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Ruth Moore
Manager, Financial Services Unit
Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2060

11 October 2019

By email: productregulation@treasury.gov.au

Dear Ms Moore

CONSULTATION - CORPORATIONS AMENDMENT (DESIGN AND DISTRIBUTION OBLIGATIONS) (DDO) REGULATIONS 2019

The Australian Finance Industry Association [AFIA] welcomes the opportunity to comment on the *Corporations Amendment (Design and Distribution Obligations) Regulations [the DDO Regulations]*. We also note and acknowledge the engagement we have had with ASIC on this topic.

AFIA KEY POSITIONS SUMMARY

By way of overview, AFIA:

- supports the provision of finance to a standard that meets community expectations
- understands that the community expects financiers to make finance decisions that strike a reasonable balance between the goals of:
 - avoiding the incidence of customers (consumer or small business) entering into a contract where they are unable to meet their contractual obligations, and
 - enabling access to finance for customers (consumers and small business) who have the desire and ability to service it.
- notes the important distinction between consumer and commercial finance and consequently that the balance referred to above may vary depending on whether the customer is a consumer or a small business.
- acknowledges the DDO Regulations have been drafted to reflect this as well as achieving other important Government policies of red-tape reduction and best-practice regulation making that sees a regulatory response proportionate to evidence-based risk of harm or market failure.

- the outcome is appropriately focusing the DDO Regulations on consumer finance where risk has been identified by excluding '*credit provided for business purposes*' and '*credit facilities that do not involve the provision of credit*'.
- in the absence of this clarity, the outcome of the primary amendments would have been a one-size fits all approach given the breadth of consumer and commercial products with scope of the definition of credit under the ASIC Act and its Regulations with potential unintentional but nevertheless significant flow-on to product-innovation or restrictions on access and increased price paid by business customers (including small / medium sized enterprises) for commercial finance.
- Requests ASIC develop regulatory guidance as soon as practical to facilitate members implementing an efficient and effective compliance program to meet the April 2021 commencement given the amount of detailed quantitative and qualitative research, information technology system changes, product and distribution channel collateral changes members will be required to make a Target Market Determination [**TMD**]. In particular, ASIC guidance on what 'best practice' for TMD's would look like and specifically, whether a TMD will be required at a granular level (e.g. home loan) or an individual product level (e.g. fixed home loan) would be particularly valuable.

More detail, including background on AFIA and our approach to obtain operational feedback to inform Treasury's consultation follows, together with comment on specific clauses of the DDO Regulations.

AFIA'S BACKGROUND – CONTEXT OF FEEDBACK

By way of background, AFIA is the voice of a diverse Australian finance industry. AFIA supports our Members to ensure a fair, equitable and competitive market for customers through representation, insights and connectivity. AFIA is uniquely placed to respond given our broad and diverse Membership of over 100 financiers operating in the consumer and commercial markets. These include both bank and non-bank members, some large participants in the market, others niche players. Further background on AFIA is available from www.afia.asn.au and below.

AFIA'S INSIGHTS -PROCESS

Reflecting the level of interest in ensuring the implementation of the DDO will be effective and efficient while achieving the underlying consumer protection benefits a significant number of our Members has informed AFIA's feedback. Our submission focuses on sections in the DDO Regulations where Members had some commentary or were seeking greater clarification. We also note that while members have contributed to inform this response, from an organisational view, the positions being

put by AFIA may not reflect every Member's specific position on all the issues. Their individual member viewpoint will get captured through the relevant member's organisationally-targeted submission.

FEEDBACK ON SPECIFIC PROVISIONS OF THE BILL

By way of more detailed commentary on the summary of key positions provided earlier:

AFIA Recommendation 1 - Item 1, Regulation 7.8A.01 – Additional persons subject to the DDO

Our members are concerned that as currently drafted finance brokers may fall within Corporations Act paragraph 994B(1)(ba)(i) (introduced by the DDO amending Act) and therefore potentially have an obligation to prepare TMD's. If that were the case, clarification is sought on whether the finance broker would follow their own TMD or the lender's TMD if they differed. AFIA also notes this could result in a multitude of various TMD's for a single product, which would make it difficult for product issuers to ensure that a product is distributed in accordance with the TMD.

AFIA recommends:

- to remove compliance uncertainty and clarify that finance brokers do not fall within Corporations Act paragraph 994B(a)(ba)(i) an exemption is provided; or
- if it is intended that finance brokers are captured and obliged to prepare TMDs, that products for which a TMD is required are specifically indicated in the table in DDO Regulation 7.8A.03. This will greatly assist operational roll out and compliance certainty.

AFIA Recommendation 2 - Item 1, Regulation 7.8A.04 –Products excluded from the DDO

AFIA notes the exclusion of the provision of a mortgage (as distinct from the credit contract secured by the mortgage) from the provisions of DDO. However, in the absence of a similar exclusion for any associated guarantees, the outcome is compliance uncertainty with the attendant flow on costs.

AFIA Recommendation:

- To ensure compliance certainty the exclusion should be extended to include, in addition to a mortgage, any associated guarantees.

AFIA Recommendation 3- Item 1, Regulation 7.8A.04 –Products excluded from the DDO

AFIA notes that there would be value in further clarification of the concept of '*business purposes*' used in the exclusions (Table 7.8A.04 item 8) in order to provide a clear understanding of what activities will fall under the scope of the exemption. For example, would this include finance provided for 'investment' purposes? We understand that finance provided for residential property investment

(which would be subject to regulation under the National Consumer Credit Protection Act [NCCPA]) would be subject to the DDO. But whether a loan to invest in shares would also be subject to the DDO is less clear.

As part of this, there may also be benefit in stating that products regulated by the NCCPA and Buy Now Pay Later [BNPL] products provided predominantly for a personal, household or domestic purpose are captured under the DDO, with all other business and unregulated products being exempt.

AFIA Recommendation:

- The concept of *'business purposes'* should be more clearly defined; for example, using the NCCPA and BNPL products provided predominantly for personal, domestic or household purposes as the 'black line'; of
- If Treasury determines this is not warranted, the DDO Regulations should include a note providing the following following products / activities as examples of credit provided for *'business purposes'* and therefore exempt from the DDO:
 - any working capital product provided for businesses
 - investment activities (such as investing in commercial real estate or shares)
 - novated leases provided as part of an employee's salary packaging
 - credit provided to self-managed super funds
 - BNPL products for businesses

AFIA Recommendation 4- Item 1, Regulation 7.8A.04 –Products excluded from the DDO

AFIA suggests that the drafting of the Kind of Financial Product that is intended to fall within the exemption provided in Table 7.8A.04 Item 9 *'credit facilities that do not involve the provision of credit'* has the potential to create confusion.

AFIA Recommendation:

- To avoid confusion and achieve the same objective sought by the current drafting, AFIA recommends redrafting of Item 9 as follows:

Item 9	Credit facilities that do not involve the provision of credit	A credit facility included in paragraph 2B(3)(b) of the Australian Securities and Investments Commission Regulations 2001.
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This clearly exempts products that fall within the list included in ASIC Regulation 2B(3)(b). If a product does not fall within that list but meets ASIC Regulation 2B(3)(a) it would not be exempt. This would be the outcome of the above wording.

AFIA Recommendation 5 – DDO Obligations and AFCA

AFIA and its Members seek further guidance on how AFCA will:

- address complaints involving persons and products excluded from the DDO noting the overriding determinative factor for complaints within their jurisdiction is fairness; legal principles are merely one element to be taken into account in considering whether that test has been met.
- approach compensation in circumstances where a customer has not suffered any loss but may not sit within a TMD.

AFIA Recommendation 6- Lender Monitoring Obligations

Finally, AFIA suggests issuers would benefit from further guidance on the concept of what would be regarded as 'reasonable steps' used in Corporations Act paragraph 994E(1) (introduced by the DDO amending Act). Further clarification would help to ensure that lenders have sufficient time to implement appropriate monitoring standards, that are not unduly onerous.

AFIA recommends:

- A further paragraph is included in the DDO Regulations to give guidance on the concept of 'reasonable steps' for the purposes of Corporations Act paragraph 994E(1).
- Further, the guidance should envisage scalability, to cater for complex situations (for example, to situations where lenders may have to monitor a significantly large number of brokers).

CONCLUSION + NEXT STEPS AFIA

AFIA Members are committed to working with the Treasury, ASIC, AFCA and other relevant stakeholders to ensure a DDO regime that operates in a way that strikes a reasonable balance between the goals of minimising risk of customer harm while enabling access by customers (both consumers and small business) that have the desire and ability to service finance to support their own and Australia's economic future.

We welcome the opportunity to discuss the contents of this submission further.

If you have any questions, please contact me at helen@afia.asn.au or Chalisa Parekowhai, Associate Director Policy at chalisa@afia.asn.au or both via 02 9231 5877.

Kind regards



Helen Gordon
Chief Executive Officer

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AFIA'S BACKGROUND

AFIA is the voice of a diverse Australian finance industry. AFIA supports our Members to ensure a fair, equitable and competitive market for customers through representation, insights and connectivity.

AFIA Members:

- include banks (major, regional and mutual/community-owned) and non-banks;
- range from ASX-listed public companies through to small businesses providing finance;
- operate via a range of distribution channels including bricks and mortar premises, intermediaries (finance brokers, dealerships, suppliers) through to online / digital access
- collectively operate across all states and territories in Australia in capital cities through to regional and remote areas: the majority operating across at least one border;
- have customers from all demographics, all age groups (legally able to borrow) in support of Australia's diverse and multi-cultural community with:
 - consumers ranging from high to low-income earners (including some whose main income source may be government welfare); many with substantial assets, others with few; single borrowers through to blended families; covering the whole range of employment scenarios, full-time, part-time, seasonal or casual employment.
 - commercial entities ranging from sole traders and partnerships through to the more complex corporates (e.g. trusts, corporate group) and government-entities some with no employees through to others with hundreds (if not thousands) of employees.
- provide a broad range of products:
 - consumer: from personal unsecured loans, revolving products (including credit cards and interest free products coupled with lines of credit), loans secured by land or personal property; consumer leases of assets (including household/electrical/IT or cars) and buy-now, pay later solutions;

- commercial: asset or equipment finance (finance/operating lease, secured loan or hire-purchase agreement or novated leases); working capital solutions (online unsecured loans; debtor and invoice finance; insurance premium funding; trade finance; overdrafts; commercial credit cards) together with more sophisticated and complex finance solutions.

Further detail on AFIA is available from: www.afia.asn.au.