Australian Royal Commission themes

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The FMA and RBNZ have requested New Zealand banks to demonstrate that 'what is happening in Australia, in relation to the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry ('the Commission'), is not happening in New Zealand.'

KPMG have previously analysed the outcomes of the first two phases of the Commission hearings to date, which focused on consumer lending and financial advice, and identified the key themes and findings that New Zealand banks may be expected to report on to the regulator. Our latest update focuses on the two most recent hearings, which covered Small and Medium Enterprises ('SME') and lending for Rural communities.

Round 3 – SME lending

The third round of hearings considered the conduct of financial services entities in respect of their dealings with SMEs, in particular in providing credit to businesses. The hearings explored the current legal and regulatory regimes, as well as self-regulation under the Code of Banking Practice. During the hearings four key themes emerged:

Theme	Findings
Responsible lending	— The Commission heard commentary on the quality of underwriting on SME lending. In particular, the rigour, skill and care taken in assessments of SME business plans was called out as an area of concern. The hearing identified instances of boilerplate plans being used, with unrealistic or overoptimistic growth and income estimates failing to be challenged. — A focus on lending growth over lending quality, driven by incentives schemes where key performance indicators (KPIs) were linked to volume-driven financial targets rather than outcomes-driven.
Lender errors and timely customer rectification	— Cases were identified whereby banks were slow to correct errors in their own systems. In one case, a system error caused overdraft interest rates to be doubled. This error turned out to be critical to some customers' personal circumstances. — In one of the instances above, remediation took 960 days from the time when the issue started, and took 240 days to rectify at the point the issue was found.
Management of customers in financial distress	— Some hearings raised instances of a lack of clarity in disclosure of terms to customers, particularly in the approach to foreclosure and the repossession or required sale of assets, and who pays the costs for this process. — Other issues included truncated timeframes for responding to and repaying costs incurred by lenders where default events had occurred. — Finally, the Commission heard challenge over how sophisticated and well-resourced SME customers should be expected to be in their dealings with banks. The question was raised on what the right balance is between banks being able to exercise their contractual rights to protect their interests and those of their shareholders and creditors, and their promise to act fairly and reasonably towards an SME in a consistent and ethical manner.
Systems and controls	— The Commission was provided with details of a lack of maturity in lender systems and controls for identifying and managing incidents of misconduct on different systems in different business units, with an inability to aggregate these for root cause analysis and investigation purposes.

Round 4 – Financial services for Rural communities

The fourth round of public hearings focused on issues affecting Australians who live in remote and regional communities, which related to farming finance, and interactions between Aboriginal and Torres Strait Islander people and financial services entities. During the hearings four key themes emerged:

Theme	Findings
Suitability of product and advice	— Unsuitable products being provided to customers, with some linkage to incentivisation of sales for a particular product. — Poor recording of customer sales and the rationales for these. — Issues over vulnerable customers – the elderly and customers without sufficient financial literacy being provided unsuitable products.
Clarity of disclosure and communication	— Conflicts over whether loans are serviceable between lenders and customers failing to be addressed. — Failure to provide valuations to clients that would have prompted earlier resolution and remediation.
Responsible lending	— Contradictions in lenders providing supplementary loans to customers whilst disagreeing with their business model and serviceability. — In one instance, a bank manager preparing significant portions of financial projections on behalf of the borrower, bringing into question the veracity of those projections to support quality lending. — Provision and use of incorrect valuations to justify lending, including some that were artificially inflated.
Management of customers in financial distress	The Commission heard instances of: — Delaying a legitimate option of a manual payment which ended up being critical to customer outcomes, including the sale of livestock and land to service a technical default. — Absence of mediation between customers and lenders to achieve better outcomes for both parties. — Failing to take into account distressing personal circumstances (e.g. cancer diagnosis, home and business assets interlinked) when pursuing foreclosure.

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