



Submission to: SACC Review Panel

The Treasury

**Subject: Review of the small
amount credit contract
laws**

Submission prepared by:

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Uniting Communities

Uniting Communities works with South Australian citizens across metropolitan, regional and remote South Australia through more than 90 community service programs.

Our vision is: A compassionate, respectful and just community in which all people participate and flourish.

We are made up of a team of more than 1500 staff and volunteers who support and engage with more than 20,000 South Australians each year.

Recognising that people of all ages and backgrounds will come across challenges in their life, we offer professional and non-judgemental support for individuals and families

Consumer Credit Law Centre

The Consumer Credit Law Centre of South Australia (CCLCSA) was established in 2014 to provide free legal advice, as well as legal representation and financial counselling to consumers in South Australia in the areas of credit banking and finance. The Centre also provides legal education and advocacy in the area of credit, banking and financial services. The Consumer Credit Law Centre of South Australia is managed by Uniting Communities who also provide an extensive range of financial counselling and community legal services as well as a range of services to low income and disadvantaged people including mental health, drug and alcohol and disability services. Uniting Communities, through the CCLCSA, is particularly interested in this enquiry due to our extensive involvement in the provision of financial counselling over many years and ongoing advocacy on a raft of measures associated with financial matters, financial stress, and financial hardship for low and modest income households. Our particular focus is providing support to low income and disadvantaged households, and to building families and communities.

Discussion Questions

“The purpose of this review is to examine and report on the effectiveness of the law relating to small amount credit contracts (SACCs) and comparable consumer leases. These laws are contained in the *National Consumer Credit Protection Act 2009* (the Credit Act).” This submission is structured as responses to the questions posed in the discussion paper release on 17th September 2015

1. Competing Objectives

The need to protect consumers outweighs the need to ensure the profitability of the industry. If SACCs were goods rather than services and were found to be as harmful to consumers, it is likely they would be banned. It may be then that the best protection from small amount credit contracts and consumer leases is to remove them from the marketplace altogether. This is the preferred position of Uniting Communities, through the CCLCSA. We believe that no-interest loans and similar community-based financing for small amount loans is far preferable for the low income people who are drawn to very high cost small amount credit.

Failing that, given that up to 25 percent of consumers using SACCs have incomes below the Henderson Poverty Line, it is crucial that consumers understand the real cost of SACCs and consumer leases, and that appropriate consumer protection measures are in place and are enforced.

The CCLCSA is of the view that in addition to reviewing the current legislative framework, the government should:

- increase funding to programmes dedicated to increasing financial literacy amongst low- and moderate-income consumers;
- encourage alternatives to SACCs and consumer leases, such as, No Interest Loan Schemes (NILS) and StepUP Loans.

2. Complexity

No comments.

3. Sanctions

The current regime seems needlessly complex and relies heavily on the courts for enforcement. A more effective approach might be, at least for low-level offences, a system similar to that in effect for traffic offences, ie expiation notices.

For example, should a payday lender breach responsible lending provisions, then a regulator would issue an expiation notice. A point system might even be implemented leading to systemic review and possible loss of licence.

4. Obligation to obtain and consider bank statements

The obligations to obtain and consider bank account statements is a necessary requirement to ascertain consumer income and expenditure from credited amounts. To make it easier for credit providers to determine whether a consumer has existing SACCs, the direct debits on a bank account should show that the debit is for an existing SACC.

Alternatively, or in addition, credit providers might require that applicants provide the last two or three quarterly utilities bills. This might provide a clearer picture of the applicant's financial capacity.

5. Restrictions on repeat borrowing

Multiple SACCs is often an indication that the SACCs are not being used to simply smooth expenditure during income or consumption shock. Assuming that Centrelink benefits are sufficient to provide for essentials such as utilities, housing, food and clothing, then repeat SACCs may be symptomatic of other issues such as gambling, substance abuse or could be evidence that a consumer is using SACCs in a debt spiral because of limited understanding and awareness of other financial options available. A financial counsellor would be able to examine this and assist the consumer manage their finances better.

We believe consideration should be given to limiting the number of SACC loans a consumer can obtain in any given year. If the consumer requires multiple SACCs throughout the year, the consumer should be required to see a Financial Counsellor (accredited and working for an established NGO – welfare agency) for counselling. The Financial Counsellor could review the consumer's financial circumstances and if the Financial Counsellor determines that:

- an additional SACC is not unsuitable and that the consumer is able to meet their financial obligations without substantial hardship; and
- the consumer does not meet criteria for alternative loans such as NLS and StepUp Loans,

then the Financial Counsellor could issue a certificate, which would allow the consumer to apply for another loan.

Further, we note that SACC providers currently rely on consumers to inform them of their existing SACCs. Our experience has been that many SACC consumers do not read or understand questions asking them about other SACC loans or whether they are in default. Alternatively, some consumers simply do not answer the questions truthfully in order to obtain the loan. The difficulty is that in determining whether the presumption applies to make a SACC unsuitable, SACC providers must, at least in part, accept and rely on information provided by consumers. The proposed database would be a useful tool in assisting SACC providers determine the number of SACCs a person has or has applied for.

We also note that whilst an appropriate poverty benchmark could be incorporated as a presumption that a loan is unsuitable, the concern is that consumers and/or SACC providers might be tempted to *adapt* figures to meet any benchmark. Therefore, any application for a SACC and financial statement should be certified by a credited financial counsellor to ensure that an individual can meet the financial obligations of any SACC.

With regard to 'poverty line' income as a measure to be considered, we suggest that while the Henderson Poverty line is an excellent measure of poverty that we have used it earlier in this submission and is updated regularly, the many variables make it cumbersome to easily apply as a test, along with other capacity to pay measures. We suggest that where a poverty line income test is helpful that the 60% median income 'poverty line' is easier to apply. Currently 60% of media equivalised income for Australia is \$27,550.

6. Ban on short-term credit contracts

The CCLCSA has not dealt with any short-term lending less than 15 days by a credit provider to comment.

7. Warnings

Clients have come to the CCLCSA who have either not read or not understood the warnings. It might be useful to create an online questionnaire/quiz that the applicant needs to complete first, as part of the application process, as a means of both explaining the warnings and as an indication that the applicant understands the warning.

The warnings might also highlight the cost of the SACC loan, both in dollar terms and the effective annual interest rate.

In addition, warning statements should also advise applicants that they may be eligible for other, cheaper loan options such as a NILS or StepUP Loan.

Case Study:

Barbara was on the DSP and her washing machine broke down. She was not eligible for a credit card and did not want a consumer lease as she knew that she would pay a significant amount more than the retail price. Barbara read the warning statement and thought that as she already had a Centrelink advance, she did not have any other options. Barbara did not have access to the internet to read the MoneySmart website. When Barbara visited the Consumer Credit Law Centre SA about her payday loans, she found out about no interest loans and StepUP Loans for the first time. Barbara would have been eligible for either but the warning statement did not mention these other options available to her.

It is our general observation that SACC and consumer lease clients do not typically use or read the MoneySmart website. Others lack the capacity to take advantage of the 'self-help' nature of the website. These clients might benefit from directed, face-to-face community education that focuses on the financially disadvantaged.

Funding should be made available to promote consumer awareness of the No Interest Loan Scheme, StepUP Loans and the Good Money stores. Consumers should be required to get financial counselling from a certified financial counsellor at an NGO before entering into a SACC.

8. Cap on costs

Prior to the current cap regime, the Consumer Action Law Centre and others lobbied strongly for a 48% cap inclusive of all fees. Industry argued that such a restrictive cap would render payday lending unprofitable resulting in lost jobs for the industry and lost opportunities for credit for consumers. The 48% cap inclusive of fees was subsequently rejected in favour of the current regime.

The current cap on costs has clearly had little effect on industry viability. The expansion and reported annual revenue of various SACC providers together with the number of new SACC providers entering the market, suggests that current caps are not hindering the industry.

Less clear is whether the cap has provided adequate protection to consumers. Lenders' profits, measured in the millions of dollars, are maintained by an effective annual interest as high as 742%. The result is that those consumers least able to afford it are paying government-approved usurious interest rates to access credit.

In our view, there are a number of ways to establish a more reasonable interest rate, for example:

- Set the rate as previously suggested at 48% inclusive of all fees; or
- Set the rate (inclusive of all fees) with reference to the Reserve Bank Cash Rate, which allows the rate to fluctuate with the market; or
- Set the rate (inclusive of all fees) with reference to the average credit card interest rate, eg no more than 10% above the average bank credit card interest rate.

9. Protection for Centrelink customers

The protection afforded consumers who receive more than 50% of their income from Centrelink benefits has not necessarily protected all Centrelink customers. This is because SACC providers predominantly rely on information provided by applicants and do not make further inquiries beyond the information supplied by customers. For example, consumers on Centrelink may not disclose that they have other SACCs, which they have recently applied for at the time of making a SACC application. These clients end up spending more than 20% on SACC repayments as the SACC provider was unable to take into account these other current SACC loans. A national database would clarify matters for both parties.

We note however, that SACC providers might consider an application with reference only to the 50/20 protection without actually assessing the customer's real capacity to re-pay the loan.

Further, there are low-income earners who are financially in the same or worse position as a Centrelink recipient who are not afforded the same protection, and probably should be.

10. National database

The CCLCSA strongly supports the introduction of a national database. The database should be used as part of the responsible lending obligations to verify that a SACC is not unsuitable by allowing the provider to check whether a consumer has defaulted or had 2 or more SACCs in the preceding 90 days.

The database should be managed by a government agency and adopt similar principles to the Personal Properties Securities Register. Specifically, the SACC provider should be able to rely on the information in the database as definitive with respect to showing how many SACCs and SACC defaults an applicant has at the time of application. It should be a mandatory requirement that a SACC provider check the database prior to approving a loan.

The database should not be managed by a third party, but rather managed by a government agency accessible to all members of the public and not limited to those who used the internet.

All SACC providers should contribute to the funding of the database. This can be accomplished through licensing fees and/or through usage fees. It should be mandatory to report both SACC applications and SACC loan disbursements. A fee should be payable by the provider upon making a mandatory notification to the register and when accessing the database to offset the administrative cost of the database. These costs should not be passed on by the provider to the customer.

The database should be accessible by consumers, SACC providers and other credit providers for the restricted purposes of verifying information and/or making responsible lending inquiries when assessing the suitability of a SACC.

11. Additional provisions

Much of the Act deals with regulating the providers, but little to address the behaviour, education, understanding and responsibility of individual consumers. There should be greater emphasis on providing support to develop financial literacy, particularly amongst the vulnerable and disadvantaged.

12. Anti – avoidance provisions

The CCLCSA does not have any comments.

13. Documentation of suitability assessments

The CCLCSA has observed that each SACC provider uses different documentation to assess suitability.

In our view, required documentation should be regulated and consistent across lenders. Perhaps a system similar to the 100-point ID check should be considered, for example:

- An assessment must be based on X points of financial documentation depending on the size of the loan;
- Each type of documentation earns a set number of points;
- Proof of income in the form of payslips or Centrelink payment summary should be compulsory.

If the applicant cannot achieve the required number of points, the application cannot be approved.

14. Comparable consumer leases

Consumer leases having the following features are comparable to SACCs:

- regardless of whether the consumer has legal title or a contractual right to acquire legal title, the consumer keeps the good and/or uses the good over the term of the good's economic life;

- consumer leases used to smooth expenditure shock and to maintain basic standard of living such as those for essential household appliances, whitegoods and furniture;
- the retail value of the goods is less than \$2,000;
- lease terms tend to be for a shorter duration than other forms of credit such as personal loans or credit cards; and
- a similar client base ie Centrelink recipients and low to moderate income earners.

Such leases are a popular means of financing whitegoods, household goods and appliances where widespread industry practice is for the lessee to retain possession for the effective life of the goods.

The CCLCSA supports amending the National Consumer Credit Protection Act to ensure that

- regulation focuses on the substance of the transaction rather than its form – there should be no distinction between consumer leases with or without a contractual right to purchase goods;
- consumer leases for amounts less than \$2,000 are treated similarly to SACCs affording the same protections and imposing the same obligations on providers; and
- all consumer lease providers are subject to pre-contractual disclosure and caps on cost to protect vulnerable and financially disadvantaged consumers.

The current regime has led to providers creating an artificial distinction between consumer leases based on whether or not the consumer has the contractual right to retain goods at the end of a lease in order to circumvent the more restrictive provisions of the NCCPA such as costs caps. As a result, consumers, particularly vulnerable consumers, end up paying much more for essential household whitegoods, appliances and furniture. The effective cost of a consumer lease as an interest rate exceeds any other form of finance.

Further, different lessors charge different amounts for the same goods and some lessors charge Centrelink recipients more for the same good. This practice is harmful to a vulnerable group of consumers with limited access to alternative forms of finance. Consumers entering into consumer leases for essential household whitegoods, appliances and furniture pay significantly more than the retail price of goods and more than what a lender is permitted to charge under a small amount credit contract.

The intent of a consumer credit protection regime is undermined if consumers are not provided any disclosure which would allow them to compare leases and other credit products. The current lack of both protections (such as costs caps) and disclosure, has caused significant harm to vulnerable and disadvantaged consumers who pay disproportionately more for leased goods (see ASIC Report, Cost of Consumer leases (September 2015)).

Case Study:

Michael receives Newstart Allowance and lives in a remote town in South Australia. After separating from his wife, he moved into rental accommodation to start his life over again. He applied for a credit card and a pay day loan and was declined. He thought about buying second-hand furniture but did not have access to a motor vehicle to collect furniture. Michael was expecting his children to come and visit and was desperate to purchase a fridge, television and fold-out lounge for their visit. Michael saw an advertisement that he could rent a fridge,

television and lounge. Michael entered into an indefinite period lease. Several years later, Michael saw a financial counsellor. The financial counsellor calculated that Michael had paid over \$9,000.00 to lease the fridge, television and lounge. Michael did not know the retail price of the goods at the time but it was clear that he had paid many times above the purchase price for these essential household items. The financial counsellor tried to negotiate with the lessor for Michael to stop paying the lease and for Michael to retain the goods, but the lessor refused to negotiate and threatened to repossess the goods and charge Michael a repossession fee if he stopped making payments.

Case Study:

Dorothy's television stopped working. Dorothy was on the Age Pension and had a GE Money credit card with a 29% credit card interest rate. Dorothy heard on ABC radio that consumers should shop around for competitive credit card interest rates. Dorothy saw that her bank were advertising a cheaper credit card interest rate. Dorothy visited her bank to see if she could get another credit card and was declined. Dorothy received a catalogue in her letterbox advertising 'rent to buy' televisions. Dorothy visited the retailer and spoke to the salesperson who told her that she would be able to keep the television at the end of the lease term. Dorothy made the lease payments over the 2 year lease period and then received a letter about gifting the television to a third party. Dorothy did not understand why she did not own the television and sought advice. Dorothy had paid the lessor \$3,552.00 over the previous 2 years. Online research showed that the retail price for the television at the time Dorothy entered the lease was \$599.00.

If Dorothy had obtained a small amount credit contract to purchase the television, she would have paid \$1,408.85. And if Dorothy used her GE credit card to buy the television outright, she would have paid \$778.00. Dorothy was horrified to discover that in trying to avoid using her GE credit card that she had paid 16 times more for the credit (\$2,953 vs \$179). Finally, if Dorothy had known or been advised about the availability of the No Interest Loan Scheme, the television would have cost \$599.00.

Case Study:

Julie was a single parent on the sole parenting pension. Julie's 12-year-old daughter attended a public school. The school introduced iPad devices into the classroom requiring students to bring their own iPads from home. If students did not bring an iPad, they were given the option of borrowing an iPad from the school. Julie's daughter spent 6 months using an iPad borrowed from the school but constantly reported to Julie that she would have to rush to get an iPad or else she would miss out. On several occasions, Julie's daughter was unable to do her school work because she did not have access to an iPad. Julie's teacher suggested that she catch up at home but Julie did not have internet at home.

Julie had previously been declined a credit card. Julie thought about saving for an iPad but felt that her daughter was getting too anxious and distressed by not having her own iPad. When Julie's daughter asked for an iPad for her birthday, Julie decided to buy one. Julie had already used her Centrelink advance to pay an unexpected ambulance bill. Julie decided to get a pay day loan to buy an iPad. She was nervous about applying for a payday loan as she had

previously applied for a payday loan to buy a laptop but was declined because the repayments would have exceeded 20% of her Centrelink income.

Julie visited a retailer. The sales person showed Julie the iPads. When Julie said that she would pay cash but first had to get a payday loan, the salesperson explained to Julie about the option of leasing the iPad and that told Julie that she would be able to keep the iPad at the end of lease. The salesperson said this option would save her the hassle of having to apply for a payday loan. Julie quickly looked over the paperwork and believing she could make the fortnightly payments, she signed the contract.

The next day, Julie had a change of heart and tried to 'cool-off' but was told there was no 'cooling-off' period.

Some months later when Julie went to see a financial counsellor about financial hardship. The financial counsellor examined the consumer lease and discovered that it did not give Julie the right to purchase the iPad at the end of the lease. Further, Julie was paying considerably more than she would had the lease been of a type covered under the cost caps prescribed by the NCCPA (section 9 consumer lease).

The financial demographics for those who enter into consumer leases are similar to those who enter small credit contracts. That is, consumers with limited funds, often receiving Centrelink benefits and requiring access to credit of less than \$2,000 generally to smooth expenditure shock for essential living. Given their vulnerability, these consumers should be afforded the same protections as those entering into small credit contracts.

15. Applying SACC provisions to consumer leases

The CCLCSA suggests that the same provisions that apply to SACCs should also apply to comparable consumer leases.

In addition, the CCLSA supports greater disclosure to consumer lessees to include:

- the purchase and/or cash price of the good leased;
- the amount the consumer will pay in excess of the purchase and/or cash price;
- the cost of the credit expressed both as an interest rate and in dollar terms;
- a warning statement that a consumer may be eligible for other options such as the No Interest Loan Scheme and StepUP loans; and
- the cost of any other financial service.

However, the CCLCSA is concerned that disclosure and warning statements alone are insufficient to protect vulnerable consumers who often report to us that they could not read or understand the information provided to them. In addition, we see clients who were not aware of 'self-help' resources such as the MoneySmart 'rent vs buy' tool. In our view, more can and should be done to assist vulnerable and disadvantaged consumers understand disclosure and warning statements. Community education programmes would provide consumers with the skills they need to make informed financial decisions. In addition, media campaigns to increase awareness of 'self-help' resources, alternatives to high cost credit and leasing, financial counselling and free legal assistance are needed.

A majority of clients who seek advice from the CCLCSA report that at the time of entering into a consumer lease or small amount credit contract, they did not know about other alternatives to Centrelink advances such as the No Interest Loan Scheme or StepUP Loans. Some clients even report they read the warning statement but did not understand from the warning statement that there were other cheaper alternatives apart from a Centrelink advance. The CCLCSA recommends that the requirement for a warning statement should apply to all consumer leases and that such a statement should specify the low cost and no cost alternatives to SACCs and consumer leases.

The CCLCSA's view is that consumers should have the same protections whether entering into a SACC or comparable consumer lease, including:

- protection for Centrelink customers (similar to section 133CC of the NCCPA and regulation 28S) earning more than 50% of income from Centrelink benefits;
- costs caps;
- mandatory warning statements;
- the presumption that a contract is unsuitable if the applicant is in default on other SACCs or consumer leases or has had more than a prescribed number in the preceding 90 days.

The CCLCSA also supports the idea that any national database introduced for SACCs should also apply to comparable consumer leases.

The CCLCSA further recommends that provisions be introduced

- to regulate indefinite term consumer leases. For example, the lease term should not extend beyond the period a good can be depreciated for taxation purposes.
(See page 204 of 247 of TR 2014/4 - *Income tax: effective life of depreciating assets*: <https://www.ato.gov.au/law/view/document?docid=TXR/TR20144/NAT/ATO/00001>)
- to establish a cooling off period;
- to limit the number of consumer leases Centrelink recipients can hold at one time.

The CCLCSA is concerned that reference to SACC provisions such as the presumption test and protections for Centrelink customers has removed the focus of providers from making individual case assessments for each applicant based on the applicant's individual circumstances.

16. Cap on costs for consumer leases

The CCLCSA supports a cap on costs for comparable consumer leases. Caps on the amount charged above the cash price are necessary to ensure that the most vulnerable people in our society are not forced to pay exorbitant prices for essential household items.

The cap on costs should be determined with reference to a percentage of the cash price of the good. The term of the lease should not exceed the period a good can be depreciated for taxation purposes.

We note however that the cash price can vary substantially between providers. Some consumer lease providers are prone to inflate cash prices. Other retailers simply do not provide a cash price to avoid the contract being construed as a credit contract and therefore subject to the NCCPA. The definition of 'cash price' in section 204, that is, '*..the lowest price a cash purchaser might reasonably be expected to pay...*' should be more narrowly defined to avoid price manipulation by providers.