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Submitted via fsi.gov.au

Dear Panel Members

Financial System Inquiry Interim Report

The Consumer Action Law Centre (**Consumer Action**) welcomes the opportunity to comment on the Financial System Inquiry Interim Report.

We welcomed the panel's interim report, particularly that fairness, as much as stability and efficiency, are important objectives for the financial system. We strongly support the panel's comments at page 3-50 that the financial system must meet the following five outcomes if it is to meet customer needs:

- Consumers should have access to products and services that help them meet their financial needs;
- Consumers should have access to the information, advice and education necessary to make effective decisions;
- Consumers should have confidence and trust in the financial system and be able to expect fair treatment;
- Financial services and products should meet the purposes for which they are sold; and
- Consumers should have access to timely, low-cost and efficient dispute resolution and remedies.

Consumers expect the financial system to be based on mutual trust, so that financial promises are delivered in accordance with their needs and expectations. From the consumer perspective, this means that financial system should deliver financial products that are simple, safe and fair. It also means that sales and distribution methods (including product disclosure and financial advice) should be honest, clear, free of conflicts of interest and of high quality.

We also submit that financial products and services need to deliver consumers real value. That is, consumers should be sold only the financial products that they need; financial products sold should be proportionate to the degree of risk a consumer is in a position to bear; and both financial products and their distribution should be based on minimum conduct standards. Markets should be based on effective, fair and responsible competition to create incentives for businesses to improve and further benefit consumers.

Our particular concern is for low-income, vulnerable or financially disadvantaged consumers. For these groups, an 'error of judgment' in the modern financial marketplace can have far-reaching consequences for their financial and general wellbeing. While not all risk can be ameliorated, the financial system should promote fairness and offer adequate protection for vulnerable consumers.

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

ABN 37 120 056 484 ACN 120 056 484

Summary of Recommendations

Banking Competition

1. that consumers are consulted in the development and implementation of the new national payments platform and that it be subject to oversight by Government to ensure it delivers public outcomes;
2. that should Government intervene to level the playing field between big and small banks, this should be complemented by policies to allow consumers to 'activate' competition, including policies that reduce switching costs and policies that responding to demonstrated consumer behavioural biases;
3. that no further reforms be considered in relation to consumer credit reporting until the effectiveness of recent reforms have been determined;
4. that lenders mortgage insurance, and its impact on mortgage lending competition and consumer outcomes, be subject to an independent inquiry;
5. that all payment systems should be subject to a regulatory system that has as its objectives: stability, innovation, competition, and consumer outcomes;

Consumer Outcomes

6. that there is recognition that effective disclosure is necessary but not sufficient to protect consumers;
7. that consumer disclosure regulation be based on the following principles:
    a. that disclosure is comprehensible;
    b. that disclosure is designed so as to present the most important information most prominently;
    c. that disclosure include product warnings;
    d. that disclosure facilitate product comparison;
    e. that disclosure be based on an understanding of how consumers use disclosure documents and make decisions; and
    f. that all consumer disclosure documents be consumer-tested;
8. that disclosure principles not only require 'product attribute' disclosure, but 'product use' disclosure;
9. that all financial products and services, including insurance, be subject to a suitability requirement;
10. default products should be developed in key consumer markets, particularly insurance and basic banking;
11. that the financial services regulator should be given the power to initiate public market studies into particular financial products, services or practices. The framework should require public consultation and findings;
12. that the financial services regulator should be given the power to intervene in the design, marketing and sale of products where it is demonstrated that those products are causing consumer detriment, following a market study;
13. that regulation of sales and advice should not be limited to particular classes of products (such as those regulated under the National Consumer Credit Protection Act);
14. that advice should be labelled in a way that allows a consumer to understand the depth and quality of the advice, for example, whether it is based on a consideration of their personal circumstances or not;

15. that the inquiry acknowledge that insurance product design is a key cause of under-insurance in the Australian market, and make recommendations designed at improving product coverage;
16. that the inquiry consider the benefits of reorienting insurance to sharing of risk across the community;
17. that the inquiry acknowledge that payday loans are an essentially unsafe product, and that their growing use does not indicate a demand for credit that will be used to improve a borrower's financial situation;
18. that the inquiry direct the Federal Government to reconsider the 2012 Treasury consultation on reducing reliance on payday lending, and develop a comprehensive policy response;

Regulatory Architecture

19. that all self-regulation arrangements should be approved by the regulator, particularly industry codes of conduct;
20. that the regulator should have more flexible powers to investigate and respond to emerging business models currently outside the regulatory framework, including through broad anti-avoidance regulatory provisions;
21. that regulators funding should be obtained from industry levies rather than government appropriations;
22. that regulator accountability mechanisms be adapted to the overall objectives of the regulatory framework, rather than particular decisions of the regulator;
23. that a last resort compensation scheme be a key component of financial services regulation;
24. that consumers should have the right to receive their personal and transaction data from financial services businesses in a standardised and machine-readable format; and
25. that the panel consider in depth the risks to consumers and the financial system from the more sophisticated use of data by businesses to engage in consumer profiling and target marketing.

About Consumer Action

Consumer Action Law Centre is an independent, not-for-profit consumer organisation based in Melbourne. We work to advance fairness in consumer markets, particularly for disadvantaged and vulnerable consumers, through financial counselling, legal advice and representation, and policy work and campaigns. Delivering assistance services to Victorian consumers, we have a national reach through our deep expertise in consumer law and policy and direct knowledge of the consumer experience of modern markets.

Banking Competition

We are not as convinced as the Panel members that the banking market is competitive. While there may be jostling between the banks, this is not translating into consumers being any more capable of picking the best deal for them. For example, a 2011 survey by ANZ of customers who were not switching found that only 30 per cent were staying put because they are happy with their current provider. Other respondents are failing to switch because they were following someone else's advice (14%), or a 'lack of choice' (9%), or because of a lack of time or belief that 'they're all the same (9%).[1]

Improving competition in banking

Broadly, the panel can contribute to improved competition in the banking sector by encouraging a focus on providing tools that allow consumers to use their market power. Some more specific ideas are below.

<u>A more effective switching package</u>
The bank switching package introduced by the previous Labor government (while well intentioned) was not well designed. This package aimed to streamline switching by allowing a customer's 'new' bank to transfer all direct debits from the old account to the new one on behalf of the consumer. The critical flaw is that the switching service only applies to simple transaction accounts, and not any credit cards, mortgages or other financial products linked to the account. Given most people have their transaction account bundled with other products and services, the switching system fails to assist large proportions of banking consumers. Amending the switching service to allow it to also extend to these products will mean it is far more likely to be used.

The new national payments platform currently in development[2] offers even greater potential for allowing trouble free bank switching. We understand that this platform will allow consumers to have one unique account number that can follow them from bank to bank. Much like the introduction of fully portable mobile phone numbers, this will allow consumers to switch between providers without needing to disconnect and reconnect recurring payments. The payments platform appears to being developed and implemented by the finance industry. We suggest there must be public policy oversight by Government, and consultation with consumer representatives, to ensure it delivers consumer outcomes.

Recommendation 1:

- That consumers are consulted in the development and implementation of the new national payments platform and that it be subject to oversight by Government to ensure it delivers public outcomes.

<u>An active competition regulator with a mandate</u>
We note that ASIC has encouraged adoption for a 'competition objective' to support its other objectives. We support this, and believe such an objective could particularly sit well with regulator market study powers, and other product intervention powers. This is described further below.

<u>Levelling the playing field between big and small banks</u>

[1] *Adult Financial Literacy in Australia December 2011: Full Report of the results from the 2011 ANZ Survey*, p 39.
[2] See http://www.apca.com.au/about-payments/future-of-payments/new-payments-platform

The interim report recognizes that small banks are at a competitive disadvantage to larger institutions due to prudential risk weightings and wholesale funding costs. We understand that larger banks have access to cheaper funding because it is considered that Governments would intervene should any of them fail and, as such, the market demands a lower return on investment. These large banks are considered 'too big to fail'. We encourage the Panel to publicly research the extent of this problem; in our assessment, it would seem that Governments would intervene if any bank failed in Australia, not just the large banks.

Should this problem be demonstrated, we would encourage Government intervention to level the playing field. A more level playing field would boost competition and serve to benefit consumers. However, should this problem be addressed by additional costs being applied to banks considered 'too big to fail' (for example, increased capital requirements or a large bank levy), we submit that measures should be adopted to ensure these increased costs aren't merely passed on to consumers. A bank levy should only be adopted if it practically allows smaller banks (free from the levy) to improve service offerings and boost competition. For this to occur, we submit that there must be consideration of actions on the demand-side of the market to improve the effectiveness of competition, including policies to reduce switching costs and developing strategies to deal with the demonstrated behavioural biases of consumers in competitive markets (such as inertia).

Recommendation 2:

- Should Government intervene to level the playing field between big and small banks, this should be complemented by policies to allow consumers to 'activate' competition, including policies that reduce switching costs and policies that responding to demonstrated consumer behavioral biases.

Personal lending competition—credit reporting reform

The interim report suggests policy options relating to consumer credit reporting assuming they may improve competition in personal lending. We strongly oppose any recommendations to further reform the consumer credit reporting system.

In March 2014, a new Part IIIA of the *Privacy Act 1988* (Cth) came into effect to provide for more comprehensive credit reporting. This reform followed significant consultation beginning with a 2008 Australian Law Reform Commission Inquiry followed by a number of parliamentary inquiries. It also included consultation with the lending industry, through the establishment of the Credit Reporting Code of Conduct. The reforms enacted are significant, adding many new data sets including a consumer's repayment history information.

We submit that no further reforms are required, given these reforms are so recent and because we are yet to determine their full impact on the financial system. The interim report suggests one option is to make the sharing of consumer credit reporting information mandatory. This ignores current industry efforts to develop reciprocity and data standards. We submit that should such industry cooperation proceed, it should be subject to ACCC processes to ensure that it does not in fact reduce competition and that there is a strong public benefit.

More broadly, we have concerns about the expansion of consumer credit reporting information—not only from a privacy perspective, but from a consumer risk perspective. There is an obvious incentive for financial institutions to use personal information to identify not only individuals' needs, but also their vulnerabilities—for example, banks and credit providers are able to use consumer data to profile and segment customers to better target credit card offers to those who don't pay back their full balance within the interest period. While the new privacy laws prohibit the use of credit reporting information for direct marketing purposes, the law does allow 'pre-screening' which enables credit reports to be used to filter direct marketing offers. It is also likely that credit reporting information obtained for credit assessment purposes will contribute to data which credit providers retain on their customers, and would therefore be available for marketing to those customers. We believe that any further policy discussion of consumer credit reporting reforms must consider these risks.

Recommendation 3:

- That no further reforms be considered in relation to consumer credit reporting until the effectiveness of recent reforms have been determined.

Lenders mortgage insurance

The interim report includes policy options designed to expand the use of lenders mortgage insurance, purportedly to increase competition in mortgage lending. We submit that lenders mortgage insurance offers the industry much more than it offers consumers, and that further inquiry is needed into the effectiveness of this product in improving consumer outcomes.

A key problem relating to lenders mortgage insurance for consumers is that it is paid for by consumers (the interim report states that a quarter of new mortgages are covered by lenders mortgage insurance) but it does not cover them—it covers the lender. This results in consumer confusion and cost. Consumer complaints about lenders mortgage insurance at the Credit Ombudsman tripled in 2012/13.[3] The Credit Ombudsman states that complaints are generally arise because

> where a loan is not fully repaid from the proceeds of the sale of the security property and the lender makes a claim on its mortgage insurance policy for the shortfall, the right to recover the shortfall is generally assigned to the lenders' mortgage insurance provider.[4]

We submit that given this right of subrogation, it is misleading to call this product 'insurance' when bought by consumers.

Efforts advanced by the previous Labor Government to improve consumer understanding of LMI stalled with the change of government. It was proposed that a key fact sheet would be introduced to better explain this product to consumers, and we think such a reform would be worthwhile. We do not think that this goes far enough, however, and we suggest two reforms which would reduce the consumer detriment associated with lenders mortgage insurance:

- abolish the right of subrogation—this would ensure the insurer actually bears the full risk being paid for, a more efficient outcome compared to a vulnerable consumer who has been foreclosed bearing this risk;

[3] There were 20 complaints regarding lenders' mortgage insurance in 2010/11 and 2011/12 (COSL 2012 Annual Review, p 23) and 58 in 2012/13.

[4] COSL Annual Report on Operations, p 29.

- making lenders mortgage insurance portable and refundable—should consumers switch mortgages during the period of insurance, then they should be entitled to a refund of a pro-rata amount of the premium and/or be able to 'port' the insurance to a cover a new mortgage.

Recommendation 4:

- That lenders mortgage insurance, and its impact on mortgage lending competition and consumer outcomes, be subject to an independent inquiry.

Payments

Our overarching comment is that payment system regulation needs a clearer focus on consumer outcomes. The debate over whether to favour stability or innovation in payments tends to attract most attention while problems that should be relatively straightforward to address remain unsolved.

For instance, credit card surcharges seem reasonable and transparent in some transactions, while in others (like airlines, taxis and event ticketing) they seem persistently to be far too expensive, and not disclosed until it is practically too late for consumers to back out. Another example is recurrent payments. Most consumers use regular direct debit arrangements, but very few would be aware that there is a difference in regulation based on whether the payment is coming from their transaction account or their credit (or scheme debit) card. Consumers are rightly baffled when they find that recurrent payments made from a credit card are much more difficult to cancel than payments from a transaction account, and credit card recurrent payments can continue to be made even after the card itself is cancelled. There is no reason why the two types of payment should behave differently.

We welcome the interim report's focus on competition in payment systems. As outlined in our initial submission, our casework experience is that consumers experience problems in payments and that challenges in resolving these problems arise particularly due to the regulatory framework focusing more on the needs of industry participants rather than outcomes for consumers.

From a consumer perspective, we consider there may be value in banning payment surcharges. After all, the payment system is an input into the particular good or service being sold, and it is not common practice for every input into a good or service to be separately charged. Separately charging for inputs into goods and services can cause consumer confusion, may be misleading and may be in breach of component pricing laws in the Australian Consumer Law.

While we understand that surcharging was designed to inform consumers about the costs of using particular payment systems (and so allow them to make an informed decision about which system offers them best value), we do not believe that it is achieving this aim. We do not believe that surcharging has given many consumers a good understanding of the price and features of different payment systems. We suspect that most consumers choose one method over another due to rules of thumb or because they feel they have no other choice (we discuss both scenarios further below). There is also no surcharging for cash payments, which gives an inaccurate signal about the true cost of competing payment systems.

Should payment surcharging continue, we reiterate that there must be a regulator responsible for ensuring surcharging relates to reasonable costs of providing the payment service. Without regulatory oversight, the existing rule (that surcharges shouldn't exceed the reasonable cost of acceptance) is meaningless and widely ignored.

We also submit that incentives should be placed into the regulatory framework so that payments are directed to the least cost and most efficient system,[5] and that consumers should be made aware of the service benefits (and costs) of using particular systems.

In our assessment, consumers are directed towards particular payment systems not due to surcharging, but due incentives from financial institutions or a lack of options. For example, most online sales still require use of scheme credit or debit payment systems; while some particular online sites push consumers to use associated payment systems (such as eBay and PayPal). Further, financial institutions encourage consumers to use their credit or scheme debit cards to make payments, by imposing fees or limiting fee-free transactions using eftpos, or through the offering of reward programs—which may offer limited, if any, real reward to consumers who use them.[6]

We note that there are service benefits associated with particular payment methods—for example, payment through credit cards or scheme debit cards gives consumers “charge back” rights. That is, consumers have the right to have a transaction “charged back” where, for example, goods or services are not provided, or the goods or services are not as were described. Our casework experience is there is very limited understanding about these sort of service benefits, and that this is likely to limit consumers’ uptake of their rights. This lack of awareness will also limit the extent to which consumers are choosing payment systems based on the actual service offered.

We note that this is a very complex area given the multiple parties involved (payment system providers, financial institutions, retailers and merchants, and consumers). It seems to us that there needs to be a much more detailed inquiry by a policy-maker or regulator that has as its focus competition and consumer protection. A particular concern with the current regulatory framework is that the Payments Systems Board of the Reserve Bank of Australia focuses primarily on efficiency in the payment system, and not on whether efficiency delivers good consumer outcomes. As noted in our initial submission, any such reform of the payments system needs to involve consumer advocacy and representation.

Recommendation 5:

[5] We think that there is opportunity here to particularly influence the incentives of merchants and financial institutions.

[6] CHOICE (citing research by Canstar) recently reported that card reward programs 'deliver little or nothing to consumers who spend less than $18,000 a year', and that a consumer spending $12,000 would likely have any reward cancelled out by annual fees.

- That all payment systems should be subject to a regulatory system that has as its objectives: stability, innovation, competition, and consumer outcomes.

Consumer Outcomes

Disclosure

We support the panel's observation that

> The current disclosure regime produces complex and lengthy documents that often do not enhance consumer understanding of financial products and services, and impose significant costs on industry participants.[7]

We also agree with the panel's two reasons offered why disclosure is not always effective:

- that disclosure may not be the best tool for solving a particular market problem; and
- that, even where disclosure is an appropriate response, disclosure documents may not be understood by consumers.

The paper goes on to ask for views on the costs, benefits and trade-offs of a number of options, such as retaining the status quo, improving existing disclosure techniques, and introducing product intervention powers.

Put briefly, our response is that all of the options on the Panel's list should be available to governments and regulators so that they have the ability to choose the most appropriate tool when addressing a specific market problem.

It is not possible to say that one of these options is the best option for the whole financial system for the indefinite future. This type of logic led us to the current position—the belief, encouraged by the Wallis review, that disclosure is the best approach unless proven otherwise. We urge the panel to avoid making the same mistake through this inquiry. Rather than throwing its support behind one option, we recommend that the panel supports the principle that regulators be given the flexibility to respond to market problems with the approach that is most effective in the circumstances.

Designing effective disclosure

With that principle in mind, disclosure should only be chosen where it is thought to be the most effective response to a problem. Where it is chosen, real thought should go into designing and testing the disclosure to ensure that it works.

By emphasising the weaknesses of disclosure as a consumer protection measure, the interim report perhaps implies that we can 'do away' with disclosure entirely. We reject this idea. Access to information is a core consumer right. The disclosure question should instead be: when and how should information be provided to consumers?

[7] Interim report, 3-56.

We submit that the full terms and conditions of any financial product marketed to consumers must be publicly available. Publication could be on the internet. However, consumers should be informed prior to purchase of a financial product of key and important information about that product. The key here is what is required for consumer understanding, and not just that communication is provided by the product provider, salesperson or adviser. In mandating product disclosure, policy-makers and regulators have the opportunity to learn from research from consumer behavioural studies and behavioural economics. We also submit that any disclosure document must be comprehensively consumer-tested for consumer understanding and comprehension.

In summary, good disclosure:

- is comprehensible;
- presents the most important information most prominently;
- includes product warnings;
- facilitates product comparison; and
- is based on an understanding of how consumers use disclosure documents and make decisions.

There is also a need to move to more use of ‘product use’ disclosure. Most disclosure is ‘product attribute’ disclosure, whereby information is communicated about the attributes or features of the product. Product use information is based on historic use-pattern information collected on individual consumers, or on consumers as a whole.

As argued by Oren Bar-Gill in his book, *Seduction by Contract: Law, Economics and Psychology in Consumer Markets,* a mixture of product attribute and use information is necessary for disclosure to be meaningful:

> Optimal disclosure design should consider the advantages of combining product-use information with product-attribute information. For example, providing information on the number of late payments made during the past year is helpful. Providing information on the total amount of money paid in late fees during the past year is even more helpful. This disclosure combines product-use information (the number of late payments) with product-attribute information (the magnitude of the fee).[8]

Timing is also important when designing disclosure mandates, specifically when use of the information is concerned. For example, the minimum payment warning on credit card statements, introduced in 2010 as part of reforms to the *National Consumer Credit Protection Act*, mandates disclosure on statements rather than in documents provided before entry to the contract. This makes sense as it is the monthly statement that consumers regularly review, not the initial product disclosure documents.

That said, we also believe that product-use disclosure is relevant in advertisements and solicitations, so as to encourage more effective competition. This could involve requiring financial institutions to release transaction data held in a machine-readable format, which would enable consumers to take this information to other product issuers and get a total price, based on their

[8] Oren Bar-Gill, 2012, Seduction by Contract: Law, Economics and Psychology in Consumer Markets, Oxford University Press.

use patterns. The release of such data could also facilitate intermediaries such as comparison sites.

Recommendation 6:

- That there is recognition that effective disclosure is necessary but not sufficient to protect consumers.

Recommendation 7:

- That consumer disclosure regulation be based on the following principles:
  - that disclosure is comprehensible;
  - that disclosure is designed so as to present the most important information most prominently;
  - that disclosure include product warnings;
  - that disclosure facilitate product comparison;
  - that disclosure be based on an understanding of how consumers use disclosure documents and make decisions; and
  - that all consumer disclosure documents be consumer-tested.

Recommendation 8:

- That disclosure principles not only require 'product attribute' disclosure, but 'product use' disclosure.

Product suitability

We support the suggestion in the interim report that all products be subject to a suitability requirement. The report notes that credit providers and credit assistance providers are already subject to an obligation that the credit product be 'not unsuitable' for the consumer, and that a 'best interests duty' is imposed on financial advisers. However, there is no such obligation in relation to issuers of other financial products, including insurance.

There are currently only very limited obligations requiring financial products and services to be 'fit for purpose'. Section 12ED of the *Australian Securities & Investments Commission Act 2001* (Cth) provides that if a person expressly or impliedly makes known the particular purpose for which the financial services are required, or the result that he or she desires the services to achieve, there is an implied warranty that the services and any materials will be reasonably fit for that purpose or are of such a nature and quality that they might reasonably be expected to achieve that result. The exception is where the consumer does not rely on, or it is unreasonable for the consumer to rely on the supplier's skill or judgment. There is also an entire carve out for insurance.[9]

The more important limitation of this provision is that it provides for an implied warranty in the contract between the consumer and the provider—it does not give the regulator any power to act for a breach of this provision whatsoever. Further, we are not aware of any judicial, regulatory or ombudsman guidance relating to section 12ED, so we question the extent to which it has been acted as a suitability requirement in practice.

[9] Section 12ED(3), ASIC Act.

Unlike the "not unsuitable" test in the credit law, the 'fit-for-purpose' provision does not appear to require a product issuer or adviser to investigate the consumer's personal circumstances. As argued by Gail Pearson in her article, *Reading Suitability against Fitness-for-purpose,*

> a suitability obligation is emphatically directed towards the person's individual circumstances. For this reason, a financial product may be fit for a purpose stated by an individual but may not be suitable for the circumstances of that individual.[10]

We submit that all regulation of financial products and advice should be subject to a suitability provision. This particularly relates to insurance where (as described below) it appears that products regularly leave consumers under-insured. We note that insurance advisers in the United Kingdom are required to comply with a suitability rule—regulations state that:

> An insurance intermediary must take reasonable steps to ensure that, if in the course of insurance mediation activities it makes any personal recommendation to a customer to buy or sell a non-investment insurance contract, the personal recommendation is suitable for the customer's demands and needs at the time the personal recommendation is made.[11]

It was the widespread breach of this provision by credit providers selling payment protection insurance (the UK term for consumer credit insurance) that led to the recent scandal and mass compensation for consumers who had been mis-sold this insurance.

Recommendation 9:

- That all financial products and services, including insurance, be subject to a suitability requirement.

Default products

The interim report also discusses the value of default products, which builds on the notion that financial products should be suitable. This acknowledges the reality that many financial products and services are essential for consumers, but are so complex or unfamiliar that many consumers find it difficult to choose the product that is best for their needs (or they avoid buying a product at all). The impact of this complexity can range from the relatively minor (a customer paying a little more for a credit card than they otherwise would) to the catastrophic (a family cannot replace their home because, unknown to them, their insurance policy excludes cover for flood).

The rollout of safe defaults could ideally be led by industry but may warrant government intervention in some cases. Some options include:

- *An effective 'standard cover' regime in insurance*
  Sections 35 and 37 of the *Insurance Contracts Act 1986* create a 'standard cover' regime, which seeks to prevent insurers from relying on non-standard or unusual terms without informing the insured of the effect of those terms before the insured enters into an insurance contract. The rationale for this provision was to counter widespread consumer

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[10] Gail Pearson, 'Reading Suitability against Fitness-for-purpose—an evolution of a rule', Sydney Law Review: http://sydney.edu.au/law/slr/slr_32/slr32_2/Pearson.pdf
[11] ICOB 4.3.1R, see http://financial-ombudsman.org.uk/publications/technical_notes/ppi/rules-codes.html

ignorance regarding the extent of their policy coverage.[12] However, insurers can satisfy the requirements of sections 35 and 37 by simply giving written notice of unusual terms before the consumer enters the contract—even if that notice is buried in the product disclosure statement's fine print. Given this, these provisions are clearly incapable of addressing the problem it was designed to solve.

An effective standard cover regime might require all retail insurers to offer policies in home building, home contents and motor vehicle that meet a minimum standard of cover. Consumers struggling to choose a policy could select the accredited 'standard cover' policy knowing that it covers the most prevalent risks. This would also promote competition, by assuring consumers that by switching they won't inadvertently lose coverage for particular risks.

- *No frills or zero fee banking accounts for low income consumers*
  Consumers applying for a transaction account with a bank could be offered a zero fee account by default if the bank is aware that they (for example) are solely reliant on Centrelink benefits or hold a low income health care card. We recognise that many banks already have these accounts, and promote them to their low income customers. However, banks could be more proactive—for example identifying social security recipients from benefit deposits and placing these customers into default no-fee basic bank accounts.

Recommendation 10:

- Default products should be developed in key consumer markets, particularly insurance and basic banking.

Product intervention and market study powers

Regulators should be given powers to intervene in the design, marketing and sale of products where it is demonstrated that those products are causing consumer detriment. We note that the interim report is wary of increased regulation of product features, finding that 'any substantial shift in the regulatory regime would require compelling evidence to support it'. Our response is that a decision to maintain current regulatory settings which are shown to be ineffective should also be supported by compelling evidence.

One model of implementing product intervention powers is to link them to 'market study' powers, which have been suggested by a number of submissions. The regulator might be required to undertake a public market study into a particular financial product or practice and thereby make a case for use of product intervention powers could be used (or other rules relating to things like distribution, sales, or marketing.

Should the regulator have a competition objective, this would require the regulator to only impose a rule that would promote, or not limit, competition. It would also allow detailed consideration of consumer behaviour in the relevant market. Studies of consumer behaviour suggest that behaviour can change depending upon particular market practices or idiosyncrasies. This model would enable the development of rules and requirements that are suitable for the particular issue at hand, without limiting the entire marketplace or stifling productive innovation. For example, the UK Financial Conduct Authority's Market Study into 'add-on' insurance from earlier this year

[12] Australian Law Reform Commission (1982) *Insurance Contracts*, Report No. 20, p 44.

proposed (among other things) that there must be a delay between the sale of the headline product and the add-on insurance, and banning pre-ticked boxes.[13] The strength of these proposals is that they do not place restrictions on the products themselves, but simply seek to eliminate problematic sales practices.

We also believe that regulators may not even have to use their product intervention or rule power—the very act of undertaking the market study, and the associated attention on good practices within a market, will encourage businesses to improve. A rule-making power is an important 'stick', however, that is necessary to provide incentives for good practice.

Recommendation 11:

- That the financial services regulator should be given the power to initiate public market studies into particular financial products, services or practices. The framework should require public consultation and findings.

Recommendation 12:

- That the financial services regulator should be given the power to intervene in the design, marketing and sale of products where it is demonstrated that those products are causing consumer detriment, following a market study.

Distribution—sales and advice

A significant problem with the regulation of credit assistance[14] and financial advice is that it is linked with the distribution of credit products and financial products respectively. This means that the focus of regulation is on the distribution of the product, rather than being about advice and assistance that is in consumers' interests.

Our submission does not focus on regulated financial advice and the discussion in the interim report about how to improve the quality of financial advice. We are concerned, however, about advice and 'assistance' that falls outside the scope of regulated credit assistance and financial advice. In our initial submission, we referred to for-profit financial difficulty businesses which included credit repair, budgeting services and bankruptcy services. As these businesses are not promoting a regulated 'credit product', nor are they engaging in 'credit assistance', they fall outside the regulatory regime.

A similar problem occurs in relation to property investment advice and spruiking, which appears to be growing in the wake of improved regulation for financial advice.[15] There have been many inquiries which have recommended that property investment advice be regulated in the same way as financial advice, and we support this.[16] We encourage the Panel to consider, in

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[13] Financial Conduct Authority (March 2014), *Market Study MS14/1: General Insurance Add-ons: Provisional findings of market study and proposed remedies*, p 8.

[14] Under the *National Consumer Credit Protection Act*

[15] See for example 'Crazy about Property: The Dangers of Hard-Sell Seminars', 9 August 2014, *Australian Financial Review*, http://www.afr.com/p/business/property/crazy_about_property_the_dangers_pWzddwPAaFI1dNbNWBpjnM

[16] See for example Parliament of Victoria, Law Reform Committee (2008), *Inquiry Into Property Investment Advisers and Marketeers: Final Report,* recommendation 8. http://www.parliament.vic.gov.au/images/stories/committees/lawrefrom/property_investment/final_report.pdf

recommendations about advice frameworks, that regulation focus on the nature of the advice and assistance given, the consumer risks involved, and not limit its scope to advice in relation to particular types of products.

We also agree with the discussion in the interim report about the need to better distinguish between different types of advice. Consumers need to know whether advice is based on their personal situation or not. If the communication is merely factual or general information, not based on a consumer's personal situation, we submit that it must be labelled in a way to allow a consumer to understand that.

Recommendation 13:
- That regulation of sales and advice should not be limited to particular classes of products (such as those regulated under the National Consumer Credit Protection Act).

Recommendation 14:
- That advice should be labelled in a way that allows a consumer to understand the depth and quality of the advice, for example, whether it is based on a consideration of their personal circumstances or not.

Underinsurance

While consumers will at times choose to self-insure or deliberately under insure, the more pressing problem is the ways that insurance products themselves lead to systemic under-insurance. One example, mentioned in our initial submission, is sum insured home building insurance. Another is unfair or unclear exclusions to cover.

Responses could include:
- efforts to improve competition, such as including last year's premium on insurance renewal statements and greater rights for consumers to get explanations of why premiums have increased;
- improving standardisation, such as through a more effective 'standard cover' regime, discussed above;
- application of unfair terms protections to insurance to give insurers impetus to remove capricious and unnecessary exclusions
- revisiting the recommendation of the Natural Disaster Insurance Review that a national reinsurance facility be established to provide premium discounts to high-risk policies, recognising that some risks are too significant to expect private insurers to cover and the need to improve the affordability of insurance.

It may also be useful to have a broader community debate about the purpose of insurance. The insurance industry is increasingly capable of individually rating risks as technology improves and insurers get hold of more consumer data. It is said that this allows insurers to better control the level of risk they take on, and ensures consumers are given better information about the risk they face (which can then be avoided or mitigated). But in reality we do not think this increasingly granular assessment of risk creates benefits for consumers. Consumers who have their home building premium increase by many thousands of dollars because of a changed assessment of flood risk by the insurer are not necessarily capable of reducing their flood risk or moving to a safer area to make insurance more affordable. They are left only the option of non-insurance. Others who find that their risk is considered far higher than their neighbour's—but are not told why this is the case, and have no capacity to challenge this assessment—are also unable to respond to the signals sent by the market. We believe there is an argument for a return to the original philosophy of insurance in sharing risk across the community.

Recommendation 15:

- That the inquiry acknowledge that product design is a key cause of under-insurance in the Australian market, and make recommendations designed at improving product coverage.

Recommendation 16:

- That the inquiry consider the benefits of reorienting insurance to sharing of risk across the community.

Access to credit

Demand for safe small amount credit

We agree with the panel's observation that 'access to reasonably-priced small amount credit may have individual and societal benefits'.[17]

Individuals on low incomes, like all people, will occasionally need to use credit to smooth large expenses (such as unexpected medical expenses or car repairs) and pay for expensive essential items (like white goods and motor vehicles). Lack of access to these goods and services prevents people from accessing an acceptable standard of living and can prevent people from contributing to the economy.

However, the reality is that those on very low incomes may not be able to afford to access commercially priced credit without experiencing financial hardship. Consumers solely reliant on Centrelink benefits may even have difficulty repaying a Centrelink Advance, despite the fact that no interest or fees are payable, amounts are relatively small and repayment is spread over six months. It follows that there is a genuine need for schemes like the No Interest Loans Scheme (**NILS**) and Step Up loans to make credit available to low income consumers at lower than market price to cover essential expenses.

While we agree that there is an undersupply of responsible small amount loans, it is not safe to assume that the volume loaned by payday lenders gives an accurate indication of actual demand, for two reasons.[18]

The first is that payday loans are predominantly used to pay for basic, recurrent expenses like bills, rent or groceries (rather than for building assets). Consumer Action's 2010 research *Payday Loans: Helping Hand or Quicksand* found that basic living expenses made up 75 per

[17] At 3-81.
[18] The panel seems to make this assumption at page 3-81.

cent of borrowing.[19] More recently, RMIT's *Caught Short* found that the seven reasons most commonly cited by borrowers for taking out their first payday loan were 'regular, weekly-type needs and expenses'.[20] These loans should not be seen as indicating demand for small amount credit because more often than not they will be irresponsible. A loan for day to day expenses like groceries or utilities bills will usually leave the borrower in a worse financial position because it creates a new liability without any long term benefit. Demand for payday loans to cover things like groceries, medicine or utilities bills indicates a need an improved social security and concessions system, not a need for credit.

The second reason is that payday loans actually drive their own demand by creating repeat borrowing. If a person who is already having trouble making ends meet takes out a payday loan to meet recurrent expenses, they will necessarily have trouble repaying the loan. This prompts the borrower to take out another payday loan which ultimately creates more debt.[21]

<u>Meeting the demand for small amount loans</u>
As well as expanding not for profit microfinance programs, there are other options for meeting (or reducing) demand for small amount loans. We provided a detailed submission to Federal Treasury in 2012 who consulted publicly on this issue.[22] Unfortunately, there were no public outcomes from the consultation. Some responses are below.

Improving access to concessions
Research into the drivers for payday lending has shown that loans are often taken out to cover large, unexpected utility bills.[23] Utilities concessions, hardship arrangements and Utilities Relief Grants are made available to help low income consumers afford energy bills, though in our experience, consumers face numerous barriers in accessing these programs.[24] This experience reflects a system wide issue identified by the Australia Institute in 2010 when it found that 168,000 Australians were missing out on $623.8 million of government assistance because a lack of awareness that assistance was available, complexity of claim procedures, and stigma.[25] It follows that improving access to utility affordability programs could significantly reduce demand for fringe credit, without requiring any further funding for programs like NILS.

[19] Zac Gillam (2010), *Payday Loans: Helping Hand or Quicksand?*, Consumer Action Law Centre. Page 6.
[20] Marcus Banks (2011), *Caught Short: Exploring the role of small, short term loans in the lives of Australians - Final Report*, RMIT University, Melbourne, pp 32.
[21] RMIT's *Caught Short* found that the third most common reason cited for taking out a loan was 'to pay back another loan': Final report p 34. It also reported that over half of the respondents to their study had taken out more than ten loans in the last two years, with most of those receiving over 20: p 37.
[22] Our submission is available here: http://consumeraction.org.au/submission-response-to-commonwealth-government-discussion-paper-on-reducing-reliance-on-payday-lending/
[23] For example, Banks 2011 found that 'bills' was the equal most common reason for taking out a payday loan: page 34. Gillam (2010) found that 21 per cent of payday loans were taken out to cover utility bills, second only to car repairs and registration (22.1 per cent): p 59.
[24] Our recent reports *Barriers to Accessing Utility Relief Grants* (http://consumeraction.org.au/report-barriers-to-accessing-utility-relief-grants) and *Problems with Payment* (http://consumeraction.org.au/report-problems-with-payment) both provide evidence that low income consumers are struggling to access energy affordability mechanisms that should be available to them.
[25] David Baker (2010) *Missing Out: Unclaimed Government Assistance and Concession Benefits*, Policy Brief No 14, p 3.

Improving access to responsible small amount loans from mainstream credit providers
We believe there is a role for mainstream commercial lenders to provide smaller personal loans (in the vicinity of $1,000 to $5,000, for example). These would be a product similar to loans offered by community development finance institutions[26], NAB's Step UP loan or ANZ's (now discontinued) Progress Loan. These loans are a key consumer product which is not generally provided by mainstream lenders. Mainstream providers instead encourage the use of credit cards (an inappropriate option for many consumers) for small amount credit.

While we think there is a role in this sector for both community finance and mainstream banks, we note that mainstream banks have an established distribution system that can provide access to many borrowers. Most community finance initiatives are limited to particular communities or locales, though there is scope for expansion. Any development of this market would need to be monitored to ensure lending is undertaken responsibly. It should be noted again that this kind of product would also not be an alternative to most payday lending, which is for smaller amounts and different purposes.

Centrelink advances
As well as microfinance like NILS, there would be benefit in improving Centrelink advance system so it is more fit for its purpose.

To our knowledge there is very little assessment of ability to repay an advance before it is granted. A key consideration for any review of the Centrelink Advance system would be to look at current assessment processes and whether they stack up against responsible commercial lending practice. For example, the larger advances for Pension recipients (up to around $1,000) have a standard 13 fortnight repayment period, meaning repayments of $74 a fortnight. This level of repayment can be unaffordable for some.

It may be worth considering whether there could be more flexibility in repayment periods of Centrelink Advances, perhaps allowing advances of up to $2000 over two years where appropriate. These repayments would be more in line with repayment amounts of community loan schemes. In addition, the advance payments could be much smaller, for example in the vicinity of $100 to $500 without onerous restrictions placed on access.[27] Recipients could be able to receive multiple such advance payments within a year.

Recommendation 17:

- That the inquiry acknowledge that payday loans are an essentially unsafe product, and that their growing use does not indicate a demand for credit that will be used to improve a borrower's financial situation.

Recommendation 18:

- That the inquiry direct the Federal Government to reconsider the 2012 Treasury consultation on reducing reliance on payday lending, and develop a comprehensive

[26] For more detail on the experience of CDFIs in Australia, refer to Alison Plant and Sue Warth (2013), *Community Development Financial Institutions Pilot Evaluation: Report*, http://www.dss.gov.au/our-responsibilities/communities-and-vulnerable-people/programs-services/financial-management-program/community-development-financial-institutions-cdfi-pilot-project/community-development-financial-institutions-pilot-evaluation
[27] A suggestion along these lines was made in the *Caught Short* interim report, page 22.

policy response.

Regulatory architecture

Self-regulation

We support effective self-regulation and there are important examples in the existing framework, for example the industry dispute resolution schemes and codes of practice or standards in some industries.

There are some key features of effective self-regulation schemes, including:

- Governance arrangements that involve equal numbers of consumer and industry representatives with an independent chair (as is the case for FOS, COSL and various code compliance monitoring bodies);
- Periodic external review (usually every three to five years); and
- Approval of arrangements by the regulator against agreed standards.

A particular benefit of such self-regulatory systems is that they can adapt to changing circumstances more quickly than regulatory requirements. For example, the EDR schemes have changed their jurisdiction a number of times following community and industry consultation.

One difference between the EDR schemes and industry codes of conduct is that it is mandatory for the EDR schemes to comply with the regulator's standards,[28] but it is not for industry codes of conduct.[29] This has meant that there are currently no industry codes that have been approved by the regulator. We think this is a key weakness of the regulatory framework, and approval by the regulator would improve consumer and community confidence in the self-regulatory scheme.

Recommendation 19:

- That all self-regulation arrangements should be approved by the regulator, particularly industry codes of conduct.

Regulatory framework

<u>The 'regulatory perimeter'</u>

At 3-99 the panel makes the observation that the regulatory perimeters could be re-examined to ensure they are targeted appropriately and can capture emerging risks. One business model which currently manages to skirt the perimeter are for-profit financial difficulty businesses (such as 'credit repair', debt agreement administrators and budgeting services). We discussed this business model in detail in our previous submission.

A re-drawing of the regulatory perimeters is needed to allow ASIC to regulate any business purporting to provide solutions regarding consumer credit, debt, insolvency and credit reporting.

[28] ASIC Regulatory Guide 139
[29] ASIC Regulatory Guide 183

But it is also necessary to give regulators more flexible powers to investigate and respond to emerging problems so that they are not prevented from responding to new problematic business models in the future. Market study and product intervention powers, along with general anti-avoidance provisions in the credit law will provide this kind of flexibility.

Recommendation 20:

- The regulator should have more flexible powers to investigate and respond to emerging business models currently outside the regulatory framework, including through broad anti-avoidance regulatory provisions.

Funding for regulators

We support the proposal to draw more regulator funding from industry levies. This has the benefit of making regulators more autonomous and more certain of the funding available to them. We note that ASIC has recently had to manage a significant cut in funding which its chairman has stated will reduce its capacity to undertake proactive surveillance. While there may well be government oversight over the level of funding received from industry levies, reliance on government funding results in peaks and troughs, inhibiting the ability of the regulator to plan long-term and be responsive to market needs. Moreover, consumers and investors are the ultimate losers of a resource-constrained regulator.

Recommendation 21:

- That regulators funding should be obtained from industry levies rather than government appropriations.

Regulator accountability

The interim report argues that giving regulators additional power to intervene in the design of financial products creates risks which warrant additional accountability requirements. We have no objection to this in principle. But accountability mechanisms need to be proportionate to the risk identified, and focused on advancing the broader objectives of the regulatory system (such as competition, efficiency and fairness).

Any risk introduced as a result of giving regulators more powers must also be weighed against the benefits that will be created by allowing regulators to respond more quickly and flexibly to market problems. Under the current system, regulators may lack the ability to respond to emerging problems (perhaps because they lack the right tools, mandate or funds). Unless the industry causing the problem is willing to address the problem, consumers will have to wait many years for a legislative solution. In the meantime, many more consumers suffer detriment and lose confidence in the financial system.

We note that the regulator is subject to existing accountability measures—for example, those who have had a licence rejected or cancelled have the right to seek merits review from the Administrative Appeals Tribunal. In our 2013 report, *Regulator Watch*, it was noted that the merits review system cannot be well adapted to the overall objectives of the financial system. For example, the report referenced AAT decisions where it appeared that the tribunal preferred the interest of the individual in maintaining an occupation over the interests of the community resulting from rigorous enforcement of consumer protection standards.[30]

There is a risk also that should there be merits review of broader regulator decisions (for example product intervention decisions) there will be a real risk that industry will strategically use the system to achieve their ends. This has been the experience in the energy industry, where independent experts found that the merits review system was being gamed by industry participants.[31] This is exacerbated where there is an absence of consumer groups acting as a contradictor in a quasi-judicial setting.

Given this, we would recommend alternative accountability mechanisms be considered. For example, subjecting the regulator to (say, five yearly) broad external reviews that are adapted to the objectives of the regulatory system (rather than one-off particular decisions) is likely to result in a more balanced and effective system. Another option would be to improve accountability to consumers, the ultimate beneficiaries of the regulator. A more substantial consumer advisory body, along the lines of the UK's Financial Services Consumer Panel (which is hosted by the Financial Conduct Authority), be established to provide public and regular reporting on consumer outcomes delivered by the regulator.[32]

Recommendation 22:

- That regulator accountability mechanisms be adapted to the overall objectives of the regulatory framework, rather than particular decisions of the regulator.

<u>ASIC's mandate</u>

We support the proposal that ASIC could be given a specific objective to promote competition, as the UK's Financial Conduct Authority has.[33] A market study power (discussed above) would assist ASIC to monitor competition in financial markets and respond to emerging problems.

We are not in favour of moving ASIC's corporate insolvency function to AFSA as we think there is value in maintaining ASIC as a 'cradle to grave' corporate regulator. Nor are we convinced there will be efficiencies to be gained by splitting this function off—it seems to us that this would necessarily require some duplication of effort as a corporation moves from ASIC's jurisdiction to AFSA.

Consumer loss and compensation

We welcome the panel's assessment that professional indemnity insurance has limited ability to provide a safety net for compensating consumer loss. The recent statistics from FOS (cited in

[30] Gordon Renouf, Teena Balgi and Consumer Action Law Centre (2013) *Regulator Watch: The Enforcement Performance of Australian Consumer Protection Regulators*, Page 143. Accessible from http://consumeraction.org.au/new-report-regulator-watch/

[31] George Yarrow, Michael Egan and John Tamblyn (2012) *Review of the Limited Merits Review Regime: Stage Two Report*, page 2. Accessible from: http://www.scer.gov.au/workstreams/energy-market-reform/limited-merits-review/lmr-review/

[32] We discussed the Consumer Panel in more detail in our submission to the 2013 Senate Economics References Committee's Inquiry into the performance of ASIC, available here: http://consumeraction.org.au/submission-the-performance-of-the-australian-securities-and-investments-commission/

[33] Mentioned at page 3-121.

the interim report) that 33 per cent of determinations in the investments jurisdiction remain unpaid provide evidence that the current arrangements are insufficient and a large number of consumers are suffering detriment as a result.

We remain of the opinion that a last chance compensation scheme is necessary, particularly in markets which are dominated by many small players. While such a scheme might be viewed as an additional cost on the industry, it should also provide an incentive for good conduct. Responsible providers may indeed form a constituency for good practice, and improvement of the conduct of less responsible conduct, as if they do not they will be faced with higher costs. Further, we submit that a last chance compensation scheme should not be limited to financial advisers, but be available for other financial product issuers such as credit and consumer lease providers.

Case study Our client, who at all material times was a disability support pensioner and had no attachable assets, entered into a number of payday loans with a particular lender. Consumer Action assisted the client to make complaints to the relevant external dispute resolution scheme on the basis that, among other things, lender had failed to meet their responsible lending obligations and had acted unconscionably. The lender later went into external administration and the EDR scheme closed our clients file as it could no longer assist the our client to achieve the outcome he sought. Our client had the option of making a complaint through the Magistrates Court of Victoria, though this would not have been straightforward and he may not have recovered any money even if he secured a judgment. Our client chose not to go ahead with this option. Given the systemic failures with the business model of this lender, large numbers of consumers would have been entitled to remedies. We expect that, like our client, the vast majority of customers would never be able to obtain these remedies because of the lack of an effective compensation scheme.

Currently, unless credit providers offer credit assistance (that is, there is some form of intermediation), they are not even required to have professional indemnity insurance. The legislation does, however, require such providers to have ‘adequate compensation requirements’.[34] We understand that compliance with this obligation is limited to provision of an annual compliance certificate by the relevant provider’s CEO. As the case study above demonstrates, and the very fact of insolvency, this requirement is meaningless from a consumer compensation perspective.

Should a last chance compensation scheme not be supported, we consider that there could be a scheme that did the minimum necessary to ensure EDR scheme and court awards are paid. To contain costs we would support a model that capped claims. Alternatively, there could be a

[34] See section 48(1) of NCCP Act and ASIC Regulatory Guide 210

requirement for ASIC approved complaints schemes to amend their terms of reference so that they can compensate consumers where determinations are unpaid.

Recommendation 23:

- That a last resort compensation scheme be a key component of financial services regulation.

Technology: use of data

Access to data

We welcome the observation that increased access by consumers to their own data has the potential to empower consumers. In response to the panel's request for information on how consumers might be given better access to their data, we recommend that a standard format for the provision of data to consumers would improve efficiency. Australian Privacy Principle 12 allows consumers the right to request personal information held by businesses. We expect that different businesses are all developing their own strategies for providing this information to consumers, and that use of the information for broader purposes (for example, product comparison) will be limited if all businesses make the data available in different formats.

Recommendation 24:

- That consumers should have the right to receive their personal and transaction data from financial services businesses in a standardised and machine-readable format.

Consumer risks and data

The interim report notes that growth in technology and 'big data' pose privacy risks for consumers. We reiterate the points raised in our previous submission about the growth of target marketing and the role of technology being used to predict consumer behaviour. In consumer lending, this technology can be used to identify consumers who are likely to be profitable, tailor and price products that the most profitable customers are likely to accept, and develop strategies to reduce the likelihood that the most profitable customers will close their accounts.[35] We submit that as the financial system becomes more 'converged', that is, there are large conglomerates that combine consumer retail and financial services, these risks will grow. Somewhat frighteningly, it has been reported that insurance risks can be identified from the supermarket buying habits of consumers.[36]

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[35] Paul Harrison, Charles Ti Gray and Consumer Action Law Centre (2012) *Profiling for Profit: A Report on Target Marketing and Profiling Practices in the Credit Industry*, Deakin University and Consumer Action Law Centre, pp 5-6.

[36] A senior Woolworths figure has said that 'customers who drink lots of milk and eat lots of red meat are very, very good car insurance risks versus those who eat lots of pasta and rice, fill up their petrol at night and drink spirits. What that means is we're able to tailor an insurance offer that targets those really good insurance risk customers'. Natasha Wallace and Sarah Whyte, September 16 2013, 'Supermarket spies: big retail has you in its sights', *Sydney Morning Herald*, http://www.smh.com.au/digital-life/digital-life-news/supermarket-spies-big-retail-has-you-in-its-sights-20130915-2trko.html

Our report *Profiling for Profit: A Report on Target Marketing and Profiling Practices in the Credit Industry* produced with Deakin University drew on the limited public information about customer management systems, but describes how banks use sophisticated systems to glean intimate personal details, using information gathered from spending patterns, call centres, product registration and point-of-sale transactions, in order to predict an individual's behaviour.

We've acknowledged that the competitive need of corporations to increase their profitability and return to shareholders unsurprisingly drives them to use personal information and new technologies for their ends, rather than to help consumers access the most appropriate products for their needs. However, this kind of conduct should be a matter for regulation if it creates risks for consumers and the financial system. We encourage the Panel to consider in more depth the techniques being used to target marketing of credit, and whether existing regulation is adequate to counter the risks it creates. Regulatory responses should be informed by an understanding of how marketing is used and how it is received by consumers.

An example may be the 2011 reforms prohibiting unsolicited credit limit increase offers, unless the customer has consented to receiving such offers.[37] These provisions were designed to address the significant consumer harm caused by the impact on many consumers who are coerced into increasing their levels of debt. Vulnerability to this sort of marketing was described in depth in our 2008 research report, *Congratulations, You're Pre-Approved.*[38]

Recommendation 25:

- That the panel consider in depth the risks to consumers and the financial system from the more sophisticated use of data by businesses to engage in consumer profiling and target marketing.

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

Yours sincerely
CONSUMER ACTION LAW CENTRE

Gerard Brody
Chief Executive Officer

David Leermakers
Senior Policy Officer

[37] National Consumer Credit Protection Amendment (Home Loans and Credit Cards) Act 2011.
[38] Paul Harrison and Marta Massi (2008), *Congratulations, You're Pre-approved: An analysis of credit limit upselling offers,* available at: http://consumeraction.org.au/policy-report-an-analysis-of-credit-limit-upselling-letters/.