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1 Introduction

1.1 Summary Information

Objective of these Guidelines:
The objective of these Guidelines is to outline ME’s responsible lending obligations and provide a framework for how we expect our accredited mortgage brokers to assist us to comply with these obligations.

This document should be read together with the Applicable Legislation/Regulatory Guidelines and Related Document(s) listed below.

Version:
2020.01

Application:
These Guidelines apply to all of ME’s accredited mortgage brokers.
These Guidelines form part of the “Standard Practices” as defined in the ME Retail Lending Aggregator Engagement Agreement.

Confidentiality:
This document should be treated as confidential by all of ME’s accredited mortgage brokers (and their staff) to whom the document is distributed. It should not be disclosed to other persons without the prior written consent of ME.

Applicable Legislation/Regulatory Guidelines:
- National Customer Credit Protection Act (Cwth) 2009
- ASIC Regulatory Guide RG209 – Credit Licensing: Responsible Lending Conduct
- APRA Prudential Practice Guide APG223 – Residential Mortgage Lending

Related Document(s):
- Credit Policy Home Loans
2 Definitions
The following terms (listed in alphabetical order) are utilised throughout these Guidelines:

- ‘ASIC’ means the Australian Securities and Investments Commission
- ‘Customer’ means any borrower. It does not include guarantors
- ‘ME’, ‘we’, ‘us’ or ‘our’ refers to Members Equity Bank Limited
- ‘NCCP Act’ means the National Customer Credit Protection Act (Cwth) 2009
- ‘RG 209’ means ASIC Regulatory Guide RG209: Credit Licensing: Responsible Lending Conduct
- ‘You’ means all ME accredited mortgage brokers

3 Overview of Responsible Lending Obligations
3.1 The responsible lending obligations
The primary outcome sought by the responsible lending obligations is to minimise the risk that customers:

- Enter into, or are encouraged to enter into or remain in, an unsuitable credit product; or
- Increase the credit limit of an existing credit product to a limit that is unsuitable.

3.2 Approach to compliance
ME will have regard to the following high-level principles when executing our responsible lending obligations:

- What the responsible lending obligations are intended to achieve and the customer harm these obligations are intended to address;
- The circumstances of the individual customer we are dealing with; and
- Whether the credit product involves a higher risk of harm to the individual customer if it is unsuitable.
3.3 When do responsible lending obligations apply?

The credit products regulated by the NCCP Act and covered by this policy are the ME home loan, credit card and personal loan products.

The NCCP Act also requires that ME conduct a responsible lending assessment before:

- Entering into a credit contract;
- Making an unconditional representation to a customer that they are eligible to enter a credit contract (e.g. by granting an unconditional loan approval);
- Providing a principal increase (e.g. a home loan top up; credit card limit increase); or
- Making an unconditional representation to a customer that they are eligible for a principal increase.

3.4 What is a responsible lending assessment?

Responsible lending is not about undertaking a credit assessment. It is about making reasonable enquiries about the customers’ requirements and objectives and financial situation; verifying this information and assessing whether:

- The loan meets the customer’s requirements and objectives; and
- The customer can repay it without "substantial hardship."

ME needs to ultimately determine that the loan being applied for is “not unsuitable” for that customer. Therefore, it’s not about assessing the risk to the bank of granting the loan – rather it’s about the risk to the customer.

As a credit licensee ME must decide how we will meet our responsible lending obligations. The NCCP Act is not prescriptive in this regard. Therefore, this policy sets out the requirements for our compliance.
3.5 What kind of enquiries and verification steps are ‘reasonable’?

The obligation is to make enquiries about the customer we are dealing with, and to verify information about their financial situation to a ‘reasonable’ standard. What we need to do to meet these obligations in relation to a particular customer will vary depending on a range of different circumstances relevant to that customer’s particular application. It may also vary depending upon the type of product being sought (e.g. a larger longer term home loan application will require more extensive enquiries compared to more basic shorter term personal loan). It can also vary according to the amount and type of credit being applied for.

For example, more extensive enquiries are likely necessary in the following circumstances:

- Where the potential negative impact on the customer is likely to be relatively serious if the loan is unsuitable (e.g. if the size of a loan is large relative to the customer’s capacity to repay the loan). This is because even a small loan can cause financial difficulties for a customer on a low income;
- The customer has limited capacity to understand the credit contract, and their payment obligations under that contract (e.g. they have limited English speaking skills);
- There is an apparent mismatch between the customer’s stated requirements and objectives and the product being considered by them (e.g. they say they want the lowest possible interest rate but have applied for a fully featured home loan);
- The customer will obtain no or limited benefit from the credit product (e.g. a loan to purchase an asset in the name of another person), or there are other indicators the customer may be the subject of financial abuse (e.g. the customer seems to be acting at the direction of a third party).

3.6 Responsible Lending flowchart

The responsible lending steps can be shown diagrammatically as follows:

- Enquiries → Verification → Further enquiries about inconsistencies (if any) → Final assessment
4 Making reasonable enquiries – the ‘Fact Find’

4.1 What is required

The first step in a responsible lending assessment is to make reasonable enquiries about the customer’s:

(a) Requirements and objectives; and

(b) Financial situation.

Both aspects are equally important.

These enquiries are to be made by you on our behalf and documented by way of our credit product application forms and processes.

4.2 Our Fact Find

New credit applications

To meet the obligation to collect reasonable information about the customer's requirements and objectives, ME’s product Credit Policies detail the minimum information that must be collected from a customer in order for their application to be considered.

Credit limit increase applications

If a customer makes an application to borrow additional funds that application is treated largely the same as an application for a new credit contract in terms of:

(a) The fact find (but noting that some enquiries have been ‘scaled down’ given the nature of a credit limit increase application); and

(b) ME’s corresponding assessment and verification.

Changes advised after submission of the application

If there are changes advised by the customer to any responses to the ‘fact find’ after submission of the application (e.g. a change to the product selected, repayment type, loan term or product feature selection), you must have a conversation with the customer in relation to why the changes are requested.

All conversations with the customer must be documented in writing in a new Responsible Lending Obligations form in the case of home loans and in system notes for credit cards. We may ask you to request additional information and/or documentation from the customer at our discretion in order for ME to determine the credit contract is not unsuitable for the customer given the advised changes.
4.3 Reasonable enquiries into the customer’s requirements and objectives

Specific enquiries must be made into the customer’s requirements and objectives in applying for credit. The customer’s requirements relate to the features of the credit product or credit limit increase the customer needs/wants (e.g. interest rate, fees, repayment amounts). The customer’s objectives are the end the customer wants to achieve by obtaining the credit product or credit limit increase (e.g. purchase an asset and repay within a specified time).

If ME’s product(s) do not meet a customer’s stated requirements and objectives, the application should not be submitted.

Home loans

ME’s home loan application form and processes contain prompts to assist customers to provide information about their requirements and objectives. Sales Staff are specifically required to make appropriate enquiries of the customer in order to document:

- What the customer wishes to achieve by taking out the home loan;
- Why a particular home loan product has been chosen; and
- Why particular product features have been selected.

The customer responses to these enquiries must be documented in sufficient detail and must be specific and consistent with the amount of the loan being applied for. For example, general descriptions such as ‘personal expenses’ is not sufficient.

Sales staff are also required to disclose details of any significant costs and/or risks associated with the preferred loan features being sought and confirm that they have provided this information to the customer and despite these disclosed costs/risks these features are still consistent with the customer’s requirements and objectives. For example, Sales Staff are expected to discuss:

- the possible risks as well as potential future break cost associated with fixing a loan;
- the higher interest rate that applies if the customer wants an offset feature and discuss with the customer whether the likely savings from using the offset are less or more than the higher rate;
- any annual fee associated with a product which will result in a lower home loan interest rate and discuss with the customer whether the likely savings from the lower rate are less or more than the annual fee for the product.

This is meant to serve as a reminder and a record of the information Sales Staff provided to and discussed with the customer with regards to the possible outcomes of the product features they are seeking.

In some instances, a customer’s stated requirements and objectives may conflict (e.g. they may express a desire to fix their loan for 5 years to get a cheaper rate but also say they want to sell the property and pay out the loan within a shorter period). In these instances, Sales Staff must ensure the customer is aware of these conflicts and allow the customer to prioritise or revise their requirements by asking additional questions (and document the customer’s responses).
Credit cards

Credit cards may be sought and used for different purposes and ME is expected to make enquiries to understand the customer’s requirements and objectives and assess whether the card being applied for meets these requirements and objectives. A key feature of the product that relates to the customer’s requirements and objectives is the credit limit the customer desires. As such, in ME’s application form we ask what limit the customer requires or alternatively offer the customer the option to have us set an appropriate credit limit, taking into account their financial situation.

In addition, as credit card products in the market have many different options, features and rates, in ME’s credit card application form we ask the customer to confirm that the card is suitable for their needs by requiring them to view the product details in the Credit Card Key Fact Sheet. This prompts the customer to consider the card features and assists in ensuring that requirements and objectives are met.

4.4 Reasonable enquiries into the customer’s financial situation

You must make the financial enquiries as detailed in the application form(s) for our credit products.

Income

As the consumer’s income is a key factor that affects their capacity to meet financial obligations Lenders need information to determine whether that income is consistent and likely to remain at that level for the term of the credit product being considered.

If the consumer has casual or seasonal employment, lenders need information about the variations in hours and pay that may be expected.

The source of the consumer’s income may also be important. For example, lenders may need to determine whether all or part of the consumer’s income is:

- comprised of social security payments;
- derived from assets and investments (e.g. rental income, dividends or superannuation); or
- dependent on third parties (e.g. maintenance or child support payments, or funds that are voluntarily made available by other persons, such as a spouse or family member, and that are dependent on the expressed willingness of that person to continue to make funds available).

Liabilities and Expenses

Brokers need enough information to determine how much of the consumer’s income is, and will continue to be, needed for outgoings including:

(a) Ongoing debts and liabilities including:

- Repayment obligations for other credit
- Higher Education Loan Program (HELP) debts; and
(b) Essential items – Some expenditure is essential to a person living and participating in modern Australian society, such as:

- Housing/rental;
- Groceries
- Clothing & Personal Care
- Telephone, Internet & Pay TV
- Transport
- Recreation & Entertainment
- Medical & Health
- Utilities & Rates
- Insurance
- Education
- Childcare

There may be categories of expenditure that exist, or are higher, because of the circumstances, lifestyle or other choices of the consumer. These are required to be stated separately from the essential items and may include expenditure items such as:

- Private school fees
- Life insurance
- Income protection insurance
- Body Corporate fees
- Child Maintenance

4.4.1 Foreseeable changes in the future

Home loans

ME’s home loan application includes an enquiry asking the customer if there are any foreseeable changes now or in the future that may impact their ability to make repayments. The customer must provide a ‘yes’ or ‘no’ response to this question.

If the customer answers ‘yes’ then the application requires the customer to advise you:

- What type of change to their circumstances are they anticipating (e.g. a temporary or permanent decrease in income; an expected large expense); and
- How they plan to continue to make their repayments (e.g. using savings; securing additional income; sale of assets; reduce expenses).
The customer is also asked to provide further details explaining their selection. If any information is missing or conflicts with other information available, you will need to make further enquiries and document the customer responses.

You must ensure that any plan to make ongoing repayments is appropriate. When reasonable, we may request that you ask the customer for any documents to verify the reasons provided. For example, if the customer states they plan to start a family in 3 months and they will be relying on savings for when they are on parental leave, you must enquire how much the customer has saved; what their saving plan is for the future and you may also be asked to view bank statements to verify the amount saved. Similarly, if the customer is planning on selling an asset, you must make applicable enquiries regarding the asset (e.g. proposed sale price). Note if the asset is the customer’s principal place of residence, the loan will be assumed to be unsuitable, unless this approach meets the customer’s requirements and objectives and this is appropriately documented.

Any plan to reduce expenses or secure additional income must also be reasonable and documented.

**Credit cards**

ME’s credit card application contains a declaration requiring the customer to confirm that they do not know of any future changes to their financial circumstances that would make it difficult for them to repay their credit card. Customers are therefore prompted to consider their future circumstances.

**4.4.2 Customers nearing retirement age – exit strategy**

**Home loans**

Given the potential term of a home loan (i.e. up to 30 years) an exit strategy is required to be collected and documented by you if any home loan applicant’s age is 50 years or over as at the loan submission date AND their age will be 70 years or over at the maturity date of their loan.

An exit strategy should detail how the customer plans to continue repayments for the loan beyond retirement and/or pay down the loan. Some examples of acceptable exit strategies include:

- Use of superannuation;
- Downsizing their place of residence;
- Selling assets;
- Reducing expenditure.

The customer is asked to provide further details to expand on their selected exit strategy. Further enquiries and/or verification will be required to be collected by you where there is insufficient or inconsistent information provided (i.e. just selecting ‘selling assets’ without any corresponding explanation of the assets and their potential value is unacceptable).

You need to ensure that any plan to make ongoing repayments is sound. When reasonable, we may also request you to ask the customer for any documents to verify the reasons provided.
Credit cards
In our credit card application, we include the exit strategy enquiry as part of the foreseeable changes declaration (rather than as a specific enquiry) given the revolving nature of a credit card facility.

4.4.3 General living expenses
ASIC has advised industry that in respect of the collection of monthly living expenses for home loan applications – actual figures for different categories (e.g. food, transport, insurance, entertainment) are required to be obtained, as opposed to obtaining a single monthly figure and relying upon benchmarking to assess suitability. Accordingly, for all home loan applications, you must collect and detail the customer’s general living expenses on an itemised basis, rather than as a single monthly figure.

5 Focus areas of responsible lending compliance

5.1 Interest Only Home Loans
Additional enquiries must be undertaken by you when assessing the suitability of an interest only loan, especially if the loan is secured by an owner occupied home.
Therefore, our home loan application includes the following:
(a) A question requiring the customer to select their reason(s) for why they want an interest only period from a list of common reasons (e.g. to purchase an investment property; to maximise cash flow; taxation, financial or accounting reasons);
(b) The customer is also asked to provide further details to explain their selection and to advise why the interest only repayment period meets their requirements and objectives.

If the customer indicates anything that seems inconsistent (e.g. they advise the loan being applied for is an owner occupied purpose but select they want to make interest only repayments for taxation reasons), you must make further enquiries to clarify any such inconsistency and document the customer’s response.

If the customer indicates anything that might result in an inability to make repayments (e.g. a reduction in income, a large non-discretionary expense), you must make further enquiries to ascertain and document how the customer will make repayments when their income is reduced, or expenditure increased.

Note in these circumstances, you must also ensure that the “foreseeable changes” section of the home loan application is also completed to capture applicable details of the foreseeable change identified by the customer in system and in the Responsible Lending Obligations form.

When reasonable, we may request that you ask the customer for any documents to verify the reasons provided. For example, if a customer states they are currently working part time, but will commence working full time in 6 months, you may need to obtain evidence from the employer to support this claim.
Similarly, for joint customers the reason for selecting an interest only loan may be because one of them is taking parental leave but is expected to return to work, in which case you may be required to ask for evidence to verify the return date and salary.

5.2 Refinancing activities

In RG 209 ASIC advises that lenders must undertake additional analysis when engaging in refinancing activities (i.e. the level of enquiries that need to be made must be ‘scaled up’).

For any home loans that have the purpose of refinancing or debt consolidation, you must:

- Ask the customer to select their reason(s) for refinancing from a list of common reasons and record this response; and
- Ask the customer to estimate the fees they expect to pay to their existing lender as a result of the refinance (e.g. break costs; discharge fees). This fee estimate is to be recorded in the application and factored into the customer’s funds position (if required).

You need to consider the customer’s reason(s) for refinancing and assess whether entering the new credit contract:

(a) Would result in overall cost savings to the customer that are likely to override any loss of benefits; or
(b) May result in minimal cost savings, but the new credit contract better meets the customer’s needs (e.g. because of convenience, greater flexibility or particular product features).

After a discussion with the customer and a consideration of the costs, risks and benefit of the refinancing, you must be satisfied that the refinancing/debt consolidation meets the customer’s requirements and objectives prior to submitting the application.

Further, if a customer is proposing to refinance or consolidate a debt into their home loan which is for a shorter term (e.g. in the case of a personal loan or credit card), you must advise the customer that even though the home loan interest rate is lower than that of a personal loan or credit card, due to the longer loan term, they may pay more interest over the term of the loan. You should encourage customers to consider whether they wish to proceed on this basis and if so, advise customers that they should consider making additional repayments in order to pay the loan off faster so they may pay less interest.

5.3 Cash out

For an application involving cash out, you must detail the reason(s) for the cash out in the application as well as the purpose for which the customer will use the funds.

In addition, you must discuss with the customer how long they expect to keep the item being purchased using the funds and document their response. It is important to take care to ensure the term of the loan relative to the likely useful life of the asset is appropriate and meets the customer’s requirements and objectives. You must therefore exercise particular care if the customer advises that the item purchased will only have a short life expectancy compared to the remaining loan term.

If the loan term exceeds the life expectancy of the item then you should encourage the customer to consider whether they wish to proceed on this basis. If so, you should advise the customer to consider making additional repayments to repay the loan faster, so they may therefore pay less interest.
5.4 Offering an amount lower than that applied for

Home loans
If we cannot offer the customer the loan amount that they have requested for any reason, we may direct you to contact the customer to discuss if a changed amount of credit or loan term may meet their requirements and objectives. All conversations with the customer are to be documented by you. In our discretion we may also direct you to request additional information from the customer in order for us to determine that the lower loan amount or loan term is not unsuitable for that customer.

Credit cards
If we cannot offer the customer the credit limit that they have requested for any reason, we can approve a lower amount if it will better suit the customer’s requirements and objectives and will be able to be serviced by the customer.

The communication sent to the customer confirming that their credit card has been approved will state the amount that they have been approved for and will note that this amount may be lower than the amount requested and prompt them to contact us if it does not meet their needs.

6 Verification of information

6.1 What is required?

The second step in responsible lending (see the diagram in 3.6 above) is to take reasonable steps to verify the customer’s financial situation.

These steps may differ depending on the circumstances of each individual customer and will be conducted in line with the relevant Credit Policy for each of ME’s credit products. Generally, verification of a customer’s financial declaration, such as income and employment information from independent sources will be undertaken in all circumstances.

ME are also required to verify that the information we are relying on is up to date. Applicable timeframes are set out in the relevant Credit Policy for each of our credit products.

6.2 Verifying income

Detailed income verification requirements are set out in the relevant Credit Policy for each of ME’s credit products.
6.3 Verifying living expenses

ME compares the living expense information collected from the customer against the Household Expenditure Measure (HEM) and in calculating serviceability, we will apply the higher of HEM or the living expenses declared by the customer.

ME do not use benchmarks as a replacement for making enquiries about a particular customer’s current income and expenses, nor a replacement for an assessment based on that customer’s verified income and expenses.

Where ME consider either that any of the individual itemised living expense items or total monthly living expenses declared by the customer in a home loan application are low then additional information must be sought from the customer to explain why this is the case. In addition, in our discretion, documentation may also be required to be collected from the customer to validate their explanation.

7 Making additional enquiries

The third step in responsible lending (see the diagram in 3.3 above) is to make further enquiries about any inconsistencies or discrepancies in the customer’s application. You are required to make additional enquiries (and make a written record of the result of those enquiries which is to be provided to us) in these circumstances, including the following:

(a) Where there are inconsistencies between the information provided by the customer and your enquiries;
(b) Where information provided is unusual or does not meet a common-sense approach (e.g. raises red flags such as where the customer’s assets are materially larger than would be expected given their circumstances);
(c) Where any of the customer’s requirements or objectives are unclear or they change after the application has been submitted;
(d) If the customer changes the amount of credit being applied for after the application has been submitted;
(e) Where information or your enquiries indicate that the customer may have difficulties understanding the credit contract;
(f) Where there are issues regarding the stability of the customer’s income;
(g) Where the customer has only been in employment for short amounts of time;
(h) If we advise you that the credit report raises issues;
(i) If the overall circumstances of the application make it appropriate (given the process of making enquiries is ‘scalable’ and may necessitate additional enquiries).
8 Making the assessment

8.1 What is required?

The last step in responsible lending (see the diagram in clause 3.3 above) is for ME to make an assessment that the loan is ‘not unsuitable’.

A loan will be unsuitable if it does not satisfy two equally important tests, either:

(a) It does not meet the customer’s requirements or objectives; or

(b) The customer will be unable to meet the repayments, either at all or without experiencing ‘substantial hardship’.

If the contract is assessed as ‘unsuitable’ then the application will be declined.

8.2 Assessing ‘substantial hardship’

The customer must only be placed into a credit contract that they can afford to repay without experiencing substantial hardship. Substantial hardship is not defined in the NCCP Act, but it describes something different to (and less than) being ‘unable’ to meet the financial obligations. For example, while being ‘unable’ to meet repayments may be equated to a circumstance of poverty or bankruptcy, the test of being unable to meet repayments ‘only with substantial hardship’ means that less extreme changes to the customer’s situation could mean the credit product is unsuitable.

The law does prescribe some circumstances in which it is presumed the customer will only be able to meet the financial obligations under the credit product with substantial hardship. One these is if the only way to repay is by the customer selling their principal place of residence, it is presumed that the loan will cause substantial hardship unless the contrary is proved. This presumption will not apply if the customer has to sell other assets, e.g. an investment property, however generally loans should be repaid from income not assets sales.

If the presumption regarding the sale of the customer’s principal place of residence applies, a very detailed written explanation (and usually an acknowledgment from the customer) will be required stating how this presumption is rebutted. For example, the presumption could be rebutted if selling the home at or before the time the loan is repayable meets the customer’s requirements and objectives (e.g. in the case of downsizing as an exit strategy).

8.3 Serviceability calculators

ME determine the customer’s capacity to repay the amount of credit requested using a serviceability calculator as set out in our credit product Credit Policies. The serviceability calculator works by calculating how much the customer’s income will exceed the customer’s expenses and existing liabilities after the credit is advanced.

If the amount of uncommitted income is small and it is not clear whether the loan will be repayable without substantial hardship, ME may require you to seek clarification from the customer about any proposed changes in lifestyle or other factors that may impact on the assessment. Any responses must be documented in writing and will be stored on the customer’s application file.
8.4 Providing a copy of the assessment

We must give the customer a copy of the written final assessment if requested within 7 years of the date the credit contract is entered into or the principal increased (the credit date). This need only be given if the credit is provided or the principal increased.

The written final assessment includes the factual information provided by the customer(s) which we used to assess the credit as not unsuitable.

9 Reviewing the outcome of assessments and credit decisions

ME periodically review their portfolio to assess whether responsible lending practices are effective at identifying individual circumstances in which credit products are unsuitable or ‘not unsuitable’ for customers.

ME conduct ongoing quality assurance checks and hindsighting reviews of a sample of our home loan applications submitted each month. Part of this ongoing review program is a focus on ensuring Sales Staff and Credit Staff are complying with responsible lending obligations.

In addition, ME conducts targeted audits and spot checks of broker compliance with responsible lending obligations as part of our audit and compliance program. We may request detailed information and documentation from you at our discretion as part of these ongoing reviews (e.g. a copy of your fact find and/or preliminary assessment in support of the application).