Unfair credit contracts – advocating on behalf of consumers

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Who is Consumer Action?

- Campaign focused casework and policy organisation
- 18 staff
- Assist 1000s of Victorian consumers each year

What are unfair credit contracts?

- There is no one meaning of unfair credit contracts, and they can come in a variety of forms.
- However, I will cover the following, which are common current issues seen by Consumer Action’s legal casework practice:
  - Mortgage refinancing; and
  - Fringe lending.

Other types of unfair credit contracts.

- Other ways in which credit providers evade consumer credit laws, include:
  - business purpose declarations (commonly obtained without consumer’s understanding/knowledge)
  - high credit charges in cost of loan (*eg*. Motor Finance Wizard);
  - consumer leases (whereby, by structuring what are essentially loans as leases, key provisions are avoided;
  - promissory notes (simple way in which fringe lenders try to avoid UCCC, although we think wrongly and could be challenged);
  - rent-to-buy agreements (often computers and cars).

Unfair mortgage refinancing

- Commonly involves consumers who are struggling with their current mortgage or seeking extra cash.
- They are visited by a mortgage broker or other non-bank lender, to ‘refinance’.
- Consumer often demonstrate varying levels of understanding about the loans they are obtaining.

Unfair mortgage refinancing (2)

- Common types of products:
  - Line of credit – an agreement by a lender to extend credit up to a specified amount for a specified time.
  - Low-doc loan – a mortgage that requires only minimal verification of income and assets. Designed for people who have intermittent income (perhaps due to self-employment).
  - Interest only facilities – borrower pays only the interest that accrues on the loan balance each month. Because each payment goes toward interest, the outstanding balance of the loan does not decline with each payment. The borrower will be expected to pay out or refinance loan at the end of the term.

Unfair mortgage refinancing (3)

- Often, the broker or credit provider provides consumer with higher amount of credit than what was requested.
- Often results in ‘equity skimming’:
  - Brokers obtain upfront and/or ongoing fees;
  - Lender obtains priority interest in property;
  - Consumer loses what equity they did have in their home.

Unfair mortgage refinancing – case study

- Mr and Mrs T (mid-50s couple) own home in regional Victoria, worth around $150k, with around $40k owing to mainstream bank.
- Mr T diagnosed with cancer (both are pensioners).
- Want extra funds to do some renovations on home and install air-con. Sought around $20k.
- Contacted by mortgage broker, who arranged low-doc loan with non-bank lender for around $140k. Paid out current mortgage, and obtained interest-only line of credit of almost $100k.
- Over one year, client withdrew around $60k for renovations and other expenses, including gambling.
- Unable to make repayments, credit provider began repossession proceedings.

How can we assist Mr and Mrs T?

- Two issues:
  - Should loan have been advanced?
  - What should credit provider do when consumer evidencing financial hardship?

How can we assist Mr and Mrs T? (2)

Should loan have been advanced?

- General consumer protection laws – unconscionable conduct.
- Issues
  - Unconscionable conduct is a high test – must have taken advantage of client's disadvantage (cf. statutory unconscionability).
  - Often, the credit provider 'hides' behind the broker's conduct and states it wasn't aware of misconduct. Common law deems broker to be agent of consumer, not lender (even where broker is remunerated by lender).

How can we assist Mr and Mrs T? (3)

Should loan have been advanced?

- Is there an obligation to assess capacity to pay?
- Answer is that it depends:
  - Section 70(2)(l) of the *UCCC* – reopening unjust transactions
  - Clause 25.1 of Banking Code of Practice (only applies to banking signatories)
  - Mortgage & Finance Association of Australia Code of Practice (only applies to members of MFAA)

How can we assist Mr and Mrs T? (4)

Should loan have been advanced?

- Has there been misleading conduct?
  - For example, did the broker/credit provider make representations that the consumer could make significant savings, or cut years off their mortgage, by leaving salary in a line of credit (often using a no-interest credit card for expenses).
  - Is this why the consumer entered into the loan?
  - More often that not, these mortgage minimisation schemes don’t work. The savings that can be made from leaving salary in a mortgage are usually insignificant, and usually much less than costs involved with the new loan.

How can we assist Mr and Mrs T? (5)

Should loan have been advanced?

- Has there been misleading conduct?
  - ASIC recently obtained Federal Court orders against Sample & Partners, a firm that specialised in 'mortgage minimisation' – found that S&P engaged in misleading conduct, and ordered that S&P set up a process by which consumers can claim compensation for any losses suffered.
  - Consumer Action is preparing a kit to assist consumers (and workers) who might have been misled by such mortgage minimisation schemes.

How can we assist Mr and Mrs T? (6)

Financial hardship

- What are the credit providers obligations when a consumer is experiencing hardship?
  - Section 66, *UCCC* – hardship variations: A debtor who is unable reasonably, because of illness, unemployment or other reasonable cause, to meet the debtor's obligations under a credit contract and who reasonably expects to be able to discharge the debtor's obligations if the terms of the contract were changed.
  - How can contract be changed? Extending period of contract, or postponing payments. Note interest rate still applied. Can still be a good option for many consumers.

How can we assist Mr and Mrs T? (7)

Making a complaint

- Consider all the possible jurisdictions, including the EDR-schemes.
- Banking Ombudsman – many non-banks are now members (check website).
- Credit Ombudsman – many credit providers and brokers are members (check website)
    - nb. Difficulty in showing that the credit provider knew or ought to have known of the broker’s conduct.
- Make complaint to Consumer Affairs department or issue proceedings in relevant court/tribunal.

What is Consumer Action doing to address systemic problems in mortgage refinancing?

- Our campaign for responsible lending is seeking:
  - National regulation of finance brokering;
  - Requirement that all brokers and credit providers be members of ASIC-approved EDR scheme;
  - Concrete up-front obligation on lenders to ensure a consumer has the capacity to repay a loan without substantial hardship before extending credit;
  - Provide that intermediaries are the agents of the lender where they are paid by the lender;
  - Empowerment of regulators to enforce consumer protections.

Fringe or pay-day lending

- Consumer Action has seen an increased level of complaints relating to fringe lenders over the past year.
- There are a variety of operators:
  - Cash Converters, Amazing Loans, Money3, Cash Loan Money Centre, City Finance, etc.
- Fringe lending is characterised by:
  - Short terms loans (from a few weeks to 2-3 years);
  - Small amounts (from a few hundred dollars up);
  - High fees and charges and interest rates (up to 800-1000%).

Fringe or payday lending (2)

- Commonly, consumers seek fringe lenders to pay for other arrears or bills.
  - This suggests that consumers who access this credit are already experiencing financial hardship.
  - As such, they may be distinguished from other small, short-term loans that are for particular items (*ie,* fridge).
- There are also commonly problems with repayment methods.
  - Use of direct debit (with risk of bank dishonour fees).
  - Roll-over or back-to-back loans sometimes used by consumers to pay out loans.

Fringe or payday lending (3)

- Advertisements directed towards disadvantaged

Global MoneyLine (Victoria)

NEED CASH? ***loans for all reasons***

Loans From
$300 - $2,000

Fast Easy Approvals

Loans To Suit Your Income
Pensioners Welcome
Centrelink Recipients Welcome
Our Mobile Lenders Will Come To You

Credit Provided by GML (Victoria) Pty Ltd. ACN 112 905 914
Trading as **Global MoneyLine (Victoria). Credit Provider Registration No. 1994**

1300 10 1300

Fringe or payday lending – case study

- Mr L is 65 years old. For at least 6 years, and possibly for many years before that, he has suffered from cognitive impairment. It is readily apparent to the ordinary observer. He manifests as unintelligent and naïve. Mr L's sole income is a disability support pension. He does not own any substantial assets.
- In 2006, Mr L entered into a contract for a loan of $750 with Amazing Loans. The contract provided for a 'Loan Advance and Administration Fee' of $750, as well as other fees of $105.16, in addition to interest of 45.5% per annum. The Loan Advance and Administration Fee is said to accrue at the date of signing of the contract.

How can we assist Mr L?

- General consumer protection laws
  - Unconscionable conduct (*ie*, taking advantage of a consumer's naivety in relation to commercial dealings);
  - Misleading conduct (*ie,* representations that contracts are 'fair' (Amazing Loans)).
- Consumer credit laws
  - Section 70, *UCCC* – unjust transactions (as previous);
  - Section 72, *UCCC* – unconscionable fees (establishment fees cannot be more than reasonable costs of determining an application for credit and the initial administrative costs – ss (3)).

How can we assist Mr L? (2)

- Negotiate directly with fringe lender to reduce fees/interest.
- Consumer Action has had some success in negotiating:
  - the waiving of all fees/interest;
  - the waiving of all/some fees (interest charged); and
  - the waiving of all interest/fees up to a total comprehensive 48% interest rate cap.
- Make complaint to Consumer Affairs department or issue proceedings in relevant court/tribunal.

Interest rate caps

- Victoria, NSW and ACT currently have interest rate caps of 48% per annum on credit contracts.
  - Only NSW/ACT effective as it is a ‘comprehensive’ cap (*ie,* includes fees/charges).
- South Australia is currently considering whether to introduce an interest rate cap
  - Media release, Minister Rankine, 27 August 2007
- Vic Minister for Consumer Affairs spokesperson has said:
  - Interest rate caps will ‘increase costs passed onto consumers, thereby locking this group out of any form of bank credit’ (Herald-Sun, 20 August 2007).

Interest rate caps (2)

- Generally, fees charged by service providers are kept in check by the market.
  - However, there is very limited competition on fees charged by fringe lenders!
- This leads to a need to regulate so that fees/charges are not unfair or unreasonable.

Interest rate caps (3)

- Current proposed amendments to UCCC:
  - proposals include an ability to challenge fees on the basis that they are *unreasonable* (new s 72).
  - a fee is unreasonable only if it charges more than credit provider's underlying costs that give rise to the fee.
- Continues to rely on consumers challenging fees on a case-by-case basis – would a comprehensive cap would be more effective?
  - Consumer Action thinks so!

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