



12 September 2023

Mr David Locke  
CEO and Chief Ombudsman  
Australian Financial Complaints Authority  
GPO Box 3  
MELBOURNE VIC 3001

Dear David Locke

### **AFCA APPROACH TO RESPONSIBLE LENDING – CONSULTATION PAPER (SEPTEMBER 2023)**

The Australian Finance Industry Association (AFIA) is the only peak body representing the entire finance industry in Australia.<sup>1</sup> We appreciate the opportunity to respond to the Australian Financial Complaints Authority (AFCA) Approach to Responsible Lending ('the approach').<sup>2</sup>

We represent over 150 members, including bank and non-bank lenders, finance companies, fintechs, providers of vehicle and equipment finance, car rental and fleet providers, and service providers in the finance industry. We are the voice for advancing a world-class finance industry and our members are at the forefront of innovation in consumer and business finance in Australia. Our members finance Australia's future.

We collaborate with our members, governments, regulators and customer representatives to promote competition and innovation, deliver better customer outcomes and create a resilient, inclusive and sustainable future. We provide new policy, data and insights to support our advocacy in building a more prosperous Australia.

### **INTRODUCTORY COMMENTS**

Our comments and recommendations reflect AFIA's purpose and belief in prosperity for all Australians by championing a thriving finance industry, always acting in the interests of customers and communities. Our feedback is designed to support AFCA to achieve its important role in the resolution of complaints and ensuring consumer's access to finance.

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<sup>1</sup> [Australian Finance Industry Association \(afia.asn.au\)](https://afia.asn.au)

<sup>2</sup> [Australian Financial Complaints Authority \(AFCA\) \(July 2023\) Approach to Responsible Lending - Consultation paper](#) and [AFCA \(July 2023\) Approach to Responsible Lending](#).

AFIA believes that external dispute resolution is an important part of a strong, accessible, competitive, innovative, efficient, and fair financial system.

Many AFIA members are required by law to be subscribers of AFCA, as they hold an Australian Financial Services Licence (AFSL) or an Australian Credit Licence (ACL). However, AFCA membership is voluntary for a number of our members that operate outside the financial products or consumer credit regulated segments, or only in the commercial or small business segments. As part of AFIA's self-regulation, AFCA membership is a mandatory requirement for our members who are signatories to AFIA's Online Small Business Lenders Code of Practice and/or the Buy Now Pay Later Code of Practice.<sup>3</sup> We believe AFCA membership for these organisations is the right thing for businesses and customers, reflecting community expectations, and enhancing confidence in the industry.

AFIA supports AFCA progressing with the recommendations of Treasury's review of AFCA, published in November 2021.<sup>4</sup> A key theme arising from Treasury's review of AFCA considered if it was meeting its objective to resolve complaints in a way that is fair, efficient, timely and independent.<sup>5</sup>

Recommendation 11 of Treasury's review stated that AFCA should conduct public consultations on the approach documents.<sup>6</sup> AFIA supports AFCA increasing the transparency and clarity for parties involved in their processes to deliver consistent and better outcomes. If material is being relied upon by AFCA in their decision-making, such as policies, procedures or guidance, we support it being made publicly available.

AFIA has significant concerns that the current draft approach is overly prescriptive and would impose risks on financial firms which go over and above the intentions of the document. As AFCA is a dispute resolution service, and not a regulator, it is crucial the approach document avoids unintentionally creating standards exceeding and/or confusing legislative requirements as well as unintentionally and adversely impacting on access to finance, financial inclusion, digitisation and innovation, and overall, better customer outcomes.

AFIA believes it is essential that the approach taken by AFCA to responsible lending obligations is clear, easily understood, consistent, relevant, legally compliant, and scalable.

The approach must:

- recognise at the outset the objectives of responsible lending obligations to inform AFCA's approach, including the objectives to minimise the incidences of unsuitable lending and appropriately maximise access to credit, and not inadvertently limiting it.<sup>7</sup>

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<sup>3</sup> [AFIA Codes of Practice webpage](#)

<sup>4</sup> [The Treasury \(24 November 2021\) Review of the Australian Financial Complaints Authority - Final Report](#)

<sup>5</sup> Treasury review of AFCA, 'Delivering against statutory objectives', [page vi](#) (n 4). See also: [Australian Securities and Investments Commission \(ASIC\) Regulatory Guide 267 \(21 September 2021\) Oversight of the Australian Financial Complaints Authority](#), Part D: AFCA Compliance requirements, page 25.

<sup>6</sup> [The Treasury \(24 November 2021\) Review of the Australian Financial Complaints Authority - Final Report](#), page 80, paragraphs 7.90-7.101.

<sup>7</sup> The Explanatory Memorandum to *National Consumer Credit Protection Bill 2009* (Explanatory Memorandum).

- avoid duplicating legislation and regulatory requirements wherever possible, to avoid risks of confusion among parties involved in their processes (including complainants, financial firms, and AFCA members of staff applying the approach in practice), as well as the public, and to avoid the risk of regulatory arbitrage or inconsistencies.
- recognise that financial firms have sophisticated digital business models and processes, and that this recognition is incorporated into AFCA's approach to responsible lending obligations.

We have provided more detailed recommendations within **Appendix A** to help mitigate and avoid these risks, and to ensure that complaints are resolved in a way that is fair, efficient, timely and independent.

## **CLOSING COMMENTS**

Thank you for providing the opportunity to respond to this consultation.

AFIA welcomes the opportunity to discuss our recommendations further and facilitate roundtables or workshops with our members and AFCA.

Our members look forward to collaboratively and constructively engaging with AFCA as the approach is developed.

Should you wish to discuss our submission or require additional information, please contact Leisha Watson, Senior Policy Advisor.

Yours sincerely

A handwritten signature in black ink that reads "Diane Tate". The signature is written in a cursive, flowing style.

Diane Tate  
**Chief Executive Officer**

## APPENDIX A: Detailed Recommendations

### Overview

AFCA is a dispute resolution body for financial services the purpose of which is to provide fair, independent and effective solutions for individuals and small businesses who have a complaint about a financial product or service.<sup>8</sup>

For AFCA to consider a dispute, the complaint must fall within the AFCA Complaint Resolution Scheme Rules.<sup>9</sup> The AFCA Rules form part of a contract between AFCA, Financial Firms and Complainants, as stated under Rule A.1.2.<sup>10</sup>

Rule A.4 states that a complaint must be made by an 'Eligible Person' about a Financial Firm who is a member of AFCA, including its employees and agents. Decisions can be determined by an Ombudsman, an Adjudicator or an AFCA Panel.<sup>11</sup>

Rule A.14 sets out AFCA's 'Decision making approach' and states that the AFCA Decision Maker must do what they consider '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 AFCA or Predecessor Schemes.<sup>12</sup>

AFCA set out their 'fairness jurisdiction' as reflecting what is fair in the circumstances of each complaint and applying a 'standard of fairness', which focusses on concepts such as fair dealing, fair treatment and fair service.

AFIA supports AFCA progressing with the recommendations of Treasury's review of AFCA, published in November 2021.<sup>13</sup> A key theme arising from Treasury's review of AFCA considered if it was meeting its

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<sup>8</sup> [AFCA's purpose webpage](#)

<sup>9</sup> [AFCA Complaint Resolution Scheme Rules \(dated 13 January 2021\)](#). Note these are subject to a recent review and consultation. Please see [Australian Financial Complaints Authority \(AFCA\) \(27 March 2023\) Rules and Operational Guidelines – Proposed amendments](#).

<sup>10</sup> [AFCA Rules](#), A.1.2. See also *Australia Capital Financial Management Pty Ltd v Australian Financial Complaints Authority Limited [2022] NSWCA 204*. The Court of Appeal noted that each member of AFCA agrees to be bound by the AFCA rules, and this forms a binding tripartite contract between the complainant, AFCA and the member the subject of the complaint.

<sup>11</sup> [AFCA Rules](#), Rule 13.1.

<sup>12</sup> [AFCA Rules](#), Rule 14.2.

<sup>13</sup> [The Treasury \(24 November 2021\) Review of the Australian Financial Complaints Authority - Final Report](#)

objective to resolve complaints in a way that is fair, efficient, timely and independent.<sup>14</sup> We note the concerns raised in the review that there appeared to be AFCA guidance or positions that were not made public, referring in particular to what constitutes good industry practice on responsible lending.

Recommendation 11 of the independent review stated that AFCA conduct public consultations on the approach documents.<sup>15</sup>

AFIA supports AFCA increasing the transparency and clarity for parties involved in their processes, to deliver consistent outcomes. If material is being relied upon by AFCA in their decision-making, such as policies, procedures or guidance, we agree it should be made publicly available.

To further enhance the accessibility, efficiency and consistency of the approach, we believe it would be beneficial for approach documents to clearly link to relevant AFCA Rules underlying it, including:

- outlining the time limits to responsible lending complaints which are set out under the Rules;<sup>16</sup> and
- where AFCA exercises its discretion under Rule A.8.3 where it would not be appropriate to continue to consider a complaint.

We note that the approach document is very prescriptive, detailing the Responsible Lending Obligations (RLOs) under the *National Consumer Credit Protection Act 2009* ('the *Credit Act*') and Australian Securities and Investments Commission (ASIC) Regulatory Guidance 277 and 209.<sup>17</sup>

We specifically note that the relevant provisions related to RLOs are outlined in ss 128-132 of the *Credit Act*.

AFIA believes an excessively prescriptive approach to assessing credit decisions is inconsistent to the relevant case law, the underlying legislative objectives of the *Credit Act* and the principle of scalability under RG209.

Firstly, the leading authority interpreting the RLO provisions is the *Australian Securities and Investments Commission v Westpac* (2020)<sup>18</sup> ('*ASIC v Westpac*'). In that case, Justice Gleeson, then of the Federal Court of Australia and now of the High Court of Australia, held that lenders bound by the existing RLOs can:

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<sup>14</sup> Treasury review of AFCA, 'Delivering against statutory objectives', page vi (n 4). See also: [Australian Securities and Investments Commission \(ASIC\) Regulatory Guide 267 \(21 September 2021\) Oversight of the Australian Financial Complaints Authority](#), Part D: AFCA Compliance requirements, page 25.

<sup>15</sup> [The Treasury \(24 November 2021\) Review of the Australian Financial Complaints Authority - Final Report](#), page 80, paragraphs 7.90-7.101.

<sup>16</sup> [AFCA Rules](#), Rule B.4. See also ASIC Regulatory Guide 267.

<sup>17</sup> [National Consumer Credit Protection Act 2009](#) and ASIC Regulatory Guides: [RG 209 Credit licensing: Responsible lending conduct](#) and [RG 277 Consumer remediation](#).

<sup>18</sup> FCAFC 111

*'[D]o what [they] want in the assessment process...what [they] cannot do is make unsuitable loans.'*<sup>19</sup>

Therefore, to the extent that any AFCA approach imposes prescriptive obligations which go beyond this understanding of the law, it is inconsistent with the core finding of the leading decision in the area which remains good law, and has not been overturned.

Secondly, any prescriptive approach to RLOs which goes beyond the holding of *ASIC v Westpac* is also entirely inconsistent with the underlying legislative purpose of Australia's credit laws.

For example, the Explanatory Memorandum to the National Credit Code (NCC), which is Schedule 1 of the *Credit Act* specifically states that the credit regulation framework's underlying purpose is:<sup>20</sup>

*'To ensure strong consumer protection through...recognising that competition and product innovation must be enhanced and encouraged by the development of **non-prescriptive flexible laws.**'*

Thirdly, a rigid or inflexible approach to assessing credit decisions is inconsistent with the principle of scalability under existing law and RG209. ASIC recognises that, in applying the RLOs consistent with the *Westpac* decision, one of the core concerns is:

**'The risk [emphasis added] or likelihood that a consumer will be harmed by taking on new financial obligations'**.<sup>21</sup>

AFIA strongly advocates for AFCA to align and not set rules and practice expectations that are inconsistent with or exceed the considerations outlined above in:

- *ASIC v Westpac*
- the principles underlying the NCC,
- the aspects of RG209 outlined above.

To the extent the approach is either inconsistent with any of these legal considerations, or adds additional criteria to those outlined in the above, this risks confusing parties and being legally inconsistent, constraining administrative decision-makers, in accordance with the relevant case law regarding the application of policies to administrative decisions.

A prescriptive approach has various pitfalls such as minimising flexibility in complex scenarios, and further risks stifling innovation and competition in finance. Financial firms use sophisticated digital business models as part of their decision-making processes, however this is not reflected in the approach.

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<sup>19</sup> Credit Act, Sections 128-131. See too *Australian Securities and Investments Commission v Westpac Banking Corporation (Liability Trial)* [2019] FCA 1244 at [81]. Upheld on appeal in *Australian Securities and Investments Commission v Westpac Banking Corporation* [2020] FCAFC 111 at [131], [141] and [171].

<sup>20</sup> Explanatory Memorandum, National Consumer Credit Protection Bill 2009 (Cth), 6.

<sup>21</sup> [ASIC RG 209.87](#).

The *Credit Act* is principles based in nature to ensure flexibility in the application of the requirements and ensure it is easily understood. The key objective of responsible lending conduct requirements is to strike a balance *'between the goal of minimising the incidence of consumers entering unsuitable credit contracts, and the goal of maximising access to credit for consumers who have the desire and ability to service it'*.<sup>22</sup>

It is essential that the approach taken by AFCA to responsible lending obligations is clear, easily understood, consistent, relevant, legally compliant, and scalable.

**AFIA recommends:**

- in publishing these approach documents, AFCA ensure that the approaches avoid duplicating legislation and regulatory requirements wherever possible, to avoid risks of confusion among parties involved in their processes (including complainants, financial firms, and AFCA members of staff applying the approach in practice), as well as the public, and to avoid the risk of regulatory arbitrage and/or inconsistencies. This further helps to future-proof the approach where there are changes to legislation and/or guidance.
- the approach recognises at the outset, the objectives of responsible lending obligations to inform AFCA's approach, including the objectives to minimise the incidences of unsuitable lending and appropriately maximise access to credit, and not inadvertently limiting it.<sup>23</sup>
- the approach clearly links to the relevant AFCA Rules underlying it.

**Section 3.1 – 'Referring to laws, codes, good industry practice and past decisions'**

AFIA notes that AFCA's Approach to Code obligations for credit providers is detailed in an online factsheet which is not referenced in the approach.<sup>24</sup> This states that AFCA:

*'[M]ay have regard to a standard set out in a Code if AFCA considers the standard represented the general law or good industry practice at the time the conduct occurred, even if a credit provider is not a subscriber'*.

AFIA members subscribe voluntarily to AFIA Codes of Practice, such as the AFIA Buy Now Pay Later Code and AFIA Online Small Business Lenders Code.<sup>25</sup> AFCA will be aware that some of our members include banks that are required as a condition of ABA membership to subscribe to the Banking Code of Practice (BCoP). Some AFIA members are also subscribers of the Customer Owned Banking Code of Practice.

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<sup>22</sup> The Explanatory Memorandum to *National Consumer Credit Protection Bill 2009* (Explanatory Memorandum), 9.122 'Objectives'.

<sup>23</sup> The Explanatory Memorandum to *National Consumer Credit Protection Bill 2009* (Explanatory Memorandum).

<sup>24</sup> [Factsheet – AFCA's Approach to Code obligations for credit providers](#)

<sup>25</sup> [AFIA Codes Hub webpage](#)

If AFCA were to determine good industry practice by deciding that the BCoP, for example, was applicable to non-subscribers of that code, that:

- was not required by law to be complied with at the time the issue the subject of the complaint arose,
- had no input to shape the code to ensure it was effective for their customers, products or services, or business models.

With retrospective effect, this would be significantly unfair and risk overlapping enforcement and regulatory regimes, including self-regulatory industry standards.

Additionally, this may risk:

- regulatory arbitrage and the risk of the creation of an ‘uneven playing field’, which impacts the broader financial market consistently understanding and meeting community expectations as:
  - new or existing financiers who are not part of AFCA may delay or defer launching products captured under AFCA Rules
  - new financiers or existing financiers who are not part of AFCA choose to take commercial advantage of the situation.
- members who joined AFCA voluntarily exiting the scheme, which will impact AFCA’s ability to achieve its stated aims of improving practices as well as undermine the efforts of lifting consumer protections more broadly across banking and finance and the important role of self-regulatory industry standards.

A clear legal and regulatory framework is vital for banking and finance. In line with AFCA’s objective of determining outcomes which are fair in all the circumstances, clarifying this approach will aid to remove duplication, reduce overlapping regulatory requirements, improve consistent understanding and application, and enhance consistent AFCA decision-making.

We recommend that AFCA be transparent and clearly set out with both financial firms and complainants their basis for determining industry good practice in each case, and provide accessible material to parties to refer to that explain how AFCA has reached its decision.

AFIA is supportive of AFCA clarifying within Section 3.1 that they consider law and standards that were in force at the time of the relevant conduct, and that obligations should not be retrospectively applied.<sup>26</sup>

**AFIA recommends:**

- AFCA be transparent and clearly set out with both financial firms and complainants, their basis for determining industry good practice in each case and provide accessible material to parties to refer to that explain how AFCA has reached its decision.
- AFCA be clear that where an industry code has been developed, this code will be applied for those subscribers as relevant for their customers, products and services, and business models.

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<sup>26</sup> [AFCA Approach to Responsible Lending](#), Section 3.1 page 19.



- AFCA be clear in the approach and the online factsheet, that if there is not a relevant industry code, they may look to the standards in another code, but in these instances, it must be appropriately applied keeping in mind the differences across financial firms and sub-sectors of banking and finance.

**1. Do you consider our approach to assessing the reasonableness of inquiries and verification steps aligns with the guidance in ASIC RG 209?**

**2. Do you have any other comments about our proposed approach to assessing the reasonableness of inquiries and verification steps?**

AFIA notes that the RLOs and associated legislation are complex, highlighted by relevant case law.<sup>27</sup> RG209 allows for a scalable approach to inquiries and verification steps which AFIA recommends should be further reflected in Section 3.2 of the approach.<sup>28</sup>

AFCA's approach to considering whether inquiries and verification steps were reasonable should consider and recognise where lower requirements for verification are appropriate, such as for a returning or repeat customer, and allow for scalability to relate to the risk of making an unsuitable loan. The approach currently refers to making reasonable inquiries and verification steps to assess '*the consumer's capacity to comprehend and understand the credit product and their obligations*' however there will be cases where extra steps to verify this will not be necessary.<sup>29</sup>

Additionally, AFCA should account for financial firms using sophisticated digital business models as part of their decision-making process, which are further technologically advanced than the approach suggests. The approach must explicitly take into account financial firm's sophisticated risk-based approaches to application verification.

The approach document states that AFCA are:

*'unlikely to find a financial firm breached its responsible lending obligations if it relies on information that it reasonably believed was accurate. This is the case even if this results in a consumer entering into a credit contract that accurate information (which the financial firm did not have) would have shown was unaffordable for them.'*<sup>30</sup>

To enhance clarity and consistency of the approach, we recommend that this statement is reflected within Section 3.2.

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<sup>27</sup> Such as *Australian Securities and Investments Commission v Westpac Banking Corporation* [2020] FCAFC 111.

<sup>28</sup> See [ASIC RG 209.81 and RG 209.86](#).

<sup>29</sup> [AFCA Approach to Responsible Lending](#), Section 3.2, page 12.

<sup>30</sup> [AFCA Approach to Responsible Lending](#), Section 3.3, page 16.

Brokers and credit providers have independent responsible lending obligations under the *Credit Act*. Section 31 of the *Credit Act* prohibits credit providers from engaging in activity with persons who are not licenced under the Act.<sup>31</sup> The approach refers to 'Where a broker is involved in the loan application' and recognises that brokers have their own responsible lending obligations under the *Credit Act*.<sup>32</sup> AFIA recommends that the approach be clear that the responsible lending obligations of financial firms do not extend to being responsible for the conduct of brokers, and that the conduct of brokers in complaints will be considered separately.

**AFIA recommends:**

- the approach is made more scalable given the above, that it is made clear that reasonable enquiries will depend on the particular circumstances, and the statement at page 16 is reflected within Section 3.2.
- the approach be clear that the responsible lending obligations of financial firms do not extend to being responsible for the conduct of brokers, and that the conduct of brokers in complaints will be considered separately by AFCA.

**3. Does our approach to considering a financial firm's assessment of reasonably foreseeable changes in a complainant's circumstances align with the guidance in ASIC RG 209?**

Financial firms are reliant on applicant's making full and accurate disclosures, and providing information on their future circumstances. AFIA notes that RG209 states:

*'The assessment you are required to make is necessarily a point in time assessment, but requires a consideration of what is likely to be the case if the consumer enters into the credit product or accepts the credit limit increase, given information currently available to the licensee about the consumer and foreseeable changes to their circumstances (e.g. changes to circumstances that affect the amount of their income or outgoings) or to the obligations under the credit product (e.g. known changes in the financial obligations under the terms of the credit product).'*<sup>33</sup>

ASIC's regulatory guidance recognises that they do not consider that the term 'likely' should be interpreted in a way that would require you to consider every possibility.<sup>34</sup> AFIA recommends that this clearly is reflected in the approach, reflecting AFCA determining complaints in line with the fairness jurisdiction, described above.

The approach provides an example of a variable interest rate on a loan changing during the term of the loan. We assume that this example incorporates increasing and decreasing rates.

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<sup>31</sup> Credit Act, Chapter 2, Part 2-1, Section 31.

<sup>32</sup> [AFCA Approach to Responsible Lending](#), Section 3.3, page 22.

<sup>33</sup> [ASIC RG 209.175](#).

<sup>34</sup> [ASIC RG 209.178](#).

The approach comments on AFCA's expectations regarding the use of benchmarks and states:

*'A benchmark should not be used as an estimate of a consumer's likely future expenses when information known to the financial firm indicates that the consumer's actual future expenses may be higher than the benchmark.'*<sup>35</sup>

*ASIC v Westpac* considered the use of benchmarks in Westpac's unsuitability assessment. The Federal Court held that in relation to the *Credit Act*:

*'...the Act leaves it open to the licensee to decide:*

- (1) what inquiries it will make under s 130(1)(a) and (b), provided that those inquiries are reasonable;*
- (2) what steps it will take to verify the consumer's financial situation under s 130(1)(c), provided that those inquiries are reasonable; and*
- (3) how it will use the results of its inquiries and verification to make the unsuitability assessment, provided that it in fact assesses whether the contract will be relevantly unsuitable for the particular consumer and noting that the licensee is otherwise motivated by the Act to refrain from entering into an unsuitable contract.'*<sup>36</sup>

Furthermore, it stated:

*'it does not follow that the statutory purpose can only be achieved by taking into account all information collected, regardless of its relevance or materiality to the assessment of unsuitability. Simply labelling an expenditure as a Declared Living Expense, and the fact that the consumer incurs that expense on their current lifestyle, does not necessarily change its nature from being discretionary. It is plain that a consumer may choose to, and can be expected to, forgo particular living expenses in order to meet their financial obligations under a credit contract.'*<sup>37</sup>

Given the above, AFIA recommends that flexibility in the approach is crucial to take into account financial firms determining the most appropriate benchmark to use.

For example, a financial firm may choose not to rely on Household Expenditure Measure (HEM) dataset because of any of the following reasons:

- income Adjusted HEM is not always the best benchmark to use for low-income applicants as there may be a greater occurrence of vulnerable customers and income adjusted HEM may allow a lower expense declaration.

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<sup>35</sup> [AFCA Approach to Responsible Lending](#), Section 3.3, page 17.

<sup>36</sup> *ASIC v Westpac* [2020], paragraph 141.

<sup>37</sup> *Australian Securities and Investments Commission v Westpac Banking Corporation* [2020] FCAFC 111, paragraph 172.

- higher income earners have greater ability to modify their behaviours before experiencing substantial hardship.
- where a lender is taking the higher of HEM and the declared expenses a conservative position is already being adopted.
- there is some discussion in the industry of location adjust HEM being removed.

Page 19 of the approach provides an example of an applicant with actual expenses higher than the HEM used in the assessment and higher than the declared expenses.<sup>38</sup> It is noted that applicant's bank accounts can commonly show higher expenses than necessary after a new loan.

AFIA recommends that AFCA make clear in the approach that they do not expect or mandate use of any particular benchmark. The approach must be clear on AFCA's expectations around reasonable inquiries where expenses were reviewed and confirmed as one off or discretionary by the applicant.

We recommend that AFCA provide clarity on what types of expenditure would be considered by them to be non-discretionary. The approach should be clear that being able to meet non-discretionary expenses is a key measurement for establishing that customers can afford to meet their financial obligations under a credit contract, without substantial hardship.

The approach further states that:

*'Where a complainant's expenses (including liabilities and general living expenses) are shared with another person, we will consider whether the financial firm reasonably apportioned those expenses between the complainant and the third party.'*

AFIA recommends AFCA clarify its expectations of a financial firms' assessment of the other person/third party.

The approach refers to parties' conduct which may be relevant to the assessment.<sup>39</sup> The conduct of the borrower will be highly relevant when considering if a financial firm has complied with its responsible lending obligations. If, for example, a customer has omitted information about their financial position, this will be particularly relevant when assessing a complainant's loss and benefit. Please see further comments below on this under Question 8.

The approach further refers to a financial firm's policies and states that AFCA may consider whether a firm complied with its own policies when it conducted an unsuitability assessment.<sup>40</sup> AFIA notes however that there will be instances where firms can deviate from their internal policies, where appropriate, which is determined by the firm. It would be helpful for the approach to outline this.

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<sup>38</sup> [AFCA Approach to Responsible Lending](#), Section 3.3, page 19.

<sup>39</sup> [AFCA Approach to Responsible Lending](#), page 22.

<sup>40</sup> [AFCA Approach to Responsible Lending](#), page 20.

**AFIA recommends:**

- AFCA clearly reflect RG209 in the approach in that they do not consider that the term 'likely' should be interpreted in a way that would require you to consider every possibility.
- the approach be reviewed given the commentary above in relation to the use of benchmarks by financial firms and appropriately recognise relevant case law above.
- the approach is made clear that use of any benchmark is not expected or mandated - AFCA's expectations around reasonable inquiries where expenses were reviewed and confirmed as one off or discretionary by the applicant must be clarified.
- AFCA clarifies what types of expenditure would be considered by them to be non-discretionary.
- the approach is clear that being able to meet non-discretionary expenses is a key measurement for establishing that customers can afford to meet their financial obligations under a credit contract, without substantial hardship.
- AFCA clarifies their expectations of a financial firms' assessment of the other person/third party.

**4. Do you think it is it reasonable for AFCA to consider that where a borrower will likely reach retirement age during the loan term, the lender should, as part of its reasonable inquiries and verification steps:**

**> assess how the borrower will repay the loan in retirement, and**

**> if it appears likely the borrower will need to sell assets to repay the loan, make inquiries about whether the sale of those assets at that time meets the complainant's requirements and objectives?**

As stated above, RG 209 recognises that they do not consider that the term 'likely' should be interpreted in a way that would require you to consider every possibility.<sup>41</sup> It is not reasonable for financial firms to predict events that will take place after a contract is in place. It will not be reasonable for a financial firm to know the retirement age of an applicant when undertaking an unsuitability assessment, unless that information is provided by the applicant. As retirement ages vary considerably with individuals and unless the information is provided upon application, a financial firm will not have the ability to determine the level of assets needed by the applicant on retirement or what their level of pension/superannuation will be.

**AFIA recommends:**

- AFCA review their approach in relation to the foreseeability of a borrower likely reaching retirement age.

**5. Do you have any comments about our proposed approach to considering the reasonableness of applying interest rate buffers to loans?**

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<sup>41</sup> [ASIC RG 209.178](#).

The Australian Prudential Regulation Authority (APRA) set out their expectations for banks in managing exceptions to housing lending policy. They state that:

*'[A] serviceability buffer provides a contingency for rises in interest rates over the life of the loan, as well as for any unforeseen changes in a borrower's income or expenses'.<sup>42</sup>*

APRA's supervision is focused on particular financial institutions, such as authorised deposit-taking institutions (ADIs), which covers banks, building societies and credit unions. This supervision does not extend to non-APRA regulated entities.

An interest rate buffer is appropriate as APRA provides, for home loans which have significantly longer terms than other loans. This may not be appropriate for other financial firms, who use other methods which make allowances for fluctuations in a consumer's finances as part of the serviceability assessment, including applying methodologies to account for fluctuating income types and buffers for expenses.

Interest rate buffers can cause a number of challenges and differing variables across banking and finance, such as:

- changes in future interest rates and ascertaining how lenders pass on increases and decreases to customers;
- how interest rates vary across different credit products, such as home loans and credit cards
- discounts on interest rates offered to consumers;
- changes in products and services as well as business models designed to serve customers with different personal and financial circumstances and needs, thereby unintentionally and adversely impacting on access to finance, financial inclusion, digitisation and innovation, and overall, better customer outcomes; and
- several other variables including the cost of living, rent increases/decreases, income and/or mortgage repayments.

**AFIA recommends:**

- re-consideration here of the wording in the approach and incorporation of the concept of scalability in the process, given interest rate buffers will not apply in all scenarios.

**6. Do you have any comments about how we propose to seek and consider further information when we find a financial firm has made an error in its assessment?**

**7. Do you have any comments about how we propose to use further information to determine whether the loan was unsuitable for the borrower?**

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<sup>42</sup> [Australian Prudential Regulation Authority \(APRA\) \(23 June 2023\) Housing lending standards: Reinforcing guidance on exceptions](#)

The approach document states that *'Once AFCA has revised a financial firm's unsuitability assessment to correct any errors, we consider whether the credit contract was unsuitable for the complainant.'*<sup>43</sup> The approach does not provide a clear definition of what is considered 'unsuitable', opening it to varying levels of subjective interpretation, which risks leaving firms in uncertain positions.

The approach refers to an assessment of an appropriate amount of uncommitted income, and that small surpluses might not be sufficient.<sup>44</sup> The approach does not provide a definition of 'small surplus', again leaving this open to subjective interpretation. While surplus remaining may be relevant, this is not a determiner of the serviceability calculations.

This approach does not incorporate the case of *Australian Securities and Investments Commission v Westpac Banking Corporation 2020*, which recognised that customers can adjust their discretionary spend to support loan repayments.<sup>45</sup>

The approach refers to AFCA obtaining further information and how this affects the assessment as to whether a loan was unsuitable.<sup>46</sup> We support the clarifying statement *'This means we take into account the information that was available to the financial firm at the time, or information that would have been available if it had undertaken reasonable inquiries and verification steps'*.<sup>47</sup> It is appropriate that, if further information is obtained and considered, that this is limited to information available at the time the decision was made.

It would be appropriate here for AFCA to clarify the expectation that the additional information that is considered by them would be limited to the information available at the time of the application.

**AFIA recommends:**

- the approach is reviewed to provide further clarity around AFCA's interpretation of 'unsuitable' and 'small surplus', recognising the *ASIC v Westpac* decision and customers adjusting discretionary spending.

**8. Do you have any comments about the way we propose to assess a complainant's loss and benefit?**

RG277 on 'consumer remediation' sets out nine principles for conducting a remediation, which includes the objective to *'Return affected consumers as closely as possible to the position they would have otherwise been in had the misconduct or other failure not occurred'*.<sup>48</sup>

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<sup>43</sup> [AFCA Approach to Responsible Lending](#), Section 3.4, page 25.

<sup>44</sup> [AFCA Approach to Responsible Lending](#), Section 3.4, page 25.

<sup>45</sup> *Australian Securities and Investments Commission v Westpac Banking Corporation [2020] FCAFC 111*

<sup>46</sup> [AFCA Approach to Responsible Lending](#), Section 3.4, page 23.

<sup>47</sup> *ibid.*

<sup>48</sup> [Regulatory Guide RG 277 Consumer remediation](#)

This regulatory guidance goes on to state that *'This should be the aim regardless of scale or complexity, and generally underpin remediation decision making'*.<sup>49</sup>

ASIC details remedies to consider when determining appropriate outcomes including a list of possible remedies to consider where misconduct is related to a consumer lease or credit contract.<sup>50</sup> This includes examples of returning fees, charges and interest, or varying the contract.

The approach currently presumes that there will be a 'gross loss' suffered by the complainant when calculating the net loss, however, there will be cases where no loss is suffered.<sup>51</sup> This could lead to confusion for complainant's expectations.

In view of AFCA's objective to resolving complaints in a timely manner, AFIA recommends including reference to current AFCA Rule A.8.3 where AFCA can exclude a complaint where the complainant has suffered no loss or *'has been appropriately compensated for such loss and AFCA would not award any further amount'*.<sup>52</sup>

It is appropriate that the calculation of loss and benefits allows for consideration of a complainant's individual circumstances. AFIA has concerns that the approach does not appropriately consider relevant benefits to complainants. The approach provides that AFCA will consider if the complainant received other benefits from the loan, other than the amount of credit provided.<sup>53</sup> The benefit which the consumer receives from the credit provided must also be taken into account. This is important in situations where, for example, the customer has had the benefit of a vehicle, and/or retain use of a vehicle with reduced or no further payments (and where the car is returned to the financial firm with a depreciated value). Further comment is provided on this point in relation to Guide One below. Or where a complainant has had the benefit of residing in a home for a number of years. If this benefit is not appropriately considered, this would not be in line with the objectives of RG277 detailed above to return the consumer to the position they would have been in.

The approach refers to AFCA applying interest to adjusted debts and further clarity it sought on how AFCA will determine the interest rate to repay the adjusted debt in a manner that is fair in all the circumstances, in line with their objectives.<sup>54</sup>

The approach details that AFCA will consider reducing compensation due to complainant conduct.<sup>55</sup> It is crucial that the approach recognises that compensation may not be appropriate if a complainant provided false information, or omitted information which met appropriate criteria for credit at the time.

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<sup>49</sup> [ASIC RG 277, Consumer remediation](#), Section C, Table 1, page 15.

<sup>50</sup> [ASIC RG 277, Consumer remediation](#), page 29, Table 2, Remedies to consider when determining appropriate outcomes'.

<sup>51</sup> [AFCA Approach to Responsible Lending](#), Section 4.2, page 30.

<sup>52</sup> [AFCA Rules A.8.3](#).

<sup>53</sup> [AFCA Approach to Responsible Lending](#), Section 4.2, page 33.

<sup>54</sup> [AFCA Approach to Responsible Lending](#), Section 4.2, page 37.

<sup>55</sup> [AFCA Approach to Responsible Lending](#), Section 4.2, page 40.



The approach must be consistent with Section 160D of the *Credit Act* in relation to giving misleading information, recognising that civil and criminal penalties may apply. This states that:

*'A person (the giver) must not, in the course of engaging in a credit activity, give information or a document to another person if the giver knows, or is reckless as to whether, the information or document is:*

- (a) false in a material particular; or*
- (b) materially misleading.<sup>56</sup>*

AFIA has concerns with the example provided entitled 'Complainant conduct reduces compensation'.<sup>57</sup> In this example, a complainant provided fraudulent payslips to a financial firm during the application process and the compensation was reduced by 25 per cent because the complainant was aware the payslips were fraudulent. AFIA requests further information and clarification from AFCA on this example.

If a customer has provided false information and the financial firm has committed no error due to that false information, this would fall under AFCA Rule A.8.3 where AFCA excludes the complaint.<sup>58</sup> AFIA recommends that this must be clarified explicitly in this section of the approach.

Section 5.1 sets out AFCA's approach in relation to joining another financial firm as a party to an existing complaint.<sup>59</sup> AFIA recommends further clarity from AFCA on how they will apply joinders for responsible lending complaints and in particular, their approach to assessing and apportioning loss if it was determined that a firm provided an unsuitable loan, and a credit representative contributed to this.

**AFIA recommends:**

- AFCA review its approach to calculating loss and benefit to address the above comments and concerns.
- AFCA clarify how it will determine a fair interest rate to be applied to adjusted debts.
- AFCA clarify within its approach to calculating loss and benefit that if a customer has provided false information and the financial firm has committed no error due to that false information, this would fall under AFCA Rule A.8.3 where AFCA excludes the complaint.
- AFCA ensure that the approach is consistent with Section 160D of the *Credit Act* and recognises that civil and criminal penalties may apply in these circumstances.

**11. We propose to determine how a complainant should repay any outstanding debt. This approach may allow a complainant to retain an asset and repay any outstanding debt over time if it is fair in the circumstances of the complaint. Do you have any comments about our flexible approach to determining fair outcomes when an unsuitable loan is secured by an asset?**

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<sup>56</sup> Credit Act, Section 160D.

<sup>57</sup> [AFCA Approach to Responsible Lending](#), page 41.

<sup>58</sup> [AFCA Rules](#), Rule A.8.3.

<sup>59</sup> [AFCA Approach to Responsible Lending](#), Section 5.1, page 42.

AFIA recommends clarification from AFCA in the approach as to whether a new payment plan is considered new credit and thereafter dealt with separately in any new proceedings, should they arise. Where a new payment plan is in place in the example of a vehicle and payments are missed, is it AFCA's expectation that the financial firm would have the ability to either default the customer or repossess the vehicle. It would be helpful for AFCA to set out their expectations clearly in these circumstances.

Furthermore, AFIA recommends that AFCA further clarify here opportunities for parties, including the financial firm and complainant, to discuss and clarify where appropriate any errors or discrepancies in the figures. It is essential that any discrepancies are able to be dealt with in a timely and effective manner, in line with the objectives of the approach to determine outcomes that are fair in all the circumstances of the complaint.<sup>60</sup>

The example provided within Guide One of the approach in relation to 'Car Loans' refers to the purchase price of the vehicle. We note that it does not reference the total lend amount.<sup>61</sup> Lending decisions and serviceability are determined on the size of the loan, not the value of the asset. This Guide and the examples provided do not reference benefits the consumer has obtained by having use of the vehicle since the loan was established. The 'benefit column' refers to when a complainant retains the car, then their benefit is usually the purchase price of the car, however this 'may be less than the purchase price' if the car was faulty.<sup>62</sup> An example is also provided that refers to a complainant obtaining a car loan from a financial firm and refers to a complainant stating that the car had faults. It is important for AFCA to note within its approach that events such as car faults that occur after a contract is in place, is not related to loss suffered by a complainant as a result of an unsuitable loan, and is out with the control of the financial firm. AFIA recommends that AFCA review its approach to take account of this.

AFIA requests clarity from AFCA in Guide One on 'consumer leases' and whether this is intended to cover 'consumer motor vehicle leases', noting the different nature of the product, and therefore, different obligations applicable under law and regulatory guidance.<sup>63</sup>

**AFIA recommends:**

- AFCA clarify in the approach as to whether a new payment plan is considered new credit and thereafter dealt with separately in any new proceedings, should they arise.
- the approach provides opportunities for parties to discuss and clarify the figures, to account for any errors or discrepancies.
- AFCA reviews the approach in Guide One on 'car loans' to recognise that events such as car faults that occur after a contract is in place, is not related to loss suffered as a result of an unsuitable loan.
- the approach clarifies whether the consumer leases guide covers consumer motor vehicle leases.

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<sup>60</sup> [AFCA Approach to Responsible Lending – Consultation paper \(July 2023\)](#), page 3-4.

<sup>61</sup> [AFCA Approach to Responsible Lending](#), Guide One, page 51.

<sup>62</sup> [AFCA Approach to Responsible Lending](#), Guide One, page 50.

<sup>63</sup> [AFCA Approach to Responsible Lending](#), Guide One, Consumer leases, page 55.

**12. Do you have any comments about our tool which has been developed to assist financial firms provide detail to us about their unsuitability assessment?**

AFIA notes AFCA’s commentary that the tool is to ‘enable financial firms to set out their unsuitability assessment clearly and simply.’<sup>64</sup> We understand that the intention is that this is a voluntary and optional tool, not to be subscribed or made mandatory. We recommend that this is made clearer in the approach.

The tool requires manual data input where financial firms would be required to duplicate information from their internal processes. This would create duplication and create resource challenges for many financial firms who have their own specific internal processes.

The approach must further recognise that financial firms have sophisticated, digital business models and processes, in particular, firms will have end-to-end digital credit and loan origination business models.

AFIA recommends:

- the approach makes clearer that the tool is not to be subscribed or made mandatory.
- recognition is given that financial firms have sophisticated digital business models and processes, and that this recognition is incorporated into AFCA’s approach to responsible lending obligations.

**13. Do you have any feedback about the ‘Quick reference guides’ included in the Approach?**

Guide Two in the approach entitled ‘information we may request from financial firms’ is very prescriptive and will not be applicable to all complaint scenarios. A prescriptive approach risks a lack of flexibility in AFCA’s approach and overly complex processes which could affect AFCA’s effectiveness.

Guide Two refers again to benchmarks used by financial firms to verify complainant’s living expenses.<sup>65</sup> We recommend that AFCA clarify in their approach that they do not mandate any use of particular benchmarks or place blanket assumptions them.

**14. Do you have any other feedback about how the draft Approach meets our objectives?**

The objectives of the approach are to outline how AFCA will:

- fairly assess financial firms’ compliance with the responsible lending obligations;
- fairly assess what loss financial firms who breach their responsible lending obligations cause consumers;
- determine outcomes that are fair in all the circumstances of a complaint;

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<sup>64</sup> [AFCA Approach to Responsible Lending](#), pages 12-13.

<sup>65</sup> [AFCA Approach to Responsible Lending](#), Guide Two, information we may request from financial firms, page 57.

- assist financial firms and complainants to understand how we consider these complaints;
- ensure our approach is consistent with applicable legal principles, regulatory guidance, good industry practice and codes of practice; and
- ensure consistent application and understanding of our approaches to lending complaints internally and externally.

As stated earlier in our submission, in order to achieve the objective of fairly assessing how financial firms have complied with the RLOs, AFIA recommends that the objectives and principles of responsible lending are outlined at the outset in the approach and reflected throughout the document.

AFIA supports the objective of AFCA in outlining the approach to determine outcomes that are fair in all the circumstances of a complaint. However, AFIA has concerns that the current draft approach is overly prescriptive and risks placing misplaced expectations on lenders which go over and above the intentions of the document. As outlined in our detailed comments.

It is essential that the approach taken by AFCA to responsible lending obligations is clear, easily understood, consistent, relevant, legally compliant, and scalable. It must recognise the objectives of responsible lending obligations, to minimise the incidences of unsuitable lending and appropriately maximising access to credit.<sup>66</sup>

AFIA recommends that the approach must avoid duplicating legislation and regulatory requirements where possible in order to avoid confusion amongst parties involved in AFCA's processes and the public.

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<sup>66</sup> The Explanatory Memorandum to *National Consumer Credit Protection Bill 2009* (Explanatory Memorandum).