Justice & International Mission
Uniting Church in Australia
SYNOD OF VICTORIA AND TASMANIA

130 Little Collins Street
Melbourne Victoria
Australia, 3000
Telephone: +61-3-9251 5271
Facsimile: +61-3-9251 5241
jim@victas.uca.org.au

SACC Review Secretariat
Financial System and Services Division
Markets Group
The Treasury
Langton Crescent
PARKES ACT 2600
E-mail: consumercredit@treasury.gov.au

Submission by the Synod of Victoria and Tasmania, Uniting Church in Australia to the Review of the small amount credit contract laws Interim Report

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The Uniting Church in Australia, Synod of Victoria and Tasmania welcomes the opportunity to make a submission to the *Review of the small amount credit contract laws, Interim Report.*

The Synod 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.

The Synod recognises that these activities meet a need for credit from consumers that experience financial exclusion. However, it shares the concerns of others that the practices and compliance shortcomings that are evident in the sector are causing some harm to its customers.

The Synod strongly agrees with all the Observations made in the interim report.

Regarding Observation 2 we agree that ASIC enforcement of the responsible lending practices of SACC providers should be a priority. In this context we believe that priority should bear reference to the large number of Australians who experience financial exclusion and so are more likely to use this form of credit. Therefore, the resources required by ASIC to adequately conduct this enforcement should be more than having regard to the relative size of this segment as part of the overall finance sector.

The Synod supports reducing the establishment fee for subsequent loans for a returning customer from 20 per cent to 10 per cent. It helps address the current incentive for SACC providers to encourage repeat borrowing. However, the Synod would encourage the impact of this measure to be evaluated after implementation to ensure that it does reduce the harm from repeat borrowing.

In order to protect vulnerable people on low incomes the Synod supports Option 2 as well, as a further safeguard. As noted in the Interim Report the NCPA's CoreData survey found that 80 per cent of lenders admitted providing SACC loans to customers who had two or more SACCs in the previous 90 days, suggesting that the bulk of the industry is at the very least reckless to the existing safeguard provisions around repeat lending.

The Synod also supports Option 3, in addition to Option 2 and does not agree that it should be one or the other than is implemented. One is a safeguard on repeating loans, while the other sets a safeguard on the amount of income vulnerable people can be required to pay towards small amount credit contracts. Given the evidence of the aggressive and unethical behaviour of some SACC providers, the greater the number of safeguards, the more likely the overall system is to be in protecting vulnerable people from harm. System measures that prevent harm are also more cost efficient than enforcement mechanisms that require investigation and prosecution. The implementation of Options 1, 2 and 3 are unlikely to impact on the business of responsible SACC providers, concerned not to harm the people take SACCs from them.

The Synod notes that MoneyMe was quoted in the media as supporting Option 1 and halving the cap on total fees that can be charged.[1]

Options 4, 5 and 6 address the issue of default payments from three distinct aspects, and to that end could each be implemented without conflicting with each other. Option 4 limits the timeframe in which a default penalty can be applied. Option 5 addresses the amount that can be demanded in repayment of a default penalty, without capping the penalty itself. Option 6 offers some protection over the size of the default penalty itself.

The Synod supports Option 4 to introduce a default window in which no default fees can be charged until the consumer has missed a payment by one payment cycle. There should still be protection from default fees being charged that are greatly inflated compared to the costs actually incurred by the SACC provider, so Option 4 on its own is not an adequate protection. We also support Option 5 being implemented with Option 4 to ensure vulnerable people are not hit with unaffordable default fee payments.

Option 6 offers some protection over the size of the default payment, which is welcome. The alternative would be to set a fixed cap on default penalties, that is in line with the actual costs to the SACC provider. A risk with Option 6 is that it may encourage some unethical SACC providers to increase the size of the loans, although this is offset by the risk to them of not having the loan repaid. Against that default rates amongst SACC clients are generally lower than for credit cards. Data from Credit Suisse found the percentage of bad debt was 4.1 per cent for Thorn consumer leasing, 10.9 per cent for Thorn financials, 7.2 per cent for all Cash Converter operations, 17.6 per cent for unsecured lending by Money 3 and 7.2 per cent for Money3 secured lending.[2] By comparison, in 2013, credit card defaults were reported to be at 15 per cent.[3] However, the lower default rates are likely to be due to people taking the loans prioritising repayment of the loans over other essentials. One of our agencies has reported high levels of emergency relief being accessed by people with small amount credit loans.

The Synod supports Option 7, provided it actually forces SACC providers to reduce the payment that would arise from early repayment of a SACC. Our preference would be for the 4 per cent monthly fee to apply to the declining balance, so that even part early payment reduces the amount the client needs to pay. This should be combined with the safeguard that fees can only be charged on a monthly basis, so that the person repaying the loan is not liable to pay the 4 per cent fee in respect of any outstanding months after they have paid the outstanding balance.

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[1] Shaun Drummond, 'Paydat lender calls for tougher rules to protect customers', *The Australian Financial Review,* 12 January 2016.
[2] Sandra McCullagh and Chris Parkes, 'Risks in payday lending and goods rental', Credit Suisse, 3 March 2015, p. 14.
[3] Veda, 'Christmas credit crunch warning: New data reveals pre-Christmas applications most likely to cause credit default pain', Media Release, 1 September 2014.

Option 8 should be implemented to prevent the practice of 'front-loading' repayments, but should still implement Option 7 to decrease the repayments if the loan is paid off earlier than the loan term.

The Synod strongly supports measures to end the regulatory arbitrage used by lease providers to avoid the tougher Consumer Credit Enhancement regulations.

Credit Suisse found that approximately 50 per cent of the revenue of Radio Rentals came from CentrePay payments, with approximately 50 per cent of that for entertainment and technology items.[4]

The Synod has been surprised that lease providers appear to have made no attempt to rein in their excessive behaviour, despite this review. The cost of items can still be exorbitant compared to purchasing the good outright. As just one example, rent4keeps offers a Layback Stroller for $4.95/week for 36 months, a total contract cost of $772.20.[5] The same stroller can be purchased from Target for $89, including free home delivery.[6] Thus, in a three year period rent4keeps would make 8.7 times the cost of the stroller compared to outright purchase.

The Synod supports Option 9 to set a cap on leases for low-value goods and that it be no more than the 48 per cent that applies to credit contracts in general. The Synod would also support that leases should not be permitted to run for more than four years to protect people from leases being extended. The Synod is aware that some lease providers suggest that the person leasing the goods can purchase them at the 'end' of the lease for a nominal fee (for example $1), but then do not make it easy for the person leasing the product to make the final purchase of the goods in question. If the person leasing the product fails to understand how to make the final purchase, the lease provider simply rolls the lease over and continues to collect lease payments.

Credit Suisse pointed out that the Radio Rental that "Rent, Try, $1 Buy" product may be misleading in that the customer does not necessarily get to buy the actual product that they have been renting, but it may be a similar product.[7] The Radio Rental website states in fine print (smaller font than the rest of the page):[8]

> *Goods available to buy using Rent, Try, $1 Buy are similar to rented good in age, dimension and features. $1 buyout is after payment of either 24, 36 or 48 (product dependent) months rental.*

Customers are notified that their contract is coming to an end, but the customer must notify in writing Radio Rentals at least 30 days before the end of the contract that they want to buy the goods. The person then needs to go into a store after notifying Radio Rentals and pay the $1 in order to gain the "Rent, Try, $1 Buy" offer. Numerous customers reported that an additional month's rent was taken out if they missed the required payment dates by just one day.[9] Credit Suisse concluded that:[10]

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[4] Sandra McCullagh and Chris Parkes, 'Risks in payday lending and goods rental', Credit Suisse, 3 March 2015, p. 3.

[5] http://rent4keeps.com.au/rental-products/baby-needs-nursery/layback-stroller/

[6] http://www.target.com.au/p/trek-layback-stroller/57461953?utm_term=57461953&utm_content=trek-layback-stroller&utm_source=google&utm_medium=merchant-site&utm_campaign=merchant-site&gclid=COH09OOzvcoCFQGAvQodkQ4IwQ&gclsrc=aw.ds

[7] Sandra McCullagh and Chris Parkes, 'Risks in payday lending and goods rental', Credit Suisse, 3 March 2015, p. 9.

[8] https://www.radio-rentals.com.au/rent-try-buy

[9] Sandra McCullagh and Chris Parkes, 'Risks in payday lending and goods rental', Credit Suisse, 3 March 2015, p. 9.

We believe that much of this contortion around executing on the $1 Buy component is to ensure compliance with Consumer Leasing regulations and ensure the contracts does not fall under Consumer Lending regulation. Thus the regulatory arbitrage is actually creating customer dissatisfaction in its execution.

Credit Suisse found that consumer leasing contracts continue on after the initial term, if the customer does not terminate them. The onus lies with the customer to take action. Otherwise, payments continue to be taken from the customer, with the contract being indefinite.[11] So in addition to placing a four year cap on contracts, the legislation should be amended to mean a lease contract automatically terminates at the end of the agreed period with the customer and the onus is on the company to recover the goods.

The Synod strongly prefers that the cap apply to all lease arrangements either by the value of the goods (less than $2,000 indexed to price increases) or the type of goods (household and electronic goods). A cap that applies to only certain types of customer would be more complex, open to manipulation (a lease provider could argue that the customer never disclosed that they were on Centrelink benefits for example) and may leave certain vulnerable customers without the protection of the cap.

The Synod supports Option 10 of including the add on features and products under the cap, as this provides simplicity for the person taking the lease.

The Synod also supports Option 11 and that the cap on net income that can be used to service all lease repayments should apply to all customers, not just those in receipt of income from Centrelink. The cap should be combined to cover all SACC repayments and lease repayments. There are issues around providers knowing what SACC and lease arrangements a person has with other providers, if the person does not disclose them to the provider. The Synod recognises consideration needs to apply to the balance between protecting the privacy of the person on the SACC on in the lease arrangement and making the safeguard effective. However, the provider of the lease should be required to review the last 90 days of bank statements of the person seeking the lease, to check for direct debits that reveal the presence of an existing SACC or lease. Of course a person might still claim not to have a bank account or provide information on one bank account while concealing others.

The Synod supports Option 12 to prescribe the maximum amount that can be charged on early termination of the contract. This is preferable to Option 13, if only one of Option 12 or Option 13 were to be implemented. The Synod would support both being implemented. Many people taking leases would find the pursuit of legal action difficult and daunting. If the legal action were pursued by an agency on their behalf, there is still the problem of making people taking leases aware this remedy exists.

Dr Mark Zirnsak
Director
Justice and International Mission Unit
Synod of Victoria and Tasmania
Uniting Church in Australia
Phone: (03) 9251 5265
E-mail: mark.zirnsak@victas.uca.org.au

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[10] Sandra McCullagh and Chris Parkes, 'Risks in payday lending and goods rental', Credit Suisse, 3 March 2015, p. 9.
[11] Sandra McCullagh and Chris Parkes, 'Risks in payday lending and goods rental', Credit Suisse, 3 March 2015, p. 11.