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General Editor's note

Karen Lee *LEGAL KNOW-HOW*

What comes to your mind if I say "wagyu"? What about "shiraz"? You are on the right track if you think I am about to mention Perram J's decision last year in *Australian Securities and Investments Commission (ASIC) v Westpac Banking Corp (Liability Trial)*.[1] By way of background, in March 2017, ASIC commenced Federal Court proceedings against Westpac to test the responsible lending provisions of the National Consumer Credit Protection Act 2009 (Cth). The matter was heard in May 2019, and Perram J handed down his decision in August 2019.

Perram J famously said:

> I may eat Wagyu beef everyday washed down with the finest shiraz but, if I really want my new home, I can make do on much more modest fare. Knowing the amount I actually expend on food tells one nothing about what that conceptual minimum is. But it is that conceptual minimum which drives the question of whether I can afford to make the repayments on the loan.[2]

His Honour awarded Westpac with a win, but ASIC filed an appeal. The matter was heard in February 2020 and in June, the Full Federal Court handed down its majority decision 2:1 dismissing ASIC's application.[3]

This decision is significant in many ways, among other things, because it provides guidance to credit providers with regard to complying with their obligation to make inquiries about a borrower's financial circumstances and capacity to service a loan, and to verify the information that borrowers give banks. In their article "Winner winner wagyu dinner: ASIC loses appeal in Westpac responsible lending case", **Andrea Beatty**, **Gabor Papdi**, **Chelsea Payne** and **Chloe Kim** (Piper Alderman) walk us through the procedural history and reasons for dismissal of the appeal. Importantly, the authors explain the decision's implications on responsible lending, including COVID-19 impact.

ASIC's product intervention power allows the regulator to temporarily intervene in a range of ways, including to ban financial products and credit products when there is a risk of significant consumer detriment. This power is one of the regulatory tools available to ASIC to improve consumer outcomes. In June 2020, ASIC released *Regulatory Guide 272: Product Intervention Power*.[4] This document contains guidance on the proposed use of ASIC's product intervention power. In their article, "ASIC's product intervention power following Regulatory Guide 272 and Cigno v ASIC: the beginning of broader intervention?", **Matt Daley**, **Vanessa Pallone**, **Nick Killalea** and **Zach Burridge** (Clayton Utz) set out for us the scope of ASIC's power and when the regulator will use it, the kinds of orders that can be made and how they are made, and lessons from *Cigno Pty Ltd v ASIC*,[5] the first and only use of the product intervention power to date.

In May 2020, ASIC announced its third and final tranche in over $160 million in remediation for consumers who have been sold junk consumer credit insurance (CCI). In its media release, ASIC stated that:

> … this follows ASIC's 2019 report (REP 622) on the sale of CCI by 11 major banks and lenders across eight years, which found that the design and sale of CCI had consistently failed consumers.[6]

In their article "A sea change concerning CCI products sees significant remediation for wronged consumers", **Andrea Beatty**, **Chelsea Payne** and **Chloe Kim** (Piper Alderman) look at ASIC's actions in each tranche, and explain how and why the regulator's approach to CCI products means lenders who continue to offer CCI need to be mindful of their sales practices and the eligibility of their customers.

I hope you enjoy reading this issue of the newsletter. Please do not hesitate to share any comments and feedback with me.

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Footnotes

1. *Australian Securities and Investments Commission (ASIC) v Westpac Banking Corp (Liability Trial)* (2019) 139 ACSR 25; [2019] FCA 1244; BC201907218.
2. Above, at [76].
3. *Australian Securities and Investments Commission (ASIC) v Westpac Banking Corp* [2020] FCAFC 111; BC202005844.
4. ASIC *Regulatory Guide 272: Product Intervention Power* (June 2020) https://download.asic.gov.au/media/5633261/rg272-published-17-june-2020.pdf.
5. *Cigno Pty Ltd v ASIC* [2020] FCA 479; BC202002876.
6. ASIC "ASIC secures over $160 million in remediation for junk consumer credit insurance" media release 20-115MR (13 May 2020) https://asic.gov.au/about-asic/news-centre/find-a-media-release/2020-releases/20-115mr-asic-secures-over-160-million-in-remediation-for-junk-consumer-credit-insurance/.

Winner winner wagyu dinner: ASIC loses appeal in Westpac responsible lending case

***Andrea Beatty**, **Gabor Papdi**, **Chelsea Payne** and **Chloe Kim** PIPER ALDERMAN*

The Australian Securities and Investments Commission's (ASIC) appeal from the Federal Court's decision[1] dismissing its claim that Westpac Banking Corp (Westpac) had breached its responsible lending obligations under the National Consumer Credit Protection Act 2009 (Cth) (NCCP Act) was dismissed by the Full Federal Court.[2] The majority judgments (Gleeson and Lee JJ, Middleton J dissenting) handed down on 26 June 2020 confirmed the primary judge's finding that Westpac had not failed to make the assessment of unsuitability required by ss 128(c) and 129 of the NCCP Act and ASIC misinterpreted these provisions of the NCCP Act.

Procedural history

The Full Federal Court's judgment comes after 3 years of legal battle beginning 1 March 2017 when ASIC initially commenced legal proceedings against Westpac for failing to assess whether potential borrowers would be able to meet their repayment obligations prior to entering into home loan contracts. ASIC alleged that Westpac had breached its responsible lending obligations in relation to 261,987 home loan contracts that it entered into by:

- using the Household Expenditure Measure (HEM) benchmark instead of the customer's declared living expenses in the "Serviceability Rule" element of its automated credit decision system and
- in relation to loans with an interest-only period, calculating repayments as if the customer made principal and interest repayments from the commencement of the loan term.

ASIC and Westpac had agreed on a $35 million (plus ASIC's costs) civil penalty but this was refused by Perram J as the parties' proposed orders did not specify any conduct that contravened the NCCP Act.[3] The case proceeded to trial and it was held that Westpac had not breached responsible lending provisions as claimed by ASIC. Piper Alderman has previously commented on the first instance decision.[4]

On 10 September 2019, ASIC filed an appeal with the Full Federal Court of Australia against Perram J's decision. ASIC's appeal was based on two broad grounds:

- The primary judge erred in finding that by means of the "70% Ratio Rule", Westpac did take into account customers' declared living expenses and that Westpac did make the assessment required by s 128(c) (declared living expenses grounds).
- The primary judge erred by finding that Westpac did make the assessment of unsuitability required by s 128(c) in using the "Full Term Method" to calculate periodic repayments on interest-only loans for the purpose of its serviceability assessment (interest-only loans grounds).

On 25 February 2020, Westpac's appeal was heard before the Full Federal Court in a 1-day hearing where ASIC's counsel criticised Perram J for his "thought experiments", claiming his Honour had erred in his prior decision, further arguing that Perram J had erred in his decision as Westpac had failed in its home loan assessment process as it was considering expenses from an "imaginary individual" rather than an actual person taking out a mortgage. However, ASIC's appeal was ultimately dismissed with ASIC also being ordered to pay Westpac's legal costs.

Reasons for dismissal of appeal

Both broad grounds of appeal centred on whether the primary judge was correct in holding that Westpac had made an "assessment" in accordance with s 129 prior to entering into the credit contracts, as required by s 128(c).

On the interest-only loans grounds, the Full Federal Court unanimously upheld the primary judge's decision that in using the Full Term Method (ie, apportioning principal repayments over the entire life of the loan, as if it were a principal-and-interest loan) to determine the repayment amounts to be used in the serviceability calculations, Westpac did make an assessment in accordance with s 129. It was held that given the nature of interest-only loans — that is, the amount that the consumer is obliged to pay varies at different times during the life of the loan, even ignoring potential interest rate changes — some estimation and making of assumptions is inevitable. It was therefore open to

Westpac to use the Full Term Method, and its inherent assumptions, to estimate monthly repayments, and the assessment thereby made was in fact based on the terms of the proposed credit contract and the consumer's financial situation.[5]

On the declared living expenses grounds, the majority upheld the first instance decision, finding that:

- the NCCP Act leaves it open to the licensee to decide how it will use the results of its inquiries and verification to assess unsuitability, provided that it in fact assesses whether it will be unsuitable for the particular consumer, and does not require a consumer's declared living expense amounts to be taken into account in all cases[6] and
- Westpac did take customers' declared living expenses into account via the 70% Ratio Rule, which was part of the automated decision system, and so contributed to the process of assessing unsuitability.[7]

Gleeson J upheld Perram J's finding that Westpac had in fact considered each customer's declared living expenses by applying the 70% Ratio Rule. The customer's declared living expenses were an input into the 70% Ratio Rule which, together with the Serviceability Rule (and around 200 other rules), formed part of the automated decision system which was the process by which Westpac made an assessment as to unsuitability.[8]

Furthermore, Gleeson J held that Div 3 of Pt 3-2 of the NCCP Act does not contain an explicit requirement for credit providers in all cases to use a consumer's declared living expenses in making an unsuitability assessment. It was noted that s 130(1)(b) of the NCCP Act does not in all cases require lenders to obtain declared living expense information (in the manner that Westpac did — itemised into various categories) from consumers.[9] Gleeson J explained that if the NCCP Act required all information collected under s 130(1) to be taken into account, it would raise further questions on whether mere consideration is sufficient or if it requires the information to be included in a mathematical calculation of the consumer's likely ability to comply with their financial obligations under the proposed contract (and if the latter, the formula for that calculation).[10] The qualifications in s 131(2) on what information can be used in assessing unsuitability were held to support the view that all information gathered during the s 130 inquiries do not need to be utilised in making an assessment in accordance with s 129, agreeing with the primary judge in this regard.[11] In addition, Gleeson J repeated with apparent approval the primary judge's view that the consumer's historical spending was not a necessary variable in assessing the consumer's likely future ability to comply with their financial obligations under their loan contract.

Lee J agreed with Gleeson J on the declared living expenses grounds,[12] but added the following:

- Sections 128 and 129 of the NCCP Act do not specify the method in which the suitability assessment needed to be conducted, other than for it to specify the period covered and to assess whether the credit contract will be unsuitable for the consumer if entered into within that period.[13]
- The statutory purpose of the provisions is not only able to be fulfilled if all information collected are taken into account in the unsuitability assessment and simply labelling an expense item as a "declared living expense" does not change its discretionary character.[14]
- Since breach of the obligation to make an assessment carries a civil penalty, ss 128(c) and 129 should be interpreted on the basis that if they obliged a licensee to take into account all information collected, they would have done so clearly and unambiguously.[15]

Middleton J dissented, holding that ss 128(c) and 129 require all relevant and material information to be used when conducting the unsuitability assessment, and that the consumer's declared living expenses are relevant and material in all cases. The licensee cannot know whether or not a particular consumer can reduce any or all of their declared living expenses without first considering what those expenses are and the characteristics of the consumer.[16] It would be open to a licensee to use the HEM benchmark instead of the consumer's declared living expenses in determining whether the consumer is likely to be able to comply with their financial obligations under the contract and without substantial hardship, but only after having considered the consumer's declared living expenses and determining that the HEM benchmark is a preferable input into the assessment. It would not, however, be open to a licensee to ignore the consumer's declared living expenses without consideration of them.[17]

Overall, the decision of the majority confirms that the NCCP Act leaves it up to credit providers to determine how they will conduct loan unsuitability assessments, subject to the requirement to specify the period covered by the assessment (which must include the credit day) and to assess whether or not the credit contract would be unsuitable for the consumer if entered into, based on the definition of "unsuitable" in s 131.

At the time of writing, the timeframe for ASIC to seek special leave to appeal this decision to the High Court has not yet expired. The fact that there was a dissenting judgment increases the probability of there being an appeal.

Implications for responsible lending

Impact on lenders

This decision confirms that the NCCP Act leaves it to lenders' discretion as to how they carry out unsuitability assessments, so long as their assessment states the period covered (which must include the credit day) and is directed at the elements of unsuitability in s 131(2). It reassures lenders that they do not need to, in all cases, incorporate the consumer's historical expenditure into an arithmetic cash flow calculation. Rather, the NCCP Act affords them a greater degree of flexibility to determine what is material to the unsuitability assessment and how it should be taken into account. Lee J's comment that where civil penalties flow from a contravention of the NCCP Act it is imperative to have legislative clarity to ensure lenders are aware of their obligations is applicable to other obligations under the NCCP Act and should give lenders some comfort when confronted with ambiguously expressed obligations.

However, lenders should note that the first instance decision, and consequently this appeal decision, concerned the narrow issue about whether or not Westpac performed an assessment as required by s 128(c) prior to entering into the credit contracts. It was not pleaded that any of the credit contracts in question were unsuitable for consumers, and therefore this issue was not explored at trial or on appeal. Lenders' discretion to determine how they will assess unsuitability, and what information they will take into account in their assessments, will be constrained by the need for the unsuitability assessment to be correct. Section 131(1) imposes separate civil penalty liability for incorrectly failing to assess a credit contract to be unsuitable for a consumer, and s 133(1) imposes civil penalty liability for entering into a credit contract that is unsuitable for the consumer.

COVID-19 impact

As identified in Middleton J's judgment "Westpac's system and multiple rules were extensive and well documented".[18] Clear documentation during the responsible lending process is vital especially during the tumultuous times brought by COVID-19. Furthermore, during the unique circumstances of COVID-19, the assessment criteria should be flexible and incorporate assumptions regarding a consumer's employment and whether they are receiving financial aids such as JobKeeper and JobSeeker. Especially as these government aids are due to finish in September 2020, credit providers need to consider how COVID-19 payment may impact the unsuitability assessment — though the key takeaway from this case is that the NCCP Act leaves it up to the licensee to determine how they will treat JobKeeper and JobSeeker in their unsuitability assessments.

In conclusion, ASIC's loss of appeal against Westpac confirms that banks have a degree of flexibility when performing an unsuitability assessment. Therefore, credit providers need to focus on whether consumers are able to comply with financial obligations as proposed in the credit contract or whether consumers would be able to comply with financial obligations in regard to substantial hardship, but are left with considerable discretion to determine what information they will use in making that assessment and how.

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Footnotes

1. *Australian Securities and Investments Commission (ASIC) v Westpac Banking Corp (Liability Trial)* (2019) 139 ACSR 25; [2019] FCA 1244; BC201907218 per Perram J.
2. *Australian Securities and Investments Commission (ASIC) v Westpac Banking Corp* [2020] FCAFC 111; BC202005844 per Middleton, Gleeson and Lee JJ.
3. *Australian Securities and Investments Commission (ASIC) v Westpac Banking Corp* (2018) 132 ACSR 230; [2018] FCA 1733; BC201810662 per Perram J.
4. A Beatty and G Papdi "Australian Securities and Investments Commission v Westpac Banking Corp (Liability Trial)" (2019) 18(8) *FSN* 107.

5. Above n 2, at [77]–[82], [87] and [164].
6. Above n 2, at [139]–[141] and [167]–[172].
7. Above n 2, at [154]–[160] and [175].
8. Above n 2, at [142] and [154].
9. Above n 2, at [113].
10. Above n 2, at [120].
11. Above n 2, at [121].
12. Above n 2, at [175].
13. Above n 2, at [170]–[171].
14. Above n 2, at [172].
15. Above n 2, at [169] and [174].
16. Above n 2, at [62].
17. Above n 2, at [63].
18. Above n 2, at [3].

ASIC's product intervention power following Regulatory Guide 272 and Cigno v ASIC: the beginning of broader intervention?

***Matthew Daley**, **Vanessa Pallone**, **Nick Killalea** and **Zachariah Burridge** CLAYTON UTZ*

Almost a year after first seeking industry consultation, the Australian Securities and Investments Commission (ASIC) has released *Regulatory Guide 272: Product intervention power*[1] (RG 272) which contains guidance on the proposed use of ASIC's new product intervention power.

The origins of the product intervention power go back as far as the 2014 *Financial System Inquiry Final Report*, which recommended that ASIC be granted a "proactive product intervention power".[2] This was later supported by the Financial Services Royal Commission, and on 5 April 2019, the power was made official upon the assent of the Treasury Laws Amendment (Design and Distribution Obligations and Product Intervention Powers) Act 2019 (Cth). These intervention powers are similar to those used by European Securities and Markets Authority (ESMA), the UK Financial Conduct Authority (FCA) and the Consumer Financial Protection Bureau in the US and mean that ASIC no longer has to rely upon legislative reform alone to address gaps in the current law.

Regulatory Guide 272

In RG 272, ASIC states that the product intervention power enables it to take a more proactive approach to regulating the market and reducing the risk of significant consumer detriment. This power represents a fundamental shift away from ASIC's previous reliance predominantly on disclosure to drive good consumer outcomes, which ASIC itself has recognised is insufficient as a consumer protection mechanism.

Scope of the power

ASIC will make a product intervention order if it is satisfied that a product (or class of products) has resulted, will result or is likely to result in significant consumer detriment.

This power can be exercised irrespective of whether there has been a breach of the law and therefore could be issued even where a person has complied with the disclosure requirements relating to financial products in the Corporations Act 2001 (Cth).

There are two types of intervention orders that ASIC can make under the power:

1) an individual product intervention order (which applies to a specified person or persons in relation to a product and is not a legislative instrument)
2) a market-wide product intervention order (which applies to a person, in relation to a class of products and is a legislative instrument)

ASIC has indicated that it would be more likely to intervene on an individual basis if the problem is specific to a particular entity or person. Meanwhile, it is more likely to make a market-wide product intervention order when it is seeking to address a practice that is relatively widespread, or if not widespread at that point of time, one that could be adopted by others.

This was the case when ASIC issued its first product intervention order to ban a model of lending used in the short-term credit industry. In 2014, ASIC had been unsuccessful in civil proceedings against two payday lenders, Teleloans Pty Ltd and Finance & Loans Direct Pty Ltd, regarding the use of their short-term lending model. Although these lenders eventually ceased operating their model, other entities began adopting this same model in their place. Therefore, in September 2019, ASIC implemented its first market-wide product intervention order to prevent other operators from adopting the model. This was eventually challenged by one operator in the case of *Cigno Pty Ltd v Australian Securities and Investments Commission*[3] (*Cigno v ASIC*), which is discussed later in this article.

What kind of orders can be made?

RG 272 provides a number of examples of the kinds of interventions ASIC could make in relation to a product (or class of products). These include:

- orders banning products in their entirety
- orders banning certain features of products or orders requiring that certain features can only be made available under certain circumstances

- orders requiring improvements to products before they are issued
- orders requiring amendments or restrictions to the marketing, promotion or disclosure material relating to products

An order might also have multiple elements, such as an order requiring that marketing material for a product be amended, or that the product can only be offered to particular classes of consumers.

There are limitations to the types of orders ASIC can make too. For example, ASIC may only intervene prospectively and therefore orders can only apply to products that are issued or sold after the date of the order. An order can also not impose requirements in relation to a person's remuneration, other than so much of the remuneration that is conditional on the achievement of objectives directly related to the product. However, ASIC has indicated that this latter limitation does not prevent it from intervening in relation to remuneration that is linked to the distribution of a product.

When will ASIC use the power?

As noted above, ASIC can make a product intervention order if it is satisfied that a product (or class of products) has resulted, will result or is likely to result in *significant consumer detriment*. In its previous response to the consultation on RG 272, ASIC indicated that it would only provide high-level guidance on when and how ASIC might use the power and did not propose to set benchmarks or thresholds so that the power would remain broad and flexible.

As a result, whether significant consumer detriment has occurred will be dependent on the circumstances of each case. RG 272 provides a number of examples where significant consumer detriment could arise. These include where:

- a product has inherent design features
- a product is issued that is not fit for purpose
- the sales and marketing techniques relating to a product prioritise commercial interests over consumer interests or
- the key features of a product are shrouded, such as fees

How is an order made?

Prior to making an order, ASIC will consult with persons who are reasonably likely to be affected by the order with the aim of this consultation being to seek feedback on its proposal to intervene. ASIC has indicated that it will invite broad feedback, but that it expects submissions to be supported with evidence and data.

A consultation document will usually be published on ASIC's website which will contain the proposed product intervention order or a description of the content of the proposed order and will invite the public to comment. The time provided for responding to the consultation will vary depending on the circumstances of the significant consumer detriment.

In describing the significant consumer detriment at consultation, ASIC may refer to:

- the nature of the product (or class of products) and its distribution and
- the circumstances of the significant consumer detriment, including:
  - — whether the detriment has already occurred
  - — the nature and extent of the detriment, including any actual or potential losses to consumers and
  - — the impact that the detriment has had or will likely have on consumers.

Once a decision to make a public intervention order has been made, ASIC will then publish the product intervention order on its website, together with a notice that:

- describes the significant consumer detriment that has resulted, will result or is likely to result from the product (or class of products) to which the order relates
- sets out why the order is an appropriate way of reducing the significant consumer detriment
- describe the consultation that ASIC undertook in relation to the order and
- if the order comes into force after the notice is published, the day the order will come into force.

Individual product intervention orders, on the other hand, must be served on any person to whom ASIC considers the order applies.

A product intervention order can be made for an initial period of up to 18 months. Following this initial period, an order can only be extended after receiving approval from the Minister.

Aggrieved individuals who are subject to an individual product intervention order have the right to complain to the Commonwealth Ombudsman or apply to the Administrative Appeals Tribunal for a merits review of the decision. However, a merits review is not available for market-wide product intervention orders since they are made by legislative instrument and are therefore subject to parliamentary oversight. Alternatively, an individual or firm may have a right to seek judicial review of a decision made by ASIC under the Administrative Decisions (Judicial Review) Act 1977 (Cth), as occurred in the recent case of *Cigno v ASIC*.

Cigno v ASIC

Prior to the release of RG 272, the Federal Court of Australia considered ASIC's first and only use of the product intervention power to date in the case of *Cigno v ASIC*.

Cigno Pty Ltd (Cigno), along with Gold-Silver Standard Finance Pty Ltd (GSSF), operated a short-term lending model under which Cigno provided services to customers to access GSSF's short term credit facilities under collateral contracts. The short-term lending model in question was said to operate the following way:

1. A short term credit provider, in this case GSSF, offered short term credit to consumers for small amounts (usually up to $1000) with the application process taking up to 2 weeks.
2. An associate of the short-term credit provider, Cigno, offered collateral services under a separate agreement to "fast track" the application in the event that the consumer wanted money immediately. The fees charged for this collateral service were very high relative to the amount borrowed.
3. The money was required to be repaid within 62 days and sometimes a shorter period of time, which increased the risk of default given that repayments were based on the term of the credit.

A case study contained in ASIC's *Consultation Paper 316: Using the product intervention power: Short term credit* (CP 316),[4] which was issued as part of the process of considering whether to make the intervention order, noted that a consumer which obtained short term credit through Cigno became liable to pay $1189 on an original credit amount of $120, or 990% more than they initially borrowed.

Following the consultation period, ASIC issued a market-wide product intervention order which had the effect of preventing GSSF and Cigno from providing their short-term lending model. Cigno therefore sought judicial review of the product intervention order.

The Federal Court's decision

The first argument raised by Cigno was that ASIC hadn't formed the requisite state of satisfaction before making the product intervention order because it was wrongly focused on the detriment said to have been caused by the short-term lending model, as opposed to the detriment caused by the financial product itself. Cigno contended that the indirect nature of their business model was not up for consideration, and so ASIC had applied the scope of "financial product" too broadly.

His Honour Justice Stewart held that Cigno's approach was too narrow, and that a significant detriment may be caused by the financial product directly or indirectly, with his Honour stating: "The causal requirement is satisfied if the detriment would not have occurred but for the financial product or the class of financial products being made available in those circumstances."[5]

His Honour then went on to find that ASIC had in fact reached the requisite state of satisfaction before issuing the product intervention order since it had sufficiently identified the class of financial product and the significant detriment caused by the circumstances of the class of financial product being made available to retail clients.

Cigno also submitted that ASIC failed to reach the requisite state of satisfaction with respect to a "class of financial products", since it had only considered the particular financial product provided by Cigno and GSSF.

His Honour also dismissed this argument, noting there was nothing in the word "class" that required there to be more than one product (or provider of a product). His Honour noted that it was also apparent that the object of the product intervention power was to provide ASIC with powers that could be used proactively to reduce the risk of significant detriment to retail clients resulting from financial products. Therefore, there didn't even have to be the existence of any product, let alone more than one, for the power to be exercised.

Future considerations

The Cigno case is subject to an appeal, which will determine whether the product intervention power will continue to receive such a broad interpretation.

In the meantime, ASIC continues to single out Cigno in its publications, this time for exploiting another credit lending model. In July of this year ASIC released *Consultation Paper 330: Using the product intervention power: Continuing credit contracts* (CP 330),[6] which seeks feedback on a class of continuing credit contracts which have resulted in significant detriment to retail clients. Similar to CP 316, CP 330 identifies Cigno, along with BHF Solutions Pty Ltd, as providers and facilitators of these types of contracts and contains several case studies analysing the detriment caused to retail clients by their business model. One of these case studies notes that a client, who was a single mother receiving Centrelink payments, was required to repay 480% of her initial loan amount of $150.

We also await ASIC's response on two other consultations in respect of its proposed use of its product intervention powers. In August 2019, ASIC released *Consultation Paper 322: Product Intervention: OTC binary options and CFDs* (CP 322),[7] which sets out ASIC's proposal to issue a market-wide product intervention order in relation to the issue and distribution of over-the-counter (OTC) binary products and contracts for difference (CFDs) to retail clients. CP 322 is the first example of ASIC taking steps to make a market-wide product intervention order in respect of investment products and is likely to result in banning the issue and distribution of OTC binary options to retail clients given ASIC's views that these types of products are akin to gambling.

This was followed in October 2019 with the release of *Consultation Paper 324: Product intervention: The sale of add-on financial products through caryard intermediaries* (CP 324),[8] which sought views on whether or not a deferred sales model should be introduced for the sale of add-on financial products through caryard intermediaries.

It's possible that ASIC will hold off on issuing these responses until the Full Federal Court hands down its decision in the *Cigno v ASIC* appeal. In any event, the release of RG 272, and the more recent release of CP 330, confirms that ASIC intends to use its product intervention power broadly. We might also see ASIC using a market-wide product intervention order in favour of an individual product intervention order given the Federal Court has indicated that a market-wide order could be used even when there was no product in existence.

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Footnotes

1. ASIC *Regulatory Guide RG 272: Product intervention power* (17 June 2020).
2. Australian Government Treasury *Financial System Inquiry Final Report* (November 2014) p 206.
3. *Cigno Pty Ltd v Australian Securities and Investments Commission* [2020] FCA 479; BC202002876.
4. ASIC *Consultation Paper CP 316: Using the product intervention power: Short term credit* (9 July 2019).
5. Above n 3, at [42].
6. ASIC *Consultation Paper CP 330: Using the product intervention power: Continuing credit contracts* (9 July 2020).
7. ASIC *Consultation Paper CP 322: Product Intervention: OTC binary options and CFDs* (22 August 2019).
8. ASIC *Consultation Paper CP 324: Product intervention: The sale of add-on financial products through caryard intermediaries* (1 October 2019).

A sea change concerning CCI products sees significant remediation for wronged consumers

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On 13 May 2020, ASIC commenced the third tranche in a three-pronged approach to consumer credit insurance (CCI) products offered by financial lenders. The third tranche sees $160 million in remediation for customers who were sold CCI since 2012. In the first tranche, Australian Securities and Investments Commission (ASIC) published Report 622 finding that the design, sale and offering of CCI had consistently failed consumers. In the second tranche, ASIC conducted and published enforcement investigations against lenders who offered CCI. The regulatory body's hard and fast approach to CCI products indicates that lenders who continue to offer CCI should be mindful of their sales practices and the eligibility of their customers.

CCI products

CCI provides insurance for consumers unable to meet their minimum loan repayments due to unemployment, sickness or injury or to pay the outstanding loan balance upon death. A legislative definition can be found under reg 7.1.15 of the Corporations Regulations 2001 (Cth), being insurance cover for:

(i) the death of the insured person; or
(ii) the insured person contracting a sickness or disease; or
(iii) the insured person sustaining an injury; or
(iv) the insured person becoming unemployed.

ASIC first published REP 256 *Consumer credit insurance: A review of sales practices by authorised deposit-taking institutions*[1] (REP 256) in 2011. It recommended 10 methods to raise industry standards and lessen the harm felt by CCI products that had been incorrectly sold to consumers.

ASIC's concerns were confirmed by the review when they found CCI products were being sold:[2]

- to consumers without their knowledge
- through using unfair tactics to coerce consumers to purchase CCI
- by misleading and making incorrect representations while making the sale and
- deficiencies present in the scripts used to sell CCI

Due to these harms and concerns, ASIC launched an examination into how CCI was being sold in Australia.

Tranche 1 — ASIC's Report 622

After REP 256 was published, ASIC released a follow-up REP 622 *Consumer credit insurance: Poor value products and harmful sales practices*[3] (REP 622) in 2019 after conducting a review of the sale of CCI by 11 major banks and lenders.[4] In publishing REP 622, ASIC considered data from 2011 to 2018.

Through their investigation, ASIC found that the design and sale of CCI had consistently failed consumers as:

- CCI is extremely poor value for money. For every CCI sold with a credit card, consumers only received 11 cents in claims for every dollar paid in premiums. Only 19 cents was recovered in claims for every premium dollar which consumers paid for CCI products sold by lenders
- consumers were being incorrectly charged for CCI including ongoing CCI premiums when they no longer had a loan;
- many lenders did not have consumer-focused processes to help consumers in hardship make a hardship claim under their CCI policy and
- CCI sales practices were causing consumers harm, as:
  - — consumers were sold CCI despite being ineligible to claim under their policy
  - — telephone sales staff used high-pressure selling and other unfair sales practices when selling CCI and
  - — consumers were given non-compliant personal advice to purchase unsuitable policies[5]

ASIC found that the CCI was being sold to customers who were ineligible and unlikely to benefit from the coverage. This was due to the customer not meeting the employment eligibility criteria.

After ASIC released REP 622, and the harms caused by poor product design and sale were revealed, all lenders were expected to incorporate a 4-day deferred sales model for all CCI products and many lenders stopped selling CCI altogether. The deferred sales model would promote consumer protections so they will be provided ample time to assess the complexities of CCI, its value and whether it would meet their needs. It would also alleviate the pressure on consumers who believe they need to purchase CCI to have their loan approved.

Tranche 2 — enforcement investigations

Due to their findings in REP 622, ASIC commenced enforcement investigations into several entities that were involved in the selling of CCI products to consumers.

After the findings were published, lenders such as Allianz took proactive action and established their own remediation program. In accordance with their program, Allianz announced they would refund over $8 million in CCI premiums and fees including interest to over 15,000 consumers.

Other lenders had court proceedings brought against them. For example, Slater and Gordon brought a class action proceeding against National Australia bank (NAB), alleging NAB had engaged in unconscionable conduct by selling CCI to customers who were ineligible or unlikely to benefit from the insurance and had engaged in misleading and deceptive behaviour when selling the CCI to customers. In November 2019, it was announced that a settlement figure of $49.5 million was agreed upon to compensate thousands of consumers.

Tranche 3 — remediation

Nearly a year after REP 622 was published, on 13 May 2020, ASIC announced over $160 million in compensation for consumers who were sold "junk"[6] insurance. ASIC has outlined the situations and compensation payable as below.[7]

Applicable situation	Compensation payable
Lenders sold consumers CCI policies although they were ineligible or unlikely to benefit or need the insurance	$105.8 million paid to over 244,000 customers
Lenders used unfair sales tactics such as pressure selling and making false representations	$37.34 million paid to over 48,000 customers
Consumers who were incorrectly charged for CCI or their claims were incorrectly declined	$13.9 million paid to over 57,000 customers
Lenders had inadequate consumer-focused processes to assist consumers in hardship or trustees of deceased estates who had an existing CCI policy to claim	$5.06 million paid to over 1000 customers
Consumers received no or very little value from the product	$5.77 million paid to over 84,000 customers

Although this was ASIC's intended "final" tranche, ASIC has announced it will continue to monitor, collect and publish how CCI products provide value to consumers, to ensure there is ongoing public transparency. ASIC also announced in August 2019 their intent to publish a follow-up review within 2 years that will reassess how CCI is being sold.[8]

Providing CCI — practical tips for providing compliant insurance

ASIC announced in their REP 622 that they have certain expectations of lenders and insurers who sell, design and price CCI and handle customer claims. If lenders and insurers are incapable of abiding by ASIC's guidelines, they should cease selling CCI or ASIC will consider taking enforcement action or otherwise intervene by utilising their product intervention power.

There are four main areas which should be carefully assessed by lenders and insurers to ensure their CCI offering abides by ASIC's expectations. These are outlined below.

A. Product design and value

Lenders should sell CCI unbundled to allow customers to select the specific insurance product they require. Furthermore, lenders should assess the product design and value of CCI, ensuring the product accurately reflects the consumer value and includes the claims ratios of new and existing products. CCI benefits should also reflect the actual needs of consumers rather than implementing arbitrary limits.

B. Compliance and monitoring

CCI products should be sold in accordance with ASIC's standards and 10 recommendations identified in REP 256. Upon review, if these standards are currently not being met then lenders should conduct a review to assess any harm felt by consumers and ensure the affected consumers are identified and remediated in a timely manner.

C. Sales practices

If there are any outbound unsolicited phone sales of CCI, they should cease.

When making informed sales, there should be stringent filters applied to ensure only eligible consumers are being contacted about CCI. To confirm eligibility, lenders should be proactive in obtaining clear consent before discussing the sale of CCI.

Furthermore, "knock-out" questions should be implemented in sale scripts to assist in differentiating eligible from ineligible customers. Lenders should also incorporate a 4-day deferred sales model for all CCI products, commencing the day after the consumer is advised their loan is approved.

D. Post-sales conduct

Lenders and insurers should not charge premiums for CCI where the primary benefits are no longer available to them under the policy. Lenders should maintain clear communication with consumers about their policy to provide annual updates about the price, limits and exclusions of their policy and remind them to lodge a claim if a claimable event had occurred within 12 months. Every 2 years, lenders and insurers should contact consumers with a CCI product about whether they would like to continue with their cover.

If a consumer applies to vary their loan contract as a result of financial hardship, lenders should notify the insurer for an assessment of their claim details. Insurers should also record details pertaining to withdrawn claims and claims which did not proceed.

In conclusion, if lenders continue to offer CCI, they should take great caution to ensure the eligibility criteria is met by potential consumers and consideration is given to the customer's best interests. Furthermore, the sale practices concerning CCI should be assessed to make sure they are "fair" and conscionable and no undue pressure is being forced onto customers.

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Footnotes

1. ASIC *Consumer credit insurance: A review of sales practices by authorised deposit-taking institutions* Report 256 (2011).
2. Above, p 5.
3. ASIC *Consumer credit insurance: Poor value products and harmful sales practices* Report 622 (2019).
4. The 11 lenders reviewed by ASIC in their investigation were Australia and New Zealand Banking Group Ltd, Australian Central Credit Union Ltd, Bank of Queensland Ltd, Bendigo and Adelaide Bank Ltd, Citigroup Pty Ltd, Commonwealth Bank of Australia — Retail Banking Services and Bankwest, Credit Union Australia Ltd, Latitude Finance Australia and Latitude Personal Finance Pty Ltd, National Australia Bank Ltd, Suncorp-Metway Ltd and Westpac Banking Corporation.
5. ASIC "19-180MR ASIC finds unacceptable sales practices, poor product design and significant remediation costs in CCI sold by major banks and lenders" media release (11 July 2019).
6. ASIC "20-115MR ASIC secures over $160 million in remediation for junk consumer credit insurance" media release (13 May 2020).
7. Above.
8. Sean Hughes, Speech, *Banking in the Spotlight*, 36th Annual Conference of the Banking and Financial Services Law Association, Gold Coast, Queensland, 30 August 2019.

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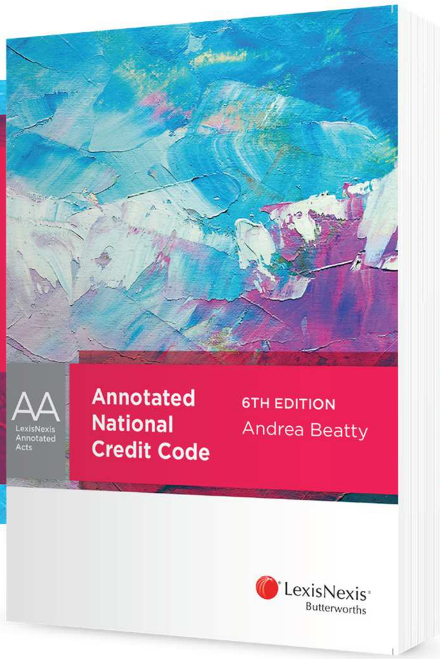

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