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## Consultation Paper 115 Responsible Lending

The Finance Sector Union of Australia (FSU) welcomes the opportunity to comment on the responsible lending consultation paper. The FSU strongly supports the transfer of credit regulation to the Commonwealth and the responsible lending provisions that have been included in the legislation.

The FSU represents 50,000 members employed in the finance sector across Australia. Our members deal with the day to day operation of financial services and have an active interest in promoting a professional, efficient, sustainable and fair marketplace for financial products.

The FSU has ongoing concerns regarding some provisions of the legislation;<sup>1</sup> however we are broadly supportive of ASIC's proposed approach within the legislated framework.

### Responsible lending, sales targets and commissions

We welcome the inclusion of provisions to mandate responsible lending into the regulation of credit – the FSU has long argued for such measures<sup>2</sup> and notes that the legislation includes a number of measures recommended in the FSU *Charter of Responsible Lending* that was launched in October 2008.<sup>3</sup>

The FSU developed the *Charter* in response to the fact that a large amount of activity in the finance sector marketplace is primarily based on short term competition for growth or market share rather than sustainable and responsible practices. This type of activity is often encouraged and even compelled by sales targets or commissions for finance sector staff and applies to a wide range of financial services, particularly the sale of credit and the increase of credit card limits. The culture of sales targets is, by definition, designed to maximise sales which (even inadvertently) leads to a higher risk of inappropriate sales occurring. When staff are constantly under pressure to achieve sales it will inevitably lead to some consumers being sold products that they may not be capable of repaying or may not even need.

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<sup>1</sup> For details see FSU's submission to the Senate Economics Inquiry into the Consumer Credit Bills - <http://www.fsunion.org.au/Policies-Submissions/default.aspx>

<sup>2</sup> FSU submission to *Inquiry into competition in the banking and non-banking sectors*, House of Representatives Standing Committee on Economics, 2008; FSU submission to the *Green Paper on Financial Services and Credit Reform*, 2008; *Inquiry into Home Loan Lending Practices and Processes*, House of Representatives Standing Committee on Economics, Finance and Public Administration, 2007.

<sup>3</sup> [http://www.fsunion.org.au/Upload/Policies%20and%20Submissions/FSU\\_Charter\\_of\\_Responsible\\_lending\\_Final.pdf](http://www.fsunion.org.au/Upload/Policies%20and%20Submissions/FSU_Charter_of_Responsible_lending_Final.pdf)

When targets are achieved bonuses or pay increases are granted. If they are not met then staff will suffer a financial loss and also suffer heightened job insecurity. This has created a culture that is designed to maximise sales at every opportunity which ultimately leads to a higher risk of inappropriate sales occurring.

The FSU supports ASIC's recent calls for commission based forms of remuneration to be banned in relation to financial advice.<sup>4</sup> We also welcome ASIC's acknowledgement that sales targets can have a distorting effect on the sale of other financial products.<sup>5</sup>

Sales targets carry the implicit message that ever increasing sales are good and desirable – the FSU does not share this view and believe it is detrimental to consumers, finance sector staff and the provision of good customer service.

The responsible lending provisions will ultimately require finance sector staff to not make sales in certain circumstances. The FSU believes this is entirely consistent with the provision of professional customer service and sincerely hopes that companies will begin to recognise this in their remuneration arrangements. The culture of sales targets simply rewards sales; in contrast the FSU advocates reward structures that reflect professional service and responsible behaviour.

The principle and practice of disclosure is widely accepted in the finance sector. Sales targets may not establish the same direct link between the individual sale and the financial incentive as is the case with sales commissions; however the fundamental issue is that sales targets do create an incentive to sell products which should be made transparent to the consumer.

The purpose of disclosures in the context of credit sales is to make explicit to the consumer significant factors that have the ability to influence the nature and size of the credit contract being proposed. There is no doubt that sales targets influence the behaviour of finance sector employees in relation to selling credit products and should therefore be disclosed to the consumer. For many finance sector employees basic wage increases are tied to sales targets – consequently staff are effectively compelled to try and make sales at every opportunity.

We understand and accept that ASIC must work within the framework provided by the legislation; however we urge ASIC to consider recommending a complete ban on sales based remuneration for financial products or, as a minimum, to ensure all credit providers fully disclose all types of commissions and sales based remuneration given the effect they can have on the sale of such products.

A recent survey of FSU members, predominantly in the established banking sector, found that:

- 59 per cent felt pressured to make inappropriate sales to meet sales targets.
- 52 per cent of workers felt obliged to try and sell debt products even when a customer didn't need them; and
- 63 per cent felt that inappropriate sales targets are having a negative impact on their ability to provide responsible customer service.

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<sup>4</sup> ASIC submission to the Parliamentary Joint Committee on Corporations and Financial Services Inquiry into Financial Products and Services – page 53.

<sup>5</sup> Parliamentary Joint Committee on Corporations and Financial Services Inquiry into Financial Products and Services, 16 September 2009, pg26.  
<http://www.aph.gov.au/hansard/joint/commttee/J12399.pdf>

Our specific comments in relation to the consultation paper appear below.

## **Reasonable inquiries**

*B1Q1 Do you agree with our proposed approach to guidance about the reasonable inquiries obligation being scalable?*

The proposed approach seems reasonable and appropriate in the circumstances. The potential impact on consumers of unsuitable credit products can be significant and we welcome guidance that would explicitly call for this to be considered. Unfortunately some lenders have been more likely to consider the impact upon themselves rather than the impact upon consumers.

The example in the consultation paper seems to suggest that where the size of the loan is smaller then less detailed inquiries will be necessary. This may be true in many instances; however for people on very low incomes the impact of an irresponsible small loan can be just as harsh as that of a large loan for people on higher incomes. We submit that the guiding principle should be the potential impact on the consumer.

We note that less extensive inquiries are envisaged where the credit contract has simple terms that can be easily understood – suffice to say we are yet to see such a contract.

*B2Q1 Do you agree with our proposed approach to guidance about making reasonable inquiries?*

The types of inquiries listed in paragraphs 23 to 24 appear to be appropriate and reasonable.

*B3Q1 Do you agree with our proposed approach to guidance about the processes we expect credit licensees to have in place to ensure they make reasonable inquiries?*

We concur with the proposed guidance contained in paragraphs 25 to 28 and endorse the need for licensees to have proper training and supervisory procedures in place. The FSU encourages ASIC to be proactive in monitoring these arrangements and ensuring that all employees are trained to discharge their credit duties and given adequate time and resources to undertake the necessary training for their roles.

## **Assessment of Unsuitability**

*C2Q1 Do you agree with our proposed approach to guidance about determining the consumer's financial situation and capacity to repay?*

The proposed guidance appears reasonable; however we suggest that it would be prudent to spell out that a licensee must take into account prospective consumers existing liabilities when assessing their financial situation and capacity to pay.

Just investigating the costs of the proposed contract as well as the borrower's income will not give a full understanding of a consumer's financial situation and capacity to pay.

*C3Q1 Do you agree with our proposed approach to guidance about substantial hardship?*

The guidance regarding substantial hardship appears to be reasonable and appropriate.

*C4Q1 Do you agree with our proposed approach to guidance about determining the consumer's requirements and objectives?*

*C5Q1 Do you agree with our proposed approach to guidance about determining whether a particular credit transaction is fit for purpose?*

The FSU is supportive of the proposed guidance in relation to C4 and C5. The “fit for the purpose” principle has long been used in relation to Trade Practices issues and appears to be a suitable and appropriate assessment technique for credit products.

If you have any questions in relation to this submission please contact Rod Masson, National Communication and Policy Manager, on (03) 9261 5330 or James Bennett, Senior Policy and Research Officer on (03) 9261 5405.

Yours sincerely

A handwritten signature in black ink, appearing to read 'L Carter', with a stylized flourish at the end.

Leon Carter  
National Secretary  
30 October 2009