4 September 2012

By email: enhancementsregulations@treasury.gov.au

Manager
Consumer Credit Unit
Retail Investor Division
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Manager

Regulations to support provisions in the Consumer Credit Legislation Amendment (Enhancements) Bill 2012

The Consumer Action Law Centre (**Consumer Action**) welcomes the opportunity to comment on Regulations to support provisions in the Consumer Credit Legislation Amendment (Enhancements) Bill 2012 (**the regulations**).

Briefly, we have serious concerns about three of the draft regulations

- 28XXC (regarding authorisations to deduct repayments from the borrower's wage);
- 28S (regarding the operation of the Protected Income Amount); and
- 79C (regarding defaults in direct debit repayments of small amount credit contracts).

These regulations will not operate as intended and will cause consumer detriment unless they are extensively redrafted.

We have significant, but less serious concerns with three more draft regulations:

- 105C (regarding the information that must be provided on the end of lease statement);
- 105L (regarding requests for consent to enter a lessee's property to repossess leased goods); and
- Form 20 (which provides information about lessee's rights if they are in default).

We are broadly supportive of the other regulations and have recommended minor amendments to some.

Our comments are detailed more fully below.

About Consumer Action

Consumer Action is an independent, not-for-profit, campaign-focused casework and policy organisation. Consumer Action provides free legal advice and representation to vulnerable and disadvantaged consumers across Victoria, and is the largest specialist consumer legal practice

Consumer Action Law Centre
Level 7, 459 Little Collins Street Telephone 03 9670 5088 info@consumeraction.org.au
Melbourne Victoria 3000 Facsimile 03 9629 6898 www.consumeraction.org.au

ABN 37 120 056 484 ACN 120 056 484

in Australia. Consumer Action is also a nationally-recognised and influential policy and research body, pursuing a law reform agenda across a range of important consumer issues at a governmental level, in the media, and in the community directly.

We also operate MoneyHelp, a not-for-profit financial counselling service funded by the Victorian Government to provide free, confidential and independent financial advice to Victorians experiencing financial difficulty.

Draft regulations regarding small amount lending

Draft regulations 28XXA and 28XXB: Small amount credit contracts – requirements for warning in premises and on website

We welcome the warning notices and we approve of the location and wording requirements for in-store and online versions. In particular we welcome that the notices give consumers specific options (calling a financial counsellor, utilities hardship, Centrelink advance payments) rather than simply advising borrowers to consider their options.

The only amendment we would recommend is to the section directing borrowers to 'the free National Financial Helpline'. ***We recommend that the statement is amended to be clear that the helpline is a financial counselling service. For example, it could read: "Talk to a free, independent financial counsellor on 1800 007 007".***

Draft Regulation 28XXC: Authorisation for Deduction

We have serious concerns about draft regulation 28XXC, which seeks to enliven a requirement at subsection 160E(2) Consumer Credit Legislation Amendment (Enhancements) Bill 2012 (**the Enhancements Bill**. The regulation is deeply flawed—rather than allowing 160E(2) to operate, it actually allows lenders to avoid those requirements entirely. We strongly recommend it be redrafted.

The problem

To explain the problems with 28XXC, it and section 160E of the Enhancements Bill need to be reproduced. The relevant parts of section 160E read:

> **160E Requirements for giving authorisation to employer**
>
> (1) This section applies to a credit provider or lessor giving, or intending to give, an employer of a debtor or lessee who is party to a credit contract or consumer lease with the credit provider or lessor an instrument that:
>
> (a) was made by the debtor or lessee; and
>
> (b) authorises the employer to:
>
> (i) make one or more deductions from one or more amounts payable by the employer in relation to the performance of work by the debtor or lessee; and
>
> (ii) pay the deductions to the credit provider or lessor.

Credit provider or lessor must give statement to employer

(2) If the credit contract or consumer lease is of a kind prescribed by the regulations, the credit provider or lessor must give the employer a statement, in the form prescribed by the regulations for that kind of contract or lease, with the instrument.

Civil penalty: 2,000 penalty units.

Credit provider or lessor must give 7 days' notice to defaulting debtor or lessee

(3) If the debtor or lessee is in default under the credit contract or consumer lease, the credit provider or lessor must give the debtor or lessee at least 7 days' notice, in a form prescribed by the regulations, of the intention of the credit provider or lessor to give the instrument to the employer.

Civil penalty: 2,000 penalty units.

(4) To avoid doubt, subsection (3) does not apply if there are not regulations in force prescribing a form for the purposes of that subsection.

Draft Regulation 28XXC reads:

28XXC Authorisation for deduction

(1) For subsection 160E (2) of the Act, this regulation applies to a credit contract or lease under which:

(a) a credit provider or lessor gives an employer of a debtor or lessee an instrument mentioned in subsection 160E (1) of the Act; and

(b) the first deduction under the instrument must be made within one month after the debtor or lessee sign the instrument.

(2) For subsection 160E (2) of the Act, the form of statement is set out in Schedule 9.

The combined effect of 160E and 28XXC is that:

- if a credit provider wants to use the 'instrument' described in 160E(1) (that is, an authorisation for an employer to deduct debt repayments directly from the borrower's wage); and
- the first deduction made under the instrument is within one month of the borrower signing the instrument; then
- the credit provider must give the employer the statement described in 160E(2). The regulations prescribe the form of this statement at Schedule 9.

The purpose of the 160E(2) statement is presumably to add a layer of consumer protection in that it tells the borrower (and their employer) that the borrower can cancel the authorisation at any time. That is, the borrower is made aware they needn't allow the deduction to occur if it would cause them hardship.

However, the (limited) protection this provides is completely undermined by the regulations as they are currently worded. As long as the credit provider does not request a deduction within one month of the borrower signing the wage deduction instrument, they can use that instrument at will without ever producing the 160E(2) statement. The form or content of the instrument in

160E(1) does not appear to be regulated and so can be in any words the credit provider chooses. That being so we fail to see the point of 160E(2) and 28XXC at all—they create a tightly prescribed statement that will never be used.

The cause of the problem
This problem appears to be created by the drafters confusing 'the instrument' as discussed in subsection 160E(1) of the Bill for the 'statement' in 160E(2).

It seems that the purpose of Regulation 28XXC is to ensure that the instrument in subsection 160E(1) can only be used if the first deduction is made within one month of the borrower signing. This is clearly not the effect of 28XXC and indeed it looks like 160E does not even allow this kind of regulation to be made.

It further appears that the confusion between 'the instrument' and 'the statement' is caused by confusion around the purpose of 160E in the first place. It is not clear to us whether 160E is designed to allow lenders an inexpensive method for garnishing the wages of a debtor who is in default, or to allow borrowers a method for paying off their loan by arranging a direct payment from their wage.

Without wanting to re-litigate arguments we have made previously, 160E is bad law in either case. If the purpose is to allow lenders to garnish wages of borrowers in default, then 160E undercuts sensible law which requires that wage garnishing can only be allowed with a court order. If this is indeed the purpose of 160E, then all this section achieves is to legitimise extremely poor debt collection conduct which until now has only been used by highly questionable fringe operators.

If, on the other hand, the purpose of 160E is to allow borrowers to arrange direct repayment of their debts through their wages, then it is a little less dangerous but completely unnecessary. A borrower and their employer can make this arrangement themselves and the credit provider need not and should not be involved.

We recommend that 28XXC be amended to require that a credit provider who wishes to rely on a wage deduction authorisation must provide the 160E(2) statement whenever they request the debtor's employer to make a deduction, regardless of the type of contract.

Draft statement: Schedule 9
The intent of the statement referred to in draft regulation 28XXC (at Schedule 9 of the regulations) is also uncertain. In particular it is not clear who the intended audience of the statement is.

The instructions on the first half of the statement are to address it to the employer of the debtor and from the credit provider. However, the following part of the statement then reads as if it is from the borrower, rather than the credit provider:

> I consent to my employer making the following deductions DIRECTLY FROM MY SALARY to meet repayments under a contract with the above credit provider:

Later, the section headed 'Important' is directed at the borrower, rather than their employer. ***We recommend the statement be rephrased so it is clearer who the intended audience is.***

We also recommend that the statement should include an additional notice to the employer which tells them that

- ***if the borrower requests that the employer not make the payment, the authority is immediately cancelled and the employer is not entitled to make the deduction; and***
- ***the authority/deduction request does not bind the employer, and they can refuse to make the payment whether the borrower cancels the request or not.***

The purpose of this additional text is to ensure the employer does not feel obliged to make the payment if they feel uncomfortable doing so. Our legal practice has handled one case where an employer who received a deduction request felt obliged to make the payment unless the authority was cancelled by both the borrower and the credit provider.

Notice where credit provider or lessee is in default: subsection 160E(3)
If a debtor has signed an authority to deduct payments from wages and the debtor is in default, subsection 160E(3) of the Enhancements Bill allows regulations to require that the credit provider give at least seven days notice before approaching the borrower's employer to request a deduction. Subsection 160E(4) clarifies that no notice needs to be given if regulations are not made for 160E(3). At this stage, no such regulations have been made.

In Treasury's commentary and consultation questions that accompanied the draft regulations, Treasury asks whether this notice is required since 'deductions need to commence within one month of the form being signed by the lessee or debtor'. As we have explained above, regulation 28XXC does not in fact require any deductions to begin within a month of signing, and indeed it does not look like the Enhancements Bill even permits regulations that would require this.

In any event, ***we recommend that the regulations be amended to require a 160E(3) notice to be provided to all borrowers or lessees if the credit provider wishes to request a wage deduction. We further recommend that the notice must clearly say that the borrower can cancel the authority to deduct payments at any time by contacting the credit provider or by requesting their employer not to make payments.*** These authorities are likely to cause significant harm if a borrower is defaulting on their loan repayments because they are in financial hardship as they will limit the borrower's ability to prioritise payment of essentials like housing and food over debt repayments. The 160E(3) notice will at least give borrowers a chance to cancel the authority before deductions are made.

<u>28S: Operation of the Protected Income Amount</u>
There are a number of serious problems with regulation 28S. It too needs to be significantly redrafted.

Eligibility
The purpose of 28S is to create a Protected Income Amount (PIA) for borrowers who are reliant on Centrelink payments. Under subregulation 28S(2), the 'class of consumers' to which the Protected Income Amount would apply are those:

- who 'are qualified for a pensioner concession card' under section 1061ZA of the *Social Security Act:* 28S(2)(a); and
- for whom social security payments make up at least 50% of their income: 28S(2)(b).

The pensioner concession card requirement excludes large numbers of people who are predominantly or solely reliant on Centrelink payments and so makes the PIA scheme of very little value. For example, this requirement would exclude most people whose sole source of income is Newstart payments.[1] It would also exclude most recipients of ABSTUDY, Austudy, Carer Payment (Child) or Youth Allowance (student) who earn little enough to be eligible for a low income health care card. This amount of income -- on average less than $438 per week for eight weeks[2] -- would put a single person with children below the Henderson poverty line[3] yet in most cases not make them a consumer to which the PIA applies. If the purpose of the PIA is to protect low income borrowers then that purpose is seriously undermined by the pensioner concession card requirement.

It will also be very difficult for a lender to be able to quickly and accurately assess if a prospective borrower is eligible for a pensioner concession card under 1061ZA unless the borrower already has the card and produces it, which they may not. Research by The Australia Institute has found that large numbers of Australians are failing to access Commonwealth benefits for which they are eligible for a variety of reasons. It also found that 14 per cent of low income households do not use their concession cards and 26 percent 'don't like' to use their card or are embarrassed to use it.[4]

In cases where a prospective borrower does not choose to present their concession card, 28S(2)(a) seems to require a lender to assess whether the borrower would be eligible for a card. This requirement invites evasion—it requires lender to undertake a relatively complex and time consuming task which may not be in their interests to perform (as it may mean they cannot provide a loan to the borrower, or must provide a smaller loan). If a lender evades this provision it will be very difficult to enforce even if the breach is reported. If the lender's assessment of eligibility is challenged, they could argue that they made reasonable attempts to make the assessment.

We do not see why the 'pensioner concession card' condition is required. We understand that the purpose of the PIA is to strengthen responsible lending laws by ensuring that those on the lowest incomes (defined as people who are predominantly reliant on Centrelink payments) could not

[1] Newstart recipients are only eligible for a pensioner concession card if they are over 60 years old and have been receiving Newstart for 39 consecutive weeks (subsection 1061ZA(2)), is assessed as having partial capacity to work, (1061ZA(2B)) or if they are single and the principle carer of a child (1061ZA(2B)).
[2] Department of Human Services, 'Eligibility for Low Income Health Care Card', http://www.humanservices.gov.au/customer/enablers/centrelink/low-income-health-care-card/eligibility; Department of Human Services, 'Income Test for Low Income Health Care Card', http://www.humanservices.gov.au/customer/enablers/centrelink/low-income-health-care-card/income-test.
[3] The poverty line for a single person, without children is currently $470.36 per week including housing costs. Melbourne Institute of Applied Economic and Social Research (2012), Poverty Lines: Australia: March Quarter 2012, p 1. Accessed from http://melbourneinstitute.com/downloads/publications/Poverty%20Lines/Poverty-lines-Australia-March-2012.pdf
[4] The Australia Institute (2010), *Missing Out: Unclaimed Government Assistance and Concession Benefits,* pp 3-4. Accessed from https://www.tai.org.au/index.php?q=node%2F19&pubid=760&act=display

lose large amounts of their income to payday loan repayments. This objective is met by the 50% requirement in 28S(2)(b) (though that requirement needs redrafting, as discussed below). If the Government is of the view that an additional eligibility requirement like the pensioner concession card requirement is necessary, then this requirement should be extended to include Health Care Card holders.

The pensioner concession card requirement undercuts the purpose of the PIA and is unwieldy. We recommend that it be removed. If the Government wanted to keep an additional eligibility requirement of this type, 28S(2)(a) should be amended to include people who are eligible to hold a Health Care Card.

The method of calculating the borrower's income and the unpaid balance of current loans held by the borrower at 28S(3) is also problematic, because:

- 28S(3) requires the credit provider to assess the consumer's income for the previous year, but will be unlikely to be able to access this information. This will be counter-productive as it will encourage lenders and borrowers to make inaccurate estimates. ***We recommend that 28S(3) be amended to instead require lenders consider the past 90 days of income.*** Lenders will be likely to have this information at hand as the Enhancements Bill requires them to obtain and consider bank statements for the previous 90 days to verify the borrower's financial position[5];
- the income calculation will include Centrelink payments like Rent Assistance or Utilities Allowance which are designed to meet very specific purposes. In our view, it is contrary to the intent of the Social Security Act that another Act or Regulation would instruct that these payments be directed to repaying high cost credit. ***We recommend that the income calculation should exclude any Centrelink payments that are designed to meet a specific purpose***;
- we believe that the PIA should protect more than 80 per cent of the income of eligible borrowers. ***As we have argued in the past, we recommend that the PIA should protect at least 90 per cent of income.*** Protecting 90 per cent of income would bring the PIA into line with existing Centrelink processes for repaying money owed to financial institutions.[6]

Finally, there is no detail on how lenders must calculate whether social security payments make up at least 50% of a borrower's income for the purposes of 28S(2)(b). ***We recommend this be calculated by reference to bank statements from the previous 90 days, as we have suggested for the income calculation in subregulation 28S(3).***

<u>28XXD: Anti-avoidance measure to prevent 'loan splitting'</u>

We welcome the inclusion of draft regulation 28XXD, which prevents credit providers from avoiding cost caps in section 32A of the Credit Code through 'loan splitting'.

However, ***we recommend a minor amendment to 28XXD to ensure the regulation prevents the splitting of the loan over two related lenders.*** For example, an existing lender may create

[5] At subsection 117(1A).

[6] See joint submission from Consumer Action and a number of other agencies in response to Treasury's April 2012 discussion paper on proposed reforms relating to Small Amount Credit Contracts, pages 21-22. The joint submission can be accessed at: http://www.consumeraction.org.au/downloads/FINAL-jointsubmission-Treasurydiscussionpaper-EnhancementsbillreformsinreSACC-May2012.pdf.

a new, shell business purely for the purpose of splitting loans and so evading the cost cap. While we are not aware of this practice occurring at present, we do know of payday loan 'brokers' who charge considerable brokerage fees without appearing to provide a brokerage service at all.

The current text of 28XXD may already capture a loan split across two businesses, this could be made certain by amending paragraph 28XXD(2)(a) to read (new text in italics):

> The credit contract is arranged in conjunction with at least one other credit contract for the consumer, *whether the other credit contracts are provided by the same or a different credit provider*

79AB: Anti-avoidance provision to prevent fees being added for related goods or services
We welcome this provision.

We do not believe there are any situations where third party fees should be permitted to be charged outside of the cost caps in section 32A of the Credit Code. In our view, these charges will only ever be a method for avoiding the cost caps. If the third party goods or services are genuinely of interest to a borrower, the lender and the third party are free to promote them, but they should not be a requirement of entering the contract.

79AC: Anti-avoidance provision to prevent evasion of cost cap by varying fees
We approve of the intent of this regulation, but think it will be easily evaded in its current form. According to paragraph 79AC(c), a variation will only breach the regulation if the debtor is requested to increase the amount of at least 50% of the repayments and the lender makes request within one month of entering the contract. A lender could avoid the regulation by making the request 32 days after entering into the contract, or by increasing only 40% of payments and may have a similar effect.

We recommend that regulation 79AC be redrafted to be more flexible, perhaps by replacing '50 % of the repayments' with 'a significant proportion of the repayments' and 'within 1 month' with 'early in the contract'. The 50 per cent and one month figures could be given as an example in a note below the regulation.

79C: Defaults in direct debit repayments of small amount credit contracts
We have serious concerns about regulation 79C. The purpose of the regulation is to protect consumers from multiple direct debit dishonour fees by preventing lenders from repeatedly attempting to make debits from an account which has insufficient funds. In addition, Treasury's commentary document which accompanied the draft regulations suggests that the 79C will prompt lenders to inquire if a borrower in hardship. As currently drafted it provides neither of those protections.

Regulation 79C prevents a lender from

> seeking a repayment due under a small amount credit contract by relying on a direct debit request if:
>
> (a) the credit provider has twice sought to obtain the repayment using the direct debit request; and

(b) the credit provider has not:

(i) told the debtor that the direct debit requests have been unsuccessful; or
(ii) made reasonable attempts to contact the debtor.

This regulation does not prevent a credit provider from repeatedly attempting to draw direct debits from borrower's account, it merely requires the lender to 'make reasonable attempts to contact the debtor' after every second attempt. Nor does it require the credit provider to ask if the borrower is in hardship or refer them to the lender's hardship procedures. As drafted, a lender could attempt to debit the account twice, send the borrower an SMS informing them that the debit is unsuccessful (so satisfying 79C(1)(b)) attempt twice more to debit the account, resend the same SMS and continue that cycle nonstop until the debit was successful.

To offer any real protection, credit providers must be required to take genuine steps to avoid creating exacerbating a consumer's financial hardship. ***We recommend that regulation 79C(1)(b) be amended to require that:***

- ***the lender make reasonable attempts to contact the borrower and inform them of their hardship procedure; and***
- ***the lender is prevented from seeking a direct debit until either the defaulted payment is paid, or the date for next repayment arrives. If the lender does not wish to wait, they can start normal debt collection proceedings.***

Draft regulations regarding consumer leases

105C: Information to be provided in end of lease statement

Regulation 105C lists information which must be included on an end of lease statement. ***We recommend that paragraphs (e) and (f) (which require the lessor to state whether they are willing to negotiate the sale of the leased goods at the end of the lease term, and if so, the details for making the purchase) be deleted***. Including these paragraphs serves to legitimise poor industry practice—arranging consumer leases so that they appear to be sales by instalment.

Lessors commonly structure lease contracts to provide the lessee the right to purchase "similar goods" at the end of the contract period for a nominal amount, or to gift the goods to a family or household members. These terms appear to be drafted to ensure that the agreement is not deemed to be a sale by instalment pursuant to section 9 of the National Credit Code.

This conduct is in our view one of the most significant problems with consumer leases, because they are achieved through confusing and artificial arrangements which give the impression that a consumer has a right to own goods at the end of the lease term when in fact they have no such right. Not having such a right means that a number of protections that apply to credit contracts (such as disclosure of the cost of credit) are not required. It is our view that contract terms that provide for such arrangements may in fact be unfair contract terms within the meaning of the *Australian Securities and Investments Act 2001* (Cth). We think that regulations supporting the consumer lease provisions of the National Credit Code should not facilitate or require such terms, particularly as this may potentially bring them beyond the purview of unfair contract term prohibitions[7].

[7] Due to the operation of section 12BI of the *ASIC Act 2001* (Cth).

Regulation 105L: Consent to enter residential property to take possession of goods

We support the recommendation made by our colleagues at Consumer Credit Legal Centre NSW (CCLC) that the consent to enter residential property must be obtained prior to an agent attending the premises to take possession of the goods. We agree with CCLC that if an agent of the lessor attends the lessee's premises without such a consent, they should only be permitted to request that the person make contact with the lessor to consent to repossession at a later date.

Form 20: Default Notice – information about lessee's rights after default

We support the recommendation made by CCLC that certain words under the 'Right to Review' section of Form 20 should be deleted.

The relevant section says that if the lessor refuses a request to make a hardship variation requested by the lessee, the lessee can

> …ask [the lessor] to reconsider. If [the lessor] still refuse[s], or if we do not respond to your request within 21 days, you can go to [*insert name of relevant external dispute resolution scheme*] by [*insert contact details and method(s) for lodging complaints*]. You should apply as soon as we refuse your request or fail to respond.

This is inconsistent with existing regulation, which would allow a lessee to lodge a complaint with the external dispute resolution scheme after the first refusal, without having to request the lessor to reconsider.

Please contact David Leermakers on 03 9670 5088 or at david@consumeraction.org.au if you have any questions about this submission.

Yours sincerely
CONSUMER ACTION LAW CENTRE

Gerard Brody
Director, Policy and Campaigns

David Leermakers
Senior Policy Officer