

Impairment of Customer Loans (May 2016)

Recommendation 1

The committee recommends that appropriate regulation and legislation be put in place to prevent banks profiting from defaulted or impaired loans by requiring banks to:

- a. levy additional costs that the bank incurs when a loan is in default or is impaired in accordance with a schedule or process approved by the Australian Small Business and Family Enterprise Ombudsman;
- b. provide transparent and accountable information to borrowers on the additional costs that the bank incurs when a loan is in default or is impaired; and
- c. where a bank charges additional fees or interest of any kind associated with a defaulted or impaired loan;
 - o the increased costs incurred by the bank must be disclosed in the loan contract, where possible, as a flat dollar figure; and
 - o any amount charged that exceeds the increased costs incurred by the bank is to be paid off the loan principal.

The Government notes the recommendation.

In response to Recommendation 1.13 of the Financial Services Royal Commission (charging default interest), the ABA Banking Code has been amended to commit signatories to not charge default interest to farmer borrowers in the event of drought and natural disasters.

Recommendation 2

The committee recommends that the banking codes of practice administered by the Australian Bankers' Association or the Customer Owned Banking Association and other regulatory arrangements be revised to require that:

- a. authorised deposit taking institutions must commence dialogue with a borrower at least six months prior to the expiry of a term loan. Further, where a monetary default has not occurred, they must provide a minimum of three months notice if a decision is made to not roll over the loan, even if this means extending the expiration date to allow for the three months following the date of decision;
- b. if a customer is meeting all terms and conditions of the loan and an authorised deposit taking institution seeks to vary the terms of the loan, the authorised deposit taking institution should bear the cost associated with the change and provide six months notice before the variation comes into effect;
- c. customer protections relating to revaluation, non-monetary defaults and impairment should be explicitly included in the code; and
- d. subscription to a relevant code becomes mandatory for all authorised deposit taking institutions.

The Government notes the recommendation.

Since this recommendation was made, the Banking Code of Practice has been updated in Chapter 23 where it specifies rules for banks to give at least 3 months' notice of a decision not to extend a small business loan, before the loan is due to be repaid in full.

Recommendation 3

The committee recommends that responsible lending provisions, including ASIC's monitoring under the National Consumer Credit Protection Act 2009, be extended to small business loans.

The Government agreed to recommendation 1.9 of the Financial Services Royal Commission, that the provisions not be extended to small businesses.

Recommendation 4

The committee recommends that the government bring forward legislation and other measures to enable the Australian Small Business and Family Enterprise Ombudsman to:

- a. lead and/or coordinate the implementation of the outcomes of this inquiry and all other reforms that relate to small business lending in order to avoid the significant risk that major gaps and flaws in the protections for small business would remain;
- b. bring together a team with expertise in financial services, ethics and education to establish standards for the conduct of bank management and their employees in relation to small business loans and to work with the banking industry to implement those standards and appropriate mediation and dispute resolution schemes;
- c. work with the banking industry to develop mandatory nationally consistent standardised loan contracts that include a cover sheet summarising the obligations of the customer and the consequences of any breach;
- d. have the power to direct the parties to a dispute to participate in mediation or dispute resolution;

In response to the review of external dispute resolution and complaints arrangements in the financial system, the Government established the Australian Financial Complaints Authority (AFCA) to be a new one stop shop to deal with financial system complaints of consumers and small businesses. The Australian Small Business and Family Enterprise Ombudsman has published documents to educate businesses on the type of available funding products, including fintech lenders, and guide businesses to resolve disputes.

<p>e. where gaps in the implementation of those standards and appropriate dispute resolution schemes remain, to act as a small business loans dispute resolution tribunal; and</p> <p>f. direct the parties to a dispute to participate in commercial arbitration for larger commercial loans.</p>	
<p>Recommendation 5 The committee recommends that appropriate legislation and regulations be put in place to:</p> <ul style="list-style-type: none"> a. prohibit conflicted remuneration for all bank staff; b. extend the clawback period on any bonus or like incentives provided to management and senior executives involved in the line approvals or systematic oversight of lending; c. require bank officers to act in the best interests of a small business customer; d. require officers from lending and credit management departments to provide consistent information to borrowers, including: <ul style="list-style-type: none"> i. copies of valuation reports and instructions to valuers; and ii. copies of investigative accountants' reports and instructions to investigative accountants and receivers; e. require lending officers and credit management officers to ensure that: <ul style="list-style-type: none"> i. the valuation instructions do not change during the term of the loan agreed in the loan contract; and ii. businesses are valued as the market value of a going concern, not just a collection of business assets and that the market value of all security supporting the loan are taken into account, not just real property. 	<p>The Government notes the recommendation.</p> <p>The Government supported recommendation 5.5 of the Financial Services Royal Commission which recommended that banks fully implement the recommendations of the Sedgwick Review. The recommendations of the Sedgwick Review addressed issues of remuneration in banks.</p>
<p>Recommendation 6 The committee recommends that nationally consistent arrangements be put in place for:</p> <ul style="list-style-type: none"> a. farm debt mediation; b. small business debt mediation; and c. the professional standards and conduct of valuations in relation to small business loans. 	<p>In response to Recommendation 1.11 of the Financial Services Royal Commission, the Government agreed to establish a national farm debt mediation scheme.</p> <p>This is being progressed by Minister for Agriculture through the Agriculture Ministers Forum. Further, an independent review of the Banking Code of Practice, which sets standards for small business lending, is currently being undertaken.</p>
<p>Recommendation 7 The committee recommends that the link between lenders and key creditors, such as builders who may be building on a developer's land, needs to be formalised so that lenders have an obligation to advise creditors once a loan is placed in default.</p>	<p>The Government notes the recommendation.</p>
<p>Recommendation 8 The committee recommends that the Parliamentary Joint Committee on Corporations and Financial Services conducts an inquiry to examine the regulatory environment for valuers with a view to:</p> <ul style="list-style-type: none"> a. reforming the industry to improve ethical and professional standards for valuers; b. improving transparency and independence within the industry; and c. preventing them from being captured by banks. 	<p>The Government notes the recommendation.</p>

<p>Recommendation 9</p> <p>The committee recommends that if an authorised deposit taking institution is intending to appoint a receiver:</p> <p>a. that is from the same company that was engaged as an investigative accountant, the borrower should be given an opportunity to request an alternate company if the borrower is concerned about a conflict of interest;</p> <p>b. in addition to the requirement to sell assets for fair market value under section 420A of the Corporations Act 2001, receivers should be required to sell a business as a going concern where possible if this will result in a higher return rather than separately selling the assets within the business; and</p> <p>c. that receivers or similar entity selling assets under section 420A be required to take every reasonable step to ensure those assets are sold at or as close to listed market value as possible under the following conditions:</p> <p>i. proof of marketing through but not limited to mainstream media, catalogues and online;</p> <p>ii. in cases with no monetary default, marketing periods consistent with Prudential Standard APS 220;</p> <p>iii. in the case where monetary defaults have occurred, the marketing period can be reduced below the APS 220 standard where a shorter marketing period can be demonstrated to be in the borrower's best interest; and</p> <p>iv. that a strong penalty regime for breach of section 420A be administered by the Australian Securities and Investments Commission.</p>	<p>The Government acknowledges this recommendation and notes that receivers are already subject to strict requirements in administering the property of insolvent companies.</p>
<p>Recommendation 10</p> <p>The committee recommends that the Parliamentary Joint Committee on Corporations and Financial Services conduct an inquiry to examine the remuneration of insolvency practitioners.</p>	<p>The Government notes the recommendation.</p>
<p>Recommendation 11</p> <p>The committee recommends that:</p> <p>a. lenders should engage independent experts nominated by the Australian Small Business and Family Enterprise Ombudsman to critically examine contentious cases to determine what, if any, restitution may be appropriate in the light of the standards developed by the Australian Small Business and Family Enterprise Ombudsman, with particular regard to unconscionable conduct; and</p> <p>b. that funding through a user pays industry funding model be provided to Australian Small Business and Family Enterprise Ombudsman –acting as a tribunal–to consider cases retrospectively in the event that lenders do not choose to voluntarily examine contentious cases as recommended above.</p>	<p>The Government acknowledges these recommendations and notes that it has actioned improvements to Ombudsman services since the recommendations were made. The Australian Financial Complaints Authority (AFCA) was established on 1 November 2018, replacing the Financial Ombudsman Service. AFCA's service is offered as an alternative to tribunals and courts to resolve complaints consumers and small businesses have with their financial firms.</p>
<p>(Dissenting Recommendation)</p> <p>That a Royal Commission be established to examine the banking and financial sector, and particularly:</p> <ul style="list-style-type: none"> • how widespread instances of illegal and unethical behaviour are within Australia's financial services industry; • how Australia's financial services institutions treat their duty of care to their customers; • how the culture, ethical standards and business structures of Australian financial services institutions affect the behaviour of these institutions; • whether Australia's regulators are really equipped to identify and prevent illegal and unethical behaviour; • comparable international experience with similar financial services industry misconduct and best practice responses to those incidents; and • other events as may come to light in the course of investigating the above. 	<p>The Government notes the recommendation. The Financial Services Royal Commission was established.</p>