

COSL Member Communication

2 February 2010

Dealing with Borrowers in Financial Difficulty

COSL has seen an unprecedented increase in the number of financial hardship cases. With the recent economic downturn and subsequent unemployment, we expect financial hardship to remain our single largest source of complaints in the next twelve months. We continue to work co-operatively with our Members (lenders and mortgage managers) in seeking realistic outcomes.

It is not of course COSL's role to advocate on behalf of a borrower experiencing financial hardship; rather we encourage Members to give genuine consideration to applications for financial hardship relief. This requires them to take into account their obligations under the law, COSL Rules and applicable industry codes of practice.

Judging from the complaints we receive from borrowers in financial distress, it is apparent that while most Members have some systems in place to address cases of financial hardship, there are still areas where businesses have yet to reach the best practice standard described in the various industry codes of practice.

The role of mortgage brokers in financial hardship cases

Mortgage and finance brokers play a key role in assisting in financial hardship referrals, as they are often the first point of contact for their clients about their loan. If a borrower informs their mortgage or finance broker that they are in financial difficulty and are not able to meet their repayments, the mortgage broker should immediately refer the borrower to the lender or mortgage manager.

The role of mortgage managers and lenders in financial hardship cases

COSL has developed its Rules to assist mortgage managers and lenders to meet best industry practice in relation to borrowers with financial difficulties. The Rules have been developed in consideration of the financial hardship provisions of the various industry codes of practice which are subscribed to by many of our Members.

Under the COSL Rules (6th Edition), *when a lender Member becomes aware that a borrower is or may be in financial hardship*, the Member must consider in good faith whether a repayment variation is reasonably appropriate.

In other words, the Member should genuinely consider whether it should offer an appropriate repayment variation as soon as it is aware that the borrower may be in financial hardship. The borrower need not specifically bring this to the lender's attention.

A loan falling into arrears or direct debits being dishonoured will generally indicate that the borrower is having difficulty in making their repayments and is likely to be in financial hardship. In these circumstances, the lender or mortgage manager should open early lines of communication with the borrower to establish whether this is the case and, if so, whether a payment variation is reasonably appropriate.

In a case we recently dealt with, a couple defaulted on their loan and advised the lender that the wife was undergoing cancer treatment for 6 months. Despite this, the lender did not consider whether a payment variation was appropriate. The couple made a complaint to COSL after the treatment had concluded and the wife had returned to work. They provided documentation to COSL that established that a payment variation would have been reasonably appropriate at the time that the lender became aware of the wife's medical condition and treatment. The complaint was settled by the lender who agreed to reverse 6 months' worth of default fees and default interest, totalling \$8,500. Given that a payment variation would have been reasonably appropriate, this amount would not have accrued had the lender considered, and agreed to, a payment variation at the time it became aware of the borrowers' situation.

In another case we considered, the lender did not send financial hardship forms to the borrower for nearly 12 months after it became aware of her financial hardship. The lender had simply declined her ongoing requests for a payment variation, without assessing whether a variation would have been appropriate. Given that a payment variation would have been reasonably appropriate in this case, the lender agreed to reverse default fees and charges totalling around \$30,000.

In view of the above, we recommend that lenders and mortgage managers establish systems and train staff to promptly identify and address potential financial hardship cases before commencing enforcement action. This will benefit both the lender and borrower, and arrears and default fees can be avoided or otherwise kept to an absolute minimum.

Tips for Lenders and Mortgage Managers

- If a borrower is in default, act quickly to assess whether a payment variation may be appropriate.
- Allow the borrower a reasonable amount of time to provide all information that is reasonably necessary for you to consider the borrower's financial circumstances.
- If a borrower has not requested a variation to their payment terms, but a variation seems appropriate, suggest to the borrower that they request this.
- Act reasonably in assessing the borrower's request to vary the payment terms and don't impose unreasonable or burdensome conditions on the borrower before agreeing to consider their financial hardship application. For example, don't ask borrowers to access superannuation or to obtain money from family or friends before considering whether a variation is appropriate.
- Notify the borrower in writing within 21 days of your decision whether or not to agree to their request for a hardship variation. If you agree to vary the payment terms, set out the particulars in writing so that the borrower knows what is expected of them. For example, if you agree to accept reduced payments for a period of time, tell them the date that they must resume regular payments. If you decline their request, set out your reasons for this and advise the borrower that they are entitled to contact COSL if they disagree with your decision.
- Consider a wide variety of possible variations that may be suitable, including reducing the interest rate for a period, converting the loan to an interest only loan for a period, waiving fees, extending the loan term and/or capitalising arrears.
- Ensure that collections staff are aware of your financial hardship obligations and that detailed file notes are kept.
- Under the COSL Rules (6th Edition) you may not be entitled to recover default interest and fees and enforcement costs if you decline a hardship application when a variation would have been appropriate.

If you would like more information please contact the Credit Ombudsman Service



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