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Dear Michael

Abacus Draft Code of Practice

Consumer Action Law Centre (**Consumer Action**) is pleased to make a submission in relation to the proposed Abacus Australian Mutuals (**Abacus**) Draft Code of Practice (**Draft Code**). As a general comment, we record our support for both the tenor and quality of the Draft Code. In our view, the Draft Code represents a significantly improvement in the level of protection for consumers of credit unions and mutual building societies. Nevertheless, there are a few areas where we consider the Draft Code could go further and we make some more detailed comments on how the Draft Code could be improved 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 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.

General comments

As outlined above, Consumer Action is, overall, very pleased with the Draft Code. Consumer Action commends Abacus on the content of the Draft Code, and is particularly pleased with the following aspects:

- the handling of debt collection and legal action;

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- the treatment of customers in financial difficulty;
- the inclusion of a responsible lending requirement;[1]
- where finance brokers are used, requiring those brokers to be members of ASIC approved external dispute resolution (**EDR**) schemes;
- the protection of co-borrowers and guarantors generally;
- the coverage of the 10 key promises; and
- the common commencement date for compliance with the Draft Code.

Consumer Action also considers there are aspects of the Draft Code that require improvement. In particular, we are concerned regarding the enforceability of the Draft Code and that the provisions relating to penalty fees, whilst a step in the right direction, may be practically difficult to enforce.

Contractual force of the draft code

Consumer Action does not support the choice not to give the Draft Code contractual force. Abacus notes in its public consultation that 'making the commitments of the code contract terms…would be at odds with the non-technical and aspirational style of drafting of the Code.' Consumer Action does not agree with this view.

We note it is commonplace and standard for many contracts to have one or more recitals clauses. Recitals clauses are aspirational in nature. The Australian Banking Association's *Code of Banking Practice* contains similarly aspirational content, but has the effect of being a term of the consumer-banker contract.[2]

Consumer Action also takes the view that the content of the Draft Code is not, and should not be, purely aspirational. One of the strengths of the Draft Code, from our perspective, is the way it gives specific procedural information about how particular matters must be dealt with.[3] While Consumer Action agrees that the drafting style of the Draft Code is accessible and non-technical, many of its sections are often specific, and set out in detail what must be done. Clearly, such detailed sections (as well as the aspirational sections) are capable of being incorporated as contractual terms.

Although Abacus notes that failure to comply with the Draft Code 'would risk breaching legal prohibitions against misleading and deceptive conduct', this is not sufficient to protect consumers. This approach would in effect require two stages of proof – first, the nature of the representation constituted by the signing of the code and, secondly, that such representation was misleading and deceptive in all the circumstances. Direct incorporation of the Draft Code into the contractual terms removes one of these hurdles. It is not reasonable to say that general statutory misleading and deceptive conduct provisions are sufficient to enforce an industry code.

[1] We note that the Draft Code goes further than the *Banking Code of Practice*, that does not have such substantial responsible lending requirements (see section 25 of the Banking Code of Practice).
[2] Section 10.3 of the *Code of Banking Practice*, Australian Bankers' Association, amended May 2004.
[3] Eg. Section 9.5 of the Draft code.

We note that Abacus states that the Draft Code will be applied by the EDR schemes to which Abacus members belong. While we obviously support this, it is our view that a Code that operates as a contract between financial institution and its members or customers (as with the *Code of Banking Practice*) enables EDR schemes to more effectively ensure that the protections are being complied with. While EDR schemes do resolve disputes with regard to the law, good industry practice (such as industry codes of practice) and what is fair and reasonable in all the circumstances, it is clear that obligations that have the force of law are more likely to result in outcomes that are in consumers' interest. We encourage Abacus to reconsider requiring subscribing members accepting contractual rights and obligations in respect of the Draft Code's commitments.

We also believe that a code that operates as a contract provides incentives for subscribing institutions to comply with its requirements. For example, a consumer who was unhappy with breach of the Code could seek a remedy in the relevant state or territory tribunal or court[4] against the subscribing member. This threat of enforcement would encourage industry subscribers to comply. This protection could not be delivered via a 'Code Compliance Committee' alone whose function, according to the Appendix in the Draft Code, is to monitor and report on compliance with the Draft Code, and to impose undefined 'sanctions' for breach of the Draft Code. It is unrealistic to think that the Code Compliance Committee could impose sanctions that would be equal to consumers' private rights exercised in the relevant state or territory tribunal. Rather, it is essential for consumers to retain private rights to enforce the terms of the code.

Consumer Action also notes a choice not to make the draft code contractual evidences an unwillingness to make enforceable the implementation of its terms. Such an unwillingness undermines the otherwise significant credibility of the code from our perspective.

Fees and charges

Consumer Action welcomes the intention of provisions of the Draft Code requiring exception fees to be 'reasonable, having regard to our costs' and also 'clearly disclosed' and 'fairly applied'. Requirements of reasonableness and fairness in relation to the levying of fees are an improvement on current general banking practice.

That said, Consumer Action believes that the protections relating to fees in the Draft Code are not compliant with the obligations relating to penalties provided by the common law. We note that the law states that liquidated damages clauses must be a genuine pre-estimate of the costs of breach of contract.[5] So as to ensure subscribing members comply with the law, Consumer Action would like to see an additional dot-point in section 4.5 of the Draft Code requiring fees to be a 'genuine pre-estimate of cost'. Alternatively, given Abacus' current proposal, Consumer Action believes that a requirement that exception fees relate to a 'reasonable estimate of costs' would more effectively ensure subscribing members are complying with the law and are providing the highest level of consumer protection to their customers.

[4] In Victoria this would be the Victorian Civil and Administrative Tribunal.
[5] *Ringrow Pty Ltd v BP Australia Pty Ltd* [2005] HCA 71.

We also consider that in the absence of a link to underlying cost, the concept of 'reasonableness' in this context is nebulous and likely to create practical difficulties in compliance and, therefore, likely to lead to a range of interpretations and applications.

Detailed analysis of the Draft Code

Consumer Action would also like to identify a number of specific areas in which it thinks the Draft Code could be improved.

Fairness (Key Promises 2 and 8)

We welcome Key Promise 2 the commitment to fairness that it contains. As a minor point, we submit that a further reference to fairness would be appropriate in Key Promise 8. Recognition that subscribing members will act lawfully, fairly and consistently with good industry practice aligns with the well recognised and understood terminology of EDR schemes.

Responsible lending practices (Section 5)

We strongly support clause 5 of the Draft Code relating to responsible lending, including the commitment that lenders will base lending decisions on, *inter alia*, a consumer's capacity to repay. We note that clause 5.2 states that subscribing members 'may' undertake their own independent credit checks. It is our view that a prudent lender *should* undertake such checks.

Subsidiary cards (Section 7)

Section 7.2 of the Draft Code states that customers will not be liable as long as they 'do not act fraudulently or otherwise contribute to those losses.' In our view, the term *otherwise contribute to those losses* is ambiguous and therefore should be removed. If consumers cancel, destroy and return a subsidiary card, it is difficult to see how it would be fair to hold them liable (except in the case of fraud). However, if there are specific circumstances in which it would be fair to hold consumers liable, these should be set out in clear terms.

Protection of co-borrower where co-borrower does not receive a benefit (Section 8)

In section 8.2 of the Draft Code subscribing members are required not to accept a person as a co-borrower if it appears that person 'will not receive a direct benefit from the loan…'. The word *tangible* should be added so the term reads, 'will not receive a tangible direct benefit from the loan…'. This change would prevent acceptance of a co-borrower who receives a direct benefit, but one that is small and insignificant compared with the value of the loan.

Consumer Action's legal practice section often deals with cases involving co-borrowers. Often, a family member receives much of the benefit of a loan, in circumstances that should have put the lender on notice of the inappropriateness of the loan.

Continuing guarantees (Section 9)

We are generally pleased with the level of detail of the commitments in the Draft Code in relation to loan guarantors. However, we believe the proposed regime needs to include a further commitment in the situation where an existing guarantee is to be extended. In these circumstances, a status report updating the borrower's financial position should be provided by the lender to the guarantor before the guarantee is extended. We believe this important to ensure the guarantor is put on notice of any deterioration in the borrower's financial position. The provision of such information is in line with the 'full disclosure' philosophy of section 9 generally. It is also arguably a prudent course of action from the lender's perspective as failure to disclose a deteriorating borrower position to the guarantor when a guarantee is being extended may give the guarantor grounds for defending a claim in the event of the borrower's defaulting.

Waiting period before signing guarantee documents (Section 9)

In section 9.9 of the Draft Code an assurance is made that customers will have 24 hours to consider guarantee documents before signing, but that 'at our discretion, we may agree to a shorter period if you (the guarantor) request this.' Guidelines should be prepared to guide the lenders exercise of discretion to reduce the 24 hour waiting period in these circumstances. Such guidelines should state that the lender can only reduce the waiting period where it is reasonable in the circumstances to do so. This would protect guarantors (and lenders) from requests for a shortening of the waiting period where pressure from another person, such as the loan recipient, is applied.

Account statements and balances (Section 13)

Consumer Action submits that it is important for customers to be given quarterly transaction account statements at no cost, and that the statements be provided in written form if the customer wants this. Having transaction account statements sent 6 monthly, as suggested in the Draft Code, does not, in our opinion, provide consumers with information sufficiently frequently. Two statements a year is not sufficient for consumers to manage their financial circumstances – particularly for those consumers (eg. elderly, not computer literate) who do not have the capacity to check their accounts electronically.

Notifying changes (Section 14)

Section 14.4 of the Draft Code sets out methods for notifying customers of changes to accounts. Consumer Action submits that the following words should be inserted at the end of section 14.4: 'In particular, in relation to any change that will significantly affect you, we will notify you by regular mail.'

Consumer Action does not believe the method of notification should be entirely within the discretion of the subscribing member, but that significant changes that effect consumers should be communicated to those consumers by the most reliable, practical method (ie. by regular mail). Notification could of course be provided electronically if a consumer elected this. It would not be fair to consumers if, for instance, a new fee or interest rate increase

was to be introduced, and information about this appeared on the subscriber's website or in newspaper advertisements but was not mailed to the consumer.

Account security breaches (Section 17)

Consumer Action believes that if a consumer alleges that there has been a security breach, and the subscribing member thereafter makes a determination about loss with which the consumer is not satisfied, then the subscribing member should advise the consumer of his/her rights to have the decision reviewed (including a right to review by the relevant industry-based EDR scheme).

Therefore, in section 17.5 an extra dot-point should be added reading: 'Advise you of your rights to have our determination reviewed.'

Privacy and confidentiality (Section 21)

In section 21.2, one dot-point allows disclosure of private information where 'there is a duty to the public to disclose the information'. Consumer Action cannot see what this dot-point refers to. The preceding dot-point requires disclosure where required by law, and we cannot see the meaning of a nebulous 'public duty' beyond legal compliance. Thus the dot-point should be removed or, if it refers to a matter of significance, be made clear.

We also believe that the Draft Code should specifically limit the use of bundled consents that may be used to disclose personal information. The use of bundled consents is neither good business practice nor a proper way of protecting privacy and is contrary to the spirit of privacy legislation. In particular, consent for the collection, use and disclosure of a consumer's personal that is necessary for the provision of that service should be sought separately from consent for additional uses of the information such as marketing.

Debt collection (Section 23)

Overall, Consumer Action strongly commends Abacus on section 23 of the Draft Code. However, we submit the following sentence be added at the of section 23.1: 'We will only sell our debts to another party if that party has undertaken to comply with the Debt collection guidelines and is a subscribing member of an industry-based EDR scheme.'

It is important that the rights of consumers to the free and fair dispute resolution services offered by the industry-based EDR schemes is not circumvented by debts being sold to debt-collectors who are not members of an industry-based EDR scheme. Ensuring that parties that buy debts are members of an industry-based EDR scheme will prevent the sale of debts to unscrupulous debt collectors.

Requirement of consumer to cooperate (Section 25)

Section 25.3 of the draft code requires consumers to cooperate with subscribing members, in the following terms: 'We may not be able to deal with your complaint if you do not continue to cooperate with us until the matter is resolved.' Whilst we understand the intent, we submit that this choice of words is capable of undesirable interpretations. It may be interpreted as

requiring the consumer to cooperate with *any* requests or stipulations of the subscribing member. It may give the impression that the subscribing member has complete discretion to set conditions with which a consumer must cooperate.

We submit that the section 25.3 be amended to clarify the situation. The inclusion of examples (eg. respond to correspondence, provide necessary information) of the required cooperation may achieve greater clarity.

Complaints handling process (Section 26)

Consumer Action believes that the Draft Code would be benefit from a clear definition of 'complaint'. The Australian Standard on Complaints Handling (AS ISO 10002) defines complaint as 'an expression of dissatisfaction made to an organisation, related to its products, or the complaints-handling process itself, where a response or resolution is explicitly or implicitly expected'. It is our view that a clear definition of complaint will assist subscribing members to apply their complaint handling procedures in a uniform and rigorous way.

We note that in our experience, correct identification of complaints and appropriate direction within an organisation continues to be a challenge for internal dispute resolution (**IDR**) processes.

Consumer Action also recommends that the complaints handling process should ensure consumers are kept informed about the progress of their complaint. Consumer detriment often arises due to consumers not being kept informed about the progress of their complaint, thereby encouraging them to make further complaints and drain industry resources. Often, as much as a satisfactory outcome, consumers desire a satisfactory and clear process

Identification of common complaints (Section 26)

Section 26.1 of the Draft Code lists 'features' of subscribing members' complaints handling process in dot-point form. We recommend the following extra dot-point be added as the first dot-point in this section: 'We will take active measures to identify and address common or systemic complaints.'

Requiring subscribing members to identify systematic problems is in the interests of consumers and business. One of the more cost-effective ways of increasing customer satisfaction is to identify areas in which repeated customer complaints are made, identify the problem causing this, and solve the problem. The identification of common complaints assists consumers (many of whom are affected if the complaint is made repeatedly). Also, the identification of common complaints is in the interests of subscribing members. Consumer feedback, in the form of complaints, is a valuable method of identifying areas for improvement. Knowledge of common consumer complaints is a form of market-research that businesses can and should use to improve their competitiveness in the market.

Providing contact details of person handling complaint (Section 26)

In section 26.1 of the Draft Code, a dot-point requires that the contact details of the complaint taker be given to the complainer. We recommend the sentence be amended so the words in italics are added to the sentence as follows: 'We will give you the name and contact details *(including work phone number and work email address)* of a person in our organisation nominated as responsible for dealing with your complaint.'

The phrase 'contact details' is ambiguous, and inserting the extra words would resolve this ambiguity.

The key objective is to provide a contact person for the consumer. This contact person must be contactable by the consumer – providing the work phone number and email of this person to the consumer is a reasonable way of ensuring that this person is contactable.

Time allowed for internal dispute resolution (Section 26)

Consumer Action does not take the view that it is reasonable for subscribing members to be given 45 days to resolve a dispute internally before it is subject to industry-based EDR.

Currently, the terms of reference of the Credit Union Dispute Resolution Centre[6] and the Financial Co-operative Dispute Resolution Scheme[7] give subscribing members 45 days to attempt to resolve disputes internally. In our view, this time period is too long. While many industry-based EDR schemes provide members with 45 days to resolve dispute internally. Consumer Action believes that there needs to be gradual change to shorten this period to 28 days.

Consumer Action is aware, however, that any change from the 45 day period could not be made unless the terms of reference of the Credit Union Dispute Resolution Centre and the Financial Co-operative Dispute Resolution Scheme are also amended. Consumer Action recommends that such amendments be considered when the terms of reference of those schemes are reviewed.

Distributed products and services

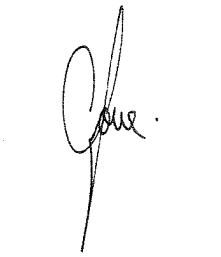
Consumer Action believes that the Draft Code could go further in regulating third party or distributed products. We accept that, if all the Draft Code subscriber does is to introduce or distribute a product on behalf of another institution, the Code should generally only apply to activities associated with the product's introduction or distribution. We note that Key Promise 5 involves a commitment to 'issue and/or distribute useful, high quality products and services…'. We submit the Draft Code should also include a commitment by subscribing institutions to monitor and periodically review the products they distribute. Code subscribers should also commit to only distributing products where the product issuer belongs to an ASIC-approved EDR scheme covering the product.

[6] Credit Union Dispute Resolution Centre Limited, *Terms of Reference*, March 2003, 2.1.
[7] Financial Co-operative Dispute Resolution Scheme, *Guidelines to the FCDRS Terms of Reference*, December 2005, 3.1.

Code compliance (Appendix)

Consumer Action welcomes the proposed Code Compliance Committee. It is our view that the Banking Code Compliance Committee has contributed positively to ensuring that banks meet the standards of practice set out in the *Code of Banking Practice.* An important role of such a committee is its public reporting functions, which should include annual reports, determinations, and regular bulletins. We also welcome the ability of the Committee to impose sanctions should a subscribing member breach the Draft Code. It is our view that the list of sanctions in the Appendix should include requiring an apology as well as provision for making suggestions as to remedial action as appropriate.

Should you have any questions about this submission, please contact myself or Gerard Brody on 03 9670 5088.



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