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**National Credit Reform Take 3:  
The Ascendance of the Commonwealth**

**Mark Sneddon**  
Partner  
Clayton Utz  
Melbourne

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26th BFSLA Conference

National Credit Law Reform - Take 3 /Takeover

Mark Sneddon, Partner

Clayton Utz

[msneddon@claytonutz.com](mailto:msneddon@claytonutz.com)

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# Overview

- Introduction to the Reforms- FSR reprise (why?)
- The Credit Activities Net: Who needs to be registered /licensed? How in practice?
- Responsible lending obligations - how will they work?
- Roles of ASIC
- Comment

# Introduction to the Reforms

- 3 July 2009: COAG agrees Commonwealth to take control
- Phase One: National Consumer Credit Protection Package -
  - 650 pages of National Consumer Credit Protection Bill and Transitional and Consequential Provisions Bill and regulations and EMs in a public consultation package released 27 April 2009 for comment by 25 May 2009 (closed industry process prior to this)
  - 25 June 2009: Revised package introduced into Parliament
  - Political pressure for speed inevitably lead to limited consultation, broad regulation requiring extensive dispensation and modification discretions in the regulator ASIC and detail deferred to Regulations
- Phase Two
  - review of specific credit issues, such as State interest rate caps, mandatory comparison rates, reverse mortgages, *credit for business and investment purposes*
  - expect legislation for phase 2 to be in place by mid-2010

# Introduction to the Reforms

- **Parallel Reforms**

- Margin lending → Ch. 7 financial product and responsible lending
- Unfair Terms in Consumer Contracts - ACL Part 1 as enacted in ASIC Act and TPA to take effect from 1 January 2010 with the Victorian FTA Pt 2B applying to consumer credit contracts now (will be aligned with ACL by end of 2010)

# How the NCCP Works

- The State based UCCC is copied and replaced (with some changes) by a single National Credit Code (NCC) (Sch 1 of NCCP Bill). Supported by State referral of powers and federal powers.
- National registration and licensing of all persons *engaged in credit activities* in respect of *credit to which NCC applies* - broadly similar to the AFSL regime, overseen by ASIC - lots of new fish in net.
- Licence conditions, conduct obligations (including responsible lending) and disclosure obligations - superintended by ASIC. FSR reprise.
- Civil penalty and criminal penalty regimes for licensee misconduct. Civil penalty infringement notices (fines) - regulated by ASIC.
- Consumer compensation remedies. Three levels of dispute resolution - IDR, ASIC-approved EDR (licence requirement), State and Federal Courts (small claim procedures for claims up to \$40,000).

# Timing to be licensed/registered?

- **Registration requirements**

- all persons currently engaging in credit activities will need to apply to ASIC for registration between 1 November 2009 and 31 December 2009
- Membership of approved EDR scheme required for registration and licensing

- **Licensing requirements**

- upon registration, persons need to apply to ASIC for licence by 30 June 2010
- From 1 January 2010, any person engaging in credit activities for the first time must apply to ASIC for a licence

# Big Net - Who must be licensed/registered?

- Persons and entities who *engage in credit activities* in respect of *credit to which the NCC applies* must be licensed or be an authorised representative of a licensee.
- *Credit to which the NCC applies* is credit to be provided under a credit contract to a natural person or strata corporation for which a charge is or may be made and is provided wholly or predominantly
  - a) for personal, domestic or household purposes; or
  - b) (NEW) to purchase, renovate or improve residential property for investment purposes; or
  - c) (NEW) to refinance credit described in (b)
- "Residential property" covers land for residential dwellings and rights to occupy aged care facility or retirement village)
- ASIC can exempt persons and classes from licensing - e.g. POS

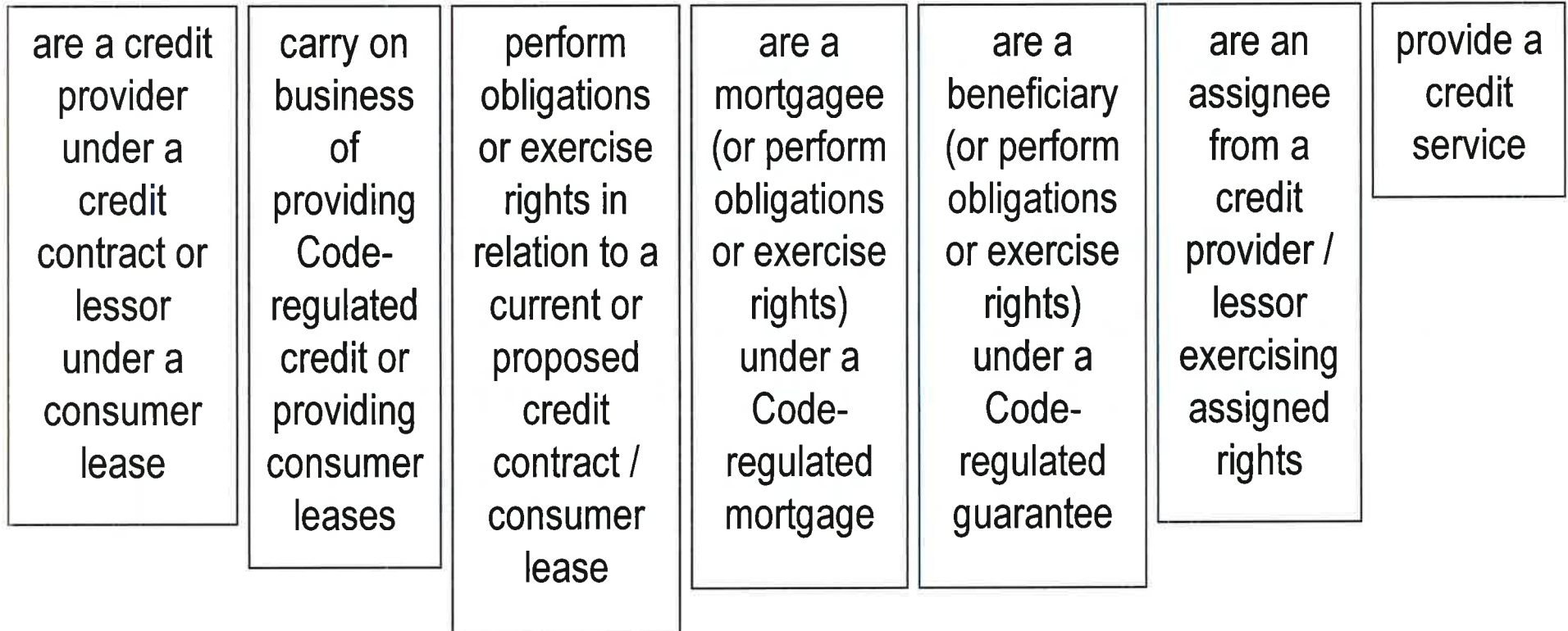


# Credit activity

- Two broad categories of credit activities:
  - *credit providers* under a NCC credit contract, *lessors* under NCC consumer leases, *mortgagees* under a NCC mortgage, *beneficiaries* of NCC guarantees and *assignees at law* of any of these;
  - persons who provide *a credit service* - defined as
    - providing *credit assistance* or
    - acting as an *intermediary* for the purpose of securing a consumer contract or a consumer lease

# Credit Activity

A person or entity will be engaging in a "credit activity" if they:



# Credit Service

- Credit Service

- A person or entity provides a "credit service" if they:
  - provide "credit assistance" to a consumer; or
  - act as an "intermediary"

- Credit Assistance

- A person or entity provides "credit assistance" if they:
  - deal directly with a consumer / consumer's agent;
  - "in the course of", "as part of" or "incidentally to" a business carried on by them in Australia; and
  - "suggest" or "assist" regarding regulated credit

# Credit Assistance: "suggest" or "assist"

- A person or entity will be regulated where they:
  - suggest consumer applies for credit or for limit increase under, or remains in, a particular credit contract / consumer lease with a particular credit provider / lessor; or
  - assist the consumer regarding application for credit or consumer lease or credit limit increase
- Must involve a particular credit contract or lease (general suggestions and assistance not caught)

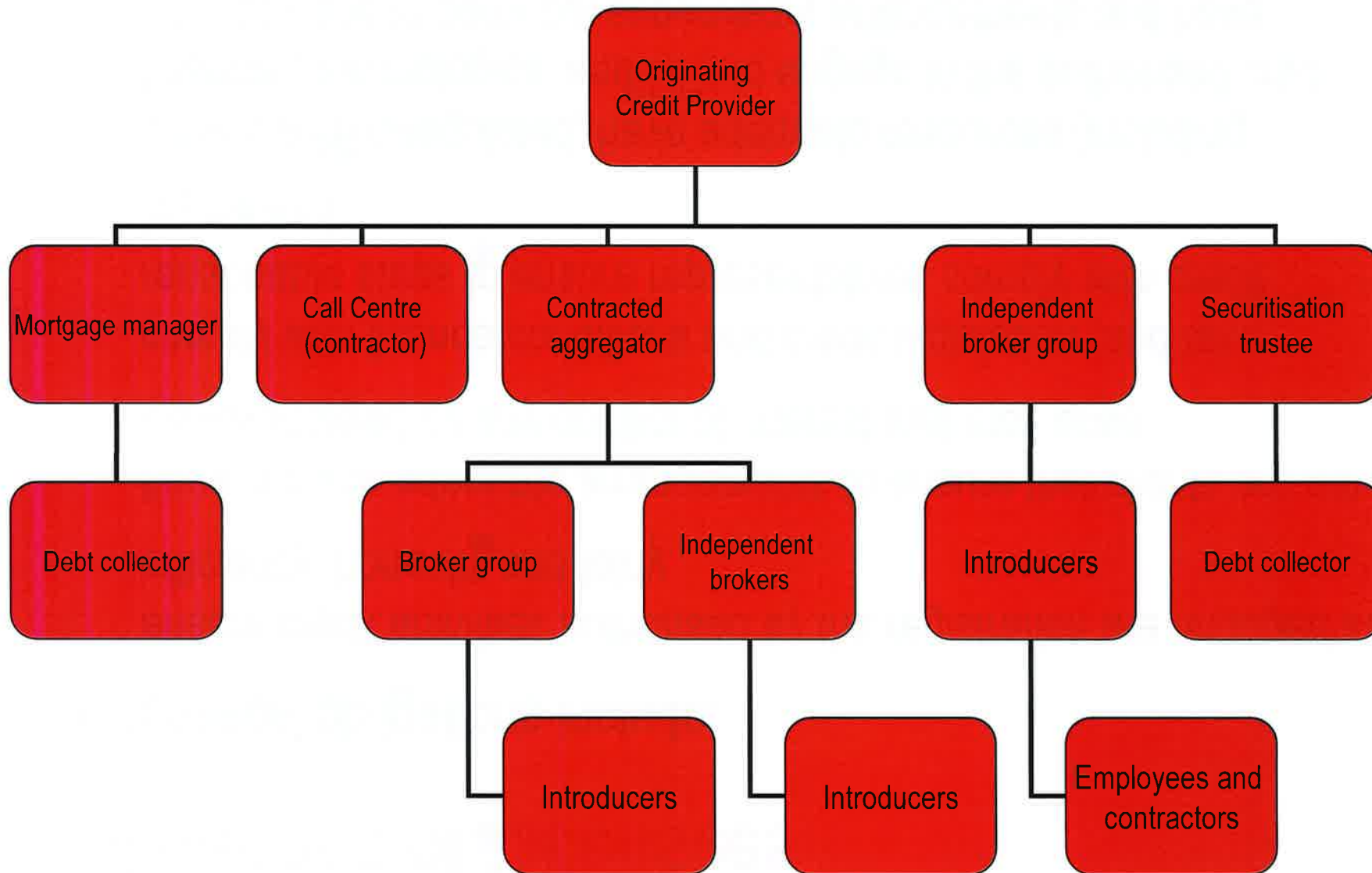
# Acting as an Intermediary

- A person or entity covered if they act as an intermediary:
  - directly or indirectly between a credit provider / lessor and a consumer, wholly or partly for securing provision of regulated credit / consumer lease
  - "in the course of", "as part of" or "incidentally to"
  - a business carried on by them in Australia
- Government intends to cover every intermediary between a credit provider and consumer (subject to exceptions)

# Credit Representatives of Licensees

- Taking another leaf from FSR, a licensee can authorise a person in writing to engage in specific credit activities on behalf of the licensee.
- Credit representatives do not need a licence when so acting.
- A body corporate representative can sub-authorise a natural person if the licensee consented in writing.
- Licensees are generally responsible for their representative's conduct for any loss or damage suffered by a client reasonably relying on that conduct.
- Licensees can authorise a person to be a representative of 2 or more licensees if each licensee consents or the licensees are related bodies corporate. Multiple licensees authorising the same representative are generally jointly and severally liable to the client. Licensees and representatives may take indemnities from each other.

# What will this do to business models?



# Obligations of Licensees

- Licensees' obligations include:
  - ensure credit activities authorised by the registration are engaged in efficiently, honestly and fairly
  - have in place adequate arrangements to ensure that clients are not disadvantaged by any conflict of interest that may arise
  - comply with licence conditions and credit legislation (and take reasonable steps to ensure representatives comply with credit legislation)
  - Unless APRA-regulated, have adequate resources (including financial, technological and HR) to engage in the authorised credit activities and to carry out supervisory arrangements and have adequate risk management systems



# Obligations of Licensees

- Maintain competence to engage in the authorised credit activities
- ensure that its representatives are adequately trained and competent to engage in the authorised credit activities
- have a compliant internal dispute resolution procedure
- be a member of an approved external dispute resolution scheme
- have compliant compensation arrangements in place
- have adequate arrangements and systems to ensure compliance with its obligations and a written plan documenting arrangements and systems
- Breach reporting was removed during consultation - instead licensees must provide an annual compliance certificate

# Responsible Lending

- Intended as a supplement to a licensee's general conduct licence obligations to operate efficiently, fairly and honestly
- Responsible lending obligations apply from 1 January 2011 when licensees:
  - enter into consumer credit contracts (or credit limit increases) with consumers or consumer leases
  - suggest a consumer enter into a particular credit contract (or credit limit increases) or consumer lease with a particular credit provider
  - assist a consumer to apply for a particular credit contract (or credit limit increases) or consumer lease with a particular credit provider
- The responsible lending obligations are slightly different depending on whether the licensee is giving *credit assistance* or a *credit provider / lessor*

# Responsible Lending - Credit Assistance Providers

- The key responsible lending obligations applicable to licensees who provide credit assistance include obligations to:
  - provide a credit guide;
  - provide a quote for credit assistance;
  - make a preliminary assessment of unsuitability;
  - disclose fees and a reasonable estimate of commissions in a credit/lease proposal disclosure document; and
  - *ensure that the licensee does not suggest or assist a consumer to enter into, increase the credit limit under, or remain in, an unsuitable credit contract or consumer lease.*

# Responsible Lending - Credit Assistance Providers

- **Exceptions - no duplication where credit provider is also assister**
- A credit provider who provides credit assistance in relation to a credit contract for which it will be the credit provider and a lessor who leases solely on proprietary contracts are not required to perform the *credit assistance* responsible lending obligations (but must perform the credit provider/lessor obligations)

# Responsible Lending - Credit Providers + Lessors

- The key responsible conduct lending obligations applicable to credit providers and lessors under consumer leases are to:
  - provide a credit guide;
  - make an assessment of unsuitability of any relevant consumer lease or relevant credit contract / credit limit increase under credit contract;
  - ensure the licensee does not enter into:
    - an unsuitable credit contract with, or increase the credit limit of a credit contract with, a consumer who is the debtor under the contract; or
    - an unsuitable consumer lease with a consumer who is the lessee under the lease.

# Responsible Lending: Assessments

- Reasonable inquiries to be made for preliminary assessment of unsuitability and for unsuitability assessment:
  - make reasonable inquiries about the consumer's requirements and objectives for the credit contract;
  - making reasonable inquiries about the consumer's financial situation; and
  - taking reasonable steps to verify the consumer's financial situation.
- Credit contract is unsuitable if either assessment finds that:
  - consumer is likely to be unable to comply with financial obligations under contract, or could only comply with substantial hardship; or
  - contract will not meet consumer's requirements and objectives.

# Responsible Lending

- Substantial hardship is presumed if a consumer could only comply with the relevant obligations by selling their principal place of residence
- Impact on refinancing
  - Level of inquiry required to meet 'reasonable inquiries' standard is likely to be greater where the consumer is refinancing (particularly where difficulties meeting repayments, in arrears, on their existing contract).
  - Where a consumer currently unable to meet repayments under contract, a contract with same or a similar level of repayments will be prima facie unsuitable

## How will suitability assessment work?

- Credit limit increases - for cards currently usage pattern and general profile generated - now dead?
- What are reasonable inquiries re financial situation?
- What are reasonable steps to verify?
- Low doc loans dead? Is that good?
- What assumptions can guide "likely to be unable to comply" with financial obligations?
- How are the consumer's requirements and objectives to be ascertained/corralled/recorded/reviewed?



# What is left to the regulations?

- Regulations to the Credit Bills will be tabled in Parliament after the enactment of the Credit laws. Regulations expected to cover:
  - treatment of interest paid in advance for residential investment property
  - setting of fees and charges for lodgement of a licence application and licence renewal
  - exemptions from licensing - for example, exemptions for state-licensed debt collectors (12 months only) and for point of sale credit assistants
  - clarifying the application of responsible lending requirements relating to certain disclosure documents
  - clarifying application of responsible lending provisions
  - establishing the infringement notice regime
  - clarifying the jurisdiction where legal proceedings must be commenced
  - streamlining to licence brokers who hold either an 'A' or 'B' class licence under the *Finance Brokers Control Act 1975* (WA)

# Role of ASIC

- ASIC needs to be resourced with money and people to act as policy maker, legislator, guide and enforcer
  - ASIC has power to exempt or modify the application of licensing requirements
  - ASIC can exclude provision of credit (by instance or class) from NCC
  - ASIC will be able to exercise discretion in imposing penalties where persons have attempted in good faith to comply
- Policy consultation and guidance papers and stakeholder engagement to Oct 09 and beyond
- Consultation papers released on 15 July 2009
  - Consultation Paper 110 - General conduct obligations for credit licenses (attaching draft Regulatory Guide 104 )
  - Consultation Paper 111 - Compensation and financial resources arrangements for credit licensees
- Regulatory guides to be released after passing of legislation and will take into account comments received on consultation papers

# Comments

An artificially short political time frame for this reform led to:

- pressed Treasury policy makers using a flawed precedent (FSR) to meet deadlines
- a consultation process constrained by confidentiality deeds and secrecy and a too short public period meaning input from business and even State and Territory
- a model of overbroad general regulation which requires too much post-enactment adjustment by regulation, and excessive amounts of regulator dispensation and discretion and guidance

Not the fault of ASIC or (principally) of Treasury but a lamentable re-run of FSR - let's not do it again for Tranche 2.

# Comments

- Don't forget unfair contract terms reforms will apply in addition to NCC unconscionable fee and charges provisions- ASIC can use both routes - be on watch re early termination and deferred establishment fees
- Licensing/ conduct obligations for some operators and RL unsuitability assessments are good ideas in principle but needed much more nuancing and practical commercial input as to how the credit business actually works.
- We are now in the era of ASIC (policy maker, legislator and enforcer) and the EDR schemes as interpreter/policy maker and judge (e.g. FOS up to \$250K) (if they can cope with the demand).

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