1 Margaret St
Sydney NSW 2000

GPO Box 4720
Sydney NSW 2001

TEL (02) 8299 9000
FAX (02) 8299 9607

Association of Building Societies and Credit Unions

Abacus
Australian Mutuals

31 July 2009

Mr John Hawkins
Committee Secretary
Senate Standing Committee on Economics
PO Box 6100
Parliament House
CANBERRA ACT 2600

Dear Mr Hawkins

Abacus – Australian Mutuals Submission
Senate Economics Legislation Committee Inquiry into the Trade Practices Amendment (Australian Consumer Law) Bill 2009

Abacus – Australian Mutuals is the industry body for credit unions, mutual building societies and friendly societies. Collectively, Abacus member institutions have more than $70 billion in assets and serve more than 6 million Australians.

Abacus welcomes the Senate Standing Committee on Economics' inquiry into the Trade Practices Amendment (Australian Consumer Law) Bill 2009, and is pleased to make this submission on behalf of Australia's mutual Authorised Deposit-taking Institutions (ADIs).

Mutual financial institutions in Australia play a critical role in delivering competition and choice in the market. Australia has a strong mutual financial services sector, including one of the largest credit union sectors in the world. As mutuals, Abacus members are committed to responsible and ethical retail banking services that put members, not profits, first.

Our commitment to our members and fairness in our dealings with them is clearly demonstrated by our performance and customer satisfaction ratings. It is enshrined in the first key principle of the Mutual Banking Code of Practice, which states to our members

"We will be fair and ethical in our dealings with you."

The Mutual Banking Code of Practice is the code of practice for Australia's credit unions and mutual building societies, the legal and moral commitment to deliver on our mutual promise to members of these institutions.

In this context, credit unions and mutual building societies are extremely concerned about some elements of the proposed Australian Consumer Law. Whilst we support this law in principle, it is vital for smaller institutions that there is certainty around the validity of standard-form contracts, given their widespread use in financial services – usage that benefits consumers and institutions alike.

Abacus strongly believes that a range of issues must be addressed before the Australian Consumer Law comes into effect. These include:

- make the existence of actual consumer detriment a central consideration of the unfairness test in the legislation;
- broaden the matters to be taken into account by a court to include consumer benefit, as well as detriment, arising from a contract term;
- remove the capacity for government to ban certain terms through regulation;
- broaden the exclusion of price terms to all price terms disclosed before or at the time the contract is entered into;
- exclude specifically negotiated terms that form part of standard form contracts;
- ensure ASIC has sole responsibility for consumer protection regulation in financial services;
- extend the commencement date of the legislation until at least 1 July 2010;
- remove the application of the regime to existing contracts that are renewed or varied.

Our detailed comments in relation to these matters are attached.

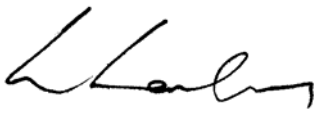
Credit unions and mutual building societies will continue to behave fairly to their members. There is little evidence in our sector of the usage of unfair contracts terms and no evidence has been put forward to suggest that our members are suffering detriment as a result of unfair contract terms.

In a difficult operating environment and with significant changes occurring in the consumer credit law area, it is critical that the proposed Australian Consumer Law does not create uncertainty for smaller institutions that rely on standard form contracts and that the law is targeted to areas where consumers are suffering detriment. Sufficient time must be provided to allow resources to be allocated to the compliance requirements without unnecessarily diverting those resources from activities that are already being applied for the benefit of credit union and mutual building society members.

Abacus members provide important competition and choice in the Australian retail banking market, but by virtue of their size, any government action that increases the regulatory compliance burden falls disproportionately on smaller institutions

Thank you again for the opportunity to comment on these proposals. If you wish to discuss the issues raised in our submission, please contact Matt Gijselman from Abacus Public Affairs on (02) 8299 9048 or mgijselman@abacus.org.au.

Yours sincerely



LUKE LAWLER
A/g Head of Public Affairs

1 Margaret St
Sydney NSW 2000

GPO Box 4720
Sydney NSW 2001

TEL (02) 8299 9000
FAX (02) 8299 9607

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Introduction

Abacus supports, in principle, the Government's intention to protect consumers through the introduction of an unfair contract terms regime as part of the Australian Consumer Law. Credit unions and mutual building societies are strongly supportive of a single, national approach to regulation in this area (as against the possibility of multiple inconsistent State-based regimes).

The mutual banking sector has taken some self-regulatory initiatives in relation to contract terms in our new Mutual Banking Code of Practice, which commenced on 1 July 2009[1]. The Mutual Banking Code of Practice includes a number of significant commitments relating to fair terms and conditions, as well as to fees and charges. These are set out in the Appendix to this submission.

Notwithstanding these commitments and our general support for carefully designed measures targeting substantive unfairness, Abacus considers that aspects of the Bill, must be reconsidered if the Government is to ensure the new regime is practical, proportionate, and fair to all stakeholders.

This submission focuses on those aspects of the regime that we consider should be modified.

Summary of Recommendations

Our recommendations are as follows:

i. make the existence of actual consumer detriment a central consideration of the unfairness test in the legislation;
ii. broaden the matters to be taken into account by a court to include consumer benefit, as well as detriment, arising from a contract term;
iii. remove the capacity for government to ban certain terms through regulation;
iv. broaden the exclusion of price terms to all price terms disclosed before or at the time the contract is entered into;
v. exclude specifically negotiated terms that form part of standard form contracts;
vi. ensure ASIC has sole responsibility for consumer protection regulation in financial services;
vii. extend the commencement date of the legislation until at least 1 July 2010; and
viii. remove the application of the regime to existing contracts that are renewed or varied.

[1] The MBCOP is the new industry code for credit unions and mutual building societies. It was developed by Abacus in conjunction with its member organisations and external stakeholders. The majority of credit unions and mutual building societies have subscribed to the Code.

Bill Provisions

a. Detriment should be central to the test for unfairness

The concept of detriment must play a much more central role in the meaning/test of unfairness than is currently envisaged in the Bill (see Schedule 1, Part 1, Division 1, Clause 3 (2)).

Our concern with the role currently assigned to this concept has a number of aspects. First, it is not satisfactory that the extent of detriment associated with the impugned term is merely something to be "taken into account"[2]. On the contrary, detriment should be an element to be proved.

Further, the onus of proof should lie with the claimant (just as it is proposed that the respondent party should be obliged to prove the impugned term is reasonably necessary to protect its legitimate interests, if it wishes to rely on this aspect of the unfairness test[3]).

Thirdly, the test should be that the term, if applied or relied on, would cause actual or material detriment, rather than merely a "substantial likelihood" of detriment, as the Bill currently proposes.

The approach Abacus supports is consistent with the Recommendation 7.1 of the Productivity Commission, as set out in the Final Report of its Review of Australia's Consumer Policy Framework. As the Commission noted in that Report, the real abuse is not the mere existence of unfair terms but their use against consumers in ways that are unfair. As the Commission also noted, evidence of detrimental impacts on consumers resulting from the existence of unfair terms is quite limited and largely anecdotal.

Given this uncertainty around the extent of the problem, requiring proof of actual detriment is the right approach to ensuring the regime is well-targeted and does not result in "regulatory overreach". For claimants and regulators to have to establish some actual material detriment to an individual or class (as applicable) will help ground use of the regime, and constrain any tendency to over zealous application.

To repeat, it is not the mere existence of supposedly unfair terms but their unfair application—resulting in detriment—that is the real abuse.

b. Matters a court must take into account should be broadened

In determining whether an impugned term is unfair a court may take into account "such matters as it thinks relevant", but must take into account the matters listed in Schedule 1, Part 1, Division 1, Clause 3 (2). These matters

[2] Schedule 1, Part 1, Division 1, Clause 3 (2)
[3] See 2.33 of the Explanatory Memorandum

are in summary: the extent of detriment or likely detriment; the extent to which the term is transparent; and the contract as a whole.

In (a) above, we submitted that detriment is something the claimant should be required to prove and that it should not just be a matter for the court to take into account. We also propose that the list of matters that the court should be required to take into account under Schedule 1, Part 1, Division 1, Clause 3 (2) should be broadened and made more balanced.

Specifically, as well as the extent to which the impugned term would cause detriment to a particular party, the court should be required to consider the extent of any benefits associated with the use of the term either to the claimant party, or to other parties to contracts including similar terms. Such benefits might include reduced transaction costs and better ability for a trader to limit opportunistic/dishonest conduct by a minority of customers. In other words, the matters the court must take into account should include efficiency as well as consumer protection considerations, and these should be required to be weighed in the balance in determining what is fair in the particular instance.

c. Provision for the regulations to proscribe terms should be removed

Abacus is pleased that the Government has decided not to proscribe particular types of terms in the initial text of the new law. However, we are disappointed that a power to ban terms outright through the regulations has been provided for (Schedule 1, Part 1, Division 2 Clause 6 (4)). This power is inappropriate and should be removed.

The outright proscription of terms runs contrary to the test of fairness in the Bill, which requires the court to consider the specific impacts of impugned terms in their specific contractual and other contexts rather than to consider terms in the abstract.

Outright proscription would involve considerable risk of regulatory error and/or overreaching. However apparently unfair a term may appear to be on its face, there may be circumstances in which its inclusion in a contract would be justified. We note that neither the UK nor the Victorian unfair contract terms regimes have relied on the outright banning of specific terms. It has not been suggested that this has limited their effectiveness in achieving the policy objectives of these regimes.

d. Exclusion of price terms should be broadened

Abacus strongly supports the exclusions set out in Schedule 1, Part 1, Division 1, Clause 5. However, the exclusion of price terms should *not* be limited to the “upfront price payable under the contract” as defined in Schedule 1, Part 1, Division 1, Clause 5 (1)(b). In our view, *all* price terms disclosed at or before the contract is entered into should be excluded.

Financial institutions such as credit unions and mutual building societies set and re-set fees on a regular basis, and these fees may apply to many thousands of account holders. The process is a complex one, and institutions need to be able to make decisions in an environment of certainty in relation to their regulatory obligations.

By contrast, the concept of fairness is inherently subjective. It is a broad ethical concept and, as such, does not include or signpost specific criteria or provide any real guidance to action. As a result, reasonable and sincere people may quite readily disagree about whether a particular fee is *fair* or not; and there is no easy way to decide who is right.

Further, a test based on the *fairness* of a fee may have unintended consequences. For instance, depending on how *fairness* is interpreted, someone with a high income and good credit record may, with some plausibility, object to the fairness of credit fees that in effect include a component of the costs associated with the provision of credit to other more high risk customers, or groups of customers. Does the mantra of *fairness* require that all of a credit provider's costs that can be attributed to particular customers or groups of customers must be directly charged to those customers? Or is the cross-subsidising of some customers permissible?

Conversely, if a fee is frequently or always waived or discounted for certain classes of high value customers (for example in a banking or finance context), would other customers be entitled to say that their continuing obligation to pay the fee is *unfair*?

Similarly, is it fair or unfair, for a lender to waive early termination fees for borrowers who are refinancing with the lender, but to require borrowers who are refinancing with another lender to pay the fee? Note that the concept of *fairness* is inherently comparative in nature, and will inevitably give rise to these kinds of questions—and, potentially, to fee disputes initiated by customers who do not get the benefit of particular policies of the lender or other supplier.

Abacus has already been made aware of circumstances whereby legal representatives have begun to challenge fees charged by an institution on the grounds that they are potentially unfair, and we hold significant concerns that without a carve out for price terms a major fee challenging industry will develop in Australia. Credit unions and mutual building societies already set fees as low as possible, whilst also recognising the need to treat all customers fairly – in recognition that not all can access banking services equally and some need to cross-subsidise to ensure equitable outcomes for all.

These are just a couple of examples (many more could be provided) of the practical difficulties associated with trying to apply as indeterminate a concept as *fairness* to fees and other price terms. Given these issues, Abacus urges the Committee to consider the scope of the proposed exclusion of price terms,

and recommend to Government that exclusion is applied generally to price terms (again subject to adequate disclosure being given).

This alternative approach would not preclude the possibility of introducing targeted measures in industry-specific legislation, when a need for such regulation was identified and the benefits of regulatory intervention were shown to outweigh the costs. For instance, the Consumer Credit Code provides some examples of a targeted approach to the substantive regulation of fees[4]. In our submission, a targeted approach of addressing particular issues *when they arise*, rather than through the use of general regulatory rules of indeterminate application is less likely to lead to regulatory overreaching and unintended side effects.

e. Extend exclusion of terms required or expressly permitted by law to include terms "contemplated" by law

We propose a minor amendment to the wording of the exclusion set out in Schedule 1, Part 1, Division 1, Clause 5 (1)(c) to cover terms *contemplated* by a law of the Commonwealth or State or Territory, as well as terms that are required or explicitly permitted.

In practice, legislation will often assume the existence and legitimacy of particular types of contractual term without necessarily *explicitly permitting* those terms. The Consultation Paper refers to some examples of this taken from the Uniform Consumer Credit Code. We submit that the amendment proposed puts the exclusion of such contemplated terms beyond doubt, and is consistent with the policy intent informing the drafting.

f. Application of the regime to individually negotiated terms in standard contracts should be excluded

Abacus fully supports the proposition that the operation of unfair contract terms legislation should be limited to standard form contracts; and we accept the approach to establishing that a contract is a standard form contract set out in the Bill (see Schedule 1, Part 1, Division 2, Clause 7).

In our view, however, the legislation should not only exclude terms that are part of non-standard form contracts. It should also exclude otherwise reviewable terms in relation to which there has been an effective opportunity to negotiate. In other words, if there has been a genuine negotiation of a particular term, a party to that negotiation should not be able to avoid that term just because, taken together with other terms, the resulting contract comes within the legislative definition of a standard form contract. We submit that this approach is consistent with the policy behind the legislation of

[4] See section 72, Consumer Credit Code, currently regulates establishment fees, early termination fees, and prepayment fees by giving power to the court to vary or annul any such fee if the court is satisfied that the fee is *unconscionable* (defined by reference to the lender's costs and/or income foregone). This provision will remain part of the national credit law regime.

limiting protection to contracts of adhesion in relation to which there is no capacity to negotiate, and where the consumer party is often not aware of the obligation imposed.

Currently, the Draft Provisions allow "an effective opportunity to negotiate" to be taken into account, but only as part of the test of whether a contract is a standard form[5]. In our view, this approach needs to be extended to allow negotiated individual terms to also be excluded.

Unless this approach is adopted, the exclusion of negotiated arrangements will be largely meaningless in the context of modern consumer (including banking and finance) transactions, where contractual arrangements are almost always based on standard form agreements (even if some aspects of the agreement may be negotiated).

Jurisdictional responsibility, implementation and administration

Abacus has significant concerns about the proposed process for implementing and administering the unfair contract terms regime.

Abacus considers that exclusive responsibility for the administration of consumer protection in relation to financial services (including credit) at the Commonwealth level should lie with ASIC, and that the ACCC and State and territory consumer agencies should not have jurisdiction in relation to financial services.

As proposed, the unfair contracts and other provisions of the Australian Consumer Law should be mirrored in relation to financial services in the ASIC Act. In addition, however, there should be a "carveout" of financial services from the Australian Consumer Law, to be administered jointly by the ACCC and the States and Territories. Such a carve out does not appear to be contemplated by the Bill. We would urge the Committee to recommend to Government a review this situation.

A carve out as proposed would be consistent with the current division of regulatory responsibilities between ASIC (under the ASIC Act) and the ACCC (under the Trade Practices Act). This arrangement has worked satisfactorily in practice in our experience, and we believe it should be continued.

The regulation of a complex area such as financial services is best administered by an industry-specific regulator. There does not appear to be any obvious advantage from a consumer perspective in having more than one agency involved. Indeed, the involvement of multiple agencies is likely to lead to confusion about responsibilities, and additional costs to Government in addressing these.

Credit unions and mutual building societies are already required to deal regularly with a range of Commonwealth Government agencies including APRA, ASIC, AUSTRAC, the Office of the Privacy Commissioner, and the ATO. Re-introducing the ACCC as a potential regulator in the consumer protection space would require our

[5] Section 7(d), ACL; section 12BK(2)(d), ASIC Act

members to commit additional resources to meeting the requirements of yet another regulator.

More critically, there would be real potential, particularly over time, for policies and approaches to differ between the two regulators, and for there to be overlap or duplication of regulatory activities. While we acknowledge the intention to develop national guidance on enforcement of the new law, experience suggests that this is likely to be an imperfect mechanism and that the quality of co-operation and liaison between regulators will vary over time.

The commencement date should be extended

The government's Australian Consumer Law implementation plan indicates that the legislation is intended to commence at the Commonwealth level on 1 January 2010[6]. This timeframe is not acceptable to mutual ADIs and will cause significant disruption of resources in what is already a challenging economic environment. Transitional arrangements must, as an absolute minimum, give businesses 12 months from the date of enactment to modify their contracts, where required.

Government should not underrate the considerable practical difficulties, as well as the costs, that the transitioning of contracts to the new regime will require. This will include the costs of obtaining legal advice, redrafting, adjusting systems and policies, printing, and staff training.

To date unfair contract terms legislation has only been enacted in Victoria, and, critically for our member organisations, the Victorian regime has only recently applied to credit. In addition, there are important differences between the Commonwealth and Victorian legislation. In Victoria, rights of action are not conferred on individual parties, but instead action can only be taken by the Director of Consumer Affairs Victoria.

The capacity through the Bill for any individual to challenge contract terms, combined with the low costs to consumers associated with accessing EDR schemes and other forums for redress, creates significant and unacceptable reputational and cost risk for institutions covered by the regime (including credit unions and mutual building societies) from the moment it is implemented.

While it may be the case that some large nationally operating businesses have adjusted practices and contracts in light of the Victorian legislation, this will by no means be true of all businesses, including many of Abacus' member organisations (many of which operate in geographically defined regions). Thus, it is wrong to assume that a short period only is required for businesses to transition to the new legislation.

We strongly urge the Committee to recommend to Government an extension of the commencement date for the legislation by at least 6 months.

[6] See http://www.treasury.gov.au/consumerlaw/content/implementation_plan.asp

The regime should not be applied retrospectively to existing contracts
The Bill indicates that the unfair contract terms regime will apply to contracts entered into before the commencement date when these contracts are renewed or varied after the commencement date (see Schedule 1, Part 2, Division 3, Clause 10 (2)(b)).

If implemented, this provision will give the legislation a substantially retrospective character in relation to banking and finance contracts. Interest rates, fees and charges, credit limits, amounts permitted to be borrowed and other similar terms of such contracts are regularly varied as part of their normal operation. The consequence of the proposal would be that large numbers of banking and finance contracts written before the legislation came into operation, or was even under consideration, will be progressively (and often within a short time frame) brought within its scope.

This situation would be both unfair to business, and extraordinarily costly and burdensome to manage.

We urge the Government to limit the operation of the legislation to new contracts entered into after the commencement date, and not to apply it retrospectively to pre-existing contracts that are varied after that date.

Appendix

Extract of Mutual Banking Code of Practice [MBCOP] provisions relating to contract terms

The MBCOP includes a number of commitments relating to fair terms and conditions. These are set out primarily in Part D.4 of the Code, which states:

> ***4. Fair terms and conditions***
>
> ***(4.1)*** *The standard Terms and Conditions applying to our products and facilities will be:*
> - *Clear, unambiguous, and not misleading*
> - *Distinct from our advertising and promotional material*
> - *Written in a plain language style, and legibly presented.*
>
> ***(4.2)*** *Our standard Terms and Conditions will be consistent with this Code and will strike a fair balance between:*
> - *Your legitimate needs and interests as our member or customer, and*
> - *Our interests and obligations, including our prudential obligations*
>
> ***(4.3)*** *We will not adopt standard Terms and Conditions that you are unlikely to be able to comply with.*
>
> ***(4.4)*** *This section:*
> - *Is not intended to limit our right to determine the pricing of our products and facilities on a commercial basis*
> - *Only applies to standard Terms and Conditions entered into after the Commencement Date of this Code.*

In addition, Part D.5, MBCOP, makes some specific commitments regarding the level of subscribing institutions fees and charges. Part D.5 states:

> ***5. Reviewing fees and charges***
>
> ***(5.1)*** *We will regularly review any fees and charges on our products and services, including their level.*
>
> ***(5.2)*** *We will make sure any exception fees we charge (including credit card late payment fees, account overdrawn or dishonour fees, direct debit dishonour fees, cheque dishonour fees, and ATM failed transaction fees) are reasonable having regard to our costs. Our costs include charges imposed by our service providers, where applicable.*

For additional information regarding this submission, please contact
Matt Gijselman
Abacus Public Affairs
Ph: 02 8299 9048
E: mgijselman@abacus.org.au