Confidential

Westpac Banking Corporation - Submissions on Auto Finance Case Study

Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry

3 April 2018

WESTPAC AUTO FINANCE CASE STUDY SUBMISSIONS

WESTPAC BANKING CORPORATION

INTRODUCTION

1. These submissions set out the findings Westpac Banking Corporation (**Westpac**) submits should be made by the Commission on the questions identified in Counsel Assisting's Closing Submissions in relation to the Westpac auto finance case study.[1]

2. The case study concerns a car loan that St.George Finance Limited (Australian credit licence 387944) (**SGFL**) provided in July 2012. SGFL is a Westpac Group entity, trading in this case as Bank of Melbourne. SGFL ceased to originate car loans on 1 March 2015 and, since that time, all car loans are originated by Westpac.

3. The submissions are structured as follows:

   a. Annexure A sets out the factual findings that Westpac submits the Commission should make with respect to the case study concerning Ms Nalini Thiruvangadam who, in July 2012, obtained a car loan from SGFL;

   b. Part A addresses whether the Commission should make findings of misconduct in relation to the loan to Ms Thiruvangadam;

   c. Part B addresses whether the Commission should make findings of conduct falling below community standards and expectations;

   d. Parts C – D address the general questions identified as arising from this case study;

   e. Part E addresses incentive structures and sets out improvements and additional measures implemented by SGFL, and subsequently Westpac, since 2012; and

   f. Part F sets out Westpac's views on proposals for reform.

A. AVAILABLE FINDINGS OF MISCONDUCT

Ms Thiruvangadam's car loan should not have been approved

4. Annexure A sets out the findings of fact that Westpac submits the Royal Commission should make in relation Ms Thiruvangadam's loan. For the following reasons, Ms Thiruvangadam's application should not have been approved:

   a. the application showed that Ms Thiruvangadam's main source of income at the time of her application was a Centrelink allowance of $2,138.50 per month, but there is no evidence that the appropriate supporting documents were obtained to verify this amount;

   b. the other income disclosed in the application, being $866.66 per month, was inconsistent with the payslip provided, and in any event was not sufficient on its own to satisfy Westpac's serviceability requirements;

   c. although the application stated that Ms Thiruvangadam had been employed in a part-time role since 24 October 2011, the payslip attached to the application indicated that Ms Thiruvangadam was a casual employee;

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[1] Closing Submissions – Personal Overdrafts, Processing Errors, Car Loans and Credit Cards: RCD.9999.0003.0001 at paragraphs 37 to 41.

d. the only document provided in relation to the debt owed to Orange was an email sent from a Collections Officer at Axess Debt Management to Ms Thiruvangadam stating: "Please be advised as discussed today that you are under no obligation to pay your Orange account…however if you would like to make payment we would be willing to accept this and will update any relevant credit file listings 7-10 days after payment." This ambiguous document ought not to have been treated as constituting proof of payment;

e. finally, the payslip was for the period 19 March 2012 to 1 April 2012, which made it (by 3 weeks) too old under SGFL's policies to constitute a verifying document for an application submitted in July 2012.

Section 47(1)(a) of the *National Consumer Credit Protection Act* and s 912A(1)(a) of the *Corporations Act*

5. Section 47(1)(a) of the *National Consumer Credit Protection Act 2009* (Cth) (**NCA**) provides that an Australian credit licensee must do all things necessary to ensure that the credit activities authorised by the licence are engaged in "efficiently, honestly and fairly". A similar obligation is imposed by s 912A of the *Corporations Act 2001* (Cth) on Australian financial services licensees in relation to provision of financial services. SGFL did not provide a "financial service" within the meaning of s 766A of the *Corporations Act 2001*. Accordingly, s 912A is not applicable.[2]

6. "Credit activities" are broadly defined. While Counsel Assisting has submitted that it is open to the Commissioner to make a finding that SGFL has breached these statutory obligations in relation to Ms Thiruvangadam, no specific element of conduct relating to Ms Thiruvangadam's loan has been singled out as inefficient, dishonest or unfair.

Conduct during the origination of the loan

7. Westpac accepts that in relation to Ms Thiruvangadam's loan it did not ensure that her income was properly verified. However, not ensuring such verification, in a single case, does not constitute or demonstrate a failure to "to do all things necessary" to ensure that its credit activities were engaged in "efficiently, honestly and fairly". Westpac submits that s 47(1)(a) sets out a standard of general application to licensees in their credit activities as a whole, and imposes a requirement of appropriate organisational systems, which would not be met in the event of a failure to put in place appropriate systems, rather than criteria for application to an individual transaction. The reference to the licensee's engagement in 'credit activities' is expressive of the overarching thrust of the provision, which looks to the systems and processes a licensee has in place, and whether they have done what is necessary to meet the general requirement for their credit activities.

8. Read in the context of s 47 as a whole, sub-s 47(1)(a) has a double function of setting a general standard of behaviour for licensees ("efficiently, honestly and fairly") and then requiring the implementation of measures which are necessary, reasonable, and adapted to achieving that standard. The qualification "reasonable" is either a necessary implication, or is necessarily entailed in

[2] *Corporations Act 2001* (Cth), s 765A(1)(h); *Corporations Regulations 2001* (Cth), r 7.1.06.

the standard of “efficiently”: strict fairness in each individual case is in tension with overall efficiency. This is reinforced by s 47(1)(k) which, when read with (a), imposes an obligation to have *adequate* arrangements and systems to ensure compliance with the duty imposed by (a). The standard of “adequacy” is expressly modified by considerations of efficiency (nature, scale and complexity) by s 47(2). For those reasons, s 47(1)(a) establishes a requirement of appropriate organisational competence, rather than an absolute standard of performance.[3]

9. In 2012, SGFL had detailed policies, processes and controls in place to ensure that Dealer Business Managers made reasonable inquiries about a customer’s financial situation, gathered appropriate supporting documents and information and conveyed those to SGFL. There were strict contractual obligations imposed on the Dealer. They included the declarations and acknowledgements in the Dealer Agreement at Schedule 1,[4] and provisions making the Dealer the guarantor of the customer if the dealer gives incorrect or misleading information in connection with the credit agreement.[5] SGFL’s processes in connection with dealers included a range of control systems, including accreditation and training. There were also policies and processes in place to ensure that SGFL assessed applications for car loans on the basis of sufficient supporting documentation.[6] By having those policies and processes in place, SGFL took the appropriate steps it could to meet its obligations and did all that was reasonably necessary to ensure that it engaged in credit activities “efficiently, honestly and fairly”.

Conduct occurring after origination

10. Over the course of the loan, Ms Thiruvangadam made frequent repayments, although she was often in arrears.[7] She applied for hardship assistance on 4 April 2013,[8] some nine months after entering into the loan contract which was processed in accordance with the Westpac hardship policies.[9]

11. Ms Thiruvangadam’s hardship application, which was based on her disclosed circumstances at that time, was approved on 18 April 2013.[10] The terms of assistance were that arrears on the car loan were capped at $2,349.73 and that there would be no fortnightly repayments due until 17 June 2013.[11] Ms Thiruvangadam complied with the arrangement but fell back into arrears by September 2013.[12] After that time, Ms Thiruvangadam continued to make ad-hoc repayments on the loan over the course of approximately four years, but remained in arrears.[13]

12. Hardship assistance is intended to provide relief to customers who are going through a temporary period of difficulty making loan repayments. It is not intended to be used where there is a reasonable

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[3] Two other features of s 47 might be noted: non-compliance with it has no express consequences in the Act; and some of its subsections restate obligations imposed elsewhere and in more detail in the Act ((1)(d), (j)).
[4] Ex 1.141.1 PG1-1 [WBC.300.055.5978]
[5] Ex 141.1.1 PG1-1 [WBC.300.055.5978 at cls 6 and 7 at .5967]
[6] Those policies and processes have been enhanced over time and are described as they are today in paragraphs 52 to 73 and 100 to 104 of Ex 1.142 Witness Statement of Phillip Godkin dated 5 March 2018 (**Godkin Case Study Statement**) [WBC.900.002.0001]
[7] Ex 1.142 Godkin Case Study Statement [WBC.900.002.0001], [22] – [28].
[8] Ex 1.142 Godkin Case Study Statement [WBC.900.002.0001], [29]
[9] Ex 1.142 Godkin Case Study Statement [WBC.900.002.0001], [13]
[10] Ex 1.142 Godkin Case Study Statement [WBC.900.002.0001], [29]
[11] Ex 1.138.12 NDT-12 [RCD.0014.0003.0041]; Ex 1.142 Godkin Case Study Statement [WBC.900.002.0001, [29].
[12] Ex 1.142 Godkin Case Study Statement [WBC.900.002.0001], [31]
[13] Ex 1.142 Godkin Case Study Statement [WBC.900.002.0001], [30] – [39].

belief that the customer will be unable to repay the loan even if the credit contract is changed. The hardship assistance provided to Ms Thiruvangadam was appropriate if the expectation at the time was that her financial circumstances would improve such that her period of hardship was short term. However, expectations of improved financial circumstances did not eventuate, as Ms Thiruvangadam was unable to resume work following her fall and her circumstances therefore became unlikely to improve.[14] In such a case, the use of the hardship provisions would not be an effective and adequate response to the repayment difficulties being faced by the customer.

13. Westpac has made a number of improvements to its hardship processes to address the kind of issues raised by Ms Thiruvangadam's case. Westpac acknowledges that in a case such as this where difficulties making repayments continue throughout subsequent periods of the loan, more can and needs to be done to explore other options with the customer. (See paragraph 70 below).

14. On 4 October 2017, the Consumer Action Law Centre, on Ms Thiruvangadam's behalf, raised for the first time concerns about whether the loan should have been made, and Ms Thiruvangadam's circumstances at the time the loan was made (as opposed to circumstances resulting from her post-loan injury).[15] Westpac undertook an investigation into her circumstances at the time of the loan and the circumstances surrounding the approval of her loan,[16] including a credit review by the Credit Quality Assurance Team. This team concluded that her loan application should not have been approved.[17]

15. On 1 November 2017, Westpac offered to resolve the matter with Ms Thiruvangadam and proposed two options for her consideration, one of which included her keeping the car (and receiving $20,000) and one which did not (receiving a payment of $24,000).[18] The settlement offers were fair in the circumstances, and consistent with the loss calculation approach of FOS,[19] based on the valuation of the car and her use of it.[20] Ms Thiruvangadam accepted the offer within two weeks, and payment was made by Westpac approximately one week later.[21]

16. The conduct that occurred after Ms Thiruvangadam's loan was granted, in all the circumstances, did not evidence or entail any breach of s 47(1)(a) of the NCA.

Section 128(a) of the NCA – reasonable inquiries about financial situation

17. For the reasons set out below, Westpac submits that there is no basis for the Commission to find that Westpac did not make reasonable inquiries in relation to Ms Thiruvangadam's financial situation.

18. Section 128(a), in conjunction with ss 129 and 130(1)(b) of the NCA, relevantly provide that an Australian credit licensee must not enter into a credit contract with a consumer unless the licensee has assessed the credit contract as "not unsuitable" for the consumer and made reasonable inquiries about the financial situation.

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[14] Transcript 21 March 2018 (N D Thiruvangadam) T:723:40-41
[15] Ex 1.142 Godkin Case Study Statement [WBC900.002.0001], [40]; Ex 1.142.17 PG2-17 [WBC.300.003.4218]
[16] Ex 1.142 Godkin Case Study Statement [WBC900.002.0001], [41]
[17] Ex 1.142 Godkin Case Study Statement [WBC900.002.0001], [42]
[18] Ex 1.142 Godkin Case Study Statement [WBC900.002.0001], [45]
[19] Ex 1.142 Godkin Case Study Statement [WBC900.002.0001], [47]; and Ex. PG2-22 [WBC.104.001.9049]
[20] Ex1.142.22 PG2-21 [WBC.300.003.4227]; Ex 1.142.23 PG2-22 [WBC.300.003.4308]
[21] Ex 1.142 Godkin Case Study Statement [WBC900.002.0001], [49]

19. Section 130 of the NCA does not require the "reasonable inquiries" to be made by the credit licensee directly of the consumer. A credit provider can comply with its obligations by making inquiries of a third party intermediary who has made direct inquiries of the consumer.[22] When relying on information provided from the third party intermediary, a credit provider should ensure it has sufficient information from that third party to comply with its own obligations and that it is reliable.

20. SGFL made reasonable inquiries about the financial situation, requirements and objectives of Ms Thiruvangadam through the Dealer Business Manager. Ms Thiruvangadam confirmed that the Dealer Business Manager asked her questions about her employment, income (including income other than from her employment), debts, expenses, and whether she owned property,[23] as the Dealership was required to do under the Dealer Agreement. Ms Thiruvangadam said she also told the Dealer about her income, that she owed about $1,500 on a credit card and that she currently paid about $1,300 per month in rent.[24] However, it appears that although the Dealer Business Manager asked relevant questions, he did not accurately record all of Ms Thiruvangadam's responses in the Sovereign application fields or in her finance application.[25] According to the information available, the information on which Ms Thiruvangadam's application was ultimately assessed was set out in Ms Thiruvangadam's signed application generated through Sovereign and the other information referred to in Annexure A at paragraph 16.[26]

21. The extent of the Dealer's inquiries as to Ms Thiruvangadam's expenses is not clear from the evidence, though it is clear some inquiries were made. There is no reason to conclude that the Dealer's inquiries were insufficient (as opposed to the results being wrongly reported). In any event, for the reasons set out in paragraphs 19-20, SGFL did make reasonable inquiries of Ms Thiruvangadam's financial situation as it made such inquiries of the Dealer who had dealt with her, who in turn had had a discussion with Ms Thiruvangadam about her financial situation. As mentioned in paragraph 9 above, in 2012, Westpac had in place a number of policies, procedures and controls to ensure intermediaries made all relevant inquiries regarding the customer's financial circumstances and requirements and objectives, and conveyed the information obtained to the Westpac Group. Those policies, processes and controls remain in place and have been enhanced over time. The obligations of Dealers to ask appropriate questions and accurately record the responses were in 2012, and continue to be, the subject of accreditation and mandatory annual training provided to the Dealer Business Manager,[27] which has been modified and expanded over time.[28]

22. In addition, in this case, the failure of the Dealer to report Ms Thiruvangadam's living expenses would be unlikely to have affected the outcome of the serviceability assessment. Because at that time SGFL relied upon to the Henderson Poverty Index (**HPI**) for living expenses other than rent (unless the expenses were over the HPI) in assessing the application, an amount for living expenses was in

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[22] Regulatory Guide 209 Credit licensing: Responsible lending conduct (**Regulatory Guide 209**), at RG209.53 – RG209.56.
[23] Ex 1.138 Thiruvangadam Statement [WIT.0001.0012.0001], [13], [18], [19].
[24] Transcript 21 March 2018 (N D Thiruvangadam) T:719: 17-21, 720:1-9, 19-23; Ex 1.138 Thiruvangadam Statement [WIT.0001.0012.0001]: [13].
[25] Ex 1.142.4 PG2-4 [WBC.300.001.0027].
[26] Ex 1.142.4 PG2-4 [WBC.300.001.0027].
[27] Ex 1.141 Witness Statement of Phillip Godkin dated 5 March 2018 (**Godkin General Statement**) [WBC.900.001.0001], [34],
[28] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [35].

each case included in SGFL's serviceability assessment (see paragraph 30 below). The failure to report expenses was subject to the control of using HPI and therefore, expenses were included in the serviceability assessment.

23. Since 2012, Westpac has implemented additional measures to ensure that Dealer Business Managers comply with their obligations. These measures are set out in more detail below at paragraphs 57 to 80.

Section 128(a) of the NCA – reasonable steps to verify financial situation

24. Section 128(a) of the NCA, in conjunction with ss 129 and 130(1)(c) of the NCA, requires the credit licensee to take reasonable steps to verify the customer's financial situation. For the reasons that follow, Westpac submits that reasonable steps were taken in relation to verification of expenses. However, Westpac accepts that, on the evidence available, it is open to the Commission to find that SGFL did not take reasonable steps to verify Ms Thiruvangadam's income and, to that extent, in the case of Ms Thiruvangadam, SGFL may not have met a part of the requirements of s 128(a) of the NCA.

25. The steps that SGFL took to verify Ms Thiruvangadam's financial situation included obtaining at least:

   a. a signed declaration from Ms Thiruvangadam that the information contained within the application was true and correct;[29]

   b. a declaration from the Dealer Business Manager that he had asked Ms Thiruvangadam all of the questions in the application, and had recorded the answers provided, or left blanks as instructed by Ms Thiruvangadam, if applicable;[30]

   c. a credit bureau report;[31]

   d. a payslip; and

   e. use of the HPI benchmark.

26. The level of verification required by s 130 will depend on the nature of the credit contract and the circumstances of each application.[32] The legislation is not prescriptive and does not mandate any particular verification step.

27. In 2012, SGFL's informal policies and processes would have required further documents which it appears were provided to verify Ms Thiruvangadam's employment and Centrelink income. It is possible that the Credit Team had access to or obtained further documents at the time of verification, but there is no evidence of this. Westpac accepts that, on the evidence available, it is open to the Commission to infer that SGFL did not take reasonable steps to verify Ms Thiruvangadam's income.

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[29] Ex 1.142.4 PG2-4 [WBC.300.001.0027 at 0033].
[30] Ex 1.142.4 PG2-4 [WBC.300.001.0027 at 0035 - 0036].
[31] This is referred to in the credit review of Ms Thiruvangadam's file in 2017: Ex 1.142.17 PG2-18 [WBC.300.003.4290 at 4292]
[32] Regulatory Guide 209, at RG209.19 and following.

28. There were no expenses declared in the loan application. Apart from the measures set out in paragraph 25 above, in most cases, Westpac does not take steps to independently verify a customer's declared, estimated expenses in the context of auto finance applications.[33] Such an approach, however, is reasonable in the circumstances and in light of the processes which are followed. Customer expenses are inherently difficult to verify. In circumstances where a customer understates their expenses, it is not possible for the financier to identify with confidence what the customer's true expenses are because the financier does not have access to the records necessary to establish the true position. The customer may have other bank accounts or cash expenses which might materially alter the position and there is no source the financier can utilise to discover all of a customer's accounts. Expenses can fluctuate significantly (eg, some large expenses like insurance and taxes might be annual) so that a person's expenses in any particular period may not be a good indicator of what they may be in another period. Some customers may understate or overstate their expenses and some customers, especially those who believe they have a real need for finance, may deliberately understate their expenses.

29. Financial institutions therefore rely heavily on the information provided and *verified* as accurate by the customer and the use of benchmarks or automated systems and tools to apply a statistically based and independent objective measure to the customer information. In this context, ASIC has endorsed the use of benchmarks or automated systems and tools as part of the process for taking reasonable steps to verify the consumer's financial situation (not as a substitute for making inquiries about the consumer's financial situation).[34]

30. Because of the difficulty in verifying expenses, it was SGFL's practice in 2012 to use the higher of declared expenses or the appropriate measure from HPI in conducting serviceability assessments. The HPI measure was used in Ms Thiruvangadam's case. This was reasonable in the circumstances. Nothing in the information provided, or available in fact, suggests that HPI was not a reasonable measure of the living expenses that would need to be incurred by her if she was to avoid substantial hardship.

Section 133 of the NCA[35]

31. Section 133 of the NCA provides that an Australian credit licensee must not enter a credit contract with a consumer if the contract is "unsuitable" for the consumer. A contract will be unsuitable for a consumer if it is likely that the consumer will be unable to comply with the consumer's financial obligations under the contract, or could only comply with substantial hardship. Pursuant to s 133(4), the relevant information to be taken into account in determining whether the contract is unsuitable is the information about the consumer's financial situation and requirements and objectives that the licensee had reason to believe was true, or that the licensee would have reason to believe was true if the licensee had made the necessary inquiries and or verification under s 130.

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[33] Transcript 21 March 2018 (P G Godkin), T:746:41-45.
[34] Regulatory Guide 209, at RG209.49.
[35] These submissions proceed on the basis that it is only civil contravention of s 133 that is in question. Were s 133(6) to be engaged issues quite different from those developed in evidence, or of which notice has been given, would have to be addressed, in particular, those arising from the operation of Chapter 2 of the *Criminal Code* (Cth).

32. Westpac accepts that by reference to its policies as they stood in 2012 the car loan made to Ms Thiruvangadam should not have been approved for the reasons outlined in paragraph 4 above. However, Westpac also submits that in the unusual circumstances of this case no contravention of s 133 has been shown. Westpac submits that the steps that were taken to verify Ms Thiruvangadam's expenses were reasonable in all the circumstances at the time the loan was made. The Dealer, as he was required to do, made reasonable inquiries about Ms Thiruvangadam's financial situation as explained above. However, the Dealer failed accurately to record and report information provided by Ms Thiruvangadam, in particular as to her expenses.

33. SGFL's liability under s 133 is to be judged by reference to the information it had at the time, and what reasonable inquiries and verification would have revealed. As to income, reasonable inquiries had been made and the information that SGFL had was broadly accurate. The main deficiency pertinent to unsuitability[36] was that SGFL believed Ms Thiruvangadam was a part time employee rather than casual.[37] But it does not follow that for Ms Thiruvangadam her employment income was in fact so much more uncertain by virtue of that distinction as to warrant being substantially discounted in assessing unsuitability. If any inference is available it is that she was confident her work would continue at least at her current rate, including by taking extra shifts when possible,[38] if she was able to borrow to buy a car. As for expenses, the problem was that despite reasonable inquiries, SGFL was misled as to her expenses, but in a manner that resisted additional verification. The critical point was a statement that she had no rent as she was boarding with her uncle. In fact she paid $1,300 per month, which would dramatically alter any assessment of her ability to repay without substantial hardship. However, this was not something that it has been suggested SGFL could readily verify apart from seeing that Ms Thiruvangadam had signed the page of the loan application form that indicated that it was so.

34. It follows that it has not been shown, by reference to the relevant base of information for the application of s 133, that the loan to Ms Thiruvangadam was necessarily unsuitable.

35. Westpac accepts that in light of all the information now available the loan to Ms Thiruvangadam ultimately was "unsuitable". However, it is not necessarily the case that any car loan would have been unsuitable for Ms Thiruvangadam in July 2012. In particular, a loan at a lower but still commercial rate, may have been within her capacities. At that time, Ms Thiruvangadam was in paid employment – indeed, it was important to Ms Thiruvangadam to obtain a new and reliable car to continue to do the work that she was doing.[39] Ms Thiruvangadam believed she would be able to repay a car loan if she could continue to work.[40] Her injury and inability to work was deeply regrettable and no doubt had a significant effect on her ability to repay the loan. But for those events, Ms Thiruvangadam might have been able to meet repayments on a car loan, as she had hoped, and without undue hardship.

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[36] Inappropriate reliance on the evidence of "repayment" of her old, outstanding debt would not have gone to unsuitability in the statutory sense, as the evidence did at least indicate she was no longer called on to repay it.
[37] This was identified by Mr Godkin as an "issue" at Ex 1.142 [15(c)]; and see [52(b)] for later policy concerning casual income.
[38] Compare the two pay slips at NDT 1, RCD.0014.0003.0002: one for the net amount of $351, the other for the net amount of $448.
[39] Transcript 21 March 2018 (N D Thiruvangadam) T:728:31 - 42.
[40] Transcript 21 March 2018 (N D Thiruvangadam) T:728:44 – 47.

36. We note this matter not to detract from Westpac's admission that the loan should not have been approved, but to highlight the fact that care needs to be taken so that responsible lending standards do not have the effect of restricting people who want and can afford credit (including by making reasonable adjustments to their expenditure) from getting it.

Banking Code of Practice

37. Clause 27 of the Banking Code of Practice provides that before a bank offers, gives the customer, or increases an existing, credit facility, the bank will exercise the care and skill of a diligent and prudent banker in selecting and applying its credit assessment methods and in forming its opinion about the customer's ability to repay the facility. Westpac accepts that the verification of Ms Thiruvangadam's financial situation falls short of the standard set by cl 27 of the Banking Code of Practice.

B. COMMUNITY STANDARDS AND EXPECTATIONS

38. This section addresses the questions raised in Counsel Assisting's Closing Address as to whether Westpac has engaged in misconduct and conduct that fell below community standards and expectations. For the reasons set out below, it is submitted that Westpac has not engaged in misconduct or conduct that fell below community standards and expectations.

Flex commissions

39. A flex commission is a commission paid as a percentage of the margin that is achieved over a base rate of interest set by the lender.[41] The amount of flex commission that can be earned by a Dealer is calculated as follows:

    a. Westpac Auto Finance Business sets a base rate of interest for the specific Dealer (**Base Rate**);

    b. the Dealer then determines the interest rate charged to the Customer (**Customer Rate**);

    c. the difference between the Base Rate and the Customer Rate is called the **Margin**;

    d. the Dealer is paid a proportion of the Margin according to percentages that are agreed at the time of entering into the Dealer Agreement;

    e. the component of the Margin that is allocated to the Dealer is the flex commission.[42]

40. The Dealer has the discretion to set the Customer Rate on a loan by loan basis. The Customer Rate is not determined by reference to the customer's risk rating.

41. In its Consultation Paper 279[43] ASIC expressed its conclusion that flex commissions: "(a) provide an incentive for intermediaries to increase the price of a credit contract in a way that can depend on the negotiating skills or vulnerability of the consumer; and (b) create a risk of unfairness in any individual transaction". Westpac agrees.

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[41] Transcript 21 March 2018 (P G Godkin) T: 752:25.
[42] Ex 1.141 Godkin General Statement [WBC.900.001.0001], Confidential Annexure D, paragraph 4.
[43] Ex 1.158 MS-4 to the Statement of Michael Saadat, [ASIC.0900.0001.0122 at .0132 at [11]].

42. Westpac acknowledged the weaknesses in the design of commission and payment structures in an Audit Report of August 2015.[44] ASIC had signalled an intent to consult on the future of the current commission model (known as Flex) and Westpac intended to be an active participant in this consultation. Consultation would be with key stakeholders across the industry and would take some time to implement. Acknowledging this and to reduce the risk of unfair customer outcomes Westpac unilaterally moved to cap interest rates. The Audit Report indicated a range of rates between 4.5% – 18.95%. An interest rate cap of 16% was put in place in November 2015. [45] Whilst there is the potential for a conflict between dealer and intermediary Westpac submits that the introduction of a cap on the product at a rate which is not much higher than a comparable market rate goes some way to managing this. The alternative product(s) to the single product available for financing at a car yard is the Flexi Loan, the Unsecured Personal Loan or if LVR is less than 110% the Secured Personal Loan. Flexi Loans currently attract a rate of 14.99%, Unsecured Personal Loans currently attract a rate of 12.99% versus Secured Personal Loans 8.99%.

43. ASIC has prepared and released a number of consultation papers to industry participants seeking feedback on potential solutions to address the challenges of flex commissions.[46] Westpac has consistently supported ASIC and industry approaches to changing the commission structure and increasing customer transparency.[47] In particular, in order to minimise the risks associated with the current industry model of Dealer commission, Westpac has supported a prohibition on flex-commissions, so as to eliminate the nexus between customer rate outcomes and dealer commission. This remains Westpac's position.

44. Flex commissions are prevalent in the car finance industry[48] and have existed for over a quarter of a century.[49] It is a pricing construct that exists as a result of the market structure of car sales and finance. As Michael Saadat, the Senior Executive Leader of the ASIC Deposit Takers, Credit and Insurers team, said in his statement the consumer demand for point of sale finance produces a market in which financiers (and insurers) compete with one another not for the custom of end-consumers but rather for the custom of the intermediary dealers.

45. As a result of the organic consequence of market structure, the issue cannot be addressed by individual lenders abandoning the practice. Michael Saadat's statement said lenders had advised ASIC on an informal basis that they were willing to move away from flex commissions to a pricing for risk model but were unable to do so because of the "first mover problem". As he said "lenders advised ASIC that … they believed that if any individual lender attempted to change to a different business model (especially one in which the interest rate was linked to the consumer's creditworthiness), dealers would simply move their business to another lender who continued to offer flex commission arrangements."[50] That would simply leave the market to others who did not abandon the practice. The outcome for customers will be the same.

[44] Ex 1.144, [WBC.300.021.7233 at .7233_0003]
[45] Ex 1.141 Godkin General Statement, Confidential Annexure D, at [5].
[46] Ex 1.187 [WBC.103.005.5591], Ex 1.158 MS-2 to the Statement of Michael Saadat [ASIC.0900.0001.0109]
[47] Ex 1.146 WBC.040.034.6510, Ex 1.186 [WBC.104.003.2122].
[48] Ex 1.158 MS-4 to the Statement of Michael Saadat, [ASIC.0900.0001.0122 at .0135 at [32]].
[49] Ex 1.158 MS-4 to the Statement of Michael Saadat, [ASIC.0900.0001.0122 at .0134 at [28]].
[50] Ex 1.158 MS-4 to the Statement of Michael Saadat, [ASIC.0900.0001.0122 at .0134 at [28]]

Disclosure of Dealers' commission structures

46. Westpac's loan agreements disclose the fact of payment of a commission to Dealers, as required by law.[51] However since the commission structure (which includes volume based incentives based on past sales) makes the amount of commission unascertainable at the time of the sale, the actual commission payable to the Dealer is not required to be disclosed.[52] Westpac accepts that many, likely most, consumers do not understand the way in which Dealers are remunerated or the level or basis of commission paid to Dealers. Information about the commission structures of car dealers is in the public domain, including through ASIC reports on the issue. Consumers would also be aware that finance through a Dealer is only one of many options available to them to obtain finance for the purchase of a vehicle.

47. While accepting that the current approach to Dealers' commission and customer transparency should be changed, Westpac does not accept that in the context of a commission structure which applies throughout the industry, the fact that Westpac allows flex commissions when consumers may not be fully informed about Dealer commission at the point of sale is necessarily conduct that falls below community standards and expectations. The issue has not been addressed by regulation in the context of the regulatory attention given to a range of auto finance issues. Other than the ASIC Instrument,[53] existing commission structures have not been the subject of any legislative restriction or disclosure obligations, despite the period during which the issue has been the subject of consultation with ASIC and the wider industry. The length of that process reflects the complexity of the issues, and the difficulty of settling upon an optimal industry wide solution. Westpac has capped rates, and consumers today are readily able to test the Customer Rate proposed by a Dealer against other rates available in the market.[54]

48. Westpac agrees however that current commission practices and the fact that they are not drawn to the attention of a purchasing consumer is out of step with other developments in the consumer credit area. Westpac remains of the view that industry wide change is necessary to address the issue and achieve better customer outcomes.

C. EFFECTIVENESS OF MECHANISMS FOR REDRESS

49. For the reasons set out in paragraphs 10 to 15 above, having regard to the overall circumstances, Westpac submits the mechanisms for redress in relation to Ms Thiruvangadam were effective and appropriate.

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[51] *National Credit Code 2009* s 17(14)
[52] *National Credit Code 2009* s 17(14)(d). See, for example, Ms Thiruvangadam's loan agreement, Ex 1.142.4, PGC2-4, [WBC.300.001.0027].
[53] *ASIC Credit (Flexible Credit Cost Arrangements) Instrument 2017/780*
[54] Various commercial loan comparison sites exist, eg: https://www.carloans.com.au; https://mozo.com.au/car-loans; https://www.canstar.com.au/compare/car-loans/.

D. STRUCTURAL ARRANGEMENTS BETWEEN BANKS AND CAR DEALERS FOR THE PROVISION OF CAR LOANS TO CONSUMERS

50. This section addresses the general questions raised in Counsel Assisting's Closing Address as to whether the structural arrangements between banks and car dealers for the provision of car loans to consumers are likely to result in contraventions of the banks' responsible lending obligations.

51. The origination of car loans through Dealer intermediaries is driven by consumer demand for finance at the point of sale of the vehicle. The Dealer is not required to hold a credit licence and the responsible lending provisions under the NCA do not apply to Dealers who do not hold a licence. The Dealer is permitted to deal with the customer without a licence in relation to the purchase and finance of the vehicle under a Point of Sale (**POS**) exemption.[55]

52. The structural arrangements that exist between Westpac and Dealers comprise the terms of engagement as well as commission and incentive structures, which are addressed elsewhere in these submissions. The framework for the arrangement also includes a number of systems and controls to ensure Westpac's responsible lending obligations are met where Dealer intermediaries originate car loans written by Westpac. The structural arrangements and framework are discussed in detail in paragraphs 57 to 80 below.

53. The responsible lending provisions under the NCA apply to Westpac. Although the responsible lending provisions do not apply to Dealers, Westpac needs and requires Dealers to comply with certain responsible lending obligations. The result is that the Dealer plays an important role, but faces no regulatory consequences. Westpac needs and requires Dealers to engage with customers, collect the required information from them, and in that engagement, comply with responsible lending obligations. Westpac provides Dealers with training and systems that are designed to ensure compliance with responsible lending obligations. Westpac has put in place a number of monitoring processes, checks and assurance reviews to detect Dealer misconduct and potential breaches. These processes, along with the enforcement of sanctions, have an important deterrent effect against future misconduct.

54. Westpac has invested significant resources in these systems and checks in recognition of the fact that Dealers' compliance is an integral component of the overall structure that ensures compliance with Westpac's responsible lending obligations. For those reasons, the Commission ought to find that the structural arrangements between Westpac and Dealers for the provision of car loans originated by Dealers are not likely to result in contraventions of Westpac's responsible lending obligations under the NCA.

E. INCENTIVES STRUCTURES AND IMPROVEMENTS SINCE 2012

55. Westpac acknowledges that the current structure of Dealer commission carries the risk that some Dealers may prefer their own interests to the interests of customers. Westpac's view on the payment and commission arrangements for Dealers in the car financing market is that they need to change.

[55] Regulation 23 of the *National Consumer Credit Protection Regulations 2010* (Cth).

Westpac has consistently supported ASIC and industry approaches to changing the commission structure, including seeking a complete prohibition on flex commissions, so as to comprehensively eliminate the nexus between Customer Rate outcomes and Dealer commission.

56. Recognising this, Westpac has implemented a series of improvements and additional measures, including increased monitoring and control mechanisms, as well as a new Specialist Finance Third Party Consequence Management Framework (**Consequence Management Framework**), to ensure that Dealer Business Managers comply with their obligations. Further detail on these measures is set out below.

Dealer Agreements

57. Under the Dealer Agreements, Dealers are obliged to follow the procedures specified by Westpac from time to time in relation to loan applications.[56] For example, the Dealer specifically agrees that in submitting a "credit offer", it will make any enquiries Westpac requires of the Dealer to assist Westpac in satisfying its responsible lending obligations.[57] The Dealer Agreement is an important part of the framework for ensuring Westpac meets its responsible lending obligations because the Dealer would understand that a failure to follow Westpac's processes could result in termination of the Dealer Agreement.

Accreditation of Dealers

58. Westpac requires a Dealer Business Manager to be accredited prior to the Dealer Business Manager originating any loans.[58] As part of the accreditation process, the Dealer Business Manager is required to undertake training and complete online accreditation modules, including on "Responsible Lending." The responsible lending training requires the Dealer Business Manager to complete scenario based assessments. That training must be completed annually.

59. Since 2012, there have been a number of improvements in the Dealer accreditation and training process, including in relation to responsible lending which was last updated in 2017. The training relating to customer fairness has also been updated. The purpose of the training is to ensure that Dealer Business Managers have the relevant knowledge about their obligations. That training includes an assessed component and completion of that training is monitored.[59] For example, the Responsible Lending Storyboard, which is part of the Dealers' training, is comprehensive and includes interactive sections and assessments.[60]

60. Accreditation can be and has been withdrawn under the Consequence Management Framework.[61]

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[56] Ex 1.141.1 PG1-1, Dealer Agreement [WBC.300.055.5963], clause 3.1.
[57] Ex 1.141.1 PG1-1, Dealer Agreement [WBC.300.055.5963] clause 1.1, Schedule 1.
[58] Ex 141 Godkin General Statement [WBC.900.001.0001], [32] – [51].
[59] Ex 1.142 Godkin Case Study Statement [WBC.900.002.0001], [52(b)]; Ex 1.141 Godkin General Statement [WBC.900.001.0001], [36] – [38], [40], Ex 1.141.4, .5, .6 PG1-C5 [WBC.300.055.7443, WBC.100.009.4879, WBC.100.009.7863], Ex 1.141.7 PG1-C6 [WBC.300.001.6570].
[60] Ex 1.141.5, PG1-C5 [WBC.100.009.4879].
[61] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [115].

Attestation

61. In 2017, Westpac introduced a requirement that Dealer Principals be provided with a bulletin about the Dealers' obligations to Westpac in relation to responsible lending, and provide an attestation that he or she has read and understood the bulletin and understands the requirements of the NCA and its regulations relating to the POS exemption, and that he or she is not aware of any breach of the NCA or its regulations.[62]

Changes to Sovereign to guide discussions

62. From September 2017, as a result of improvements to Westpac's origination platform, Sovereign, Dealer Business Managers are specifically required to complete mandatory fields in Sovereign which require the Dealer Business Manager to insert information about the customer's financial situation, including the customer's income, assets, liabilities, fixed expenses and monthly living expenses. [63]

63. Dealer Business Managers are now specifically required to complete the mandatory fields in Sovereign, which ask (among other things): (a) whether the customer is over the limit, in arrears or a hardship arrangement in respect of any of their fixed expenses; and (b) whether there are any special circumstances which might result in the customer having a higher than normal living expense when compared to the normal living expense for his or her household type.[64] The Dealer Business Manager is required to go through a line-by-line question as it pertains to expenses, which cannot default to zero.

64. In addition, undisclosed minimums are applied to certain fields, including in relation to rent and living expenses.[65] If the information entered by the Dealer Business Manager is too low, the application will be automatically referred to a credit officer for further inquiries of the Dealer Business Manager.[66] There are also a number of other questions the Dealer Business Manager is required to ask the customer that are specifically directed towards the satisfaction of Westpac's responsible lending obligations. [67]

Westpac's Responsible Lending Policy and Manual

65. In July 2017, Westpac updated its Responsible Lending Policy and Responsible Lending Policy Manual.[68] These documents set out minimum standards for responsible lending across the Westpac Group.[69] The responsible lending obligations apply to Westpac employees in the Credit Team and Settlements Team, who are involved in approving and settling loans. Westpac employees in those teams are required to undertake responsible lending training on an annual basis.

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[62] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [41] – [42], Ex 1.141.15 PG1-13 [WBC.100.009.2349].
[63] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [47] – [51].
[64] Ex 1.142 Godkin Case Study Statement [WBC.900.002.0001], [52(c)]. Mr Godkin gave evidence that those changes were "in manufacture" by February 2017: Transcript 21 March 2018 (P G Godkin) T:766:1-7.
[65] Transcript 21 March 2018 (P G Godkin) T:747:12-15
[66] Transcript 21 March 2018 (P G Godkin) T:747: 10-14; 770: 32-39; 776:22-27.
[67] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [47] – [51]; Transcript 21 March 2018 (P G Godkin) T:747: 10-14; 770: 32-39; 776:22-27.
[68] Ex 1.141.35 PG1-31 [WBC.300.055.7113]; Ex. PG1-C32 [WBC.300.057.1013]
[69] Ex 1.141 Godkin General Statement [WBC.900.001.0001], Annexure C, [2].

66. The Credit Team and Settlements Team review information obtained by the Dealer Business Manager in relation to the customer loan application. Where a loan is referred for manual credit review, the Credit Team performs a number of checks to assess the information obtained by the Dealer Business Manager against Westpac's credit policies, and also has the necessary training and experience to monitor compliance with responsible lending obligations. Further, the Settlements Team conducts a review of supporting documentation before the loan is settled. Documents are checked for verification purposes and for signs of fraud.[70] If any of the checks conducted by the Credit Team or the Settlements Team reveal inconsistencies or omissions, the application is returned through Sovereign to the Dealer Business Manager and the application does not proceed until the deficiencies identified have been addressed.

67. Part G of the Responsible Lending Policy Manual focuses on the need for controls to ensure information passed on by Dealers is reliable and accurate.[71] This is discussed in paragraph 57 above.

Improved verification processes

68. In February 2015, SGFL changed its benchmark from HPI to the State based HEM. HEM is a more nuanced measure of likely expenses that would be necessary to incur in order to avoid substantial hardship, taking into account, for example, whether the customer lives in a rural or suburban area. The HEM benchmark used by Westpac is subject to a number of adjustments made by Westpac (eg, the number of dependents can exceed three) and is scalable for income. The HEM benchmark used by Westpac was introduced into the calculation of a customer's serviceability, with the higher of the customer's declared expenses or the HEM benchmark being used for the purpose of calculating the customer's likely living expenses.[72]

69. A further change is that a new Income Verification Standard team is to be established which will be independent of the Credit or Settlements Teams. This is a change to current process which will facilitate the collection of income verification documents prior to settlement occurring. This team will manage all income verification for auto finance applications, and deal with both simple and complex proof of income processes.[73]

Hardship

70. In October 2016 the hardship processes, which had been carried out for Westpac by Collection House, were brought "in-house".[74] Westpac now undertakes earlier reviews of cases where customers are repeatedly in arrears over a long period, and takes a more proactive approach in proposing the option of applying for hardship to customers in appropriate situations. In addition, Westpac will soon implement a regime whereby cases in which a car loan customer's default on the first repayment date will be the subject of a review, including in relation to the circumstances of the

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[70] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [55] – [59] and [66] – [70].
[71] Ex 1.41.36 PG1-C32 [WBC.300.057.1013 at 1070].
[72] Ex 1.141 Godkin General Statement [WBC.900.001.0001]: Annexure C, [1(a)].
[73] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [73].
[74] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [109]

origination of the loan. Further, changes to monitoring are being scoped to produce reports where: (i) customers default on their first and second payments; (ii) a customer applies for hardship or is delinquent within the first 12 months; or (iii) a loan is written off directly within the first 12 months.

Sales Practice Quality Assurance monitoring

71. In February 2017, Westpac enhanced its sales practice quality assurance monitoring in respect of auto loans. [75] This involves the targeted review of approximately 300 loans settled in the previous month, focussing on customers with characteristics that give rise to a heightened risk that a car loan may be "unsuitable" for them. The purpose of the review is to ensure that the responsible lending requirements are being fulfilled at the point of sale. [76] The results of that monitoring are set out in a monthly report, along with its comments and recommendations.

72. By way of example, the recommendations may include requesting further information from a Dealer, providing a Dealer Business Manager with further training, or recommending a review of credit policies and processes.[77] In addition, monthly quality assurance monitoring is conducted over Dealer Call Reports, to ensure that Westpac's Relationship Managers are carrying out any risk related phone calls with Dealer Business Managers and that those discussions are being properly recorded.[78]

Credit review monitoring

73. In September 2016, Westpac established the Credit Quality & Assurance Team, which is responsible for conducting monitoring over the car loan application and assessment process. [79] Each month, the Credit Quality & Assurance Team conducts a review of between 100-150 files focussing on the practices of Dealers in making inquiries and appropriate judgments about the customer's requirements and objectives and the customer's financial situation.

Settlements Team monitoring

74. Under Westpac's current policies and processes a quality assurance check of between 3% and 9% of applications settled per month is undertaken by the Settlements Team during the compliance check processes, which include income verification checks.[80] The expected rate of the quality assurance result is that at least 97% of the files reviewed are assessed as satisfactory. The aim of this ongoing quality assurance is to detect errors, and to identify and measure systemic issues and training needs.[81]

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[75] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [89] – [96].
[76] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [89] – [96].
[77] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [89] – [94], Ex 1.141.23 PG1-22 [WBC.100.009.4848].
[78] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [95].
[79] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [100].
[80] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [52(e), (f)].
[81] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [104].

75. There are also additional controls to detect oversights which may have occurred in the verification of applications. This includes the reviews by the Credit Quality Assurance Team and sales practice quality assurance monitoring.

Customer call monitoring

76. In 2017, Westpac implemented a new customer call monitoring practice in NSW whereby, each month, the Westpac Auto Finance Business selects 200 files from selected Dealer groups and the top 5 commission-earning Dealers in NSW and an external provider conducts a survey of 50 customers, focussing on key compliance and disclosure items.[82] Call monitoring is an important tool to identify potential issues with the loan application assessment and approval process as a whole, and is therefore of indirect benefit to all of Westpac's auto finance customers. Customer call monitoring will be rolled out to other States and Territories this year.[83]

Fraud monitoring

77. The Equifax Fraud Check and the Lorica Fraud Detection platforms generate fraud alerts relating to the Westpac Group as a whole which are reviewed by the Risk & Fraud Operations team. Those transactions which have been identified as suspicious are actioned in accordance with the Westpac Group's "Incident Management Procedures and Guidelines".

Complaint monitoring

78. The Customer Advocacy Group within the Westpac Auto Finance Business track and review all customer complaints. More specifically, the Customer Advocacy Group is responsible for:

    a. analysing complaints to determine their root cause, trends and areas of focus;

    b. allocating action items to the relevant business units; and

    c. assisting to resolve customer complaints.

79. Where the complaints relate to the conduct or practices of a Dealer Business Manager, they are referred to the Auto Finance Quality Assurance Team and addressed appropriately, for example, by providing feedback to the Dealer Business Manager or, in more serious cases, following the Third Party Consequence Management Framework in relation to further actions to be taken against the relevant Dealer Business Manager. [84]

Consequence Management Framework

80. In September 2017, the Westpac Auto Finance Business established the Consequence Management Framework, which governs the approach of Westpac's Specialist Finance business (which includes

[82] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [97]-[99], Ex 1.141.24 PG1-23 [WBC.103.041.9072], Ex 1.141.25 PG1-24 [WBC.300.055.8250].
[83] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [97] – [99].
[84] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [106] – [107].

the Westpac Auto Finance Business) to the control of third party intermediaries. [85] The Consequence Management Framework sets out the approach of Specialist Finance to any failures by third parties to meet specified objectives in managing its relationship with third party intermediaries, including that:

a. third parties are accredited before acting as a representative of the Westpac Group;

b. there is training and support in place to help third parties be successful in their role;

c. third parties have agreed to their obligations as part of their agreement with the Westpac Group and by completing the required training and accreditation.

d. third parties understand and adhere to the obligations and standards expected of them;

e. corrective action is taken where minimum standards have not been met; and

f. consequences are applied in event of failures or breaches.[86]

F. PROPOSALS FOR REFORM

81. The inherent problem, given the Dealer's position, is the Dealer's discretion to determine interest rates or make decisions that ultimately have an effect on their commission. As Michael Saadat said in his statement "flex commissions create distortions in the cost of finance in a way that is more likely to disadvantage financially vulnerable consumers."[87] ASIC's objective in addressing flex commissions has been to seek comprehensive changes across the entire car finance industry where this form of remuneration was prevalent.[88] Mr Saadat also said in his statement that "car dealers had concerns about the impact of the prohibition on their financial viability. While its [ASIC's] primary concern was to address the consumer harm caused by flex commissions, ASIC recognised the need to understand the potential effect on car dealers before making a final decision."[89]

82. Westpac accepts that customer outcomes would be improved if more accurate and comprehensive information could be obtained relating to a customer's financial situation. Comprehensive credit reporting[90] and the proposed open banking regime[91] will provide greater opportunities for credit providers to access and verify information relevant to the credit assessment. This topic is addressed in more detail in Westpac's Credit Card Limit Submissions.

83. Westpac notes that any changes to the POS exemption would represent a major shift for the industry. While Westpac sees benefits to the consumer in this removal, any consideration of this reform should take into account the impacts to all stake holders.

84. Westpac believes that financiers should in any regulatory framework continue to take responsibility for origination of all loans that are financed using their balance sheet.

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[85] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [112] – [116], Ex 1.141.30 PG1-27 [WBC.103.041.9066], Ex 1.141.31 PG1-28 [WBC.103.053.1037], Ex 1.141.34 PG1-30 [WBC.100.009.4568].
[86] Ex 1.141 Godkin General Statement [WBC.900.001.0001], [112] – [116].
[87] Ex 1.158, Statement of Michael Saadat [WIT.0001.0003.0001], at [16]
[88] Ex 1.158, Statement of Michael Saadat [WIT.0001.0003.0001], at [23]
[89] Ex 1.158, Statement of Michael Saadat [WIT.0001.0003.0001], at [37]
[90] https://treasury.gov.au/consultation/c2018-t256276/
[91] See the Report on behalf of Treasury by Mr Scott Farrell, https://static.treasury.gov.au/uploads/sites/1/2018/02/Review-into-Open-Banking-_For-web-1.pdf.

85. Westpac believes that as an industry there needs to be commitment to developing a payment and commission arrangement which meets the following key principles:

a. Minimise conflicts of interest

i. The industry should seek to minimise conflicts of interest in relation to the financing of cars in the car sales process.

ii. To that end a prohibition on flex commissions should be introduced to comprehensively eliminate the nexus between customer rate outcomes and dealer commissions.

b. Minimise the potential for cross subsidisation between customers

i. With the prohibition of flex commissions, credit providers should create risk based pricing solutions to address this.[92]

c. Provide sustainable commission for services provided

i. Introduce a structure which recognises the value dealers provide for customer and credit providers in the loan origination and establishment.

ii. There should be no nexus between amounts paid as commission and the customer rate.

d. Provide transparency on fees and costs charged to customer

i. The current law should be strengthened so that fees, costs and any dealer commission from the lender should be disclosed at the time the loan contract is entered into, and if the amount is uncertain then the basis for calculation should be disclosed.

ii. Disclosure should occur preferably at the time of the loan application or at the time of the loan contract, at the latest, and in a manner which gives it appropriate prominence.

e. Provide a level playing field for industry change

i. Change should be structured so that it can be consistently applied across the industry.

[92] Risk based pricing occurs where lenders offer consumers different interest rates or loan terms on the basis of the risk that the consumer will fail to pay back the loan. For example, a consumer with a low risk of default may be offered a lower interest rate to a consumer who has a higher risk of default.

ANNEXURE A:

PROPOSED FACTUAL FINDINGS IN RELATION TO MS THIRUVANGADAM'S LOAN

Background

1. At the time that Ms Thiruvangadam applied for the loan, she had two children[93] and worked as a personal care attendant.[94] Ms Thiruvangadam also received a Centrelink allowance.[95] Over the course of six months, Ms Thiruvangadam approached a number of lenders and car dealers in relation to a car loan but not been able to obtain a loan, apparently because of her credit history.[96] It was important to Ms Thiruvangadam to obtain a new car, because her then current vehicle was unreliable and she needed a car for family and work purposes.[97]

Entry into the car loan with the Dealer Business Manager

2. Ms Thiruvangadam found the Dealership on the internet. Ms Thiruvangadam said she called the Dealership and was put through to the Dealer Business Manager.[98] She gave evidence that she explained to the Dealer Business Manager that she was having difficulty in obtaining a loan, but says the Dealer Business Manager assured her that he would be able to arrange a loan if she came to the Dealership.[99]

3. Ms Thiruvangadam gave evidence that when she arrived at the Dealership, the Dealer Business Manager asked her a series of questions and appeared to complete an application for a loan. Ms Thiruvangadam said she gave him information about her financial position, including about her income, that she owed about $1,500 on a credit card and that she currently paid about $1,300 per month in rent.[100]

4. Ms Thiruvangadam gave evidence that she was at the Dealership for a long time and well after closing time.[101] During that time, she said she was taken for a test drive by another member of staff at the Dealership.[102]

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[93] Only one of whom she appears to have classed as a dependent: Ex 1.142.4 PG2-4 [WBC.300.001.0027 at .0028; .0044]; Ex 138.2 [RCD.0014.0003.0003]. In relation to Ex 1.142, it should be noted that the pages are not in correct order: the Finance Application pages 1 and 2 are .0026 and .0033 respectively; and the Privacy Act authorisation pages 1 and 2 are .0031 and .0030 respectively.
[94] Transcript 21 March 2018 (N D Thiruvangadam) T:719: 27; Ex 1.138 Witness Statement of Ms Thiruvangadam dated 5 March 2018 (**Thiruvangadam Statement**) [WIT.0001.0012.0001]: [4], [12].
[95] Transcript 21 March 2018 (N D Thiruvangadam) T:719: 29 - 34; Ex 1.138 Thiruvangadam Statement [WIT.0001.0012.0001]: [4].
[96] Transcript 21 March 2018 (N D Thiruvangadam) T:718: 9-14.
[97] Transcript 21 March 2018 (N D Thiruvangadam) T:717:38-45; Ex 1.138 Thiruvangadam Statement [WIT.0001.0012.0001]: [11].
[98] Transcript 21 March 2018 (N D Thiruvangadam) T:718:35-47; Ex 1.138 Thiruvangadam Statement [WIT.0001.0012.0001]: [11].
[99] Transcript 21 March 2018 (N D Thiruvangadam) T:719:1-2; Ex 1.138 Thiruvangadam Statement [WIT.0001.0012.0001]: [11].
[100] Transcript 21 March 2018 (N D Thiruvangadam) T:719: 17-21, 720:1-9, 19-23; Ex 1.138 Thiruvangadam Statement [WIT.0001.0012.0001]: [13].
[101] Transcript 21 March 2018 (N D Thiruvangadam) T:722 – 20-24.
[102] Transcript 21 March 2018 (N D Thiruvangadam) T:721:40-44.

5. Finally, the Dealer Business Manager asked Ms Thiruvangadam to sign a series of documents, including the loan documents, which she said he did not explain.[103] The documents signed by Ms Thiruvangadam on 26 July 2012 included a contract for the purchase of a demonstrator vehicle,[104] a Finance Application with SGFL,[105] a direct debit request,[106] and a Fixed Rate Loan Agreement.[107] Ms Thiruvangadam said she had no time to read the documents before she signed them.[108]

6. Ms Thiruvangadam said in evidence in chief that her call to the Dealership and her visit occurred on the same day. However, in re-examination she was asked whether it was possible that she might have spoken to the Dealership on the phone a day or two before she visited. Initially, Ms Thiruvangadam said that was correct, but then said she does not remember.[109]

7. Westpac's records indicate that Ms Thiruvangadam's application was first submitted on 24 July 2012.[110] It is noted that her signed privacy consent is dated 23 July 2012.[111]

Contact with the Dealer Business Manager the next day

8. Ms Thiruvangadam said that having reviewed the documents provided to her by the Dealer Business Manager overnight, she called the Dealership the next morning and explained that she no longer wanted the car. Ms Thiruvangadam says that the Dealer Business Manager said that she had already bought the car and had signed the documents and that she had to accept it.[112] Westpac was not made aware of this request to the Dealership.

9. Pursuant to the Dealer Agreement, Dealers were in 2012, and are still, required to notify Westpac of any request by a customer to withdraw any credit offer, and of any complaints made by or on behalf of a customer in connection with the purchase of the car.[113] At that time, the Dealer Business Manager was required to, but did not, bring this request to SGFL's attention.

10. When Dealers contact Westpac to advise that a customer has requested to withdraw from a credit contract, it is Westpac's practice to offer customers the option of "flat cancelling" their loans in circumstances such as where the structure or frequency of the loan repayments is not what the customer expected or where the customer is dissatisfied with the vehicle or the loan.[114]

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[103] Transcript 21 March 2018 (N D Thiruvangadam) T:720:11-4, 721:7-26.
[104] Ex 1.138.4 NDT-4 [RCD.0014.0003.0006].
[105] Ex 1.142.4 PG2-4 [WBC.300.001.0027 at .0033].
[106] Ex 1.142.4 PG2-4 [WBC.300.001.0027 at .0041].
[107] Ex 1.142.4 PG2-4 [WBC.300.001.0027 at .0046].
[108] Transcript 21 March 2018 (N D Thiruvangadam) T:721:10-12.
[109] Transcript 21 March 2018 (N D Thiruvangadam) T:729:15-17.
[110] Ex 1.139 - WBC.104.003.7572_R at 7572.
[111] Ex 1.142.4 PG2-4 [WBC.300.001.0027 at 0030].
[112] Transcript 21 March 2018 (N D Thiruvangadam) T:722:27-30.
[113] Ex 1.142, Godkin Case Study Statement [WBC.900.002.0001], [20].
[114] Ex 1.142, Godkin Case Study Statement [WBC.900.002.0001], [21].

Assessment and approval of Ms Thiruvangadam's car loan application

11. The process in place for the assessment and approval of car loans by SGFL in 2012 is described by Mr Godkin in his two statements.[115] The process that was followed in relation to Ms Thiruvangadam's car loan application is set out below.

12. The application was referred to the Credit Team for manual credit review. [116]

13. The application was conditionally approved on 25 July 2012 subject to evidence being provided of payment of the debt to Axess Debt Management Pty Ltd.[117]

14. The application was resubmitted on 26 July 2012[118] and re-approved. The application appears to have been re-submitted due to changes in the loan amount and in the description of the vehicle to be purchased.[119]

15. On 30 July 2012 the application was "approved as submitted".[120] Mr Godkin gave evidence that "approved as submitted" should be read as indicating that the condition (referred to in paragraph 13) had been met.[121]

Verification of the loan application

16. On 30 July 2012, Ms Thiruvangadam's loan application was forwarded to the Settlements Team, with the following supporting documents:

    a. a Medicare card;

    b. a Driver's Licence; and

    c. a payslip for the period 19 March 2012 to 1 April 2012, which recorded net pay for that fortnight of $447.89 and YTD pay of $889.38, and described Ms Thiruvangadam as a casual employee.[122]

17. Ms Thiruvangadam's income was verified "at branch" on 30 July 2012.[123] This means that income information was verified by the Credit Team, before the application was directed to the Settlements Team.

18. Mr Godkin gave evidence about the verification of Ms Thiruvangadam's loan application by reference to material available to him on the files held by Westpac, being the documents held on Westpac's

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[115] Ex 1.142 Godkin Case Study Statement [WBC.900.002.0001 at 0002, 0003]; Ex 1.141 Godkin General Statement [WBC.900.001.0001 at 0006 – 0016].
[116] Ex 1.142 Godkin Case Study Statement [WBC.900.002.0001, [15].
[117] This is recorded in the screenshot of Westpac's auto finance origination system, Sovereign, Ex 1.139 [WBC.104.003.7572 at 7573]. The person who approved the loan was identified by Mr Godkin during his oral evidence by reference to the screen shot: Transcript 21 March 2018 (P G Godkin) T:790:15-17; Ex 1.139 [WBC.104.003.7572_R at 7573].
[118] This is recorded in the Sovereign screenshot, Ex 1.139 [WBC.104.003.7572_R at 7572]. The persons who re-approved the loan are also identified in the screenshot.
[119] This is recorded in the Sovereign screenshot, Ex 1.139 [WBC.104.003.7572_R at 7576].
[120] Transcript 21 March 2018 (P G Godkin) T:739:35.
[121] Transcript 21 March 2018 (P G Godkin) T:739:40-44.
[122] Ex 1.142.4 PG2-4 [WBC.300.001.0027 at 0038 – 0040].
[123] The expression "poi at branch" is used in the Sovereign screenshot, Ex 1.139 [WBC.104.003.7572 at 7575].

auto finance origination system, Sovereign.[124] According to these documents, Ms Thiruvangadam's loan application was verified by reference to the information referred to in paragraph 16 above. According to Mr Godkin's evidence,[125] it is possible that other documents were available to the Credit Team at the time of verifying Ms Thiruvangadam's financial situation, but were not uploaded to Sovereign. However, given the state of the evidence this remains only a possibility.

19. Ms Thiruvangadam's loan was settled by the Settlements Team on 30 July 2012. The loan provided was a Fixed Rate Loan of $23,643.31 with fortnightly payments of $259.75 over 60 months at an interest rate of 14.6% per annum, made for the purpose of purchasing a Ford Focus Ambiente. The amount financed included the vehicle price, an establishment fee of $375, the dealer origination fee of $465.91 and a premium of $1,295 for a "shortfall" insurance policy for the term of the loan.[126]

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[124] Transcript 21 March 2018 (P G Godkin) T:737:1-33.
[125] Transcript 21 March 2018 (P G Godkin) T:737:17 -22.
[126] Godkin Case Study Statement [WBC.900.002.0001], [14]; Ex 1.142.4 PG2-4 [WBC.300.001.0027].