



choice



3 November 2017

By email: consumercredit@treasury.gov.au

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Dear Sir/Madam

Small Amount Credit Contract and Consumer Lease Reforms

We write in relation to the Exposure Draft Bill (**the Bill**)¹ and Explanatory Materials implementing the Government's response to the Small Amount Credit Contracts Review (**the Review**).

We strongly support the proposed reforms to small amount credit contracts (**SACCs**) and consumer leases. Our organisations were actively involved in the consultation period of the Review, and some of our submissions were noted in the Review Final Report. We regard the proposed cap on costs for consumer leases, and the 10% protected earnings amount for

¹ *National Consumer Credit Protection Amendment (Small Amount Credit Contract and Consumer Lease Reforms) Bill 2017 (Cth)*.

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consumer leases and payday loans as particularly critical reforms that would provide much needed protections for vulnerable borrowers. We would strongly oppose more lenient caps, which would entrench ongoing financial exclusion and fail to address the harm caused by these products.

Where this submission is silent on proposed reforms, we can be taken as being supportive. Our additional comments below relate largely to technical amendments.

The Government's response to the SACC Review

Following a comprehensive consultation period, the Review Panel made twenty-four recommendations that would provide significant additional protections for vulnerable consumers, and reduce the harm caused by SACCs and consumer leases. The Government accepted most of these recommendations in November 2016.

The recommendations, and the Government's subsequent response, were made following thorough consultation with the industry and the community sector, having regard to significant data and academic research. The Government has taken a sensible approach to balancing the interests of all parties, considering the need to protect vulnerable people and promote financial inclusion. As noted by the Review Panel, access to finance irrespective of the cost does not necessarily mean that a consumer is financially included.²

Data released following the Government's response

Since the Government's response, we have continued to see payday lenders and consumer lease providers causing harm to vulnerable people, and flouting the law. Significant ASIC enforcement actions since the response include:

- requiring consumer lease provider The Rental Guys to refund more than \$100,000 to vulnerable consumers;³
- requiring consumer lease provider Motor Finance Wizard to pay over \$11 million in remediation over responsible lending concerns;⁴
- requiring payday lenders Good to Go Loans Pty Ltd and Web Moneyline Pty Ltd to write off and stop offering loans intended to avoid payday lending regulation;⁵

² Review of the Small Amount Credit Contract Laws, *Final Report*, March 2016, p. 3, available at: https://static.treasury.gov.au/uploads/sites/1/2017/06/C2016-016_SACC-Final-Report.pdf.

³ Australian Securities and Investments Commission, *17-243 The Rental Guys refund more than \$100,000 to vulnerable consumers*, 20 July 2017, available at: <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2017-releases/17-243mr-the-rental-guys-refund-more-than-100-000-to-vulnerable-consumers/>.

⁴ Australian Securities and Investments Commission, *17-150MR Motor Finance Wizard to pay over \$11 million in remediation over responsible lending concerns*, 24 May 2017, available at: <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2017-releases/17-150mr-motor-finance-wizard-to-pay-over-11-million-in-remediation-over-responsible-lending-concerns/>.

⁵ Australian Securities and Investments Commission, *17-343MR ASIC concerns see Good to Go Loans Pty Ltd stop offering loan products*, 12 October 2017, available at: <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2017-releases/17-343mr-asic-concerns-see-good-to-go-loans-pty-ltd-stop-offering-loan-product/>. See also: <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2017-releases/17-344mr-asic-concerns-see-web-moneyline-pty-ltd-stop-offering-loan-product/>.

- banning the director of an unlicensed payday lender for three years;⁶
- obtaining a \$730,000 fine against payday lenders for a diamond trading avoidance 'sham';⁷ and
- cancelling the credit licence of consumer lease provider Rent to Own Appliances.⁸

The Credit and Investments Ombudsman (CIO) has also released data suggesting systemic problems in the consumer lease and payday loan sectors. The CIO's recent Annual Report on Operations reported that small and medium amount lenders accounted for 12.2% of complaints, the second-highest following debt collectors. Most of the complaints about small and medium amount lenders related to inappropriate finance including irresponsible lending (56.1% of those complaints). The report also stated that some consumer lease providers had begun filing police reports for payment defaults.⁹ The CIO also identified unconscionable conduct by a consumer lease provider targeting vulnerable people in remote NSW, which saw the lease provider ejected from the scheme.¹⁰

We have also seen data released by the industry itself that suggests there are serious systemic problems with the fringe finance industry. According to payday loan industry data, in the 2015/16 financial year¹¹ there were 619,549 new payday loans with \$476.8 million advanced. Two in five (39.8%) people who entered into a SACC loan in this period were unemployed and one in four (26.4%) SACC loans were given to people receiving more than 50% of their income from Centrelink. One in six (16.7%) SACC loans were entered into with a customer with an existing SACC loan. In Q2 2015, 75% of lenders admitted to providing SACC loans to customers who have had two or more SACCs in the previous 90 days,¹² despite these loans being presumed to be unsuitable for borrowers under the NCCP Act.¹³ The data also shows that most people now apply for loans online (78.3% in Q2 2016), making these loans quicker and easier to obtain than ever before. The same industry data for 2015/16 indicated that the average size of a new payday loan entered was \$770, and the average length was 134 days.¹⁴ This is equivalent to a comparison interest rate of 190.2%.¹⁵

⁶ Australian Securities and Investments Commission, *17-336MR ASIC bans director of unlicensed payday lender*, 6 October 2017, available at: <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2017-releases/17-336mr-asic-bans-director-of-unlicensed-payday-lender/>.

⁷ Australian Securities and Investments Commission, *17-060MR Payday lenders fined \$730,000 for diamond trading 'sham'*, 10 March 2017, available at: <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2017-releases/17-060mr-payday-lenders-fined-730-000-for-diamond-trading-sham/>.

⁸ Australian Securities and Investments Commission, *16-403MR ASIC cancels credit licence of Rent to Own Appliances*, 23 November 2016, available at: <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2016-releases/16-403mr-asic-cancels-credit-licence-of-rent-to-own-appliances/>.

⁹ Credit and Investments Ombudsman, *Annual Report on Operations 2016/17*, October 2017, p. 35, available at: <https://www.cio.org.au/assets/4130557/CIO%202017%20Annual%20Report%20on%20Operations.pdf>.

¹⁰ Ibid p. 71.

¹¹ National Credit Providers Association, *CoreData Small Amount Credit Contract Research*, December 2016, available at: <http://www.ncpa.net.au/assets/reports/2017/Core%20Data%20SACC%20Report%20Dec%202016.pdf>.

We note the most recent CoreData research is not available to the public on NCPA's website as at 3 November 2017.

¹² National Credit Providers Association, *Submission to the Review of the Small Amount Credit Contract Laws*, 15 October 2015, p. 15, available at: <http://www.ncpa.net.au/assets/submissions/2015/NCPA%20Submission%20to%20SACC%20Review%20October%202015%20-%20FINAL.PDF>.

¹³ *National Consumer Credit Protection Act 2009* (Cth) s131(3A).

¹⁴ National Credit Providers Association, *CoreData Small Amount Credit Contract Research*, December 2016, available at: <http://www.ncpa.net.au/assets/reports/2017/Core%20Data%20SACC%20Report%20Dec%202016.pdf>.

¹⁵ Comparison rate calculations completed using RiCalc software assuming maximum permitted fees and charges, and fortnightly repayments. 190.2% comparison rate calculated using a 134 day loan of \$770 with total repayments of \$1078.

Since the Government's response, the United Kingdom financial regulator, the Financial Conduct Authority (**FCA**), has also released research that shows people whose payday loan applications are rejected are generally better off as a result.¹⁶ The FCA found that the majority (63%) of declined consumers believe they are better off as a result. While declined applicants were on a trajectory of increasing debt, this trend was not accelerated after their applications were declined. Many individuals' accumulation of debt slowed down. The FCA said they had not seen a significant 'waterbed effect' with consumers increasing their use of other high cost credit products after failing to get a payday loan, with 60% of declined applicants not going on to borrow from other sources. Further, while 20% of declined individuals reported that they needed the loan to pay a bill, only 1% stated that they missed a bill payment as a result of not receiving credit.

Importantly, the FCA did not see evidence of a rise in illegal money lending because of the price cap, or that declined or former users of payday loans were increasingly turning to illegal money lenders. That FCA also suggested that consumer demand for payday loans was firm-led, rather than led by necessity. When asked their main reason for choosing a payday lender, the most common answer people gave was that they had been attracted by the firm's advertising, with 27% of the surveyed group giving this response.

Given this overwhelming evidence, we reiterate our strong support for the reforms proposed in the Bill.

Commencement

Under the Bill, the proposed reforms would not apply until 12 months after the date of Royal Assent. In our view, this transition period is overly generous. The industry has been on notice about these reforms since November 2016 when the Government responded to the Review. Given the importance of these reforms, we recommend the provisions in the Bill apply from 6 months after the date of Royal Assent.

Recommendation 1: Apply the reforms from 6 months after the date of Royal Assent.

Item 1 – Definition of consumer lease for household goods¹⁷

The Bill introduces the concept of a 'consumer lease for household goods'. This is a new definition, which specifically excludes motor vehicles. The cap on costs and anti-avoidance provisions apply to all consumer leases, including motor vehicles. We are very supportive of these provisions applying to all consumer leases. However, we are concerned that the remaining consumer lease reforms in the Bill would only apply to consumer leases for household goods. The Government flagged consideration of motor vehicle consumer leases in its response to the Review, and consultation process for the Review was extensive. For this reason, motor vehicle consumer lease providers cannot claim to have had no opportunity to contribute to this debate and ignorance of the consultation process is no defence.

¹⁶ Financial Conduct Authority, *High-cost credit including review of the high-cost short-term credit price cap – Feedback Statement FS17/2*, July 2017, available at: <https://www.fca.org.uk/publication/feedback/fs17-02.pdf>.

¹⁷ See s5(1) and *National Credit Code* s204.

Motor vehicle lease providers target consumers that cannot access mainstream motor vehicle finance due to their financial position or credit history. We have received many complaints in relation to motor vehicle consumer lease providers Motor Finance Wizard¹⁸ and Carboodle.¹⁹ As noted above, ASIC has also recently taken enforcement action against Motor Finance Wizard in relation to irresponsible lending. Under the enforceable undertaking, Motor Finance Wizard was required to pay over \$11 million to vulnerable consumers across Australia.²⁰

Like consumer leases for household goods, these products generally charge highly inflated prices and contracts can lock consumers into long-term arrangements. Repayments on these arrangements can also take up a high proportion of a borrower's income, just like consumer leases for household goods. Returning the vehicle may impose a termination fee, which is unaffordable to the average person who is targeted by these providers. We recommend removing the distinction between consumer leases for household goods and other consumer leases in the Bill. This would effectively require motor vehicle consumer leases to comply with the new suite of protections in the Bill, including disclosure about the cost of credit.

Recommendation 2: Remove the distinction between consumer leases for household goods and other consumer leases.

Items 10 and 22 – Unsolicited SACC invitations²¹

Items 10 and 22 would prohibit SACC providers and credit assistance providers from making an unsolicited SACC invitation to a current customer, or a customer who has had a SACC within the last two years. The provisions do not prohibit third parties generally (other than credit licensees) from making unsolicited invitations, but a SACC provider is exposed to losing its charges if it enters into a SACC with the recipient of such a communication.

However, a credit licensee would only breach these provisions if they *knew* the person had received an unsolicited invitation. We anticipate the proving knowledge of a credit licensee for the purposes of these provisions would be very difficult. In addition, requiring proof of knowledge is inherently inconsistent with the provision's classification as a strict liability offence. Offences of strict or absolute liability do not require proof of fault elements (such as knowledge) and consist of physical elements only.²² In our view, the provisions set an unreasonably high evidential barrier,

¹⁸ Consumer Action Law Centre, *Motor Finance Wizard - general information*, 27 September 2012, available at: <http://consumeraction.org.au/motor-finance-wizard-general-information/>.

¹⁹ Consumer Action Law Centre, *ASIC raises concerns about Carboodle's potentially misleading representations*, 9 April 2013, available at: <http://consumeraction.org.au/asic-raises-concern-about-carboodles-potentially-misleading-representations/>.

²⁰ Australian Securities and Investments Commission, *17-150MR Motor Finance Wizard to pay over \$11 million in remediation over responsible lending concerns*, 24 May 2017, available at: <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2017-releases/17-150mr-motor-finance-wizard-to-pay-over-11-million-in-remediation-over-responsible-lending-concerns/>.

²¹ See ss124C(5), 133CG and 133CF(5).

²² *Criminal Code Act 1995* (Cth) Schedule – The Criminal Code, Division 5 and Attorney-General's Department, *The Commonwealth Criminal Code: A Guide for Practitioners*, p. 49, available at: <https://www.ag.gov.au/Publications/Documents/GuideforPractitioners.pdf>.

and are logically inconsistent with the classification of these provisions as strict liability offences. We therefore recommend amending Items 10 and 22 to remove the knowledge element.

The Bill also limits the prohibition on making an unsolicited SACC invitation to current customers, or customers who have had a SACC within the last two years. This two-year limitation was not recommended by the Review Panel, nor did it form part of the Government's formal response. This limitation is also inconsistent with the total prohibition on the unsolicited selling of financial products²³ and the proposed prohibition on unsolicited credit card limit invitations.²⁴

Recommendation 3: Amend Items 10 and 22 (ss 124C(5)(a) and 133CF(5)(a)) to remove the knowledge requirement, which adds an unnecessary fault element to the strict liability offence for making an unsolicited SACC invitation.

Recommendation 4: Apply the prohibition on unsolicited SACC invitations to all consumers. At a minimum, the prohibition should apply to all current and previous SACC customers.

Items 6, 14, 27 and 33 – Providing assessments electronically²⁵

The Bill clarifies that licensees can provide suitability assessments electronically in accordance with the *Electronic Transactions Act 1999* (Cth). While we support this clarification, we recommend suitability assessments only be provided by electronic means where the consumer has consented to receiving documents electronically. There remains a significant proportion of the population who are not regularly connected to the internet, including financially vulnerable people, rural and regional Australians and seniors.²⁶ People should be able to access their relevant suitability assessments in the format that suits their needs – either in hard copy or electronically.

Recommendation 5: Suitability assessments only be provided electronically if the borrower has consented to receiving documents in this manner.

Items 19, 21 and 34 – Protected earnings amount²⁷

We strongly support the proposed protected earnings amount for payday loans and consumer leases, which would see repayments capped at 10% of a person's net income. The Bill amends the *National Consumer Credit Protection Act 2009* (Cth) (**the NCCP Act**) to remove the requirement for the protected earnings amounts to apply to a 'class of persons'. This would clear the way for amendments to the *National Consumer Credit Protection Regulations 2010* (**the Regulations**) that would implement the 10% protected earnings amount. We support these

²³ *Corporations Act 2001* (Cth) s 992A.

²⁴ *Treasury Laws Amendment (Banking Measures No. 1) Bill 2017* (Cth) Sch 6, Pt 2.

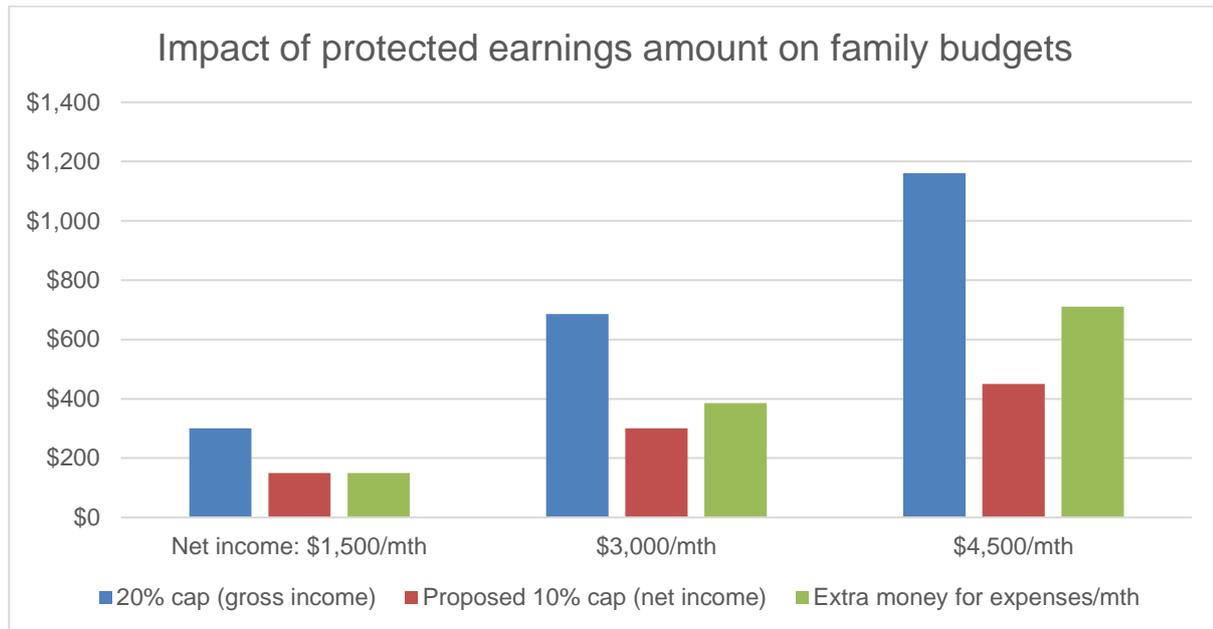
²⁵ See ss120(1A), 132(2A), 143(1A) and 155(2A)

²⁶ For example, see Telstra, *Measuring Australia's Digital Divide*, 2017, <https://digitalinclusionindex.org.au/wp-content/uploads/2016/08/Australian-Digital-Inclusion-Index-2017.pdf>.

²⁷ See ss133CC, 133CD, 156A, and 156B

amendments in the Bill, but note that it is critical that the Regulations take effect at the same time as the Bill.

This reform will ensure that people who use payday loans and consumer leases are not overcommitting their income to these harmful products, and have more money available for everyday expenses. The graph below demonstrates the positive impact the new protected earnings provisions would have on family household budgets:²⁸



The new protected earnings amount would apply to everyone, not just those receiving income from Centrelink. Given the significant increase in the proportion of financially stressed Australians using payday loans, as opposed to the traditional target market of financially distressed people, we believe this expansion of the provision is timely and necessary.²⁹ Our casework experience shows that it is not just Centrelink recipients who are harmed by these products, as demonstrated by the case study below:

Philip's story

Philip (name changed) has a gambling addiction, and has been using payday loans to pay his bills and gamble. Philip has had a relationship breakdown because of his gambling addiction. Philip can't control his impulse to gamble, even when it has negative consequences for him and his loved ones.

²⁸ Calculated using ATO Gross Pay Estimator with the following assumptions: individual non-business, Australian resident, TFN supplied, claimed Tax Free Threshold, not claiming Medicare levy exemption, no HELP, SSL, TSL or Student Financial Supplement Scheme debt, paid monthly. 20% cap applies only to people receiving the majority of their income from Centrelink: <https://www.ato.gov.au/Calculators-and-tools/Gross-pay-estimator/>.

²⁹ Digital Finance Analytics, *The Stressed Finance Landscape*, October 2015, available at: <http://consumeraction.org.au/wp-content/uploads/2015/10/The-Stressed-Financial-Landscape-Data-Analysis-DFA1.pdf>.

Philip has paid more than \$31,000 in payday loan repayments after taking out a total of 42 loans in a year. At any point in time, Philip had between 10 and 17 payday loans within the last 90 days.

Philip's net income is approximately \$4354 per month. The average payday loans provided to him between 10 October 2016 to 10 October 2017 was a little more than 50% of his gross income. Philip's financial counsellor estimates that he spent over 70% of the borrowed funds on gambling.

Case study provided by a Salvation Army financial counselling service in Victoria.

The Review recommendation to remove the presumptions of unsuitability³⁰ was conditional on the concurrent introduction of the 10% protected earnings amount.³¹ We therefore recommend that consultation on the Regulations be limited to consideration of technical amendments to avoid delays to implementation. Broader consultation about the necessity of a protected earnings amount is unnecessary, as thorough consultation about this recommendation has already been undertaken.

Recommendation 6: Ensure the 10% protected earnings amount in the Regulations take effect at the same time as the Bill.

Recommendation 7: Consultation on the Regulations be limited to consideration of technical amendments only.

Items 20, 21, 22, 34, 42, 58 and 62 – Civil remedies³²

We have significant concerns about the drafting of the civil remedies provisions in the Bill. The drafting of some provisions is unclear and could be subject to very different interpretations. Depending on the interpretation of the provisions, some may weaken the remedies available to consumers currently. We have made further detailed comments below.

Interpretation of Items 20 and 21 (ss133CC and 133CD)

Item 20 (s133CC(3)) provides that a provision that imposes a monetary liability to pay a fee or charge prohibited by s31A of the *National Credit Code* is void 'to the extent that the provision relates to that liability' (emphasis added). The reference to 'to the extent that the provision relates to that liability' is ambiguous. Does it make void the provision in the contract to not allow the monthly fee and establishment fee to be charged, or is the charging provision only void in so far as it breaches the protected earnings cap in the Regulations?

³⁰ The relevant provisions have been repealed in the Bill – see Items 5, 7, 13 and 15.

³¹ Review of the Small Amount Credit Contract Laws, *Final Report*, March 2016, available at: https://static.treasury.gov.au/uploads/sites/1/2017/06/C2016-016_SACC-Final-Report.pdf.

³² See ss 133CC(3), 133CD(3), 133CE, 133CG, 156A(3), 156B(3), 31C(2), 175AB(2), 175AC and 179VB.

Further, Item 21 (s133CD) says that a licensee cannot accept payment unless it 'does not exceed the amount which meets the requirements prescribed by the regulations for the purposes of s133CC' (emphasis added). However, s133CD(3)(a) refers simply to 'the payment', while s133(CD)(3)(b) refers to 'any payment'. Does s133CD therefore allow full disgorgement of all payments, or are the payments capped as foreshadowed in s133CC?

We are also concerned that the lack of clarity of these provisions may result in Item 42 (s31C(2)(b)), which relates to refunds of unexpired permitted monthly fees, being read down by a court so that this is no longer considered a proactive obligation. We note that we strongly support the requirement for SACC providers to refund overpayments of monthly fees to consumers.

Given these are criminal offences, we recommend that these provisions be clarified to provide that the debtor not be liable for future payments and is entitled to recover any amounts already paid under the contract in the event of a breach. This aligns with the approach taken under s180 of the NCCP Act for breaches of s29, which relates to engaging in unlicensed credit activities.

We also note that under s133CE, which prohibits licensees from entering into a SACC with unequal repayments, there is no remedy available for a debtor. While the provision would allow ASIC to take enforcement action against the licensee, the debtor would still be liable to make the repayments and would not be entitled to compensation.

Recommendation 8: Amend ss133CC and 133CD to provide that a debtor is not be liable for future payments and is entitled to recover any amounts already paid under the contract in the event of a breach.

Recommendation 9: Provide a remedy for debtors under s133CE, which prohibits licenses from entering into a SACC with unequal repayments.

Interpretation of Items 34 and 58 (ss156A, 156B, 175AB and 175AC)

Similar to above, we query whether the remedies contained in ss156A, 156B, 175AB and 175AC permit full recovery of all amounts paid, or are limited to a refund of payments up to the base price. The confusion arises as the drafting of ss156A and 175AB refers to 'the extent that the provision relates to the liability', while ss156B and 175AC refers to 'any payment made by the lessee to the lessor or person'.

As above, given these are criminal offences, we recommend that these provisions be clarified to provide that the debtor not be liable for future payments and is entitled to recover any amounts already paid under the lease. Full disgorgement would also incentivise compliance and provide appropriate redress to debtors, who may otherwise choose not to pursue their claim.

Recommendation 10: Amend ss156A, 156B, 175AB and 175AC to provide that a debtor is not be liable for future payments and is entitled to recover any amounts already paid under the lease in the event of a breach.

Relationship with ss178, 179 and 199 of the NCCP Act

It appears that the remedies contained in the Bill are intended to be in addition to existing remedies under the NCCP Act, which we strongly support. However, the current drafting of the Bill leaves it open to interpretation whether debtors would be precluded from relying on other remedies in the NCCP Act (such as ss178-179), and would instead be limited to those offered in the Bill. We recommend clarifying that the civil remedies in the Bill are standalone remedies and causes of action, which (for the avoidance of doubt) are in addition to those already available under the NCCP Act and *National Credit Code*. It would also be useful to clarify any time limits that apply.

We also recommend s199 of the NCCP Act be amended to allow debtors to make claims under these sections in the small claims court. Ideally, s199 would be amended to allow claims arising from breaches of any provision relating to SACCs and consumer leases under the value of \$40,000 in the small claims court.

Recommendation 11: Clarify that the civil remedies in the Bill are standalone remedies and causes of action, which are available in addition to current remedies under the NCCP Act and *National Credit Code*.

Recommendation 12: Amend s199 of the NCCP Act to allow claims arising from breaches of any provision relating to SACCs and consumer leases under the value of \$40,000 in the small claims court.

Status of leased goods

The status of leased goods in the event of a breach is not addressed in the civil remedy provisions relating to consumer leases. As the Bill is effectively creating a new regime for consumer leases of household goods, we recommend more detailed redress provisions that deal with the ownership and delivery of goods in the event of the breach. Debtors should be given the option to retain the goods or return the goods to the lessor, which would broadly align with the redress available under ss178 and 177(g) of the NCCP Act for other causes of action.

The Australian Consumer Law provisions relating to the ownership of unsolicited goods, which provides consumers with the option to return the goods or notify the business of a collection address, could provide drafting guidance.³³

Recommendation 13: Provide more detailed redress provisions that deal with the ownership and delivery of goods in the event of the breach.

³³ *Competition and Consumer Act 2010* (Cth) Schedule 2 - Australian Consumer Law, ss 41 and 85.

Loss of charges under Items 22 and 62 (s133CG and 179VB)

Further to our comments on page 5, we note that ss133CG and 179VB would require a debtor to prove both knowledge of the licensee and that a 'reasonable person' would conclude the consumer entered into the contract because of the unsolicited invitation. The equivalent provisions in the Australian Consumer Law relating to unsolicited sales do not require knowledge or reliance on the part of the consumer. We consider this to be an unreasonably high evidential barrier for a consumer, and recommend removing these requirements to ensure consistency and fairness. In the alternative, we recommend reversing the onus of proof in relation to knowledge and reliance elements of the provisions.

Recommendation 14: Remove requirements under ss133CG and 179VB to prove knowledge of the licensee and that a 'reasonable person' would conclude the consumer entered into the contract because of the unsolicited invitation in a claim. In the alternative, we recommend reversing the onus of proof in relation to knowledge and reliance elements of the provisions.

Item 38 – Anti-avoidance

There has been a long and consistent history of attempted avoidance of credit legislation, particularly in relation to cost caps. Prior to the enactment of the national credit law, consumer advocates documented at least nine avoidance mechanisms in NSW alone, some of which were closed down by specific amendment only to be replaced by the next innovative scheme.

While the national credit law has seen some reduction in this activity, we continue to see cases where lenders and their associates structure their business arrangements with clear intent to avoid the law – both the caps on costs, and the general and SACC-specific responsible lending obligations. With the introduction of a cap on the cost of consumer leases and the tightening of the applicable responsible lending provisions, we anticipate an increase in avoidance behaviour in this space also – indeed the consumer lease market has long operated at least in part as legal avoidance of the cost caps and more stringent responsible lending provisions that applied to SACCs.

Consequently, we strongly support the anti-avoidance provisions in the Bill. The circumstances described in the proposed s323A combined with the effect of s323C, particularly the operation of sub-sections (3) & (4), appear particularly effective to address known avoidance models, while giving sufficient scope to enable ASIC to address future innovation aimed at circumventing the intent and effect of the protections provided by the credit law.

However, s323B gives us cause for considerable concern. As currently drafted s323B could have the effect that if a scheme is structured so that the credit contract component of the scheme meets the criteria for an exemption under s.6 of the *National Credit Code*, the anti-avoidance provisions would not apply even if the purpose of the scheme is demonstrably to avoid application of the NCCP Act and *National Credit Code*. The logic is somewhat circular, but having used the comprehensive criteria in s323A to establish that a particular scheme or arrangement meets the criteria for avoidance, s323B then says that those very provisions do not apply if the contract is excluded by s6 of the *National Credit Code* (among others). This is particularly concerning given

the known use of s6 of the *National Credit Code* as an avoidance mechanism (*Australian Securities and Investments Commission v Teleloans Pty Ltd* [2015] FCA 648 (*ASIC v Teleloans*)).

We note that Regulation 50A was introduced after *ASIC v Teleloans* to address this type of business model avoidance, but we continue to see clients affected by Teleloans, Finance and Loans Direct Pty Ltd and their successors, Cigno and Gold-Silver Standard Finance Pty Ltd (**GSSF**):

Mary's story

Mary (name changed) is 19 years old, indigenous, with a history of mental health issues including schizophrenia. She's had a pretty hard life to date including witnessing domestic violence and her father going to jail. At the time she came to the National Debt Helpline her sole source of income was Youth Allowance. She had 3 SACCs and a consumer lease which she could not afford. One of the loans was provided by Cigno/GSSF and had grown from \$150 to \$740.

Case study provided by Financial Rights Legal Centre.

Sarah's story

Sarah (name changed) was a young mother on Parenting Payment Single. When her father died she was forced to rent on the private market for the first time and struggled financially. When she sought assistance from the National Debt Helpline she was struggling with 3 SACCs. One of them was from Cigno for \$150. At that time she had already paid back \$380 and they were seeking a further \$1020 in fees and default charges, far in excess of the maximum amount permitted under the law (section 39B of the *National Credit Code*).

Case study provided by Financial Rights Legal Centre.

In both above cases no assessment of unsuitability was made as required under the responsible lending provisions of the credit law. When challenged Cigno/GSSF continue to quote *ASIC v Teleloans* in support of their claim that the credit law does not apply, despite the introduction of Regulation 50A. While these matters (and several others) were settled on satisfactory terms we remain very concerned for consumers who do not seek advice and assistance and continue to be given unsuitable loans and charged amounts far more than that allowed by the legislation.

We submit that it is consistent with the intention behind the introduction of Regulation 50A that the principles set out in s323A should apply to a determination as to whether a contract is caught or excluded from the purview of the NCCP Act under section 6 etc. The effect of s323B should not be to exclude the operation of s323A completely, but to clarify that the mentioned sections continue to have effect in so far as they exclude the legitimate use of these contracts, but not

where that exclusion is achieved by the same artificiality, complexity or contrivance used as an indicator under the preceding sub-section.

We are also concerned that the anti-avoidance provisions do not address avoidance of the law more generally, but are confined to schemes aimed at avoiding the SACC and consumer lease provisions in particular. While avoidance of the cost caps and more prescriptive responsible lending provisions are a particular driver of potential avoidance, attempts to avoid the 48% cap on larger loans, the general responsible lending provisions, licensing and compulsory external dispute resolution membership also occur. Financial Rights Legal Centre, for example, recently settled a matter in the NSW Supreme Court involving a \$25,000 fee for organising a \$19,000 loan secured against real property which attempted to avoid the credit law using a false business purpose declaration. Lenders in the medium amount credit contract (**MACC**) space are also often keen to maximise their returns by avoiding cost caps, and compliance.

We would support a broader construction of s323A or a separate similar provision which addressed avoidance of the credit law *in its entirety*. For example:

*A person must not (either alone or with others) enter into, or carry out (to any extent), a scheme if it is reasonable to conclude that a purpose of the person doing so is to prevent a contract (the **contrived contract**) covered by the following paragraphs from being a regulated contract or a regulated consumer lease:*

- a) the contract is between a consumer and either the person or someone else who is or was connected with the person;*
- b) the contract is connected with the scheme.*

Recommendation 15: That the anti-avoidance provisions be amended to clarify that the principles which apply to establishing whether particular scheme amounts to avoidance are equally applicable to the determination required under s323B.

Recommendation 16: That the anti-avoidance provisions be extended to include avoidance of the credit law more generally, rather than simply the SACC and consumer lease provisions.

Items 42, 45 and 66 – Prohibition on unexpired permitted monthly fees³⁴

Under the Bill, SACC providers will be prohibited from charging or requiring payment of an ‘unexpired permitted monthly fee’ where the consumer has fully repaid the balance of the SACC before the end of the original term. We strongly support this reform, which would encourage people to repay expensive payday loans more quickly.

The term ‘unexpired permitted monthly fee’ is defined in Item 66 as ‘each permitted monthly fee that is in respect of a month that commences after the date of pay out or other discharge of that contract’. In practice, this means that if a monthly fee is billed on 1 June 2017, and a person pays out the loan on 2 June 2017, then the person would still be liable for the entire June monthly fee. We believe it would be fairer for the final monthly fee to be calculated on a pro-rata basis.

³⁴ See ss 31C and 82(3), and 204(1) of the *National Credit Code*.

Further, the amount required to pay out a SACC under Item 45 would be the principal amount of credit, all fees and charges up to the date of termination and reasonable enforcement expenses. We are concerned that the wording of this section leaves scope for SACC providers to make additional fees payable for early termination in contracts, or to seek excessive 'enforcement expenses'. We recommend clarifying that the fees and charges referred to in Item 45 (s45(3)(b)) are limited to the fees in s31A(1) of the *National Credit Code*.³⁵ We also recommend permitting ASIC to declare by legislative instrument that specified fees are 'reasonable enforcement expenses'.

Recommendation 17: Amend the definition of 'unexpired permitted monthly fee' to ensure the final monthly fee payable is calculated on a pro-rata basis.

Recommendation 18: Clarify that the fees and charges referred to in Item 45 (s45(3)(b)) are limited to the fees in s31A(1) of the *National Credit Code*.

Recommendation 19: Allow ASIC to declare by legislative instrument that specified fees are 'reasonable enforcement expenses'.

Item 55 – Disclosure of total cost and base price for household goods³⁶

Item 55 requires lessors of household goods to disclose the base price of the goods, and the difference between the base price of the goods and the total amount payable under the lease. Item 55 also provides that ASIC may by legislative instrument require additional information to be provided. We strongly support this reform, which would assist people to make more informed financial choices, and highlight the true cost of consumer leases.

However, we are concerned that consumer lease providers will bury these disclosures in the fine print of their contracts rather than have prices prominently displayed to potential customers. We therefore recommend that Item 55 be amended to require disclosure in advertisements, particularly where the advertisements feature a weekly repayment amount for a product.³⁷ This would avoid consumers focussing on a low weekly repayment amount, rather than the overall cost. We also recommend requiring disclosures to be prominent in any credit advertising, similar to the requirements under section 164 of the *National Credit Code*.³⁸

We have made additional comments about the calculation of the 'base price' below.

³⁵ Section 31A of the *National Credit Code* provides that: A small amount credit contract must not impose or provide for fees and charges if the fees and charges are not of the following kind:

- a) a permitted establishment fee;
- b) a fee or charge (a **permitted monthly fee**) that is payable on a monthly basis starting on the day the contract is entered into;
- c) a fee or charge that is payable in the event of a default in payment under the contract;
- d) a government fee, charge or duty payable in relation to the contract.

³⁶ See *National Credit Code* s174.

³⁷ Similar requirements apply to comparison rates in advertisements: see *National Credit Code* Pt 10 Div 2.

³⁸ *National Credit Code* s164 provides that: A comparison rate in any credit advertisement must not be less prominent than:

- a) any annual percentage rate stated in the advertisement; and
- b) the amount of any repayment stated in the advertisement.

Recommendation 20: Require consumer lease price disclosures in advertisements, particularly where the advertisements feature a weekly repayment amount for a product.

Recommendation 21: Require consumer lease price disclosures to be prominent in any credit advertising, similar to the requirements under section 164 of the *National Credit Code*.

Item 58 – Cap on fees and charges for consumer leases³⁹

The Bill introduces a cap on costs for all consumer leases, which is calculated on the base price of the goods plus 4% per month for a maximum of 48 months. We strongly support this reform, but note that the proposed cap amount is a compromise position for consumer advocates. We would have preferred the cap to align with the 48% annual cost rate cap that applies to goods leases regarded as sale by instalments. We would strongly oppose any higher cap on costs, as a higher cap would almost certainly entrench ongoing financial exclusion and regulatory arbitrage. The cost cap in the Bill is crucial to protect consumers from extortionate pricing by consumer lease providers.

As noted in the Final Report, ASIC has found evidence of some consumer lease providers charging up to equivalent interest rates of 884% for basic household goods.⁴⁰ This predatory pricing has been allowed to flourish due to the absence of cost caps in this market.

However, we consider the complex calculation of the 'base price' is unnecessary. The concept of a 'cash price' for consumer leases already exists in the *National Credit Code*, which we consider would be a more appropriate basis for the cost cap calculation.⁴¹ There are significant risks that the concept of 'recommended retail price' would also be manipulated, particularly by consumer lease providers that manufacture their own goods.

Section 204 of the *National Credit Code* defines the 'cash price' of goods or services as:

- a) the lowest price⁴² that a cash purchaser might reasonably be expected to pay for them from the supplier; or
- b) if the goods or services are not available for cash from the supplier or are only available for cash at the same, or a reasonably similar, price to the price that would be payable for them if they were sold with credit provided—the market value of the goods or services.

Having separate definitions for 'base price' and 'cash price', which both apply to consumer lease contracts and relate to the value of leased goods, is unnecessarily complicated and confusing for both consumer lease providers and consumers. There are also logical inconsistencies with the

³⁹ See s175AA, 175AB and 175AC of the *National Credit Code*.

⁴⁰ Australian Securities and Investments Commission, *15-249MR ASIC finds the cost of consumer leases can be as high as 884%*, 11 September 2015, available at: <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2015-releases/15-249mr-asic-finds-the-cost-of-consumer-leases-can-be-as-high-as-884/>.

⁴¹ See the concept of 'cash price' is in ss 9, 11, 12 and 170 of the *National Credit Code*, which mainly relates to goods leases with option to purchase being regarded as sale by instalments.

⁴² The 'lowest price' is further defined as 'the lowest price including any goods and services tax but unaffected by any discount between the credit provider and the supplier.'

concept of an ‘agreed purchase price’,⁴³ when a consumer lease contract does not give the consumer the right or obligation to purchase the good. If the consumer had the right or obligation to purchase the good, it would be considered a ‘sale by instalments’ and would be regulated as a credit contract.⁴⁴

We recommend the permitted cap be calculated by reference to the ‘cash price’ of the goods. This definition could apply to both new and used goods, as it does currently. We believe the cash price calculation would more accurately reflect the market value of leased goods, particularly second-hand goods.

In relation to second-hand goods, we are concerned that the proposed base price calculation in section 58 has artificially capped depreciation at a maximum of 30%. This is an unfair outcome for consumers as the market value of second-hand goods is likely to be much less than this. This unfairness is exacerbated by the fact consumers would be charged 4% of this inflated base price per month in fees. At a minimum, second-hand goods should be depreciated in accordance with Australian Tax Office depreciation rates, which would be a more accurate reflection of the actual value of the goods. Alternatively, a much more realistic depreciation formula should be included in the legislation—it is patently unfair for a refrigerator valued new at \$1,500 to be given a base price of over \$1,000 five or seven years after manufacture. Its true value would be far lower than this and people who have limited capacity to purchase new items should not be forced to pay such extortionate amounts.

It will be important, also, for goods (second-hand or not) to be appropriately described in contractual documents so that the ‘base price’ can be easily challenged. Too often contracts are described without specificity, for example, ‘30 inch TV’ or ‘5 seater lounge’. While item 55 above requires disclosure of the base price, this must be twinned with a requirement to adequately disclose the goods in the contractual document. At a minimum, the consumer lease provider should identify the make and model of the good, and whether it is new or used. This will aid dispute resolution. We note that this might be achieved through an ASIC legislative instrument made under proposed section 174(1B) of the *National Credit Code*.

Further, we are concerned that excluding reasonable delivery fees from the cost cap is providing an opportunity for consumer lease providers to engage in avoidance activities, and is inconsistent with the approach taken to ‘permitted installation fees’. We therefore recommend that ASIC be empowered to make legislative instruments regarding ‘permitted delivery fees’. It should also be clarified that ASIC is able to cap delivery and installation fees by legislative instrument.

Recommendation 22: The permitted cap be calculated by reference to the cash price of the goods, as defined under section 204 of the *National Credit Code*. At a minimum, second-hand goods should be depreciated in accordance with Australian Tax Office depreciation rates.

Recommendation 23: Goods (second-hand or not) to be appropriately described in contractual documents so that the ‘base price’ can be easily verified and challenged.

⁴³ Section 175AA(7).

⁴⁴ *National Credit Code* s9.

Recommendation 24: ASIC be empowered to make legislative instruments regarding ‘permitted delivery fees’. It should also be clarified that ASIC is able to cap delivery and installation fees by legislative instrument.

Items 62 and 66 – Canvassing of consumer leases at home⁴⁵

Item 62 would prohibit door-to-door selling of consumer leases for household goods. However, the prohibition would not apply if ‘there is a prior arrangement with a person who resides at the property.’ This is a significant loophole that does not align with the Review Panel’s recommendations or the Government’s response. It also allows considerable scope for consumer lease providers to circumvent the reforms.

Lessons can be learned from the experience of regulating door-to-door sales under the Australian Consumer Law.⁴⁶ Amendments were ultimately made to the definition of ‘unsolicited consumer agreement’ due to businesses obtaining ‘invitations’ through surreptitious means to avoid the consumer protections relating to unsolicited sales. Section 69(1A) of the Australian Consumer Law relevantly provides that a consumer is not taken to have ‘invited the dealer to come to that place, or to make a telephone call, merely because the consumer has:

- a) given his or her name or contact details other than for the predominant purpose of entering into negotiations relating to the supply of the goods or services; or
- b) contacted the dealer in connection with an unsuccessful attempt by the dealer to contact the consumer.’

The Australian Consumer Law also provides that ‘an invitation merely to quote a price for a supply is not taken to be an invitation to enter into negotiations for a supply.’

Despite these provisions, which are significantly more robust than those proposed in the Bill, the recent Australian Consumer Law Review concluded that ‘pressure selling and consumer detriment occurs in at least some industry sectors’, and that the level of consumer detriment caused by unsolicited selling may require ‘some degree of additional intervention’.⁴⁷

We therefore recommend that Item 62 be amended to remove the words “except by prior arrangement” onwards. In the alternative, we suggest that Item 62 be amended to reflect the wording in section 69(1A) of the Australian Consumer Law.

Recommendation 25: Item 62 (s179VA(1)) be amended to remove the words “except by prior arrangement” onwards. In the alternative, Item 62 be amended to reflect section 69(1A) of the Australian Consumer Law.

⁴⁵ See s179VA and 204(1) of the NCC

⁴⁶ *Competition and Consumer Act 2010* (Cth) Schedule 2.

⁴⁷ The Treasury, *Australian Consumer Law Review – Final Report, March 2017*, p. 58, available at: https://cdn.tspace.gov.au/uploads/sites/86/2017/04/ACL_Review_Final_Report.pdf.

Please contact Katherine Temple, Senior Policy Officer on 03 9670 5088 or at katherine@consumeraction.org.au if you have any questions about our comments on the review.

Yours sincerely



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Care Inc Financial Counselling Service and the Consumer Law Centre of the ACT

Care Inc. Financial Counselling Service has been the main provider of financial counselling and related services for low to moderate income and vulnerable consumers in the ACT since 1983. Care's core service activities include the provision of information, counselling and advocacy for consumers experiencing problems with credit and debt. Care also has a Community Development and Education program, provides gambling financial counselling as part of the ACT Gambling Counselling and Support Service in partnership with lead agency Relationships Australia; operates outreach services in the region and at the Alexander Maconochie Centre and makes policy comment on issues of importance to its client group. Care also operates the ACT's first No Interest Loans Scheme, which was established in 1997, and hosts the Consumer Law Centre of the ACT.

CHOICE

Set up by consumers for consumers, CHOICE is the consumer advocate that provides Australians with information and advice, free from commercial bias. By mobilising Australia's largest and loudest consumer movement, CHOICE fights to hold industry and government accountable and achieve real change on the issues that matter most.

Consumer Action Law Centre

Consumer Action Law Centre is an independent, not-for profit consumer organisation based in Melbourne. We work to advance fairness in consumer markets, particularly for disadvantaged and vulnerable consumers, through financial counselling, legal advice and representation, and policy work and campaigns. Delivering assistance services to Victorian consumers, we have a national reach through our deep expertise in consumer law and policy and direct knowledge of the consumer experience of modern markets.

Consumer Credit Legal Service (WA) Inc

Consumer Credit Legal Service (WA) Inc. (CCLSWA) is a not-for-profit charitable organisation which provides legal advice and representation to consumers in WA in the areas of credit, banking and finance, and consumer law. CCLSWA also takes an active role in community legal education, law reform and policy issues affecting consumers. In the 2015 / 2016 financial year, CCLSWA provided comprehensive legal advice to 1350 clients on 1424 matters.

Financial & Consumer Rights Council Inc.

The Financial and Consumer Rights Council Inc (FCRC) is the peak body and professional association for financial counsellors in Victoria. FCRC provides resources and support to financial counsellors and their agencies who assist vulnerable Victorians experiencing financial difficulty. FCRC works with government, the banking, utilities, debt collection and other stakeholders to improve approaches to financial difficulty for vulnerable consumers.

Financial Counselling Australia

FCA is the peak body for financial counsellors. Financial counsellors provide information, support and advocacy for people in financial difficulty. They work in not-for-profit community organisations and their services are free, independent and confidential. FCA is the national voice for the financial counselling profession, providing resources and support for financial counsellors and advocating for people who are financially vulnerable.

Financial Rights Legal Centre

Financial Rights is a community legal centre that specialises in helping consumers understand and enforce their financial rights, especially low income and otherwise marginalised or vulnerable consumers. We provide free and independent financial counselling, legal advice and representation to individuals about a broad range of financial issues. Financial Rights operates the National Debt Helpline, which helps NSW consumers experiencing financial difficulties. We also operate the Insurance Law Service which provides advice nationally to consumers about insurance claims and debts to insurance companies. Financial Rights took almost 25,000 calls for advice or assistance during the 2016/2017 financial year.

Indigenous Consumer Assistance Network

In line with its vision of '*Empowering Indigenous Consumers*', the Indigenous Consumer Assistance Network (ICAN) provides financial counselling assistance to alleviate consumer detriment, education to make informed consumer choices and consumer advocacy services to highlight and tackle consumer disadvantage experienced by Indigenous peoples. ICAN is an independent member of the National Indigenous Consumer Strategy - Reference Group that comprises all territory, state and national consumer protection agencies.

Uniting Church in Australia

The Uniting Church is the third largest Christian denomination in Australia and the first church to be created in and of Australia. The Uniting Church in Australia sees as part of its mission to act with God alongside the oppressed, the hurt and the poor. The Uniting Church in Australia, Synod of Victoria and Tasmania, has a number of community service agencies that provide financial counselling services. It also incorporates UCA Funds Management which currently excludes payday lending and some consumer leasing businesses from investment under the Synod's Ethical Investment Policy.