Why I signed the "Save Fair Lending" Letter

Determined not to let a good crisis go to waste, the Federal Government is pushing through some ideologically, but not evidence, based policies – one of which is the jettisoning of Responsible Lending Obligations (RLOs). The proposal to remove RLOs for much of consumer lending from the relevant legislation, under the guise of supporting economic recovery, and unsurprisingly supported by the banks, has provoked widespread opposition.

That opposition is reflected in the "Save Fair Lending" letter addressed to Australian Parliamentarians and signed by over 120 community organisations and a similar number of academics, financial counsellors and other concerned, well informed, individuals.

Getting group agreement on the details in such petitions is always problematic and signatories will often have different reasons for giving support. Financial counsellors and community welfare organisations have seen first-hand the adverse consequences of irresponsible lending for their clients. Others will have been influenced by the proceedings and findings of the recent Hayne Royal Commission which, if anything, would seem to support tightening rather than abolition of RLOs.

My reasons for signing, in addition to those, reflect my consideration of the economic and social consequences of removing RLOs. I am willing to accept the arguments of lenders that RLO obligations add to their costs, and may increase the time lag involved in processing loan applications.

But how significant are those costs (and whether it is bank shareholders or borrowers who bear them), and how inconvenient are those lags is another matter. And evidence is scanty. Ultimately, good policy needs to weigh up those costs against the significant benefits of RLOs.

And the arguments advanced to warrant change should be credible – which in this case they are not.

First, RLOs are legislated, but enforced by regulations made under that legislation by ASIC. Much of the criticism of RLOs has been directed at ASIC's implementation of regulations. If that has been the problem, the obvious solution is to address the regulatory approach rather than removing RLOs from legislation.

Second, ASIC consulted widely on RLOs in 2019 and released a new guidance note (RG209) in December 2019. Following that, the "Wagyu and Shiraz" judgement effectively lowered the standard required of lenders for borrower expenditure verification. Abolishing RLOs, rather than waiting to see the effect of these changes, smacks of an ideological rather than an economic motivation.

Third, one rationale for the change is argued to be that it will increase lending. Well it may do so – but if that involves an increase in poor quality lending, that is hardly a desirable outcome. And the argument that reducing the lag time involved in loan approvals will increase lending is a bit of a card trick. If the rate of applications per week is unchanged, the rate of approvals per week will stay the same (except for a temporary blip as approvals of new applications overlap approvals already in the pipeline but involving longer lags).

Fourth, we are currently at a time when "fintech" is making loan application and processing less costly and cumbersome and reducing time lags in such processes. We have just introduced open banking, enabling easier access to and use of customer data, and fintechs are busy developing products to cost-effectively apply that data. So, if costs are the issue, why change the rules (abolishing RLOs) when a cost-reducing and time saving revolution is in progress?

Finally, the argument that APRA's oversight of bank lending practices can guard against irresponsible lending is, with all due respect to APRA, silly. APRA's mandate is to ensure the safety of the institutions it supervises. Yes, it does require lenders to assess customer repayment ability for a loan at both current and possibly higher interest rates. But it has no capacity to consider whether individual borrowers would be put into financial hardship by taking out such a loan.

One could hope that banks and other lenders have learnt important lessons from the Hayne Royal Commission process and that "responsible lending" will now be part of their genetic make-up, making RLOs redundant. Moreover, RLOs help protect vulnerable individuals from making poor borrowing choices due to low financial literacy, over-optimism, or other behavioural biases.

Why abolish a valuable safeguard in favour of operating on a wing and a prayer as seems to be the case here?

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