CONSUMER INTERACTION

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Welcome to the August/September edition of **Consumer InterAction**.

Consumer Action's legal practice, policy department and financial counselling service share clear understanding of the financial hardship caused by payday loans. Consumer Action's staff have heard payday loan horror stories, listened to everyday Australians burdened by huge interest rates, and witnessed the regularity at which these cases come through our door.

But, with the Federal Government introducing payday lending regulations into Parliament, there is a renewed optimism that something is being done to stop the damage caused by these loans. That's why we've decided to dedicate this edition of Consumer InterAction to payday lending.

This edition looks at the problems with payday loans, what is being done about it, and highlights why the Government's proposed reforms need to pass unamended. We'll also turn out attention to busting some of the myths being spread by lenders. It seems some at least will say whatever it takes to avoid regulation.

You can support the campaign by promoting our campaign website, www.debttrap.org.au, throughout your network, and by getting your organisation to endorse the open letter to Minister Shorten at http://debttrap.org.au/take-action/an-open-letter-to-minister-shorten/.

IN THIS EDITION…

1. Payday loans – the cold, hard facts

What are payday loans?

Payday loans are high-cost short term loans which typically involve borrowers paying effective annual interest rates of between 400 and 1,000 per cent.

This sounds bad enough, especially since most of us think our credit card interest rate of around 20 per cent, is high. But, sadly, the more you look into these loans the worse the story gets.

Repayment is usually due in two or four weeks and is often secured through direct debit. To ensure they get their money ahead of the borrower's other financial priorities, lenders set up the direct debit to withdraw the money from their client's account on their payday or pension day.

And, if borrowers were short of cash for their last pay period and needed to borrow, repaying an expensive loan out of their current pay is going to leave them with an even bigger shortfall – this often leads to borrowers taking out another loan, and another - the beginning of a dangerous reliance on debt.

Who are taking out these loans?

Despite what the industry would have you believe, Consumer Action's research shows that low income earners represent the vast majority of payday lending clients. Only 45 percent are earning a full time wage and, of those who are employed, 73 per cent reported earning a below average income and 23 per cent reported an annual income of less than $20,000. These are the people who can least afford to be paying grossly inflated interest rates.

In the recently released *Caught Short*, a report into payday lending by RMIT, The University of Queensland, Good Shepherd and the NAB, 78 per cent of borrowers surveyed were receiving a Centrelink payment or pension.

What are they typically being spent on?

Our research shows that the majority of borrowers - 75% - are taking out loans to pay for day-to-day living expenses such as food, utilities and rent. So, clearly, most borrowers are already in financial hardship and can't afford such expensive credit.

When *Caught Short* asked borrowers why they first took out a loan 'the most commonly cited reasons were to meet regular, weekly-type needs and expenses.'

About the industry

The payday lending industry has grown rapidly since the first lender opened its doors in 1998 and is now believed to be worth around $800 million annually. As an indicator of the pace of the industry's growth, in the last financial year Cash Converters experienced a 58 per cent increase in their payday lending profits which totalled $24.4 million (*Cashies facing leaner paydays*, Australian Financial Review, 22 September 2011). Payday lending now represent Cash Converters' biggest income stream, bringing in far more money than its more traditional products.

Lenders typically conceal the cost charged on the principal loaned by characterising interest as a 'fee', which is itself rarely advertised. Online lenders generally avoid disclosing the cost of the loan on their home-page and most require the consumer to at least request a loan before disclosing the cost. Others do not disclose cost until the consumer has had direct contact with a sales representative.

What will the proposed changes do?

The proposed regulations would place a cap on the amount of interest and fees lenders can charge for loans under $2,000. Interest rates will be capped at 10 per cent upfront and 2 per cent per month in all states and territories.

The regulations would also restrict lender from rolling one loan over into another, helping to lessen the risk of borrowers falling into a debt trap. And lenders would be required to publish links to the Government's MoneySmart website on their own websites.

The draft legislation to regulate payday loans was introduced to parliament on 20 September. It has been referred to not one but two committees – the Senate Economics Committee Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011 inquiry, and the Parliamentary Joint Committee on Corporations and Financial Services inquiry into that same bill.

Submissions to each are due 21st and 14th of October respectively.

2. Busting common myths

Unhappy that the proposed cap on interest rates will affect their huge profit margins, payday lenders are running a scare campaign and spreading a range of myths. So we thought we'd clear up a few things:

Myth #1: Payday lenders won't be able to make a profit if an interest rate cap is implemented.

Payday lenders already operate in Queensland, New South Wales and the ACT under harsher restrictions than what the Government is proposing. This suggests that they are either operating effectively within the cap or avoiding the law.

Given Cash Converters recently announced that their "New South Wales payday lending business is profitable and is expected to remain profitable" under a 48 per cent cap (Cash Converters announcement and press release, *Response to article in the Australian Financial Review*, 1 June 2011), the idea that payday lenders won't be able make a dollar under the proposed regulations seems a little far-fetched.

Myth #2: Payday lenders offers responsible credit and don't loan to repeat borrowers

We really wish this one was true—but it isn't. Our legal team has helped clients who have had numerous payday loans, including one alarming case in which our client took out 64 loans over a three year period. And of the payday lending clients surveyed for the RMIT's *Caught Short* report, over half "had taken out more than ten loans, with many saying they had received over 50 loans' (*Caught Short*, p. 11).

We also know that payday lenders aim their marketing at existing clients—even sending them birthday cards in some instances.

Myth #3: If payday lending disappears people will turn to the black market for credit

We'll keep this one quick: there's not a shred of credible evidence here, or anywhere else in the world, to support this claim. Even though a more onerous cap than the one the Government is proposing is already in place in Queensland, New South Wales and the ACT. And even though a cap is in place in parts of America and Canada, as well as in: France, Germany, Italy, the Netherlands, Poland, Portugal, Slovakia, Spain, Greece, Ireland, Malta, Belgium and Estonia.

Surely if caps led to a surge in business for black market lenders there would some recorded evidence of it. Furthermore it fails the logic test - are people currently accessing loans from a high street lender really about to turn to a knee-breaker if the lender they know disappears?

Myth #4: Without payday loans low income earners will be left in the cold

Any responsible financial counsellor will tell you that there are other, more financially prudent options available. Community organisations like the Brotherhood of St. Laurence offer low or no interest loans to help people suffering financial hardship, welfare recipients may be eligible for a Centrelink advance, and all banks and utility providers are required to offer hardship provisions to help people struggling to pay their mortgage or utility bills - http://debttrap.org.au/debt-help/alternatives-to-high-cost-payday-loans/.

If you're in financial trouble you can always speak to a free, independent and confidential financial counsellor by calling MoneyHelp on 1800 149 689 if you're in Victoria, or the financial counselling hotline on 1800 007 007 if you reside in any other state.

3. Policy and Campaigns

Letter to the Hon. Bill Shorten, Minister for Financial Services & Superannuation, Assistant Treasurer

Consumer Action, along with a range of consumer and financial counselling organisations Australia wide, has been pushing for payday lending reform for many years. So when the Government proposed regulation we believe will effectively address the problem, we were more than happy to lend our support.

We published an open letter supporting the proposed regulations which was co-signed by a number of other consumer, financial counselling and emergency relief organisations. Following the letters publication, its content was endorsed by more organisations and an updated version of the letter was sent to all Federal Members of Parliament. The letter can be viewed at http://debttrap.org.au/take-action/an-open-letter-to-minister-shorten/, and its content has now been endorsed by:

Bribie Island and District Neighbourhood House	CHOICE
Bribie Island and District Neighbourhood House	
Brotherhood of St Laurence	Homelessness Australia

Caloundra Community Centre	Caxton Legal Centre
Care Financial Counselling and the Consumer	Financial Counselling Australia
Consumer Credit Legal Centre (NSW) Inc	Moneycare, The Salvation Army
Financial and Consumer Rights Council Inc	Good Shepherd Youth and Family Service
Financial Counsellors' Association of Queensland	UnitingCare Wesley Adelaide
Flemington and Kensington Community Legal Centre Inc.	
Footscray and Wyndham Community Legal Centre	Kildonan UnitingCare
Gambling Help Caboolture and Redcliff Peninsular	
George Street Neighbourhood Centre Association	
Loddon Campaspe Community Legal Centre	EACH Social & Community Health
PILCH Homeless Persons' Legal Clinic	Anglicare Victoria
St Vincent de Paul Society, National Council of Australia	Law Centre of the ACT
Townsville Community Legal Service Inc.	Australian Council of Social Service
Victorian Local Governance Association	UnitingCare Moreland Hall

Debttrap.org.au

A coalition of consumer and financial counselling organisations has also launched a new website to ensure the hard truths are told about payday lending: www.debttrap.org.au. The new website delivers the confronting facts about payday loans, busts myths currently being spread by payday lenders, and outlines safer credit options available to low income earners.

The website, sponsored by the Consumer Action Law Centre, Financial Counselling Australia and the Consumer Credit Legal Centre, gives consumers and financial counselling organisations a much needed voice in the debate, as well as a chance to set the record straight.

Financial Counsellors march on Cash Converters

In an unprecedented move for the financial counselling sector, the Financial and Consumer Rights Council's (FCRC) interrupted its annual conference to protest against the payday lending industry.

Around fifty of the financial counsellors attending the conference put proceedings on hold to march on Cash Converters' Geelong branch and deliver their message straight to the lenders themselves—interest rates must be capped!

Consumer Action and our MoneyHelp financial counselling service were well represented and made their voices heard. Pictures from the protest can be viewed at http://debttrap.org.au/take-action/campaign-images/.

4. Case studies

Earlier this year Consumer Action released *Mission Incomplete: a snapshot of consumer experiences of short-term loans post the national consumer credit reforms*. The report provides a snapshot of consumer experience of high-cost short-term loans following the introduction of Phase 1 of the Commonwealth credit reforms, and in particular responsible lending laws. The case studies suggest that responsible lending laws are ineffective in addressing the particular dynamics that are involved in this type of credit provision. We've decided to reprint a few of the case studies sourced from financial counselling colleagues here (these aren't the borrowers real names):

Jane's story

Jane was a 26 years old, single mother with five kids under 6 and was working full time. As it was taking her two hours to get to work on the bus, she wanted to buy a car.

She borrowed $660 for a car deposit from a payday lender in March 2011 and paid back $980 two weeks later. Then Jane realised she had no money for the rest of the fortnight—then and there the lender offered her another loan, this time for $650.

Jane is a repeat borrower who also has loans with three different lenders. She described them as "like an addiction".

Mike's story

Mike had originally taken out a loan for $300, which was to be repaid from his Centrelink benefits over two fortnights. The annualised interest rate was 300%.

He found he could not survive and have the amount demanded taken out—he approached the payday lender and was told that they would roll the loan over into another one.

Mike allowed this to happen and the original loan of $300 was to cost him $760.95 by the time he had made the final payment on the new loan. This was not feasible and I (the financial counsellor) approached the payday lender (by letter) and asked that the interest be waived and that the total cost of the loan would be reduced by payments of $30 per fortnight, commencing on the Mike's next Centrelink benefit day. I also requested that the Mike receive no further loans from the lender, given that the lender advised me that the Mike had had fourteen (14) loans between May 2010 and December 2010.

I was advised by the Head Office of the lender that she would need to have the Mike submit a Statutory Declaration to the effect that he was not to be given any further loans. He has now been approached with this request.

A total of fourteen (14) loans were rolled over in the seven month period, and he borrowed on as often as a fortnightly basis.

Was he in a debt spiral? Absolutely! He was being set up to fail by the sheer size of the amount of his Centrelink benefit that he was expected to pay each fortnight. He presented with overdue accounts for gas, phone, rent and had also taken the Advance Payment from Centrelink.

Kelly's story

Kelly didn't have a great credit rating, her son was having an 18th birthday party and the family was coming to visit—so the pressure was on to entertain.

She was given $600 from a payday lender, as half of her assessable income. Virtually all her next fortnight's pay went to paying it off. From September to December 2010 she paid a minimum of $350 in fees—in total she paid $950 in fees for the $600 loan over 6-7 fortnights. She'd go in to pay off the loan and sign new contract at same time.

Kelly stopped going in December and owes them $1000. She has now seen a financial counsellor and is doing a payment plan of $200 a fortnight, but the lender is demanding $267 or threatening to go to collections.

5. Stories from financial counsellors

We thought we'd ask some financial counselors, the people who see the effects of payday loans first hand, for their thoughts:

"The sad thing is that if people would call a financial counsellor before going to the payday lenders instead of after, the financial counsellor would be able to provide them with information about their rights and the other option available to them, which include applying for hardship, Centrelink advances, and NILS loans - unfortunately many people aren't aware of these options."

-Dianne Dejanovic, Financial Counsellor, MoneyHelp

"Experience has shown that Payday Loans not only impact on the borrower and their finances. Many of our clients have chronic health conditions such as mental illness and drug and gambling addictions which are exacerbated by the stress and worry that are a byproduct of these loans. Clients have often used loved one's assets as security for these loans and the thought of losing their child's X Box or partner's or parent's jewellery can be traumatic.

Clients who are caught in this spiral experience further low self esteem and a pessimistic outlook on life which often manifests in relationship breakdowns and relapsing back into old behaviours and crime. Once caught in this cycle of unaffordable debt repayment and the accompanying degradation, clients face a downward slide which is difficult to extricate themselves from."

-Garry Rothman, Senior Financial Counsellor, UnitingCare Moreland Hall

"In my job with Financial Counselling Australia I talk to financial counsellors all the time about issues they are seeing in their casework. I often hear about the problems payday lenders are causing. Financial counsellors are passionate about getting effective regulation to stop people being trapped in a cycle of debt.

We had hoped that the Federal Government would have extended the 48% interest cap already in place in Queensland, New South Wales and the ACT, to the rest of Australia. While there has been some avoidance of this cap, we know a cap works if it is backed up by adequate enforcement.

The proposed new laws will go a long way to ameliorating some of the more insidious practices involved in payday lending, including exorbitant interest rates and loan roll overs. That's why we are supporting the Government's approach."

- **Fiona Guthrie, Financial Counselling Australia**

"As a Financial counsellor I have seen the fall-out from short term high interest loans. They may get someone over a 'bump' in the personal cash flow one fortnight, but what happens after the bump when there is even less available income because of the direct debit? For years I have been disappointed that government has not taken steps to prevent situations where someone going through a time of vulnerability can worsen their plight in this manner.

No one in their right mind would willing and knowingly pay the sort of changes these loans charge. It is not unusual to have people come into our services, penniless, with bills to pay and only pocket money left as future income because of these ‘offers’ from pay day loan providers. And the more pay day lenders involved at any one time the more complex the situation becomes. Reform in this area is needed urgently.”

- **Carolyn Joy, Senior Practitioner, UnitingCare Community**

6. Payday lending in the media

Short-term loan, long-term inequity

The Age, 26 September 2011

An editorial from The Age highlighting the need for payday lending reform and calling for the Government to provide other credit options for low income earners.

Bankrupt mum backs protections for borrowers

ABC News, 21 September 2011, Sheryle Bagwell

A follow-up story on the ABC's news website focusing on the issues raised in Sheryle Bagwell's radio story earlier in the morning.

Proposed cap on payday lenders

ABC Radio National Breakfast, 21 September 2011, Sheryle Bagwell

A report on the proposed changes to the payday lending industry with comments from Consumer Action's Catriona Lowe.

Counsellors back laws on lending

Wyndham Weekly, 14 September 2011, Dan O’Sullivan

This story quotes Shungu Patsika from Anglicare Werribee who voices her support for reforms to the payday lending industry.

A bridging loan can sink you

Sydney Morning Herald, 14 September 2011, Barbara Drury

Consumer Action's co-CEO and a former client feature in this article about the pitfalls of payday loan.

Payday loans protest

Geelong Advertiser, 10 September 2011, Mandy Squires

Mandy Squires reports on a protest against payday lending in which Consumer Action's Gary Rothman is quoted.

Debt Collector cheers payday lender reform

Sydney Morning Herald, 8 September 2011, Alison Bell

Roger Mendelson from Prushka Fast Debt Recovery Pty Ltd backs payday lending reforms.

Cash Converters hot by micro-lending legislation

Lateline Business, 31 August 2011, Ticky Fullerton

Minister for Finance & Superannuation, The Hon. Bill Shorten, discusses his proposed payday lending reforms.

No interest loans

Today Tonight, 31 August 2011, Jackie Quist

Consumer Action's Carolyn Bond features in this story about low and no cost loans which are providing many with an cheaper alternative to payday loans.

Screws turn on loan sharks

Sydney Morning Herald, 28 August 2011, Jessica Wright

Consumer Action's Carolyn Bond talks about the dangers of pay-day loans leading to a debt cycle that borrowers are unlikely to escape from.

How a little extra cash became a debt trap

Wyndham Weekly, 28 August 2011, Jessica Wright

This case study leaves readers with no doubt about the dangers of payday loans.

Fee caps proposed for pay-day lenders

The Australian Financial Review, 26 August 2011, Matthew Drummond

Consumer Action's Carolyn Bond is featured in this article about proposed regulations for pay day lenders.

New law to cap interest on money lending a first for the nation

Herald Sun, 26 August 2011, Karina Barrymore

Consumer Action's co-CEO Catriona Lowe is quotes in this article about the Federal Government's proposed regulations on payday lending.

New restrictions for payday lenders

Perth Now, 25 August 2011, Nick Evans

Consumer Action's co-CEO Catriona Lowe is quotes in this article about the Federal Government's proposed regulations on payday lending.