



Fairer banking for small business

2017 has been a major year for Australia's big banks with reviews, parliamentary inquiries, talk of royal commissions, and media exposés. As a result, things are changing for small business with banks committing to better behaviour towards their small business customers. Here's a summary of the situation to date.

Inquiry into Australian bank lending practices

On 31 August 2016, the federal Minister for Small Business, the Hon Michael McCormack commissioned the Australian Small Business and Family Enterprise Ombudsman (ASBFEO), Kate Carnell to review the small business lending practices of Australia's major banks and other lenders.

The findings of the ASBFEO Business Loans Inquiry were detailed in a comprehensive report delivered to government, and publically released in February 2017.

This Inquiry considered the submissions of 23 affected bank customers, and included an intensive forensic analysis of six of those submissions.

The ASBFEO found that a third of the cases considered were the result of poor business decisions by the small business owner, another third were the result of both poor business decisions by the borrower and poor practices by the bank. The final third represented poor bank practices and possible unconscionable conduct on the part of the banks involved.

Recommendations

The ASBFEO report made 15 recommendations, 11 of which were directed at the banking industry and four for the government, all to address the overall finding that the big four banks consistently engaged in practices that could significantly hurt their small business customers. The businesses engaged in agriculture, building, construction, hospitality and tourism were amongst those cited as being most at risk from banks 'behaving badly'.

Two of the ASBFEO's recommendations were about enhancing small business access to external dispute resolution, including the establishment of a one-stop-shop with a dedicated small business unit for disputes for matters up to \$5 million, and the ability to include disputes with third parties such as valuers, investigating accountants and receivers.

Other recommendations included:

- banks having to provide at least three months' notice to business customers on whether loans of up to \$5 million would to be extended
- no 'default action' being taken by banks on loans under \$5 million where the business has complied with the terms, and
- a revised Code of Banking Practice to be written in plain English and include a dedicated small business section.



Banks' responses

On 24 August 2017, the Australian Securities and Investment Commission (ASIC) and the Australian Small Business Family Enterprise Ombudsman (ASBFEO) announced that the big four banks (Commonwealth, Westpac, NAB and ANZ) had agreed to change their loan contracts for small business clients to eliminate unfair terms as follows:

- Loan documents will no longer contain 'entire agreement clauses' that absolve the bank from responsibility for the conduct, statements or representations they make to borrowers outside the written contract.
- Operation of the banks' indemnification clauses will be significantly limited. For example, the banks will no longer be able to require their small business customers to cover losses, costs and expenses incurred due to the fraud, negligence or wilful misconduct of the bank, its employees or a receiver appointed by the bank.
- Clauses which gave banks the power to call in a default for an unspecified negative change in the circumstances of the small business customer (known as 'material adverse change event' clauses) have now been removed – so banks will no longer have the power to terminate the loan due to an unspecified negative change in the circumstances of the customer.
- Banks have restricted their ability to vary contracts to specific circumstances, and where such a variation would cause a customer to want to exit the contract, the banks will provide a period of between 30 and 90 days for the consumer to do so.

In making changes to their practices to address the concerns raised, the banks have taken different approaches, in some instances going even further than the law requires.

For example, NAB has taken an industry-leading position about the application of non-monetary default clauses, while the Commonwealth Bank will provide an industry-leading 90 calendar days' notice for any changes to loan contracts that the small business customer does not wish to accept.

All four banks have limited the use of financial indicator covenants in small business contracts to certain classes of loans (eg. property development and specialised lending such as margin loans). The banks have agreed that financial indicator covenants will not be applied to property investment loans.

The banks have agreed that all customers who enter or renew contracts after 12 November 2016 – when the protections for small businesses began – will have the benefit of the changes agreed with ASIC.

To ensure that the new clauses do not operate unfairly in practice, ASIC will monitor the individual bank's actual use of these clauses to determine if they are in fact applied or relied on in an unfair way. ASIC will work with ASBFEO when assessing the results of this monitoring.

ASIC will publish more detailed information about the changes agreed with the big four banks so that other lenders to small business can consider whether changes to their contracts may be required.

For more information visit smallbusiness.wa.gov.au or call 13 12 49

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