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2021 Code Review  
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Dear Mr Callaghan

## **Norton Rose Fulbright Australia – Submissions to the 2021 Independent Review of the Banking Code of Practice**

### **1 Introduction**

- 1.1 Norton Rose Fulbright Australia welcomes the opportunity to make this submission as part of the Australian Banking Association's (**ABA**) 2021 Independent Review of the Banking Code of Practice (the **Code**).
- 1.2 Norton Rose Fulbright Australia is a trusted advisor to many ABA members and other financial institutions advising them on the implementation, application and effect of the Code. We have seen, in practice, the significance of the Code to the banking sector and bank customers alike.
- 1.3 We set out in the proceeding paragraphs a number of observations regarding the Code that we consider to be of most significance for your consideration.

### **2 Small Business Lending - consequences of more complex lending products being subject to the Code**

- 2.1 Small business operators often seek to take advantage of lending products that are more complex and/or technical (in their terms and structure) than more straightforward interest-bearing business loans or other lending products.
- 2.2 Examples of these products include receivables or payables financing products. Such products are often offered by the trade finance arms of major banks. They typically contemplate a discounting of invoiced amounts (on invoices issued by a supplier, where that supplier is the bank's customer in a receivables financing, or on invoices issued to a buyer, where that buyer is the bank's customer in a payables financing). This will include a discounting calculation which reflects the credit risk of the buyer in a receivables financing and the buyer in a payables financing.
- 2.3 We note that the Code acknowledges that each such product is a 'specialised lending transaction'.<sup>1</sup>

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<sup>1</sup> Code, Part 6 *Lending to small business*, para 85(b).  
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2.4 In circumstances where a small business (as defined in the Code) enters into such transactions, the Code will apply to the product and the relationship between the bank and the small business. In particular, paragraphs 15 (clear information to allow for an informed decision), 17 (clear and timely communication), 25 (including clarity on the interest rate to apply and the method of its calculation) and 73 (provision of a plain English document setting out the key general terms of the loan) of the Code will apply.

2.5 Clarity and usefulness of information are often a matter of judgment and interpretation for the parties involved (and the judgments and interpretations that can be made can well differ as between the customer, the bank and their advisers (if any)). Given the possibility of such differences between the parties (because, for example, of the understandable differing levels of respective knowledge or professional experience), some consideration could be given to the following:

- (1) The Banking Code Compliance Committee (**BCCC**) (or other relevant body) providing guidance, from its experience in monitoring the Code, on good examples of clarity and usefulness of information/communication in relation to the more complex 'specialised lending transactions' referred to above.

This could include examples of text or wording for market participants to consider and which the BCCC (or other relevant body) believes would typically demonstrate material compliance with the Code.

- (2) Any such examples provided as contemplated under (1) above should be presented as non-binding and non-exhaustive guidance (similar to guidance published from time to time by Australian regulators, including the Australian Securities and Investments Commission). In effect, these would be suggestions that a bank could consider when seeking to comply with the Code provisions that will apply to such 'specialised lending transactions' because the counter-party is a small business.

2.6 We also raise for consideration whether there is any scope for narrowing the breadth of the 'small business' definition where it is applied in connection with a specialised lending transaction. The intention behind this would be to provide a reduced subset of 'smaller' or 'less sophisticated' small businesses who would, and should, continue to benefit from the protections afforded by the Code.

2.7 The rationale for the above suggestions is based on the question as to whether relevant obligations in the Code (set out in paragraphs 15, 17, 25 and 73) are appropriate to apply universally to all small businesses who are accessing relatively complex specialised lending transactions. We submit that they are not. Given the technicality and specialisation of such transactions, it could be argued that only businesses with the requisite knowledge should access them, in which case the protections afforded by the Code (and the accompanying regulatory burden on the finance provider) are unnecessary, resulting in a corresponding negative impact on market efficiency.

2.8 A practical example is the application of paragraph 73 (provision of a plain English document setting out the key general terms of the loan) of the Code to a complex specialised lending transaction. Unlike the provision of such a document to an individual in the context of, for example, a transaction account or basic loan product (where the utility of that type of plain English document is apparent), its application to a complex specialised lending transaction, where, because of the nature of the product, a translation into 'plain English' is not always going to be possible, practical or necessary in the circumstances (given the relevant borrower or guarantor for these types of product will typically either be separately advised or otherwise readily familiar with their terms and operation).

### 3 **Impact of mandatory breach reporting regime for credit licensees**

3.1 From October 2021, credit licensees will be subject to new mandatory breach reporting obligations. These obligations mirror the breach reporting obligations for financial services licensees.

3.2 An issue for consideration as part of the review of the Code is the interplay between the new breach reporting obligations, the role of the BCCC and a bank's obligations to report non-compliance or systemic issues to the BCCC. This will become particularly important if/when enforceable provisions are incorporated into the Code.

#### 4 Proposed abolition of responsible lending laws

4.1 The Commonwealth Government announced in September last year that the responsible lending laws (as they appear in the *National Consumer Credit Protection Act 2009* (Cth) (**NCCPA**)) would be abolished. The proposed reforms have been described as deregulatory, benefiting lenders and borrowers alike.

4.2 The Code is underpinned by the Statement of Guiding Principles. Relevantly, two of those principles say:

(1) We will be fair and responsible in our dealings with you.

(2) We will take a responsible approach to lending.

4.3 Additionally, under the Code, banks commit to letting a customer know, if their loan is regulated by the NCCPA, that the customer can obtain a copy of the unsuitability assessment that was made.

4.4 It is unclear at this stage how this commitment, and the Guiding Principles, will be interpreted if the responsible lending laws (and the unsuitability requirement embedded within those laws) are abolished. We would recommend that this be kept front of mind once the industry knows more about the status of the proposed responsible lending law reforms.

#### 5 Rights under a Guarantee

5.1 Part 7 of the Code provides guidance from the moment a guarantor considers giving a guarantee to the final stage of enforcing the guarantee. Whilst for the most part this has, in our view, been addressed well by the current Code, there are areas which need revision in order to provide clarity of the bank's and guarantor's rights.

5.2 The Code requires that the terms and conditions of a guarantee must contain a notice that the guarantor can request information about the transaction or loan from the bank.<sup>2</sup> It is important that the guarantor is able to be kept informed about the transaction or loan they are guaranteeing. However, it is unclear what information is said to relate to 'a *transaction or loan*'. For instance:

(1) Is a guarantor entitled to request information about or a copy of a settlement deed which was agreed between the borrower and bank in full and final settlement of the loan? Settlement deeds are generally subject to a confidentiality clause and the guarantor may not be a party to the deed.

(2) Is a guarantor entitled to any information about, or documents pertaining to, the appointment of an agent over property held by the borrower in order to recover outstanding debt owed under the facility or the appointment of receivers and managers by the bank?

(3) Is a guarantor entitled to bank and loan statements that relate to the debt and borrower they are guaranteeing?

5.3 There needs to be a clear distinction on the type of information that can be requested by the guarantor, and disclosed by the bank, in order to protect the borrower's financial position and personal information and having regard to a bank's privacy and confidentiality obligations.

5.4 Further, the right of the bank to enforce a guarantee requires further clarification and consideration. The bank is required to first enforce any mortgage or other security that the borrower has provided before pursuing the guarantor.<sup>3</sup> It would be useful for the bank to understand after how many attempts, or to what extent of enforcing the borrower's security, is the bank justified in pursuing the guarantor. We suggest including a time period for the bank to exhaust all avenues to enforce the borrower's security before it is allowed to enforce the guarantor's security.

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<sup>2</sup> Code, Part 7 *Guaranteeing a loan*, para 96(e).

<sup>3</sup> Code, Part 7 *Guaranteeing a loan*, para 113.

- 5.5 There are circumstances where the bank is not required to first enforce any mortgage or other security that the borrower has provided and can immediately enforce the guarantor's security.<sup>4</sup> For instance, if the bank reasonably expects that the net proceeds of that enforcement will not be sufficient to repay a substantial portion of the guaranteed liability. The sections around this right need further clarification, particularly what constitutes a reasonable expectation or a "*substantial portion*".
- 5.6 The Code could address this issue by:
- (1) 'reasonably expect' - providing a non-exhaustive list of factors which the bank can look to for guidance in satisfying itself that there is no reasonable expectation that the net proceeds of the enforcement will be sufficient; and
  - (2) 'substantial portion' - quantify a percentage of the debt which a bank can rely on when determining whether the funds can repay a substantial portion of the guaranteed liability. This could be at least 70% of the debt.
- 6 Notice periods under the Code**
- 6.1 The Code imposes a number of obligations on a bank to provide notice and/or information to consumers within relevant periods.
- 6.2 Notably, a bank is obliged to provide a small business notice of its decision not to extend the expiry date of a loan, at least 3 months before the small business is required to repay the loan in full.<sup>5</sup> This obligation only applies if the small business is not in default and the principal amount owing on the loan is not due to be fully repaid at the end of its scheduled term by regular periodic payments.<sup>6</sup>
- 6.3 In principle, we share the view that at least 3 months' notice is frequently necessary to enable a small business to make alternate arrangements should a bank decide not to extend the term of an existing loan.
- 6.4 However, there are a variety of credit facilities to which the application of a strict 3 month notice period may produce unintended results, such as:
- (1) pay-day loans, which are intended to be short term facilities that expire on a chosen pay date;
  - (2) receivables or payables financing products, where access to funds is intended to increase and decrease as the value of invoices change and repayment is made;
  - (3) small business overdrafts or on-demand facilities, where access and use of the facility is intended to be flexible. We note that small business overdrafts and on-demand facilities are both excluded from the notice period in relation to defaults under a loan;<sup>7</sup>
  - (4) operating leases, "*where the loan term is intrinsically tied to the useful life of the asset*";<sup>8</sup> and
  - (5) any other facilities where the contracted term is less than 3 months.
- 6.5 Accordingly, we submit that some consideration should be given in the review about whether banks should be excluded from an obligation to provide a 3 month notice period not to extend a loan in circumstances where it would be unreasonable to do so by taking into account the nature and term of the facility. This could also apply where a bank and its customer have otherwise negotiated terms of a standstill or forbearance arrangement.

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<sup>4</sup> Code, Part 7 *Guaranteeing a loan*, para 115(b).

<sup>5</sup> Code, Part 6 *Lending to small business*, para 86.

<sup>6</sup> *Ibid.*

<sup>7</sup> Code, Part 6 *Lending to small business*, para 75.

<sup>8</sup> Phil Khoury, Independent Review of the Code of Banking Practice, 31 January 2017 (**Khoury Review**), 8.7.1.

7 **Code structure and presentation**

- 7.1 Following the Khoury review's recommendation that the Code be re-drafted in a modern structure and style,<sup>9</sup> the Code was amended using more accessible language and the implementation of a clearer structure.
- 7.2 We support previous amendments to the structure and the introduction of a "*plain language*" Code.
- 7.3 However, we consider that the Code could further be improved through the introduction of flow charts covering every complaint stage, from internal and external dispute resolution, complaints to the Australian Financial Complaints Authority (**AFCA**), and to the imposition of sanctions by the BCCC. The visual representation of these processes will enhance consumer accessibility to, and knowledge of, the complaints process for grievances and breaches of the Code.
- 7.4 Guidance could be taken from the presentation of the AFCA Rules for examples of the types of visual aids that could be included in the Code.<sup>10</sup>

We are happy to discuss any of our comments above if that would be of assistance.


Yours faithfully



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<sup>9</sup> Khoury Review, Recommendation 1.

<sup>10</sup> Australian Financial Complaints Authority, Complaint Resolution Scheme Rules, 13 January 2021 (**AFCA Rules**).