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Consumer protections post regulatory change

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Overview



Overview

- Small amount credit contracts and consumer leases
- ADI credit standards
- Non-ADI credit standards
- AFCA
- Duty of care – common law
- ASIC Act
- National Credit Code
- Banking Code of Practice



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Small amount credit contracts and consumer leases



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Small amount credit contracts and consumer leases

- Responsible lending obligations retained



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Prudential Standard APS 220



APS 220

40. An ADI must undertake a comprehensive assessment of a borrower's credit risk which would consider and be proportionate to the nature, type and size of the exposure. An ADI must use experienced credit judgement in adopting a scalable and flexible approach to its credit risk assessment of a borrower.

41. An ADI must assess credit risk primarily on the strength of a borrower's repayment capacity. The ADI must not place undue reliance on collateral provided by the borrower as a substitute for a comprehensive credit assessment.

42. An ADI must not place undue reliance on external credit ratings. An ADI must obtain adequate information to undertake a comprehensive credit assessment of a borrower.

43. An ADI must give due consideration to the integrity and reputation of the borrower as well as its legal capacity to assume liability.



APS 220 - Exposures to individuals

44. For exposures to individuals, an ADI's credit assessment must include consideration of the following criteria, where relevant:

- (a) the purpose and structure of the exposure and sources of repayment, including making reasonable inquiries and taking reasonable steps to verify income or cash flows;
- (b) the current risk profile of the borrower, including making reasonable inquiries and taking reasonable steps to verify commitments and total indebtedness;



APS 220 - Exposures to individuals

(c) the borrower's repayment history and capacity, assessed under various scenarios such as:

- (i) an increase in interest rates;
- (ii) a change from a fixed-rate to a floating interest rate (and vice versa);
- (iii) a decrease in income or cash flows, particularly for less stable income or cash flow sources; and
- (iv) for exposures with an interest-only period that subsequently converts to principal and interest payments, on a principal and interest basis of repayment;



APS 220 - Exposures to individuals

- (d) the borrower's expenses, including the collection of reasonable estimates. Expense benchmarks must not be used as a substitute for an ADI making reasonable enquiries of a borrower's expenses;
- (e) the proposed terms and conditions of the exposure, including covenants designed to limit the ADI's exposure to changes in the future risk profile of the borrower to an acceptable level to the ADI; and
- (f) where applicable, the adequacy and enforceability of collateral, guarantees and other risk mitigants, including under various scenarios.



APS 220 – Credit process

54. An ADI must document the credit assessment and approval process and identify the approval authority for each exposure, so that it is clear which personnel are accountable for the individual credit decision.

55. An ADI must ensure personnel involved in the credit assessment and approval process have appropriate experience and knowledge to exercise prudent credit judgement commensurate with the nature, size and complexity of the transaction to which they are involved.

56. An ADI must have prudent credit risk policies and processes with respect to overrides, waivers or exceptions, including clear identification of approval authorities and limits that reflect the maximum level of allowable overrides, waivers or exceptions.



APS 220 – Third parties

58. Where an ADI uses a third party, such as a broker, to undertake any aspects of the credit assessment or approval, an ADI must implement appropriate oversight processes of the third party. An ADI must monitor and test the integrity of the third-party assessment and approval on a regular basis, either directly or through operationally independent personnel to ensure it aligns with the ADI's credit assessment and approval criteria.



Enforcement

- Banking Act section 11AG – an ADI must comply with a standard
- Banking Act section 11CA(1)(b) – APRA can issue directions if standard not complied with
- Banking Act section 11CG – failure to comply with a direction is an offence



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Non-ADI credit standards



Non-ADI credit standards

- Will be substantially the same as APS 220
- Licensee must comply
- ASIC enforcement



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AFCA



AFCFA jurisdiction

A.14.2 When determining any other complaint, the AFCFA Decision Maker must do what the AFCFA Decision Maker considers is **fair in all the circumstances** having regard to:

- a) legal principles,
- b) applicable industry codes or guidance,
- c) good industry practice and
- d) previous relevant Determinations of AFCFA or Predecessor Schemes.



Exclusion re credit complaints

C.1.3 AFCA must exclude:

a) A complaint about the Financial Firm's assessment of the credit risk posed by a borrower or the security to be required for a loan unless the complaint is about:

(i) **Maladministration** in lending, loan management or security matters; or

(ii) the variation of a credit contract as a result of the Complainant being in financial hardship;

b) A complaint about a Small Business (including Primary Producer) credit facility:

(i) of more than \$5 million or higher amount that applies as a result of an adjustment in accordance with rule D.4.3; and

(ii) where the complaint is submitted by the borrower or a guarantor of the borrower's debt.



Maladministration

Maladministration means an act or omission contrary to or not in accordance with a duty or obligation owed at law or pursuant to the terms (express or implied) of the contract between the Financial Firm and the Complainant.



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Duty of care – common law



Duty of care – common law

- At common law, a bank does not owe a duty of care to a customer except in very narrow circumstances ... mostly where a bank has embarked on provision of advice.



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ASIC Act



Australian Securities and Investments Commission Act

Section 12ED Warranties in relation to the supply of financial services

- (1) In every contract for the supply of financial services by a person to a consumer in the course of a business, there is an implied warranty that:
 - (a) the services will be rendered with due care and skill; and
 - (b) any materials supplied in connection with those services will be reasonably fit for the purpose for which they are supplied.



Australian Securities and Investments Commission Act

Section 12ED Warranties in relation to the supply of financial services

(2) If:

- (a) a person supplies financial services to a consumer in the course of a business; and
- (b) the consumer, expressly or by implication, makes known to the person:
 - (i) any particular purpose for which the services are required; or
 - (ii) the result that he or she desires the services to achieve;

there is an implied warranty that:

- (c) the services supplied under the contract for the supply of the services; and
- (d) any materials supplied in connection with those services;

will be reasonably fit for that purpose or are of such a nature and quality that they might reasonably be expected to achieve that result, except if the circumstances show that the consumer does not rely, or that it is unreasonable for him or her to rely, on the person's skill or judgment.



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National Credit Code



Section 76 Unjust contracts

- (2) In determining whether a term of a particular credit contract, mortgage or guarantee is unjust in the circumstances relating to it at the time it was entered into or changed, the court is to have regard to the public interest and to all the circumstances of the case and may have regard to the following:

.....

- (l) whether at the time the contract, mortgage or guarantee was entered into or changed, the credit provider knew, or could have ascertained by reasonable inquiry at the time, that the debtor could not pay in accordance with its terms or not without substantial hardship;



Shannon v Permanent Custodians Limited

[2020] WASCA 198

It may, of course, be perfectly correct to say that there is no such 'duty' or 'obligation' on a lender at general law to assess the capacity of a borrower to repay a loan. That does not, however, mean that the failure of a lender to do so (i.e. assess the capacity of the borrower) cannot, in some circumstances, lead to a contract that is 'unjust' within the meaning of the National Credit Code.

Quinlan CJ & Tottle J at [176]

Nor, depending upon the circumstances, is the relevance [of] a credit provider's failure to make inquiries limited to cases of actual or constructive knowledge. The failure to inquire itself may be a relevant factor to take into account in the assessment of all of the circumstances, including the public interest.

Quinlan CJ & Tottle J at [180]



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Barker v GE Mortgage Solutions Limited

[2013] QCA 137

.... the fact that a party cannot afford a loan has been held to be insufficient on its own to result in a finding that the loan contract is unjust under comparable legislation: see Australian Society Group Financial Services (NSW) Ltd v Bogan [1989] ASC 55-938 in respect of similar legislation

White JA at [72]



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Banking Code of Practice



Banking Code of Practice

49. If we are considering providing you with a new loan, or an increase in a loan limit, we will exercise the care and skill of a diligent and prudent banker.

50. If you are an individual customer, that is not a business, we will do this by complying with the law.

Doggett v Commonwealth Bank of Australia [2015] VCSA 351 – if duty had been exercised properly, loan would not have been approved.



Customer Owned Banking Code of Practice

6. Responsible lending practices

6.1. We will always act as a responsible lender and will comply with responsible lending laws.

6.2. We will base our lending decisions, including decisions to extend existing credit facilities, on a careful and prudent assessment of your financial position and requirements and objectives as indicated to us. We will periodically review our credit assessment procedures and criteria for the products we issue.

6.3. We will generally only lend amounts to you that we believe, on the information available to us, you can reasonably afford to repay. However, different criteria will apply in the case of some products, such as bridging finance arrangements and reverse mortgage loans (if we offer these).

6.4. We expect you to provide honest and accurate information to us when applying for a loan or the extension of a credit facility. We will also take reasonable steps to verify your financial situation.

6.5. We will promote the responsible use of credit to our customers using a range of approaches.