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Response to Treasury Consultation Paper – Credit Cards

Cuscal appreciates the opportunity to respond to Treasury's May 2016 Consultation Paper *Credit Cards: improving consumer outcomes and enhancing competition.*

Cuscal is an end-to-end payments provider that services more than 100 established and challenger brand clients with access to Australia's financial system and payments landscape.

Our credit card issuing services include card production, transactional processing (switching), fraud and settlement. More recently Cuscal has begun offering clients access to a new credit card platform that will enable clients who take up this service to enhance their credit card offerings and increase their ability to compete for customers with the big banks which currently account for about 80% of the Australian market. Within this platform, Cuscal manages the majority of credit card processes while customer service and provision of credit remains with our clients. Credit cards offered by our clients, including customer owned banking institutions as well as a number of regional banks and challenger brands, typically have lower average rates, more interest free days and lower annual fees.

The proposed changes therefore have both a direct and an indirect impact on Cuscal.

Cuscal supports Treasury's goals of improving consumer outcomes and enhancing competition in the Australian Credit Card market. Cuscal believes that this needs to be achieved efficiently and in recognition of the advantages that access to a flexible credit tool provides to customers, including those that may be susceptible to the risks of behavioural bias. In addition, the introduction of further regulation on the credit card industry can impose a dis-proportionate cost burden on smaller competitors, putting upward pressure on the fees and interest they must charge to maintain the viability of their products. This may have the unintended consequence of decreasing competition in the market.

Our comments below reflect these balances.

Proposal 1

Prescribe a credit limit to be unsuitable if a customer cannot to repay the limit within a reasonable time period.

Cuscal believes that this proposal may have unintended consequences which overall may have greater costs than benefits for consumers.

The proposal seeks to have the dual aims of reducing indebtedness (by lowering credit limits) and making it more affordable for customers to pay off their maximum debt more quickly, thereby reducing the interest paid over the life of the card.

We are not optimistic that the proposal will achieve those outcomes for the following reasons:

1. We have not seen evidence to support the proposition that consumers will react to a lower credit limit by increasing their monthly repayments. We note the research referred to in the consultation paper, indicating there to be a small proportion of customers who regularly pay only the minimum amount, or a small amount above the minimum amount (which the Consultation Paper refers to as the "anchoring effect"). We think that this anchoring effect will make likely that consumers who are currently disposed to pay only the minimum monthly payment would continue to pay only the minimum monthly payment under a lower credit limit, even if they could afford to pay more.

2. While we expect that the introduction of this proposal will lower credit limits generally, it may be hard to judge the overall outcome because of risk buffers that credit providers apply in assigning credit limits. To some extent credit providers may be able to adjust other risk settings to reduce those buffers, such that an increase in the serviceability assessment does not translate to an equivalent reduction in credit limits.

3. We have concerns that the proposal will have the effect of reducing access to credit cards by those consumers who may currently only be able to apply for cards at the lowest available credit limit. While that may reduce credit stress for some customers, we think that reducing the access of this cohort to credit cards is unlikely to eliminate their demand for credit, for example to meet unexpected costs. Instead these customers may be forced into higher interest credit contracts (e.g. from payday lenders).

4. In addition, if the proposal is successful in lowering credit limits overall, this may disadvantage a majority of customers who are not at high risk of credit stress but benefit by the ability to use the larger credit limit from time to time.

5. A reduction in credit limits on individual cards may have the effect of increasing the average number of cards held by consumers, which could perversely increase overall credit limits.

We therefore do not think that this proposal offers an efficient means of protecting customers.

Alternative proposal for consideration:

We note that Treasury has already considered an option to raise minimum repayment amounts though it is not preferred. The detail of that option has not been set out in the Consultation Paper.

Cuscal proposes that Treasury consider a related alternative which we believe have a greater impact on customer protection with less disadvantage to customers overall. This could be achieved by retaining current assessment standards for credit limits but requiring a customer's minimum payment to be sufficient to cover the interest charges and fees for each statement period <u>plus</u> an amount to reduce the outstanding balance. [1]

[1] We suggest the initial credit assessment would remain based on 2% of the maximum credit limit. Where the interest, fees and 1% of the outstanding balance amounted to less than 2% of the outstanding balance, then the minimum repayment would revert to 2% of the balance.

For example a customer with a credit limit of $5000, an outstanding balance of $4000 including interest and fees of $60 for the month, would currently have a minimum repayment of $80 (based on 2% of the balance.) If the customer was required to pay the interest and fees plus a reduction of remaining balance by 1%, the minimum repayment would be increased to $99.40.

Under this rule, every minimum payment would always have the effect of lowering the balance so that interest would not accrue on previous interest. There may be some short term disadvantage to revolving customers while they adjust to the slightly higher minimum payment requirements, but this could be overcome by transition provisions.

The application of this rule would force a behavioural change on those customers who are in the habit of only paying the minimum repayment. It would not reduce access to credit and would not disadvantage "transactors" who regularly pay off their card balance.

We acknowledge the "costs" to consumers that Treasury has identified at page 34 of the Consultation Paper also apply to this alternative, but we suggests that those costs are less than the costs associated with Treasury's preferred proposal and that the benefits are greater.

Other Considerations – Comprehensive Credit Reporting

We think that Treasury's goals would be substantially boosted if comprehensive credit reporting (CCR) were utilised universally. CCR allows credit providers to view the actual number of credit cards a customer holds and each limit, as well as a depth of repayment history. With this information, card issuers are much more likely to identify those customers who are more at risk of financial hardship and adjust credit limits accordingly.

Without this information, credit assessments must rely on customer disclosure and less reliable indicators of credit stress, such as the number of previous card applications, and defaults recorded. While larger lenders often have access to customer transaction accounts, or other loan accounts, from which they can verify customer income and expenses, smaller or specialised lenders without that information have comparatively more difficulty applying the principles of responsible lending and must place more reliance on customer disclosure.

Although the legislative framework and the infrastructure for CCR now exists in Australia, the system is not maximising its potential for increasing responsible lending because contribution to CCR data remains voluntary, and the banks who control the majority of this data have been unwilling to share it. Cuscal would urge Treasury to examine the benefits of mandatory CCR reporting as an alternative or addition to its proposals.

Proposal 2

Prohibit Unsolicited Credit Card Limit Increases

Cuscal acknowledges there are divergent views on this issue and supports the closure of loopholes currently being utilised to circumvent the intention of current legislation.

Proposal 3

Standardise application of interest free periods and the effect of part payments.

Cuscal agrees that the application of interest free periods can be complex and inconsistent and that in general interest free periods are lost unless balances are paid off in full. We are less convinced that this results in consumer detriment, as we would expect that the reward associated with full repayment of balance should act to stimulate more "transactor" behaviour and less "revolver" behaviour, thereby decreasing overall indebtedness and the overall amount of interest paid by consumers.

Cuscal also notes that interest calculations of this type are likely to involve considerable changes to core banking systems and card management systems with which we are familiar. If this proposal is implemented, we expect the once off costs to be very significant and stakeholders will need considerable time to complete their own implementations.

We also anticipate that any revenue that may be lost by credit card providers associated with this change is likely to find its way back to customers through increased fees or interest charges along with a recoupment of the costs of implementation. We expect that the implementation costs of this change will affect smaller issuers disproportionately, and that the change may therefore have an adverse impact on competition.

Proposal 4

Provide simple options for electronic cancellation of credit cards.

While Cuscal agrees in principle that credit card accounts should be easy to close we would question whether having an electronic means of cancellation will lead to more customers who are at risk of hardship cancelling their credit card. We suspect that the reason for customers in this category not closing credit cards is one of motivation, rather than ease of closure.

While Treasury has listed a benefit of this proposal as being increased competition by providers because of an increased threat of losing business, we think simplifying account closure alone is unlikely to lead to increased switching. There is already considerable competition in the market as indicated by the number of zero dollar balance transfers currently available. In our view a much greater impediment to credit card switching is the time associated with the transfer of direct debit and recurring payment authorisations. We think measures to facilitate the transfer of those authorisations to new card numbers would be much more effective at promoting competition. Those measures could include extending current switching legislation covering transaction accounts to credit card accounts and encouraging merchants to simplify their processes for updating card information.

We also think this proposal could have important ramifications depending on its final detail. For example, if credit providers are able to receive and provide a customer's instructions to close an existing account with another institution, we think this would favour larger banks who could commit more resources to promoting the closure of accounts held with smaller lenders.

Proposal 5

Provide better information and clearly display annual costs and fees.

Cuscal broadly supports this proposal but would appreciate the ability to review and comment on the proposed detail and format of the information once that detail is formulated.

Proposal 6

Clearly disclose interest rate and annual fee in advertising and marketing materials.

Cuscal broadly supports this proposal but notes the complexity associated with multiple rates that apply to credit cards (e.g. purchase rates, cash advance, special promotions and introductory offers).

Because the actual cost of credit usage is dependent on how that card is used, we do not think it appropriate to attempt to blend rates or provide some equivalent to the mortgage "comparison rate". We recommend that the required enhanced disclosure be limited to the purchase rate and on-going annual fees.

We also note that this proposal seems to overlap with the purpose of the "Credit Card Key Fact Sheet" which was designed to allow comparability between cards. We suggest that Treasury analyses the current effectiveness of the Key fact sheets and considers its removal upon the implementation of this proposal.

Proposal 7

Issuers to provide personalised information on potential savings from alternative credit card products.

Cuscal has reservations about the benefits and the ability of the industry to implement this proposal. Credit cards are no longer generic products. Card issuers have differentiated their products through benefits and incentive programs that attach to their cards. Card issuers make information on their card range available to customers when they apply for cards, and the information is generally readily available on their web site. It is then up to the customer to decide the trade-off between a low rate and low cost card with minimum additional benefits, as opposed to a higher rate or cost card with higher benefits. The market is well served by comparison card web-sites that compare cards based on these various features.

As the credit provider does not typically have access to many factors influencing a customer's choice, we are not sure how a credit card provider would determine the basis for recommending a lower cost credit card and we think it would be very hard to standardise this across the industry.

We think that the goals of this proposal (of informed choice and increased competition) should be achieved by a combination of Proposal 5 and 6 which would increase competition by allowing customers to more easily compare their existing cards against current offerings between competitors, rather than just the offerings of a single competitor.

Proposal 8

Provide Consumers with timely electronic notifications regarding the expiry of introductory offers and credit utilisation.

Cuscal supports the policy behind this proposal but notes that this may be burdensome for some credit card providers to implement and that the cost burden is likely to disproportionately affect small credit providers. We assume the proposal would only apply to customers who gave permission to be contacted electronically.

Proposal 9

Consumers be provided the option to commit to higher repayments and proactively contact consumers making small repayments.

We think these need to be looked as separate proposals. Payment commitments can be fully automated, and many credit card issuers already offer this. For those that do not, we note that the cost burden is likely to be disproportionate for smaller providers.

It would also be possible to automate contact with consumers making small repayments, for example by text or email to alert them to the possibility of increasing those payments although again, there is a disproportionate cost burden to smaller providers associated with implementation.

If this proposal requires personal contact with each high risk customer to discuss tailored repayment options, then we do not think the extra consumer benefit would justify the significant costs that would be required to set up and maintain such a program. We think the cost imposition on smaller providers will have adverse impacts on competition.

While accounts remain in order (i.e. minimum payments are being met) credit providers cannot necessarily conclude that customers are in hardship. Customers may also find it presumptive of card issuers to assume they are approaching financial difficulty. We note that existing hardship protections already impose a number of measures on credit providers to help identify and assist customers who are facing financial hardship.

Overall, we think our alternative to Proposal 1 would be a more efficient way of improving minimum payment behaviour.

Thank you for the opportunity to comment. Please feel free to contact me if you wish to discuss our submission further.

Yours sincerely

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