



**AUSTRALIAN BANKERS' ASSOCIATION INC.**

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3 November 2011

Mr Paul Gretton  
Assistant Commissioner,  
Trade and Economic Studies  
COAG Reform Agenda Study  
Productivity Commission  
GPO Box 1428  
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Dear Mr Gretton,

**Impacts of COAG Reforms - Business Regulation**

Thank you for the opportunity to provide a submission on this important new Study by the Commission. We apologise for not providing this submission earlier.

By way of introduction, the Australian Bankers' Association (ABA) is the peak national body representing banks (other than mutuals) that are authorised by the Australian Prudential Regulation Authority to carry on banking business in Australia. The ABA's membership of 23 banks comprises the four major banks, former regional banks that now operate nationally and foreign banks that are represented and carry on banking business in Australia as Australian banks.

In this submission the ABA wishes to focus on the Commonwealth Government's and the Council of Australian Governments' (COAG) credit regulatory reform program.

**Overview of credit reform program**

The credit reform program is extensive. It has coincided with some other major regulatory reforms<sup>1</sup>. In its earlier stages the credit reforms were complicated with

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<sup>1</sup> Examples include banking prudential reforms, wholesale reform of personal property securities laws commencing January 2012, Financial Claims Scheme February 2012, Account Switching July 2012 and Future of Financial Advice legislation July 2012

troubled consultation processes. More recently, the "fast tracking" in 2011 of the credit card reforms and the failure for sufficient account to be taken for the implementation arrangements and commencement timing have combined making the reform program resource intensive, costly and a significant business undertaking.

The reforms have been a mix of regulation to address perceived consumer protection aspects and to aid increased competition between banks and other credit providers.

Consultation with The Treasury on these reforms has been conducted over a period commencing in mid 2008 and is still continuing. The last of the primary legislation to complete the reform program is proposed to be in place by mid-2012. Subordinate legislation in the form of regulations is likely to follow.

The reform program has comprised two key phases and when completed will involve four separate pieces of primary legislation. Two of the legislative reforms have been passed by the Parliament, a third has been introduced into the Parliament for passage in the current sittings and a fourth is to be introduced in the first quarter of 2012 for passage by mid-2012.

In 2008 the then Minister announced that the Commonwealth Government had reached agreement with the States and Territories at a COAG meeting for the Commonwealth to assume responsibility for regulation of all consumer credit. Consumer credit includes personal loans, credit cards, pay day lending and micro loans.

The announcement included a statement that the then consumer credit regulation was "duplicated, patchy, very hard to change or even non-existent and does very little to protect Australians, whilst imposing unnecessary red tape on business".

In October 2008 the Minister announced that the credit reform program would be conducted in two phases. A copy of the Minister's two-phase plan agreed with COAG ministers can be viewed at

[http://www.treasury.gov.au/documents/1381/PDF/NCC\\_Brochure\\_02102008.pdf](http://www.treasury.gov.au/documents/1381/PDF/NCC_Brochure_02102008.pdf)

Consultation on the Phase one elements commenced in late October 2008.

The then existing State and Territory based uniform Consumer Credit Code was the key regulatory instrument for regulating consumer credit by the States and Territories. Under some individual States' and Territories' credit administration laws there was some licensing (or negative licensing) provisions and some regulation of finance brokers.

The national Commonwealth scheme replaced these differences with a single national law, the National Consumer Credit Protection Act 2009 (NCCP Act) that created comprehensive and significantly expanded regulatory requirements and obligations for the industry.

The following is a chronology of key steps and outcomes that have occurred and are ahead for the credit industry:

- (1) In December 2009 the NCCP Act was enacted providing for the registration and licensing of credit providers and credit assistance providers (for example finance brokers), transfer, with some modifications, of the States and Territories based Consumer Credit Code to the Commonwealth (renamed National Credit Code) and a legislated responsible lending regime for credit and credit assistance providers.
- (2) On 1 January 2011 the responsible lending requirements of the NCCP Act commenced for banks, other authorised deposit taking institutions and registered finance companies.
- (3) On 24 March 2011 a National Consumer Credit Protection Amendment (Home Loans and Credit Cards) Bill 2011 (Home Loans and Credit Cards Bill) was introduced into the Parliament and was passed on 4 July 2011. This Act amended the NCCP Act by adding a series of further compliance obligations on credit providers; for home loans, the preparation and publication of key fact sheets for consumers; for credit cards, seven key operational requirements impacting the relationship between the credit provider and the customer.
- (4) The House of Representatives Standing Committee on Economics report on its inquiry into the Home Loans and Credit Cards Bill recommended that commencement of the home loans provisions (obligations on credit providers to provide home loan key facts sheets to consumers) should be deferred from 1 September 2011 to 1 January 2012 because there would be insufficient time for industry to adequately prepare for compliance. The Committee noted its expectation that there would be a 12 month period for finalisation of the credit cards regulations aspects of the Bill that would be developed in "the near future"
- (5) The detailed regulations to be made under Home Loans and Credit Cards Bill (now an Act) that will be essential in shaping a bank's compliance and implementation projects for the credit cards amendments are expected to have been approved by the Executive Council at its 3 November meeting. These regulations will require further changes to deal with some drafting issues.
- (6) On 1 January 2012 the home loans provisions (obligations on credit providers to provide home loan key facts sheets to consumers) of the Home Loans and Credit Cards Act will commence.
- (7) The Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011 (first enhancements bill) is the first of two enhancements bills proposed to be legislated over the next 12 months. The first enhancement bill amends the NCCP Act. The second enhancements bill is being prepared for introduction and passage in 2012. Consultation on this second Bill is expected to commence in November 2011. This Bill is likely to cover reforms in relation to the following topics: extending the NCCP Act to products that are currently unregulated (home reversion schemes, exempt leases, solicitor lending and peer-to-peer lending), avoidance issues and

what is expected to be a substantial overhaul of the existing consumer credit pre-contractual disclosure regime.

- (8) Further, if any need for regulation is identified by the Government and COAG in respect of lending to small businesses and lending for investment purposes, Treasury has advised these reforms will also be introduced through this second enhancements bill.

### **Concerns over the pace of reforms**

The reforms are moving at a pace that is at odds with the significant regulatory burdens they impose on industry. In the ABA's view, the pace of the reform program fails to take sufficient account of industry's need to implement these reforms in planned, orderly and workable timeframes. This is required to be done along with other major financial services reforms due to commence in early and mid-2012.

Much of the legislative credit reforms to date have relied extensively on subordinate regulation-making powers that are conferred under the primary legislation. Regulations tease out the detailed, prescriptive aspects of the compliance regime. This reliance on regulation making powers is expected to continue for the remainder of the program.

With commencement dates fixed in legislation, any delay in the finalisation of regulations means less time for credit providers to implement their compliance arrangements. This was the case with the Government's proposed home loan key facts sheets and is currently the case with commencement on 1 July 2012 of the credit cards reforms.

In all, there are 3 substantial pieces of credit reform legislation requiring industry implementation over the next 7 months<sup>2</sup>.

In setting the commencement timing for these reforms, banks need to plan the necessary resourcing and funding of these implementation projects. This includes IT systems modifications and implementation of compliance frameworks. For example, banks set periodical "windows" where they are able to open up their IT systems for making normal business changes and changes necessitated by regulation to avoid ad hoc, ill-timed interventions into these systems. Documentary, procedural and staff training changes are critical for banks to ensure their compliance frameworks are adequate. These steps are sequential in a process that depends on necessary preceding changes having been made before another step is taken.

These are changes that have to be made in a planned and orderly way and not just at the "flick of a switch" to ensure change risk is minimised and to achieve consistency. Management of change risk includes not only with IT systems

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<sup>2</sup> Banks implement IT systems "freeze" periods from December to mid-January to ensure that systems are able to serve this traditionally high customer transactions period and to provide for seasonal staff and consultants' leave arrangements.

changes but also all relevant processes, documents and staff training to avoid risk to both the bank and its customers.

### **Implementation costs**

It is difficult to provide the Commission with details of these costs. Many of the more recent implementation costs are still work in progress towards 2012 commencement dates.

In July 2011 the ABA provided the House of Representatives Economics committee with an estimate of the costs banks face in implementing the credit cards reforms. At this time the proposed regulations specifying the actual measures banks would need to put in place to comply with the legislation were not available because the relevant regulations were not in place. Based on the costs of implementation of previous, comparable regulatory reforms, the ABA informed the Committee that the costs to the banking industry to implement the credit cards reforms alone would be in the order of \$100 to \$150 million dollars.

Further, it is important to note that the costs to industry are not solely related to the temporary transitional period of implementing required changes. There are significant longer term and ongoing costs associated with annual operational costs, the loss of revenue and opportunity costs. Annual ongoing operational costs are estimated to be \$40 million per annum across the industry for the credit cards reforms. These annual operational costs may be attributable to: ongoing training requirements, customer communication costs (to establish, for example, opt-in or opt-out choices for customers), ongoing compliance and record-keeping, system updates and rebuilds and replacement of paper based application forms and key facts sheets to ensure compliance with the 'up to date' provisions of the law.

The ABA observed that a comprehensive cost-benefit analysis should have been undertaken by the Government during the policy development stage of the credit cards reforms. Apparently a Regulatory Impact Statement (RIS) was not required because the reforms to credit cards were the subject of a pre-election policy announcement in 2010. Yet, as a number of the credit cards reforms were part of the COAG's reform agenda had these reforms gone ahead in that process it is assumed a RIS would have been necessary.

The ABA will endeavour to provide the Commission with an estimate of the overall costs of the credit reform program to date. Closer to July 2012 there should be a better guide to the overall costs assuming the reform project has been completed.

### **The Commission's Approach**

The ABA understands that the Commission is posing the hypothesis that the credit reforms will deliver a net economic benefit to consumers and the community. A factor that could validate this hypothesis would be evidence that there has been a reduced incidence of financial stress in Australian households. The hypothesis is that this reduction would be attributed to the reforms,

particularly the responsible lending requirements of the NCCP Act, in helping people avoid going into financial crisis.

The main causes of consumers falling into financial difficulties with their loans are unemployment, illness and family breakdown. Banks' lending standards are recognised as very high and were demonstrated during the course of the global financial crisis in 2007/2008, particularly when compared with overseas lending experiences. Default rates with bank lending are extremely low relative to non-bank lending in Australia and overseas. Also, banks have the major share of consumer lending in Australia.

These factors together would suggest that consumer credit reforms, particularly the new responsible lending obligations, may have an impact on the customers of non-bank lenders, but overall impact of the reforms on households could be expected to be, in the main, marginal. It follows that the costs of the credit reforms imposed on banks as the major lender group to Australian households could be seen as disproportionate compared with the benefits gained.

It is too early to fully assess the impacts of the credit reforms as some of the reforms, such as the credit cards reforms, will not take effect until July 2012.

The ABA understands the Government has undertaken to conduct a review of the first phase of the reforms after the first 18 months of operation. The ABA looks forward to participating in that review that could provide a guide to an alternative basis for regulation of financial services in the future.

Yours sincerely

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Ian Gilbert