15 March 2021

Hon. Rebekha Sharkie MP
1/72 Gawler St
Mount Barker SA 5251

By email: Rebekha.Sharkie.mp@aph.gov.au

Dear Ms Sharkie,

RE: National Consumer Credit Protection (Supporting Economic Recovery) Bill 2020

We recently communicated with you last year to express our serious concerns about the *National Consumer Credit Protection (Supporting Economic Recovery) Bill 2020* (the Bill), and have more recently provided you with our submission made to the Senate Economics Legislation Committee (the Committee).

We understand that the Senate Economics Legislation Committee report is due to be presented to the Senate this Friday 12 March 2021. We understand that the Senate may vote on the Bill early next week. We are deeply concerned from what we hear that there will be pressure on independent Senators to support this Bill and of claims there will be duplicate and equivalent consumer protections. We urge Centre Alliance not to support this Bill because it:

- Is totally adverse to the recommendations from the Royal Commission;
- Will not increase economic activity;
- Will impact adversely on small businesses as people will have less money to spend at local small businesses;
- Will cause harm to vulnerable Australians who will lose valuable consumer protections.

Further detail

We are writing now in response to the Senate Committee recent public hearings relating to the Bill on 19 and 26 February 2021. In response to matters Committee Members raised and evidence presented at the hearing on 26 February 2021, we seek to highlight that there is nothing redeemable in the Bill. We are calling for the previous National Consumer Credit Protection Amendment (Small Amount Credit Contract and Consumer Leases) Bill 2019 (No 2) to be passed to avert the chaos that will be brought to consumer credit protection if the Bill proceeds:

- Default rates are not a proper measure of consumer harm as borrowers prioritise repaying credit contracts at expense of going without food or other basic essentials. This puts pressure on other welfare service providers and state governments.
- The logic seems flawed that Responsible Lending Obligations on the one hand are causing issues with timeliness of credit (six days to six weeks), yet the same obligation to make inquiries and verify information will remain part of the APRA standards.

- The Royal Commission showed that compliance with the law cannot be taken for granted simply because parliament passes legislation, particularly where there is lack of enforcement of the law.

- The Banking Code of Practice or other industry codes of practice can be implied as a term in credit contracts for subscribers to the Code. This is determined by industry and whether it creates a contractually binding obligation that can be enforced by a consumer at AFCA or in court, depends upon whether the statements are promissory. Subscribers could at any time amend the wording of the relevant code so that it is not promissory or change their obligations at any time. Subscribers could also unsubscribe themselves from industry codes.

- It is uncertain whether AFCA in determining the contractual duty to exercise care and skill of a prudent and diligent lender will apply APRA standards to an individual borrower. AFCA is not a judicial body and the mandate of APRA, dealing with systematic procedures and policies creates serious risk for consumers not being able to get redress.

- The internal policies of credit providers are difficult to obtain so a consumer would not be able to measure whether there is a case of maladministration and consumers will be making blind claims at AFCA.

- The removal of RLOs will lead to an increase in the number of bankruptcies as people lose the ability to raise responsible lending disputes to leverage a settlement outcome with their lender.

Case study

We refer you to our case study below which is an example of how consumers will be detrimentally effected should the Bill be passed:

Current state of affairs under the existing National Consumer Credit Protection Act 2009 (Cth), including responsible lending obligations

Joshua is eighteen years old. He lives with his grandparents and works as a permanent part-time employee for a local fast-food franchise. Joshua was interested in buying a second-hand motor vehicle and went to the local car dealership with his grandfather. Joshua was introduced to the finance person who asked Joshua to present his payslips. Joshua brought in all of his payslips since he started working six months earlier. Joshua believed he was doing the right thing. The finance person filled in the loan application form for Joshua and asked him to sign the documents. Joshua did not know the finance person had selected only some of his payslips where he had worked overtime and that the income stated on the loan application was based on weeks that he had been offered overtime hours. Joshua very quickly fell into financial difficulty as he was unable to manage the car repayments and the usual expenses associated with owning a vehicle such as insurance, tyres, maintenance and registration on his usual permanent part-time income. As Joshua was naïve to commercial transactions and his only experience was entering into a mobile phone contract, he did not realise that he could negotiate the price to purchase the car from the car dealership and agreed to pay a price higher than the average market value for the vehicle. Further, he did not realise that the finance person would enter an inflated amount on the loan application for his income and trusted the finance person.

Joshua received a Notice of Default and was referred to the CCLCSA. The CCLCSA was able to represent Joshua for a responsible lending dispute against the lender for failing to verify the information stated on his loan application. With the assistance of the CCLCSA, Joshua entered into a settlement agreement to return the car and for the credit provider to discharge and release Joshua from the contract without further payment. The car sold at auction only twelve months after Joshua purchased the car for less than half of the price he purchased the vehicle.

Without RLOs, Joshua would have had a shortfall debt of $20,000.00 and would have faced financial ruin into his future.

This case study about Joshua also demonstrates what is occurring with RLOs. The RLOs provide a remedy for consumers against lenders that do not abide by RLOs. Removing RLOs and the detriment that will be caused in reprehensible.

Alternative case study if the Bill is passed

Joshua is eighteen years old. He lives with his grandparents and works as a permanent part-time employee for a local fast-food franchise. Joshua was interested in buying a second-hand motor vehicle and went to the local car dealership with his grandfather. Joshua was introduced to the finance person who asked Joshua to present his payslips. Joshua brought in all of his payslips since he started working six months earlier. Joshua believed he was doing the right thing. The finance person filled in the loan application form for Joshua and asked him to sign the documents. Joshua did not know the finance person had selected only some of his payslips where he had worked overtime and that the income stated on the loan application was based on weeks that he had been offered overtime hours.

Joshua very quickly fell into financial difficulty as he was unable to manage the car repayments and the usual expenses associated with owning a vehicle such as insurance, tyres, maintenance and registration on his usual permanent part-time income.

As Joshua was naïve to commercial transactions and his only experience was entering into a mobile phone contract, he did not realise that he could negotiate the price to purchase the car from the car dealership and agreed to pay a price higher than the average market value for the vehicle. Further, he did not realise that the finance person would enter an inflated amount on the loan application for his income and trusted the finance person.

Joshua had his car repossessed and the lender sold it at auction and then pursued Joshua for the shortfall debt of $20,000.00. Joshua faced financial ruin into his future and was contemplating bankruptcy.

Joshua called the regulator, APRA, who told him that they were unable to assist him with his individual complaint. Joshua was told by his legal advisors that they did not have a copy of the internal lending policies of the lender to assess whether the lender had not complied with its own lending policies. Joshua was told he could lodge a dispute with AFCA and the lender may supply their internal lending policies to AFCA but that Joshua may not a get a copy to assess whether there was a breach of lending policy. The only way to do this was to get pre-action discovery orders from court but that would be costly. Joshua did not have the funds to go to court to get discovery.

Moreover, if Joshua filed a dispute with AFCA, it was not clear whether AFCA would apply APRA standards when determining if the lender was in breach of contract to exercise the care and skill of a prudent and diligent lender. Further, AFCA was not a judicial body and without any express law that provided Joshua with rights as an individual borrower, the legal situation remained unclear. Lenders could ask to use the test case provision of AFCA rules to have the position determined by a court. If

the court took the view that APRA standards are limited to systems and processes rather than extending to any contractual duties to borrowers, then all borrowers like Joshua would be without a remedy. Joshua looked at the AFCA website and saw that AFCA said they would look at principles of fairness and was left confused. Joshua did not understand the lack of transparency.

This case study about Joshua also demonstrates what will happen if RLOs are removed. The RLOs provide a clear remedy for consumers against lenders that will be at risk if removed. Significantly, even if AFCA applies APRA standards (or equivalent for non-ADIs), this will not protect vulnerable Australians where the loan was unsuitable for their requirements and objectives. Removing RLOs and the detriment that is reprehensible. Further, APRA standards will only deal with serviceability and not extend to requirements and objectives. People impacted by financial abuse will therefore not have the same redress in circumstances where a lender was not in position to have known facts the person was not exercising free will and/or did not understand the nature of the transaction. If APRA standards are part of contractual duties owed to borrowers, it will not protect people who are coerced into loan agreements as either borrower or guarantor. The role of the court is to interpret legislation but if rights of consumers are not express in the form of statutory consumer protections, there is great risk contract law will not protect all vulnerable Australians.

The Australian Financial Complaints Authority (AFCA)

Contrary to the views of Senator Bragg, AFCA haven't applied APRA standards in the past and AFCA have not indicated that they will apply APRA standards to individual borrowers' disputes. Therefore it is unclear whether consumers will have the same level of protection currently afforded by RLOs should the Bill pass. More specifically:

i. AFCA is not a judicial body. In order for AFCA to apply law, there needs to be legislation or common law developed by courts;
ii. AFCA cannot compel members to provide commercially sensitive material (such as credit assessments) to consumers to enable them to assess whether there have been breaches of policies;
iii. AFCA cannot decide facts where there is a dispute of facts – i.e. verbal statements made that are contested/not being able to subpoena and cross-examine witnesses;
iv. If the Bill is passed remnant laws will be extremely complex. It is likely that consumers and AFCA case workers will struggle to understand the complexities of remnant laws to apply them properly.

The Australian Prudential Regulation Authority (APRA)

The role of APRA is to ensure the financial stability of ADIs and funds of deposit holders – this is separate from consumer protection and enforcing individual borrower rights as successful claims reduce profits.

Why modifying APRA rules will not be adequate for consumer protection and present complex remnant laws that will be ineffective for consumers to access unsuitable lending

Passing the Bill and with amendments directing what APRA must include in APRA lending will not adequately protect consumers and will instead make consumer credit protection more complex. Once the statutory rights of individual borrowers are stripped away, the value of AFCA will become limited for borrowers and guarantors sold unsuitable credit as the remnant legal principles will not support consumers for maladministration of lending disputes. Nor will it become efficient to create one place to ascertain lending standards as the law will be different for ADIs and non-ADIs. Further, contractual

duties rather than statutory consumer protections will become the primary ground to dispute loans and will vary between each and every lender.

Even with APRA's amendment to APS 220, requiring that an ADI assess individual borrowers' capacity to repay without substantial hardship, the current Responsible Lending Obligations cannot be duplicated in APRA standards for the following reasons:

1. The lending standard does not require ADIs to assess whether a proposed contract is not unsuitable with regards to requirements and objectives of the borrower. As outlined in our submission, removal of the requirement to assess that a proposed loan is not unsuitable in context of requirements and objectives of borrowers, will cause harm to people impacted by economic abuse and vulnerable consumers with poor financial literacy. Similarly, the Bill will allow lenders to rely on information provided by the consumer, unless there are reasonable grounds to believe it is unreliable – the Royal Commission showed that borrowers were not always aware that information was incorrect and this will not prevent financial abuse of people who are coerced or have another person submit the loan application that can otherwise be identified with the current requirement to verify information.

2. APRA standards deal with systematic processes and do not provide rights to individual borrowers unless they can prove breach of the ADI's requirement for lending procedures and processes across portfolios rather than individual loans. This will become near impossible as copies of plans will be kept in-confidence.

3. Consumers cannot access documents to assess internal policies, procedures and processes to assess a claim the lender did not systematically ensure borrower's capacity to repay without seeking discovery orders at the Supreme Court. AFCA cannot subpoena documents and consumers cannot require discovery before making a claim as they can currently provided by the requirement to produce copies of credit assessments. Consumers effectively will have no recourse to enforce APRA standards and will rely entirely on APRA for enforcement.

4. The twin peak regulator model will be dismantled. APRA's mandate is to protect the interest of depositors and balance objectives of financial safety and efficiency, competition, contestability and competitive neutrality as outlined by section 8 of the Australian Prudential Regulation Authority Act 1998. The role of APRA, with legislative amendments to extend to consumer protection, will detract away from it optimally protecting deposit holders if APRA is expected to protect borrowers. Most concerning, expecting APRA to protect consumers is in direct conflict with the mandate to protect financial stability of ADIs. These functions are distinctly separate and should remain with separate regulators. Whilst APRA has done well to avoid a bank collapse, the Royal Commission and the subsequent capability review of APRA[1] revealed a lack of transparency and that '*APRA has a strong preference to do things behind the scenes with regulated entities*'. The propensity for secrecy due to the close relationship between ADIs and APRA also shows that APRA alone is not the appropriate regulator for consumer protection.

5. Remnant consumer protection laws will not enable consumers redress through AFCA as AFCA will unlikely be in any position to grant remedies as it can under our existing regime with the removal of borrower rights for breach of civil penalty provisions.

6. AFCA is not a regulator and does not have the powers or remit of a regulator. It is unclear whether AFCA can have regard to APRA standards that deal with requirements of ADIs to have

[1] https://treasury.gov.au/sites/default/files/2019-07/190715_APRA%20Capability%20Review.pdf at xviii

systematic processes and procedures, when assessing maladministration of lending disputes. Nor should AFCA be the sole interpreter of the law and the only source of redress for consumers against financial service providers. For example, the Consumer Credit Law Centre SA is currently seeking counsel opinion as to the way AFCA have interpreted and applied the law in South Australia and it is not certain that AFCA necessarily make decisions consistent with judicial bodies in South Australia for South Australian complainants. This is especially because decision makers in AFCA are located in eastern states and do not necessarily practice law in the state of South Australia. Most significantly, the remnant laws will be more difficult and result in becoming near impossible for consumers to defend against contractual claims seeking interest, fees and charges. The ultimate result of this Bill will be that for maladministration of lending disputes, credit providers will retain profit in the form of interest, fees and charges for loans that were unsuitable in the first instance.

The bulk of claims the Consumer Credit Law Centre SA assists consumers with involve breach of responsible lending obligations. The Bill proposes to remove the legal grounds relied upon by consumers for redress for unsuitable lending. The remnant laws will not provide consumers with adequate protection for maladministration of lending claims and these remnant laws are briefly summarised below:

1. Common law

A credit provider has no duty of care to a borrower, in terms of ensuring that a loan is prudent or not unsuitable for the borrower. The traditional common law principle is that a borrower will have their own opportunity to seek advice about whether they should obtain a loan or not, similar to the principle of caveat emptor or buyer beware.

2. Breach of contract – maladministration of lending

A borrower can make a breach of contract claim for breach of implied contractual duty to exercise care and skill of a prudent and diligent lender at the time of offering or providing credit – the standard of care to discharge the contractual duty is comparably a much lower standard compared to the responsible lending statutory duties. Further, to assess if a lender has breached their own internal policies for lending, requires a consumer to have a copy of the internal policies which are commercially sensitive and not all lenders will release these documents.

Alternatively if the lender is a subscriber to the Code of Banking Practice or other voluntary code of conduct developed by industry at the time of offering the credit or loan AND the lender makes promissory statements in credit offer to incorporate the Code of conduct, then a borrower can claim breach of contract for failure to:

- Exercise the care and skill of a diligent banker;
- Take reasonable steps to ensure the borrower understands the risks associated with entering into the loan and satisfied there is no financial abuse when information provided in the course of applying for a loan, the applicant will not receive a substantial benefit.

However, judicial commentary has in the past criticised the drafting of the Code of Banking Practice for not being precise and ascertainable. The same criticism industry have raised about the drafting of the National Consumer Credit Protection Act has equally applied to the drafting of industry's own code of conduct by judges who interpret the law. In order for any statement to be contractually binding, it must be promissory and not vague or uncertain. There is a real risk courts in future can interpret the Code as not giving rights enforceable contractual obligations. Similarly,

a credit provider can at any time vary the drafting of a credit offer so that any terms in the credit contract referring to the code are not promissory so that the code can no longer be incorporated as contractual terms. Alternatively, a subscriber can unsubscribe to an industry code at any time. Moreover, even if terms are not void for being vague and uncertain, the contractual obligations are not as extensive as responsible lending obligations and therefore serve less protection. For example, in cases of financial abuse, the contractual term is to take reasonable steps to check there is no financial abuse where the information provided does not show that a borrower will receive a substantial benefit. The ADI can rely on information presented rather than having to initiate the enquiries. Therefore the risk of parliament relying on common law principles of contract law and industry self-regulation to ensure loans are not unsuitable to consumers is fraught with danger.

3. Equity law

3.1 Misrepresentation - verbal representation incorporated as term - verbal representation as a collateral contract

AFCA are not able to cross-examine or subpoena witnesses where there is a factual dispute of what was said. AFCA can exclude disputes in cases where court is a more appropriate forum to determine factual disputes as to any oral representations. From a litigation point of view, these cases are risky unless file notes of the lender corroborate and support the borrower's contentions as to what was stated to them at the time before entering the contract.

With regards to collateral contracts, often terms in a standard form contract contain an entire agreement term to exclude the operation of a collateral contract claim or verbal statement being incorporated as a contractual term.

3.2 Unilateral mistake

This requires evidence of what the lender knew or ought to have known about the mistaken understanding of the other party at the time of entering into the contract. The evidence is often not followed with a paper trail and as above, requires witness testimony in court.

3.3 Undue influence

The law in Australia does not go so far as the United Kingdom that a lender is put on constructive notice when a transaction is not in the individual borrower's favour to put the lender 'on inquiry'. In Australia, undue influence can be applied if a borrower can show actual undue influence or a presumption of undue influence and the party receiving the benefit was acting on behalf of the financial institution. The law developed by the courts in Australia is not as high or as protective as the law in United Kingdom to insist on an appropriate level of advice before documents are executed.

4. Statutory and equity law

4.1 Misleading and deceptive conduct

It must be the conduct that has led the member of the target audience into error and not the erroneous assumptions held by members of the target group. Omission can also constitute misleading and deceptive conduct. Often for consumer claims relating to misleading and deceptive conduct, where the conduct is not reduced and recorded into writing, a factual

dispute as to what in fact was verbally stated or presented to the consumer cannot in many instances be determined by AFCA.

4.2 Unconscionable conduct

Recent case law such as *ASIC v Kobelt* [2019] HCA 18 demonstrates the high threshold to succeed in claim of unconscionable conduct and that emphasis is not about a bad bargain reached due to the mere inequality of bargaining power but requires the stronger party taking advantage of a weaker parties vulnerability to obtain a benefit not otherwise obtainable. Removing consumer protections and reverting back to common law means that any borrower can enter into an unsuitable loan contract or bad bargain and their financial literacy does not in and of itself create grounds to set aside the agreement.

4.3 Section 47 of the ASIC Act -duty to act honestly, fairly and efficiently

It is unclear how this will apply but if there is no prescribed duty for a credit provider to make verifications of information, it would be difficult to see how this provision can be used and clearly is not an adequate substitute for responsible lending provisions.

4.4 Unfair contract terms

The requirement for a term to be struck down as void is that the term does not legitimately protect the commercial interests of the party seeking to rely on the term. It is unclear how this will protect consumers in relation to unsuitable loans as Senator Bragg seemed to suggest.

We are available to discuss our concerns and data from our casework in more detail with you. Please contact David Ferraro at the Uniting Communities Consumer Credit Law Centre on (08) 8342 1800 to organise a suitable time, or for further comment.

Yours sincerely,

Simon Schrapel AM
Chief Executive
Uniting Communities