7 May 2012

By email: christian.mikula [at] treasury.gov.au; sue.bonnett [at] treasury.gov.au

Christian Mikula and Sue Bonnett
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Mr Mikula and Ms Bonnett

Discussion paper - Proposed reforms relating to Small Amount Credit Contracts

The following is a joint submission in response to Treasury's April 2012 discussion paper on proposed reforms to Small Amount Credit Contracts (**'the Discussion paper'**).

This submission has been prepared by Consumer Action Law Centre, Consumer Credit Legal Centre (NSW) and Financial Counselling Australia. The following organisations have also contributed to or endorsed this submission:

- Care Financial Counselling Service and the Consumer Law Centre of the ACT
- Community Information and Support Victoria
- Consumer Credit Legal Service WA
- Financial and Consumer Rights Council Victoria
- Financial Counsellors Association of New South Wales
- Financial Counsellors Association of Queensland
- Financial Counsellors Association of Western Australia
- Financial Counselling Tasmania
- Flemington and Kensington Community Legal Centre
- Footscray Community Legal Centre
- Good Shepherd Microfinance
- Redfern Community Legal Centre
- The St Vincent de Paul Society
- The Salvation Army, Moneycare
- South Australian Council of Social Service
- South Australian Financial Counsellors Association

Details on each of the contributing organisations can be found in the Appendix.

In brief, we:

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- continue to believe a comprehensive 48 per cent cap on costs would be the most effective consumer protection, and we support the cap originally proposed for Small Amount Credit Contracts by the Enhancements Bill (a 10 percent of amount borrowed establishment fee, and 2 percent of amount borrowed monthly fee)—the measures raised in the discussion paper and considered below would probably be unnecessary if an effective cap on costs was introduced;
- recommend that Government consider including a broad anti-avoidance provision in the Enhancements Bill and ensure ASIC is given adequate resources to enforce payday lending regulation to address inevitable attempts by lenders to avoid consumer protections;
- recommend that, whichever consumer protection measures are adopted, the Government's purpose needs to be to create a comprehensive package of measures rather that a disconnected collection of measures which will have less effect;
- recommend that the definition of Small Amount Credit Contract in proposed section 5(1) of the Enhancements Bill be changed to include only loans of below 12 months in length;
- regarding disclosure requirements:
    - support improved disclosure, though consider that disclosure of any variety will do nothing to prevent the harm caused by payday lending;
    - recommend that all disclosure must include an indication of costs expressed as an annual percentage rate;
- recommend that the prohibition on multiple loans, refinancing and credit limit increases are necessary and should remain in place. However, if the Government decides to weaken these protections it should:
    - require that any refinancing, issuing of concurrent loans or increases in credit limits be presumed to be unsuitable; and
    - prohibit any consumer accessing more than one refinance, one limit increase or holding more than two payday loans at any one time;
- regarding repeat borrowing:
    - recommend that repeat lending be addressed through a system which caps the number of loans that can be advanced to a person in a given period and introduces a payday loans register so lenders can easily access a borrower's lending record;
    - consider that additional disclosure will not prevent repeat borrowing;
- support a prohibition on single-repayment loans, but consider that a minimum term of three months (and a minimum of six approximately equal repayments within that period) would be a better solution;
- regarding payment by direct debits:
    - support an outright ban on lenders requiring or suggesting repayment by direct debit for small amount credit contracts. We believe this will change risk appetite of lenders, as borrowers are able to choose whether they direct income to repayments or essential expenditure;
    - if a ban is not introduced, lenders should be required to offer customers at least two payment options, and should suspend a direct debit arrangement after two rejections for insufficient funds;
- are wary of the proposal to introduce a Protected Earnings Amount. We consider it may have potential to limit harm to payday loan borrowers, but it is complex and problematic and has the potential to become a de facto replacement for proper credit assessment

pursuant to the responsible lending provisions. If such a scheme is introduced the protected amount of income should be at least 90 per cent.

Our comments are detailed more fully below.

Broad remarks

Cap on costs

We continue to believe that a 48 per cent comprehensive cap will be the most effective solution to the problems caused by payday lending. We still support the cap on costs for Small Amount Credit Contracts originally proposed by the *Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011* (**'the Enhancements Bill'**), that is a maximum 10 per cent of the amount borrowed as an establishment fee plus a maximum monthly fee of 2 per cent per month of the amount borrowed (**the 10+2 cap**) as a compromise from the 48% cap.[1] While we recognise that this discussion paper does not address the proposed cap on costs, it is important to point out that the measures raised in the discussion paper and considered below would probably be unnecessary if an effective cap on costs were introduced.

We do not believe any of the measures discussed below can replace an effective interest rate cap, however they are necessary to bolster the cap on costs that is now being proposed (a maximum 20 per cent establishment fee and maximum 4 per cent per month - **the 20+4 cap**) because it will be insufficient to protect vulnerable consumers from the harm caused by payday loans. Lenders have indicated that a 20+4 cap will mean that very short-term loans are still profitable, meaning that they will be widely available in the marketplace. A key goal of a cap at a lower level is to make very short-term loans unviable and to encourage lenders to offer loans on terms that are more reasonable and affordable.

Anti-avoidance Provisions and Enforcement

In our experience, it is standard practice for payday lenders to seek to avoid any regulation that affects their business. Whichever consumer protections are adopted, it is important that attempts at avoidance can be countered by regulators. We recommend that:

- Government consider including a broad anti-avoidance provision in the Enhancements Bill; and
- that ASIC be given the resources necessary to make enforcement of payday lending regulation a priority.

Suitability of Regulations

Broadly, we believe that the measures covered in the discussion paper are substantive consumer protections which should be included in legislation rather than regulation. We recommend that, once a decision is made on which consumer protections are to be adopted, Government consider the merits of placing them in the *National Consumer Credit Protection Act 2009* rather than regulations to that Act.

Need for a comprehensive approach

[1] At proposed subsections 31A(2) and (3) of the Enhancements Bill.

When considering the consumer protection measures raised in the discussion paper (and possibly others) it is important that the Government's purpose is to create a comprehensive package of measures which aims to reduce the harm caused by payday loans. If Government simply selects a disconnected collection of protections, it will create at best piecemeal protection and not achieve meaningful reform.

Definition of Small Amount Credit Contract

While the discussion paper does not propose any changes to the definition of 'Small Amount Credit Contract', we think it is worthwhile making some points on this issue here.

Small Amount Credit Contracts are currently defined at proposed subsection 5(1) of the Enhancements bill as contracts which (among other things), are for an amount of $2000 or less and a term of 2 years or less. Contracts that are not defined as a Small Amount Credit Contract would have a cap on costs of 48 per cent per annum (with some exceptions).[2] These boundaries were originally developed with the understanding that the cap on costs for Small Amount Credit Contracts would be the 10+2 cap. If the cap is to be increased to the 20+4 cap as is proposed, this will create two serious and unintended consequences.

The first is that the 20+4 cap creates a very rough transition between the Small Amount Credit Contract cap and the 48 per cent cap. As Table 1 demonstrates, a consumer borrowing $2000 over 24 months (regulated by the 20+4 cap) would pay up to $2320.00, while a consumer borrowing $2001.00 (regulated by the 48% cap) would pay up to $1,171.84. This is undesirable because of the increased potential to distort the market.

The NAB report *Do you really want to hurt me?* [3] (that has been heavily relied on by payday lenders to argue that a 48 per cent per annum cap is not viable for smaller loans) found that

> large fringe lenders, say with portfolios between $20 million and $100 million, are capable of delivering interest rates well below the 48% cap where the average loan size is around $1,000 [assuming a 12 month term].[4]

Where NAB found that 48 per cent cap was sufficient for large fringe lenders, the Enhancements Bill will actually permit lenders to charge the equivalent of an Annual Percentage Rate of over 100 per cent. It is difficult to see how this can be justified for loans of up to $2000 for periods over 12 months, even allowing some leeway for smaller, less efficient operators.

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[2] Under proposed section 32A.

[3] NAB (2010) *Do You Really Want to Hurt Me? Exploring the Costs of Fringe Lending - A Report on the NAB Small Loans Pilot*, Accessed from http://www.nab.com.au/wps/wcm/connect/nab/nab/home/About_Us/7/4/3/6/

[4] NAB (2010), p 14.

Table 1: Comparison of returns permissible for Small Amount Credit Contracts and contracts with 48 per cent cap

Amount	Loan term	Interest cost 48% p/a	Total charges (10+2)	Total charges (20+4)	Difference 20+4 and 48%	20+4 cap: Amount of returns above 200%
$1,500	12 mths	$ 417.95	$510.00	$1,020.00	$602.05	0
$1,500	2 yrs	$816.12	$870.00	$1,740.00	$923.88	$240.00
$2,000	12 mths	$557.26	$680.00	$1,360.00	$802.74	0
$2,000	2 yrs	$ 1,148.16	$1,160.00	$2,320.00	$1,171.84	$320.00

The second unintended consequence is that the proposed cap on costs allows lenders to make a return that is more than twice the amount loaned (prior to the application of any default fee or other contingency expense). For example, if lenders issue a 24 month loan of $2,000, their return will be $2,320. This is contrary to the intent expressed in proposed section 39B of the Enhancements Bill, which prohibits lenders recovering more than twice the amount loaned when the borrower is in default.

When the Enhancements Bill was introduced to Parliament, a press release from the (then) Assistant Treasurer Bill Shorten said that:

> The Gillard Government is determined to protect vulnerable consumers from the potential dangers of accessing credit with hidden risks or excessive interest rates.[5]

While the proposed cap on costs has changed, the intent of the Government to protect consumers from the dangers of these loans has not. However, under the current proposal, consumers will be exposed both to hidden risks (a $2000 loan costing over $1000 more than a $2001 loan) and excessive interest.

We recommend that the definition of Small Amount Credit Contract in proposed section 5(1) of the Enhancements Bill be changed to include only loans of below 12 months in length. These type of loans accord more with traditional 'payday loans' sought to be regulated by this bill. We are not aware of loans of between $1,000 and $2,000 for a period of greater than 12 months being offered by commercial lenders[6]—as such, this proposal should have limited impact on the market. Conversely, failure to amend the definition could see these loans being the cause of new problems, as lenders may be attracted to the higher returns they provide.

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[5] 'New Consumer Credit Protections Introduced into Parliament', Press Release, The Hon Bill Shorten MP, 21 September 2011. Accessed from: http://assistant.treasurer.gov.au/DisplayDocs.aspx?doc=pressreleases/2011/133.htm&pageID=003&min=brs&Year=2011&DocType=0

[6] One exception we are aware of in NSW is lenders offering loans in this range for terms ostensibly longer than 12 months. However, this appears to be an artifice avoid the current NSW rate cap—we are not aware of a single borrower who has not "opted" to pay the loan out over a shorter period and incur a deferred establishment fee in the process. In practice these loans are usually paid out over around seven months.

To be abundantly clear, we firmly believe that a cap on costs of Small Amount Credit Contracts should be designed to make the shortest term loans unviable and encourage the payday lending industry to offer longer term contracts which will cause less financial hardship for borrowers. We explain this point in more detail below. However, to move to the situation described in the table above would be a substantial over-correction and probably cause more problems than it solves.

Disclosure statements

General remarks

Broadly, we support improving disclosure to warn consumers of the risks and costs of payday loans and to draw their attention to better alternatives. However, it is important to recognise that disclosure of any type will not prevent the harm caused by this product. In the financial services arena, governments are increasingly coming to accept that disclosure is insufficient to protect retail investors—this was a driving impetus for recent financial advice reforms. There is no reason to suggest that disclosure will operate so as to effectively protect payday loan borrowers from harm. In fact, given the circumstances of most borrowers, it is far less likely to have the desired impact.

As argued by Consumer Action Law Centre's report *Helping Hand or Quicksand*, consumers take out payday loans because they have insufficient income to meet basic expenses.[7] Consumers in this position are generally in financial stress and see no other source of relief besides a payday loan. Disclosure will rarely be effective in this situation. Clients overwhelmingly report that they either do not understand or simply ignore the paperwork they are given—they are focussed entirely on the immediate needs which motivate them to enter the transaction. Further they do not "choose" a product or opportunity in the sense that an investor may be said to do so, they simply take whatever product is available to meet their driving needs.

It is also important that any disclosure does not overstate the availability of alternatives for potential borrowers and raise false expectations. While there are other options available in terms of community-based loan schemes, hardship programs & financial counselling, our experience suggests that many borrowers are seeking money for purposes that are simply not covered by other lending initiatives (for good reason). Further, a proper application of responsible lending assessment processes would exclude many of the clients we see from eligibility for other loans.

Need for cost to be disclosed as an Annual Percentage Rate

All disclosure statements, whether online or in-store should disclose cost of credit as an Annual Percentage Rate (**APR**). Although lenders may not be able to disclose the exact APR that will apply to a contract that has not yet been entered into, lenders could show a range of typical APRs.

The purpose of disclosing APR is to ensure consumers can compare the cost of payday loans with other credit on an apples for apples basis. Without an APR, it will be very difficult for most consumers to make this kind of comparison. In particular, we are concerned that lenders will be

[7] Zac Gillam and the Consumer Action Law Centre (2010) *Payday Loans: Helping Hand or Quicksand? Examining the Growth of High-Cost Short-Term Lending in Australia, 2002-2010*, p 60, 63.

permitted to advertise the cost of a loan as '20 per cent of amount borrowed upfront and a 4 per cent monthly fee‘, which (though accurate in itself) will mislead consumers by making the product appear cheaper than it is, and make comparison with other credit products nearly impossible. Even a consumer with average levels of financial literacy may mistake the 4 per cent monthly fee as being an annual rate and so compare a small amount credit contract favourably compared to mainstream credit products. While many current pay day lending clients do not compare products or read disclosure statements, a worst case scenario would be if other segments of the community not currently using these products were attracted to them as a result of being misled by advertising quoting the flat rates applicable under the cap.

Consumer Action Law Centre's research established that there is little if any price competition among lenders. The research found that less than 10 per cent of borrowers chose a particular lender based on price, while 54 per cent chose a lender because they were nearby, and 17 per cent because they had used that lender before.[8] In addition, borrowers appear to be largely unaware of the cost of their loans, either in percentage or dollar terms. When asked to report the cost of their loan, borrower responses varied widely but the most common response was $0.[9] A relatively small number of people nominated figures that could realistically be the cost of the loan.[10] Treasury's 2011 Regulation Impact Statement on the regulation of payday lending also cited overseas research which concludes that normal price competition does not appear to apply in the short term high cost lending market.[11] Given this, it is our view that if there is to be any form of disclosure, it should demonstrate the high expense of these loans and use an APR to allow comparison with other products.

As Treasury will be aware, lenders argue that APR is not an appropriate measure of the cost of a short term loan because it does not make sense to use an annual measurement on a loan with a term of less than one year. Lenders claim that, by using the APR calculation to measure the cost of a payday loan, the true cost is distorted and the loan looks more expensive than it is because of its short term. We agree that the short term nature of these loans contributes to their high APRs, but we do not agree that this is a distortion. On the contrary, the APR calculation helps show that it is precisely the short terms of these loans that make them so unaffordable. For this reason, APR is actually an excellent indicator of their cost to consumers in comparison with other loans. If payday lenders are required to disclose an indicative APR of their loans, a consumer will be able to quickly see that this product is far more expensive than any other loan on the market including credit card cash advances (another short term loan which is measured with APR).

Further, research[12] and experience[13] also demonstrates that many borrowers have numerous payday loans, and some are continually in debt to a payday lender for years at a time. For these

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[8] Gillam (2010), page 66.

[9] 12.9 per cent of respondents gave this response. Gillam (2010), pages 64-5.

[10] For example, 7.1 per cent responded with $100. Gillam (2010), page 65.

[11] Treasury (2011), *The Regulation of Short Term, Small Amount Finance: Regulation Impact Statement,* Australian Government, Canberra, pages 19-20.. Accessed on 6 October from http://ris.finance.gov.au/files/2011/09/RIS-Short-term-small-amount-finance.pdf.

[12] The interim report of RMIT's *Caught Short* research found that "over half the [112] respondents had taken out more than ten loans, with many saying they had received over 50 loans" since they first began borrowing. Seventeen people in the sample had only borrowed once. Marcus Banks (2011) *Caught Short: Exploring the Role of Small, Short Term Loans in the Lives of Australians, Interim Report*, page 11. Accessed from http://mams.rmit.edu.au/pvvp5ou0qcic1.pdf.

borrowers, the APR not only is an indicator of the cost of the debt but may actually represent the actual cost paid by the borrower.

Focus questions

(a) *What information should the disclosure notices include, given that it should be short and succinct to maximise its impact?*

To be most effective, disclosure needs to be short, high impact and be able to direct consumers to where they can seek help if they need it. We propose something along these lines:

> The loans provided by this lender are very expensive. A normal loan from this lender costs between [x% and y% per annum].
>
> If you are having money trouble, you should talk to a free and independent financial counsellor by calling 1800 007 007 before you apply for a loan.
>
> No interest loan schemes may be able to help you with payments for some essential household items. Emergency relief agencies may be able to help you in an emergency.
>
> A financial counsellor can provide information about all of your financial options.
>
> This statement is an Australian Government requirement under the National Consumer Credit Protection Act 2009.

We do not recommend that disclosure statements directly refer consumers to services such as the No Interest Loan Scheme (NILS). Research indicates that a large proportion of payday loans are taken out to pay bills and other expenses.[14] NILS loans are not available for such recurrent expenses, but are generally provided for the purchase of assets such as furniture or whitegoods.[15] There may be alternatives other than payday loans for many types of expenses, such as utilities or banking hardship schemes. It will be more effective to direct consumers to a financial counsellor who will be able to advise consumers of a number of options more appropriate than payday loans (including NILS, where eligibility criteria are met).

We do not recommend that disclosure statements link consumers to the Government's MoneySmart website. While MoneySmart is a very useful resource, a financial counsellor is better equipped to provide immediate, tailored advice that a person in financial distress needs.[16] If referral to an online service is warranted (and we are wary about whether it is), it might be better to refer consumers to websites established to provide advice specific to debt such as the

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[13] For example, one client of Consumer Action Law Centre was issued at least 64 loans by Cash Converters in a three year period, that is, almost one every fortnight during that period. *Payday Lending Practices Challenged in Court*, Consumer Action Law Centre Media Release, 17 October 2011. Accessed from: http://www.consumeraction.org.au/downloads/paydaylendingpracticeschallengedincourt-171011.pdf

[14] Gillam (2010), pages 59-60; Banks (2011) page 15.

[15] However, Good Shepherd Youth and Family Services advises that NILS programs for more specific needs, including loans for women setting up home after leaving domestic violence or after leaving prison, are now available in some areas.

[16] We also note that MoneySmart's personal loan calculator is not appropriate for users of payday loans, as it only allows users to enter an interest rate up to 25 per cent.

Victorian Government funded Money Help website, or the Financial Counselling Australia website soon to be launched to accompany the 1800 007 007 hotline.

The Government should consider requiring that translations of the disclosure notice also be provided where a store is located in an area where a significant proportion of the population speak English as a second language.

(b) Should the website and the shopfront disclosure have the same content?

Yes, although online disclosure could also link to websites for financial counselling services (as well as providing the number for the 1800 007 007 hotline).

(c) What is the appropriate placement for the storefront notice—for example, immediately next to the entry door, or on the door if no window or glass placement is available?

We recommend notices should be displayed prominently on or next to the entry door, and also at each loans desk.

(d) What timing/placement would be most effective in providing information to consumers in relation to the website disclosure? For example, should it be displayed on every webpage, say as a banner on top of each page (this would allow for consumers to see the information irrespective of their entry page to the website), or should it be a pop-up box that must appear on the application page before the consumer can commence a loan application ?

We recommend that disclosure notices should be provided both in a banner at the top of each page and as a pop-up before a loan application can be commenced. This is the nearest equivalent to the in-store requirement of a sign both at entry point and at the loans desk.

(e) What is the likely impact of requiring information about alternative options to be included in the Credit Guide? In particular, is the timing of the provision of this document likely to be helpful to consumers?

Providing information about alternatives in the Credit Guide will have very little impact. The evidence cited above about consumer awareness of the cost of payday loans suggests very few borrowers read or understand even the most significant obligations under their contract. Further, despite the intention for Credit Guides to provide information to consumers before they enter into a loan, our experience is that Credit Guides are not provided at the time of the loan application process and therefore has very limited use.

Prohibitions on multiple concurrent contracts, refinancing and increasing credit limit

General remarks

The Parliamentary Joint Committee on Corporations and Financial Services expressed concerns about restrictions on multiple concurrent contracts, refinancing and increasing credit limits on the following grounds:

- there is no way for lenders to know whether a borrower already has a loan with another lender;
- these restrictions may increase rather than reduce financial hardship; and

- the restrictions do not appear consistent with responsible lending regime under the *National Consumer Credit Protection Act 2009* (**the NCCP Act**) and may not be suitable for borrowers who are not experiencing financial hardship[17]

The committee considered that a better approach would be to:

> ...require short-term lenders to consider whether the proposed short-term loan or increased credit limit is unsuitable given the consumer's repayment obligations under existing credit contracts. This obligation should only apply to the extent that the short term lender is informed of existing credit contracts by the consumer in response to the lender's inquiries.[18]

We agree with the committee's concern that these restrictions are not enforceable without a payday loan register, and we recommend the introduction of a register below. However, we disagree with the committee's other findings and its conclusion that enhanced responsible lending requirements are a suitable response.

The Committee appeared to rely on a two arguments made by lenders in coming to these findings. The first argument is commonly explained by lenders through a scenario consumer who could borrow (for example) $1000 without hardship but has an immediate need for only $500 so borrows the lesser amount. However, in the week after taking the $500 loan, the borrower meets another unexpected expense and cannot borrow the other $500 to cover it even though they can afford it.[19] This account—along with the industry's broader argument that payday loans are used harmlessly by borrowers for one-off, unexpected expenses—is not the experience of most borrowers who refinance, take out concurrent loans or seek credit increases.

The real driver for this behaviour is the business model of payday lending itself—issuing high cost credit to low income borrowers with insufficient income to meet essential, recurrent expenses. Borrowers take out payday loans to provide short term relief from an income shortfall and in doing so simply get further into debt. This cycle is extremely profitable for the industry—so profitable that, as an industry representative said to the Parliamentary Joint Committee, large parts of the industry may not exist without it:

> The focus has been on the interest and cost cap. The reality is that... at least 28 per cent of the payday lenders will go because at least that number are dependent, in part—whether good or bad; but this is an economic fact—on some form of rollover or refinancing opportunity.[20]

These cycles of debt cause considerable harm to payday loan customers. In one example, a client of the Consumer Action Law Centre was trapped in a cycle of payday lending to such an

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[17] Australia, Parliamentary Joint Committee on Corporations and Financial Services (2011), *Inquiry into Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011*, paragraphs 5.229-5.230. Accessed from http://www.aph.gov.au/Parliamentary_Business/Committees/Senate_Committees?url=corporations_ctte/Consumer_Credit_Corporations_2011/index.htm

[18] At paragraph 5.231.

[19] For example, Parliamentary Joint Committee on Corporations and Financial Services (2011), paragraphs 5.152-5.153.

[20] Phillip Smiles, cited at Parliamentary Joint Committee on Corporations and Financial Services (2011), paragraph 5.149.

extent that he took out at least 64 loans from Cash Converters over the course of three years—on average almost one per fortnight.[21] In our experience it is scenarios like this, and those in the case studies below, are a more realistic picture of consumers who borrow repeatedly from payday lenders.

Case study - Matthew

Matthew (not his real name) is a Disability Support Pensioner with an income of $749 per fortnight. When Matthew approached a community legal centre for advice he had two payday loans from different providers with around $2000 to repay total.

Matthew's bank statements showed that these loans had not been isolated. Statements from mid September to late December 2011 show fortnightly repayments on 3 small payday loans from different providers totalling about $321 per fortnight. After rent, a lease payment for a household appliance and repayments for a Centrelink lump sum advance previously received, Matthew had $132 per fortnight for all other expenses.

When asked how many loans he had, Matthew responded that

> "I used to get cash advances from [one lender] pretty much every fortnight. They started out at about $70 or $80 and went up to $100 or so (I think) once I proved I would pay. I was doing this for months, possibly a year. I also had other loans from [the same lender]—they would let me get it down to about $180 each time before they would lend me another $600, so I would get about $420 in the hand by the time they paid out the previous loan.
>
> [A second lender] would not let me get a new loan until I had paid off the old one. I would go in with my bank statements as soon as I had paid one off and they would give me another one right away. I am not sure [how long this was going on for], certainly months, maybe years...I think one year at least. It was always the same lenders and always pretty much back to back loans."

When asked what he lived on the client responded that he "didn't eat much", that he occasionally got food vouchers from the Salvos and Vinnies and food hampers from friends. Matthew also mentioned that he "never bought clothes" and was "always behind" on his power bills.

Matthew also said that:

> I knew they were sharks and I was feeding them but I was stuck in a cycle I couldn't get out of. They got me to sign petitions and things supporting them which I did because I wanted the money at the time but I also resent that now.

[21] *Payday Lending Practices Challenged in Court*, Consumer Action Law Centre Media Release, 17 October 2011. Accessed from: http://www.consumeraction.org.au/downloads/paydaylendingpracticeschallengedincourt-171011.pdf

Case study: Edward

Edward (not his real name), an aged pensioner in his seventies, was referred by a financial counsellor to a community legal centre in November 2011. At the time of the referral, Edward had four concurrent loans, of $300, $400, $600 and $2020 respectively from four different lenders.

Edward says he borrows the money because he can't keep up with living expenses on the pension any more. He says he gets a loan half paid off and then another bills comes in so he gets another loan partly to refinance the old loan and partly to pay the latest expense. Edward says it's easy to get the money—if you are new to the lender you have to take in a Centrelink statement and bank statements but once they know you they just refinance without anything further required.

Case study: Maria

Maria (not her real name) was referred to a community legal centre in 2012. She has been a victim of domestic violence and experienced long-term homelessness. Her recent income has been predominantly worker's compensation with bouts of intermittent part-time employment. She has a teenage son.

Maria went bankrupt in 2008 (and was discharged in 2011) and a debt to payday lender was among her provable debts. The same lender provided her with two more loans totalling $1500 while she was still bankrupt (Maria answered 'no' when asked if she was or had been bankrupt on her application). Also while bankrupt, Maria received another loan from an online lender for around $400, and a fourth from a telephone lender which started at $300 and is now over $1200 as a result of default fees. She is considering a second bankruptcy.

It should clearly follow that the industry does not oppose restrictions on refinancing out of concern for its consumers, and indeed that the opposite is true—it opposes them because such a ban will harm its profitability, despite the harm this practice causes its customers.

Another argument put to the committee was that that banning refinancing, multiple loans and increasing credit limits would force people to borrow more, which would create more indebtedness. Further, it was argued that this would create such harm that, according to the Financiers Association of Australia '[e]very three months you would double your default rate.'[22]

These arguments are so logically flawed as to be incoherent. We find it hard to accept that a borrower (much less a large number of borrowers) would borrow more money than they need to cover an expense which has not yet arisen and they are unaware will arise. It is also hard to see how issuing high cost credit to cover a low income borrower's unforseen and nonspecific 'forward contingencies' would meet the a borrower's requirements and objectives, and so the lender's responsible lending obligations under the NCCP Act. Even if a large number of borrowers did borrow to cover such expenses that didn't yet exist and lenders were not

[22] At paragraph 5.154

prohibited from issuing these loans by the NCCP Act, this would not 'double the default rate every three months' as suggested. If lenders were experiencing this level of defaults, they would cease making these kinds of loans.

An extension of responsible lending obligations will not address the problem of repeat borrowing, as hoped by the Joint Parliamentary Committee. We have discussed in the past why responsible lending is ineffective at limiting harmful lending by this sector.[23] Similarly, Treasury have also found that, despite the fact that "responsible lending requirements could be expected to have the greatest impact on very short-term loans with a single high repayment... there do not appear to have been any significant changes to practices in this area".[24] Different and more direct restrictions on this practice are clearly justified and we strongly recommend that the prohibitions on multiple concurrent loans, refinancing and credit increases are appropriate and should remain.

Consumer advocates have expressed concern throughout this debate that the ban on refinancing does not go far enough. In addition to rolling over loans, consumers also report getting another loan on the same day they make the final payment on a previous loan, or within the same pay cycle (most often fortnightly), in order to address the cash flow deficit created by the earlier loan repayment. Indeed we have seen a loan contract for a Disability Support Pensioner where the purpose of the loan is stated as “cash flow deficit”. We have long argued that the ban should extend to borrowing within the same pay cycle (or at least the same fortnight) as this would capture the majority of cases.

If the Government decides to weaken these protections, the regulations should:

- require that any refinancing, issuing of concurrent loans, increases in credit limit or provision of a new loan when a small amount credit contract has been repaid within the current or previous pay period be presumed unsuitable unless there is clear, documentary evidence to demonstrate otherwise. Evidence should include receipts to demonstrate that the previous loan was spent in accordance with the purpose indicated on the original loan application (for example, a mechanic's receipt for car repairs). Lenders must be required to keep a copy of this evidence and ASIC should be empowered and resourced to investigate this type of lending regularly.
- prohibit any consumer accessing more than one refinance, one limit increase or holding more than two payday loans at any one time to limit the potential of cycles of debt.

These are clear, unambiguous requirements that may make responsible lending obligations simpler to enforce. However, we reiterate that these measures will not be as effective as the prohibitions originally proposed.

[23] For details, see Consumer Action Law Centre Submission to the inquiries into the Credit and Corporations Legislation (Enhancements) Bill 2011, pages 8-9.
[24] Treasury (2011), page 38.

Focus Questions:

(a) *What would be the practical implications of requiring lenders to consider the borrower's best interests? It this approach was adopted, how would the content of the obligation be defined?*

While a best interests duty might appear to be a promising consumer protection measure, we are wary of applying such a duty in this situation. As it is described in the attachment to the discussion paper, such a duty might be satisfied if a lender could demonstrate that they have acted reasonably in the circumstances. It is hard to see how such a requirement is different to responsible lending obligations.

As noted above, there is widespread agreement that responsible lending obligations are insufficient to protect payday loan borrowers—this fact is endorsed by the Parliamentary Joint Committee.[25] One of the key problems with the responsible lending obligations is that they are difficult to enforce. Our experience is that payday loan borrowers are, in general, less likely to raise a dispute (with a court, tribunal or ombudsman scheme) than other borrowers, are less likely to be prepared to provide evidence to a regulator and, even when they do, their understanding of the transaction and other factors reduce the likelihood that they will be identified as useful by the regulator. This all leads to enforcement of the responsible lending laws in this sector being extremely difficult, and would be unlikely to be adequate to change industry practices. We believe that any best interests duty would similarly suffer from enforcement complexities.

Apart from enforcement problems, it seems almost impossible to define what constitutes the borrower's best interest in any given situation. For example, it could be argued that it is better for the borrower to pay his or her rent than not get a further advance on another loan that is still outstanding. However, this test completely ignores the problem repeat borrowing creates—that of a perpetual drain on income over time which prevents the borrower meeting their essential expenses in the longer term. If the test is intended as suggested in the paper to be confined to situations where the charges or repayments are lower than those offered by the current contract, then it would be better to simply define the exception to the prohibition in the those narrow terms, preferably only where the charges and repayments were lower than the current contract (not only where the charges *or* repayments are lower, as suggested in the discussion paper).

(b) *If exceptions are to be defined by a category of transaction (for example, by the characteristics or circumstances of the borrower), how are these categories to be defined? In particular, can these transactions be defined in a way that is clear and unambiguous as to when the exception applies?*

Refinancing, concurrent loans and increasing credit limits are dangerous in themselves. We do not see the value of drawing distinctions based on what will necessarily be arbitrary categories of transaction or borrower. This will also add further complexity and loopholes to the law.

[25] At paragraph 5.224.

(c) *If the approach of providing for an unsuitability presumption was adopted, what circumstances or transactions should the presumption apply to?*

As above, all requests for refinancing, credit limit increases or concurrent loans should be considered unsuitable unless clear documentary evidence proves the contrary.

Repeat lending/successive loans

Focus Questions

(a) *To what extent is the repeated use of SACCs indicative of a class of consumers who may be experiencing psychological or social barriers to seeking advice or assistance? Where this is the case, will repeated disclosure (under Option 1) overcome or lower these barriers?*

Additional disclosure will not prevent harmful repeat borrowing. We do not think there is any explanation for a consumer repeatedly taking out expensive short term loans except that they are in financial distress. As outlined above, disclosure will have very limited impact on a borrower in severe financial stress.

While it is true that many consumers are unaware of the existence of services such as financial counselling, this is not necessarily because of “psychological or social barriers”—more simply it is generally because there are few services. In comparison, payday lenders have high street level visibility and prolific advertising.

We also disagree with the assessment in the discussion paper that some repeat users of payday loans may benefit simply by "improving budgeting skills". It needs to be recognised that the presence of payday loans is itself the reason for repeat borrowing of payday loans. These loans attract customers by posing as a solution to financial trouble, but only serve to exacerbate it. As we have explained above, repeat borrowing is a typical and predictable consequence of the way payday lenders issue their loans, not a weakness on the part of borrowers. No amount of budgeting skills will prevent repeat borrowing.

(b) *What are the advantages and disadvantages of the options considered above to address repeated use of SACCs? What should be the appropriate trigger for each such option?*

AND

(c) *What additional responsible lending obligations could apply, if that was required, in relation to repeat borrowers?*

AND

(d) *Are there any other options that should be considered to regulate repeated use of SACCs?*

We recommend that repeat lending be addressed through a system which:

- caps the number of loans that can be advanced to a person in a given period; and
- a payday loans register so lenders can easily access a borrowers lending record.

We believe this approach will provide the greatest level of consumer protection if a cap set at an effective level (such as the 48 per cent cap or the 10+2 cap) is not available. We urge Government to consider implementing this kind of approach when assessing the merits of other options mentioned in the discussion paper.

This system has been adopted successfully in some US states. For example, in Washington State the following rules have been established:

- A borrower cannot have one or more outstanding payday loans totaling $700 or equaling 30% of their gross monthly income, whichever is less;
- A borrower cannot obtain a payday loan where they have an installment plan to pay off a previous payday loan;
- A borrower cannot obtain a payday loan where they are in default on a payday loan;
- A borrower cannot take out more than eight loans in any 12 months period;
- The lender is required to access a database that contains detailed information about payday loans made to Washington consumers by all lenders licensed to do business in that state. The database includes borrower's social security numbers (or equivalent identification numbers) and gross monthly income information, and will determine whether a consumer is eligible for a payday loan and, if so, for what amount.

Data from that state's regulator demonstrates that when this requirement was introduced, the number of loans fell from 3,595,873 (worth $1.36 billion) in 2009 to 1,093,776 (worth $434 million) in 2010.[26]

This data again demonstrates that much payday lending does involve repeat borrowing—a practice that even the industry agree is harmful.[27] The data from Washington cited above suggests that, before reforms were introduced, over two-thirds of loans were taken out by consumers who had already borrowed at least 8 times in the previous twelve months. Analysis of the Washington model suggests that it was the cap on the total number of loans that can be issued over a period of time that was the particular the reason why repeat lending was reduced so drastically.

If this approach were taken, a decision would have to be made as to the total number of loans that could be issued and over what period. In our view, the number allowed in the Washington example is too many—eight loans in 12 months will in most cases demonstrate financial distress. An important difference between the Washington model and the current proposal for Australia should be noted—in Washington, the maximum amount of a payday loan is $700, while the definition of Small Amount Credit Contracts is up to $2,000. If a cap on the number of loans in a given period is enacted, lenders might respond by advancing larger loans repayable over a short period.[28] A smaller number on the cap on loans might be one way to address this.

[26] Washington State Department of Financial Institutions, *2010 Payday lending report*, page 2, available at: http://www.dfi.wa.gov/cs/pdf/2010-payday-lending-report.pdf.
[27] For example, in its submission to the Parliamentary Joint Committee, the National Financial Services Federation made a proposal for a regulation to "control debt spirals".
[28] Washington also has a cap on costs, but this allows lenders to earn an APR of 390% on a 14 day loan, and hence can make a profit on these short loans.

Whatever the number permitted, this system would still need to be supported by regulations recommended above that presume a repeat loan to be unsuitable if a consumer has repaid another payday loan in the current or the previous pay period. Applying for two payday loans in two pay consecutive pay periods or less should suggest in almost all cases that the consumer is borrowing because their income is insufficient to meet basic expenses. As discussed above, lenders should only be able to overcome the presumption with unambiguous documentary evidence that the consumer can afford the subsequent loan.

We reiterate that we believe this kind of system—a hard cap on the number of loans over a particular period, supported by a loans database—should be considered the best alternative to an effective cap on costs.

Restrictions in relation to single repayments

We agree with the statement in the discussion paper that loans required to be repaid through a single repayment increase the risk of financial stress for borrowers. However, we disagree with the suggestion that this practice is relatively uncommon in Australia. Research conducted by Consumer Action Law Centre in 2008 found that 34% of payday loans had a repayment period of equal to or less than two weeks. Similar research in 2002 (albeit with a smaller sample) found that 41% of loans had a term of two weeks or less.[29] This suggests that a large number of loans are paid off in a single repayment, or at least within a single pay period.

While we support a prohibition on lenders requiring borrowers to pay off the whole loan in a single repayment, we believe a better solution would be to require a minimum term for small amount credit contracts. We suggest the regulations should require a minimum term of three months and a minimum of six approximately equal repayments within that period.

In our view, three months (or six pay periods) is the minimum repayment period necessary to ease pressure on low income borrowers. As Consumer Action Law Centre have demonstrated previously[30], repayments on a typical payday loan can be expected to cost around 25 per cent of a typical borrower's income over a 28 day term (also typical). Repaying the loan over six fortnights will still divert a significant portion of borrower income (and may be unsuitable in many cases) but will be much more manageable than current standard practice.

As Table 2 shows, a minimum three month term will create less strain on a budget of a typical borrower even though under the 20+4 cap will mean a three month term will attract more monthly fees than a shorter term.

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[29] Gillam (2010), page 84.

[30] Consumer Action submission to Parliamentary Committee inquiries regarding the *Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011*, p 4. Accessed from http://www.consumeraction.org.au/downloads/CALCsubmission-ConsumerCreditandCorporationsLegislationAmendmentEnhancementsbill-141011.pdf

Table 2: Impact on budget of typical borrowers of repaying a $300 payday loan under the 20+4 cap over terms up to three months

Term (fortnights)	1	2	3	4	5	6
Total to be repaid	$372	$372	$384	$384	$396	$396
Repayments per fortnight	$372	$186	$128	$96	$79.20	$66
Repayment as % of income assuming $923 per fortnight	40.3%	20.1%	13.9%	10.4%	8.5%	7.1%
Repayment as % of income assuming $749 per fortnight	49.6%	24.8%	17%	12.8%	10.6%	8.8%

Realistically, a ban on single repayment loans would require a minimum term requirement in any case. Without a minimum term, a lender could require a loan to be repaid over two repayments in a single fortnight which would have the same impact on the borrower as a single repayment loan (that is, the borrower is required to repay the entire loan in one pay period).

If the Government decides to either require a minimum term or prohibit lenders issuing single-repayment loans, consumers should be free to pay off loans in a single repayment (or at any point before the end of the loan term) if they choose. However:

- repayment schedules and direct debit authorities must be based on the prescribed minimum term; and
- if borrowers choose to repay early, lenders must not be permitted to charge monthly fees which have not accrued at the time of repayment or early repayment fees. We understand that these fees should already be prohibited by proposed sections 23A and 31A of the Enhancements Bill.

Focus Questions

(a) *What effect will the introduction of the proposed cap on SACCs and other proposed reforms have on single repayment SACCs? Could it be expected that it will result in a reduction in this type of lending?*

We do not believe the proposed cap on SACCs will have any impact on single repayment loans, without further protection such as a minimum term. As noted above, it is our view that the proposed 20+4 cap will have a very limited impact on the marketplace, and that large lenders will continue to offer very short-term small amount loans. While the cap on costs *may* prevent some very small loans being issued with single repayments,[31] we cannot see why it would prevent lenders from continuing to offer loans in the higher range of those currently available with a single repayment period. Unless the cap is set at a level that will make very short-term loans unviable (and we do not believe that a 20+4 cap achieves this objective), then further protections such as a minimum term of a ban on single repayment loans will be necessary.

[31] Because under the 20+4 model, a single repayment loan will at most return 20 per cent establishment fee plus a 4 per cent fee for the first month. On the smallest loans, this may not provide an acceptable return for a lender.

(b) *What would be the impact of introducing a ban on contracts with single repayments? How would this compare with the impact of a presumption in relation to suitability?*

A ban on contracts with single repayments would mean that these loans are no longer available in the marketplace, and that loans that are available are likely to be more affordable for borrowers by allowing them to repay them by instalments over time.

A presumption that contracts with single repayments are unsuitable is unlikely to reduce the availability of such loans, without clear and robust guidance about what evidence is required for this presumption to be overturned. Without such guidance, lenders could merely state that because a borrower could repay a single repayment loan (through, for example, a direct debit transaction), then that might be evidence that the loan is not unsuitable. As stated frequently throughout this submission, enforcement of this type of provision is fraught with difficulty in this market and is considerably less likely to have any real impact on lending practices than a clear prohibition.

(c) *Are there any other options that should be considered to address SACCs with single repayments?*

Yes, a minimum three month loan term as proposed above.

If the prohibition on single repayment loans is introduced rather than a three month minimum term, the discussion paper suggests that this prohibition could be evaded by the lender requiring a first repayment of the entire debt less $1, and a second repayment of $1. This could be prevented by a prohibition on any repayment which (including any interest, fees, charges etc) is greater than 50 per cent of the total debt.

Use of Direct Debit repayment options

<u>General remarks</u>

We support an outright ban on lenders of small amount credit contracts requiring or suggesting repayment by direct debit. However, consumers should be permitted to set up their own automated payment arrangement through their bank if they wish to do so.

The common practice of requiring repayment by direct debit is part of the reason why payday loans are both harmful for consumers and profitable for lenders. Lenders generally obtain direct debit authorities from borrowers as part of the application process. Lenders then debit a borrower's bank account as soon as pay or benefits are deposited, securing the loan. When a borrower is already on a limited income and unable to afford basic needs, this impinges on their capacity to pay for essentials like food or rent, prompting additional financial stress and further borrowing.

Requiring direct debits allows for a relatively low risk of default on payday loans, even though a typical payday loan for a typical client is likely to create financial stress. The lender has taken first stake in the borrower's income so the borrower is more likely to 'default' on their rent or groceries, than on their loan repayments. This means that lenders are currently wearing an artificially low risk of default on what would otherwise be loans too risky to issue.

If repayment by direct debit is prohibited for small amount credit contracts we expect lenders to experience an increase in the rate of defaults as consumers with insufficient income prioritise essentials like rent and groceries over repayment of the debt. We stress that this increase would not reflect a rise in the rate of financial hardship caused by payday loans, it would simply indicate that the default rate was moving to a more 'natural' level from a point which is artificially low. This will have the effect of making irresponsible loans more risky for lenders and so dilute the incentives to issue them, which in turn might bring back default rates to levels acceptable to the lenders.

Despite improving the rate of loan repayment for lenders, direct debit arrangements carry a significant risk to the borrower of double penalties (fees imposed by both the bank and the lender) in the event that there are insufficient funds in the account. This risk is borne by any consumer using direct debit payments but is highest for those living on low incomes as is typical for payday loan borrowers. A ban on direct debits would remove this risk and limit the cost of the loan to those charges imposed by the lender. This is consistent with the overall scheme of limiting the costs of SACC contracts, including charges imposed by third parties.

Focus Questions

(a) *What are the likely outcomes from banning direct debits? In particular would it be expected to result in an increase in the rate of defaults?*

As discussed above, banning direct debits will force lenders to assess lending applications more rigorously. It may also increase the level of defaults experienced by lenders if lending practices remain unchanged.

(b) *Should consumers always be provided with choices for making repayments (for example, a minimum of three options)? If so, what other payment options would be considered appropriate?*

If the Government does not wish to prohibit repayment by direct debit on small amount credit contracts, lenders should at a minimum be required to offer at least two repayment options with equal prominence. However, it must be noted that this will have little impact on the proportion of loans that are repaid by direct debit. Lenders have powerful incentives to make direct debit the default repayment option, and we expect few consumers would question this arrangement.

(c) *What would be the impact of suspending the use of a direct debit request where it has been rejected three times because of insufficient funds in the borrower’s account?*

If the Government does not prohibit payment by direct debit, we recommend that direct debits should automatically be suspended after two (rather than three) rejections due to insufficient funds. This measure is appropriate because it does nothing more than what most consumers would do themselves if they were aware they had the option (that is, cancel the direct debit authority). In our experience, consumers will rarely cancel direct debit arrangements which are causing them harm, either because they are unaware that they can cancel them, have had difficulty getting their bank to act on the instruction to cancel, or because they think that doing so would put them in breach of contract. Automatically suspending the direct debit arrangement overcomes these barriers. Suspending the use of direct debits where it has been

rejected would have the added benefit of limiting default fees charged by both the borrower's financial services institution and the lender in the event of a direct debit dishonour.

(d) *What would be the impact of increasing the triggers for credit providers to provide a Form 11 direct debit default notice (for example, when the consumers signs a direct debit authority)?*

This would have very little impact. As discussed above, we do not believe in general that improved disclosure will reduce the harm caused by payday loans. While we support the intention of this form, we note that it is one and a half pages of text, and that borrowers are unlikely to read such additional material when they take out a loan or sign a direct debit authority.

Introduction of a Protected Earnings Amount (PEA)

General remarks

We are wary of this proposal. We believe it has potential to limit harm to payday loan borrowers, but it is complex and problematic for a number of reasons:

- the effectiveness of the PEA scheme would depend on the amount of income to be protected;
- the earnings calculation could be rorted either by the lender or by a desperate consumer;
- earnings of people on low incomes can vary considerably from week to week, so previous earnings may give very little indication of ability to repay a debt in future;
- there is a risk that lenders will use the PEA as a substitute for responsible lending obligations, and a PEA regime will at least create confusion around obligations of lenders; and
- simpler measures, such as the three month minimum term or a limit on total number of loans per year recommended above may create greater benefit.

For these reasons we do not at this stage recommend a PEA regime is introduced. However, we are happy to engage in further discussions on this topic.

The protected amount

If a PEA system was introduced, the protected amount would need to be much higher than 65 per cent. A system which only protects 65 per cent of income offers no effective protection at all. While we are still open to discussion on this point, we believe the protected amount would need to be at least 90 per cent to be effective.

For comparison, the Australian Housing and Urban Research Institute considers a household to be in 'housing stress' if it is in the lowest 40 per cent of income distribution and spends more than 30 per cent of its income on housing. If directing 30 percent of income to housing is problematic, then directing 35 per cent of income to repay a payday loan should also be expected to cause considerable financial stress (particularly because these borrowers are predominantly on low incomes[32] and will also have to meet other essential expenses). It follows

[32] For discussion on this point, see Consumer Action Law Centre Submission to the inquiries into the Credit and Corporations Legislation (Enhancements) Bill 2011, page 4.

that leaving 35% of income unprotected would be to explicitly condone loans which put payday loan borrowers into financial trouble.

Similarly, where debts are owed to Centrelink that the payment recipient cannot pay off in a lump sum, Centrelink typically requires repayment at a rate of 15 per cent of the person's main Centrelink payment each fortnight. The rate can be higher than 15 per cent if the person has other income such as earnings from employment or investments.[33] The Centrelink Code of Operation with Participating Financial Institutions also states that financial institutions cannot access more than 10 per cent of each pension, benefit or allowance payment to repay money owed to them. We see no reason why payday lenders should be able to gain access to a greater proportion of borrowers' Centrelink income in comparison with other financial institutions that are signatories to this Code.

Focus Questions

(a) *What are the likely outcomes from the introduction of a PEA? In particular, information is sought on the level of repayments charged to borrowers under SACCs, both currently and under the foreshadowed 20/4 cap, and whether they would ordinarily be less than 35% of the borrower's income?*

Although we would oppose a PEA which only protected 35 per cent of borrower income, this may still offer more protection to consumers than current regulation. Consumer Action Law Centre recently assisted a client who was issued a $300 loan by The Cash Store which required her to repay 476.62 in the space of a fortnight. The client's sole income was a Disability Support Pension payment of $671 per fortnight. This loan—issued well after responsible lending obligations came into effect—would have left our client with income of just $194.38 for two weeks, reducing her pension by around 71 per cent.[34]

(b) *What are the advantages and disadvantages of each of the models considered above?*

AND

(c) *Are there any particular categories of borrower who would particularly benefit from the introduction of a PEA requirement?*

If a PEA is introduced, it should apply to all borrowers. As already noted, the typical borrower of a payday loan is on a low income, is using the loan to pay for basic, recurrent expenses and repaying the loan will be a significant burden to their budget.[35] Even those borrowers on higher incomes can be presumed to be in some kind of financial stress before they decide to take out a

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http://www.consumeraction.org.au/downloads/CALCsubmission-ConsumerCreditandCorporationsLegislationAmendmentEnhancementsbill-141011.pdf

[33] http://www.centrelink.gov.au/internet/internet.nsf/payments/owing.htm#reduced

[34] *Ombudsman asked to consider lending practices of payday loan provider*, Consumer Action Law Centre Media Release, 6 March 2012. Accessed from http://www.consumeraction.org.au/downloads/Ombudsmanaskedtoconsiderlendingpracticesofpaydayloanprovider-060312.pdf

[35] See the discussion on these points in the Consumer Action Law Centre Submission to the inquiries into the Credit and Corporations Legislation (Enhancements) Bill 2011, pages 4-5. http://www.consumeraction.org.au/downloads/CALCsubmission-ConsumerCreditandCorporationsLegislationAmendmentEnhancementsbill-141011.pdf

payday loan and so are also vulnerable. We do not see the value in protecting some vulnerable borrowers with through this measure but not others.

However, if Government believes the protection should not apply to all borrowers, at a minimum it should apply to all borrowers receiving Centrelink payments.

There is a clear Commonwealth policy expressed in section 60(1)of the *Social Security Administration Act 1991* (Cth) that social security payments are needed for basic necessities and are inalienable. This policy serves two important objectives:

- ensuring that all Australians receiving social security payments have an income which allows them to afford basic goods and services; and
- ensuring that taxpayer funding of social security payments are directed only to meeting those basic needs.

This reasoning applies whether Centrelink benefits are the borrower's sole income or only part of it. The protection should apply to Centrelink recipients in either case.

Some industry representatives have suggested that a PEA requirement would replace the need for other measures such as banning single repayment loans or setting minimum terms, banning refinancing, or indeed having a cap at all. We strongly oppose this argument and reiterate our comments about the need for a comprehensive package. Further, if the PEA requirement were confined to Centrelink recipients, the other measures canvassed in this discussion paper would clearly be needed to protect other borrowers as the harm discussed throughout this submission often applies equally to borrowers earning income from other sources.

(d) How would the PEA interact with existing responsible lending obligations?

A PEA scheme, if enacted, should not replace responsible lending obligations, but be additional to such obligations. If a PEA was introduced, it should be made clear that a lender does not comply with its responsible lending obligations simply by complying with the PEA scheme.

A PEA scheme only considers income and doesn't consider a borrower's other liabilities or financial commitments. Even if a borrower has a reasonably high income, after considering other debts and financial commitments, a payday loan may be unsuitable and cause financial hardship, and therefore be irresponsible. Similarly, even if the percentage was set at very low level, many Centrelink recipients have no surplus after essential expenses with which to meet repayments under a loan. In no way should a regulatory framework that adopted a PEA approach replace the existing responsible lending obligations.

However, as noted above, we are also concerned that a PEA scheme would likely confuse both lenders and consumers as to the lenders' responsible lending obligations. Many might use PEA as a rule of thumb and believe because the borrower satisfies a PEA requirement, the loan is presumed to be responsible. The scheme would need to be carefully designed to avoid this problem.

Thank you for the opportunity to provide this submission. If you have any questions, please do not hesitate to contact us. Our contact details are in the Appendix.

Yours sincerely

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Financial Counselling Australia

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Endorsed by:

- Carmel Franklin, Care Financial Counselling Service and the Consumer Law Centre of the ACT
- Kate Wheller, Executive Officer, Community Information and Support Victoria
- Faith Cheok, Principal Solicitor, Consumer Credit Legal Service WA
- Cheryl Buttigieg, Chair, Financial and Consumer Rights Council Victoria
- Jim Connolly, Financial Counsellors Association of New South Wales
- Saskia ten Dam, Financial Counsellors Association of Queensland
- John Talbert, President, Financial Counsellors Association of WA
- James Davis, Financial Counselling Tasmania
- Anthony Kelly, Executive Officer, Flemington and Kensington Community Legal Centre
- Denis Nelthorpe, Manager, Footscray Community Legal Centre
- Adam Mooney, CEO, Good Shepherd Microfinance
- Jacqui Swinburne, CEO, Redfern Community Legal Centre
- Dr John Falzon, Chief Executive Officer, The St Vincent de Paul Society
- Tony Devlin, The Salvation Army, Moneycare
- Ross Womersley, Executive Director, South Australian Council of Social Service
- Sharon Brinkley, Chair, South Australian Financial Counsellors Association

Appendix: About the contributors

Consumer Action Law Centre

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.

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.

Contact: David Leermakers, Senior Policy Officer: david@consumeraction.org.au; 03 9670 5088.

Consumer Credit Legal Centre NSW

Consumer Credit Legal Centre (NSW) Inc (CCLC) is a community-based consumer advice, advocacy and education service specialising in personal credit, debt and banking law and practice. CCLC operates the Credit & Debt Hotline, which is the first port of call for NSW consumers experiencing financial difficulties. We provide legal advice and representation, financial counselling, information and strategies, and referral to face-to-face financial counselling services, and limited direct financial counselling. CCLC also operates the Insurance Law Service, a national service assisting consumers with disputes with their insurance company.

A significant part of CCLC's work is in advocating for improvements to advance the interests of consumers, by influencing developments in law, industry practice, dispute resolution processes, government enforcement action, and access to advice and assistance. CCLC also provides extensive web-based resources, other education resources, workshops, presentations and media comment.

Contact: Karen Cox, Coordinator, 02 8204 1340 or karen.cox@cclcnsw.org.au

Financial Counselling Australia

Financial Counselling Australia is the peak body for financial counsellors in Australia. FCA's members are each of the State and Territory financial counselling associations.

Financial counsellors provide information, support and advocacy to consumers in financial difficulty. Their services are free, independent and confidential. Financial counsellors work in not-for-profit, community organisations.

Financial counsellors frequently see clients who have payday loans. A survey of over 300 financial counsellors undertaken by FCA in 2011 documented the harm caused to clients by these loans.

Community Information & Support Victoria

Community Information & Support Victoria (CISVic) is the peak body for the community information and support sector in Victoria. CISVic provides operational support, sector development, representation and advocacy for the information and support sector. CISVic also engages in research & data collection across a range of social and welfare issues that impact on vulnerable families and individuals.

Consumer Credit Legal Service (WA) Inc

Consumer Credit Legal Service (WA) Inc. is a community legal centre which provides specialist legal advice to consumers on consumer credit matters, particularly where consumers may have disputes with their lenders.

Financial Counsellors Association of NSW Inc

Financial counsellors in New South Wales are accredited with the Financial Counsellors' Association of NSW Inc (FCAN). There are strict rules as to who may be a financial counsellor, primarily that financial counsellors hold no allegiance to the credit industry and act solely out of interest for the well-being of the consumer. Only financial counsellors who are not funded by, or employed by, credit providers are eligible for membership. Service provision must also be free of charge. Financial counsellors must have successfully completed an accredited training program and continue to attend a specified amount of training each year. Financial counsellors must also have regular supervision from an FCAN accredited supervisor and must be covered by a professional indemnity insurance policy.

As well as supporting and educating the client in various forms, a financial counsellor can provide the following for their clients:

- A full assessment of their financial situation, including regular income and expenditure, assets and liabilities.
- Information as to entitlements to government forms of assistance.
- Information and options for change and improvement.
- The ability to negotiate on behalf of the client with credit providers, government agencies and other business providers.
- Information on credit laws, the debt recovery process, bankruptcy and other areas of legislation such as superannuation, insurance and harassment to name a few.

Financial counselling is a worthwhile and valuable community service that is able to empower and assist clients to gain control of their financial situation.

Flemington & Kensington Community Legal Centre

The Flemington & Kensington Community Legal Centre Inc. (FKCLC) seeks to ensure that people in the community have equal access to justice. We provide free legal advice and

casework service to community members and community legal education to groups and local services.

Footscray Community Legal Centre

Footscray Community Legal Centre and Financial Counselling Service is a non-profit, community managed incorporated association. The Centre has a Legal Service and a Financial Counselling Service. Our purpose is to address systemic injustice by providing free legal and financial counselling services on an individual level and more broadly through community education, law reform and advocacy. We assist people who live, work or study in the City or Maribyrnong. Our service gives priority to those who cannot afford a private lawyer and/or do not qualify for Legal Aid.

Redfern Community Legal Centre

Redfern Legal Centre (RLC) is an independent, non-profit, community-based legal organisation with a prominent profile in the Redfern area. RLC has a particular focus on human rights and social justice. Our specialist areas of work are domestic violence, tenancy, credit and debt, employment, discrimination and complaints about police and other governmental agencies. By working collaboratively with key partners, RLC specialist lawyers and advocates provide free advice, conduct case work, deliver community legal education and write publications and submissions. RLC works towards reforming our legal system for the benefit of the community.

<u>RLC's work in Credit & Debt</u>

RLC identifies economic rights as important in the attainment of a just society. RLC has long recognised that, without the ability to exercise their economic rights, people are unable to maintain other rights. Economic rights are essential to effective and productive participation in society, including keeping families together, safe housing, jobs, and freedom. For this reason, RLC has continued to emphasise casework delivery to people in relation to banking, credit and debt problems. RLC provides specialist credit and debt face-to-face and telephone advice services.

RLC also provides a support service to financial counsellors in NSW, whereby financial counsellors are able to call or email our credit and debt solicitors to obtain legal information and assistance as they need it.

Good Shepherd Microfinance

Good Shepherd Microfinance delivers programs in partnership with more than 228 accredited providers at over 400 locations around Australia, making this the nation's largest microfinance response. Since 1981, Good Shepherd Microfinance has contributed towards maintaining and enhancing social participation by providing safe, fair and affordable credit to people who face financial exclusion and are vulnerable to experiencing profound crisis. Underpinned by the basic principles of trust, respect and non-judgement of people and their financial circumstances, these small and no interest loan programs enable people to build assets, engage in community life and/or find, or keep, a job. To facilitate and further build upon this leadership role in the Australian microfinance space, 2011 sees the celebration of Good Shepherd Microfinance as a new, independent agency.

The St Vincent de Paul Society
The St Vincent de Paul Society is a volunteer-based organisation operating in every state and territory with nearly 50,000 members and volunteers committed to the work of social assistance and social justice. We are accountable to the people in our community who are marginalised by structures of exclusion and injustice.

The Salvation Army - Moneycare

The Salvation Army has been offering caring support for Australians at every stage of life for 131 years. The Salvation Army is one of the largest providers of social services, material aid, crisis support, and disaster relief in Australia. Just as at the beginning, The Salvation Army sees its mission to be a combination of Christian witness and social ministry. The Salvation Army Helps over 1 million Australian each year. Services provided include Community Welfare Centres, Crisis Accommodation, Moneycare financial counselling and a no interest loan program.

South Australian Council of Social Service
The South Australian Council of Social Service (SACOSS) is the peak non-government representative body for the health and community services sector in South Australia. SACOSS believes in justice, opportunity and shared wealth for all South Australians and has a strong membership base representing a broad range of interests in the social services area. Our core activities include analysing social policy and advocating on behalf of vulnerable and disadvantaged South Australians; providing independent information and commentary; and assisting the ongoing development of the health and community services sector.

The South Australian Financial Counsellors Association
The South Australian Financial Counsellors Association (SAFCA) is the peak body for financial counsellors in Australia. SAFCA promotes protection, fairness and equity for consumers in credit and debt recovery practice and legislation. SAFCA's vision is to help alleviate poverty in South Australia by providing key leadership in advancing the financial counselling sector.