
Australian Securities and Investments Commission v Channic Pty Ltd

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Introduction

Australian Securities and Investments Commission (ASIC) continues its focus on regulating and enforcing responsible lending under the National Consumer Credit Protection Act 2009 (Cth) (NCCP), with a recent significant enforcement outcome after ASIC took legal action against a lender and broker¹ in *Australian Securities and Investments Commission v Channic Pty Ltd (No 4)*.² ASIC's focus on compliance with responsible lending laws is not only in the car loan space and across the industry, but also on ensuring vulnerable customers are not taken advantage of.³ This case came as a result of work by ASIC's Indigenous Outreach Program, which gathers intelligence from Indigenous consumers, implements financial literacy programs, works with industry to improve access to products and services, and undertakes surveillance.⁴

The proceedings were filed by ASIC against the lender Channic Pty Ltd (Channic), the broker Cash Brokers Pty Ltd (Cash Brokers) and the sole director of both companies, Mr Colin William Hulbert. Both companies were Australian credit licensees under the NCCP that sold and offered high-interest rate credit contracts to consumers to purchase cars in one of Australia's most disadvantaged local areas.

ASIC alleged that Channic and Cash Brokers breached NCCP responsible lending laws⁵ and engaged in unconscionable conduct⁶ in relation to a series of loans given to consumers for the purchase of second motor vehicles from a Cairns-based motor dealer, Supercheap Car Sales (Supercheap), which was also owned by Mr Hulbert. ASIC argued that the defendants did not assess whether second-hand car loans were affordable to, or met the requirements and objectives of, consumers that largely relied on Centrelink income and who lived in the isolated Aboriginal community of Yarrabah.⁷ ASIC further claimed that the credit contracts entered into by Channic with consumers were unjust.⁸

While there was nothing particularly novel or unexpected in the judgment as far as the NCCP is concerned, which is reasonably straightforward in terms of what it seeks to achieve, this case is important as it demon-

strates the Federal Court's approach to various sections of the NCCP based on factual evidence. To assist banking and financial institutions and their in-house counsel understand its full impacts, in this article we explore the methodology of the court to establish breach, the main failings of the defendants including commission incentives resulting in disincentive to properly investigate, unsophisticated nature of the customers, the lack of investigation and verification and the lack of the defendants' "own inquiring mind",⁹ and key learnings for institutions.

Summary of facts of the case

According to facts of this case, as set out in the judgment, Cash Brokers as credit assistance provider, assisted consumers who were either welfare recipients, former bankrupts or persons with poor credit history,¹⁰ to obtain loans from the credit provider, Channic, to purchase cars from Supercheap. Cash Brokers provided an application form and preliminary test completed by Mr Kevin Humphreys, to Mr Hulbert, who relied on them to fill out other documentation needed to complete Channic's purported discharge of its credit provider obligations under the NCCP. Mr Hulbert knew how Mr Humphreys went about completing the documents and also knew (because he set the terms) that Mr Humphreys was remunerated only by commission payments for the sale of the cars through Supercheap and upon a consumer entering into a credit contract with Channic. He also knew of Mr Humphreys's knowledge that a positive surplus on the preliminary test was a significant criterion for a consumer to obtain credit from Channic.¹¹

The cars were financed by Channic loans with a 48% interest rate. Cash Brokers also charged the customer a direct brokerage fee of either \$550 or \$990 to arrange loans with Channic, which were financed under the loans.¹² The borrowers provided consent to repossession of the car in the event of default, and remained liable for any outstanding loan amount after repossession. The cars purchased were worth less than the loans provided to customers.¹³

Methodology of the court — Channic as credit provider

There were multiple factual issues at play in this case, including taking advantage of a disadvantaged community; responsible lending being conducted through a form ticking exercise; lack of supporting documentation (including bank accounts and Veda credit reports, where both would have shown a pattern that would have revealed it was not within the requirements and objectives of the borrower or would cause material hardship); the use of questionable benchmarks which did not provide for many of the expenses; the lack of interrogation of the borrower; and the timing of NCCP documents. Ultimately, however, the value of this case is that it provides a very technical overview of the NCCP and its operation, and the methodology the court used to determine statutory breaches under the NCCP.

In arriving at its decision, the court asked itself the following questions in relation to Channic's conduct as credit provider:¹⁴

1. It firstly established that the credit provider entered into a credit contract with the consumer, which was uncontested.
2. It then asked, did the credit provider, within 90 days of entry into the credit contract, make an assessment that purports to comply with s 128(c) of the NCCP?
3. If so, did the assessment specify the period the assessment covers, as required by s 129(a) of the NCCP?
4. If the credit provider did make an assessment, does it assess whether the contract will be unsuitable for the consumer if the contract is entered into in the period the assessment covers, as required by s 129(b) of the NCCP?
5. Is it likely, at the time of the assessment, that the consumer will be unable to comply with the consumer's financial obligations under the contract if the credit contract is entered into in the period covered by the assessment?
6. As to question 5 above, if it is not likely that the consumer will be unable to comply with those obligations, is it likely that the consumer could only comply with those obligations with substantial hardship?
7. Is it likely, at the time of the assessment, that the credit contract will not meet the consumer's requirements or objectives if the credit contract is entered into in the period covered by the assessment?
8. If the answer to questions 5, 6 or 7 above is yes, the credit provider must assess that the credit contract will be unsuitable for the consumer by reason of s 131(1) of the NCCP.
9. Does the assessment cover the period in which the credit day occurs, which in this case was the date of entry into the contract under s 128(c)(ii) of the NCCP?
10. Has the credit provider, before making its assessment, made reasonable inquiries about the consumer's requirements and objectives in relation to the credit contract, in accordance with ss 128(d) and 130(1)(a) of the NCCP?
11. Has the credit provider, before making its assessment, made reasonable inquiries about the consumer's financial situation in accordance with ss 128(d) and 130(1)(b) of the NCCP?
12. Has the credit provider, before making its assessment, taken reasonable steps to verify the consumer's financial situation in accordance with ss 128(d) and 130(1)(c) of the NCCP?
13. If the assessment does not cover the period in which the credit day occurs, or if the credit provider failed to do the things contemplated by questions 9, 10 and 11 above, then the credit provider has failed to comply with s 128(d) of the NCCP.
14. If the credit provider fails to comply with s 128(c) or (d) of the NCCP, it must not enter into a credit contract with a consumer who will be the debtor under the contract (s 128(a) of the NCCP).
15. Apart from any question concerning the making of an assessment as required by s 128 of the NCCP, is it likely, at the time the credit contract is entered into, that the consumer will be unable to comply with his or her financial obligations under the contract as per s 133(2)(a) of the NCCP?
16. As to question 15 above, if it is not likely that the consumer will be unable to comply with those obligations, is it likely that the consumer could only comply with those obligations with substantial hardship, as per s 133(2)(a) of the NCCP?
17. Is it likely, at the time the credit contract is entered into, that the credit contract does not meet the consumer's requirements or objectives in accordance with s 133(2)(b) of the NCCP?
18. If the contract is unsuitable by reason of s 133(2) of the NCCP, then the credit provider must not enter into the credit contract with a consumer who will be the debtor under the contract, according to s 133(1).

Methodology of the court — Cash Broker as credit assistance provider

Reviewing the questions the court asked in order to assess whether Cash Broker breached the NCCP might help credit assistance providers better understand the methodology a court will follow. In this case, the court asked:¹⁵

1. Did the credit assistance provider, provide credit assistance to the relevant borrower by suggesting that the borrower apply, or assisting the borrower to apply, to the particular credit provider for a particular credit contract?
2. If so, did the credit assistance provider, within 90 days of that day, make a preliminary assessment that purports to comply with s 115(1) of the NCCP?
3. If so, does it specify the period the assessment covers, as required by s 116(1)(a) of the NCCP?
4. Does the preliminary assessment, if made, assess whether the credit contract with the credit provider will be unsuitable for the consumer if he or she enters into the credit contract in the period of the assessment, as required by s 116(1)(b) of the NCCP?
5. If the answer is no to either of questions 3 or 4 above, then the credit assistance provider failed to comply with s 115(1)(c)(i) of the NCCP.
6. If a preliminary assessment is made, is it likely, at the time of the preliminary assessment, that the consumer will be unable to comply with his or her financial obligations under the credit contract if the credit contract is entered into with the credit provider in the period proposed for it to be entered?
7. If the consumer will be able to comply with those obligations, is it likely that such compliance could only be achieved by the consumer with substantial hardship?
8. Is it likely, at the time of the preliminary assessment, that the contract with the credit provider will not meet the consumer's requirements or objectives if the contract is entered into in the period proposed for it to be entered?
9. If the answer is yes to any of questions 6, 7 or 8 above, the credit contract will be unsuitable by reason of s 118(2) of the NCCP. If the contract is unsuitable, then the credit assistance provider must assess, by reason of s 118(1) of the NCCP, the credit provider credit contract as unsuitable for the consumer, in making the assessment required by ss 115(1)(c)(i) and 116(1)(b) of the NCCP.
10. Also, does the preliminary assessment cover, as required by s 115(1)(c)(ii) of the NCCP, the period proposed for the entering of the contract?
11. Did the credit assistance provider make reasonable inquiries as required by ss 115(1)(d) and 117(1)(a) of the NCCP, about the consumer's requirements and objectives concerning a contract with the credit provider?
12. Did the credit assistance provider make reasonable inquiries as required by ss 115(1)(d) and 117(1)(b) of the NCCP, about the consumer's financial situation?
13. Did the credit assistance provider take reasonable steps to verify the consumer's financial situation as required by ss 115(1)(d) and s 117(1)(c) of the NCCP?
14. If the answer is no to any of questions 2, 3, 4, 10, 11, 12 or 13 above (or yes to any of questions 6, 7 or 8), then the credit assistance provider failed to satisfy s 115(1)(c) or (d) of the of the NCCP, and must not provide credit assistance to the consumer by suggesting or assisting him or her to apply to the credit provider for the particular credit contract (s 115(1) of the NCCP).
15. Apart from the questions arising out of the operation of s 115 of the NCCP going to the preliminary assessment, is it likely, at the time the credit assistance provider provides credit assistance to the consumer, that he or she will be unable to comply with his or her financial obligations under the credit contract if the contract is entered into in the period proposed for it to be entered?
16. As to question 15 above, if it is not likely that the consumer will be unable to comply with those obligations, is it likely that the consumer could only comply with such obligations with substantial hardship?
17. In any event, is it likely, at the time the credit assistance provider provides credit assistance to the consumer, that the credit contract will not meet the consumer's requirements or objectives, if the contract is entered into in the period proposed for it to be entered?
18. If the answer is yes to questions 15, 16 or 17 above, then the credit contract will be unsuitable for the consumer by reason of s 123(2) of the NCCP.
19. If the contract is unsuitable by reason of s 123(2) of the NCCP, then the credit assistance provider must not provide credit assistance to the consumer

by suggesting that the consumer apply, or by assisting the consumer to apply for the particular credit contract with the credit provider (s 123(1) of the NCCP).

20. Did the credit assistance provider, at the same time as providing credit assistance to the consumer, give the consumer a credit proposal disclosure document in accordance with s 121(2) of the NCCP?

Summary of key Federal Court findings

Channic as credit provider, the party to whom all of the consumer's contractual obligations is owed,¹⁶ should have asked as its primary obligation, whether the credit contract will be unsuitable for the consumer after making an assessment and whether, at the time of the assessment, it was likely that the consumer will be unable to comply with those obligations or could only comply with them with substantial hardship.¹⁷ Section 130 of the NCCP casts an obligation on the credit provider to make reasonable inquiries about the consumer's requirements and objectives for the credit contract; make reasonable inquiries about the consumer's financial situation; and take reasonable steps to verify the consumer's financial situation. Channic's assessments could only properly be made under the NCCP if before the credit contract was made, Channic had carried out the required inquiries and verification and satisfied itself about the consumer's requirements and objectives.¹⁸

The Federal Court ultimately found that Channic and Cash Brokers breached NCCP responsible lending laws, which the court described as "not simply a 'tick the box' compliance exercise".¹⁹ The court also found that Channic engaged in unconscionable conduct and that the loan contracts were unjust transactions.²⁰ Greenwood J said:

It must have been obvious ... that having regard to the educational qualifications of the consumers, their background, their financial circumstances and their lack of commercial experience, that they would not have comprehended the content, in a meaningful way, of the loan contracts.²¹

The court also held Mr Hulbert personally liable, stating that Channic and Cash Brokers were "no more than wafer thin transparent membranes between the consumer and Mr Hulbert".²² It found that Mr Hulbert did not inquire or verify the living expenses of the particular consumer, and considered an expenses benchmark to be a "perfectly proper substitute for any inquiry into or verification of a consumer's actual expenses".²³

Interestingly, in relation to the commissions paid by Channic to Mr Humphreys (particularly given as part of the Financial System Inquiry, the government requested ASIC undertake an industry-wide review of mortgage broker remuneration²⁴), the court felt that the incentives to Cash Brokers were operating against the credit assistance provider's discharge of reasonable inquiries about the customer's financial situation and requirements and objectives, and against taking reasonable steps to verify the customer's financial situation. In these circumstances, Channic simply relied upon the Cash Broker material but needed, as a matter of statutory obligation, to bring its:

... *own inquiring mind* to the relevant statutory matters, *first* because it had a duty to do so under the NCCP Act and *second*, because Mr Hulbert needed to ensure that each contract was not unsuitable for the consumer *having regard* to the potentially distorting remuneration incentives operating within [Cash Brokers].²⁵

The court found that simply "filling out" a Sch 1 Loan Inquiry Checklist as a process matter and then "telling" the consumer about the loan rather than interrogating the consumer about their requirements²⁶ is not acceptable. The court found that the state of Channic's inquiries and verification steps:

... could rise no higher than the flawed character and quality of the material assembled by Mr Humphreys with all its limitations as earlier discussed because Mr Hulbert did not go beyond it and he knew its limitations. Secondly, Channic did not make its own inquiries and did not bring an independent "credit providers" mind to the statutory tasks.²⁷

Lessons learned and conclusion

While ASIC continues to make examples of the smaller players in the banking and finance market, it is also sending a very clear message to *all* credit providers about its expectations in relation to responsible lending and that non-compliance will not be tolerated. For lenders and credit assistance providers, having a culture which is detrimental to responsible lending will lead to problems. In this case, on 7 April 2017, the Federal Court fined Channic \$278,000, Cash Brokers \$278,000 and the sole director of both companies, Mr Hulbert, \$220,000 — a total of \$776,000 for breaching consumer credit laws relating to responsible lending. The court also ordered they pay ASIC's legal costs of \$420,000.²⁸

Australian credit licensees should therefore ensure adequate resources and systems are dedicated to carry out responsible lending and that compliance with NCCP is not a tick-a-box exercise. A credit provider must interrogate the information customers provide, even if it arrives via an intermediary.²⁹ This also means that you should collect detailed information about actual living expenses, rather than rely on benchmarks, and find out a

customer's objectives and requirements, rather than simply tell the customer about the product. If finance institutions do rely on benchmarks to verify living expenses, these should be appropriately adjusted to more accurately reflect a customer's expenses given the circumstances (for example, adjusted for the increased cost of living in remote locations). Licensees should also have robust and consistent practices for recording the inquiries you make and the basis for your assessment.³⁰

The real value of this case to banking and finance institutions is not knowing that the court found in favor of ASIC, which is unsurprising based on the facts. It is of value because it shows a court's detailed consideration given to the NCCP regime, its structure and application, as well as to the issue of when a person should be considered to be "involved" in a contravention of the NCCP.³¹

According to Deputy Chairman Peter Kell, we can expect, and rightfully so, that:

ASIC will take action where vulnerable people are deliberately targeted by lenders who engage in unconscionable conduct. [ASIC has] a strong focus on lenders and financial services firms who push poor quality and unsuitable financial products to indigenous consumers, particularly where they fail to meet responsible lending obligations.³²

Fines and remediation costs for lenders will likely grow as ASIC continues to pursue Australian credit licensees for compliance with responsible lending, and as it appoints independent reviewers (either voluntarily or as part of an enforceable undertaking) who may uncover broader inadequacies in a licensee's compliance with NCCP. As a result, banking and financial institutions could see even greater costs of compliance.³³



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Leonie Chapman's experience extends to banking and finance, consumer credit and mortgage lending, contract negotiation, trade practices and fair trading legislation, intellectual property and trade marks, corporate and financial services. After completing her Bachelor of Laws and Bachelor of Commerce in 2002, Leonie went on to work both in private practice and as senior in-house lawyer supporting a specialist lender and then for 6 years, Macquarie Bank Ltd. Having achieved a Master of Laws in 2009 specialising in banking and

finance law, Leonie's main focus now as Principal of LAWyal Solicitors is on regulation and compliance for banking and financial institutions.

Footnotes

1. K J Maynes, A Moczulski and A W Taylor, *Are You Ready for Your Close Up? ASIC Continues to Target Lenders on Responsible Lending Non-compliance*, 10 November 2016, www.lexology.com/library/detail.aspx?g=5982e9c0-caab-4f9b-b133-b0a91bb5bffa.
2. *Australian Securities and Investments Commission v Channic Pty Ltd (No 4)* [2016] FCA 1174; BC201608412.
3. Australian Securities and Investments Commission "ASIC action sees BMW Finance pay \$77 million in Australia's largest consumer credit remediation program" 16-417MR (6 December 2016) <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2016-releases/16-417mr-asic-action-sees-bmw-finance-pay-77-million-in-australias-largest-consumer-credit-remediation-program/>.
4. Australian Securities and Investments Commission "Cairns-based car yard lender and broker breached consumer credit laws" 16-335MR (30 September 2016) <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2016-releases/16-335mr-cairns-based-car-yard-lender-and-broker-breached-consumer-credit-laws/>.
5. National Consumer Credit Protection Act 2009 (Cth), ss 128, 130, 131 and 133 (in relation to Channic); and ss 113, 114, 115, 117, 118, 121 and 123 (in relation to Cash Brokers).
6. Australian Securities and Investments Commission Act 2001 (Cth), s 12CB.
7. Above n 1.
8. *National Credit Code* (Sch 1 to the NCCP), s 76.
9. Above n 2, at [1804].
10. J Brereton, *ASIC case update*, 16 November 2016, www.listgbarristers.com.au/uploads/Brereton-J-ASICCaseUpdate.pdf.
11. Above n 2, at [1804].
12. Above n 4.
13. Above n 10.
14. Above n 2, at [187].
15. Above n 2, at [186].
16. Above n 2, at [1798].
17. Above n 2, at [14].
18. Above n 2, at [1798].
19. Above n 2, at [1800].
20. Above n 4.
21. Above n 2, at [1837].
22. Above n 2, at [1821].
23. Above n 2, at [1736].
24. Australian Securities and Investments Commission *Review of Mortgage Broker Remuneration* Report No 516 (March 2017) www.treasury.gov.au/ConsultationsandReviews/Consultations/2017/ASIC-review-of-mortgage-broker-remuneration.

25. Above n 2, at [1804].
26. Above n 2, at [1812].
27. Above n 2, at [1813].
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30. Above n 1.
31. Above n 5, s 5.
32. Above n 4.
33. Above n 1.