



7 June 2016

Consumer Credit
The Treasury
Langton Crescent
PARKES ACT 2600

By email: consumercredit@treasury.gov.au

Dear Sirs & Mesdames

Review of the small amount credit contract laws – The Final Report

Consumer Credit Legal Service (WA) Inc. (**CCLSWA**) is pleased to provide this submission in response to the Department of Treasury's Final Report of the independent Review of Small Amount Credit Contracts (**SACCs**), and to the 24 recommendations made in relation to SACCs and consumer leasing laws.

1. About CCLSWA

- 1.1. CCLSWA is a not-for-profit community legal centre based in the Perth metropolitan area. We advise and advocate for consumers on consumer credit issues and Australian Consumer Law related problems.
- 1.2. CCLSWA operates a telephone advice line service, which allows consumers to seek information and legal advice. CCLSWA also provides:
 - Assistance for financial counsellors and other consumer advocates who work closely with disadvantaged and low-income individuals for the resolution of their credit and debt related problems;
 - Community legal education programmes relating to credit and debt issues and the Australian Consumer Law;
 - Financial literacy programmes to high school students and select groups within the community;

- Contributions to relevant policy and law reform initiative; and
 - A training and supervision programme for law student and graduate volunteer paralegals.
- 1.3. In providing these services CCLSWA aims to create awareness, knowledge and understanding of consumer issues related to banking and financial institutions, and the Australian Consumer Law.
- 1.4. We seek to assist the Western Australian community with developing just and fair relationships with banks and financial institutions. We also aim to advance public interest and awareness through participating in community legal education and policy and law reform.

2. Executive summary

- 2.1. The review concerned the effectiveness of the law relating to SACCs, and whether any of the provisions, which apply to SACCs, should be extended to regulated consumer leases.
- 2.2. The Panel was required to consider a number of specific issues, including competition, fairness, innovation, efficiency, access to finance, regulatory compliance costs, consumer protection, and the current economic climate.
- 2.3. CCLSWA acknowledges the importance of balancing the above policy considerations in order to ensure that the competitiveness of industry participants is not disproportionately affected. CCLSWA believes that consumer protection should be the overarching consideration of any review of consumer credit legislation.
- 2.4. CCLSWA supports the majority of the recommendations made by the review committee; however, CCLSWA has a number of reservations about the efficacy of these recommendations.
- 2.5. We are of the view that the most significant shortcoming of the existing SACC regime is not the provisions themselves, but rather the inconsistency of compliance with these provisions.

3. Small amount credit contract recommendations and comments

Recommendation 1 - Affordability

Extend the protected earnings amount regulation to cover SACC's provided to all consumers.

Reduce the cap on the total amount of all SACC repayments from 20 per cent of the consumers' gross income to 10 per cent of the consumers net income.

- 3.1. Section 133CC(1) of the *National Consumer Credit Protection Act* provides protections for consumers who derive at least 50% of their gross income from Centrelink.

- 3.2. Regulation 28S(3) of the *National Consumer Credit Protection Regulations* provides that that total amount of repayments in each cycle of income must not exceed 20% of gross income.
- 3.3. In theory, a bright line test expanding the protected earnings amount to ensure that no consumer could devote more than 10% of net income to repayments for SACCs would go significantly toward reducing the number of consumers trapped in debt spirals. But in light of recommendation 6, there remains governance and regulatory compliance concerns.
- 3.4. CCLSWA has advised a number of clients whose situations represented a clear trigger of the existing rebuttable presumption of unsuitability. For the majority of these clients, no sensible assessment of their financial situation would result in the client becoming suitable.
- 3.5. To an extent, the payday lending industry is characterised as much by a strong and consistent consumer-driven demand for payday lending products, as it is by predatory lending.
- 3.6. Many consumers are heavily reliant on a consistent stream of small amount loans to fund weekly expenditure. For this class of consumers, a bright line test in place of a rebuttable presumption will have negligible material impact.
- 3.7. Lenders will remain content overlooking SACC laws in order to provide loans to this class of consumers. This represents a fundamental shortcoming of the existing regime, and one that has not been addressed in the recommendations.
- 3.8. These concerns should be balanced with the fact that section 133CC is a civil penalty provision and criminal penalty provision. In theory, the strengthening of this provision should deter irresponsible lending, alleviating some concerns about the efficacy of a rebuttable presumption.
- 3.9. CCLSWA strongly supports extending the protected earnings amount to cover all consumers; however, CCLSWA remains concerned about the present inadequacy of the existing regime in addressing the inconsistent of regulatory compliance of industry participants.
- 3.10. Further, the lender should be required to make this assessment some time *prior* to a consumer entering into the SACC, as opposed to “at the time the SACC is entered into...”. This measure should be taken to ensure true regard is given to the consumer’s objectives and financial position.

Recommendation 2 - Suitability

Remove the rebuttable presumption that a loan is presumed to be unsuitable if the consumer is in default under another SACC, or in the 90- day period before the assessment, the consumer has had two or more other SACCs.

This recommendation is made on the condition that it is implemented together with Recommendation 1).

- 3.11. If Recommendation 1 is implemented and strictly enforced, the existing presumption of unsuitability becomes unnecessary, and as such, CCLSWA is in favour of its removal.
- 3.12. A bright line test is a clearly defined standard of what a SACC lender can, and cannot do. This is superior to a rebuttable presumption from a regulatory perspective. However, as stated above, concerns should remain in relation to regulatory compliance. The report states the following as reasons the rebuttable presumption has been unsuccessful in addressing repeat borrowing and debt spirals:

“It has resulted in uncertainty and complexity for SACC providers and increased compliance costs in circumstances where these issues can be more effectively dealt with by a bright line requirement...”

- 3.13. Requiring a credit provider to conduct an assessment of a consumer’s net income and total SACC repayments in a given cycle is a no less onerous responsibility on lenders. While presenting a lower hurdle, the existing presumption of unsuitability requires a less complex and uncertain assessment to be undertaken by a lender.

- 3.14. The report continues:

“If a consumer is in default under another SACC, it is likely that a lender would breach their responsible lending obligations by lending to them, and therefore that limb of the rebuttable presumption is not necessary”

- 3.15. It does not follow that, simply because a consumer triggers the presumption of unsuitability, the lender has engaged in irresponsible lending. One arm of the presumption is that a consumer with two or more SACCs is presumed to be unsuitable. This arm aims to directly address the issue of repeat borrowing, an issue that the responsible lending obligations do not address in their current form.

Recommendation 3 – Short term credit contracts

Maintain existing ban on credit contracts with term of less than 15 days.

3.16. CCLSWA is in favour of retaining the existing provision that this recommendation relates to.

Recommendation 4 – Direct debit fees

Direct debit fees should be incorporated into the existing SACC fee cap.

3.17. CCLSWA is in favour of this recommendation.

Recommendation 5 – Equal repayments and sanction

In order to meet the definition of a SACC, the credit contract must have equal repayments over the life of the loan (noting that there may need to be limited exceptions to this rule).

Where a contract does not meet this requirement, the credit provider cannot charge more than an annual percentage rate (APR) of 48 per cent.

3.18. CCLSWA is in favour of this recommendation.

Recommendation 6 – SACC database

A national database of SACCs should not be introduced at this stage. The major banks should be encouraged to participate in the comprehensive credit reporting regime at the earliest date.

3.19. CCLSWA acknowledges the importance of policy considerations taken into account in coming to the above recommendation. However, the reasoning provided appears duplicitous and in favour of the credit providers. The report states the following as reasons a database would be beneficial:

“A national SACC database could improve the capacity of SACC providers to comply [with] responsible lending obligations”.

“A SACC database may also improve ASIC’s capacity to monitor trends and practices in the SACC market”.

3.20. The report states the following as justification for recommending against a database:

“Benefits come at a cost to the industry”

“The majority of credit providers argued it would be expensive and sufficient information is already available (for example, through the collection of bank statements)”

- 3.21. CCLSWA does not deny that the cost to the industry would be high. While this policy consideration is logical, CCLSWA steadfastly maintains that the paramount shortcoming of the existing SACC regime is the inconsistency of regulatory compliance, rather than the strength of the SACC provisions themselves.
- 3.22. A regulated SACC database has been successfully implemented in numerous jurisdictions in the United States and a regulated SACC database was supported by a number of credit providers, consumer advocate groups, and ASIC.
- 3.23. A regulated database would serve to strictly enforce the proposed bright line test, and provide important governance and oversight to all regulated SACC lenders.
- 3.24. CCLSWA solicitors are currently assisting a number of clients who are in severe financial hardship due to debt spirals directly resulting from predatory lending.
- 3.25. In the majority of these cases, a SACC database is highly likely to have ensured compliance with responsible lending, where instead; the clients were merely asked whether they had two or more SACCs on foot. This behaviour in itself suggests a clear and consistent pattern of avoidance, and exemplifies the ability of credit providers to circumvent responsible lending obligations.
- 3.26. CCLSWA acknowledges the cost to the industry, however we aver that the benefits and protections consumers would experience as a result of a regulated database, far outweigh the potential costs to lenders.

Recommendation 7 – Early repayment

No 4 per cent monthly fee may be charged for a month after the SACC is discharged by early repayment. If a consumer repays a SACC early, the credit provider under the SACC cannot charge the monthly fee in respect of any outstanding months of the original term of the SACC after the consumer has repaid the outstanding balance and those amounts should be deducted from the outstanding balance at the time it is paid.

- 3.27. CCLSWA is strongly in favour of this recommendation.

Recommendation 8 – Unsolicited offers

SACC providers should be prevented from making unsolicited SACC offers to current or previous consumers.

- 3.28. CCLSWA is strongly in favour of this recommendation. CCLSWA has advised a number of clients who have been regularly offered additional SACCs. This recommendation, if adopted should improve the incidence of repeat borrowing and debt spirals.

Recommendation 9 – Referrals to other SACC providers

SACC providers should not receive a payment or any other benefit for a referral made to another SACC provider.

- 3.29. CCLSWA is strongly in favour of this recommendation.
- 3.30. A provision prohibiting payments or benefits to SACC providers for referrals to other SACC providers will discourage collusion among lenders in the industry. It will also discourage lenders from referring unsuitable consumers to other lenders willing to offer SACCs in breach of the SACC laws.
- 3.31. The long-term impact of this recommendation, if adopted, would be stronger competition between lenders, and lower fees, in order to attract borrowers and remain competitive.

Recommendation 10 – Default fees

SACC providers should only be able to charge a default fee that represents their actual costs arising from a consumer defaulting on a SACC up to a maximum of \$10 per week.

The existing limitation of the amount recoverable in the event of default to twice the adjusted credit amount should be retained.

- 3.32. CCLSWA is strongly in favour of this recommendation.

4. Consumer lease recommendations and comments

Recommendation 11 – Cap on cost to consumers

A cap on the total amount of the payments to be made under a consumer lease of household goods should be introduced. The cap should be a multiple of the Base Price of the goods, determined by adding 4 per cent of the Base Price for each whole month of the lease term to the amount of the Base Price, as reflected by the following formula:

$$[P \text{ (Base Price of Goods)}] + [0.04 \times P \times M \text{ (Duration of Lease in Months)}]$$

For a lease with a term greater than 48 months, the term should be deemed to be 48 months for the purposes of the calculation of the cap.

- 4.1. CCLSWA is strongly in favour of a cap on total payments to be made under a regulated consumer lease and agrees that this cap should be based on the regular retail price, or agree upon price of a good.

- 4.2. CCLSWA believes that a cap will significantly improve the protection of consumers, particularly those in rural communities who are targeted by consumer lease providers; however CCLSWA has a number of reservations concerning the recommendations with in relation to consumer leases.

Example outcome: \$1000 Television, 24-month lease:

$$\text{Cap on total cost} = \$1000 + [0.04 \times 1000 \times 24] = \$1000 + \$960 = \$1960$$

Example outcome 2: \$2000 Fridge, 48-month lease:

$$\text{Cap on total cost} = \$2000 + [0.04 \times 2000 \times 48] = \$2000 + \$3840 = \$5840$$

- 4.3. The proposed cap remains relatively high. As the above examples demonstrate, a 24-month lease for a \$1000 television will result in a consumer paying almost twice the base price over two years, while not owning the good at the conclusion of the contract. The longer the contract term, the more the consumer will have to pay. As Example 2 demonstrates, a \$2000 fridge leased over 48 months will result in the consumer paying three times the base price, again, without owning the goods at the conclusion of the contract.
- 4.4. Further, the proposed cap disregards the yearly depreciation in the value of leased goods. In the same way an asset depreciates; the value of new goods depreciates in each year of ownership. Consumers should not have to pay a fixed yearly fee (4% of base price) for the duration of a contract for goods that decrease in value for each year of the lease.
- 4.5. CCLSWA proposes the following cap for goods, using a 48-month contract as an example:

Proposed alternative method of calculation:

$$\text{Cap on Total Cost} = P \text{ (Base Price of Goods)} + [0.04 \times P \times 12 \text{ (Year 1 of Lease in Months)}] + 0.03 \times P \times 12 \text{ (Year 2 of Lease in Months)} + [0.02 \times P \times 12 \text{ (Year 3 of Lease in Months)}] + (0.01 \times P \times 12 \text{ (Year 4 of Lease in Months)})$$

Example outcome 2 (using alternative approach):

$$\text{Cap on Total Cost} = \$2000 + [0.04 \times 2000 \times 12] + [0.03 \times 2000 \times 12] + [0.02 \times 2000 \times 12] + [0.01 \times 2000 \times 12] = \$4500$$

This results in a \$1340 reduction in the total cap over a 48-month period.

- 4.6. This alternative approach has benefits for both consumers and for business. It will reduce the total cap on costs, alleviating the financial burden on consumers.

- 4.7. It also appropriately accounts for the expected depreciation in the value of new goods over time. A consumer should not have to pay the same fixed fee rate for leased goods in the first year of the lease, as in the fourth year of a lease.
- 4.8. Further, this approach allows the business who leases goods to a consumer to receive a modest rate of return - one that reflects the real depreciation in value of the asset - while still able to lease the goods out again at the conclusion of the initial lease as second-hand goods.

Recommendation 12 – Base price of goods

The Base Price for new goods should be the recommended retail price or the price agreed in store, where this price is below the recommended retail price.

Further work should be done to define the Base Price for second hand goods.

- 4.9. CCLSWA is in favour of a base price reflecting the recommended retail price. In considering a “base price” for second hand goods, regard must be had to the age of the goods, number of years of use, and the base price of equivalent or substitute new goods in the market.

Recommendation 13 – Add-on services and features

The cost (if any) of any add-on services and features, apart from delivery should be included in the cap. A separate one-off delivery fee should be permitted. That fee should be limited to the reasonable costs of delivery of the leased good which appropriately account for any cost savings if there is a bulk delivery of goods to an area.

- 4.10. CCLSWA is in favour of recommendation 13.

Recommendation 14 – Consumer leases to which the cap applies

The cap should apply to all leases of household goods including electronic goods.

Further consultation should take place on whether the cap should apply to consumer leases of motor vehicles.

- 4.11. CCLSWA has limited experience with consumers in relation to motor vehicle leases. As such, we will refrain from offering a comment on this point of consultation.

Recommendation 15 – Affordability

A protected earnings amount requirement be introduced for leases of household goods, whereby lessors cannot require consumers to pay more than 10 per cent of their net income in rental payments under consumer leases of household goods, so that the total amount of all rental payments (including under the proposed lease) cannot exceed 10 per cent of their net income in each payment period.

4.12. CCLSWA is strongly in favour of this recommendation.

4.13. CCLSWA will address recommendations 16 to 18, collectively.

Recommendation 16 – Centrelink implementation

The Department of Human Services consider making the caps in Recommendations 11 and 15 mandatory as soon as practicable for lessors who utilise or seek to utilise the Centrepay system.

Recommendation 17 – Early termination fees

The maximum amount that a lessor can charge on termination of a consumer lease should be imposed by way of a formula or principles that provide an appropriate and reasonable estimate of the lessors' losses from early repayment.

Recommendation 18 – Ban on the unsolicited marketing of consumer leases

There should be a prohibition on the unsolicited selling of consumer leases of household goods, addressing current unfair practices used to market these goods.

4.14. CCLSWA is in favour of the above recommendations.

5. Combined recommendations

5.1. CCLSWA will address recommendations 19 to 24 collectively.

Recommendation 19 – Bank Statements

Retain the obligation for SACC providers to obtain and consider 90 days of bank statements before providing a SACC, and introduce an equivalent obligation for lessors of household goods.

Introduce a prohibition on using information obtained from bank statements for purposes other than compliance with responsible lending obligations.

Recommendation 20 – Documenting suitability assessments

Introduce a requirement that SACC providers and lessors under a consumer lease are required at the time the assessment is made to document in writing their assessment that a proposed contract or lease is suitable.

Recommendation 21 – Warning statements

Introduce a requirement for lessors under consumer leases of household goods to provide consumers with a warning statement, designed to assist consumers to make better decisions as to whether to enter into a consumer lease, including by informing consumers of the availability of alternatives to these leases.

Recommendation 22 - Disclosure

Introduce a requirement that SACC providers and lessors under a consumer lease of household goods be required to disclose the cost of their products as an APR.

Introduce a requirement that lessors under a consumer lease of household goods be required to disclose the Base Price of the goods being leased, and the difference between the Base Price and the total payments under the lease.

Recommendation 23 – Penalties

Encourage a rigorous approach to strict compliance by extending the application of the existing civil penalty regime in Part 6 of the National Credit Code to consumer leases of household goods and to SACCs, and, in relation to contraventions of certain specific obligations by SACC providers and lessors, provide for automatic loss of the right to their charges under the contract.

Recommendation 24 - Avoidance

The Government should amend the Credit Act to regulate indefinite term leases, address avoidance through entities using business models that are not regulated by the Credit Act, and address conduct by licensees adopting practices to avoid the restrictions on the maximum amount that can be charged under a consumer lease of household goods or a SACC, or any of the conduct obligations that apply to a consumer lease of household goods or a SACC.

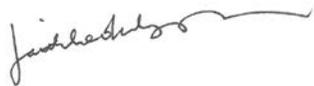
5.2. CCLSWA is in favour of the above recommendations.

We are grateful for the opportunity to provide further comments.

If you have any questions or would like to discuss this matter further, please contact Faith Cheok, Principal Solicitor, on (08) 6336 7020.

Yours faithfully

Consumer Credit Legal Service (WA) Inc.



Per
Faith Cheok
Principal Solicitor

