



Submission by  
Care Inc. Financial Counselling Service  
& The Consumer Law Centre of the ACT

in response to:

**Review of the small amount credit contract laws**  
September 2015

*Contacts:*

Carmel Franklin

Director

[carmel.franklin@carefcs.org](mailto:carmel.franklin@carefcs.org)

Liisa Wallace

Policy Officer

[liisa.wallace@carefcs.org](mailto:liisa.wallace@carefcs.org)

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

Telephone 02-62571788

Date: 14<sup>th</sup> October 2015

## **Agency information**

Care Inc. Financial Counselling Service and The Consumer Law Centre of the ACT (Care) has been the main provider of financial counselling, legal 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 (AGCSS) in partnership with lead agency Relationships Australia; makes policy comment on issues of importance to its client group and operates the ACT's first No Interest Loans Scheme which was established in 1997. Across Care's service delivery programs, the agency responds to over 2000 new requests for assistance every year.

Care welcomes the opportunity to provide comment on the **Review of the small amount credit contract laws**.

## **Background**

As a financial counselling and legal service funded to work with low to moderate income earners, we assist clients who are experiencing a range of financial hardships, including clients struggling to make payments on Small Amount Credit Contracts (SACCs). In 2014, over fifty per cent of Care's clients were wholly dependent on Centrelink payments<sup>1</sup>; many of the remaining fifty per cent of clients, including those who were working, also received part Centrelink payments. The majority of clients that contact this service do so when they are unable to pay their debts as they fall due. They are often in a highly emotional and distressed state, and are looking for ways to address their financial situation. The financial counsellors and consumer credit solicitors work with clients to address their debts and to try and structure their finances to fit within their income.

Care's clients experience a range of circumstances that lead them to be in financial difficulty. For some it is long-term chronic poverty where they have been existing for long periods of time on low incomes. For others there has been a change in circumstances such as illness, relationship breakdown or unemployment that impacts their finances and means they cannot pay their commitments as they fall due. Many clients also experience chronic physical illness or mental illness and a number identify as being survivors of trauma, including domestic violence and childhood trauma.

Care sees clients in some of the most 'at risk' groups for financial difficulty and therefore vulnerable to accessing SACCs or 'payday loans'. This includes people with mental illness, sole parents (particularly women as sole parents), aged people, gamblers, public housing tenants, prisoners, Culturally and Linguistically Diverse clients and Aboriginal and Torres Strait Islander clients.

Despite clients' efforts to constantly juggle their finances to make the best of their limited resources, things break down from time to time particularly when unexpected expenses occur. Clients seen at Care are borrowing from payday lenders to fill a gap when they are desperate and have no savings, cannot access affordable credit options and don't have any family or friends to turn to. A list compiled from the financial counsellors as to the reasons clients say they borrow from payday lenders includes: food, rent, medical and dental, children's expenses

---

<sup>1</sup> Care Annual Report 2014 [www.carefcs.org](http://www.carefcs.org)

(including clothing and school needs), travel to attend funerals, gambling, general bills, household items (lounges, tvs) Christmas, car repairs, to pay other creditors, pharmaceuticals and for mobile phones.

Our interest in this review stems from the issues we observe being created by 'payday lending', particularly where a client has received several of these loans in succession. Far from being a resolution to the cash shortage a low income consumer experiences, a SACC loan will almost always end up being a burden, drawing much needed money from the borrower and putting it into the pockets of the lenders. The result is often a borrower trapped into a repeat cycle of borrowing and financial dependency on the lender.

While we will argue for a tightening of laws that restrict the SACC industry and therefore is more protective of consumers than is currently the case; we are acutely aware of the need for alternative *affordable* forms of credit to be available for low income consumers in particular. We encourage government to look at ways to expand and extend the No Interest Loan Scheme (NILS) and associated products to ensure that low income, vulnerable and disadvantaged consumers have access to financial products that meet their needs and do not place them at risk of further financial harm.

### **Question 1: Competing objectives**

Regarding the current situation as one of 'competing objectives' downplays the vast imbalance between low income borrowers and the SACC lenders and clouds the circumstances under which a borrower is likely to approach a SACC lender. We regard the need to protect vulnerable consumers as paramount and their interests should over-ride the needs of a highly profitable industry that benefits from their often desperate clients' circumstances. Unlike mainstream lending where borrowers generally access money for lifestyle related products, in our experience borrowers with SACC loans borrow for basic necessities and essentials. Further, these borrowers are likely to be highly vulnerable when accessing a payday loan as Lily's\* case below illustrates.

#### Case Study 1

*Lily had become unwell with a mental illness, had lost her casual job and had been homeless in the past. She was desperate to maintain her current tenancy and turned to a payday lender when she couldn't pay her rent:*

*"I didn't really think I would get stuck like this...I can't see a way out of having to take money even though it's not what I want to do....they do give me the money, but I reckon they charge through the nose for the fact of borrowing plus I missed a few payments and have to pay that back as well. Now my rent is costing me pretty much double what it should because of how much I have to pay back each pay. It's really getting me down...." Lily*

If the industry is to continue to extend credit to vulnerable and disadvantaged consumers such as Lily, there needs to be a strengthening of consumer protection laws so that they are **at a minimum** in line with provisions in the National Consumer Credit Protection Act 2009 (NCCPA) that apply to other types of credit contracts.

The vulnerable nature of borrowers who are highly stressed and desperate at the time of taking out a SACC loan, leads to questions about whether a borrower should have received the loan in the first place, and what their ability to understand the contract actually was when they took it

out. There is reason to think that SACC lenders could in fact be held to *higher standards* than mainstream lenders, given the vulnerable nature of the borrowers they deal with; this is particularly the case for repeat borrowers who risk becoming trapped in an unhealthy dependency on the lender.

Unlike No Interest Loan Schemes, where there is no charge associated with borrowing the money, SACCs are profit driven. In our experience they do not fill a gap in the market that could not be addressed better by other forms of more responsible lending. If the industry wants to remain, it needs to change the way it does business, particularly in regard to ensuring borrowers are not financially disadvantaged by borrowing, and that they are not trapped in an increasing debt spiral. The industry needs to also alter the way it sells and advertises itself and its products as a whole. We do not regard this as a balancing act: the starting point should be to ensure that vulnerable consumers are *always* protected when accessing credit, in the same way that other consumers are.

### **Question 2: Complexity**

We consider that the current regulatory regime with respect to all credit contracts is complex. Each category of contract (short term, small amount, medium and other credit contracts) has its own regulatory framework. For example a small amount credit contract can charge a maximum 4% monthly fee and a medium amount credit contract can charge a maximum of 48% per annum. There is no compelling reason why there should be so many categories. Care considers a flat 48% cap on all credit contracts provided by non-ADI lenders is a fair and simple option.

We also want to be sure that some of the other protections currently in place are retained or possibly further strengthened to protect consumers (we address the percentage of income for Centrelink recipients that can be taken as repayments on a SACC loan later in this submission).

Further we would welcome exploration of an enforceable limit to repeat borrowing: with a possible designated maximum number of loans in a twelve month period depending on amounts borrowed; and a prohibition on lending to consumers in default.

### **Question 3: Sanctions**

There are difficulties associated with imposing sanctions on credit providers given the vulnerability of clients of Care who use these loans. Clients do not wish to proceed in prosecuting their matter because they feel they will need to have access to the loans provided by the credit provider again in the future. Despite informing clients of their right to contact ASIC (or have Care or the CLC contact on their behalf) where breaches to the small amount credit contract obligations in the Credit Act have occurred, no client has chosen to do so and therefore none of the breaches we have seen have resulted in a sanction being imposed on the credit provider.

We consider a number of enhancements could be made to the sanctions regime to make it more effective. These include

- increasing ASIC funding for the purpose of prosecuting breaches of the Credit Act,
- improving the licensing regime of credit providers, and
- detailing civil penalty sanctions where there have been breaches of responsible lending obligations, additional disclosure requirements or the Centrelink protection cap of 20%.

These civil penalties could include civil penalty sanctions similar to the maximum cost requirements for SACCs such as relieving the borrower from making payments and recovering payments already made in excess of the principal, for example. We consider having a clearly enunciated civil penalty will assist vulnerable clients with arguing their case and relieving them of the burden of having to pay exorbitant amounts of interest on loans they should not have been provided.

#### **Question 4: Obligation to obtain and consider bank account statements (TOR 1.1)**

Requiring bank statements is standard practice in mainstream financial institutions for loan applications and is also a requirement of the No Interest Loan Scheme. They can provide valuable information about the applicant's day to day financial situation including if an applicant is regularly overdrawing their account. The issue for lenders then becomes how they regard an overdrawn account and what further information might be needed from an applicant before they would accept/decline the application for a loan.

Although SACC loans are only for a small amount of money this should not mean that less information is required. Given the tight budgets of most applicants, it is important that the bank statement and the information it provides is considered carefully by the prospective lender. Evidence that the lender has received and appropriately reviewed an applicant's bank statements should be ticked off as part of assessment tool that can be provided (if requested) to the applicant or the applicant's advocate. There is also the need for other evidence to be obtained such as pay slips, Centrelink statements and evidence of other debts. The lender should also complete an income and expenditure statement that is realistic and reflective of an individual's circumstances. Care has seen a generic figure of fifteen percent (15%) used for 'living expenses' by SACC lenders. Clearly this figure is inadequate and could not possibly cover necessary items including food, utilities, transport, phone and other costs such as medical.

Under no circumstances should SACC providers be able to use bank account statements for purposes other than complying with the responsible lending obligations. They should never be used for marketing purposes. Bank statements when provided are for the specific purposes of assessing suitability for a loan and complying with responsible lending obligations. Using them for other purposes is highly unethical.

#### **Question 5: Restrictions on repeat borrowing (TOR 1.2)**

Under the current legislation:

For loan applicants who are borrowing with the same lender, they need to have up to date records and access to these for their assessing staff so that they can check the borrowing record of the loan applicant to determine under s.118 (3A) of the NCCPA:

- If the applicant is in default under another SACC; or
- if they have had two or more other SACCs in the 90 days period preceding the current application

Despite this current requirement, Care has seen clients such as Jess\* who have received a further payday loan from the same provider when they were in default on the previous loan:

## Case Study 2

*Jess received a SACC loan when she had to attend a funeral interstate and contribute to the costs of the funeral. This loan was for \$1200 and she met the repayments until she became ill and had to further reduce her part-time hours at work.*

*She then approached the SACC lender again as she was struggling with everyday living costs. Despite being in default on the original loan **and** on a reduced income, she was granted a further loan for \$360.*

*In our opinion, the lender contravened its responsible lending obligations contained in Chapter 3 of the National Consumer Credit Protection Act 2009 (Cth) (NCCPA). The presumption of unsuitability arises when a borrower is in default under a SACC; in Jess' case she was not only in default but also had a change in circumstances which reduced her income significantly. It should have been apparent to the lender that the second loan was unsuitable.*

If the client is not borrowing from the same lender, this requires a different approach from the SACC lender. It is standard practice when lending in mainstream financial institutions to obtain and verify information about other credit an applicant has. The SACC lender's enquiries about other SACC loans should be part of a general investigation of the affordability of a loan. They should:

- ask the prospective borrower for information about other SACC loans that they have that are current.

- if the prospective borrower confirms that they have other SACC loans obtain relevant documents from the prospective borrower or and where these are not available from the prospective borrower or need clarification, obtain the applicant's consent in writing to communicate with the other SACC lender(s) to obtain documents as needed.

Care believes a restriction on repeat borrowing is necessary to protect consumers and is preferable to the rebuttable presumption approach. For a comparison, particularly for those applicants who receive part or full Centrelink payments, the Centrelink Advance (or loans) system could provide a guide. There are strict limits for Centrelink Advances on both the amount an applicant can borrow and the number of advances (or loans) they can obtain within a twelve month period. The amount that can be borrowed is set at a percentage of a Centrelink recipient's payment<sup>2</sup>.

If a limit on the number of loans able to be obtained in a twelve month period was introduced, this should reduce the complexity and presumably the associated costs for SACC lenders. Care regularly sees clients with several loans in train under current rules, reducing access to these loans should reduce costs, including those costs associated with compliance.

We do not regard the use of a benchmark, such as the Household Expenditure Measure or Henderson Poverty Index as necessary. If a borrower's financial circumstances are examined adequately and information is verified (including bank statements, Centrelink Income Statements and pay slips) it should be evident whether an applicant for a loan can afford the

---

<sup>2</sup> <http://www.humanservices.gov.au/customer/enablers/advance-payment>

loan and repayments. SACC lenders have an obligation to not keep lending to already indebted consumers.

Restricting access to the number of loans in a twelve month period would also reduce the damage that occurs to consumers when their accounts are overdrawn by direct debits failing and then associated late and penalty fees being charged. Care sees clients who have informed the SACC lender that they want to suspend or alter a direct debit arrangement only to be told it has either been done and they find out it hasn't, or that the debit cannot be stopped. This leads to further penalties that are a huge impost on low income consumers and adds to their ongoing financial difficulty. SACC lenders need to update their systems to enable timely suspension of payments on request by a borrower who states that they are in financial hardship.

#### **Question 6: Ban on short term credit contracts**

Care has not seen any clients with loans with a term of 15 days or less and therefore cannot comment on this question.

#### **Question 7: Warnings (TOR 1.4)**

Care considers it extremely important that there are adequate warnings about the costs of SACCs available before people borrow including:

- that the current information would be more useful if it were clearer that the 1800 007 007 is a free-call to speak a financial counsellor to provide possible alternatives to accessing credit and not just about 'debts and bills'. This needs to be in a different colour to the rest of the warning information and a link provided for access to the Financial Counselling Australia website to locate a financial counsellor near where people live

- the warning needs links to NILS providers and MoneySmart websites that people can click on and access

- there needs to be a comparison between a NILS loan cost (for a regularly borrowed for item e.g. a tv or mobile phone) and the cost of borrowing a SACC loan for the same item via a loan calculation that automatically pops up on the screen.

#### **Question 8: Caps on costs (TOR 1.5 & 1.6)**

The cap on costs has led to a boom in the payday lending sector at the expense of consumers. We reiterate our call for a 48 per cent cap, bringing it in line with medium amount credit contracts.

In addition, we consider the current regime does not provide adequate protection to consumers in respect of default fees and from our casework we have observed numerous clients being charged large amounts of default fees per month on small amount credit contracts. We consider the cap on default fees needs to be further reduced, including the fee itself every time there is a default. See Narelle's\* case below:

### Case Study 3

*Narelle borrowed \$1,300 from a payday lender. The loan length was 40 days. The establishment fee was 20% of the principal and the monthly credit fee was 4% of the principal. However, there was a payment dishonour fee of \$35 each time a payment was not made in full or at a time a payment is scheduled forward at the client's request. Narelle struggled with payments from the start of the loan.*

*In addition, there was a default fee of \$7 per day to allegedly cover the cost of administering the account while it is in arrears. Narelle was to make 4 payments but failed to meet each payment. As a result, she incurred a total of \$1,600 in default fees, some of which were written off for going over the 200% cap.*

*In this case there is no restriction on the credit provider charging whatever default fee it wants, as long as it (along with the other fees and costs) do not exceed the 200% cap. In this case the client did not want to challenge the default fee total on grounds of it being a penalty, as the client wanted to continue to access credit with this provider.*

*This case illustrates that some additional restrictions should be imposed on credit providers around the default fees they charge so that they are commensurate with the loan amount and a realistic estimate of administration costs.*

### **Question 9: Protection for Centrelink customers (TOR 1.7)**

For borrowers in receipt of any amount of Centrelink payments (including part payment recipients), it is likely a SACC will be unaffordable. Clients seen at Care who are receiving Centrelink at 50% or more of their income will certainly be struggling with making ends meet and for those clients we see who are wholly reliant on Centrelink for their income, 20 per cent of their income in SACC repayments is far too high. This amount in repayments puts them at great risk of becoming trapped in repeat borrowing.

For example a client on Newstart Allowance (\$529.60 per fortnight inclusive of Pharmaceutical Allowance) who has health conditions that need managing, would have a *severely restricted lifestyle and be at risk of becoming trapped in a payday borrowing cycle* if they could not meet their repayments in any given fortnight.

Table 1 below illustrates the disproportionate amount of income for a SACC repayment at 20 per cent of Newstart Allowance.

Table 1

Income: Newstart	\$529.60 per fortnight
Rent @ 25% income (client in public housing – many clients pay more than this in rent)	\$130.85
Food	\$140.00
Electricity	\$65
Transport	\$20
Pre-paid mobile	\$20
Medication /Doctor	\$28
Physio	\$17
<b>SACC @ 20% income</b>	<b>\$104.68</b>
Deficit	-\$2.13

Care regards any figure above 10% of a person’s gross income in repayments, especially those on full Centrelink payments to be too high. The 10% amount is in line with the Centrelink Code of Operations<sup>3</sup> which applies to debts that arise from customers overdrawn accounts in Approved Deposit Taking Institutions (banks, credit unions etc.). The default position in this code is that a customer should be able to retain *at least 90 per cent* of their income support payment or Department of Veterans’ Affairs payments in any fortnightly period.

Any group that has a comparable level of income to Centrelink recipients (including part-Centrelink recipients, Department of Veterans’ Affairs payment recipients and low wage earners) should have repayments on SACC loans set at no more than ten per cent of their gross income.

**Question 10: National database (TOR 2.1)**

Care regards the establishment of a database for SACC loans as potentially a useful development but we have concerns that unless its function is purely to improve compliance with responsible lending obligations it could become a negative for the clients who access these loans. It must not be used as anything other than a register for recording basic SACC information and the following must be adequately addressed:

- the reasons for such a database are clear and transparent
- that the database is there to protect consumers and to enable SACC providers to do their assessment properly
- access to such a database is clearly defined, including who can record data and who can access it
- privacy concerns for potential borrowers are uppermost in both design and use of the system
- borrowers should be able to access their information free of charge to ascertain if it is accurate and up to date
- incorrect entries are able to be corrected without charge or penalty by borrowers

<sup>3</sup> <http://www.humanservices.gov.au/corporate/publications-and-resources/code-of-operation>

- only *current loans* are recorded on the database and as loans are paid out they automatically drop off the database
- only the minimum of essential information is stored on the database about borrowers and their loans such as current loans, the amounts and date obtained
- SACC lenders should be required to check the database for a potential borrower's loan history prior to completion of the loan process. The lender should also provide evidence they have done this if requested by borrowers or advocates
- the database should be there *only* to assist SACC lenders to discharge their responsible lending obligations by providing targeted information about SACC loans to lenders
- the database would allow a SACC lender to ascertain if an applicant has loans with other SACC lenders and thereby exclude those borrowers who do from borrowing (under the current unsuitability test)
- managing the database should be done by a government agency preferably
- funding should be from penalties imposed on SACC lenders for breaches of their obligations
- reporting of key information should be mandatory if such a database is introduced
- if SACC providers are charged a fee to access the database, this cost should not be passed onto consumers
- the establishment of a database will not reduce the need for the lender to comply with other responsible lending obligations. Rather it should provide information to assist in more accurate assessments and support the decision to lend/not lend to a potential borrower.

**Question 11: Additional provisions for SACCs**

Given our experience that clients seen at Care are struggling with SACCs that appear to have been beyond their reach to repay (sometimes from inception of the loan), we recommend a specific provision outlining how SACC providers document a decision that a SACC was not unsuitable.

**Question 12: Anti-avoidance provisions (TOR 2.2)**

Care strongly recommends a general anti-avoidance provision to ensure that SACC lenders do not engage in regulatory avoidance strategies and continually try and re-invent ways to trap vulnerable consumers into SACC loans.

We have recently worked with two clients who have fallen victim to avoidance practices in relation to the Credit Act from credit providers with whom they had sought funds. Their cases John\* and Jeff\* follow:

#### Case Study 4

*John needed \$1,400 urgently and found a credit provider on line offering personal loans. He applied for a loan and was sent a number of documents to complete and return to the credit provider. John completed the loan application and signed all the documents. He obtained what he thought was a loan of \$1,400 and repaid it in a year along with \$1,800 in additional payments.*

*It was only when John visited Care about his financial circumstances that a financial counsellor identified that John had purported to sell a number of his household goods to the credit provider and then lease them back from the credit provider, paying a total of \$3,200 in the year.*

*John thought he had entered into a loan arrangement and was shocked when Care staff explained to him what arrangement he had actually entered into and how he had paid far more than he should have if the arrangement was characterised as a loan by the credit provider.*

#### Case Study 5

*Jeff borrowed \$400 from company X but made an application through company Y. The agreement with company X was that he repay the loan amount of \$400 plus a \$20 fee in four fortnightly payments of \$105. Jeff was additionally charged by company Y:*

- *1 x \$90 establishment fee*
- *monthly account keeping fees*
- *1 x \$20 change of payment fee*
- *1 x \$40 bank dishonour fee*

*Company X and Company Y are claiming they are separate entities; one provided a loan application service to Jeff for credit and the other provided the loan to Jeff. They claim that there was no direct relationship and that one company provided the loan and the other the service and there was no contravention of the Credit Act. Company X and Y shared the same IDR address.*

#### **Question 13: Documentation of suitability assessments (TOR 2.2)**

In Care's experience, when requesting evidence of assessment of unsuitability there is a wide variation in information received back from the SACC lender. Some lenders provide several pages of documents, others provide next to nothing. We have also had difficulty obtaining these documents and have on occasion had to make several requests. Our experiences fit with ASIC's

*Report on Payday lenders and the new small amount lending provisions*<sup>4</sup> which outlined inconsistencies in both record keeping and assessment information, and we recommend that there is a stronger emphasis on record keeping within the sector and a need to be able to demonstrate actual compliance with requirements.

SACC lenders should definitely be required to document the assessment process and the evidence should be available on first request to consumers and advocates. The assessment should demonstrate clearly the reasons the consumer was granted or refused a loan, whether it was not unsuitable and the purpose they received the loan for.

## **Comparable Consumer Leases**

### **Question 14: Comparable consumer leases (TOR 3)**

Care's regularly sees clients who have obtained consumer leases, generally for household goods and items. The following is generally the case for the clients we see:

- they are unaware of the actual costs of renting the goods when compared with buying outright or obtaining a NILS loan; most are genuinely shocked when the calculations are provided to them
- they think they will own the goods outright at the end of the lease
- they have not had the documents they signed explained to them
- they have had difficulties negotiating a satisfactory outcome with the lease company when experiencing financial hardship

We do not think there is anything to be gained from defining 'comparable consumer leases', as it would most likely add unnecessary complexity to the regulatory regime. We do however; recommend that the NCCPA no longer distinguish between consumer leases and credit contracts based on whether they provide a right or obligation to purchase.

### **Question 15: Applying SACC provisions to comparable consumer leases (TOR 3)**

Care recommends additional disclosure for comparable consumer leases including:

- the cash price of the goods,
- the total price of the goods,
- the amount the consumer will pay in excess of the cash price
- the cost of credit as a comparative interest rate, and
- the cost of any additional services (such as delivery and repair)

Care considers the cost of complying with any such additional disclosure requirements should be borne by the providers. We refer to our earlier point about SACC lenders, in that the lease industry is also highly profitable, and in our experience repeatedly takes advantage of vulnerable low income consumers. It is the interests of these consumers that should be protected.

---

<sup>4</sup> <http://download.asic.gov.au/media/3038267/rep-426-published-17-march-2015.pdf>

**Question 16: Cap on costs for consumer leases (TOR 3)**

Care recommends:

- applying the 48% cap on costs to consumer leases
- that the NCCPA no longer distinguish between consumer leases and credit contracts based on whether they provide a right or obligation to purchase, and
- in calculating the cash price of the goods, the definition used for sales by instalment under the Code should be used.

Thank you for the opportunity to provide these comments.

*\*clients' names and some details have been changed*