Level 6, 179 Queen Street
Melbourne, VIC 3000

info@consumeraction.org.au
consumeraction.org.au
T 03 9670 5088
F 03 9629 6898

23 March 2023

By email: creditreforms@treasury.gov.au

Director, Consumer Credit Unit
Financial Services Division, Treasury
Langton Cres
Parkes ACT 2600

Dear Mr McAuliffe

Exposure draft – consumer credit regulations

Thank you for the opportunity to provide feedback on the Exposure Draft National Consumer Credit Protection Amendment (Financial Sector Reform) Regulations 2023 (**Draft Regs**), and Explanatory Statement (**ES**). A list of all the contributing and supporting organisations to this submission is provided at the sign off to this letter, and our logos are above (**Our Organisations**).

Our Organisations routinely advise and assist people who have multiple payday loans and/or consumer leases that they took on due to their financial hardship, but which only further entrench their hardship. We are all members of the Stop the Debt Trap Alliance, a broad group of community and consumer focused organisations that have advocated for the reforms contained in the *Financial Sector Reform Act 2022* (**FSR Act**) to be implemented for years.

We strongly support the majority of the content of the Draft Regs and ES. If made, they will do a good job of ensuring that the FSR Act reforms operate as recommended in the final report of Treasury's 2016 Independent Review of Small Amount Credit Contracts (**SACC Review**).[1] However, there are some sections that may need amending to ensure the SACC Review recommendations are delivered in full.

[1] The Australian Government the Treasury, *Review of the small amount credit contract laws – Final report*, March 2016, available at: https://static.treasury.gov.au/uploads/sites/1/2017/06/C2016-016_SACC-Final-Report.pdf

Once these issues are resolved, we urge the Government to make these regulations as quickly as possible, so that they commence when the provisions in the FSR Act applying to small amount credit contracts (**SACCs**) and consumer leases come into effect on 12 June 2023.

A summary of recommendations is available at **Appendix A**.

Regulation 28HB – additional verification requirements

We support the introduction of reg 28HB and the requirement for SACC and consumer lease providers to obtain the information in income and deduction statements issued by Services Australia where they exist for potential customers, and particularly support the need to obtain deduction statements to assess consumer lease affordability.

SACCs and consumer leases are products that are targeted at people on low incomes. A significant portion of the people likely to apply for these products will rely on Centrelink or other social forms of social security payments as part of their income. This is reflected in our casework relating to these products as well – a majority of our clients using these products are in financial hardship.

For SACC or consumer lease providers to undertake a proper affordability assessment (especially considering this will need to involve confirming 'available income'), they should be obtaining these documents. In our experience, the current methods used by both SACC lenders and consumer lessors to assess affordability are systematically flawed and regularly result in significant errors that result in people being signed up to products requiring repayments which cause them substantial hardship (e.g.,being on notice that the prospective borrower is receiving a social security payment and using a general figure reflecting that payment rather than sighting the specific amount the borrower receives). We accordingly support the introduction of this requirement as a step that will improve the accuracy of these assessments.

Deduction statements particularly important for consumer leases

The obligation for consumer lessors to obtain a deduction statement is particularly important while it continues to be possible to pay for consumer leases via Centrepay.

Many consumer lessors prefer to use Centrepay as their method of charging consumers eligible for it as they are effectively guaranteed payment, regardless of the other expenses customers may be struggling to manage, including essentials not on Centrepay, like food. In our view, continuing to permit consumer leases to be paid via Centrepay is a concerning arrangement that can exacerbate financial exclusion. It means high cost credit payments will continue to be prioritised over other essentials. While the reforms in the FSR Act will reduce the harm this causes, the underlying problem will remain.

That said, for consumer lessors to ensure compliance with the protected earnings amount cap under the new s 156B of the *National Consumer Credit Protection Act 2009* (**NCCP Act**) introduced by the FSR Act, it is essential that they identify all other ongoing payments a potential lessee is making for other consumer leases. With a significant portion of the market using Centrepay for payments, obtaining these deduction statements will go some way to verifying when a portion of available income is already committed to other lease arrangements.

Guidance should prohibit obtaining MyGov or Services Australia login details

We support designating income and deductions statements by Services Australia as constrained documents as per reg 28LCC in the Draft Regs. We assume the Government is satisfied that this will sufficiently address any risk of these documents, and the information in them, being used for any other purpose than assessing compliance with responsible lending obligations.

However, we have some concern around the methods industry will use to obtain these statements. In order to obtain bank statements for affordability assessments, screen scraping has become commonplace amongst these

industries, a process which requires the applicant to provide their banking username and password to a third party. Alternatively a SACC or consumer lease provider may simply ask and obtain the passwords to download the required documents on behalf of the customer themselves. Presumably, the equivalent for Services Australia statements may involve requiring the MyGov or Services Australia usernames and passwords for on the spot compliance.

Treasury should liaise with Services Australia about this issue and the risks it involves, including whether individuals may be breaching terms of their Services Australia or MyGov platform use by doing this, and if there may be consequences for doing so. If there is, we urge the Government to consider proactively clarifying for SACC and consumer lease providers that this business practice will not be acceptable. Possible ways this could be achieved may be via a note in the regulations, or via ASIC guidance, though stronger options may be necessary if the risks to consumers experiencing vulnerability are greater.

RECOMMENDATION 1. Take steps to clarify (whether in the regulations, ASIC guidance or otherwise) that SACC and consumer lease providers must not obtain the Services Australia or MyGov usernames and passwords of potential customers to meet the requirements in reg 28HB of the Draft Regs.

Drafting issues

In the first line of the second paragraph on page 4 of the ES, we believe the word 'licenses' should read 'licensees'.

Regulations 28LCA-28LCD – protected earning amount (PEA) caps

We strongly support the introduction of PEA caps for both SACCs and consumer leases, and their being set at 10% of available income. We understand the definition of available income to effectively mean net income after tax – and that this would be the same for social security payment recipients - though we are not experts in Australian taxation laws and urge Treasury to ensure that this definition would effectively describe real net income for social security recipients as well.

This is consistent with the recommendations of the SACC Review,[2] and with the intention described in the Explanatory Memorandum to the FSR Act.[3] We are aware that the SACC and consumer lease industries each significantly lobbied for these restrictions to be relaxed in different ways, such as by increasing the 10% caps, or treating SACCs and consumer leases as a combined 20% cap. We would strongly oppose any amendments that relaxed this requirement in any form. These are high cost credit products and committing any more than 10% collectively to either product (whether across one or many loans/leases) is a strong indicator that a person is in financial hardship.

However, we hold concerns about the way regs 28LCA and 28LCB are drafted. It appears the application of the provisions would cause problems if the repayment periods are different to the intervals at which someone is paid their income. We are concerned this may raise problems:

- if, for example, a person is paid monthly, but repayments on a SACC/lease are fortnightly, their income in a fortnightly repayment period when they do get paid would effectively mean 10% of their monthly income could be taken up by a fortnightly repayment.
- conversely, this would probably also result in an alternate fortnightly repayment period where the person's available income would be zero (as they do not receive monthly pay), meaning no lending is possible.

This would likely mean that lenders and lessors would be required to match their repayment periods with an applicant's income payment frequency. This would not be the worst outcome if intended, but we flag this issue. In

[2] https://treasury.gov.au/consultation/review-of-small-amount-credit-contracts-final-report
[3] Available at: https://www.aph.gov.au/Parliamentary_Business/Bills_Legislation/Bills_Search_Results/Result?bId=r6909

particular, we urge the Government to ensure that there is no risk these provisions could be worked to artificially inflate the available income of consumers if misused by SACC or lease providers.

RECOMMENDATION 2. Ensure that the definition of repayment period and the way it applies in relation to the PEA Caps at regs 28LCA and 28LCB does not create a risk of available income figures being calculated at a rate that is higher than actually reflects a consumer's true financial situation, due to differences in pay cycles and repayment periods.

Avoidance schemes

We generally support providing extra guidance in relation to the interpretation of the anti-avoidance provisions contained in the FSR Act.

Draft regulation 40

We particularly support the factors set out at reg 40(3) relating to avoidance of the various fee limits that apply to SACCs. The obscene fees charged by Cigno as a pseudo credit broker cause some of the worst harm in the credit market at present, and we anticipate that these provisions would help capture harmful similar models. The absence of any realistic avenue for external dispute resolution against Cigno is a major problem, and we support the inclusion of reg 40(5) in particular.

However, we are not sure reg 40(2) of the Draft Regs would help these provisions work as intended, and may risk having the unintended consequence of reducing the scope of the anti-avoidance provisions. For example:

- if a scheme was making use of one of the subsections of the National Credit Code (**NCC**) listed to avoid the application of the credit law, under this provision would it be more or less likely to be considered to have an avoidance purpose? We assume the intent is that a model relying on these exemptions is indicative of an avoidance purpose, but could an argument be made that a credit product designed to fall within specific exemptions in the NCC actually indicates a legitimate basis for otherwise sitting outside the scope of the credit law?[4]
- if applying to a scheme that strongly appeared to have an avoidance purpose but the model did not involve the listed subsections of the NCC, would mandating the consideration of this provision by the court risk requiring the conclusion that it did not have an avoidance purpose? This provision appears to be drafted to address the existing Cigno models, but it doesn't mean all possible harmful models will involve the same characteristics. While we recognise that s 323B(2) of the FSR Act clarifies that the list of mandatory considerations does not limit other things that can be considered, we urge the Government to ensure this would not unintentionally restrict the scope of the anti-avoidance provisions.

While helpful for the Cigno model, we also question whether reg 40(4) could hinder cases against otherwise clearly avoidant models that do not involve two contracts in future, as well. If a model involved more costly fees but only one contract, would this provision risk forcing a conclusion that the model's costliness was not relevant to the question of whether it had an avoidant purpose?

We appreciate providing additional guidance without restricting the scope of the anti-avoidance provisions can be difficult, and would generally support the primary purpose of ensuring that known harmful models like Cigno will be captured. However, we suggest Treasury consider whether it would be valuable to insert statements such as, "without limiting the scope of section #" at the start of these subregulations, to reduce the risk of limiting the breadth of the anti-avoidance provisions.

[4] In our view, these exemptions (particularly NCC sections 6(1) and (5)) are outdated and inappropriate. We strongly encourage Treasury and the Government to consider their removal.

RECOMMENDATION 3. Ensure that the mandatory considerations prescribed by the regulations will not have the unintended effect of restricting the application of the anti-avoidance provisions.

Commencement date

The Draft Regs are proposed to commence on 12 June 2023, which is appropriate for most provisions linked to the FSR Act. However, the anti-avoidance provisions have already commenced operating. If the Regs could commence sooner, Regs 40 and 41 should commence immediately.

Consumer lease provisions

Disclosure

We support the additional obligations proposed to be included at reg 104A of the Draft Regs. Consumer lessees we assist routinely do not understand the fees involved in their consumer leases. Marketing in the industry almost universally focuses on a "low" per week or per fortnight payment which downplays the significant overall lease cost compared to the value of the good, as well as the other costs involved. While there are always limits to the impact disclosure can have upon consumer understanding of complex financial products like these, requiring clear information to be displayed prominently in the terms and conditions should be standard practice.

We also recommend that there be a requirement that goods leased be described in detail in the contractual documents, sufficient for the base price of goods to be adequately identified. Too often contracts are described without specificity, for example, '30 inch TV' or '5 seater lounge'.

RECOMMENDATION 4. Add a requirement in reg 104A that lease contracts contain sufficient detail to identify the specific product leased, including brand names and model numbers where relevant.

Base price of goods

We support what appears to be the general intent of draft reg 105AA to set the base price of leased goods at roughly the reasonable retail price of the good, as this reflects the SACC Review recommendation. That said, this is a very generous starting point for the lessor as it allows fees to be calculated on a price that already allows for an intermediary to profit from the sale.[5]

It is vital that this provision ensures a reasonable retail value is the *highest* that the base price can be set, but we are significantly concerned that this is not guaranteed by the drafting because:

- in some circumstances, lessors could artificially increase the value of the mechanisms for calculating the base price; and
- the intent of some of the subsections in reg 105AA(3) is not clear.

Under reg 105AA, the base price of new goods is the lesser of:

- recommended retail price (**RRP**), if it can be ascertained;
- the circumstances in reg 105AA(3)(ii) (discussed below); or
- if neither of the two above can be determined, the market value of the goods – which is 'fair market value'.

Alternatively, if a price agreed between the parties is lower than any of the above that apply, then that price will apply. We support this provision, though it does not offer any protection from manipulation of base prices, as lessors wield the power in these arrangements and would have no incentive to agree upon a lower price.

[5] SACC Review, p 55.

Recommended retail price

Where the leased good is widely available for purchase by retail customers in multiple stores, we assume a RRP is likely to be set and could be reasonably ascertained and reliable. However, if this is not possible the base price could be manipulated by lessors to effectively increase the fees which may be charged under a lease.

One situation where this could arise is if the lessors have the power to set (or influence) the RRP – a figure normally set by the supplier. Some lessors[6] sell their own branded products. While these products are often very similar to other products on the market, the lessor is probably the supplier in these situations, and so could set the RRP at their own discretion. A similar circumstance could arise if the lessor is the only retailer partner of a wholesale supplier – they may be able to influence the RRP a supplier sets through their business relationship.

Under reg 105AA, this RRP would be the base price, and it would determine the fees that may be charged under the lease. Manipulation of this figure is a real risk and one that needs to be addressed in this provision. The current drafting is insufficient in this regard. Use of RRP as a base price needs to require some guarantee that the product is genuinely available elsewhere (preferably for outright purchase) in the retail market, or needs to involve some requirement to ensure it is unable to be set at a price significantly higher than other like products on the market.

The simplest fix we can see would be to replace the use of RRP with "cash price", as defined in section 204 of the NCC. This definition is already used throughout the NCCP Act, and is less susceptible to manipulation.

However, if there was concern that this would sell lessors short, the current reg 105(3)(a)(i) could be expanded to allow the RRP to be the base price, **but only if** the goods are reasonably available for outright purchase from multiple retail stores.

RECOMMENDATION 5. Address the risk of lessors manipulating the recommended retail price of leased goods that are not widely available from other retailers, by setting the base price as the cash price in these circumstances.

Reg 105AA(3)(a)(ii) intention unclear

Adopting the cash price definition may also dispense with the need for an alternative backup mechanism for determining the price if no RRP was ascertainable. The cash price definition also defaults back to the fair market value of the goods if a cash price cannot be reasonably ascertained.

However, if this approach is not taken or if a backup is still required, reg 105AA(3)(a)(ii) may require revising, as its meaning is not clear to us as is currently drafted, and it appears to be inconsistent with the intended meaning described in the ES. The proposed meaning in the ES[7] would be an appropriate and useful mechanism, though it is quite similar to "cash price" as defined in the NCC.

RECOMMENDATION 6. Revise subregulation 105AA(3)(a)(ii) so it reflects the intent in the Explanatory Statement.

Fair market value

The final fallback, fair market value, is not defined in the Draft Regs or NCC and so we would assume would take on its ordinarily understood meaning. This appears likely to be resistant to artificial increases in value if the goods were not otherwise available on the market, though we encourage Treasury to consider if it is a sufficient safeguard for situations where the lessor is the "supplier".

Second-hand goods

The concerns we raise with regard to RRP also apply to its use in reg 105AA(4)(a)(i), for second hand goods.

[6] We are aware Radio Rental, or Thorn, have done this in the past. At the time of writing their website indicated they were not offering new leases though.
[7] Last line of page 14 – though we note that we think "ordinary" should read "ordinarily".

We generally support the approach to depreciation described in the Draft Regs for second hand goods. Due to the vast variety of the kinds of goods leased, in practice there will be great variation to the true rate at which some leased goods depreciate compared to others, as the lifespan of different household goods varies greatly. However, we accept that setting a general standard may be the simplest approach.

Termination fees

We strongly support the introduction of the substantial hardship provision in reg 105F of the Draft Regs. This is an appropriate mechanism to ensure that people already in substantial hardship can reasonably stop their consumer lease debts if they wish to do so without further penalty.

We also support the general approach taken to termination fees in the Draft Regs, which we think reflects the fact that the regulated contracts are leases and not hire purchase agreements, so lessors should not be entitled to impose additional fees if a person cancels the lease.

We understand however that (despite this mirroring the CHERPA Code of Conduct clause on Termination or Break Fees)[8] some lessors have expressed concern that this may create a moral hazard where lessees can return a good after 90 days without any penalty and go and sign up to a new lease for a newer product, leaving the lessor with a second hand item that is more difficult to lease.

We are not convinced that this is of significant concern – there are risks and downsides for a consumer in doing this, including that lessors will likely stop doing business with them as well as the time and logistical costs involved in replacing goods frequently. In our experience, moral hazard concerns raised by industry are often based far more in the theoretical than in real world experience. If Treasury are particularly concerned about the financial implications of this situation on lessors, we suggest consideration of a reduced depreciation rate for determining the base price of near new re-leased goods where this has occurred.

<u>Cleaning, repair and replacement costs</u>

We do not oppose clarification that lessees have a general obligation to take reasonable care of goods and in some circumstances may appropriately be liable for damage or deterioration if reasonable care has not been taken of the goods. However, we urge Treasury to consider the inclusion of an exception if damage has been caused by circumstances beyond the lessee's control, particularly in relation to domestic or family violence, extreme weather events or issues relating to systemic financial hardship, and especially when subregulation 105F(4) also applies.

Our organisations regularly assist people on low incomes who have consumer leases and who are victim-survivors of family or domestic violence. Unfortunately, the damage or destruction of leased goods by perpetrators of abuse is not uncommon. These clients are often experiencing severe vulnerability. The same can be said for individuals who have lost household goods as a result of extreme weather events. Other common issues for clients who turn to consumer leases are deeply rooted in systemic disadvantage and financial hardship, such as overcrowded houses and forced sharing of goods widely across a family. This can sometimes also lead to damage to property that is realistically not within the control of the lessee. To help account for such extremely vulnerable circumstances that arise, we recommend Treasury consider introducing a provision that at least requires lessors to consider waiving cleaning, repair or replacement costs if the damage to the goods has occurred as a result of family violence, extreme weather events, systemic financial hardship or other similarly distressing circumstances beyond the control of the lessee.

We also urge Treasury to ensure that use of the term "fair commercial prices" for restoration, cleaning and replacement fees is the most appropriate term to use to ensure fees charged are reasonable and prevent artificial

[8] http://cherpa.com.au/wp-content/uploads/2017/10/CHERPA-Code-of-Conduct-v10-10-2017-_draft.pdf, clause 6.1

increases. An alternative may be fair (or reasonable) market costs, similar to the terminology used in the base price calculation provision.

RECOMMENDATION 7. Require lessors to at least consider reducing or waiving cleaning, repair or replacement costs upon termination where damages caused to leased goods are caused by traumatic circumstances beyond the lessee's control, such as family violence, extreme weather events or issues related to systemic financial hardship.

Absence of cap on total default fees

The Draft Regs do not set a limit on default fees that may be charged under a consumer lease, as is possible under section 179GA of the FSR Act. While we understand that this is an intentional approach, we urge Treasury to reconsider this position and introduce some guidance on this issue. Even if the guidance was simply clarifying that that the fee for any individual default must not amount to a penalty or be disproportionate to the reasonable losses of the lessor, this guidance would be helpful in dissuading any attempt by the industry to recoup fees no longer permissible to be charged by the new 4% per month fee cap.

RECOMMENDATION 8. Introduce a regulation that sets a limit on the amount that may be recovered for a default by a consumer lessor (per s 179GA of the FSR Act). The limit should require that default fees are limited to a reasonable estimate of the loss arising for the lessor as a result of the default.

Further information

Please contact Policy Officer **Tom Abourizk** at **Consumer Action Law Centre** on 03 9670 5088 or at tom.a@consumeraction.org.au if you have any questions about this submission.

Yours Sincerely,

CONSUMER ACTION LAW CENTRE

FINANCIAL COUNSELLING AUSTRALIA

MONEYMOB TALKABOUT

FINANCIAL RIGHTS LEGAL CENTRE

NILS TASMANIA

WESTJUSTICE

VICTORIAN ABORIGINAL LEGAL SERVICE

CARE, ACT

THE SALVATION ARMY

THE ST VINCENT de PAUL SOCIETY NATIONAL COUNCIL

UNITING COMMUNITIES CONSUMER CREDIT LAW CENTRE SA

CONSUMER CREDIT LEGAL SERVICE WA

WOMEN'S LEGAL SERVICE VICTORIA

APPENDIX A - SUMMARY OF RECOMMENDATIONS

RECOMMENDATION 1. Take steps to clarify (whether in the regulations, ASIC guidance or otherwise) that SACC and consumer lease providers must not obtain the Services Australia or MyGov usernames and passwords of potential customers to meet the requirements in reg 28HB of the Draft Regs.

RECOMMENDATION 2. Ensure that the definition of repayment period and the way it applies in relation to the PEA Caps at regs 28LCA and 28LCB does not create a risk of available income figures being calculated at a rate that is higher than actually reflects a consumer's true financial situation, due to differences in pay cycles and repayment periods.

RECOMMENDATION 3. Ensure that the mandatory considerations prescribed by the regulations will not have the unintended effect of restricting the application of the anti-avoidance provisions.

RECOMMENDATION 4. Add a requirement in reg 104A that lease contracts contain sufficient detail to identify the specific product leased, including brand names and model numbers where relevant.

RECOMMENDATION 5. Address the risk of lessors manipulating the recommended retail price of leased goods that are not widely available from other retailers, by setting the base price as the cash price in these circumstances.

RECOMMENDATION 6. Revise subregulation 105AA(3)(a)(ii) so it reflects the intent in the Explanatory Statement.

RECOMMENDATION 7. Require lessors to at least consider reducing or waiving cleaning, repair or replacement costs upon termination where damages caused to leased goods are caused by traumatic circumstances beyond the lessee's control, such as family violence, extreme weather events or issues related to systemic financial hardship.

RECOMMENDATION 8. Introduce a regulation that sets a limit on the amount that may be recovered for a default by a consumer lessor (per s 179GA of the FSR Act). The limit should require that default fees are limited to a reasonable estimate of the loss arising for the lessor as a result of the default.