

NSW GOVERNMENT

FINAL SUBMISSION TO REVIEW OF BANKING CODE OF PRACTICE

JUNE 2001

1. Introduction

Banking is an essential service and, as such, the delivery of banking services in a fair, accessible and affordable manner is an issue that affects almost all consumers in NSW.

The Code of Banking Practice (CBP) is important in providing signatory banks with a benchmark for the delivery of banking services. The review of the CBP is timely in that it provides interested parties with an opportunity to assess its effectiveness and propose areas needing further attention.

The NSW Government has welcomed this opportunity and outlined issues and recommendations in its submission to the Review (August 2000). The Review of the Code of Banking Practice Issues Paper, February 2001 has addressed many of these issues.

The NSW Government is pleased to submit further comments relating to the recommendations in the Issues Paper.

2. Code Coverage

The current CBP only covers customers that are individuals who acquire a banking service that is wholly and exclusively for their private or domestic use. The NSW Government submission raised problems with this narrow definition of customer in the CBP and recommended that the definition be expanded to cover banking services that are provided 'wholly or predominantly for personal, domestic or household purposes' (p1). In addition, it was recommended that the CBP be expanded to cover banking services to small business, with further work undertaken to devise an appropriate definition of small business.

The Issues Paper recognises problems associated with the narrow definition of customer, particularly anomalies with the Australian Banking Industry Ombudsman (ABIO) Scheme's expansion to include complaints from small business. The interim recommendation that the Code apply to any banking service provided to an individual, whether alone or jointly with another individual is supported by the NSW Government. The interim recommendation to extend the operation of the Code to small business is also supported. It is acknowledged that further work is required to develop a suitable definition of small business.

3. Effects of bank closures on small communities

The impact of bank closures on communities, whether they be in suburbs or non-metropolitan areas, is major. Communities need time to consider alternatives and re-arrange their banking. This is particularly difficult where the branch closing is the last one.

The NSW Government submission recommended the CBP should include a requirement to comply with a branch closure protocol. This should include:

- ♣ 6 months notice of closure in non-metropolitan areas where the last branch is closing;
- ♣ 3 months notice of closure in other cases; and
- ♣ a requirement to waive exit penalties and fees for moving accounts and loans to another institution for customers of closed branches.

The Issues Paper reviews the examination of this issue by the House of Representatives Standing Committee on Economics, Finance and Public Administration (The Hawker Committee) which conducted an inquiry into regional banking services. Its final report Regional Banking Services – Money too far away was released in March 1999 and contained a number of recommendations on branch closures. The interim recommendation that the CBP incorporate the proposals made in recommendations 20.1 to 20.4 of the Hawker Report is supported by the NSW Government.

The Australian Bankers' Association (ABA) announced, as part of its package of initiatives (26 March 2001), that banks who are covered by the CBP would provide three months notice for the closure of rural and remote branches.

However, the NSW Government submission recommended a 6 month notice of closure in non-metropolitan areas where the last branch is closing. The Hawker Report only recommends 3 months. While this would be an improvement to the current situation where there is no requirement for any formal notice to be given to customers, the NSW Government believes a longer period is appropriate for rural and regional communities who are losing their last bank branch. Metropolitan customers may have the option of banking in another suburb or moving to a credit union or building society. In small towns, communities need time to consider alternatives that may include attracting a credit union or community bank to their town. A 6 month notice period would allow time for community discussions and a feasibility study.

Recommendation 1

That the CBP should include a 6 month notice of closure in non-metropolitan areas where the last branch is closing.

4. Fee disclosure at ATMs

The issue of whether current fee disclosure arrangements are adequate is being considered by a number of processes.

The Parliamentary Joint Statutory Committee on Corporations and Securities released the Report on Fees on Electronic and Telephone Banking in February 2001. The Inquiry found that the lack of fee disclosure at the point of transaction of electronic banking is a major shortcoming. It recommended that a framework for a real-time

disclosure regime on electronic and telephone banking be established in no more than 2 years and implemented within 6 months of the finalisation of the framework (EFTPOS excluded on technical grounds). The Federal Government has not responded to this report.

The Australian Securities and Investments Commission (ASIC) established a working group to look at the issue of transaction fee disclosure. ASIC released the draft Guide to Good Transaction Fee Disclosure for Banks, Building Societies and Credit Unions in April 2001. While this draft Guide is subject to amendment following a consultation process, its recommendations include:

- ♣ consumers should know at the transaction point whether they could be charged a 'foreign ATM fee' because the ATM is not part of their institution's network; and
- ♣ institutions should commit to providing real-time transaction fee disclosure when they redesign and upgrade their equipment, so that consumers know the cost of a transaction prior to the transaction being completed.

The NSW Government submission (p4) recommended banks should provide information on the cost of electronic banking transactions (eg via ATM, phone banking, Internet banking, direct business banking) at the time of the transaction. This information should include:

- ♣ the cost of the transaction;
- ♣ the number of remaining fee free transactions for the month; and
- ♣ an opportunity to terminate the transaction without penalty.

The timetable for implementation depends on the time needed to revise interchange standards, revise computer programs and (if necessary) upgrade equipment. An implementation period of up to two years is recommended.

The Issues Paper recommends waiting for the outcomes of the ASIC Transaction Fee Disclosure Working Group before considering this matter, possibly through a supplementary issues paper. ASIC has however released a draft Guide that will be finalised following a consultation process.

The draft ASIC Guide is a good set of principles regarding disclosure of fees. The points at which fee disclosure is important for consumers and options for providing this information are outlined in the draft Guide. Suggestions for good fee disclosure practices, particularly statements, will go some way in providing useful information to consumers. The most important issue however from a consumer perspective is real-time disclosure or disclosure at time of transaction. The draft Guide suggests '*ideally, institutions should commit to a timeframe for implementing real time disclosure*'.

Recommendation 2

The CBP should contain a good fee disclosure requirement, based on the ASIC draft Guide. This should include a commitment by banks that are signatories to the CBP to a timeframe for real time disclosure.

5. Credit Issues

It is noted that the Uniform Consumer Credit Code (UCCC) has specific provisions regulating consumer credit, including guarantees and co-borrowers. The Issues Paper recommends that any significant overlap between CBP provisions and other laws,

particularly the UCCC, is undesirable and that overlapping CBP provisions be deleted. This recommendation is supported.

5.1 Credit assessment and capacity to repay

The NSW Government submission expressed concern over rising personal debt levels in Australia, particularly debt on revolving credit, which is currently growing by about 30 percent per annum. The NSW Government has been examining credit over-commitment and possible options for encouraging responsible lending practices. This has included:

- ♣ Discussion Paper on Credit Over-commitment and Responsible Lending, July 2000 tabled by the Minister for Fair Trading at the Ministerial Council on Consumer Affairs;
- ♣ Consumer Week 2000 Credit Phone-in (December 2000) where over 1,000 callers were surveyed about credit problems; and
- ♣ Consumer Credit Round Table Conference, 22 February 2001 where industry, consumer and government representatives discussed credit over-commitment and areas for reform.

One of the specific areas of concern is credit assessment. If adequate assessment procedures were in place, consumers would be less likely to be given credit that they cannot afford. The NSW Government submission argued that the present BCP clause on a bank's obligation to assess a customer's capacity to repay before being provided credit [para 15.1] is inadequate because the clause:

- ♣ only requires the bank to *consider* the issue, not decline credit if the consumer does not have the capacity to repay;
- ♣ is completely subjective, as a bank is only required to consider the factors that *the bank* considers relevant; and
- ♣ only lists the factors that *may* be relevant.

The NSW Government submission (p5) recommended the value of a uniform code of practice on credit assessment criteria should be investigated as an option for standardising credit application and assessment criteria. Such a standard would make it harder for a credit provider to justify lending to over-committed debtors and would encourage consumers to give full disclosure of their financial status.

The Issues Paper acknowledges the existing BCP provision (clause 15.1) on credit assessment fails to set any objective standards and compares poorly with the recently approved Mortgage Industry Association of Australia Code of Practice provisions. The interim recommendation that the existing clause 15.1 be replaced with the following wording would go a long way in tightening credit assessment:

'A bank will exercise the care and skill of a diligent and prudent banker in assessing the level of credit or loan funds it agrees to lend to a customer in order to satisfy itself that the level of credit or the loan funds are suited to the customer's stated financial needs and within the customer's capacity to repay.' (p69)

In addition, the NSW Government is currently carrying out research on credit over-commitment, particularly looking at existing industry credit assessment procedures. This research is also reviewing existing Uniform Consumer Credit Code provisions¹

¹ Section 62 (3) relating to changes to credit limits and Section 70. 2 (1) relating to reopening of unjust contracts

in relation to credit assessment to assess their adequacy in relation to credit over-commitment.

5.2 Implementing Family Court decisions

The NSW Government submission (p6) raised difficulties faced by parties to a Family Court settlement or ruling where joint debts are involved and recommended:

- ♣ Where a Family Court ruling or settlement involves the removal of one party from a joint mortgage, the Code should require a bank to effect the mortgage transfer and consent to any related transfer of title.

The Issues Paper interim recommendation that banks publish guidelines by 1 July 2001 on how they will effect Family Court determinations is supported.

6. Guarantors and Co-borrowers

6.1 Coverage

The application of the CBP to guarantees is far too narrow, as acknowledged by the Issues Paper. However, while the NSW Government submission (p7) recommended the Code's provisions for guarantors should only exclude loans where the borrower is a public corporation, the Issues Paper has opted for a more limited option. The interim recommendation to extend Code provisions to individuals who guarantee a loan to an individual or small business, whether incorporated or not is however supported as this will cover more people than current provisions.

6.2 All money guarantees

All money mortgages are a particular trap for guarantors as the bank can extend credit far exceeding what the guarantor anticipated. While all money guarantees are not common, the NSW Government submission (p7) points out that there may be many all money guarantees which were accepted before the credit part of the CBP came into force. The submission (p8) recommends that the CBP require banks to revise all guarantees with an all moneys clause in order to limit liability. This recommendation is rejected by the Issues Paper as being beyond the scope of the CBP and would need to be pursued through legislative means.

6.3 Information provided to a guarantor

Inadequacies within the existing CBP regarding information provided by the bank to the prospective guarantor have been acknowledged in the Issues Paper. The main deficiency is the requirement for the borrower's consent before a bank can provide the prospective guarantor with a copy of the loan contract and recent account statements.

The NSW Government submission (p8) recommended banks should be obliged to provide the prospective guarantor with all the information that the bank had available to assess the loan risk (or a summary). If the borrower does not consent, the bank should refuse to accept the guarantee.

The Issues Paper covers this through the interim recommendation that banks provide prospective guarantors with all the relevant information in their possession and that this is not conditional on the principal debtor's consent. The Issues Paper does not specifically mention a bank's responsibility to provide information to a prospective

guarantor where a guarantee is obtained over existing credit. It should be clarified that provisions for the disclosure of information to prospective guarantors apply equally to existing credit.

6.4 Reducing guaranteed amount

The NSW Government submission (p7) points out that circumstances relating to a guarantee may change, for example the financial situation of either the borrower or guarantor may deteriorate or their relationship may change. In this circumstance, the guarantor should have the right unilaterally to vary the amount of the guarantee, with some exceptions to protect the bank's interests. This is covered by the Issues Paper interim recommendation that the guarantor be given a contractual right to vary the guarantee by reducing the cap on liability or limiting the amount or nature of the liabilities guaranteed, subject to appropriate qualifications to protect the bank's financial position and is therefore supported.

6.5 Independent legal advice

Problems associated with independent legal advice were raised in the NSW Government submission (p9), in addition to several other submissions. The Issues Paper canvasses these matters in some detail and proposes a number of interim recommendations. These recommendations would result in additional information being provided to the prospective guarantor by the bank, referral to independent legal advice, a one day gap between receiving information and signing the loan documents and signing the loan documents in the absence of the borrower. These measures are supported.

The issue of independent legal advice is the most complex, for reasons outlined in the NSW Government submission (p9). The interim recommendation to provide additional information to the prospective guarantor, namely, all relevant information in the bank's possession, will improve a lawyer's ability to advise the prospective guarantor. The Issues Paper however does not adequately deal with the issue of independent legal advice – who pays for this, whether this absolves the bank and whether solicitors are prepared to give this advice.

7. Applications requiring face to face interviews

The NSW Government submission (p9) raised concerns about situations where information is not adequately communicated to a potential borrower because of the absence of a face to face meeting with the lender. Entering into loan contracts is getting easier with the introduction of electronic banking and quick over the phone loan approvals. While this may not be a problem for some consumers, it is problematic for co-borrowers and guarantors who need to fully understand their risk and obligations.

It was therefore recommended that the Code should specify the kinds of contracts where a face to face meeting is necessary to ensure the customer understands the key features and risks of a banking service.

The Issues Paper does not contain an interim recommendation that would address this issue. It is an area that requires attention and the CBP is an appropriate document to provide direction to banks in this area. In this regard, it is noted that the Issues Paper

does recommend that all guarantors be informed of the legal effect of the guarantee in a face-to-face interview in the absence of the principal debtor.

Recommendation 3

That the CBP should specify the kinds of contracts where a face to face meeting is necessary to ensure the customer understands the key features and risks of a banking service.

8. Joint accounts

Problems currently exist where a bank may require all joint or secondary credit cards to be surrendered before advances can be stopped. Where relationships break down, this becomes very difficult or impossible. This approach by banks is in contrast to situations where a card is lost or stolen and an immediate stop on further transactions can be made by the bank.

The NSW Government submission (p10) recommended the CBP should require a bank to immediately cease further advances on a credit facility at the request of an account holder (regardless of whether it is a joint account or a single account with a secondary card).

The Issues Paper interim recommendation - that where a primary cardholder advises the issuing bank that it wants a subsidiary card cancelled, the primary cardholder shall not be liable for continuing use of the card, provided the primary cardholder takes all reasonable steps to procure the return of the subsidiary card to the issuing bank - is supported by the NSW Government. The term 'reasonable steps' however needs some clarification. If it is left to the banks discretion, it is unlikely to resolve the current problems faced by women when relationships break down and they want to stop access to their credit facility by their estranged partner.

The NSW Government submission (p10) recommended that the Review should consider whether the CBP should require joint credit applications to offer a choice between joint and several liability versus a specified proportion of the outstanding debt. This would allow parties in a relationship to nominate a proportion of the debt they would be responsible for at the outset and avoid one party being pursued by a bank for the entire debt.

The Issues Paper partially addresses this issue with the interim recommendation that either party may terminate their liability for further advances by written notice to the bank. This could be strengthened to limit liability at the outset of a joint loan.

9. Monitoring and reporting

Monitoring of compliance and public reporting are central to the effective operation of the CBP. The current provisions are inadequate, as acknowledged in the Issues Paper. A more effective process would involve monitoring and review by an organisation that is experienced in consumer banking issues, independent of banks and able to independently verify compliance with the CBP, as argued in the NSW Government submission (pp9-10).

The interim recommendations in the Issues Paper relating to monitoring and reporting capture the features proposed by the NSW Government, and, in fact provide additional detail on sanctions, education of CBP members, broad promotion of the CBP and external representation and consultation. This approach will strengthen monitoring and reporting processes.