

Article Information

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Westpac wins responsible lending case against ASIC

Westpac has won against ASIC in a responsible lending case.

Our [previous newsletters](#) have discussed the significant Westpac and ASIC case where ASIC alleged that Westpac had breached the *National Consumer Credit Protection Act 2009* (Cth) (**NCCP Act**) by engaging in irresponsible lending. On 13 August 2019, Justice Perram of the Federal Court dismissed ASIC's case, finding that Westpac did have regard to declared living expenses when using its automated decision system.^[1]

In summary, the main findings of the case are:

1. the NCCP Act requires lenders to make reasonable inquiries about their customer's financial situation, which Westpac had done
2. the NCCP Act requires lenders not to provide loans that would result in a consumer being unable to comply with the loan obligations, or could only meet them with substantial hardship, and the assessment under s 129 must be directed towards that question
3. ASIC offered no evidence that any Westpac customers either defaulted or suffered substantial hardship in avoiding default; and
4. the adequacy of HEM was an irrelevant issue, as s 129 does not require a lender to use the consumer's actual or declared living expenses in assessing their capacity to meet obligations under the credit contract.

In 2017, ASIC commenced proceedings in the Federal Court against Westpac, alleging that it had breached responsible lending laws more than 261,987 times between 2011 and 2015.^[2] ASIC alleged that Westpac's use of the HEM Benchmark (**HEM**), which did not accurately reflect their expenses, instead of the customers' declared living expenses in a serviceability calculation in the loan assessment process caused Westpac to breach its obligation under s 129 to assess whether or not the credit contract will be unsuitable (in the 'unable to comply or could only comply with substantial hardship' sense).

On 4 September 2018, ASIC and Westpac reached a settlement where the bank would pay a \$35 million civil penalty for the alleged breaches of responsible lending laws. However, in mid-November Perram J did not approve the agreed order as the statement of agreed facts did not disclose any contravention of s 128 of the NCCP Act.

On 13 August 2019, the Federal Court dismissed ASIC's case against Westpac and ordered it to pay Westpac's costs.^[3] Perram J rejected ASIC's first allegation that Westpac breached the NCCP Act on 261,987 occurrences by not using the consumer's declared living expenses in answering the questions under s 131(2)(a) of the NCCP Act as the allegation failed on both facts and statutory construction.^[4] Furthermore, Perram J rejected ASIC's second allegation that Westpac breached the NCCP Act in calculating repayments on interest free loans based on the interest only period, as it is impossible to determine future repayments on a variable rate loan due to the potential for the interest rate to change over the term of the loan - whether the loan is interest-only, principal-and-interest or a combination of the two.^[5]

Living expenses

One of the most pertinent aspects of Perram J's judgment was in regards to assessment obligation under ss 128(c) and 129. Perram J held that those sections of the NCCP Act require a credit provider only to ask whether the consumer will not be able to comply with the financial obligations outlined in the contract or whether consumers could only comply with substantial hardship.^[6] They do not impose a quality or accuracy requirement on the assessment; merely considering and evaluating the s 131(2) criteria for assessing unsuitability is sufficient.^[7]

A customer's declared living expenses were held not to be required to be taken into account in all cases, as the mere fact that they are characterised as living expenses did not make them relevant to the s 131(2)(a) criteria for unsuitability. Living expenses are only relevant if they cannot be reduced forgone or reduced beyond a fixed minimum.^[8]

To conceptualise this argument, Perram J gave the widely reported example of a consumer who consumes "Wagyu beef washed down with the finest shiraz" on a daily basis – if they have a desire to obtain a new home they could survive on more modest food without suffering substantial hardship.^[9] The fact that such expenditure is characterised as expenditure on "food" does not require it to be taken into account in determining whether or not the credit contract will be unsuitable. Whilst an extreme example, it illustrates the point that unsuitability can be assessed on the assumption consumer can be expected to compromise their lifestyle to some extent in order to be able to afford to repay a loan.

Perram J also held that ASIC's case failed on the facts. Whilst Westpac used the HEM value instead of a consumer's declared living expenses in the 'serviceability rule' element of its automated credit decision system, it used a consumer's declared living expenses in the '70% ratio rule' element of that system.^[10]

Interest only loans

Another significant aspect of the case was ASIC's allegation that Westpac had not made the assessment required by ss 128(c) and 129 in respect of loans with an initial interest-only period because, in its serviceability calculation, it included a value for repayments calculated as if the principal had amortised from the commencement of the loan rather than the expiry of the interest-only period.^[11] Perram J rejected ASIC's argument on the basis that Westpac's only obligation under ss 128(c) and 129 was to assess the s 131(2) criteria for unsuitability.^[12]

Perram J argued that this part of the regulator's case could be "readily dispatched" as the interest is variable and it is not possible to ascertain what the repayments will be at the end of the interest-only period.^[13]

ASIC argued that Westpac had failed to take into account the consumer's financial situation as the repayments the consumer would actually be required to make after the expiry of interest-only period were not the ones Westpac had used in its assessment. Perram J found this argument to be "self-defeating" because, if Westpac had used the payments expected to be payable following expiry of the interest-only period, it would be arguable that Westpac failed to take into account the consumer's financial situation at the commencement of the loan and during the interest-only period.^[14]

Evidently, this decision will have lasting ramifications on how lenders assess loan applications, unless the NCCP Act is amended. Despite initially being willing to settle for \$35 million on a statement of agreed facts that did not disclose any contravention of the NCCP Act, ASIC in a media release explained that this was a 'test case' which tested the ambit of responsible lending laws.^[15] After their careful consideration of the judgment, whether the corporate regulator will appeal the decision, or whether they will push for an amendment of responsible lending laws will be interesting to observe.

^[1] Australian Securities and Investments Commission v Westpac Banking Corporation (Liability Trial) [2019] FCA 1244 ('ASIC v Westpac') [2].

^[2] Ibid [6].

^[3] Ibid.

^[4] Ibid [6].

^[5] Ibid [98].

^[6] Ibid [3].

^[7] Ibid [87]-[92]. The quality and accuracy of the assessment are dealt with by the obligation in s 133 to not enter into an unsuitable contract with a consumer.

^[8] Ibid [75]-[76].

^[9] Ibid.

^[10] Ibid [21]-[27].

^[11] Ibid [8].

^[12] Ibid [3].

^[13] Ibid [98].

^[14] Ibid [99].

^[15] ASIC, '19-210MR ASIC's responsible lending case dismissed by Federal Court' (Media release, 13 August 2019).