Submission by the

Credit and Investments Ombudsman Service Limited

to

The Review of the Small Amount Credit Contract Laws

October 2015

1. Introduction

The Credit and Investments Ombudsman Service Limited (**CIO**) appreciates this opportunity to respond to the Discussion Paper on the Review of the Small Amount Credit Contract Laws[1] (**the Discussion paper**). CIO notes that the Review is also considering the regulation of those consumer leases which are 'comparable' with small amount credit contracts.

CIO is an external dispute resolution (**EDR**) scheme approved by ASIC under its RG 139 for holders of Australian Credit Licences as required by section 47(1)(i) of the National Consumer Credit Protection Act 2009 (**NCCP**).

CIO is well placed to consider many of the questions asked in the Discussion Paper based on its casework experience. We do not, however, have substantial submissions to make on all the questions in the Discussion Paper. Our principal submissions are summarised below.

SACC lenders

CIO has more than 20,000 financial services provider (**FSP**) members. 287 of these are small amount lenders (**SACC lenders**). This is down from the same time last year when CIO had 314 small amount lenders. There has been some consolidation in the industry.[2]

In the financial year 2014/15[3], SACC lenders generated 5.8% of all complaints (283 complaints) handled by CIO, despite representing only 1.3% of CIO's entire membership. 18.4% of complaints about SACC lenders were in relation to responsible lending.

Consumer lease providers

Consumer lease providers generated 9.3% of all complaints handled by CIO during the same period, although they only represent 1.4% of CIO's entire membership. 8.4% of complaints about consumer lease providers were in relation to responsible lending.

2. Principal Submissions

2.1 Restrictions on repeat borrowing (TOR 1.2)

CIO supports the current restriction on repeat borrowing as being necessary to protect consumers, but observes that the rebuttable presumption approach in the current legislation can create systemic compliance difficulties for some SACC lenders.

[1] Discussion Paper, Commonwealth Treasury, September 2015.
[2] ASIC also notes a small (6%) decline in small amount lending licences over a similar period. See ASIC Report 426 'Payday lenders and the new small amount lending provisions' March 2015, p 24
[3] CIO Annual Report on Operations 2015.

CIO submits that the rebuttable presumption of unsuitability be replaced with an outright ban on SACC loans if:

(a) the consumer is in default under another SACC loan, or

(b) in the 90 day period before the loan assessment, the consumer had two or more other SACC loans.

This will, in our view:

- reduce complexity,
- increase consumer protection, and
- reduce compliance costs.

2.2 Anti-avoidance provisions (TOR2.2)

CIO takes a broad approach to the application of the Credit Act to credit transactions in order to overcome attempts by lenders to avoid regulation. However, CIO submits that a broad anti-avoidance provision, similar to that which applies to conduct regulated under Chapter 7 of the Corporations Act would:

- increase consumer protection,
- decrease complexity by discouraging elaborate avoidance models, and
- better facilitate the application of the NCCP, where appropriate, by CIO, other EDR schemes and the Courts.

2.3 Documentation of unsuitability assessments (TOR 2.2)

CIO submits that SACC lenders should be required to document their unsuitability assessments, including the reasons for concluding that a contract is not unsuitable, on all occasions in order to achieve:

- increased transparency in the assessment process,
- increased consumer protection,
- decreased irresponsible lending, and
- increased integration of demonstrable compliance with actual compliance.

2.4 Comparable consumer leases (TOR 3)

CIO submits that:

(a) consumer leases for household goods with a value of $2,000 or less are comparable with SACC loans,

(b) consumer leases for other goods (such as motor vehicles) up to $5,000 are comparable with MACC loans, and

(c) there should be greater consistency between the regulatory requirements that apply to SACC loans and comparable consumer leases.

2.5 Applying SACC provisions to comparable consumer leases (TOR3)

CIO submits that:

(a) the additional disclosure requirements listed in Question 15 of the Discussion Paper should apply to comparable consumer leases, and

(b) the following SACC provisions, appropriately modified, should apply to comparable consumer leases:

(i) the ban proposed at 2.1 above,

(ii) a modified warning statement,

(iii) a modified cap on the total amount recoverable by a consumer lessor for a comparable consumer lease (whether in default or not), and

(iv) a modified protected earnings provision.

2.6 Cap on costs for consumer leases (TOR 3)

CIO submits that:

(a) the modified cap should limit the total amount recoverable by a consumer lessor to, say, twice the modified cash price for the leased goods, and

(b) the cash price should be modified (and disclosed as submitted above), so as to incorporate the:

(i) cash price as defined for instalment contracts in Pt 13 of the National Credit Code (**NCC**), plus

(ii) an additional component to account for the reasonable costs of the lessor providing:

A. a replacement warranty for the leased goods for the period of the lease,

B. delivery and collection costs of leased goods.

2.7 Obligation to obtain and consider bank statements (TOR 1.1)

CIO submits that the obligation to obtain and consider bank account statements is necessary to the responsible lending obligations of SACC lenders, but notes that there appears to be:

(a) inconsistent and frequently non-transparent use of the information in the bank statements by some SACC lenders, and

(b) a disturbing tendency by some SACC lenders to treat the mere collection of the statements as a 'safe harbour' for compliance with their responsible lending obligations.

CIO submits that its submission at 2.3 above to require more explicit documenting of suitability assessments will enhance the appropriate use of bank statements in the assessment process.

3. Repeat Borrowing

3.1 The existing provisions

Section 133(3A) of the NCCP Act provides:

(3A) If the contract is a small amount credit contract (the relevant contract) and either of the following apply:

(a) at the time it is entered or the credit limit is increased:

(i) the consumer is a debtor under another small amount credit contract; and

(ii) the consumer is in default in payment of an amount under that other contract;

(b) in the 90-day period before the time it is entered or the credit limit is increased, the consumer has been a debtor under 2 or more other small amount credit contracts,

then, for the purposes of paragraph (2)(a), it is presumed that the consumer could only comply with the consumer's financial obligations under the relevant contract with substantial hardship, unless the contrary is proved.

3.2 CIO's observations

Responsible lending and unjustness complaints make up 18.4% of all complaints about SACC lenders dealt with by CIO. This is at least three times the average level for this category of complaint for all other classes of FSP members of CIO.[4]

Not all of these necessarily involve repeat borrowing but many do, and it is the observation of CIO that the lending staff of SACC lenders appear to have difficulty with the concept of a 'rebuttable presumption.' Our case managers report that the transaction files of some SACC lenders do not demonstrate a clear understanding of what they must identify, analyse and record to rebut the presumption of unsuitability in a compliant way.[5]

This is not surprising as the training materials and operational guidance manuals of some SACC lenders that CIO has seen during its systemic issue investigations, do not appear to either address this issue adequately or do so in inappropriate ways. For instance, one SACC lender, in its guidance document for lending staff, approached the presumption as though it placed an 'onus of proof' on the consumer for its rebuttal. As well as being contrary to ASIC RG209,[6] this led to an overly simplistic approach where the SACC lending staff purported to satisfy their obligations to rebut the presumption by asking the consumer whether they would

[4] Ibid
[5] This is consistent with ASIC's findings in Report 426 at paragraphs 159 - 166
[6] ASIC RG209 Credit Licensing: Responsible Lending Conduct at RG209.112 clearly places the onus to rebut the presumption on the credit licensee.

suffer hardship if offered a new SACC loan, and recording the consumer's (predictably negative) answer.

CIO has also observed some SACC lenders appearing to manufacture the basis for rebutting the presumption of unsuitability in an ex post facto manner. Even then, the analysis was, in one case, deeply flawed in that the FSP reasoned that a consumer was 'credit worthy' (itself non-compliant language) because the consumer's bank had allowed the consumer an informal overdraft and this was apparent from the bank statements.

3.3 A difficult concept

The 'presumption' in s133(3A) (and 118(3A)) of the NCCP is 'rebuttable' in the sense that it applies 'unless the contrary is proved.' 'Rebuttable presumptions' are a familiar concept for lawyers and are rules of evidence more than substantive rules of law.[7] Even then, for experienced lawyers, they are fraught with difficulty:

> Nothing could be simpler, more easily administered, more effective to prevent confusion and conflict. Yet there is no class of case more confused or confusing, more difficult to analyse than those which deal with the effect of presumptions on the burden of proof.[8]

The 'responsible lending space' of a SACC lender, whether a real room or somewhere in cyberspace, is not a court and SACC lending assessment staff are not lawyers and judges.

ASIC RG 209, in its declaratory text, when dealing with rebutting this presumption gives substantial guidance on what information may be required by a SACC lender to establish whether the presumption applies and to consider its rebuttal. Despite this, it is clear to CIO that the lending staff of some SACC lenders find it difficult to understand the concept of a rebuttable presumption.

3.4 A simpler solution

Section 133(3A) (and 118(3A)) seeks to address the problem of multiple loans leading to over commitment and consumer detriment.[9] This serious problem was described in the relevant Explanatory Memorandum as diminishing the standard of living of consumers and resulting in 'adverse health effects on the borrower.'[10]

This reasoning echoes the view of Professor Gail Pearson who has equated inappropriate and unsuitable lending with 'unsafe products.'[11] Product safety is an area where consumer protection laws do not merely regulate products but can ban them.[12] While not seeking to equate purely economic loss and hardship with the loss of life and limb which can be occasioned by some unsafe consumer

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[7] Bohlen, F 'The effect of rebuttable presumptions of law on the burden of proof', (1920) 68 Pennsylvania Law Review 307
[8] Ibid at 307-308
[9] Revised Explanatory Memorandum to the Consumer Credit Legislation Amendment (Enhancements) Bill 2012 at 4.7-4.8
[10] ibid
[11] Pearson, G 'Reading Suitability against Fitness for Purpose – The Evolution of a Rule' (2010) 32(2) The Sydney Law Review 311 at 388
[12] Part 3-3 of the Australian Consumer Law

goods, if the harm presented by multiple small amount credit contracts is so severe, then the case can be made that the solution is to prohibit, as much as possible, its occurrence.

One of the criteria for submissions in the Discussion Paper is to address complexity. Some matters are, by necessity, complicated and simple solutions will be inadequate. CIO submits that this is not one of them and that an outright prohibition on multiple small amount credit contracts will simplify compliance for SACC lenders and better protect consumers. This is, in our view, preferable to the current and more complex rebuttable presumption approach.

Legislatively, this could be achieved by the deletion of the words 'unless the contrary is proved', rendering the presumption of substantial hardship incapable of rebuttal and the proposed SACC loan unsuitable. SACC lenders are not permitted to provide credit products which are 'unsuitable' for the consumer[13]so this will be, effectively, an outright ban.

CIO submits that the rebuttable presumption of unsuitability be replaced with an outright ban on SACC loans if it appears to the SACC lender that:

- the consumer is in default under another SACC loan, or
- in the 90 day period before the loan assessment, the consumer had two or more other SACC loans.

This can be achieved by deletion of the phrase: 'unless the contrary is proved' from s133(3A) of the NCCP. Similarly with s118(3A).

4. Anti-Avoidance

4.1 The existing provisions

There is no 'broad' anti-avoidance provision in the NCCP. Section 334(1) provides that:

> A provision of a contract or other instrument by which a person seeks to avoid or modify the effect of this Act (other than the National Credit Code) is void.[14]

Like all 'contracting out' provisions, this assumes the application of the Act and, therefore, is ineffective to capture business models or methods which purport to operate outside NCCP regulation.

The balance of section 334 NCCP is concerned with 'indemnities' from various parties to the credit provider in order to 'cover' the latter should its contracts otherwise prove unenforceable. While necessary regulation, these provisions do not create an effective anti-avoidance option for regulators, courts and EDR schemes like CIO.

[13] NCCP s133.
[14] This section mirrors the earlier (and still applicable) section 191 of the NCC.

4.2 CIO's observations and cases

Some credit providers operating in the SACC sector of the market have purported to escape NCCP regulation and, therefore, the jurisdiction of CIO, by structuring their transactions to avoid its application.

4.2.1 In one CIO dispute, the credit provider engaged in conduct which was very similar to that dealt with by the Queensland Civil and Administrative Tribunal in the matter of Fast Access Finance (Beaudesert) Pty Ltd and Anor v Charter and Anor.[15] (**Fast Access**).

In summary, the consumer, upon application for loan funds, was told these were not available but that they could buy a diamonds from the credit provider at a certain price, on credit. The consumer was then invited to sell the diamonds back to a related entity (in the same room), for approximately 50% of the purchase price. The consumer then walked away from the transaction with a sum of money and owing the credit provider twice that amount.

As the QCAT adjudicator said at first instance, the 'not regulated view' of the transaction:

> … is so highly unlikely, improbable and implausible as to be a complete fiction. It is ridiculous that a person would wish to enter a business premises in order to buy a product no matter what it be, to sell it immediately and make a loss.[16]

The Fast Access model has recently been the subject of an action by ASIC and, while final orders have not yet been made, has been held by Justice Dowsett of the Federal Court to be:

> …a pretence or sham brought into existence as a mere piece of machinery to conceal the true nature of the transaction, which was the provision of credit.[17]

Some nine months earlier, CIO formed a similar view, held the transactions in question to be regulated, and, ultimately, unjust.[18] CIO took a broad view consistent with the only relevant legal authority available at that time, to find that the NCCP applied despite attempts to avoid its application by the credit provider in the way it structured its transaction.

CIO's reasoning did not only apply the QCAT decision as being 'on all fours' in the simple sense of following of a precedent, albeit one which was not strictly binding. The CIO Determination also contained its own independent reasoning, relying on the beneficial nature of the legislation as analysed in other cases[19], its purpose as outlined in the Explanatory Memorandum to the Act[20], and its analysis

[15] [2012] QCATA 51 on appeal from Rachael Carter & Michael Sinclair v Fast Access Finance (Beaudesert) Pty Ltd and Diamond Clearing House Pty Ltd [2011] QCAT
[16] [2011] QCAT
[17] ASIC v Fast Access Finance Pty Ltd [2015] FCA 1055 at [277]
[18] http://www.cio.org.au/cosl/assets/File/Determination%2017%20December%202014(1).pdf
[19] Such as Permanent Mortgages v Cook [2006] NSWSC 1104 at [88]
[20] Explanatory Memorandum, NCCP Bill 2009, para 8.3

of the effect of the transaction on the consumer, to conclude that it involved, despite the protestations of the credit provider, regulated credit.

In this case, the credit provider seemed to accept that the purpose of the structure of the transaction was avoidance, but still submitted to CIO that:

> Commercial enterprises are freely able to structure their businesses in any manner they please so long as they do so in a legal manner. There is no impediment to conducting business in the manner that [the FSP] did. Likewise, there is no impropriety in avoiding the operation of a legislative prohibition by not transacting in the way that breaches the law.
>
> …
>
> In addition to the comments above, we point out that [the consumer's] ultimate intention when he approached [the FSP] was to obtain a sum of money – and this is what he received. [The consumer] was obviously not picky about the manner in which he achieved that aim, otherwise he would not have freely entered into the agreement that he did. [21]

It is also salient that the credit provider insisted on pursuing this argument to a CIO Determination despite earlier opportunities to accept CIO jurisdiction and resolve the matter, at far less cost, on a non-determinative basis.[22]

4.2.2 In another CIO (COSL) decision, the credit assistance provider sought to rely on the 'short term' credit exemption in section 6(1) of the NCC. Again, this credit provider did not accept an earlier preliminary review by CIO and insisted on pursuing its argument that the relevant transactions were exempt from the NCC and, therefore, the NCCP, to a Determination. This Determination found that the transactions did not satisfy the requirements of section 6(1) of the NCC and that they were unjust and that the credit assistance provider had engaged in multiple failures to meet its responsible lending obligations.[23]

In that case, the FSP also made a detailed submission to the effect that the loans in question were not regulated, part of which is as follows:

> Neither [the FSP] nor [the Credit Provider] engages in any activity that falls within the definition of Financial Service under the Credit Ombudsman Service Rules (8th Edition) (**CIO Rules**).
>
> Accordingly, we do not believe CIO to have the jurisdiction required under clause 6.1(b) of the CIO Rules to investigate this complaint, which clearly relates to the alleged provision of credit under the Act.
>
> To explain further, the credit contracts [the credit provider] enters into with customers fall within the short term credit exemption contained in section 6(1)-(3) of the National Consumer Credit Code (**Code**) under the Act and [the credit provider] is not required to comply with any responsible lending obligations under the Act.
>
> Firstly, the financial supply fee, same day direct deposit fee and account keeping fees payable to [the FSP] for services that [the FSP] solely provides to the customer. Those fees are payable under an agreement between the customer and [the FSP]. Those fees are not imposed or provided for under the credit contract between [the credit provider] and the borrower.

[21] Note 15 above at para 15.
[22] Note 15 above at paras 3-6.
[23] http://www.cio.org.au/cosl/assets/File/Determination%2015%20December%202014%20with%20Rec_%20attached.pdf

> The term ‘under’, which appears within the phrase ‘under the contract’ at section 6(1), refers to an obligation created by, in accordance with, pursuant to or under the authority of, that contract. See, Chan v Cresdon Pty Ltd (1989) 168 CLR 242 at 249 (per Mason CJ, Brennan, Deane and McHugh JJ) (concerned with the scope of the word 'under' when concerned with the obligations imposed 'under this lease'). The narrowness of the term is impliedly acknowledged by section 6(2), which deems certain fees and charges to be imposed or provided for ‘under’ the contract, 'whether or not payable under the contract'.
>
> In this case, the only charges that the contract between [the credit provider] and the borrower imposes or provides for ‘under’ the credit contract are what are described as the ‘Total Credit Charges’. Those credit charges are fixed at 5% of the amount of the credit provided under the credit contract. As the only credit fees and charges imposed or provided for under the credit contract do not exceed 5% of the amount of credit, those charges are within section 6(1)(b).
>
> Secondly, the fees imposed by [the FSP] for services that it renders to customers do not fall within any of the categories of fees and charges that the Code deems at section 6(2) to be imposed or provided for under the credit contract.
>
> For instance, none of the charges imposed by [the FSP] are for ‘an introduction’ to [the credit provider] (s.6(2)(a)). Customers are free to deal directly with [the credit provider] , and if they do so due to a referral from [the FSP], there is no charge to the customer for the introduction. Moreover, [the credit provider] does not introduce customers to [the FSP], so section 6(2)(b) is inapplicable.
>
> Finally, the debtor does not pay anything to [the credit provider] for any service related to the provision of credit, except the credit charges that are fixed at 5%. Thus, nothing is added to the credit charges by operation of section 6(2)(c).
>
> [The FSP] will zealously adhere to its obligations under the Act with respect to any credit activities that it engages in that are related to credit contracts to which the Code applies. Based on the foregoing, however, the Code does not apply to the business undertaken by the [FSP] and nor to the credit contracts entered into by the [the credit provider] .[24]

The 'zealotry' of the FSP’s adherence to its obligations under the Act did not withstand careful and detailed scrutiny of its transactions by CIO. They were found to be regulated and non-compliant with the FSP’s responsible lending obligations.

Here again, CIO was able to penetrate a pretence at structuring transactions to avoid NCCP regulation, but the credit provider insisted on the success of its avoidance strategy and did not take the opportunity to resolve matter less expensively by agreement.

4.2.3 The most acute example, however, in the SACC lending space of the need for a general anti-avoidance provision is the recent case of ASIC v Teleloans Pty Ltd.[25] In that case, Teleloans Pty Ltd (**Teleloans**) held an ACL as a credit assistance provider and charged consumers to complete loan application forms, conduct preliminary assessments, refer them to Finance and Loans Direct Pty Ltd (**FLD**) (and no other lender), and otherwise assist in the 'administration' of consumers’ loans. FLD entered into short term loan contracts with consumers and only charged them the 5% allowed under the exemption from regulation in section 6(1) of the NCC. Teleloans, however, charged for its services amounts which

[24] Ibid at para 51
[25] [2015] FCA 268

resulted in the effective overall cost of the credit obtained by consumers who approached Teleloans, but received credit from FLD, being well in excess of that permitted under the SACC lending provisions of the NCCP and the NCC.[26] In almost every transaction, the consumer had no direct dealings with FLD and only dealt with the staff of Teleloans.

Although FLD and Teleloans were not 'related' entities under the Corporations Act, former directors of FLD were the directors of Teleloans and the mother of one of the Teleloans directors was a major investor in FLD. FLD operated from adjoining premises sub-let from Teleloans. Teleloans also was in a 'Loan Service Management Agreement' with FLD, but the fees paid under this agreement and the sub-lease were not held to be commissions. Teleloans and FLD submitted that these relationships were 'nothing to the point' and that Teleloans was not a credit provider but a 'helper' or assister. Its submissions on this and other matters were accepted by Justice Logan of the Federal Court. [27]

ASIC submitted that the 'arrangement' between Teleloans and FLD was such that it rendered the 'overall' transaction as one contract and, therefore, the Teleloans service fees were a charge made for the provision of credit. The Court specifically rejected this approach saying:

> 'Arrangement' is a word of such generality that it is apt to capture the relationship between Teleloans and FLD. But the position which obtains remains that credit is provided only under the contract with FLD. There is no credit provided under the contract with Teleloans. The charges made under that contract are a fee for services provided by Teleloans to the would be borrower. Those charges have no direct relationship with the loan which comes to be made by FLD under its separate contract with the borrower. In these circumstances, the Code is not applicable.[28]

His honour said that:

> In any event, a difficulty with any such development would be that, even though there is no general anti-avoidance provision in either the Act or the Code, s 6(2) of the Code contains some particular anti-avoidance measures. The presence of these would make it difficult to conclude that some more general doctrine ought to be imported…Had Parliament wished further to extend the definition of 'contract' or the anti-avoidance measures found in earlier State consumer credit models so as to extend to 'helpers', it could have done so.[29]

So, in this case, consumers responded to marketing for small amount loans from Teleloans. They received loans from FLD (despite only ever dealing with Teleloans) and paid more than twice the cost of credit for such loans than they would had they entered into properly regulated small amount credit contracts. Despite this, the Court held that the contracts were unregulated credit and the Teleloans charges could stand.

The 'particular' anti-avoidance provisions were not enough in the absence of a general anti-avoidance provision to capture these transactions.

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[26] One consumer borrowed an amount of $120 lent over 14 days, which cost the consumer only $6.00 under the FLD loan agreement, but a further $51.90 under the Teleloans 'Service Agreement.' This total cost of $57.90 for a 14 day $120.00 loan compares with $29.00 for a SACC regulated loan for the same amount and period. The evidence in the case showed each consumer entered into multiple loans with FLD arranged by Teleloans. See Note 25 at Annexure A [68]-[84].
[27] Ibid at [37] – [38]
[28] Ibid at [44]
[29] Ibid at [42]

4.3 The value of anti-avoidance provisions

Australian courts are familiar with anti-avoidance provisions, particularly, in relation to taxation laws. Specific anti-avoidance provisions in legislation have the advantage of their detail and specificity. They address a limited subject matter and are usually textually positioned within legislation adjacent to other provisions dealing with that same subject matter. Specific anti-avoidance provisions look much the same as other provisions and will set out, in some detail, the arrangements, factors and circumstances, which, if present, prevent the avoidance of regulation which would otherwise apply.

They sometimes have a 'purpose' test but this is not always necessary. The difficulty with specific anti-avoidance provisions is that they are often only temporarily effective. A detailed and specific provision is always susceptible to industry developing new means of avoiding its application, as in the Teleloans case discussed above.

General avoidance provisions, while often described as 'rules of last resort,' do not suffer as much from this temporal weakness. They rely almost entirely on a 'purpose test', though the effect of a particular scheme which is designed to avoid regulation will also be important.[30]

The value of such provisions is two fold:

- It provides the 'rule of last resort' if the examination of transactions when measured against specific provisions of the relevant legislation does not clearly determine whether they are regulated or not, and

- It sends a clear message to industry that time and resources spent on developing elaborate avoidance schemes may well be wasted.

4.4 Anti-Avoidance in financial services

The Corporations Act, as amended by the Corporations (Future of Financial Advice) Act, provides at section 965:

> (1) Subject to subsection (2), a person must not, either alone or together with one or more other people, enter into, begin to carry out or carry out a scheme if:
>
> (a) it would be concluded that the person, or any of the people, who entered into, began to carry out or carried out the scheme or any part of the scheme did so for the sole purpose or for a purpose (that is not incidental) of avoiding the application of any provision of Part 7.7A (which includes the conflicted remuneration provisions) in relation to any person or people, and
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> (b) the scheme or the part of the scheme has achieved, or apart from this section, would achieve, that purpose.

[30] For a detailed analysis of the differences between specific and general anti-avoidance provisions, see Kendall, K 2006, 'The Structural Approach to Tax Avoidance in Australia', *The Tax Specialist*, Vol 9 No 5 (June 2006), p. 291.

This general anti-avoidance provision is directed at the consumer investor protection provisions of the Corporations Act, in particular, those prohibiting conflicted remuneration. ASIC, in its Regulatory Guide 246, has said in relation to this provision:

> The anti-avoidance provision is designed to ensure that the policy intent of the FOFA Acts, including the conflicted remuneration provisions, is not avoided through industry or transaction restructuring.

And that:

> In administering the anti-avoidance provision, we are less likely to scrutinise schemes that are normal commercial transactions conducted in the ordinary course of business.

4.5 A similar provision for consumer credit

CIO submits that the entire consumer credit regime would benefit from a general anti-avoidance provision directed at any scheme or arrangement which has the purpose and effect of avoiding the application of the NCC and, consequently, the NCCP. This would provide a useful tool in the regulation of the market for SACC loans.

It would avoid the difficulties presented by cases such as Fast Access and Teleloans and send a clear signal to industry that the development of elaborate schemes to avoid NCCP regulation will be unsuccessful.

CIO submits that the Code be amended to include a general anti-avoidance provision.

The anti-avoidance provision could look like the following:

1. A person must not, either alone or together with one or more other people, enter into, begin to carry out or carry out a scheme if:

   (a) it would be concluded that the person or any of the people who entered into, began to carry out or carried out the scheme or any part of the scheme did so for a purpose (whether incidental or not) of avoiding the application of any provision of this Code or the National Consumer Credit Protection Act 2009 and relevant regulations; and

   (b) the scheme or the part of the scheme has achieved, or apart from the operation of this section, would achieve, that purpose.

This creates an offence and would need supplementation with provisions enabling a court to treat the transactions entered into as part of such a scheme as if they were regulated by the NCC and the NCCP. Perhaps as follows:

2. Any transaction under such a scheme under sub-section (1) above may be treated by a court or tribunal as if it were regulated by this Code or the National Consumer Credit Protection Act 2009 and relevant regulations.

5. Recording unsuitability assessments and bank statements

5.1 The current provisions

There is no specific statutory obligation to record unsuitability assessments, merely to make them under sections 128 – 130 of the NCCP.

ASIC says that the 'primary obligation' of a credit provider under its responsible lending obligations is:

> to conduct an assessment that the credit contract or consumer lease is 'not unsuitable' for the consumer: see Section C. This assessment is referred to as a 'preliminary assessment' (if you are providing credit assistance) or a 'final assessment' (if you are the credit provider or lessor).[31]

Section 132 stipulates that a credit provider must provide a copy of the assessment to the consumer if they request it. ASIC says that: "In practice, this means that you must keep a record of the assessment in a form that allows you to provide the assessment to a consumer promptly and in writing."[32]

ASIC further qualifies this statement by saying:

> Note: A licence condition supports this obligation, by requiring the credit licensee to keep a record of all material that forms the basis of an assessment of whether a credit contract or consumer lease will be 'not unsuitable' for a consumer in a form that will enable the licensee to give the consumer a written copy of the assessment if a request is made under s120, 132, 143 or 155, …

We note that the ASIC guidance refers to the 'material that forms the basis' of an assessment' but not to the 'reasons' for the assessment. Later in the same Regulatory Guide, ASIC does deal with "What Information should be included in a written assessment?" and says, helpfully:

> You should ensure that the written assessment you provide to consumers will:
>
> (a) assist consumers in understanding that the credit contract has been assessed as 'not unsuitable' for them, and
>
> (b) assist you in demonstrating compliance with the responsible lending obligations. [33]

The Guide does refer to such assessments showing the 'factual' basis on which they are made and, for instance, to set out the consumer's income and expenses to demonstrate their capacity to meet the loan repayments without hardship. It does not say, however, that the assessment should expressly and explicitly analyse the 'factual basis' to conclude that the consumer can or can't make the repayments required without hardship. The question is implied rather than expressly asked and answered in the document. There is a potential disconnection between 'demonstrating' compliance and 'actual' compliance with the responsible lending obligation.

[31] ASIC RG209.2
[32] ASIC RG209.138
[33] ASIC RG209.142

Indeed, at RG209.146, ASIC says:

> We do not expect you to disclose the commercially sensitive lending criteria on which your credit decisions are based. Only the information that specifically relates to the statutory concepts of 'requirements and objectives', 'capacity to repay' and 'reasonable inquiries' should appear in the written assessment.[34]

5.2 CIO's observations

5.2.1 CIO, in the course of its investigation of complaints against SACC lenders, inspects the loan files of such lenders. In the course of these inspections, CIO has observed that files of most SACC lenders do contain information about:

- the income and expenses of the consumer,
- their payslips (if any),
- bank statements as required by the SACC lending provisions.

These are frequently noted on a document described as a 'Suitability Assessment' or 'Suitability Checklist' and, indeed, many of these documents are checklists. They have a list of required documents or scripted questions with a 'tick box' beside them. The conclusion to be drawn from such documents is that if the boxes are 'ticked', the loan is not 'unsuitable' and can be approved as being compliant with the lender's responsible lending obligations, including those particular to SACC lenders.

However, what is frequently missing is an express statement that the repayments required under the loan, based on the consumer's financial position as investigated and verified by the credit provider, can be met without hardship. Technical compliance can be demonstrated, but it is not clear whether it has been actually achieved in individual cases. What is disturbing is when all the documents required by such 'checklists' and by the regulations, such as the 90 days of bank statements, are present in the lender's file, but the consumer has met with hardship and has made a complaint to CIO.

5.2.2 As stated above, CIO has observed in its inspection of SACC lender files in the course of its investigation of disputes that:

- there appears to be inconsistent and frequently non-transparent use of the information in the bank statements by some SACC lenders, and

- a disturbing tendency by some SACC lenders to treat the mere collection of the statements as a 'safe harbour' for compliance with their responsible lending obligations.

Without an express statement that the bank statements have been considered and their implications analysed, their presence on the file is only evidence of compliance with the requirement to collect them. It is not, in the view of CIO, proof of their proper consideration and, therefore, of actual compliance by the lender with its responsible lending obligations. It may well be that the SACC

[34] ASIC RG209.146

lending officer does consider 'in their head' the core questions for responsible lending, namely the capacity to repay without hardship, but their assessment documents, frequently, do not explicate this reasoning.

We refer again to our observations about the rebuttable presumption at 3 above, and say that these are also examples of the 'misuse' or 'under use' of bank statements and other verification documents by SACC lenders. How the presumptions are rebutted is not always clear from the documents on the file.

5.3 An express obligation to record

CIO submits that section 128 of the NCCP should be amended to include the words "and recorded" after "made."

This will create a positive obligation on all credit providers, not just SACC lenders to record more explicitly their credit assessments. It will, in CIO's view, be particularly important in the SACC lending market.

CIO further submits that RG209 be amended, probably after RG209.146 to make it clear to all lenders, particularly SACC lenders, that their recorded credit assessments must expressly state that the financial information provided and verified (along with the stated needs and objectives of the consumer) supports (or does not support) an assessment that the repayments required by the proposed credit product can be made by the consumer without hardship.

CIO recognises that this too could become a 'safe harbour' and its completion a formulaic process. However, forcing the SACC lending officer to consider this statement and approve it in an express way will better integrate actual compliance with the responsible lending obligation with compliance demonstrated by the collection of documents.

6. Comparable Consumer Leases

6.1 Consumer leases are comparable with SACC loans

CIO submits as follows:

- Consumer leases for household goods with a value of $2,000 or less are comparable with SACC loans.
- Consumer leases for other goods (such as motor vehicles) up to $5,000 are comparable with MACC loans.
- There should be greater consistency between the regulatory requirements that apply to SACC loans and comparable consumer leases.

CIO shares the concerns of ASIC in its Report 447 into the 'Cost of Consumer Leases for Household Goods' particularly:

> In light of ASIC's findings, there are four areas of concern that could be given further consideration to improve consumer outcomes:

(a) the high cost of consumer leases, particularly those over a longer term (e.g. leases that are two years or longer),

(b) the lack of consumer understanding about consumer leases,

(c) the impact of high-cost consumer leases on Centrelink recipients, and

(d) the lack of consistency in regulatory treatment of consumer leases compared with other small amount credit contracts.[35]

In the casework experience of CIO, the market for consumer leases for household goods overlaps in large measure with that for SACC loans. ASIC found that 24% of 288 loans which were the subject of their Report 426 were to consumers who received more than 50% of their income from Centrelink.[36]

While not all SACC lenders will lend to Centrelink recipients, it is the experience of CIO (and the finding of ASIC) that the majority of consumer lessees for household goods are Centrelink recipients.[37]

These two markets are, therefore, very comparable. Regulation should, where possible, be 'neutral' as between comparable products provided to the same market. The alternative is anti-competitive and bad for consumers and industry.

6.2 Applying SACC loan provisions to comparable consumer leases

6.2.1 CIO agrees with the observations of ASIC in its Report 447 that there is pronounced lack of understanding about:

- the nature of their lease contracts among many consumer lessees for household goods,
- the true cost of their lease contract compared to the initial cost of the goods in question.

CIO, therefore submits that the additional disclosure requirements listed in Question 15 of the Discussion Paper should apply to comparable consumer leases.

These include:

- the Cash Price of the Goods with modifications to be discussed below,
- the amount the consumer will pay in excess of the Cash Price
- the cost of credit expressed in dollars,
- the cost of credit expressed as an interest rate.

We note that the Discussion Paper also refers to "other services financed through the rental payments" and gives examples such as a warranty or delivery costs. To

[35] ASIC Report 447 para 76
[36] ASIC Report 426 para 132
[37] Ibid para 29. In fact, in ASIC's data, all of the 69 leases from two different lessors were paid through the Centrepay system.

this we would add collection costs though, as ASIC reports, most consumer leases do not result in a surrender of the leased goods.

We suggest it would be simpler if the Cash Price was determined using the formula in Part 13 of the NCC for determining the Cash Price of goods which are the subject of instalment contracts with an additional component to cover warranty and delivery. This 'modified cash price' could be disclosed and used to calculate the cost of credit and for other purposes to be discussed below.

6.2.2 Repeat leasing/borrowing.

CIO submits that either the outright ban proposed at 2.1 above or the existing rebuttable presumptions in relation to repeat borrowing and/or leasing be applied to comparable consumer leases for household goods.

There does not appear to be any salient difference between the problem of repeat borrowing of SACC loans and repeat leasing of consumer leases or, and more likely, the combination of the two to produce overcommitted consumers.

Consumer lessors are still subject to the responsible lending obligations of all ACL holders, but these were held to be insufficient for SACC lenders. So should they also be for comparable consumer lessors. For instance, if the consumer lessor identifies from the consumer's bank statements that the consumer has entered into SACC loans or other consumer leases within the previous 90 days, it should be prevented from providing a new consumer lease. The 'default' provisions should also apply to consumer leasing.

6.2.3 A modified Warning Statement

CIO submits that a Warning Statement be mandated for the websites and other communications of comparable consumer lessors prompting consumers to consider whether they really need the goods in question and other, less expensive, means of acquiring those goods.

Such statements are mandated for SACC loans and CIO sees no reason why they should not also be for comparable consumer leases.

6.2.4 A modified cap on the total amount recoverable

CIO submits that there should be a cap which limits the total amount recoverable by a consumer lessor from a consumer to twice the modified cash price for the leased goods.

Such a cap exists for SACC lending and, as ASIC has reported in its Report 447, that consumer lessors are often paying many times more for the credit represented by their consumer lease than they would if they had borrowed the cash price of the goods from a SACC lender.[38]

This is not appropriate for a market made up of mostly vulnerable consumers.

[38] ASIC Report 447 paragraph 67

6.2.5 Protected Earnings

CIO submits that the protected earnings provisions for SACC lenders also be applied to consumer lessors so that the payments due under a consumer lease can never exceed 20% of their income from Centrelink.

Again, this would lead to comparable consumer leases being regulated in the same way as SACC lenders and the policy reasons for it have been largely explicated above. ASIC Reports that SACC lenders have responded well to the protected earnings provisions and that they have been largely a success.[39]

Consumer lessors should do the same.

[39] ASIC Report 426 paragraphs 128-130