

Article Information

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Is it responsible to remove ‘responsible lending’?

Treasurer Josh Frydenberg has announced a major overhaul of responsible lending obligations.

The Treasurer intends to remove the current responsible lending regime. Draft bills have been released to effect this. The question is – will they work or muddy the waters?

On 4 November 2020, the [Treasury released proposed legislative reforms to the consumer credit regulatory regime for public consultation](#).

These proposed reforms follow Treasurer Josh Frydenberg’s announcement on 25 September 2020 that changes will be made to remove responsible lending. That is, changes to Australia’s consumer credit framework identified in the *National Consumer Credit Protection Act 2009* (Cth) (**NCCP Act**) to reduce the timeframe for individuals and small businesses to access credit while still upholding protections for vulnerable consumers. These reforms are aligned with Treasurer Frydenberg’s desire to replace the current “lender beware” approach with a “borrower responsibility” approach. Subject to legislation passing, the reforms will commence on 1 March 2021.

In summary, the intended reforms will:

- remove responsible lending obligations from the NCCP Act, except in relation to small amount credit contracts (**SACCs**), SACC-equivalent contracts provided by ADIs and consumer leases;
- clarify the application of responsible lending obligations to small business lending; and
- implement a new framework which will apply key elements of APRA’s ADI lending prudential standards to non-ADIs (except for SACCs and consumer leases). ADIs will still be required to comply with APRA’s prudential standards.

National Consumer Credit Protection Amendment (Supporting Economic Recovery) Bill 2020: A new regulatory framework for the provision of consumer credit

From 1 March 2021, the existing responsible lending obligations contained in the NCCP Act will only apply in relation to SACCs, SACC-equivalent loans provided by ADIs and consumer leases. ADIs will no longer be expected to abide by responsible lending obligations, rather they will be subject to APRA’s prudential standards. Non-ADI credit providers, will need to establish and maintain systems, policies and processes that comply with the Standards to be determined by the Minister, based on obligations similar to those imposed on ADIs.

Upon this becoming legislation, the Minister will have the ability to make standards that require non-ADI credit providers to implement systems, policies and processes in relation to their credit assessment and approval conduct. The standards may also require a licensee to provide the consumer with a copy of a specified document.

The best interests obligations currently legislated for mortgage brokers will be extended to all broker-like credit assistance providers.

A civil penalty of up to 5,000 penalty units (currently \$222 per penalty unit) is specified for contraventions of the various obligations to be introduced by the Bill.

National Consumer Credit Protection Amendment (A New Regulatory Framework for the Provision of Consumer Credit) Regulations 2020

The proposed Regulations will limit or repeal the provisions made redundant from the Bill's removal of responsible lending obligations for credit contracts other than SACCs, SACC-equivalent loans provided by ADIs and consumer leases. In accordance with the Regulations, the existing regulations 28HA, 28J and 28LC will be made redundant as the Bill limits the applicability of provisions of the NCCP Act to SACCs, SACC-equivalent loans by ADIs and consumer leases. It also reduces the period of the responsible lending exemptions provided for in the existing regulation 28RB, which is a temporary COVID-19 exemption. The exemption period was meant to end on 2 April 2021, but the Regulations shortened the period to the end of the day before the Bill commences which is currently expected to be 28 February 2021.

The Regulations will also modify the Bill's definition of 'non-ADI credit conduct' in relation to credit card contracts. The conduct of a licensee providing a consumer with a credit card for the purpose of entering into a credit contract that is formed or entered into by the consumer using or activating the credit card will also fall within the definition of 'non-ADI credit conduct'.

National Consumer Credit Protection (Non-ADI Credit Standards) Determination 2020

The Standards will require non-ADI credit providers to establish and maintain systems, policies and processes relating to non-ADI credit conduct. They will impose procedural obligations rather than individual contract-level conduct requirements. This will shift the credit assessment criteria from a 'one-size-fits-all' prescriptive framework for lenders and borrowers. It will instead support risk-based lending which is tailored to the characteristics of the borrower and the particular credit product.

The Standards are based on aspects of APRA's updated prudential standard APS 220 (as due to commence in January 2021). This relates to an ADI's lending standards and management of credit risk exposures. However, while APS 220 is concerned with an ADI's risk management for the benefit of the ADI and broader financial system stability, the Standards are concerned with assessing whether a consumer could comply with their obligations under the credit contract only with financial hardship.

In relation to the assessment and approval of credit applications, the Standards will require a non-ADI credit provider to have in place systems, policies and processes which are adequate to ensure that the credit provider does not engage in non-ADI credit conduct unless:

- (a) it has established credit assessment criteria that meet the requirements set out in the standards (section 7 of the Standards);
- (b) it assesses whether the consumer is likely to be able to comply with their financial obligations under the credit contract without substantial hardship if the credit contract is entered into or the credit limit is increased (section 8 of the Standards), with that assessment:
 - 1. being performed against the credit assessment criteria established by the licensee in compliance with the Standards; and
 - 2. assessing the consumer to be unable to comply without substantial hardship if they could only comply by:
 - 1. (a) selling their principal place of residence when they do not intend to sell their principal place of residence in order to comply with their obligations under the credit contract;
 - 2. (b) failing to make rental payments in relation to their principal place of residence; or
 - 3. (c) for a credit card contract, if the consumer could not repay an amount equal to the credit limit within three years (section 9 of the Standards); and
 - 3. complying with the "information requirements" set out in the non-ADI credit standards (section 8(2) of the Standards)
- (c) it has approved the non-ADI credit conduct, and does not approve non-ADI credit conduct if the assessment is that the consumer would be unable to comply with their financial obligations under the credit contract without substantial hardship if the credit contract is entered into or the credit limit is increased (section 10 of the Standards).

The Standards will require a non-ADI credit provider's credit assessment criteria to:

- (a) enable it to assess whether it is likely that the consumer will be able to comply with their financial obligations under the credit contract without substantial hardship if the credit contract is entered into or credit limit is increased;
- (b) allow for the assessment to be proportionate to the nature, type and size of the credit; and
- (c) require the assessment to consider each of the following relevant factors:
 - 1. the purpose of the credit;

2. the structure of the credit;
 3. the consumer's sources of repayment, including their income and cash flow;
 4. the current risk profile of the consumer, including their total indebtedness and other payment obligations;
 5. the consumer's repayment history and the consumer's capacity to repay the credit without substantial hardship in a range of situations involving reasonably foreseeable changes in the consumer's obligations under the credit contract, including:
 1. (a) a change from a fixed interest rate to a floating interest rate or vice versa; and
 2. (b) if the credit contract has a limited interest-only period, a requirement to repay both principal and interest;
 6. the consumer's reasonably foreseeable expenses; and
- (d) the proposed terms and conditions of the credit contract.

The Standards will also require a non-ADI to provide a consumer with a copy of the assessment on request by the consumer. This will replicate credit providers' current obligation under section 132 of the NCCP Act (if enacted, the Bill will confine section 132 to operate only in relation to SACCs and SACC-equivalent ADI credit contracts).

The Standards will be enforceable by way of prohibitions in the NCCP Act.

A civil penalty of 5,000 penalty units will be prescribed for contravention of each of these obligations.

What you need to do now

1. Written plan

A requirement under the consumer credit reforms is for non-ADI's to have and to be able to provide upon request, a written plan which documents the systems, policies and processes established and maintained by the credit provider to comply with the Standards. Many credit providers may have their systems, policies and processes dispersed across the business, prior to the March 2021 date. These should now be consolidated and reviewed to ensure they comply with the responsible lending requirements

2. Broader obligations

Credit providers should continue to be aware of their obligations in the operation of the business. As a change in responsible lending compliance systems may affect the rest of the operation of the business, credit providers should be conscious of their general obligations. This includes the requirement to act efficiently, honestly and fairly, ensuring consumers are not adversely affected by conflicts of interest and maintaining compliance with credit laws.

Furthermore, to comply with the impending design and distribution obligations credit providers will need to ensure that the credit products distributed to consumers fall within the target market. Awareness should also be given to the seemingly creeping concept of "best interests" duty.

3. Consideration of 'substantial hardship'

Credit providers are still required to assess whether consumers will be capable of complying with their financial obligations without 'substantial hardship'. Accordingly, credit providers will still need to have appropriate assessments in place to ensure this is adequately conducted.

The consultation phase for the proposed consumer credit reforms closed on 20 November 2020. The Government will now consider the submissions received before finalising the reforms.