

Submission

AFCA's Approach to Appropriate Lending to Small Business

September 2023

**Commercial & Asset Finance
Brokers Association of Australia**

Prepared September 2023



Commercial & Asset Finance Brokers
Association of Australia

Lead Ombudsman – Small Business & Transactions
Australian Financial Complaints Authority
GPO Box 3
Melbourne VIC 3001

29 September 2023

By email: consultation@afca.org.au

RE: AFCA Approach to Appropriate Lending to Small Business

The Commercial & Asset Finance Brokers Association of Australia Limited (CAFBA) is a strong voice for issues within the commercial finance sector, and we welcome the opportunity to submit our commentary to AFCA regarding its approach to lending to small business. CAFBA members are professional commercial finance brokers committed to providing the best quality service to our business clients. Through this submission, our members are keen to make you aware of the intricacies of small business lending whilst adhering to best industry practice in assisting small business the crucial access to finance and obtaining business credit.

The CAFBA board members, staff, and our members are pleased to continue working with AFCA and are willing to make ourselves available to assist you with the development of final recommendations.

CAFBA would also like to commend and support the submission of the MFAA. Many of our members belong to both associations depending on their activities. CAFBA supports a unified approach on appropriate lending to small business and agrees with the conclusions of the MFAA.

Yours sincerely,



David Gandolfo, OAM
Advocacy Chair

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Matthew Atkin CAFBA
CAFBA President

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Background on CAFBA

CAFBA is the industry association for professional commercial finance brokers in Australia, whose prime area of business is the distribution of commercial finance facilities to their clients. Our members include over 1,200 firms and brokers nationwide and our affiliate members are represented by Australia's major finance providers.

CAFBA works on behalf of our members to promote and encourage policies that advance the commercial finance industry and access to finance in Australia through government and legislative lobbying, education, and professional development.

In 2020, CAFBA commissioned East & Partners, a global leading banking and business advisory firm, to undertake a Broker Channel Analysis in the Australian Asset and Equipment Finance Markets. The research concluded that 72% of new commercial equipment finance is sourced through commercial brokers, up from 64% in 2017.

CAFBA is a member of the Council of Small Business Organisations of Australia ("COSBOA") and The Australian Finance Industry Association ("AFIA").

CAFBA members know that providing Australian small businesses with access to finance is crucial to economic growth. Although brokers are commonly associated with home loans, CAFBA members work in a complex environment to provide a boutique service. Without the work of CAFBA's professional members, many Australian small business owners would struggle to navigate the complexities involved with commercial and equipment finance.

CAFBA embodies the strengths of its members in a unified approach for dealing with financiers and legislators at a national level and regularly seeks the views of members. As an association, CAFBA provides the framework and support to professionally assist our members in their daily activities. This involves education and training, legislative and regulatory updates and forums where the members can interact and exchange ideas with their peers.

CAFBA prides itself on being self-regulating and maintains strict membership standards on probity, continuing professional development, industry experience, and reputation. It is a condition of CAFBA membership that commercial finance brokers must belong to AFCA.

Preface

CAFBA for many years has made the distinction to both government and regulators of the significant differences between consumer and business finance, as they are completely different markets with different customers and required outcomes. We are pleased that this difference is well understood.

CAFBA welcomes the approach on how AFCA will assess whether credit was appropriately provided when considering small business lending complaints, which include:

- the types of small business complaints AFCA can consider under AFCA's Rules
- how AFCA assesses if a financial firm's credit assessment was appropriate
- how AFCA considers industry codes, regulatory guidance and good industry practice in its decision making
- how AFCA determines a fair outcome where a firm has provided an inappropriate loan, and
- how AFCA calculates loss and determines how much compensation should be paid.

Recommendations

CAFBA agrees the approach that AFCA will utilize when reviewing a firm's decision and have regard to:

- the financial firm's obligations at the time of the decision.
- information that was reasonably available at the time, including resources available.
- if the financial firm should have known information or sought further information.
- the financial firms lending policies at the time.

We do however request that AFCA recognizes that our members and many lenders are voluntary AFCA members. There are of course many small business lenders who are **not** AFCA members and AFCA can only consider complaints against financial firms that are CAFBA members.

This has the effect of unfairly targeting AFCA members. If a CAFBA member introduces a transaction to a financial firm that is not an AFCA member, then often the complainant will make that complaint against the AFCA member even though no fault is attributed.

This of course acts as a disincentive for smaller financial lenders belonging to AFCA. This should be an important consideration when considering a complaint against a commercial broker where the lender is not an AFCA member, and whether the complaint against the broker is legitimate in the circumstances.

We note that on page 40 of the Approach, AFCA states that it may join other parties (including brokers) to a complaint where that party has contributed to the loss.

Again, this has the potential for a joinder between the broker and small business lender, or where the small business lender is not an AFCA member and so the complaint is instead made against the broker. With respect to complaints where the broker is an AFCA member, but the lender is not, it is not appropriate for AFCA to allow such a complaint to proceed simply because the only avenue for AFCA to facilitate the complainant is against the broker.

The AFCA member should never be the "soft target".

Additionally, there should be no compensation for fraud or fault. Where a complainant has been found to be complicit in these activities, then AFCA should immediately dismiss the complaint.

Small business lending is more complex than consumer lending, with varying products available that may equally suit client's needs. AFCA's approach must be cognizant of this and understand the nuances of small business lending, maintaining a balance.

The requirements of the borrower need to be considered in any assessment eg a contractor may require an item of equipment urgently to meet the requirements of a particular project. Therefore, the expediency of the credit approval may outweigh the cost of capital. There are many factors that influence the choice of loan product.

Consideration also needs to be given to the size of the loan. Less information may be sought for a small ticket loan (eg laptop computer) than a higher cost item.

Conclusion

CAFBA broadly agrees with AFCA's approach to considering appropriate lending to small business. Our members are diligent in their assessment of borrower's requirements, but often can be targeted by complainants due to their AFCA membership where no other option is available.

CAFBA members are small businesses in their own right and any unfair complaint is costly and time consuming.

We strongly request AFCA to consider this in any determination.

For further discussion please contact

David Gandolfo OAM on [REDACTED], or at [REDACTED]

Appendix

Stakeholder Questions

1. *Do you have any comments about our proposed approach to assess whether a small business loan is appropriate?*

As discussed in our submission a commercial loan can be complex and will rely on numerous factors. Situations and circumstances will greatly influence the type of loan, term, etc and may be suitable at the time of approval, however changing circumstances will affect the suitability going forward. Being too prescriptive in the assessment may stymie the access to finance for small business, which is needed for growth.

Any retrospective review always has the benefit of hindsight and should therefore be balanced with the circumstances and information available at the time of approval. For instance the notion of “prospect for success” is difficult for a lender when other considerations may be at play.

2. *Do you have any comments about the non-exhaustive list of factors on page 19 that we may consider were appropriate for a financial firm to obtain or consider during their lending assessment?*

The point is made that the loan purpose (eg credit card or commercial property) will be considered when taking into account the list of factors, however the list is quite exhaustive and a considerable amount of subjectivity would need to be employed as to when any of these factors are taken into consideration. Commercial finance needs to be flexible and not too prescriptive to allow good credit decisions. The assumption is all this information would be readily available which is not always possible.

3. *Do you have any comments about the list of common warning signs on page 24 that AFCA may consider should prompt a financial firm to make further inquiries during the credit assessment process?*

Many of these questions will depend on the loan type, size, and purpose. They are useful reminders to any lender but may not be suitable when assessing all loans. As stated in hindsight they may appear relevant, but any assessment should be based on the circumstances at the time. Further information would be helpful on when AFCA would consider these warning signs in assessing a complaint.

4. *Do you have any comment about our proposed approach to calculating loss and determining fair outcomes?*

AFCA’s role is important to the continuing protection of small business; however, it is CAFBA’s view that the legislation is heavily weighted towards the complainant. Whilst vexatious complaints are discouraged, anecdotally there seems to be a financial incentive available to making a complaint, as there are no associated pecuniary costs if the complaint is not upheld. The costs for any complaint are borne by the AFCA member.

We have had many instances of member feedback that whilst the complaint has eventually been determined in favour of the AFCA member, it has nevertheless come at considerable cost to the member in time and legal advice (and mental stress). Whilst we appreciate there is discretion under the rules for vexatious complaints where there is no loss to the complainant, nevertheless there is still a cost borne by the member to defend the complaint and prove innocence. There is also no right of appeal, which denies natural justice to the member.

The issue for CAFBA members, as commercial brokers who introduce loans to lenders is exacerbated by the fact that not all lenders are AFCA members. Therefore, if the lender does not belong to AFCA the complaint is subsequently lodged against the broker, where the issue really should rest with the lender. This makes the commercial broker an “easy target” for complaints, particularly as there are no associated costs for the complainant.

It is CAFBA's view therefore, that whilst we support the complaint process, there should be a sharing of costs where complaints are made. At present there is really a disincentive to belong to AFCA due to the unfair apportionment of costs involved.

5. *Do you have any comments about the examples provided in the Approach? Are there any other examples you would like to see in the Approach?*

We would like to draw from real life examples of our members to assist in the formulation of the Approach, which can be provided on your advice.

6. *Do you have any comments about the use of the phrase "appropriate lending" as a description of the standard to be applied for small business lending?*

We are comfortable with this term.

7. *Do you have any other feedback about changes that could be made to the draft Approach to better achieve our objectives?*

The Approach is very detailed and quite prescriptive; however, any assessment needs to have flexibility and be cognisant of the loan purpose and information available at the time of assessment. We would welcome the opportunity to address this at a stakeholder roundtable.