14 August 2017

By email: lenderrules@treasury.gov.au

The Manager
Banking, Insurance and Capital Markets Unit
Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Sir/Madam,

New APRA powers to address financial stability risks - non-ADI lender rules

The Consumer Action Law Centre (**Consumer Action**) and CHOICE are pleased to comment on the draft *Treasury Laws Amendment (Non-ADI Lender Rules) Bill 2017* (**the draft Bill**).

We support the proposal to provide the Australian Prudential Regulation Authority (**APRA**) with new powers in respect of the provision of credit by entities that are not authorised deposit-taking institutions (**non-ADI lenders**). We understand that these new powers would be applicable to non-ADI lenders with loan books valued at more than $50 million. We agree that enabling APRA to monitor non-ADI lending practices would enhance the overall stability of the financial system, given the potential risks to financial stability that currently exist in the mortgage and personal finance markets.

Our responses to the draft Bill are detailed more fully below.

About the contributors

Consumer Action Law Centre

Consumer Action is an independent, not-for profit consumer organisation based in Melbourne. We work to advance fairness in consumer markets, particularly for disadvantaged and vulnerable consumers, through financial counselling, legal advice and representation, and policy work and campaigns. Delivering assistance services to Victorian consumers, we have a national reach through our deep expertise in consumer law and policy and direct knowledge of the consumer experience of modern markets.

CHOICE

Set up by consumers for consumers, CHOICE is the consumer advocate that provides Australians with information and advice, free from commercial bias. By mobilising Australia's largest and loudest consumer movement, CHOICE fights to hold industry and government accountable and achieve real change on the issues that matter most.

APRA powers for non-ADI lenders

Under the current regulatory system, only ADIs are subject to APRA's prudential requirements and ongoing supervision. In our view, it is critical that the Australia's prudential regulation builds trust and confidence in the financial sector as a whole, which requires monitoring and regulation of both ADIs and non-ADI lenders. We therefore support the proposal to provide APRA with new powers to make rules with respect to lending finance by non-ADI lenders.

There has been a surge in non-bank lending in recent years.[1] This has occurred in the context of record-breaking Australian household debt levels. Australian households owed debt in the March quarter equal to 190 per cent of their yearly disposable income—a new all-time high.[2] In the 2016/17 financial year over 160,000 calls were made to the National Debt Helpline. This is an 11% increase on the previous year. Calls have increased year on year since the National Debt Helpline started.[3] This is no surprise given that the Reserve Bank of Australia (**RBA**) recently reported that one-third of Australian borrowers have not built up a repayment buffer, or are less than one month ahead on their home loan repayments.

The RBA warned of the risks our household debt levels pose to Australia's financial security, saying "rising indebtedness can make households more vulnerable to potential income declines and higher interest rates… a highly indebted household sector is likely to be more sensitive to declines in income and wealth and may respond by reducing consumption sharply."[4] The

[1] Michael Roddan, The Australia, *APRA has eyes on non-bank lenders,* 10 April 2017, available at: http://www.theaustralian.com.au/business/financial-services/apra-has-eyes-on-nonbank-lenders/news-story/456bc394117341f2cccd5408dfa3ebda; Clancy Yeates and Shaun Drummond, The Sydney Morning Herald, *Non-banks set to boom thanks to APRA crackdown on property investors,* 31 July 2015, available at: http://www.smh.com.au/business/banking-and-finance/nonbanks-set-to-boom-thanks-to-apra-crackdown-on-property-investors-20150731-giowoi.html; David Chin, BasisPoint, *The Suprrising rise of non-bank lending in the Australian property market,* 30 August 2016, available at: http://basispoint.com.au/surprising-rise-non-bank-lending-australian-property-market/.

[2] Reserve Bank of Australia, *Statistical Tables,* accessed 14 August 2017, available at: http://www.rba.gov.au/statistics/tables/ as quoted in Jackson Stiles, The New Daily, *Australian household debt breaks new records,* 3 July 2017, available at: http://thenewdaily.com.au/money/finance-news/2017/07/03/australia-debt-new-records/.

[3] Financial Counselling Australia, *National Debt Helpline Annual Data Report - 2016-17 Financial Year & Fourth Quarter 2016-17*,

[4] Reserve Bank of Australia, *Financial Stability Review,* April 2017, p. 19, available at: https://www.rba.gov.au/publications/fsr/2017/apr/pdf/financial-stability-review-2017-04.pdf as quoted in Carrington

Australian Housing and Urban Research Institute (**AHURI**) also recently warned that growing household debt would pose more risks to macro-economic stability in Australia, following research undertaken on its behalf by researchers from the University of Sydney.[5] The report found that "Macroeconomic policy-makers should acknowledge the potential risks associated with high levels of household debt and rising household income-to-debt ratios", and noted the important role played by prudential regulation of the financial system in this context.

Some industry participants argue that record household debt is not a risk to system instability. It is sometimes proffered that Australians, on average, are many months ahead on their mortgage repayments.[6] These statistics, however, should not be accepted uncritically. First, they statistics provided are an average—there is other data that suggests that almost 25 percent of households are experiencing mortgage stress defined as households at risk of default in the next 12 months.[7] This amount is likely to significantly increase should interest rates rise. Second, most of the data about households being ahead in mortgage repayments appears to relate to banks. As noted above, non-bank lenders are a significant part of Australia's credit markets.

While the proportion of non-bank lending fell from the its highs due to the Global Financial Crisis, it appears that non-bank lending is increasing. Capital investors keen to make a higher return may look to non-bank lenders due to the potential for a higher return than the regulated big banks. Securitisation of mortgages is also on the rise.[8] In this context, it should be remembered that unbridled securitisation was a key contributor to the Global Financial Crisis.

In this context, it is entirely appropriate that non-ADI lending be subject to prudential requirements. The risk that Australia is headed for a 'debt disaster' can be curbed by additional regulation by APRA and the Australian Securities and Investments Commission (**ASIC**).

We agree that APRA should be provided with flexible powers to make rules in relation to non-ADI lenders. We also support the proposal that APRA be required to consult with ASIC before making any non-ADI lender rules, as there will likely be overlap between the two regulators given ASIC's responsibility for regulating responsible lending conduct.

Clarke, ABC News, *Reserve Bank warns one-third of Australian borrowers have little to no mortgage buffer,* 14 April 2017, available at: http://www.abc.net.au/news/2017-04-13/reserve-bank-financial-stability-review-april-2017/8442242.

[5] K. Atalay et. al., Australian Housing and Urban Research Institute, *Housing prices, household debt and household consumption,* June 2017, available at: https://www.ahuri.edu.au/research/final-reports/282.

[6] Michael Bennet, The Australian, *Homeowners gallop ahead on their mortgage repayments,* 30 May 2016, available at: http://www.theaustralian.com.au/business/companies/homeowners-gallop-ahead-on-their-mortgage-repayments/news-story/52e24d1d66b47a25fe916b833e0ba52d

[7] Digital Finance Analytics, *What's the correlation between mortgage stress and loan non-performance,* 22 June 2017, available at: http://www.digitalfinanceanalytics.com/blog/whats-the-correlation-between-mortgage-stress-and-loan-non-performance/.

[8] Michael Bennet, The Australia, *Non-conforming loans on the risk in banking,* 23 November 2016, available at: http://www.theaustralian.com.au/business/financial-services/nonconforming-loans-on-the-rise-in-banking/news-story/d8884f28b417612e9389871cd6f16de4.

Data collection

We support the proposal to broaden APRA's ability to gather data from non-ADI lenders under the *Financial Sector (Collection of Data) Act 2001* (**FSCODA**). We believe that APRA needs access to detailed, reliable and consistent data across its regulatory portfolio in order to properly monitor the financial stability implications of the non-ADI lender sector. We also support the new definition that will seek to capture entities who engage in material lending activity, irrespective of whether it is their primary business.

Please contact Katherine Temple on 03 9670 5088 or at katherine@consumeraction.org.au if you have any questions about this submission.

Yours sincerely

Gerard Brody
Chief Executive Officer
CONSUMER ACTION LAW CENTRE

Erin Turner
Head of Campaigns and Policy
CHOICE