



DAILY BULLETIN

Friday, 30 September 2011

Designing better regulation - the consumer credit experience, Christian Mikula, Australian Treasury

Christian Mikula offered analysis on issues that, from Treasury's perspective, commonly arise when drafting legislation. Looking to the drafting of future Phase 2 reforms, Christian asked that those making submissions consider the principles used by Treasury in framing regulation: prohibition versus regulation, whether a prescriptive or flexible approach should be used and the selection of appropriate penalty and enforcement outcomes. Submissions that focus on whether reforms match the harm presented and are workable in practice without resulting in unintended consequences, may be of most assistance to Treasury.

In selecting a flexible or prescriptive approach, the nature and scope of the conduct being addressed and the potential outcomes of any proposed reform are key issues. Prescriptive approaches deal in absolutes and provide certainty. Flexible approaches deal in 'standards', with determination of those standards lying with the courts and increasingly, with EDR schemes. Prescriptive approaches will usually be limited to the uncommon case where the prescribed process addresses all situations. Likewise, the choice to prohibit or regulate certain conduct will often depend on the scale of the harm and a consideration of the impact any prohibition would have on mainstream business practice.

In his discussion of penalties and enforcements, Christian noted that the *Enhancements Bill's* 48% cap on interest and fees marks a shift in how regulation is approached in this area. That reform applies the key requirements and associated civil

penalty regime for the first time to a "conduct" obligation.

Panel: Impact and repercussions of government regulatory changes to credit products, Katrina Bills & Stacey Hester - BOQ, Ian Gilbert - Aust Bankers Association

The panel initiated an interesting discussion on the newly introduced and revised regulatory requirements, including home loan key fact sheets, exit fees, hardship provisions and credit card and price signalling related legislation.

The session highlighted some practical implementation issues, such as the difficulties associated with persuading Senior Management of Financial Institutions to invest more time and funding into regulatory compliance and the training of staff due to Senior Management being concerned that the need for introducing the new legislation and revising the existing legislation has not been clearly spelled out by the government.

It was suggested that it would be beneficial for the Financial Services Industry if the government could:

- a) explain more clearly the legislative intention (including the intended benefits to consumers) before the new and revised legislation is enacted;
- b) provide longer consultation periods for exposure drafts so that the relevant business units have a better opportunity to assess the impact of proposed changes and provide more focused comments;
- c) be more responsive to errors in draft legislation during its development (e.g. the provisions on director and



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- secretary remunerations had drafting errors, which were not rectified before meeting notices had to be sent, causing non-productive expense);
- d) early consideration of the transitional measures for new developments (including the treatment of applications already in “the pipeline”);
 - e) define critical terminology at the stage of consultation, rather than in the regulations which are not finalised until a later stage (e.g. the industries covered by the price signalling legislation);
 - f) provide greater clarity on practical matters such as timeframes in regulatory processes, what “starts the clock ticking” in hardship applications and the manner of giving disclosure documents (e.g. Key Fact Sheets); and
 - g) consider imposing statutory obligations on customers (such as provision of supporting information for hardship applications).

It was recommended that the legislation should be clear, flexible and in response to clearly articulated policy needs so that the legislative objectives could be achieved without causing undue or disproportionate burden on the financial sector.

Implementation of responsible lending obligations - problems and issues, Philip Trinca - Blake Dawson & Frances Russell-Matthews - Westpac

Phillip and Frances offered an entertaining, insightful and thought provoking discussion on the new challenges and opportunities facing responsible lending. Frances described the requirements in a positive light, commenting that Westpac views the obligations as an opportunity to “put customers at the centre of what Westpac do” which has resulted in

increased communication in the “end to end process” of products resulting in a positive outcome for Westpac’s brand positioning.

Looking forward, the speakers noted that further consideration should be given to the role of the consumer in the responsible lending setting, indicating that a consideration of the role of the consumer is not incompatible with the concept of responsible lending. It was also suggested that in enacting legislation, consideration should be given to providing sufficient flexibility to enable older borrowers’ participation in the financial system. In terms of improving future responsible lending practices, Frances suggested that industry should be aware of consumer trends relating to credit cards, as Westpac experience indicates that consumer choice is not as haphazard as the industry may believe but rather such choice is often linked to particular objectives.

Both Philip and Frances acknowledged the spirit of cooperation with Treasury and ASIC. Frances also encouraged delegates to embrace the shorter disclosure regime and to add colour to disclosure documents, suggesting that more traditionally complex documents such as contracts and terms and conditions be consistent with the intent, if not the format, of the KFS regime. Frances suggested that while disclosure documents should not be overly simplistic, they should not be represented in a format which is unnecessarily complicated and that consideration be given to including pictures and diagrams to create a coherent, effective and user-friendly message, to ensure that disclosure obligations comply with legal requirements, to achieve the desired outcome for consumers and industry.

Brokers and other intermediaries, Jon Denovan, Gadens Lawyers

Jon Denovan provided a high level summary

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on the impact of the consumer credit regime on brokers and other intermediaries and highlighted the areas of law which may require further development.

Jon confirmed that the consumer credit regime has made substantial contribution to consumer protection including protecting borrowers from unsuitable loans and providing a greater level of information about the proposed financial products and services. However, he also noted that the financial institutions, particularly brokers and other intermediaries have been significantly burdened by the costs associated with credit law compliance. It was recommended that the government must apply a more balanced approach when it engages in regulatory intervention.

Issues associated with the current regulations in relation to brokers and other intermediaries:

- a) Under the licensing regime, many brokers elect to operate as a credit representative (**CR**) rather than hold their own Australian Credit License (**ACLs**). A contributing factor to this is the high level of compliance costs. As a CR, the brokers carry on credit activities on behalf of the Licensee. The Licensee is required to notify ASIC of CR appointments including whether the CR has the same authority as the Licensee under the ACLs. However, if the CR's authority is different from the Licensee, an ASIC search will not show the scope of the CR's authorisation;
- b) It is difficult for the aggregators to monitor CRs' activities because the CR usually transacts directly with the credit provider. Presumably monitoring will be impossible when the CR carries on credit activities with an "off-panel" credit provider to whom the aggregator does not have any business relationship;

- c) Brokers may "blindly" adopt the credit policies of a Licensee without independent review and assessment of their suitability; and
- d) Referrers are exempted from the application of the consumer credit regime. However, if referring loans forms a part of the referrers' business (not incidental to their business), the referrer exemption should not apply to such activities.

Small business lending & business banking, Bridget Powell - HSBC and Alison Deitz - Norton Rose

Treasury will be considering whether regulatory reform is appropriate in relation to small business lending in October / November of this year. Bridget and Alison emphasised that discussion on this topic has been largely theoretical to date and that as a starting point consideration should be given to whether current regulatory measures are failing, and if so, whether specific tailored reforms are preferable rather than extending current regulation to cover small business lending.

Extension of the current regime to small business lending may be problematic as:

- responsible lending requirements may make lending unobtainable, given that statistically, 80% of small businesses fail within the first year
- costs – the cost of industry implementing the regulations may have the consequence that products offered to small business in the future are more expensive and therefore beyond the reach of many small business borrowers
- there is uncertainty as to what definition of 'small business' will be adopted

However, both Bridget and Alison recognised that extending the credit licensing regime



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could be beneficial, specifically from a regulatory perspective, as it would enable ASIC to police the market more effectively by “eliminating cowboys” and non-compliant fringe lenders.

Exempt third parties, Steve Edwards, CreditWise

Steve offered a detailed presentation on the third party exemptions under the consumer credit regime, including exemptions applicable to referrers, point of sale vendors and debt collectors. As the Credit Licensee is regulated by ASIC, the third parties are “regulated” by the Licensee. It was highlighted that the exempted third parties must understand their obligations in order to maintain their exemption. Steve stated that the Treasury is seeking ministerial approval to release a paper for public comment in relation to the point of sale exemption.

Gala Dinner

Just like previous years, the Gala dinner was a huge success and a great networking opportunity. Great venue, food, entertainment and stellar service.



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