financial institutions to offer a commercially viable product that is consistent with existing and standard personal loan products; and (2) aligning product availability with appropriate market conditions and consumer demand conditions, especially given the global financial crisis and availability of other Government rebates and incentives.
- Limited to ensure unnecessary practical, technical and administrative constraints (such as technology, systems, processes and documentation) were minimised as well as to enable banks flexibility to leverage existing products and systems. (A 'Green Loan' product as proposed by the Government would require the development of a new product by a bank due to the various program specifications and non-standard product rules and payment features.)

¹ The ABA refers to Minister Garrett's media release (<http://www.environment.gov.au/minister/garrett/2010/pubs/mr20100219.pdf>).

- Significantly simplified and aligned with existing products to avoid changes to banks' distribution networks. (A 'Green Loan' product offered via a nationally operating bank would require the bank to implement new processes and systems across the entire bank, including branch and electronic banking channels as well as involve substantial implementation and integration management (i.e. product development, systems and procedures changes, disclosure and communications, legal and compliance, staff training, etc)).
- Revised to make sure the expected implementation period enabled banks and other financial institutions to conduct appropriate feasibility studies and product development work as well as enabled Government to address the outstanding issues which needed to be resolved.

Irrespective of the banking industry's reservations with the proposed program, two banks found that offering a 'Green Loan' product could be done, albeit with significant dedication of resources. We are advised that these banks became initially involved in the 'Green Loans' program due to a number of reasons, including CSR initiatives, commercial interests and broader sustainability motivations, but subsequently discovered consumer demand to be stronger than initially expected.

2.2 Basis on which the Government determined the amounts of the loan to be made available and Government subsidy

The ABA understands that the decision regarding the loan amount and subsidy payment was made by the Federal Government. The loan subsidy payment covers the interest on borrowing up to \$10,000 for a period of up to four years. The loan amount would be assessed by the bank based on compliance with the Government's loan eligibility criteria and bank's lending standards.

The ABA and member banks provided feedback to the Government on proposed loan subsidy and fee restrictions issues. The proposed loan subsidy model was based on a calculation being the cash rate plus 5% as specified by the Government. The subsidy amount provided to financial partners was 50% of the funds dispersed on each application. At the time, banks indicated that current interest rates for unsecured lending were in excess of this subsidy, implying that a bank would be required to carry the capital cost of the difference between the commercial rate available at the time and the loan subsidy.

Furthermore, the proposed administration fee was determined to be \$150. At the time, banks indicated that the fee restrictions would result in a bank being required to absorb the additional administration and servicing costs. It was noted that loan origination and set up costs for all unsecured personal loans are fixed, which means these costs are more difficult to recover on small loans, even at current interest rates.

The ABA and member banks provided feedback that the inadequacy of the subsidy as well as the fee restriction, coupled with the delay in payments of the subsidy and administration fee, would mean that banks would be required to carry the risk of the loan for a period and not be able to recoup the costs of managing the loan over its lifetime. The inability to charge standard service fees further exacerbated the difference between the loan subsidy and the costs of servicing the loan.

2.3 Early reduction by the Government in the number of Green Loans to be offered, and subsequent discontinuation of the loans, including by financial institutions in advance of the Government's announced date of discontinuation

2.3.1 Discontinuance of loans component by the Government

The ABA understands that the decision to discontinue the loan component of the 'Green Loans' program was taken by the Federal Government without consultation with existing financial partners or other banks and financial institutions.

The ABA subsequently provided the Federal Government with our views on the announcement and outlined areas that required attention with regards to the loan subsidy deed and other obligations between the Government and individual banks as well as banks and their customers.

The ABA highlighted a number of concerns, including:

- *Impact on banks:* The ABA advised that the banking industry invested significant time and resources in implementing the 'Green Loans' program, including liaising on program structure, product design and rules, delivery mechanisms and other administration and legal issues; conducting feasibility studies and market research; and for those banks that offered 'Green Loan' products, developing and launching loan products across their retail bank network. Direct and indirect costs associated with discontinuance of the program are being carried by banks. Reputational and customer relations difficulties associated with the discontinuance of the program are also being borne by banks.
- *Impact on individual bank customers:* Banks and other financial institutions offering a 'Green Loan' product have completed loans, but at the time of the announcement, also had a significant number of loan applications outstanding. It was noted that it is unclear how banks were expected to work with customers to ensure fair treatment of their customers. Subsequent to the announcement, and in consultation with the ABA, the Department produced a fact sheet for financial partners setting out arrangements for the end of the subsidy. Individual banks also had to negotiate immediate transition arrangements pursuant to the specifics contained in their loan subsidy deed. For example, banks and financial institutions had in place differing arrangements with the Government as agreed in their loan subsidy deed. Differing arrangements would have different contractual implications. Uncertainties and inconsistencies associated with discontinuance of the program had ramifications for how banks interacted with customers with existing loans and outstanding loan applications.
- *Impact on small business customers:* The ABA is advised that banks have provided working capital and access to credit to businesses engaged in providing goods and services as part of the Government's various environmental and home sustainability programs. It was noted that it is unclear how banks were expected to work with small business customers to ensure lending risks generated due to business interruption and the discontinuance of these various programs are responsibly managed.

The ABA and the two member banks worked with the Department to identify a workable strategy for banks and their customers to ensure that the discontinuance of the program was administered in a way that minimised the adverse impact on bank-customer relationships.

The ABA notes the Ministerial Statement made by Minister Wong on 10 March 2010 and we commend the efforts to resolve the outstanding issues with discontinuance of the loan component of the program and subsequent impact on banks, other businesses and consumers. However, we are advised that there are still some outstanding issues with the Government.

2.3.2 Discontinuance of loans offered by banks and other financial institutions

The ABA understands that the loan subsidy deed generally stipulated that the Federal Government could discontinue the program and end the subsidy by notifying the financial partner. Minister Garrett announced that the program would be discontinued on 19 February 2010. The Department notified financial partners of the end of the subsidy also on 19 February 2010. In accordance with the loan subsidy deed, the Government provided notice of 30 days and indicated that the end date was 22 March 2010.

The ABA highlights several considerations with the discontinuance of the program and provides reasoning for banks and other financial institutions ceasing to take applications ahead of the stipulated end date, including:

- *Loan subsidy deed:* The loan subsidy deed was entered into between the Government and individual banks and other financial institutions. The contractual arrangements contained within the loan subsidy deed reflected negotiations about the management of the partnership. Specific obligations contained within the individual loan subsidy deed would need to be followed. Therefore, differing legal arrangements regarding loan approvals would ultimately have different contractual implications, and therefore require different actions by financial partners as part of winding down of the program.
- *Loan processing:* Processing of loans required banks and other financial institutions to work with the Department to verify applications generally using the Department's "e-portal". Technology functionality problems associated with the "e-portal" resulted in mismatches between assessment numbers included in the loan application and eligibility assessment, which ultimately resulted in a backlog of applications. Banks' experience with loan processing indicated that timing of around 30 days may not be adequate to complete the loan process with the Department as required prior to the end date. Loan processing would require a combination of manual procedures and system interventions, and therefore allocation of adequate resources. Understandably, due to the backlog created by the Department's technology, banks and other financial institutions needed to stop accepting new applications so that outstanding applications could be addressed within the specified period and customer expectations could be met. Therefore, difficulties regarding loan processing would ultimately have an impact on how financial partners would need to withdraw availability of 'Green Loan' products from the market as well as bank-customer relationships. We are advised that complaints made to banks increased significantly as those applicants that had been assessed wanted to lodge a new loan application. A significant number of these complaints came from customers who had been waiting since November and December 2009 for their assessment to be received from the Department.

3. Concluding remarks

The ABA and the two member banks will continue to work with the Federal Government to ensure that the discontinuance of the program happens in a streamlined and manageable way, in particular ensuring all outstanding program difficulties and uncertainties are addressed.

The ABA also will continue to work with the Federal Government to ensure that the community is aware of the status of the 'Green Loans' program, in particular ensuring that the Government publishes information about the discontinuance of the loan component of the program. We believe that the Government should revise the name of the changed program so that it is not misleading – for example, "Home Sustainability Assessment Program". Unless there is a new name introduced for the program, we are concerned that banks will continue to be required to filter enquiries into the future.

Overall, the banking industry was keen to assist the Federal Government design and implement a 'Green Loans' program that enabled banks to offer new, commercially viable products to assist households to invest in environmentally sustainable home improvements. Higher than expected consumer demand for 'Green Loan' products suggested a viable business. However, ultimately banks were disappointed with the unanticipated announcement to discontinue the program and early withdrawal of support for the program by the Government.

With this in mind, the ABA is concerned that banks' experience with programs, such as the 'Green Loans' program, will impact on banks' consideration of partnering with the Federal Government on programs in the future. Therefore, we consider that it is essential that Government understands that:

- Business certainty is crucial if banks embark on such programs, in particular as it ensures a smooth and efficient service for their customers. A lack of business certainty (or the likelihood of political risk) leads to market distortions and increased transaction costs, which ultimately are carried by banks or passed on to their customers.
- Early consultation and ongoing dialogue with the banking industry is vital if market-based initiatives are to be successfully designed, especially programs which are to be delivered through the banking system. A lack of consultation leads to sub-optimal outcomes, which in this case has led to business disruption and inconvenience to bank staff that are subsequently required to deal with disgruntled customers.

Yours sincerely

Steven Münchenberg