

26 August 2019

Phil Khoury
Independent Reviewer
Customer Owned Banking Code of Practice Review

Email: cobcop.review@crkhoury.com

Dear Mr Khoury

Customer Owned Banking Code of Practice Independent Review 2019 Report One

The Customer Owned Banking Association (COBA) welcomes the opportunity to make a submission to Report One of the Independent Review of the Customer Owned Banking Code of Practice (Report One).

COBA notes that Report One is the first report of a series of three reports that will be released by the Independent Reviewer (the Reviewer). We note that each report will focus on a different aspect of the Customer Owned Banking Code of Practice (COBCOP), explain the Reviewer's recommendations and be accompanied by an initial redraft of the relevant parts of the COBCOP.

COBA appreciates the Reviewer's emphasis in Report One that the initial drafting should be viewed as a "shorthand, convenient way" of setting out the Reviewer's content recommendations, as the initial drafting will not have been tested with stakeholders. We note that the Reviewer expects the drafting to evolve as discussions occur with stakeholders.

COBA understands that the purpose of Report One is to provide an update on the progress of the Review, an explanation of the intended process of the Review and the Reviewer's recommendations on some foundational issues for the Review.

COBA appreciates that, through the three-report process, the Review is aiming to maximise transparency to all stakeholders and provide an opportunity for participation in a timely fashion, so that stakeholders can contribute to shape the Review and the new COBCOP.

COBA strongly supports this approach (over a single end-of-Review report) and agrees with the Reviewer that this will enable progressive input from stakeholders and be a more efficient process. We consider that a key success factor to the Review is to ensure that stakeholders are provided appropriate opportunities to contribute.

This submission provides COBA's general and detailed comments on key elements of Report One, including in relation to the guiding principles, code structure, key promises, language and style and small business provisions. Our comments are set out at the **Appendix** of this submission.

COBA notes that Report Two will cover recommended changes to the detailed obligations in the COBCOP (currently Part D of the COBCOP), and that it will be accompanied by a complete initial redraft of this part of the COBCOP for testing and revision with stakeholders.

We also note that Report Three will cover recommended changes to the COBCOP administration provisions (current Part E of the COBCOP), and that Report Three will also be accompanied by a complete initial redraft of that part of the COBCOP for testing and revision with stakeholders.

COBA appreciates the range of views that have been expressed by stakeholders to date and we continue to respectfully encourage the Review to carefully consider all views raised.

We look forward to continuing to work with the Reviewer and stakeholders to progress the Review and help facilitate a smooth and efficient transition to a revised COBCOP.

If you have any questions or comments in relation to any aspect of our submission, please contact Tommy Kiang, Senior Policy Manager, on 02 8035 8442 or at tkiang@coba.asn.au.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Michael Lawrence', with a stylized flourish at the end.

MICHAEL LAWRENCE
Chief Executive Officer

A. Proposed Principles to guide the Review

COBA **supports** the Reviewer's proposed five principles to guide the Review.

B. Recommended changes to the structure of the COBCOP

COBA recognises that the Review presents an excellent opportunity to make structural changes to the COBCOP to further enhance the user-friendly nature of the COBCOP, without compromising its intent.

COBA appreciates the Reviewer emphasising that the 10 Key Promises of the COBCOP "is a significant strength of the current version and should be a feature of the revised Code".

COBA strongly agrees with this statement and would like to re-emphasise that the 10 Key Promises in the COBCOP are part of the contract with customers (i.e. the promises are part of the COBCOP).

The 10 Key Promises are not a non-binding preamble or guidance. This is a key distinguishing aspect of the COBCOP from the Australian Banking Association's (ABA) Banking Code of Practice (BCOP). While the BCOP includes "guiding principles", those principles are not part of the BCOP itself and are therefore not part of the contract with customers.

COBA **supports** the Reviewer's recommended changes to the structure of the COBCOP (**Recommendation 1**):

- a. The paragraphs of Parts A and B of the Code that explain the Code should be excised from the Code and instead form part of the covering explanatory piece by the COBA CEO.
- b. The Code should be restructured so that:
 - i. Part A of the Code sets out the obligation to comply with the Code and the key promises to customers
 - ii. Part B of the Code sets out the detailed obligations (including the specific obligations that are currently located in Parts A to C of the Code).
 - iii. Part C of the Code sets out the Code administration provisions.
 - iv. An Appendix sets out the definitions.
- c. The entire Code, including the key promises, should be enforceable by customers as provisions incorporated in the customer contract with the customer owned bank.

COBA notes that this recommendation seeks to streamline the structure of the COBCOP, further strengthen the message that all of the COBCOP is enforceable and address the Reviewer's observation that there is some repetition between different passages of the COBCOP.

C. Recommended changes to the Key Promises

COBA **broadly supports** the Reviewer's recommendation that the COBCOP's current 10 Key Promises should be replaced with new key promises that are based on the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (the Royal Commission) six norms of conduct (**Recommendation 2**):

The existing Key Promises should be replaced by new Key Promises along the following lines:

1. Customers are our owners and the reason we exist; we will deliver banking services in the interests of all of our customers.
2. We will obey the law.
3. We will not mislead or deceive.
4. We will act fairly.
5. We will provide products and services that are fit for general purpose.
6. We will deliver services with reasonable care and skill.

7. If we provide advice to you, we will act in your best interests.
8. We will contribute to the community in which we operate.

Specific obligations currently in Part C should be moved so as to become part of the detailed obligations (currently Part D but our proposed new Part B of the Code).

COBA notes the Reviewer's emphasis that the Royal Commission proposed the six norms to cover a broad range of environments within financial services. We particularly appreciate that the Reviewer is also recommending some changes and additions to the norms of conduct to allow for the particular context of customer owned banks.

COBA recognises that the Review is taking place at a time of heightened scrutiny of the culture and accountability of financial institutions, particularly from the Royal Commission. However, as the Reviewer is aware, no customer owned banking institutions were called to appear before the Royal Commission, and none were subject to criticism by the Royal Commission.

As we explained in our earlier submission, eight of COBA's larger members were asked by the Royal Commission at an early stage to provide information concerning instances of misconduct or conduct falling below community standards and expectations. The responses explained the natural customer focus of our model and indicated that the level of conduct risk in our sector is relatively low. Importantly, the responses emphasised our sector's culture of response and remediation when problems occur.

COBA is working closely with its members to carefully consider the potential practical implications of adopting Recommendation 2. In the interim, we would like to provide the following preliminary feedback on the Reviewer's recommended new key promises 1 and 7.

- Recommended **Key Promise 1** "Customers are our owners and the reason we exist; we will deliver banking services in the interests of all of our customers."
 - COBA strongly supports the intent of this recommendation. We had suggested in our 18 April submission¹ to the Review Issues Paper a new Number 1 Key Promise that is focussed on the customer owned banking model and purpose:
 - "Promise 1: We will always recognise that our customers are our owners and the reason we exist

Our customers are our owners and we exist to meet their needs. Our customers, as our owners, can choose to have a say in how we operate. We are a mutual company and that means each member of the company has no more than one vote at a meeting of the company."
 - Respectfully however, COBA's preference continues to be the new Number 1 Key Promise that we suggested in our submission, as we consider that our suggestion more strongly expresses the customer owned banking model and purpose.
- Recommended **Key Promise 7** "If we provide advice to you, we will act in your best interests."
 - COBA is concerned that this promise may blur the lines between the provision of general and personal advice. Subsection 766B(3) of the *Corporations Act 2001* defines personal advice as advice where "the provider of the advice has considered one or more of the person's objectives, financial situation and needs" or where "a reasonable person might expect the provider to have considered one or more of those matters".
 - The advice provided by most COBCOP subscribers would be considered as general advice (i.e. advice that does not take into account a person's objectives, financial situation or needs).
 - However, if COBCOP subscribers committed to providing advice in a customer's 'best interest', this advice would necessarily have to take into account the customer's personal objectives, financial situation or needs and therefore would no longer be considered as general advice.

¹ COBA submission to the Customer Owned Banking Code of Practice 2019 Independent Review, 18 April 2019.

- In this respect, this recommended key promise, as drafted, may inadvertently expose COBCOP subscribers to significant legal risk. COBA would suggest rephrasing the recommended Key Promise 7 to remove any legal uncertainty. If this is not possible, we would suggest omitting this recommended key promise.

D. Language and style

COBA **notes** the Reviewer's recommended changes to the language and style of the COBCOP (**Recommendation 3**):

The Code should be drafted so as:

- a) to add to the law rather than simply restate the law; and
- b) to focus on commitments by customer owned banks, rather than placing an onus on customers to act before the bank obligation applies.

COBA's view is that the COBCOP must continue to be customer facing, easy to understand, brief and succinct. This is a strength of the current COBCOP and COBA supports the Reviewer's aim to see a revised COBCOP that continues to be a plain language document that can be readily understood by both customer owned banking institutions and their customers.

E. Small business provisions

COBA appreciates the Reviewer's recommendation of a possible approach to have small business lending explicitly recognised in the revised COBCOP.

While the customer owned banking sector's involvement in small business lending is limited compared to its residential lending exposure, COBA's view is that there needs to be a degree of explicit recognition in the future COBCOP of the sector's involvement in small business lending.

COBCOP subscribers and their small business lending customers stand to benefit from a new COBCOP that shifts away from its current conflation of responsible lending in the consumer and small business contexts.

COBA **broadly supports** the Reviewer's recommended approach to incorporating a new small business lending provision in the revised COBCOP (**Recommendation 4**):

- a) The Code should define "Small Business" so as to include businesses or groups of fewer than 100 FTE employees, with loans of up to \$5 million.
- b) A new Small Business lending provision should be included that incorporates the key protections now considered to be good practice (consistent with those in the ABA Banking Code of Practice but expressed more succinctly).

COBA notes that the Reviewer's recommended definition adopts the definition provided in Recommendation 1.10 of the Royal Commission², being "any business or group employing fewer than 100 full-time equivalent employees, where the loan applied for is less than \$5 million".

Importantly, it would appear that the \$5 million cap is on a *per loan* basis, as opposed to being based on the total value of loans outstanding for a business. In this respect, adopting this definition would mean that the recommended small business provisions would also apply to a business with multiple individual loans of less than \$5 million, as there does not appear to be a cap on the number of loans.

Given the potentially broad scope of the Reviewer's proposed small business definition, COBA is working closely with its members to carefully consider the potential practical implications of adopting this definition and determine whether this is feasible.

² Royal Commission Recommendation 1.10 — Definition of 'small business': "The ABA should amend the definition of 'small business' in the Banking Code so that the Code applies to any business or group employing fewer than 100 full-time equivalent employees, where the loan applied for is less than \$5 million.