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By email: bankruptcy@ag.gov.au

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Dear Ms Crawford

Legislative Instruments Consultation: Bankruptcy Amendment (Debt Agreement Reform) Act 2018

The Consumer Action Law Centre, Financial Rights Legal Centre and Financial Counselling Australia welcome the opportunity to comment on the Legislative Instruments Consultation Guide for the *Bankruptcy Amendment (Debt Agreement Reform) Act 2018* (Cth) (**Act**).

Information about the contributors is available at **Appendix A**.

We support the majority of the recent reforms to the debt agreements under Part IX of the Bankruptcy Act (**Part IXs**) in the Act, particularly the focus on fair treatment of debtors, affordable Part IXs, and restoring the lost trust in the debt agreement administration industry. Whether these reforms achieve this intention will depend on the policy settings in the legislative instruments.

We strongly support the three proposed industry-wide conditions in Legislative Instrument 1, particularly compulsory membership of the Australian Financial Complaints Authority (**AFCA**) for all registered debt agreement administrators (**Administrators**). This submission recommends:

- additional conditions that would help to build trust in the Part IX regime;
- a shift to outcomes-based disclosure requirements, by placing the onus on Administrators to ensure their clients understand the risks, consequences and cost of a Part IX, rather than 'tick and flick' compliance;
- amendments to the advertising guideline, including review and remediation of people affected by misleading advertising of Part IXs.

We are strongly opposed to the proposed figures for the 'payment to income' ratio in Legislative Instrument 2. The proposed figures would see people living in poverty on annual incomes above $12,500 go without essentials to make patently unaffordable repayments on credit card and other unsecured debts. Unless the prescribed amounts are dramatically raised, the Parliament's intention of ensuring affordable, sustainable repayments under Part IXs will be defeated. We strongly recommend amending

the prescribed figures so that the payment to ratio creates an effective minimum annual income threshold based on:

- the Base Income Threshold Amount (**BITA**) ($57,239) to align Part IX repayments with income contributions in bankruptcy;
- alternatively, the National Minimum Wage ($37,398), which is formulated with the living standards and the needs of the low paid in mind and is intended to guarantee a modest but adequate standard of living.

An analysis of the payment to income ratio (based alternatively on BITA, the National Minimum Wage, and the Department's proposed figures) applied to case studies is available at **Appendix B**.

This submission refers to our joint submission and case studies provided to the Senate Legal and Constitutional Affairs Legislation Committee Inquiry into provisions of the *Bankruptcy Amendment (Debt Agreement Reform) Bill 2018* (**Senate Inquiry Submission**).[1] Our Senate Inquiry Submission is included at **Appendix C**.

A full list of recommendations is available below.

[1] Submission available at: https://policy.consumeraction.org.au/2018/03/07/submission-debt-agreement-reform/ .

LIST OF RECOMMENDATIONS

Industry-wide conditions

1. Introduce additional industry-wide conditions:
    a. holding Administrators responsible for the conduct of aligned brokers;
    b. banning lead generation by Administrators, brokers and paid referrers;
    c. that Administrators must make inquiries, and take reasonable steps to verify, the debtor's financial situation in preparing *all* Part IX proposals (not just those that fail the payment to income ratio);
    d. that total repayments including all fees cannot exceed a prescribed percentage (less than 100%) of the debtor's original total debt;
    e. that set-up fees cannot be collected until after the debt agreement proposal is accepted by creditors;
    f. requiring Administrators to provide, within 10 days of termination for arrears or request by the debtor, a clear and simple statement setting out the original debts, payments received and disbursed, amounts owing to creditors, and a referral to an accredited financial counsellor;
    g. requiring Administrators to act honestly and fairly.
2. Amend the Inspector-General's Practice Guideline 1 to:
    a. require review and remediation of all clients affected by a breach of the Guideline;
    b. require that firms must not misrepresent their services using high impact terms like 'free', 'minutes' and 'seconds' suggesting that debt assistance will be quick and at no cost;
    c. stop use of 'alternative to bankruptcy";
    d. stop use of 'NDH' or 'National Debt Helpline' in Google sponsored advertising;
    e. clarify that the Guideline applies to any debt help, credit, credit repair. or other advertised service that ultimately ends up in the sale of a Part IX;
    f. clarify that the Guideline applies to telephone conversations;
    g. clarify that a breach of the relevant legislation is a breach of the industry-wide condition;
    h. clarify the meaning of 'unsuitable debtors';
    i. explicitly refer to section 29(1)(l) of the Australian Consumer Law.
3. Codify the aims of disclosure and place responsibility for achieving these aims on Administrators.
4. Arrange consumer testing of proposed disclosure obligations.
5. Award appropriate remedies at AFCA including voiding agreements, and compensation for loss and damage.
6. Any monetary award in the debtor's favour at AFCA should not form part of the debtor's bankrupt estate if the debtor bankrupts after terminating or voiding a Part IX.

Payment to income ratio

7. Set, and update annually, the Low Income Debtor Amount and Prescribed Percentage to create an effective minimum income by reference to the Base Income Threshold Amount ($57,239) or, alternatively, the National Minimum Wage ($37,398).

Other recommendations

8. Introduce a seamless regulatory framework for all debt management firms, including appropriate remedies which may include voiding agreements, payment of compensation or loss and damage.
9. Empower the Australian Financial Security Authority (**AFSA**) or the Australian Securities and Investments Commission (**ASIC**) to undertake file reviews of the quality of advice provided by Administrators to debtors.
10. Properly fund AFSA to gather and publish data on the performance of the Part IX regime and to scrutinise Administrators' certification duties.

LEGISLATIVE INSTRUMENT 1 – INDUSTRY-WIDE CONDITIONS

Consultation Point 1.1 – The Department seeks stakeholders' consideration of and comment on the proposed first tranche of conditions A, B and C to be included in the industry-wide conditions for registered debt agreement administrators

We strongly support the proposed first tranche of industry wide conditions. Our comments on the proposed conditions are detailed below.

However, some of the current problems in the Part IX regime, detailed in our Senate Inquiry Submission, will not be addressed by the Act or the proposed conditions. The main areas of ongoing concern are:

- conflicted and poor-quality advice on debt options;
- role of brokers;
- lead generation;
- affordability and verification of the debtor's actual financial position;
- excessive and unwarranted fees;
- exiting from terminated Part IXs; and
- gaming of the system by Administrators and loopholes.

Conflicted advice

While the recent reforms will help to improve standards in the debt agreement industry, the central conflict of interest remains: administrators stand to earn fees from recommending a Part IX over other (often more suitable) options, such as hardship arrangements, debt waivers, and bankruptcy.

Please refer to our comments on poorly informed debtors and conflicted advice (Senate Submission pages 10-13). We also note the shocking findings of the Where To survey commissioned by the AFSA, which found that the vast majority of Part IX debtors were initially looking for a debt consolidation (42%) or way to manage debts (42%)—not personal insolvency.[2]

We recommend that the regulator—either AFSA or ASIC—be empowered to undertake file reviews to examine the quality of advice provided by the administrator to the debtor. This should include an assessment of whether the outcome was beneficial for the debtor, compared to other realistic options available to the debtor at the time. Such an approach will improve the standards of advice given by Administrators and enhance trust and confidence in the industry.

Brokers

Comprehensive reform is needed to curb the harm caused by largely unregulated brokers and paid referrers operating in the debt advice industry. Many of these unregulated brokers attempt to shield Administrators from scrutiny of inappropriate debt agreements and mis-selling. We are concerned that many Administrators are not effectively supervising their brokers. While we would support the removal

[2] Where To, *Assessing the experiences of debtors and creditors with practitioner during the personal insolvency process – a market research report for the Australian Financial Security Authority*, 25 May 2017.

of all intermediaries from the debt agreement regime, at the very least the Bankruptcy Act or industry-wide conditions should hold Administrators responsible for the conduct of brokers.

We also note that advice role of debt management firms will be the subject of an upcoming Senate Inquiry.[3]

Lead generation

A related problem is the use of lead generation in the debt agreement industry.[4] AFSA has requested that such engagements cease and will focus on this issue as part of it 2017-18 inspection program.[5] In our view, lead generation in the debt agreement industry should be banned.

Consumer Action has published a report on lead generation which identifies a range of problems for consumers,[6] including:

- Disempowerment: when marketing consent is hidden behind unrelated activities (i.e. searching online), or is bundled with mandatory terms and conditions, is overly broad or simply not sought, consumers are denied their opportunity to protect their privacy and can lose control of how their personal information is used.
- Manipulation: people's behavioural biases are exploited in order to source leads. An offer of 'free' assistance can deflect attentions from the marketing consequences that will arise. It's also been shown that people will provide much more information online than they intend.
- Misleading conduct: third party lead generators appear willing to take greater risks with their advertising than their clients would, increasing the risks that consumers can be misled.

A debt agreement is a form of insolvency with serious consequences that requires a careful consideration of a person's situation and available options. It is not a product to be "sold" using high pressure sales tactics to anyone with debt. People who are *genuinely insolvent* will seek advice on their insolvency options when they need it, not when the phone happens to ring from an outbound call centre. We recommend an industry-wide condition banning lead generation by debt agreement administrators, brokers and paid referrers.

Affordability and verification of actual financial position

We have seen many examples of debt agreements, certified by the Administrator and accepted by AFSA for processing, that involve repayment obligations that the debtor is unlikely to meet, or only meet with substantial hardship. This is may be caused by an unrealistic or inaccurate assessment by the Administrator of the debtor's likely income and actual expenses over the life of the Part IX.

Examples from our Senate Inquiry Submission:

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[3] See https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/Creditfinancialservices.
[4] AFSA, *Personal Insolvency Regulator* (December 2017, Volume 15, Issue 4), p4.
[5] Ibid.
[6] Consumer Action Law Centre, *Dirty leads: consumer protection in online lead generation,* March 2018, available at: https://policy.consumeraction.org.au/2018/03/16/dirty-leads-consumer-protection-in-online-lead-generation/.

- In Jemila's proposal (Case Study 3), the budget allowed only $12 per week for payments to creditors not included in the debt agreement, even though she owed over $5,000 to these creditors;
- Jen's proposal (Case Study 4), the budget allowed a total of $2 per week ($104 per year) for clothing, shoes and haircuts;
- Marie's proposal (Case Study 2) stated, despite their age, health and low employment prospects: "After a term of 52 weeks, both the Debtor and Partner intend to be working, affording additional payment to the DAP."

When preparing Part IX proposals, Administrators should be held to similar standards as lenders making lending decisions—they should inquire about, and take reasonable steps to verify, the debtor's *actual* income and actual expenses. This requirement should apply to all Part IXs, not just those that fail the payment to income ratio. At a minimum, income and expenditure projections should not incorporate income which is higher than the individual has historically earned and should not utilise expenditure allowances which are lower than the individual has historically incurred. Similarly, stepped-up repayments as in Marie's case should not be allowed—these are often unrealistically optimistic in the face of an uncertain future.

Fees

The Act does not address the excessive and unwarranted set-up and administration fees charged by some administrators. This is an area of ongoing concern for consumers and creditors. We recommend an industry-wide conditions requiring that:

1. Total repayments including all fees cannot exceed a prescribed percentage (less than100%) of the debtor's original total debt; and
2. Set-up fees only become payable after the debt agreement proposal is accepted by creditors.

The first condition would prevent debt agreements where the fees are greater than the amount of the original debt, which is great source of confusion and complaints by consumers who are marketed a 'debt reduction' or 'debt relief,' only to pay more once fees are added.

The second condition is consistent with the Advance Fee Ban in the United States that applies to telemarketers of for-profit debt relief services following amendments to the *Telemarketing Sales Rules* in 2010.[7] This would reduce incentives for Administrators to charge high upfront fees without regard to the likelihood that a Part IX will be accepted and incentivise the timely lodgement of proposals. This reform would improve the integrity of the regime and encourage administrators to undertake a realistic and accurate assessment of the debtor's capacity to make the proposed repayments.

[7] United States' Federal Trade Commission, Media release, 'FTC Issues Final Rule to Protect Consumers in Credit Card Debt,' 29 July 2010, available at: https://www.ftc.gov/news-events/press-releases/2010/07/ftc-issues-final-rule-protect-consumers-credit-card-debt.

Orderly exit from a failed Part IX

We refer to our comments on reforms to assist an orderly exit from a terminated Part IX at page 25 of our Senate Inquiry Submission. We recommend that Administrators provide, upon termination for arrears or request by the debtor, a clear and simple statement setting out the original debts, payments received and disbursed under the debt agreement, amounts owing to creditors, and a referral to an accredited financial counsellor. This should be provided within 10 days of termination.

Duty to act fairly and honestly

We recommend a general duty to act honestly and fairly. This is consistent with the legislative intention of improving trust and confidence in the debt agreement industry and will be a useful catch-all to deter new unscrupulous practices from emerging and gaming of the system.

Consultation point 1.2 – In relation to proposed industry-wide condition A, the Department seeks stakeholders' consideration of and comment on using Inspector-General Practice Guideline 1 as the basis for industry-wide conditions relating to advertising of debt agreements.

A robust industry-wide condition on advertising of debt agreements would reduce the number of people duped into a Part IX that they don't need or that won't help. Problematic and misleading advertising has been a long-standing problem in the sale of Part IXs. Many of our clients contacted their Administrator or an aligned broker in response to an tv, radio or, increasingly, online advertisement. We refer to our Senate Inquiry Submission at page 13, Consumer Action's report on website advertising of Part IX,[8] as well as ASIC's recent enforcement action[9] as further support for this important industry-wide condition.

The Inspector-General's Practice Guideline 1 (**Guideline**) is a good starting point for Condition A. We are pleased that the Guidelines also applies to advertising by brokers. However, we consider the following amendments and clarifications are needed to the Guideline.

Review and remediation of affected clients

Where an advertisement falls foul of the Guideline, the Administrator should be required to review its files and remediate all clients who may have been impacted by the advertising and marketing. This should include, for example, a refund of all fees where a client would not have engaged the Administrator but for the misleading advertising. Simply requiring the Administrator to remove or amend the advertisement does nothing to put affected clients back in the position they would have been, if not for the misconduct. We refer to detailed guidance on review and remediation programs in ASIC *Regulatory Guide 256: Client review and remediation conducted by advice licensees.*

[8] Consumer Action Law Centre, *Fresh start or false hope? A look at the website advertising claims of Debt Agreement administrators*, April 2013, available at: https://consumeraction.org.au/wp-content/uploads/2013/05/Fresh-start-or-false-hope-April-2013.pdf.

[9] See: https://asic.gov.au/about-asic/news-centre/find-a-media-release/2018-releases/18-148mr-fox-symes-pays-37-800-for-misleading-advertising/.

Use of the word 'free'

We are concerned by advertising that offers a 'free' consultation or free credit report but ends in a high-pressure sales pitch for a Part IX and note ASIC's recent enforcement action.[10] We refer to ASIC Regulatory Guide 234 on good practice advertising in credit and financial services, which provides detailed guidance on the use of the term 'free' and advertising complex products. The Guidelines should state that firms must not misrepresent their services using high impact terms like 'free', 'minutes' and 'seconds' suggesting that debt assistance will be quick and at no cost.

Bait and switch

Similarly, we are concerned by business models that sell Part IX but advertise a different service, such as credit repair or debt consolidation loans. We receive complaints from people who call firms for credit repair because they want to obtain a loan, only to end up in a vastly different Part IX that will further impair the creditworthiness. The Guideline must apply to any debt help, credit or credit repair other advertised service that ultimately ends up in a Part IX.

Telephone conversations

We receive complaints from people about Administrators and brokers engaging in high pressure sales tactics during early telephone calls. The Guideline should make clear that telephone conversations, include any free consultation, are 'advertising and marketing' to which the Guideline applies. We note the protections applying to telemarketing of debt relief services in the United States.

'Alternative to bankruptcy'

We strongly encourage all Administrators (and AFSA) to stop referring to Part IXs as 'an alternative to bankruptcy'. This phrase has great significance to many of our clients who do not want to bankrupt due to the stigma—even when it may be the best option, were they provided with balanced and impartial advice. The words 'debt agreement' do not suggest insolvency, and some people are shocked to learn to its true nature later. The confusion and potential to mislead debtors would greatly reduce if the Guideline required Administrators to refer to 'a different type of bankruptcy' or a 'form of insolvency' instead of an 'alternative to bankruptcy'. This would flag at a critical early stage that a 'debt agreement' is in fact a type of insolvency with very serious consequences.

Ban use of 'NDH' or 'National Debt Helpline' in Google sponsored advertising

Administrators and brokers should not use these words in Google advertising. A simple online search for 'National Debt Helpline' reveals paid advertising for Administrators and brokers. We receive complaints from people who mistakenly think they are speaking with a financial counsellor but are in fact dealing with an Administrator or broker.

Incorporation of relevant laws and regulations

It should be clear that a breach of the relevant legislation is a breach of the condition. This should trigger the consumer's right to apply to void their debt agreement if adversely affected by the breach—for example, where they believed they had entered a debt consolidation, or that it was a government scheme.

[10] Ibid.

Explicitly refer to section 29(1)(l) of the Australian Consumer Law (ACL)

Section 29(1)(l) of the ACL relates to false or misleading representations concerning the 'need' for any goods or services. We are concerned that some advertising overstates the negative consequences of bankruptcy, giving debtors the impression that they 'need' to enter a Part IX debt agreement to solve their financial problems.

'Unsuitable debtors'

We note that Clause 3.2 does not define 'unsuitable debtors'. Guidance on who is unsuitable would assist. Our firm position is that Part IXs are only suitable for a very narrow band of debtors, being those who:

1. are otherwise facing bankruptcy (not temporary hardship);
2. face an adverse consequence in bankruptcy being:
    a) the likely seizure of an asset;
    b) work restrictions; or
    c) paying income contributions for those earning over the Base or Actual Income Threshold Amounts; and
3. can realistically afford the proposed repayments without ongoing hardship.

Consultation point 1.3 – In relation to proposed industry-wide condition B, the Department seeks stakeholders' consideration of and comment on:

i. what types of disclosures a debt agreement administrator should make to a debtor, and
ii. when those disclosures should be made during the course of a debt agreement administrator's contact with a debtor.

Outcomes-based obligations

We consider that disclosure-based reform is generally less effective at improving consumer outcomes than reform that requires firms to improve standards of behaviour and treat consumers fairly.[11]

The recent evaluation of the Part IX regime by Chen, O'Brien and Ramsay found that the current Prescribed Information notice is an ineffective form of consumer protection:

> The Prescribed Information notice is printed in a small font, without clear headings that identify the sections relevant to debt agreement debtors. Large portions of the document are inapplicable to debt agreement debtors, diverting attention from the relevant sections. More than half the document describes the consequences of bankruptcy, while the section on debt agreements comprises only a few paragraphs. The notice uses technical terms and presumes a great deal of legal and financial knowledge. For example, it explains that a debt agreement will be recorded on the NPII, but does not explain the implications of this. This section of the document refers readers to a subsequent paragraph on the ability to obtain credit, located further down the page. However, this latter paragraph is part of a separate section on the consequences of bankruptcy and makes no explicit

[11] For more information, see our recent submission to the NSW Office of Fair Trading Easy and Transparent Trading Consultation Paper, 28 August 2018, available at: https://policy.consumeraction.org.au/wp-content/uploads/sites/13/2018/08/180827-NSW-Easy-and-Transparent-Trading-Consultation-Paper-FINAL.pdf.

> reference to debt agreements. Importantly, the Prescribed Information notice does not clearly state that proposing a debt agreement is, of itself, an act of bankruptcy. The vast majority of debtors who enter debt agreements are financially stressed and are likely to find this document difficult to navigate and comprehend.[12]

The deficiencies of disclosure have also been acknowledged by the Productivity Commission[13] and ASIC:

> …disclosure alone is not working to drive fair consumer outcomes. For example, the Financial System Inquiry noted that disclosure alone is unlikely to correct the effect of broader market structures and conflicts that drive product development or distribution practices that result in poor consumer outcomes.[14]

Consumer Action encourages the Attorney-General's Department to focus on *outcomes* for debtors, rather than the fact of disclosure itself. That is: does the highly stressed debtor actually comprehend what is being disclosed?

The Victorian Essential Service Commission (**ESC**) has taken this approach in its recent work on information provided on energy bills. Consumer Action notes and strongly endorses the ESC's 'purpose driven philosophy,' as expressed by Chairman Dr Ron Ben-David:

> Under our proposed approach, the Code will outline the reason why certain information must be provided to customers. This means retailers' actions won't only be judged against whether they've provided the information, but whether they've done so in a way that enlivens the purpose given for providing that information. This means obligations like the provision of information move beyond traditional principles of transparency and disclosure, and are elevated to higher principles of responsibility and accountability. Retailers become responsible for enlivening the objective and purposes described in the regulations and they can be held accountable for doing so.[15]

The ESC's recent Draft Decision proposed to codify the consumer outcomes that the regulatory obligations are intended to deliver. Doing so means energy retailers won't be able to adopt a simple tick-the-box approach to complying with these new obligations. Instead, retailers will need to turn their minds to how they achieve these outcomes while meeting their compliance obligations.

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[12] Chen, O'Brien and Ramsay, An Evaluation of Debt Agreements in Australia (2018) 44(1) Monash University Law Review (Forthcoming) p 44.

[13] Productivity Commission, Inquiry into Competition in the Australian Financial System – Final Report, August 2018, p. 87, available at: https://www.pc.gov.au/inquiries/completed/financial-system#report: "Australia's regulatory framework relies heavily on disclosure to protect and empower consumers, however the traditional notion that more information (versus, say, better information) leads to improved consumer outcomes is not always the case."

[14] Australian Securities and Investments Commission, Submission: Design and distribution obligations and product intervention power, August 2018, pp. 34-40, available at: https://download.asic.gov.au/media/4849144/design-and-distribution-obligationsand-product-intervention-power-revised-exposure-draft-legislation-submission-by-asic.pdf.

[15] Essential Services Commission, *Building trust through new customer entitlements in the retail energy market: Draft Decision*, 2018, pp v-vi.

This welcome shift in regulatory philosophy should be applied to the Part IX regime. We know that highly stressed debtors are susceptible to poor or imbalanced advice and misleading representations by Administrators, which are difficult to overcome with later disclosure. It is clear from our casework and AFSA's Where To report that many people entering Part IXs do not understand its nature, cost or consequences.[16] It's time to shift the onus onto Administrators to take steps to ensure the clients paying and relying on them actually understand.

Applying a purpose-driven philosophy to Part IXs, we recommend codifying the aims of disclosure and place responsibility for achieving these outcomes on Administrators. This includes:

- Ensuring that debtors understand all of their available options to deal with unmanageable debt and the merits of each option;
- Ensuring that debtors understand the nature, cost and serious consequences of a Part IX;
- Ensuring that Part IXs are suitable and properly targeted at the right debtors.

Administrators would be responsible for demonstrating that these outcomes are being met. They could demonstrate this for example by asking an independent party to verify these factors by contacting a random sample of the Administrator's clients.

Types and timing of disclosure

The critical points (which may overlap) at which clear information should be provided to, and understood by, the consumer include:

1. The first interaction with the DAA or broker, often in the form of a free telephone consultation
2. At the time that the DAA or broker gives information or advice on options
3. At the time the consumer is considering signing the Part IX proposal.

<u>First interaction with the Administrator or broker</u>

The early interactions are particularly important, as these will be persuasive in forming the debtor's understanding of the nature, cost and consequences of a Part IX and other options. The UK Financial Conduct Authority found that consumers are very unlikely to shop around for help with debt and, once engaged with a company, are 'susceptible to influence or may make choices that are not in their best interests.'[17] The Administrator/broker should ensure that the debtor understands, at a minimum:

- free options that could assist, including the National Debt Helpline, EDR schemes, and creditor and utility hardship programs;
- total amount of fees payable, including set-up and likely administration fees if Part IX accepted;
- key terms of the services contract if they proceed with the Administrator or broker's services.

<u>At the time of advice on options</u>

The Administrator should ensure that the debtor understands, at a minimum:

- that a Part IX is a type of insolvency;

[16] Above n 2.

[17] Financial Conduct Authority, *Thematic Review TR15/8: Quality of Debt Management Advice*, June 2015, available at: https://www.fca.org.uk/publication/thematic-reviews/tr15-08.pdf.

- that a Part IX is not a debt consolidation loan;
- their other options for managing debt;
- the key risks and all consequences of signing a Part IX Proposal, including that:
    - it is an act of bankruptcy and what this means;
    - it may result in difficulty obtaining loans, credit cards, utilities and rental accommodation.
    - the consequences are very similar to many of the consequences in bankruptcy;
- the consequences of defaulting on Part IX repayments;
- the total amount of fees payable, including set-up and likely administration fees if Part IX accepted.

<u>At the time the consumer is considering signing the Part IX proposal</u>
The Administrator should ensure that the debtor understands, at a minimum:

- the total amount of fees payable, including set-up and likely administration fees if Part IX accepted;
- the consequences of signing a Part IX Proposal (as above); and
- the availability of internal and external dispute resolution including contact details.

However, we remain concerned that any 'key fact sheet' or other written disclosure will arrive too late and become 'tick and flick' compliance. Clients are often fully invested with the Administrator (or aligned debt management firm) by the time key risks are disclosed, having diverted payments from creditors toward the Administrator or firm, and feel they must push the process along to get creditors off their backs. Our above recommendation on banning collection of fees until the Part IX is accepted would reduce this problem. Alternatively, Administrators should be required to disclose key risks before collecting any fees.

All information must be in plain language and translated where needed. Administrators should consider any literacy, language, or comprehension barriers that exist for particular clients.

We strongly recommend that the Attorney-General's Department arranges consumer testing of the proposed disclosure obligations.

We recommend that Administrators and brokers should be required to maintain records, including call recordings, to substantiate that these obligations have been met.

Consultation point 1.4 – In consideration of the further information on AFCA at Attachment A, and as found in AFCA's Complaint Resolution Scheme Rules and Operational Guidelines, the Department seeks stakeholders' consideration and comment on requiring debt agreement administrators to join AFCA and offer internal dispute resolution.

We strongly support internal and external dispute resolution obligations, which are essential to restoring trust and confidence in Administrators and ensuring affordable and accessible justice for debtors.

Many registered administrators are already familiar with the process of internal and external dispute resolution from licensing conditions for other services offered. Prudent Administrators have nothing to fear from AFCA membership. Indeed, effective dispute resolution processes can assist Administrators to identify and resolve problems in their business that are generating customer complaints.

One of the barriers to justice for aggrieved debtors who terminate their Part IX, often for arrears, and then bankrupt is that pursuing a complaint about the administrator or broker's misconduct is not worth the time, effort and stress when any return of fees would form part of their bankrupt estate and go to their creditors. Complications also arise from requiring the Trustee's permission to commence legal action.

To resolve this problem, we recommend that any monetary award in the debtor's favour at AFCA should not form part of the debtor's bankrupt estate if they bankrupt after terminating or voiding a Part IX. This will reduce the incentives for Administrators to collect set-up fees towards Part IXs that were always unlikely to proceed or complete because the debtor could not sustain repayments. We refer to Marco's case study in our Senate Inquiry Submission.

LEGISLATIVE INSTRUMENT 2 – PAYMENT TO INCOME RATIO

Consultation point 2.1 – The Department seeks stakeholders' consideration of and comment on the initial figures proposed for the payment to income ratio's prescribed percentage and low income debtor amount.

We strongly support the intention of the Act to ensure repayments under Part IXs are affordable and sustainable. To achieve this, the payment to income ratio must prevent unaffordable Part IXs that prolong hardship.

We are deeply concerned that the prescribed figures for the payment to income proposed in the Consultation Guide will defeat the intention of the legislation.

Setting the Low Income Debtor Amount at $25,000 and the Prescribed Percentage at 200% creates an effective minimum income threshold of $12,500 per annum for Part IXs. A single person living (let alone supporting a family) on an annual income of $12,500 is almost certainly living in poverty, and simply does not have the income to make repayments on unsecured debt, however much they may want to. Any such repayments will mean that meagre funds are diverted from life's essentials: putting food on the table, a roof over their head, keeping a car on the road and the electricity connected. It will also set up debt agreements to fail.

There are rare cases where a debtor on an income under $12,500 has other sources of funds to sustain repayments. These rare cases can be resolved by the additional certification duty in s184C(4D) of the Act, enabling access to a Part IX. The ratio should not be set by reference to these rare cases. It must be set on the basis that the effective minimum income is the only available income, and that income must be sufficient to meet essential living costs, repay debts not included in the Part IX (such as car loans, fines and child support) and regain financial stability.

In preparing this submission, we considered a range of measures by which to set the effective minimum income. We strongly recommend that the Low Income Debtor Amount and Prescribed Percentage be set, and updated annually, to create an effective minimum income by reference to:

1. The **Base Income Threshold Amount ($57,239)** – Eligibility to enter a Part IX should be aligned with the threshold for income contributions in bankruptcy – the Base Income Threshold Amount in the *Bankruptcy Act 1966* and Regulations. To achieve this with a Prescribed Percentage of 200% and the current BITA of $57,239, the Low Income Debtor Amount should be set at $114,478.

2. Alternatively, the **National Minimum Wage ($37,398)** – This is in accordance with the recommendation of Chen, O'Brien and Ramsay, who noted that "minimum wages are formulated with the 'living standards and the needs of the low paid' in mind and are intended to guarantee a modest but adequate standard of living."[18] To achieve this with a Prescribed Percentage of 200%

[18] *Fair Work Act 2009* (Cth) s 284(1)(c); see also Chen, above n 12, 42.

and a current annual minimum wage of $37,398, the Low Income Debtor Amount should be set at $74,796.

We applied our recommended measures to Consumer Actions' case studies on unaffordable Part IXs in the Senate Inquiry Submission, both over the actual term as proposed (often in excess of 3 years), and on the stated weekly or fortnightly repayments if the debt agreement were limited to 3 years (as will be the case in future). We undertook this analysis to assess whether these concerning Part IXs would have been helpfully prevented by the proposed payment to income ratio. The short answer is no.

Table 1: Actual term

Case study	Would the proposed Part IX fail the payment to income ratio?		
	Proposed figures: $12,500	Minimum Wage: $37,398	Base Income Threshold: $57,239
1 – Marco	**No**	**Yes**	**Yes**
3 – Jemila	**No**	**Yes**	**Yes**
4 – Jen	**No**	**No**	**Yes**
5 – Narelle	**No**	**Yes**	**Yes**

Table 2: If term limited to 3 years

Case study	Would the proposed Part IX fail the payment to income ratio?		
	Proposed figures: $12,500	Minimum Wage: $37,398	Base Income Threshold: $57,239
1 – Marco	**No**	**Yes**	**Yes**
3 – Jemila	**No**	**Yes**	**Yes**
4 – Jen	**No**	**No**	**Yes**
5 – Narelle	**No**	**Yes**	**Yes**

Our full analysis, including actual ratios, is at **Appendix B.**

This analysis shows that the proposed prescribed figures would not prevent any of the unsuitable Part IXs from being proposed. Even where the weekly or fortnightly repayments were limited to a maximum term of 3 years (thereby reducing total overall repayments), Consumer Action's four case studies would still pass the ratio, confirming that the proposed figures will not achieve the legislative intention of preventing unaffordable Part IXs. The safest effective minimum income would clearly be BITA, followed by the minimum wage.

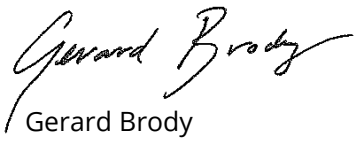
Passing the ratio should not replace Administrators' certification duties under the Act. We refer to Marie's case study in the Senate Inquiry Submission. Marie's Part IX would be exempt from complying the payment to income ratio due to her interest in the family home. However, our analysis revealed that her Marie's payment to income ratio would be a whopping 556%. As we have previously stressed, the family home will not be saved by unaffordable Part IXs that terminate for arrears or that contribute to mortgage arrears. Marie's example highlights the importance of AFSA's scrutiny of Administrators' certification

duties and its new discretion to reject Part IXs that will cause 'undue hardship,' particularly for Part IXs like Marie's which will be exempt from the payment to income ratio.

We recommend additional funding for AFSA to ensure it can properly scrutinise Part IX proposals for compliance with these new obligations.

Contact details
Please contact Cat Newton on 03 9670 5088 or at cat@consumeraction.org.au if you have any questions about this submission.

Yours sincerely,



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Appendix A: About the Contributors

About Consumer Action

Consumer Action is an independent, not-for profit consumer organisation with deep expertise in consumer and consumer credit laws, policy and direct knowledge of people's experience of modern markets. We work for a just marketplace, where people have power and business plays fair. We make life easier for people experiencing vulnerability and disadvantage in Australia, through financial counselling, legal advice, legal representation, policy work and campaigns. Based in Melbourne, our direct services assist Victorians and our advocacy supports a just market place for all Australians.

About Financial Rights Legal Centre

The Financial Rights Legal Centre is a community legal centre that specialises in helping consumers understand and enforce their financial rights, especially low income and otherwise marginalised or vulnerable consumers. We provide free and independent financial counselling, legal advice and representation to individuals about a broad range of financial issues. Financial Rights operates the National Debt Helpline, which helps NSW consumers experiencing financial difficulties. We also operate the Insurance Law Service which provides advice nationally to consumers about insurance claims and debts to insurance companies. Financial Rights took close to 25,000 calls for advice or assistance during the 2017/2018 financial year.

About Financial Counselling Australia

FCA is the peak body for financial counsellors. Financial counsellors provide information, support and advocacy for people in financial difficulty. They work in not-for-profit community organisations and their services are free, independent and confidential. FCA is the national voice for the financial counselling profession, providing resources and support for financial counsellors and advocating for people who are financially vulnerable. Financial counsellors frequently see clients who have been given inappropriate debt agreements.

Appendix B: Applying the payment-to-income ratio to Senate Inquiry Submission case studies

CASE STUDY	ELEMENT	AGD PROPOSAL		MINIMUM WAGE		BITA	
(Page ref)							
	Effective minimum income to propose Part IX	$ 12,500		$ 37,398		$ 57,239	
	Low income debtor amount (A)	25,000		74,796		114,478	
		Actual	**3-year**	**Actual**	**3-year**	**Actual**	**3-year**
"Marco"	Total repayments under Part IX **(B)**	$ 19,890	$ 11,934	$ 19,890	$ 11,934	$ 19,890	$ 11,934
Page 7	Debtor's after tax income **(C)**	$ 23,823	$ 23,823	$ 23,823	$ 23,823	$ 23,823	$ 23,823
	Payment to income ratio (A+B)/C	**188%**	**155%**	**397%**	**364%**	**564%**	**531%**
	Prevent bad Part IX (more than 200%)?	**N**	**N**	**Y**	**Y**	**Y**	**Y**
		Actual	**3-year**	**Actual**	**3-year**	**Actual**	**3-year**
	Total repayments under Part IX **(B)**	$ 43,264	$ 22,464	$ 43,264	$ 22,464	$ 43,264	$ 22,464
"Marie"	Debtor's after tax income **(C)**	$ 12,287	$ 12,287	$ 12,287	$ 12,287	$ 12,287	$ 12,287
Page 8	**Payment to income ratio (A+B)/C**	**556%**	**386%**	**961%**	**792%**	**1284%**	**1115%**
	Prevent bad Part IX (more than 200%)?	**Y**	**Y**	**Y**	**Y**	**Y**	**Y**
		Actual	**3-year**	**Actual**	**3-year**	**Actual**	**3-year**
"Jemila"	Total repayments **(B)**	$ 11,700	$ 9,360	$ 11,700	$ 9,360	$ 11,700	$ 9,360
Page 11	Debtor's after tax income **(C)**	$ 22,620	$ 22,620	$ 22,620	$ 22,620	$ 22,620	$ 22,620
	Payment to income ratio (A+B)/C	**162%**	**152%**	**382%**	**372%**	**558%**	**547%**
	Prevent bad Part IX (more than 200%)?	**N**	**N**	**Y**	**Y**	**Y**	**Y**
		Actual	**3-year**	**Actual**	**3-year**	**Actual**	**3-year**
"Jen"	Total repayments **(B)**	$ 24,475	$ 14,664	$ 24,475	$ 14,664	$ 24,475	$ 14,664
Page 14	Debtor's after tax income **(C)**	$ 49,764	$ 49,764	$ 49,764	$ 49,764	$ 49,764	$ 49,764
	Payment to income ratio (A+B)/C	99%	80%	199%	180%	279%	260%
	Prevent bad Part IX (more than 200%)?	**N**	**N**	**N**	**N**	**Y**	**Y**
		Actual	**3-year**	**Actual**	**3-year**	**Actual**	**3-year**
"Narelle"	**Total repayments (B)**	$ 31,720	$ 19,032	$ 31,720	$ 19,032	$ 31,720	$ 19,032
Page 23	**Debtor's after tax income (C)**	$ 37,544	$ 37,544	$ 37,544	$ 37,544	$ 37,544	$ 37,544
	Payment to income ratio (A+B)/C	151%	117%	284%	250%	389%	356%
	Prevent bad Part IX (more than 200%)?	**N**	**N**	**Y**	**Y**	**Y**	**Y**

Notes

1. All client names have been changed for privacy reasons
2. Marco's figures based on instructions, not a Part IX proposal
3. Otherwise, figures generally as stated on the Part IX proposal - client instructions and actual figures may differ
4. Marie's case would be exempt from complying with the payment-to-ratio due to an interest in the principal place of residence
5. Debtor's after tax income (C) based on Item H on Part IX Proposal (Debtor's taxable income less income tax and Medicare levy expected in the next 12 months)
6. Minimum Wage as at 15 October 2018 was $719.20 per 38 hour week: https://www.fwc.gov.au/documents/awardsandorders/html/pr606629.htm
7. Base Income Threshold Amount (BITA) as at 15 October 2018: https://www.afsa.gov.au/insolvency/how-we-can-help/indexed-amounts-0