

17 May 2016

The Treasury  
Langton Crescent  
PARKES ACT 2600  
AUSTRALIA

By email: [consumercredit@treasury.gov.au](mailto:consumercredit@treasury.gov.au)

Dear Treasury,

### **Review of the Small Amount Credit Contract Laws – Final Report**

We write in relation to the final report by the Small Amount Credit Contracts Review Panel (**Review Panel**) into matters relating to small amount credit contracts (**SACCs**) and consumer leases. Consumer Action Law Centre (**Consumer Action**) was actively involved in the consultation period of the inquiry, and our submission is noted in the report. In addition to this brief submission, we **attach** our submissions to both the initial Discussion Paper, and the Review Panel's Interim Report.

#### **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.

#### **Consumer Action Submission: SACC Review Panel Final Report**

Following a comprehensive consultation period the Review Panel has made twenty-four recommendations which would provide significant additional protection for vulnerable consumers, and reduce the harm caused by SACCs and consumer leases.

While the full range of recommendations provide for a significantly improved consumer protection framework, Consumer Action regards the following eight recommendations as being of primary importance for vulnerable consumers:

- Recommendation 1 – Affordability (SACCs)
- Recommendation 8 – Unsolicited offers (SACCs)
- Recommendation 11 – A cap on cost (consumer leases)
- Recommendation 15 – Affordability (consumer leases)
- Recommendation 16 – Centrepay implementation
- Recommendation 18 – Unsolicited marketing (consumer leases)
- Recommendation 22 – Disclosure of APRs (SACCs and consumer leases).

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- Recommendation 24 – Avoidance

The recommendations are considered and measured, and have been made with the key objective of facilitating financial inclusion.

Unfortunately, the recommendations do not go far enough to address the issue of affordability and prevent ongoing debt spirals that often lead to financial exclusion and costs to the community through provision of emergency services, legal support and financial counselling.

Where this submission is silent on proposed reforms, Consumer Action can be taken as being supportive. As outlined below, our additional comments relate to cost caps and affordability measures that we believe should be taken into consideration in any Government response to the report.

### **Cost caps**

We welcome the extension of cost caps to consumer leases, however we urge reconsideration of the proposed cap.

The Review Panel has recommended that consumer lease providers be permitted to charge 4 per cent per month on top of the “Base Price” of the good which they are leasing, for every month of the lease. The report makes clear that this equates to an annual percentage rate (**APR**) of between 68 per cent and 82 per cent. Such a high APR is excessive, especially for a product that is relied upon by lower income Australians.

The report proposes to define the Base Price as the recommended retail price (**RRP**). The report notes that this is a very generous starting point, given that lessors commonly receive a discount on the RRP when purchasing goods. It is of course common for retailers to include a retail margin in the supply of goods—Consumer Action is advised that at least one large lessor already imposes a mark-up on their goods of over 20 per cent.

What the report doesn’t make clear, however, is that the proposed approach presents an opportunity for a lessor to further inflate a RRP, knowing that the permitted monthly fee can be charged on top of that. This is particularly an opportunity for lessors that lease their own branded range of goods. Given that they are the only business that supply these goods, there is no obvious comparison point to confirm that the RRP is a competitive one.

It is crucial to understand the consumer base for consumer leases when considering regulation to promote financial inclusion. A forthcoming University of Melbourne research report examining consumer lease contracts recently interviewed community workers, community solicitors, and financial counsellors in Victoria and New South Wales. Those interviewed stated that in their case work experience, consumer leases are exclusively obtained by community members who are welfare dependent or otherwise financially vulnerable.<sup>1</sup> Given that consumer leases are an extremely

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<sup>1</sup> Mcrae, C (May 2016) pers comm

expensive way to acquire consumer goods (more expensive, in fact, than taking out a SACC), and given that the consumer base for consumer leases is overwhelmingly low-income, and very often welfare dependent, it is difficult to see how consumer leases can be regulated to promote financial inclusion without seriously addressing the issue of cost. While it is pleasing that the SACC Review Panel have recommended at least some price control, the recommendation does not go nearly far enough to facilitate financial inclusion.

Given these risks, we urge any Government response to limit the amount lessors can charge to a maximum APR of 48 per cent. This would have the added benefit of ensuring regulatory consistency with credit contracts of similar types (i.e., contracts of more than \$2,000 lasting more than one year).

We are also disappointed about the lack of any change to the cost cap for SACCs. The Review Panel considered reducing the cap for establishment fees from 20 per cent of the amount borrowed to 10 per cent, but rejected this option on the basis that it would not allow recovery of lenders' costs of establishing a loan (including general business and advertising costs).

This contention doesn't stand up to analysis. First, the Review Panel does not appear to have analysed the costs incurred by lenders, but rather accepted assertions of lenders. Second, the establishment fee is expressed as a percentage of loan, when establishment costs for a loan are likely to be primarily fixed. Finally, reducing the establishment fee would help reduce the incentive for lenders to structure loans as short-term (this is explained further below).

The Review Panel's report, helpfully, describes the cap for SACCs as a concession from the 48 APR per cent cap that applies to consumer credit generally. Yet the Review Panel has not adequately explained the reasoning for maintaining this current concession, nor any basis for the structure of the cap. Given this, we recommend that the cap for SACCs be limited to a maximum APR of 48 per cent.

### **Affordability measure**

We generally support the proposals to cap the total amount of SACC and consumer lease repayments to a percentage of a consumer's net income. However, we believe that the Review Panel has overlooked some unintended consequences.

With regard to SACCs, the Review Panel has recommended limiting SACC repayments to 10 per cent of the consumer's net income, but has also recommended removal of the rebuttable presumption that a SACC should be considered unsuitable if the borrower has had two or more SACCs in the previous 90 days. While there is some logic to this recommendation (the affordability requirement should limit the risk of debt spirals), we believe that it will result in more consumers becoming repeat (back-to-back) users of SACCs.

The Review Panel suggests that the 10 percent net income cap would encourage longer loan terms. However, we submit that there remains a strong incentive for lenders to structure SACCs as relatively short-term (one to three months in length) given that the cost cap provides a large upfront establishment fee for each loan. Further, the tables included in the report confirm that for minimum wage earners, a 3 month \$500 SACC will result in repayments below the 10 per cent cap. For loans of

lower amounts, it is likely that even shorter loans (with a higher APR) will result in repayments below the 10 per cent case.

The risk is that at the end of a short loan period, the lender could re-contact the customer and entice them into another loan. Such marketing would not be considered unsolicited if the consumer has opted-in to receive such offers when taking out the previous loan—and this could be achieved with a simple tick box on the application form. The behavioural aspects of borrowing, the generally poor rate of financial literacy in the community, and the tendency of lenders to seek to establish ongoing relationships with their customers, will likely mean that many people will become repeat borrowers without considering other options such as more affordable finance or the availability of free financial counselling.

The continuing need for small amount credit contracts is often predicated on the basis that they are sometimes necessary for “one off” emergencies, and their high cost is justified on the basis of administrative costs. Removing the rebuttable presumption (and thereby enabling ongoing repeat borrowing) puts a lie to both of these justifications. Consumer Action notes that on May 12, 2016 Google announced that from July 13 an international ban on payday loan ads will apply to their website. The ban will apply to loan contracts with a repayment period of less than 60 days, and in the US will apply to products with an APR of 36% or higher. This is a significant statement by Google, and effectively places payday loans in the same category as other dangerous goods such as firearms, tobacco and explosives. We raise the action of Google to demonstrate that the debt spiral effect and the dangers of repeat borrowing have long been widely acknowledged. We believe that any sensible reform of small amount credit contract laws should address this issue – and would need to go further than the SACC Review Final Report recommendations in order to do so.

To “short circuit” the tendency of borrowers to take out another loan immediately on repayment of their previous loan, we recommend that a cooling off period of 60 days should be instituted, in lieu of the repeat borrowing rebuttable presumption. This would prevent borrowers from taking out another SACC within 60 days of repaying their previous loan, and would break the pattern of repeat borrowing. If SACCs truly are for one-off emergencies, then there should be no need for consumers to have access to such high cost credit on an ongoing, continuing basis.

While this proposal has not been made by the SACC Review Panel, it is not without international precedent. The Consumer Financial Protection Bureau (**CFPB**) has proposed a 60 day cooling off period for payday loans in the United States, precisely for the purpose of ending ongoing reliance on high-cost credit.<sup>2</sup>

With regard to consumer leases, we submit that the long term nature of lease contracts should be taken into account when considering the Review Panel’s recommendation of limiting lease repayments to 10 per cent of net income.

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<sup>2</sup> CFPB Press Release, March 26 2015 (<http://www.consumerfinance.gov/about-us/newsroom/cfpb-considers-proposal-to-end-payday-debt-traps/>)

If the cost caps for leases are allowed to be charged over a 48 month period (i.e. 4 years), it is not inconceivable for products to tend to that length. This is a much longer term than SACCs, which commonly run for a period of 3 months.

We submit that the proposed affordability mechanism be adapted to deal with this difference between leases and SACCs. Rather than limiting rental repayments to 10 per cent of the consumer's net income, this should be reduced to 5 per cent. This would recognise that 10 per cent of a consumer's income over 4 years is a substantial amount of money compared with the same amount over 3 months for a typical SACC. For lower income Australians, taking 10 per cent of their income over 4 years is likely to leave them without sufficient money to live on and will not deliver financial inclusion. This is particularly so when one considers that the market for SACCs and consumer leases largely overlaps – meaning that under the SACC Review's current recommendations, low income earners could be committing up to 20% of their income to servicing SACC and consumer lease repayments. In our view, this is an unaffordably high percentage, and would not have the intended effect of promoting financial inclusion.

### **Other recommendations**

The following comments relate to two other key recommendations:

#### **Unsolicited sales and marketing:**

We strongly support the proposed recommendations and believe that there needs to be much better alignment of the regulatory approach to unsolicited sales across all consumer products, including SACCs and consumer leases.

For example, section 156(1) of the NCCP Act prohibits credit canvassing at home, but not in other contexts and this does not apply to consumer leases. Section 992A of the Corporations Act regulates the hawking of financial products, but this is also limited: the prohibition doesn't apply to expenses-only funeral products and there can be limited remedies available when there is a breach.

In the context of the Review of the Australian Consumer Law (**ACL**), we are recommending a complete prohibition on unsolicited sales. This should be replicated for all credit and financial statements, and include all forms of communication (whether in person, phone or by electronic means). We refer to our forthcoming submission to the ACL Review.

In terms of the definition of unsolicited, we believe that there must be measures to prohibit lenders from obtaining invitations or consent to contact through ulterior means. For example, lenders are likely to bundle consents in terms of contracts, or through tick boxes on loans of applications. This could be dealt with by a provision which states that a consumer is not taken to have invited the provider or provided consent unless that they have done so for the predominant purpose of entering into negotiations to obtain a loan or lease. This is similar to section 69(1A) of the Australian Consumer Law which extends the definition of unsolicited consumer agreement in a similar way.

**Avoidance:**

We believe that any anti-avoidance mechanisms must be drawn broadly. We are also aware of concerns that such a provision would require referral of powers from state and territory governments. Attached is an advice from Brind Zichy-Woinarsky QC regarding the bases on which the Federal Parliament could enact anti-avoidance measures without the for further referrals of power

Please contact Zac Gillam, Senior Policy Officer on 03 9670 5088 or at [zac@consumeraction.org.au](mailto:zac@consumeraction.org.au) if you have any questions about this submission.

Yours sincerely

**CONSUMER ACTION LAW CENTRE**



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Chief Executive Officer



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**Attachments:**

- 1- Consumer Action submission to initial Discussion Paper.
- 2- Consumer Action submission to SACC Review Panel Interim Report.
- 3- Brind Zichy-Woinarsky QC advice re: anti-avoidance provisions.