PARLIAMENTARY JOINT COMMITTEE ON CORPORATIONS AND FINANCIAL SERVICES

Inquiry into impairment of customer loans – questions on notice

1. **Are qualifications required for payday lenders?**
    a. **If so please describe who is responsible for oversight and the registration process that applies to payday lenders.**

Answer:
Any individual or business seeking to engage in credit activities such as providing small amount loans or payday loans needs to obtain an Australian Credit Licence. These licenses are granted by the Australian Securities and Investments Commission (ASIC).
The individual or business seeking to be licensed is required to demonstrate that they have the organisational competence to engage in credit activities. ASIC Regulatory Guide 206: *Credit licensing: Competence and training* provides potential applicants and credit licensees with information on the required competence for Australian credit licensees.
ASIC assesses the organisational competence of the credit licence applicant by assessing the qualifications and experience of the people who manage the credit business and are ultimately responsible for the day-to-day decisions in relation to the provision of the credit activities of the business. We refer to these people as responsible managers.
Responsible managers must have completed:

- a credit industry qualification to at least the Certificate IV level; or
- another general higher level qualification (e.g. a diploma or university degree) in a relevant discipline.

ASIC recognises that the diversity of the credit industry is reflected in the diverse qualifications held by people working in that industry and we have generally not set specific requirements on qualifications. In the case of a credit provider such as a payday lender, relevant qualifications that responsible managers could have might include a Certificate IV in Financial Services, a Diploma in Financial Services (Banking) or a university degree in a financial discipline (e.g. economics, commerce, business, accounting or equivalent)
ASIC must also consider whether certain people in the applicant's business (e.g. directors and senior managers) are fit and proper people to engage in credit activities.
All applicants seeking an Australian Credit Licence (including payday lenders) must complete an application form and provide supporting materials such as a business description summary and police checks. Licensees must be a member of an ASIC approved external dispute resolution scheme (currently the Financial Ombudsman Service or Credit and Investments Ombudsman) and have the appropriate competencies and training to engage in credit activities.

ASIC Regulatory Guide 204: *Applying for and varying a credit licence* provides information on how to apply for an Australian Credit Licence.

2. **In the case of inappropriate lending;**
    a. **Can any person associated with the borrower report to ASIC or can it only be the borrower?**
    b. **If fault is found, what compensation is paid to the original borrower?**

Answer:

(a)
ASIC regulates credit providers in accordance with the consumer credit regulatory framework in the *National Consumer Credit Protection Act 2009*, the *Australian Securities and Investments Commission Act 2001*, and related laws.

ASIC appreciates receiving reports of alleged misconduct from members of the public about their experiences with consumer credit providers. These reports provide ASIC with valuable intelligence information and help us to understand consumer concerns.

ASIC will assess the information provided to determine if the concerns raised suggest breaches of the laws we administer, and whether we have sufficient grounds to take further action in response to any alleged breaches.

Any person can lodge reports of alleged misconduct about a loan, including the borrower or an associate of the borrower. For ASIC to raise specific concerns with a credit provider about a particular loan, we will likely need the consent of the borrower. This is because these matters will generally relate to the borrower's personal circumstances and personal information.

Where an associate of a borrower has lodged the report of alleged misconduct with ASIC, ASIC may be limited in how we can pursue any concerns, if the associate does not provide us with written consent from the borrower for the associate to act on the borrower's behalf. In addition, the focus of ASIC's regulatory action must be the public interest, and ASIC's role does not generally extend to taking actions against consumer credit providers on behalf of individual borrowers in relation to their personal circumstances.

ASIC provides information about how customers can seek to resolve disputes with credit providers in our Information Sheet 174 *Disputes with financial services or credit providers*.

(b)
ASIC regulates credit providers in accordance with the consumer credit regulatory framework in the *National Consumer Credit Protection Act 2009*, the *Australian Securities and Investments Commission Act 2001*, and related laws.

These laws include a range of obligations on credit providers, including the responsible lending obligations in Division 3 of the *National Consumer Credit Protection Act 2009*. Broadly, the responsible lending obligations require credit providers to make inquiries into a loan applicant's circumstances to determine if the proposed loan would not be unsuitable for the application. The responsible lending obligations are civil penalty provisions, each with a maximum penalty of 2,000 penalty units (currently $360,000).

ASIC is unable to comment specifically on what remedy may be available to a particular borrower if they are successful in a private dispute against their lender in relation to their loan.

The remedies available in a private action will depend on what the parties may agree when resolving the dispute privately, or what remedies can be issued by the external body that

resolves the dispute, such as an external dispute resolution scheme or a Court. This could include compensation orders or damages.

ASIC is aware that where borrowers have been successful against lenders for disputes about the suitability of their loans, external dispute resolution bodies have tried to design orders where the borrower is placed in the position as though they had not taken out the loan.

This often means that the borrower will need to repay the loaned amount to the credit provider, less any interest or principal repayments or other charges to the credit provider for taking out the loan. This may mean the borrower is required to sell any property purchased with the loaned funds, or to refinance the loan with another lender.

3. **Are there any legal requirements that preserve customers' terms and conditions where a customer has signed a contract with a second tier bank (e.g. St George) that is then acquired by a first tier bank (e.g. Westpac)?**
    a. **Are the original terms and conditions still binding or can the first tier bank impose its own contract terms and conditions onto the pre-existing contracts without notice or option to refinance, particularly where the second tier bank continues to operate under its original name?**
    b. **Also, when a second tier bank is bought out by one of the big four banks do their regulatory requirements for either bank change?**

Answer:

There is no such legal requirement. The original terms of the loan contract will continue to apply unless and until the acquiring bank varies the terms of the contract in accordance to what is permitted under the contract.
It is common practice for loan contracts to include provisions which permit the bank (either the original bank or the bank which has made the acquisition) to unilaterally vary the terms and conditions of the loan.
A loan contract will ordinarily require a bank to give the customer notice of any variation to the terms, including in some cases notice by publication in a newspaper.
In exercising a unilateral right to vary the contract, the bank must act reasonably.
The customers' terms and conditions will not necessarily change following an acquisition, however, the acquiring bank may exercise those rights to make changes to the contract - for example, the acquiring bank may wish to transfer the contract from the other bank's banking systems onto their own systems and in that case, the contract may need to be varied to reflect the new system).

a)

As noted above, the original terms of the loan contract will continue to apply unless and until the acquiring bank varies the terms (assuming the contract permits the bank to do so). The notice periods will normally be specified in the contract.

A consumer may seek to refinance their loan on receiving notice that a particular variation is being made or following that variation. Whether the customer has an option to refinance without an additional charge, is a matter for the contract.
Whether the acquiring bank continues to use the original bank's name in its business does not affect either the acquiring bank's ability to vary the terms and conditions of the loan or the consumer's ability to refinance.

b)

This will depend on how the acquisition of the second tier bank by the first tier bank is given effect.
From ASIC's perspective:

- if the second tier bank is maintained as a separate entity, the regulatory requirements for both the banks do not change. The second tier bank will maintain its own licenses (i.e. Australian financial services licence and Australian credit licence) and will be required to manage its own compliance programs.
- if the business of the second tier bank is transferred into the first tier bank by the transfer process established by the *Financial Sector (Business Transfer and Group Restructure) Act 1999*, the first tier bank will be responsible for the combined

business as it becomes the successor in law of the transferring bank and is subject to the duties, obligations, immunities, rights and privileges previously applying to the original bank. This would preserve the consumer's rights in respect of acts or omissions of the original bank. The company which operated the original bank is generally deregistered and ceases to exist after the transfer. The decision for the transfer to take effect under the *Financial Sector (Business Transfer and Group Restructure) Act 1999* is made by the Australian Prudential Regulation Authority (APRA). The licence of the acquiring bank must cover the activities of both combined businesses with the resultant obligations (e.g. responsible managers, complaints, conflict of interests)

We note that the banks' prudential requirements will be affected by the acquisition. APRA will be able to provide further information in respect of this issue.

4. **In your submission you listed complaints that have been received in relation to matters that are the subject of the loans inquiry. Could you inform the committee of the extent to which the people who have submitted those complaints have also made submissions to the inquiry?**

Answer:

Paragraph 28 of ASIC's submission to the inquiry states that, in the five years from 1 July 2010, we received 66 reports of alleged misconduct from people raising concerns about a bank's or non-bank financial institution's treatment of commercial loans that relate to the issues raised in the inquiry's terms of reference. Generally these 66 reports of alleged misconduct came from the director of the company that borrowed the funds.

These 66 reports of alleged misconduct include 14 from people or entities who we can identify as making submissions to the inquiry in their name. ASIC is unable to ascertain whether any authors of name withheld or confidential submissions also lodged reports of alleged misconduct with ASIC that were counted in these 66 reports.

Paragraphs 34-35 of ASIC's submission provides general information on ASIC's response to the 66 reports of alleged misconduct, and why we determined not to take further action.

http://www.aph.gov.au/Parliamentary_Business/Committees/Joint/Corporations_and_Financial_Services/customer_loans/Submissions

5. **Page 21 of ASIC's submission sets out requirements regarding default notices. How does ASIC check whether those requirements are being met?**

Answer:
ASIC's submission sets out the requirements for default notices as they apply to consumer credit under the National Credit Code. ASIC does not conduct regular spot checks on compliance with the default notice requirements and conducting such checks would necessarily require resources to be diverted away from other regulatory activities conducted by ASIC. However, ASIC may check a lender's compliance with these requirements when assessing reports of alleged misconduct regarding the enforcement of a credit contract. Notwithstanding any checks by ASIC, there are a number of other ways that any potential consumer harm arising from a lender's non-compliance with the default notice provisions of the National Credit Code can be addressed.

Where a consumer is concerned about the enforcement of a credit contract, and is not able to resolve the matter directly with the lender, the consumer can take the dispute to an external dispute resolution scheme. Generally, dispute resolution schemes will look at all the circumstances surrounding such complaints including whether the default notice and hardship provisions of the National Credit Code have been complied with. External dispute resolution schemes can make determinations in relation to disputes with individual consumers that are binding upon lenders. In addition, where external dispute resolution schemes identify any systemic issues with a lender's conduct they will seek to address this directly with the lender and will also report to ASIC on the issues identified and the steps taken by the lender to address them.

In addition, a lender's compliance with the default notice requirements of the National Credit Code may also be scrutinised by the Court in the context of private legal proceedings related to the enforcement of credit contracts.

6. **Is ASIC aware of the percentage of receivers who are not members of ARITA or another professional body?**
    a. **What accountability arrangements are there for receivers who are not a member of a professional body?**

Answer:

ARITA's submission to the Productivity Commission regarding the *Business Set-up, Transfer and Closure Inquiry* (page 4) states that 76% of registered liquidators are ARITA members.

There were 705 registered liquidators as at 31 December 2014. Based on information ASIC obtained from registered liquidator annual statements lodged with ASIC, 652 of 679 registered liquidators who hold a certificate of public practice (meaning that they are principals of practices that provide public services) are members of one or more of the accounting professional bodies (that is bodies other than ARITA).

Section 418 of the Corporations Act 2001 requires a receiver to be a registered liquidator.

Being a receiver is a role that a registered liquidator performs in relation to a company. The role usually ends when the receiver realises all assets subject to the security interest and accounts to the company.

The *Corporations Act 2001* imposes certain obligations on a registered liquidator appointed as a receiver of a company. The obligations apply to registered liquidators who are appointed as receivers regardless of whether they are a member of a professional body.

Some of the accountability measures under the *Corporations Act 2001* include:

- section 420A – duty of care in exercising power of sale
- section 423 – supervision of controller by the Court if not faithfully performing functions or has not faithfully performed functions
- section 424 – controllers (which includes a receiver, or a receiver and manager) can apply to the Court for directions regarding any matters arising in connection with the performance or exercise of functions or powers
- section 425 – receiver's remuneration may be fixed or varied by the Court upon application by certain persons
- section 434A – Court may remove a controller who has been guilty of misconduct in connection with performing or exercising of any of controller's functions and powers
- section 432 – controller is required to lodge 6 monthly accounts with ASIC

Furthermore, receivers are registered liquidators who still need to observe relevant professional standards, other relevant legislation and common law. They need to adequately and properly perform their duties and functions having regard to accepted professional conduct.

7. **What processes are in place to check that receivers do achieve the best price that is available when liquidating assets?**

Answer:

Section 420A of the Corporations Act is primarily focused on whether a proper process was undertaken by the receiver to sell the property in all the circumstances. The section does not impose an obligation to achieve the best possible price.

If there are concerns with the sales process, primarily, the borrower, or the directors, can either bring Court proceedings or report alleged misconduct to the relevant regulatory or industry bodies.

ASIC reviews all such reports of misconduct in accordance with its procedures. ASIC can further review a receiver's compliance with section 420A if it appears a proper sales process has not been followed or undertake a broader review of the practitioner's conduct as part of its surveillance activities.

The dominant view is that a breach of s420A does not confer a right to damages.

8. **Could ASIC provide information on how many occasions a court has made orders that alter the remuneration of the receiver, liquidator, voluntary administrator or deed administrator?**

Answer:

ASIC cannot provide information regarding the number of occasions a Court has made orders altering the remuneration of a receiver, liquidator, voluntary administrator or deed administrator.

It is not a requirement that ASIC be served with this type of application.

ASIC generally does not get notified of a Court's decision for this type of application.

9. How are creditors able to initiate a review of a receiver's remuneration?

Answer:

The receiver's remuneration is a matter of contract. Their entitlement to remuneration is usually contained in the loan agreement between the secured party and the company.

A creditor may apply to the Court to inquire into the conduct of a receiver under section 423 of the *Corporations Act 2001* based on remuneration concerns.

In addition, if a receiver applies to the Court to fix his/her remuneration under section 425 of the *Corporations Act 2001*, any creditor may give the receiver a notice of objection to the remuneration claimed and the grounds of objection (rule 9.1(3) of the Corporations Rules).

ASIC or a liquidator or administrator appointed to the company also has standing under section 425 to apply to the Court for an order to fix (or vary an order of the Court made under the section) the amount of remuneration to be paid to a receiver.

10. At the hearing in Sydney on the 18th of November, Senator Williams asked the following questions of the ARITA representative: .

> **Senator WILLIAMS: Given that it costs ASIC $10 million to police your industry and you contribute just $40,000 a year in registrations, you will not mind tossing a bit at ASIC's pocket, will you?**
> **Mr Winter: We have very strong concerns about ASIC's performance and effectiveness in that space. If it is costing $9 million to find—**
> **Senator WILLIAMS: 10.**
> **Mr Winter: Nine is the number that they have published in their funding model.**
> **Senator WILLIAMS: I have not looked at the latest model.**
> **Mr Winter: If they are only able to get six administrative outcomes a year, which is the average since 2011, and they are administrative outcomes, that is $1.4 million per outcome, and they have got 25 or so staff working on it. I would submit that either there is not the profound problem that there is claimed to be, or they are not very effective in getting it. It is one or the other.**

Could ASIC respond to Mr. Winter's comment that "*I would submit that either there is not the profound problem that there is claimed to be, or they are not very effective in getting it. It is one or the other*."

Answer:

These comments and the conclusion do not reflect evidence readily available from ASIC's public reporting regarding insolvency practitioners.

This reporting demonstrates legitimate concerns with a minority of practitioners that we believe could undermine overall confidence in the profession. Our concerns usually relate to independence, competency and improper gain.

This serious risk element aside, our recent program addressing lack of compliance by registered liquidators with basic lodgement obligations and publishing notices shows there is a concerning lack of compliance with these obligations more broadly. The obligations are important because they help maintain transparency and confidence in the insolvency process. Importantly, in some instances, lack of compliance with these basic obligations has proven to be a significant 'red flag' for more systemic problems with certain practitioners.

Our programs aim to promote a better compliance culture within the profession. We regularly write about our project work, and other enforcement work, in various editions of ARITA's industry association journal.

Mr Winter refers to 25 ASIC staff working on the regulation of registered liquidators. We assume this refers to staff in ASIC's Insolvency Practitioner Team. It is incorrect to suggest that all of these staff members only work on enforcement matters against insolvency practitioners. These staff also work on matters supporting registered liquidators (for example, our Assetless Administration Fund work which leads to enforcement action against directors and others). Of course, the $9 million does not include the costs associated with the latter type of work.

Mr Winter refers to an 'average of six administrative outcomes a year' by ASIC since 2011. In fact, fulsome information about all of ASIC's activities in supervising registered liquidators

(including both its compliance activities and enforcement outcomes) has been published each and every year since 2011.[1]

Having regard to this published information Mr Winter's evidence is incorrect. The total number of enforcement outcomes for the period 1 July 2011 to 30 June 2015 is 37. As our published material shows the matters involve a range of misconduct in the areas of independence, competency and improper gain and comprise:

- 7 CALDB[2] 'conduct' applications (six successful with one decision pending). These applications go to serious conduct issues.
- 1 CALDB 'administrative' application. This relates to more procedural concerns.
- 7 Enforceable Undertakings
- 15 Voluntary Undertakings
- 3 Court matters including one court inquiry
- 5 decisions by ASIC delegates regarding the ability to practice as a liquidator.

These CALDB outcomes, and the enforceable undertakings and voluntary undertakings, have often resulted in the following:

- the person's registration as a liquidator being cancelled or voluntarily surrendered; and/or
- the person agreeing to an independent party being appointed to review the conduct of future external administration appointments.

Labelling these outcomes as "*administrative*" suggests matters of a minor nature. However, for practitioners, suspension or cancellation of their registration as a liquidator is clearly a very serious matter impacting their livelihood.

Cost of regulation

As previously stated, the amount of $9 million, (cited in in Treasury's consultation paper concerning the government's proposal for an industry funding model for ASIC), is not wholly attributable to "enforcement" outcomes. Our public reporting of ASIC's work in regulating registered liquidators and Treasury's public consultation paper on ASIC's proposed funding model notes our forecast regulatory activities for registered liquidators include surveillance (50%), education (5%) and enforcement (45%). The $9M reflects the cost of all of these identified activites in regulating the profession.[3] Apart from the enforcement outcomes we have already achieved, a key part of the $9 million relates to current investigations and surveillance work that have not yet resulted in public outcomes. There is a significant pipeline of this work.

To suggest an "average cost" for an enforcement outcome by a division of total costs by a number of reported "enforcement" outcomes conveys nothing as a measure or indication of the extent of market misconduct or public confidence. It ignores, for example, the different types of action, their complexity, the intensity with which a person of interest defends an

[1] Report 480 ASIC regulation of registered liquidators: January to December 2014
Report 389 ASIC regulation of registered liquidators: January to December 2013
Report 342 ASIC regulation of registered liquidators: January to December 2012
Report 287 ASIC regulation of registered liquidators: January to December 2011

[2] CALDB or the Companies Auditors and Liquidators Disciplinary Tribunal is a statutory body that can suspend or terminate a person's registration as a liquidator.

[3] As noted in Treasury's consultation paper, costs include both ASIC's cost of direct supervision and ASIC's overhead costs

ASIC action, the disciplinary forum in which proceedings are commenced and the final outcome. An enforcement action might involve a critical market issue or market participant, which impacts the market more significantly than another action. For example, ASIC's action to remove the liquidators in the Walton Constructions case[4] resulted in a decision of the Appeal Court which set a clear test of independence for all registered liquidators.

ASIC is comfortable with its anticipated expenditure on corporate insolvency matters given the seriousness of misconduct we have seen in a number of instances as demonstrated, for example, by various Parliamentary inquiries in recent times.

[4] *ASIC v Franklin (liquidator), In the matter of Walton Constructions Pty Ltd* [2014] FCA 85

11. Would ASIC please advise the committee about your understanding of the extent to which business customers (that are not small businesses) are able to negotiate loan contract terms as discussed in the attached excerpt from the Committee Hansard on 18 November 2015.

Answer:

We understand that the size of the business involved in the negotiation, and the amount of money being borrowed, are factors which may have an effect on the ability for a business to negotiate the terms of a loan with a bank. However, we are unable to comment any further on this point as we are not familiar with the negotiation policies of particular banks in respect of such large business customers.