



**CODE COMPLIANCE MONITORING COMMITTEE
(the CCMC)**

Guidance Note No. 8

Guarantees

The CCMC is an independent Code compliance monitoring body established under clause 36 of the Code of Banking Practice (the Code).

The CCMC oversees the compliance of subscribing banks with their Code obligations by:

- a. independently monitoring compliance with the Code
- b. investigating code breach allegations, and
- c. monitoring any aspects of the Code that are referred by the Australian Bankers Association (the ABA).

This Guidance Note has two purposes:

- a. to indicate the CCMC's likely approach when it considers potential breaches of the "guarantees" obligations under clause 31 of the Code, and
- b. to share the CCMC's view of good industry practice, which in some cases may extend beyond the strict requirements of the Code.

When considering whether a Code subscriber has complied with the provisions of the Code, the CCMC will also have regard to the key commitments made by that bank to act fairly, reasonably and ethically in the provision of services to its customers and to comply with all relevant laws.

It is important to understand that the CCMC considers all matters on the basis of their individual circumstances and this document is not intended to anticipate all possible issues that might come before the CCMC.

Guidance Notes are subject to change by the CCMC and this document reflects the CCMC's views as at the date of its publication. Any reference to "bank" in this Guidance Note means a bank which subscribes to the Code. Any reference to the "Code" is a reference to the 2013 version of the Code, unless otherwise stated. Any reference to a "consumer" or "customer" means an individual or small business that is either a customer or potential customer of a bank.

For more information about the CCMC, please visit its website: (www.ccmc.org.au).

Introduction

Definition

1. For the purposes of clause 31 of the Code, a 'guarantee' or 'indemnity' is an undertaking given by a person (the guarantor) to repay a debt or an obligation in the event of a default on a credit facility held by another individual or small business¹. In this document the word *guarantee* is used to refer to both guarantees and indemnities.

This Guidance Note

2. This Guidance Note does not review each requirement under clause 31. Instead, its objective is to indicate the CCMC's likely approach when assessing banks' compliance with their guarantees obligations under the Code and to share the CCMC's recent experience in dealing with matters related to guarantees.
3. The CCMC recommends this Guidance Note is read together with:
 - 3.1 Publications by the CCMC on banks' compliance with clause 31 which may include recommendations and examples of good industry practice², and
 - 3.2 the Financial Ombudsman Service (FOS) approach to the Code of Banking Practice and to disputes lodged by guarantors³.

The Code's Obligations

4. Banks' obligations to guarantors and potential guarantors are set out in clause 31 of the Code. A copy of these obligations can be accessed using the hyperlinks set out in footnote four, below⁴.
5. The obligations under the Code relating to guarantees apply where:
 - 5.1 the guarantor or potential guarantor is an individual at the time the guarantee is taken, and
 - 5.2 the purpose of the guarantee is to secure a financial accommodation or credit facility provided by the bank to another individual or small business.
6. In assessing compliance with the Code's guarantee obligations the CCMC may consider:
 - 6.1 the banks' key commitments to act fairly and reasonably in a consistent and ethical manner towards the guarantor or potential guarantor and to comply with all relevant laws⁵
 - 6.2 the obligation banks have under the Code to promote better informed decisions about their banking services⁶, and
 - 6.3 recent court decisions about the rights and responsibilities of guarantors, in particular cases involving:

¹ 'Small business' is defined in the Code.

² <http://www.ccmc.org.au/2013/06/05/guarantees-inquiry/>

³ <http://www.fos.org.au/publications/our-approach/?sstat=257685>

⁴ For the 2004 Code see: <http://www.bankers.asn.au/Industry-Standards/ABAs-Code-of-Banking-Practice>
For the 2013 Code see: <http://www.bankers.asn.au/Industry-Standards/ABAs-Code-of-Banking-Practice/Code-of-Banking-Practice-2013--Online-Version#1e31>

⁵ Code clauses 2.2 and 3.2 of the 2004 and 2013 Codes respectively.

⁶ See clauses 2.1 and 3.1 of the 2004 and 2013 Codes respectively. 'Banking service' is defined in the Code.

- guarantors that are considered vulnerable, for example, due to limited language and/or financial literacy skills
 - spousal guarantors and other categories of consumer that courts have identified as ‘volunteers’, and
 - ‘pure asset’ lending.
7. The Code sets out a limited number of exceptions where the guarantee obligations do not apply, such as where the guarantor of a credit facility is a commercial asset financing guarantor or sole director guarantor, director guarantor or trustee director.
 8. Guarantors have an obligation to carefully consider both their personal circumstances and the potential consequences of a guarantee before entering into such arrangements with a bank.
 9. However, banks also have a very important role to ensure potential guarantors are provided with relevant information and appropriate time to make informed and independent decisions before agreeing to sign a guarantee. The importance of that role is supported by clauses 31.4 and 31.5 of the Code which prescribe steps for banks to follow when offering and/or entering into guarantees. The CCMC will adopt a strict approach when considering whether a bank has complied with these steps.

Monitoring compliance with Code obligations

10. In determining whether the Code’s obligations have been met, the CCMC will assess whether the banks’ monitoring and assurance program facilitates compliance with the guarantee obligations. This program should include:
 - 11.1 robust policies and procedures to ensure compliance with clauses 3, 4 and 31
 - 11.2 effective training for staff in their engagement with guarantors and borrowers, and
 - 11.3 timely and effective dispute resolution in accordance with Code obligations.
11. It is the CCMC’s view that:
 - 12.1 where complaints and monitoring have identified knowledge and skills gaps in relation to guarantees, additional training should be provided to staff members, and
 - 12.2 an example of staff training may include making staff aware of the impact of providing incorrect advice in relation to guarantees, particularly upon guarantors that are considered vulnerable or spousal guarantors and/or ‘volunteers’.

Independent advice

12. The Code requires a bank to give a proposed guarantor a prominent notice to seek independent legal and financial advice on the effect of the guarantee, before taking a guarantee from them. The Code also states a bank will not ask a potential guarantor to sign a guarantee or accept it unless it has provided that notice (along with additional information prescribed by the Code)⁷.
13. The CCMC has reviewed recent court decisions about the engagement between a bank and a guarantor or potential guarantor concerning independent advice. Banks may be asked by the CCMC as a result to explain information, warnings, conduct and advice given in relation to clause 31.4(i).

⁷ Code clauses 28.4 (a) & 28.5 and 31.4(a) & 31.5 of the 2004 and 2013 Codes respectively.

14. The common law suggests that to be considered 'independent', the advice must be independent of both the bank and the borrower/proposed borrower.

Good Industry Practice

15. The CCMC has identified some broad examples of good industry practice in the course of its Code monitoring and compliance investigation functions that it seeks to share with Code subscribers.
16. These examples may:
 - 17.1 assist banks to comply with their Code obligations and promote better informed decisions about their banking services
 - 17.2 enhance effective disclosure of information to their customers when discharging their guarantees obligations
 - 17.3 be considered by the CCMC when assessing factors that have led to non-compliance with clause 31 and the interaction between the guarantees obligations and the key commitment provisions in clause 3 and 4
 - 17.4 support the banks' ability to comply with the Key Commitments obligations, including acting fairly, reasonably and ethically towards customers⁸.
17. It has been the CCMC's experience that:
 - 18.1 the information made available to guarantors and potential guarantors about guarantees can be complex and difficult to understand
 - 18.2 information about guarantees is more likely to be effective and meet good industry practice when:
 - it is easy to read and accessible to both bank staff and consumers
 - it clearly describes the rights and responsibilities of potential guarantors under the Code, and
 - notices about rights, responsibilities and risks under the guarantee are prominent and clearly brought to the guarantor or potential guarantor's attention.
18. Banks are encouraged to record the advice and information staff provide to potential guarantors about the potential risks associated with the proposed transaction. This includes instances where:
 - 19.1 a potential guarantor is advised to obtain independent financial advice in respect of the financial, business or other specific risks related to the guarantee that could lead to the guarantee being called upon
 - 19.2 the bank has formed a view that it will not proceed with a proposed guarantee transaction unless the proposed guarantor obtains independent legal or financial advice or expressly declines to do so, and
 - 19.3 the bank has formed the view that the advice provided to the guarantor is not sufficiently independent of the borrower and the bank, for the bank to be able to rely on the provisions in clause 31.5 of the Code.
19. To further facilitate the effective exchange of information required under clause 31, the CCMC encourages banks to ensure their staff, agents and representatives understand their key Code obligations and the bank's processes and procedures.

⁸ Code clauses 3.1(b)(i) and 3.2 of the Code (2013 version) respectively.