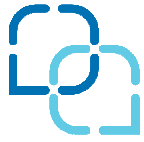

Consumer Credit Legal Centre NSW

July 2009

Submission to the Senate Economics Committee

In relation to the

National Consumer Credit Protection Bill 2009 & related Bills

Consumer Credit Legal Centre (NSW) Inc

Consumer Credit Legal Centre (NSW) Inc ("CCLC") is a community-based consumer advice, advocacy and education service specialising in personal credit, debt and banking law and practice. CCLC operates the Credit & Debt Hotline, which is the first port of call for NSW consumers experiencing financial difficulties. We provide legal advice and representation, financial counselling, information and strategies, and referral to face-to-face financial counselling services, and limited direct financial counselling. CCLC also operates the Insurance Law Service, a national service assisting consumers with disputes with their insurance company. CCLC took over 15,000 calls for advice or assistance during the 2008 financial year.

A significant part of CCLC's work is in advocating for improvements to advance the interests of consumers, by influencing developments in law, industry practice, dispute resolution processes, government enforcement action, and access to advice and assistance. CCLC also provides extensive web-based resources, other education resources, workshops, presentations and media comment.

Introduction and summary of submissions

Thank you for the opportunity to make a submission in relation to these Bills. Consumer Credit Legal Centre (NSW) Inc ("**CCLC**") also made an extensive submission to Treasury in relation to the Exposure Draft.

We appreciate that a number of our submissions were accepted, or partially accepted, and resulted in changes in the *National Consumer Credit Protection Bill 2009* ("**the Bill**") and associated Bills and Explanatory Memoranda (collectively "**the Bills**"). We particularly support the following:

- The extension of the responsible lending provisions to consumer leases (we hope that a broader review of consumer leases will also lead to amendments to the National Credit Code in Phase 2);
- The presumption against relying on the sale of borrower's home to repay credit contracts;
- The amendments to remove any ambiguity about whether an assessment of capacity to pay covers reasonably foreseeable future matters, not just the borrower's current circumstances;
- The prohibition on taking caveats to secure broker fees; and
- The increased scope of the small claims procedures.

We were disappointed with a number of changes that have occurred since the Exposure Draft, specifically the delayed introduction of the responsible lending provisions, and the non-applicability of the new $500,000 hardship variation threshold to existing contracts. These matters are discussed in detail below. We were also dismayed at the exemption for retail "point-of-sale" credit salespeople and look forward to the consideration of this issue in Phase 2.

While we have a number of other concerns in relation to the Bills, not least of which is the loss of the right to challenge excessive broker fees, and general unjust broker conduct in NSW, we have confined our comments in this submission to those matters which we consider are not only major issues for consumers, but also consistent with the governments stated intentions and policy parameters.

In brief we seek the following:

1. Deletion of the section which allows credit providers to rely on information verified by brokers (credit assistants and other intermediaries);
2. Clarification that EDR Schemes can award compensation to consumers in the absence of a declaration by the Court that a contravention or offence has occurred;
3. Introduction of the responsible lending provisions for credit assistants (brokers) in January 2010, and preferably for credit providers also, or at least non ADI credit providers;
4. Assurance that, depending on the response to item 3, that the appropriate State regulation (broker regulation and interest rate caps) will remain in place to ensure that there is no gap in protection for consumers, and in the case of the 48% cap, sufficient overlap with the responsible lending provisions to conduct a meaningful evaluation of their relative merits;
5. Credit providers should be required to assess a borrower's capacity to repay the entire debt within a reasonable term, not just their capacity to meet minimum repayments (as in the case of credit cards);
6. A commitment to considering a much broader range of practices under the umbrella of responsible lending in Phase 2, including all aspects of credit provision from marketing and advice, through to debt collection practices;
7. The Quote required to be accepted by consumers prior to a broker providing credit assistance should also include details of the consumer's credit requirements;
8. The amount of broker fees that can be financed into a loan should be limited to greatly reduce the potential for predatory lending, in the form of *equity stripping,* without directly controlling price;
9. The regime should take heed of the long history of creative avoidance of the law in this industry, as can be attested to by the State Consumer Protection Agencies, and give the Federal Court the power to declare arrangements which have the same effect as credit contracts to be caught by the Bills;
10. Licensees and their representatives should be required to commence action against consumers in the court registry nearest to where the consumer resides, or at the very least the State in which they ordinarily reside, or if this is not known, the State in which the contract was made. There should be penalties for non-compliance;
11. Further changes must be made in relation to dealing with financial hardship given the state of the global economy and record home repossessions-
    a. The new hardship threshold (and compulsory EDR) must apply to all existing home loans

b. The hardship options available under the Bills must be more flexible
c. The credit provider must have a responsibility to identify and reasonably respond in writing to all requests for financial hardship
d. If the lender refuses the request for financial hardship, it must give reasons for refusing the request
e. The lender must not take further legal action until a response to the request for hardship has been given in writing
f. When a lender commences legal action in a state court, such as the Supreme Court of a State in relation to home loans, the borrower must be able to apply for a stay in the Federal Magistrates Court or other local court/magistrates under the small claims procedure.

Detailed Submissions

Responsible Lending

Reliance on broker verification

The apparent intention of the responsible lending provisions of the Bill is to improve the quality of lending decisions in Australia, and particularly, the ability of the law to respond to unsatisfactory lending practices that may place the Australian economy at risk of the types of problems that have beset the United States, with ramifications for the global economy. With this in mind, we consider that section 130(3) is at odds with this underlying policy intention.

Section 130 (3) allows a lender to rely on information in a lending decision that has been verified by a credit assistant (broker) as part of a preliminary assessment of the suitability of a particular credit contract. This means that lenders can effectively outsource the verification of consumer information to a third party (who in many cases will be acting as the borrower's agent). We submit that this is undesirable for a number of reasons:

- It is inconsistent with the principle that lenders should be held accountable for their lending decisions. The ability to be able to shift risk to third parties has the potential to result in poorer lending decisions.
- This section weakens the current legal position, where lenders have in some circumstances been held to account for a failure to look behind information presented by a third party on behalf of a consumer.
- It does not improve the capacity of the law to respond to poor lending practices in the market place. On the contrary, it creates a situation where lenders who rely on the broker verified information might be in a better position than those who make their own enquiries and cannot therefore claim the benefit of a statutory defence (130(3)).

Sections 130(3) and 131(4) of the National Consumer Credit Protection Bill create an exception to the principle in the responsible lending Chapter, that lenders should be held accountable for their lending decisions. The exception applies in that a lender does not need to verify information that was:

- contained in a preliminary assessment, and

- used in the preliminary assessment.

A preliminary assessment will, by definition always be made by a broker or intermediary, while Section 130 only applies to lenders.

1. In our experience, subsection 130(3) is likely to be raised as a defence, and could be interpreted by the Courts and EDR schemes as limiting the credit provider's overarching responsibility to assess loan suitability, including verification, under sections 128, 130 and 131. This would completely undermine the intention of the legislation. Information is broadly defined and would cover both original documents (such as wage-slips) as well as information about the consumer's financial objectives. A lender can therefore properly maintain that information in a preliminary assessment meets the requirements in Section 131(4), that is, that it is either information which the lender reasonably believes to be true or information which, if the lender had made the inquiries or verification required by the broker, would reasonably believe to be true. Given that this is a criminal offence the courts are likely to adopt a strict interpretation of when an offence has been committed.
2. It follows that by relying on information in the preliminary assessment, and not making any additional inquiries, a lender can always transfer the risk of credit being unsuitable to a third party, the broker or intermediary. This has implications for the quality of lending and for the ability for consumers to seek an adequate remedy (their indebtedness being to the credit provider).

3. Even if section 131(4) proves sufficient in some cases to hold credit providers responsible after the fact, some credit providers may draw false comfort from 130(3) and allow a loan to proceed based on inadequate or inaccurate information provided by a broker. It is far preferable that unsustainable loans are not made than to seek to remedy the situation after the event.

The experience with business purpose declarations where fringe lenders were better able to argue that the Uniform Consumer Credit Code ("the UCCC") did not apply where they had made fewer inquiries that might displace the relevant presumption, indicates that there is likely to be lenders who will take advantage of this provision to systematically make unsuitable lending decisions while hiding behind a third party.

In two different matters in the NSW Supreme Court, one decided under the unjust contracts provisions of the Uniform Consumer Credit Code, and the other under the Contracts Review Act (NSW), the Court found that a contract was unjust in circumstances where "verified" information supplied by a 3rd party broker proved incorrect or unreliable. In the matter of *Permanent Mortgages v Michael Robert Cook and Karen Cook [2006] NSW SC 1104 (24 October 2006)* a broker supplied the lender with an accountants certificate verifying the borrowers capacity to pay in circumstances where the borrowers had never met the accountant and had provided no information upon which the accountant could have formed any view about their capacity to repay the loan. In *Small & Ors v Gray & Ors [2004] NSW SC 97 (5 March 2004)* the comments of the Justice McDougall at 55 are worth repeating in full:

> "*The Loan Enquiry Centre [broker] was not the agent of the plaintiffs [lenders] in any way. On the evidence, it was acting in the interests of Jarrod and Katrina [borrowers], and was remunerated by them, although the funds for its remuneration were provided out of the mortgage advance. If Mr Shoostovian [broker] had made any enquiry of Jarrod, Katrina and Kristine at the time of their meeting, it must have been apparent to him that they could not afford to meet their obligations under the proposed loan. Yet he was prepared to*

> *commission Mr Michael [accountant], as a purportedly independent expert, to provide a certificate that conveyed the very opposite impression. It is apparent that Mr Michael had received many such referrals from the Loan Enquiry Centre.*"

These cases may have been decided differently if the lenders had been able to point to statutory authority for their acceptance of the "verification" provided by the respective brokers above in the form of accountant's certificates.

While we accept that lenders may rely on brokers to obtain documentary evidence from borrowers to support their loan applications, we submit that the role of determining when, and in what manner, further verification of that information should occur should rest firmly with the lender. The potential for duplication created in the Bill (by both brokers and lenders conducting the same inquiries) would be better resolved by removing the requirement for verification of information from the credit assistant, and imposing this duty squarely on the credit provider.

We concur with the underlying intention in the Bill to improve the professionalism and accountability of credit assistants (brokers and other intermediaries). We do not, however, accept that the imposition of the licensing regime can altogether negate the structural incentives for brokers, who stand to benefit financially from the approval of any loan application and bear none of the default risk, to indulge in the types of practices described above. A broker either acts as agent for the lender in seeking to verify loan application information, in which case the lender should be ultimately responsible for any flaw in that process, or the lender should undertake the verification itself. Asking borrowers agents to verify borrower information is tantamount to getting borrowers to do it themselves, thereby completely defeating the purpose of the requirement.

Section 130 (3) allowing credit providers to rely on information verified by credit assistants should be deleted. Credit assistants are compelled by section 33 not to present any document that is false in material particular or materially misleading. Section 117(c) requiring brokers to verify information should be deleted.

Consumer's access to compensation

It is not clear whether sections 178 and 179 of the NCCP Bill mean that a consumer can only seek compensation if a civil penalty breach has been declared (or an offence is found to have been committed).

The Explanatory Memorandum says at 4.20 that "*consumer remedies are an important element of the enforcement package as it enables consumers to take direct action against a licensee who breaches the law and causes them loss or damage. Private suits are considered a useful way of influencing and curbing market behaviour, particularly in relation to the National Credit Code (Code)."* Also at 4.9 *"wherever possible, parties will be encouraged to resolve disputes without resorting to litigation. It is expected that courts would generally only be utilised where IDR and EDR processes have not resolved the matter, or where EDR is considered inappropriate."*

In order to give effect to both these stated intentions it is necessary that it is abundantly clear that and EDR scheme can find that a breach of the responsible lending provisions have occurred and that the consumer be granted appropriate remedies. We accept that it is not the role of EDR to apply civil penalties, but compensation to consumers under section 178, and the orders available under section 179, must be the subject of EDR consideration even in the absence of a declaration that an offence or contravention has occurred.

EDR schemes must be able to award damages and other remedies in the absence of a declaration that an offence or contravention has occurred.

Delayed introduction of responsible lending provisions

The delayed implementation of the Responsible Lending Conduct provisions of the Bill, which will not come into force until January 2011 is seriously disappointing. We are particularly concerned about the consequences of this delay in relation to brokers and fringe lenders.

Brokers (credit assistants)

We note that all the substantive obligations on brokers with the exception of the requirement to register with ASIC, join an EDR scheme, and subsequently obtain a licence, are found in the Responsible Lending provisions. While lenders have substantive obligations under the *Uniform Consumer Credit Code ("**the UCCC**")*, which will be carried over with some enhancements to the National Credit Code, in relation to disclosure, hardship, fees and unjust contracts (to name a few), there are no such obligations on brokers. NSW, ACT, Victoria and Western Australia all have varying degrees of broker regulation at present, but there is no equivalent law in the remaining States and the Northern Territory. Further, if the States were to *turn off* their credit legislation at the commencement of the *National Credit Consumer Protection Bill* in January 2010, there would be no regulation of broker activities for a full 12 months, including in States that currently regulate broker activities. This would be a significant loss of consumer protection in those States and an unacceptable result.

The proposed Responsible Lending Conduct provisions include:

- A requirement for brokers to disclose the nature of their services, including the range of lenders on their panel, and any fees payable by the consumer;
- A requirement to assess the suitability of any loan proposal, including whether the borrower has the capacity to repay the loan;
- A prohibition on upfront fees (payable prior to securing the loan); and
- A prohibition on using caveats on the borrower's home to secure broker fees.

We submit that these obligations, if some amendments are made, are both reasonable, and essential to addressing some of the most pressing problems in the credit market. In our experience, broker originated loans are overrepresented in irresponsible and predatory lending. Further, most reputable broking businesses would be substantially compliant with the above obligations, and were gearing up for the State-based *National Finance Broker Bill 2007*.

Consumer groups have lobbied since prior to 2003 for comprehensive national broker legislation. We are very disappointed to have to wait another 18 months. Further, unless the States and Commonwealth agree on urgent action to address the situation, the law may instead go seriously backwards in four States, including the most populous states, for a period of twelve months.

Fringe lenders

CCLC is also concerned about the activities of fringe lenders who have to date successfully avoided the UCCC. While section 70 of the UCCC, in conjunction with various industry codes of practice, have placed some parameters on the lending activities of mainstream lenders, other market players have acted without regard to the interests of the borrower. Asset lending relying on the borrower's home as security has been the norm in some parts of the market, usually relying on business or investment purposes declarations to avoid the operation of the UCCC. It would be ironic if the amendments to the UCCC in the National Credit Code were to capture these lenders within the regulatory net, but there were no substantive obligations within the law to address their undesirable practices (in the form of an obligation to assess capacity to pay). It is vital that these lenders are brought squarely within the new regime as soon as possible, in the interests of protecting vulnerable consumers and the broader economy.

The excessive cost of small amount lending (of which payday lending is a subset) is also a concern. In those States without interest rate caps, there are few substantive protections in the law (now, and in the Bills) in the absence of the Responsible Lending provisions. We are very concerned that these consumers are being left unprotected at a time of likely widespread financial stress due to rising unemployment.

Treasury has taken the view that the responsible lending provisions will be sufficient to address the harm associated with expensive, short-term lending and Minister Sherry announced that there would be a period in which both interest rate caps and the responsible lending regime would co-exist for the purpose of determining their relative effectiveness[1].

We are not convinced that the responsible lending provisions are adequate to address this problem. However, at a minimum, the responsible lending provisions must commence in January 2010 for these lenders or the interest rate caps must remain in place until at least 12 months after this date to allow meaningful evaluation to take place. Arguably, given the complexity of setting up appropriate comparative research, and the period over which outcomes may need to be observed[2], this period may need to be even longer.

We submit that either the responsible lending provisions should commence in January 2011 as originally planned or:

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[1] "NICK SHERRY: Yeah, payday lenders will be covered by this legislation. I think three states have a 48 per cent cap. That will be retained. What we are doing is adding this new responsible lending principle for the first time. Those states that don't have a 48 per cent cap, we're going to ask them not to impose a 48 per cent cap, and then we will assess the outcomes; we'll look at what has happened in the states that have a 48 per cent cap and those that don't, with a responsible lending provision that has come into force, and we'll look at what the outcomes are and determine whether it is appropriate to maintain that 48 per cent cap. It's a good example, I think, of a practical way to assess the evidence in an area where there was strong disagreement between the various people, organisations who were consulted. This was one of the - an important area, one of the relatively small areas where there was disagreement during the consultations." Transcript of joint press conference with Tony D'Aloisio, 27 April 2009, available at

http://ministers.treasury.gov.au/DisplayDocs.aspx?doc=transcripts/2009/021.htm&pageID=004&min=njs&Year=&DocType=2

[2] In order to evaluate the effectiveness of the new provisions it will no doubt be necessary to not only observe developments in the market, but also to attempt to use the different provisions available in a casework context to determine their effectiveness in responding to the problems the legislation is designed to address.

- The relevant provisions commence in January 2010, but allow a longer transition provision for some lenders such as Authorised Deposit Taking Institutions (we recognise this may have ramifications for competition);

- The relevant provisions commence in January 2010 for brokers (credit assistants) and January 2011 for credit providers.

In the latter scenario we would seek the support of the relevant States, and the Commonwealth, to ensure that the interest rate caps currently in place remain operational and enforced until at least January 2012 for the reasons outlined above.

Capacity to repay should reflect borrowers' ability to pay off the entire loan within a reasonable time, not their ability to meet minimum repayments for the term of their natural lives

While the NCCPB addresses increasing credit limits without making a proper assessment of the borrower's financial circumstances, it does not address the fact that a borrower's ability to meet a minimum repayment on a credit card, for example, is not evidence of their ability to repay the debt in full.

The Reserve Bank of Australia reported credit card debt nationally at a total of $44.6 billion dollars in August 2008,[3] bringing the average credit card debt at that time to an unprecedented $3,200.[4] In CCLC's experience, many consumers owe significantly more than the reported average, a figure that is substantially distorted by the large number of accounts that are paid out fairly regularly, if not every month. Of 2553 callers to the CCLC with credit card debts between 1 September 2004 and 30 June 2006, for example, 500 callers owed $3000 or less, 2,005 owed between $3000 and $80,000, with 48 owing more than $80,000. In fact the average amount owed per person was $14,099, and the average amount owed on each card account was $9,843, both significantly higher than the somewhat misleading national average.

When lenders assess a consumer's capacity to meet credit card payments, they appear to rely on their ability to meet the minimum contractual repayment. This approach is consistent with the approach to responsible lending taken in the Bill.

Minimum repayments rates and interest rates available on the market in October 2008[5]

Note, the minimum repayment schedule for NAB card is based on a minimum credit limit if $500, but $1,000 for all other cards.

Credit card provider	Min Repayment %	Retail purchases interest rate
ANZ Low Rate Mastercard	2.0% > $10	12.99%
ANZ First Visa	2.0% > $10	19.99%
Bendigo Basic Black	3.0% > $10	10.75%

[3] Credit and charge card data, Reserve Bank of Australia website: http://www.rba.gov.au/Statistics/Bulletin/C01hist.xls

[4] Reported widely, see for example: Credit Card Debt hits record $44 billion, http://www.news.com.au/business/money/story/0,25479,24191393-14327,00.html, call for cut in credit card rate, http://www.abc.net.au/am/content/2008/s2386018.htm

[5] See Page 25 for Table 6 References.

Citibank Clear Visa	2.0% > $30	12.49%
Commonwealth Awards	$25	20.14%
Commonwealth Low rate	$25	12.64%
Bank SA Vertigo MasterCard	2.0% > $10	11.89%
Bank SA Starts Low Stays Low	2.0% > $10	12.99%
David Jones Amex	2.5% > $30	20.49%
David Jones Store Card	2.1% > $10	24.49%
GE CreditLine	3.0% > $40	29.49%
Myer Visa	2.2% > $10	19.99%
NAB Low Rate Visa	2.5% > $10	12.70%
NAB Visa Mini	2.5% > $10	19.74%
St George Starts Low Stays Low	2.0%	12.99%
St George No Annual Fee	2.0%	18.75%
Westpac Altitude	2.0% > $10	20.74%
Westpac Earth Card	2.0% > $10	17.99%

A GE Creditline card at 29.49% per annum assessed at 3% of the maximum balance, would take over 5 years to pay (assuming the borrower cannot afford to pay more than this) and result in more being paid in interest than the amount borrowed, even when the initial repayment is maintained (not reduced along with the balance[6]) and irrespective of account keeping fees (routinely applied) or penalty fees for late or missed payments. A David Jones store card at 24.49%, assessed at a minimum repayment of 2.1%, would usually take over 14 years to pay and cost multiples of the amount borrowed in interest. A Westpac Altitude at 20.74% interest assessed at 2% of the balance, would take over nine years to pay and cost more than the amount borrowed in interest. By contrast, the Bendigo Basic Black product, at 10.75% per annum and assessed at 3% of the maximum balance, would take under 4 years to repay and cost less in interest than the amount borrowed.[7]

While increasing minimum repayments (legislatively) would have an impact on this problem, it is a blunt tool that does not take into account the impact of different interest rates. A preferred approach would be to require credit providers to assess whether a loan can be repaid within a reasonable term, as part of the initial assessment, even if the loan is to have no fixed term. That is, a loan may be a continuing credit contract such as a credit card, but the lender must ensure that the borrower has the *capacity* to repay the loan within a *reasonable time frame* should they choose to do so.

In addition to the current problem with credit card debt, the focus in the responsible conduct provisions on the consumer's ability to meet repayments in the absence of any requirements in relation to the term of the loan, may lead to other contracts being structured to have lower repayments over an unreasonably long term.

Credit providers should be required to consider whether a loan can be repaid within a reasonable period, taking into account the purpose of the loan; or where there is no contractual obligation to repay the loan within a specified period (for example continuing credit contracts), whether the borrower has the capacity to repay the loan within a reasonable nominal term.

[6] If the repayments are reduced along with the minimum repayment shown on the statement the term stretches out considerably, often to over 90 years.

[7] Many of these products also involve in annual fee ranging from $24 -$100. The impact of Annual fees, or any other applicable charges, have not been taken into account in these calculations.

A more comprehensive approach

We draw your attention to the fact that the Consumer Credit Act in the UK recently added "the identification of irresponsible lending" as a matter to which the OFT must have regard to when it considers businesses' fitness to hold a consumer credit licence. The OFT is currently examining a wide range of issues including *advertising and marketing, selling techniques, product design, use of appropriate credit scoring techniques, and handling of defaults or arrears as well as behaviour and practices around a borrower's ability to repay credit*, with a view to developing regulatory guidance.

CCLC is concerned that the narrowly construed concept of responsible lending in the Bill, built entirely on disclosure and assessment of product suitability, will undermine the power of the regulator to address these broader issues effectively. The Government has described the responsible lending provisions of the Bill as "world leading".[8] We submit that while the legislation is detailed and prescriptive about some aspects of the credit process, it is out of step with the broader notion of responsible lending being adopted in other jurisdictions.

We encourage the government to adopt an equally broad view of the matters relevant to responsible lending in Phase 2.

The Government should commit to considering a much broader approach to responsible lending in Phase 2, including all aspects of credit provision from marketing and advice, through to debt collection practices.

Consumer's Credit requirements

A licensee must provide a quote for the credit assistance that is to be provided before providing credit assistance to a consumer. The quote advises the consumer of the maximum cost of the credit assistant's services and other information about the service to be provided. This document must be signed (or otherwise accepted) by the consumer. The Explanatory Memorandum to the Bill at 3.49 suggests that this *might* include the scope of the credit assistance to be provided, such as the consumer's requirements or the type of loan the consumer is looking for.

We submit that this obligation should be expressly defined in the legislation and substantially consistent with the uniform state *National Finance Broker Bill 2007* requirement for a Broker Agreement, about which extensive consultation was undertaken.

Specifically the quote should identify:

(a) the amount of credit sought by the consumer or (if the amount is not known) the maximum amount of credit, or the credit limit, sought by the consumer;

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[8] Media Release, Minister Bowen, *National Consumer Credit Protection Reform Package*, 25 June 2009, viewed at http://mfsscl.treasurer.gov.au/DisplayDocs.aspx?doc=pressreleases/2009/002.htm&pageID=003&min=ceba&Year=&DocType=0

(b) if the credit is to be for a fixed term, the term of the credit sought by the consumer;

(c) the maximum interest rate that (at current interest rates) the consumer would be prepared to accept in respect of the credit;

(d) the date by which the credit is to have been secured for the consumer; and

(e) a description of any special loan features (such as redraw facilities) that are required by the consumer.

Predatory Lending

Limiting the extent to which broker fees can be financed by a loan -Extract from CCLC submission to Treasury

Whereas the majority of brokers obtain their income from commission paid by lenders, some brokers (some of whom are classified as “introducers” by lenders rather than brokers) obtain their income from significant fees charged directly to the consumer and paid upon settlement of the loan out of the funds advanced (this may or may not be in addition to a commission paid by the lender). While we understand that the current squeeze on lender commissions may drive additional broker licensees to charge fees directly to the consumer, as a general rule these amounts are proportional to the work involved in providing the credit assistance. In the worst cases of predatory lending, however, these fees are substantial, exploitative, and could not be paid by the borrowers unless they were financed as part of the loan.

As demonstrated by the following table showing the amounts paid to brokers by actual clients of consumer assistance agencies compared to their loan amount[9], the amounts charged by some brokers bear no relationship to the amounts borrowed and are arguably more an indication of the relevant borrowers’ personal disadvantage or desperation (and arguably the risk perceived by the broker in undertaking a “dodgy” transaction).

Brokerage by Loan Size		
Loan amount	Brokerage	Percentage of loan
$122,000	$19,615	16%
$255,000	$19,855	7.7%
$255,000	$8,920	3.4%
$502,000	$16,000	3.1%
$110,000	$2,995	2.7%
$223,750	$5,500	2.4%
$300,000	$4,030	1.3%

[9] Details derived from an unpublished survey conducted by CCLC in May 2005 of legal aid, community legal centre and financial counselling clients who had refinanced their home loan in the previous five years in response to financial difficulty and then found themselves in financial difficulty again. More details are available in the CCLC submission to the Productivity Commission review of the Consumer Protection Framework, Submission 95 available at http://www.pc.gov.au/inquiry/consumer/submissions

$170,000	$1,105	0.65%
$256,000	$300	0.12%

In short, this practice is simply equity stripping – the brokers takes his or her fee at settlement and the lender later recovers the entire amount plus interest and default charges from sale of the security property when the borrower inevitably defaults.

In March 2008 the Australian Securities and Investment Commission **("ASIC")** issued Report 119, Protecting wealth in the family home: An examination of refinancing in response to mortgage stress. As part of the research informing that report, ASIC undertook an independent examination of 10 files covering mortgage transactions conducted by two brokers (5 files from each) who promoted themselves in advertisements as providing refinancing solutions for borrowers in arrears.

That examination found that one broker charged on average 5 times higher than industry standard remuneration and the other 16 times higher on average. The highest fee charged by either was 22 times higher than industry standard remuneration. Fees charged also represented between 4.4% and 30% of the borrowers existing equity in the property. ASIC found that there was no correlation between the fees charged and the amount of the loan, and no apparent relationship between the fees charged and the amount of work undertaken by the broker.

Limiting the amount of brokerage that can be financed as part of a loan is potentially an effective way to limit predatory lending, without direct price control. The worst examples of predatory lending seen by our agencies involve high returns to the broker on individual transactions and this is a key motivation to set up such loans. Taking away the significant profits available in this type of brokerage would go a considerable way to preventing such loans from occurring. This is far preferable than trying to address the damage after the event.

Further, unlike the "not unsuitable" product provisions, this measure could be more easily enforced because the matters to be proven are objective. Unscrupulous brokers, with an eye to their own lucrative commission, will often convince desperate consumers to agree to document false purposes (and no doubt objectives and requirements) and it becomes a case of whose evidence is the most credible in the event of a dispute. This means that the "not unsuitable" provisions may be the *least effective* against the *most reprehensible* conduct in the market.

While some consumers may be complicit in undesirable conduct, from carelessness (signing blank application forms) to varying degrees of fraud, this behaviour is often suggested, normalised and facilitated by the broker who stands to profit considerably from the transaction, and indulges in this conduct systemically (as opposed to in one desperate and ultimately self-damaging act). Further, as demonstrated by the sub-prime crisis in the US, where the terms "*liar loans*" and "*NINJA*[10]" loans originated, complicity or otherwise by borrowers has no effect on the potential for unsustainable loans to wreak havoc on the economy. A policy measure that decreases the incidence of such loans, without imposing additional obligations on the vast majority of industry participants is well worth considering.

This provision would represent good policy as it removes the economic drivers for brokers to engage in predatory conduct and, if the lender reimburses broker indirectly, then they are also actively involved in process and cannot point the finger at the broker and deny responsibility. This would reinforce the intention of the legislation – to reduce irresponsible

[10] No income, no job

lending - and would also address predatory lending in particular, which has not been done in any of the other provisions.

Limit the amount of broker fees that can be financed under a credit contract (as a dollar amount or a percentage of the loan or a combination of the two). This could be expressed as an amount and/or percentage to be set by the regulations to allow time to consult with industry about an appropriate amount.

Contravention of this provision should result in an automatic order for the loan to be reduced by the amount by which the broker fee exceeds the maximum amount. Any amounts payable to a third party credit assistant, or an associated entity, upon settlement should be presumed to be broker fees unless the contrary is established.

Avoidance

The UCCC has required a series of amending acts over the years to address loopholes as lenders innovate new ways of avoiding the application of all or part of the legislation. An extensive overview of the way in which lenders have systemically avoided the Code and facilitated predatory lending was provided in Appendix A of CCLC's original submission to Treasury in response to the Exposure Draft and is annexed to this submission.

While many of these arrangements have been designed to avoid the 48% cap in states where it has applied, they have not exclusively been used for this purpose. The desire to avoid compliance with disclosure obligations, hardship provisions and notice requirements have also inspired avoidance, in addition to the re-opening provisions of section 70 and 71 of the UCCC. In fact avoidance has also thrived in States without an interest rate cap. The licensing requirements included in this draft, in addition to the responsible conduct provisions we are yet to see, will add greater motivation to operators keen to minimising their obligations.

Many of the loopholes listed in Appendix A have been closed via specific amendments. Each amendment, however, has taken a lengthy period to become law, and is usually made redundant within a short time as a new avoidance method emerges.

Quick intervention into new ways of avoiding the credit law is crucial to maintaining its effectiveness. We recommend that the Federal Court be empowered with the ability to declare particular schemes or arrangements as "credit" under sections 3 and 4 of the National Credit Code and hence ineffective to avoid the operation of consumer credit legislation. This would facilitate timely intervention by regulators as problematic practices emerge, without relying on slow process of legislative amendments.

The Federal Court should be given the power to declare an arrangement, or series of contracts or arrangements, "consumer credit" where the net effect of the arrangement(s) is to extend access to funds to a consumer for a Code purpose in return for repayment of the funds extended plus additional interest or fees.

Access to justice

Appropriate jurisdiction

There are a range of problems created by consumers being sued in a jurisdiction outside the State in which they live. Even where the proceedings can be successfully stayed in the other

jurisdiction, there are a range of challenges in getting to that point. These challenges create barriers to justice for consumers and impose additional resource imposts on funded services where they are available to assist. In many cases, however, there are no appropriate services and consumers must fend for themselves. We are aware of consumers who have simply paid debts they did not owe because they had been quoted a prohibitive price for defending interstate proceedings by private lawyers. Worse, those same consumers are affected in multiple ways because the judgment is listed on their credit report, making it difficult for them to obtain credit in the future and/or driving them to higher cost alternatives.

The range of considerations for the transfer of proceedings in the legislation is perhaps useful and necessary but far from sufficient, because it requires somebody to actually plead the case for a transfer. We note that the legislation preserves the right to make further obligations in the regulations. We submit that this is absolutely necessary.

Credit providers should be required to commence proceedings at the court registry nearest to where the consumer resides, or at the very least in the State where the debtor resides, or if that is unknown, the State where the contract was made. There should be a penalty for non-compliance with this requirement.

There should be a simple process for consumers to object to jurisdiction and for licensees to be required to withdraw the proceedings at their own expense and recommence in the appropriate jurisdiction.

Financial Hardship

Summary: What needs to be done to ensure consumer's have adequate access to financial hardship

The Bill must be amended to include the following:

1) The new hardship threshold (and compulsory EDR) must apply to all existing home loans
2) The hardship options must be more flexible
3) The lender must have a responsibility to identify and reasonably respond in writing to all requests for financial hardship
4) If the lender refuses the request for financial hardship, it must give reasons for refusing the request
5) The lender must not take further legal action until a response to the request for hardship has been given in writing
6) When a lender commences legal action in a state court, such as the Supreme Court of a State in relation to home loans, the borrower must be able to apply for a stay in the Federal Magistrates Court or other local court/magistrates under the small claims procedure, without first having to apply.

The above are the bare minimum legislative changes required to ensure borrowers get adequate access to financial hardship assistance.

A failure to get access to hardship right means that borrowers will suffer terrible consequences including losing their home when they were going to be able to repay, losing the right to sell their home with dignity, stress, homelessness, rising bankruptcies and family breakdown.

With record numbers of home repossessions in NSW in particular, and rising unemployment forecast, this issue is both important and urgent. However, this is not about a "knee jerk" reaction to a temporary crisis which will result in long lasting laws that will soon lack relevance and prove a burden to industry without adequate cause. It is about developing sensible, well-balanced rights and processes that should be enduring. Hardship is a perennial issue. No one can guarantee that they will not have a problem with paying a loan over an extended period (up to 30 years or more) without facing problems such as illness, accident, unemployment, business failure or family breakdown, to name the most common causes of financial hardship. These laws will always be necessary; they will simply be called upon less in times of economic prosperity. The current crisis is not the only reason for having effective hardship laws, but it does provide the impetus for getting this right, and for getting it right as urgently as possible.

Inapplicability of hardship threshold and EDR membership to apply to existing contracts

The effect of the Transitional and Consequential Provisions is that the new hardship threshold of $500,000 will not apply to existing credit contracts. Similarly, credit providers (or debt collector assignees) will not be compelled to be licensed or to be members of an EDR scheme if they are only managing or collecting contracts which predate the commencement of the Bills.

This is at odds with the Governments public statements in relation to these matters[11] and a serious problem for consumers:

- Many current home loan borrowers may be affected by financial hardship now (as a result of the global financial crisis or otherwise) and into the future and will not benefit from the increase in the threshold. Data included below reveals that NSW in particular is already in the midst of record numbers of home repossessions. The then Minister for Financial Services, Superannuation and Corporations Law estimated that thousands of people would be assisted by the increase in the hardship threshold when in fact very few people are likely to benefit at all for some time after the changes have been introduced.
- A number of credit providers in the market are no longer granting new loans as a result of the credit crunch. Some of these lenders are non-conforming lenders (sub-prime) who offered loans at higher than average interest rates, and even higher default rates of interest. Borrowers with these loans are more likely to be affected by hardship (as a result of both the higher interest rates and the fact that they are more likely as a demographic group to be in more marginal, insecure employment) and yet

[11] The Assistant Treasurer's section of the Treasury Portfolio Minister's website alone has six transcripts of radio interviews highlighting the benefits to consumers of these new developments and never mentions their non-applicability to existing contracts, in fact quite the opposite is implied: ABC AM Program, 27 April 2009, 8.12am, interview with Emma Griffiths, "From November, people with mortgages of up to half a million dollars will, by law, be able to ask for assistance such as loan extensions or a repayment holiday from their bank," introduction by Tony Eastley; ABC Hobart Breakfast, 27 April 2009, interview with Tim Cox; 2UE Breakfast, 6.47am, 27 April 2009, interview with Mike Carlton and Sandy Aloisi; ABC2 News Breakfast, 7.50am, 27 April 2009, Interview with Virginia Trioli and Joe O'Brien; ABC Newsradio Breakfast, 8.18am, 27 April 2009, interview with Glen Bartholomew; 2GB Breakfast, 7.24am, Interview with Chris Smith – all viewed at http://www.treasurer.gov.au/listdocs.aspx?doctype=2&PageID=004&min=njs

these lenders will not be compelled to be members of an EDR scheme and none of these borrowers will benefit from the higher hardship threshold.

- Many borrowers in financial difficulty also have credit cards and personal loans. It is often these loans that can tip the balance in relation to whether a borrower can maintain repayments on their home loan, and/or lead to personal bankruptcies. When UCCC was introduced the hardship provisions under sections 66-68 of the UCCC were immediately applied to continuing credit contracts. Not even existing continuing credit contracts appear to be caught by the new provisions. While the new threshold is less likely to have any relevance for these personal debts, the requirement to be a member of an EDR scheme could benefit consumers who are being pursued by debt collector assignees.
- In contrast to the Governments assurances that the new system would be easier to understand and apply[12], the transitional arrangements will create a complex dual system that will be difficult understand, apply and advise upon. The Commonwealth Government will no doubt also have to take over the regular publishing of the applicable hardship threshold from the States to ensure that it continues to be available for anything up to 25-30 years after the legislation commences (the term of many home loans).

As we understand the situation the Government has been advised that applying these provisions to existing contracts would not be consistent with section 51(xxxi) of the Constitution, specifically that the Commonwealth may make laws with respect to acquisition of property on just terms. While we are not constitutional lawyers, we suggest that:

1. The Commonwealth's power to enact this legislation stems from the referral from the States and is not dependent on section 51(xxxi) for validity; and

2. The provision does not in any event breach section 51(xxxi) of the constitution because the power to increase the threshold by regulation has always been provided for under the existing law. That is, as the right arises under statute it is always susceptible to change by the parliament, and therefore the rights of the parties on this issue are not fixed at any point in time.

In relation to the latter point we note the following observation of the Deputy President of the Victorian Civil & Administrative Tribunal: "*I do not consider that my interpretation involves an impermissible retrospective application of s22A of the Regulations. The debtor hardship provisions, of their nature, apply to contracts already made. Section 22A does no more than change the ceiling from a fixed ceiling to a floating one for the purpose of the application of the debtor hardship provisions. This does not affect the point at which that ceiling applies. That point is when the debtor applies to the credit provider for a change of contract. Section 66(3) itself contemplates that the $125,000 figure there mentioned can be changed by regulation.*" [Harding v National Australia Bank Ltd (Credit) [2007] VCAT 1234 (9 July 2007) paragraph 35].

Given the previous public commitment of the Government we believe it is appropriate that further advice from more senior persons is obtained. We note that the legislation is to be supported by a referral of power from the States, and, while acknowledging that

[12] Minister Sherry, *"This measure will also provide greater certainty to credit providers – because the threshold has varied from between $295,790 and $368,390 since 2004, making it difficult for providers and consumers to know if a loan qualifies."* Press Release of 25 June 2009.

we do not have expertise in this area, believe that this may allow for different considerations to apply in relation to the interpretation of the legislation.

The ability to seek a stay or a hardship variation after proceedings have commenced in a State Court such as the Supreme Court

There appears to be no presumption that matters can be moved from a State Court to the relevant part of the Federal Court. The new Federal Court jurisdiction should be a jurisdiction of specialist expertise. Consumers should have access to the small claims procedure in appropriate cases, even those involving home loans that will be commenced in the State Supreme Courts. This procedure appears to only apply to the Magistrates court (Local Court in NSW) and the Federal Magistrates Court, meaning that hardship applications, and stay of enforcement applications, on home loans that are brought after the commencement of the proceedings may need to be pleaded as a cross-claim in the Superior Court.

This is in contrast to the current situation in NSW, where consumers can make an application in the Consumer Tenancy & Trader Tribunal for either a stay of enforcement, or a hardship variation, even after enforcement proceedings have been commenced in the Supreme Court. This right is vital for the law to be accessible as the superior court is only located in Sydney, expensive, and procedurally intimidating. Further any other arrangement would represent a diminution of rights for consumers and has the potential to contribute to unnecessary home repossessions.

It needs to be made clear that these applications can be brought in the Federal Magistrates Court after legal action has commenced in a State Court, or indeed that a stay can be pursued through the small claims procedure in a Local Court or Magistrate's Court near the debtor's residence. A stay order made in the Federal Magistrates Court, or other lower court, also needs to be recognised by the Supreme Court and procedures put in place to ensure that the Supreme Court is made aware of relevant orders.

The legislation should clarify the interaction between the State and Federal jurisdictions to ensure that the Federal jurisdiction is the forum of choice and to enable consumers to transfer matters where appropriate, and/or apply for a stay of proceedings in the Federal Magistrates Court, or other lower court exercising the small claims procedure, after enforcement proceedings have been commenced in a State jurisdiction, with appropriate procedures and protocols to ensure that this is workable in practice.

Other legislative changes required in relation to hardship

- Require lenders to consider the application for a hardship variation reasonably and in good faith - solutions must be tailored to the individual's circumstances
- Require lenders to give reasons for rejecting a hardship application as part of their response under section 72(3) of the NCP
- Offer a more flexible list of loan variation options including:
    - Reducing repayments under the contract and extending the term of the contract;

- Postponing repayments due under the contract, and extending the term of the contract if necessary;
- Capitalising arrears and extending the contract if necessary;
- Allowing reduced repayments for a period of time followed by increased repayments for a specified period of time to cover the resultant arrears;
- Interest only repayments for a specified period of time;
- Waiving fees;
- Temporary reductions in the applicable interest rate;
- Reducing repayments and capitalising the arrears during a specified period during which the borrower may attempt to sell the property.

- An automatic stay of all proceedings (including preventing the commencement of proceedings) should apply in all circumstances until 30 days after the borrower has received the lender's written response (unless a longer notice period is required by law).
- If the application is granted, all default and enforcement fees applicable from the date of the application should be waived and no further default or enforcement fees should apply while the variation is on foot.
- The Bill should clarify that access to a variation on the grounds of hardship can be obtained after default judgment. However, it should be clear that the relevant provisions could not be construed as requiring the lender to return secured property that has already been the subject of an enforceable third party sale contract. The hardship variation provisions should continue to apply to any shortfall after the sale of secured property.

Financial Hardship - Extract from CCLC Submission to Treasury

Hardship statistics

Research by Datamonitor shows that mortgage stress continues to affect more than 1.3 million households nationwide as of May 2009, despite the RBA's rapid reduction of interest rates by 4.25% since September last year[13]. More conservative figures from Fujitsu Consulting show that the number of households in mortgage stress have fallen from a peak of 900,000 in August 2008 to 568,000 in April 2009[14], but with another 460,000 on the edge of falling into mortgage stress, Fujitsu is also predicting that more than 1.2 million households will be in mortgage stress by December 2009 if unemployment rises to 7.5%[15].

[13] Mortgage stress affects one in four, AAP, May 10, 2009, http://www.news.com.au/business/money/story/0,28323,25456921-5013951,00.html
[14] Mortgage Stress-O-Meter Update, April 2009, Fujitsu Consulting, https://www-s.fujitsu.com/au/whitepapers/april_2009_mortgage_stress_report.html
[15] Low interest rates help ease mortgage stresses, Turi Condon, Property editor | April 01, 2009, http://www.theaustralian.news.com.au/business/story/0,28124,25272561-20501,00.html

The number of households facing foreclosure or sale increased 3% in the month to April 2009[16], and at least 101,000 households are still at risk of foreclosure or sale due to higher unemployment[17]. The RBA estimates that in December 2008 approximately 20,000 mortgage holders were in arrears for more than 90 days[18]. Defaults on non-conforming, low-doc loans that are over 30 days overdue hit a record high of 19.73% in March 2009[19]. In NSW alone, more than 300 writs a month have been issued by the Supreme Court since January – the same number of writs being issued when interest rates were still increasing in early 2008[20].

First home buyers, many of whom have been attracted to the housing market by the government's first home buyer grant boost are especially vulnerable, with Fujitsu Consulting predicting up to a third of the 125,000 first home buyers who purchased in the last year falling into mortgage stress if unemployment rises to 7.5% by December 2009[21].

Western Sydney suburbs are already facing the brunt of unemployment. The percentage of consumers in western Sydney who are late on their loan repayments by at least 90 days is triple the national average[22], as the unemployment rate around Liverpool and Fairfield rose to 10.5%[23]. Sheriffs in Bankstown were reporting an average of 15 houses being repossessed each week – triple the numbers from three years ago[24].

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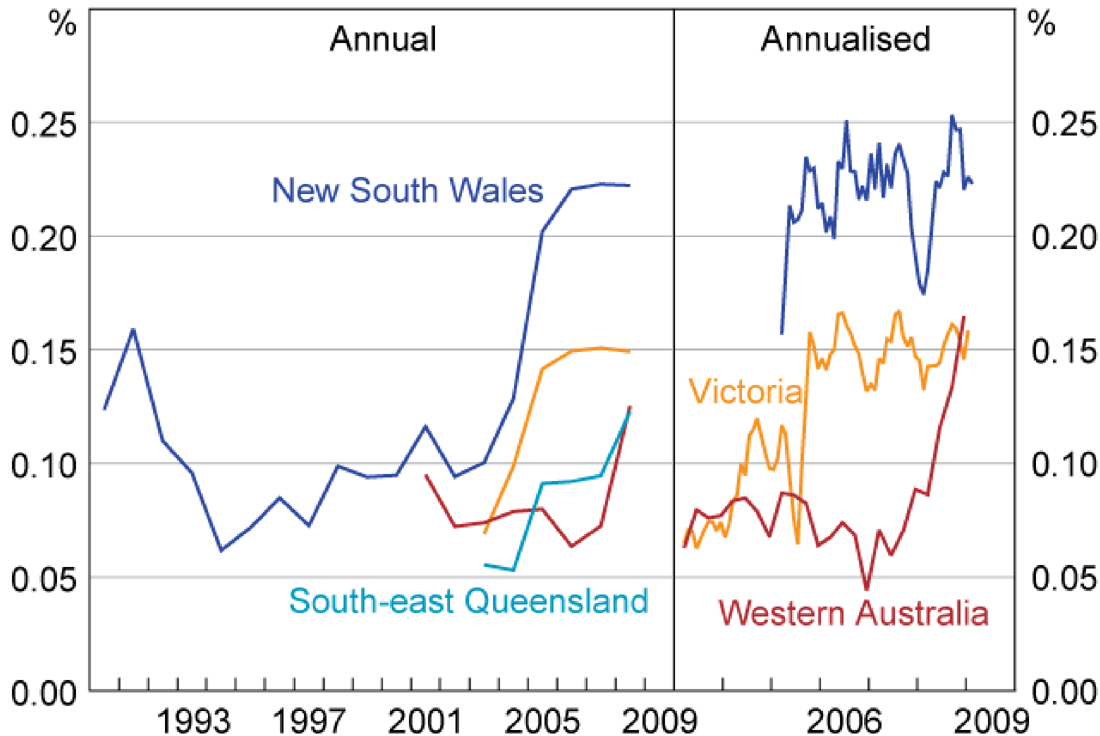
[16] Mortgage Stress-O-Meter Update, April 2009, Fujitsu Consulting, https://www-s.fujitsu.com/au/whitepapers/april_2009_mortgage_stress_report.html
[17] Mortgage Stress-O-Meter Update, April 2009, Fujitsu Consulting, https://www-s.fujitsu.com/au/whitepapers/april_2009_mortgage_stress_report.html
[18] Thousands living on borrowed time, Jacob Saulwick, April 29, 2009, http://business.smh.com.au/business/thousands-living-on-borrowed-time-20090428-am0w.html
[19] Mortgage delinquencies rise, March 31, 2009, http://www.theaustralian.news.com.au/business/story/0,28124,25268991-36418,00.html
[20] Thousands living on borrowed time, Jacob Saulwick, April 29, 2009, http://business.smh.com.au/business/thousands-living-on-borrowed-time-20090428-am0w.html
[21] Low interest rates help ease mortgage stresses, Turi Condon, Property editor | April 01, 2009, http://www.theaustralian.news.com.au/business/story/0,28124,25272561-20501,00.html
[22] *Mortgage suffering: the suburbs on the edge*, Jessica Irvine, Sydney Morning Herald, September 26, 2008
[23] New South Wales tops mortgage default list, Joe Hildebrand & Vikki Campion, The Daily Telegraph April 28, 2009, http://www.news.com.au/business/money/story/0,28323,25397470-5013951,00.html
[24] *When pain persists, they arrive,* by Jonathan Dart and Jessica Irvine, Sydney Morning Herald, March 28, 2008



RBA Financial Stability Review, March 2009

As demonstrated by the above graph from the Reserve Bank of Australia March 2009 Financial Stability Review, and the statistics above, NSW consumers are already facing record repossession levels. Disturbingly, CCLC's anecdotal experience based on advising borrowers suggests that the real impact of the downturn in the economy is yet to hit these statistics, with many borrowers currently in the late stages of the repossession process being in that position for reasons other than fairly recent unemployment, including for example:

- Arrears dating back to the period of high interest rates last year;
- High current interest rates charged by non-bank lenders who have not lowered their rates in line with the remainder of the industry as a result of funding problems;
- Enforcement of other debts (such as garnishees), neglected during the period of high interest rates, now impacting on their ability to repay the home loan;
- Perennial reasons such as family breakdown and illness;
- General over-indebtedness.

Calls to the Consumer Credit Legal Centre's Credit and Debt Hotline in relation to home loan repossessions rose by 38% in 2006, a further 36% in 2007 and another 104% in 2008. So far calls in 2009 are slightly lower than in 2008 but are still significantly closer to 2008 than 2007 levels. Further, after slightly less calls in January-April 2009 (more than likely as a result of lower interest rates and government stimulus measures), the number of calls in

May 2009 in relation to home loan repossession was very high even in comparison to 2008 averages.
The number of hardship complaints handled by the Credit Ombudsman Service has shot to 20% as a proportion of all complaints, compared to an average of 5%[25].

Despite the slight easing of defaults for mainstream loan in the first quarter of 2009[26], these figures are clearly set to worsen with the IMF predicting that unemployment in Australia will rise to 7.8% by 2010[27]. These financial difficulties are not restricted to mortgage holders, with 29 per cent of all consumers predicting difficulties paying their bills over the next 12 months[28].

Hardship Issues

Hardship is an area that lenders are not adequately addressing. We submit that the NCCP Bill should have tackled this issue more effectively. Whilst we applaud the increase of the hardship threshold to $500,000 and the introduction of s66(2A) into the Code, we are disappointed that further strengthening of the law relating to financial hardship has not eventuated.

ASIC has also identified hardship provisions as an area concern and recently released a report "*Helping home borrowers in financial hardship*" in May 2009[29]. This report identified several key deficits in the practices of the 15 lenders surveyed[30] in dealing with hardship variations, including:

1. introducing additional and sometimes arbitrary criteria for assessing financial hardship applications, such as the age of the loan or the number of days past due;
2. bias towards providing short-term assistance such as moratoriums, in preference to of looking at a repayment arrangement to suit the needs of the borrower;
3. reliance on collections officers to identify customers experiencing financial hardship;
4. providing information about financial hardship options only when borrowers have already defaulted;
5. failure to provide information to help consumers understand their options and make informed choices;
6. suggestions for consumers to apply for an early access to superannuation, where this would only result in a temporary delay to a foreclosure.

These findings accord with CCLC's casework experience, including short-term moratoriums that are contrary to the borrower's best interests, and the failure to consider a second hardship application when a poorly tailored solution has failed.

Why the Principles[31] released by the Treasurer are not enough – CCLC's experience

[25] Thousands living on borrowed time, Jacob Saulwick, April 29, 2009, http://business.smh.com.au/business/thousands-living-on-borrowed-time-20090428-am0w.html
[26] AAP, *Mortgage arrears decrease on low interest rate, 3, June 2009,* http://www.news.com.au/business/money/story/0.28323.25580601-5013951.00.html
[27] Swan admits jobless could top 10pc and refuses to rule out raising taxes, Christian Kerr | April 23, 2009, http://www.theaustralian.news.com.au/story/0,25197,25373834-601,00.html
[28] Mortgage stress affects one in four, AAP, May 10, 2009, http://www.news.com.au/business/money/story/0,28323,25456921-5013951,00.html
[29] Helping home borrowers in financial hardship, ASIC Report, May 2009, No 152
[30] 7 banks, 4 credit unions and friendly societies and 4 non-banks
[31] Media release 05/05/2009, No.034, Relieving Mortgage Stress, The Principles: A common approach or assisting borrowers facing financial hardship available at http://www.treasurer.gov.au/DisplayDocs.aspx?doc=pressreleases/2009

In our experience the Principles released by the Treasurer and to which the major banks have made a public commitment are not working. The following 5 cases are recent callers to CCLC who have been unable to access hardship despite the principles (each lender has been named to demonstrate that problems are not isolated to one or two institutions):

Case study 1

Mrs M rang St George Bank (now Westpac) on 2/6/09 to request financial hardship because she is now unemployed and accepts that she will remain so for the foreseeable future given her age. Mrs M needs time to sell her home. Her sole source of income is government benefits. Mrs M rang the bank and told them about her circumstances. The bank offered a 3-month hardship arrangement with payment of 50% of the scheduled repayments. Mrs M could not afford 50% repayments on Centrelink and, given a 6 week settlement period, 3 months was not long enough to sell her home. The bank told Mrs M that the bank would not offer any other arrangement.

Case study 2

Ms. P decided to buy a home and approached a local finance broker for assistance. Ms. P was given a line of credit loan by National Australia Bank. Unknown to Ms. P the home loan is an on-demand facility which can be called up for payment at any time. Ms. P went into financial hardship for 3 months in 2008 due to developing cancer. Ms. P has now returned to work. All arrears have been paid. The bank reviewed the loan and decided not to renew it and has issued a default notice requesting repayment of the whole loan. CCLC rang the bank to request that the loan not be called up and mentioned the Principles. NAB informed CCLC that the Principles do not apply to this type of home loan. NAB has just (May 2009) issued a notice to vacate to my client even when a complaint was lodged in the Financial Ombudsman Service some weeks ago. Ms P continues to pay the required repayments on her loan.

Case study 3

Ms. L rang CCLC when she was in the course of being evicted from her home by the sheriff. Ms. L had informed the Commonwealth Bank, her mortgage lender, that she was in financial hardship. Ms. L was just about to return to work when the eviction occurred. CCLC contacted the bank and asked for an urgent response as Ms L was homeless. The bank responded after two weeks. A letter was provided to the bank from Ms. L's employer confirming her absence from work due to illness and her start date for return to work. CCLC has convinced the bank to allow Ms L to return to her home and resume mortgage repayments. The bank has also agreed to set aside the judgment against her if she maintains her agreed repayments for a period of 3 months. While this is a good result, the bank maintains that they did not do anything wrong and that the Principles do not apply to her case. Further, we are convinced that without our intervention Ms L. would have lost her home permanently.

Case study 4

Ms X had a $96,000 mortgage with ANZ. She was involved in a car accident and developed post-traumatic stress disorder which caused her to forget about several mortgage repayments.

Ms X called ANZ to apply for a hardship variation and was mailed hardship forms. She had difficulties filling them out, and called ANZ for assistance. She was told over the phone that if she could not fill in the forms, not to bother with applying for hardship. At the time she applied for hardship, she was only $2000 behind in repayments and began making additional repayments to clear the arrears.

The bank has now issued a statement of claim against her. Despite the additional repayments, the amount in arrears had increased to around $4000 due to enforcement costs.

Case Study 5

A client contact CCLC in late May 2009. She is unemployed but not yet behind on her mortgage repayments in relation to her apartment. She contacted Westpac to request a 3 month moratorium while she looked for work and was informed that no such arrangement was available for her because her apartment had dropped in value and she had no equity.

In summary, while the banks will no doubt have many examples of the customers they have been able to extend hardship arrangements to, our experience of the brief period since the Principles were announced suggests that many borrowers are still being denied appropriate assistance. We do not believe that this is a fair and accountable way for the government to ensure access to hardship. It is also not an effective way of minimising the *snowball effect* of loan defaults in a financial crisis, by reducing unnecessary repossessions and bankruptcies (from negative equity sales and other unsecured debt), both of which tend to amplify the impact of an economic downturn.

The Principles are:

- not enforceable
- applied in an *ad hoc* fashion
- not applicable to the other lenders in the market
- not addressing key issues raised by ASIC such as the failure to tailor the solution to the customer's circumstances
- not subject to an adequate audit process

The principles are not enforceable

This means that if the bank fails to adhere to the principles, the consumer does not have any way to make the bank agree to the principles. While the consumer is permitted to complain to the Financial Ombudsman Service ("FOS"), the principles are so broad and arbitrary it is difficult to envisage what pressure FOS could bring to bear apart from persuasion to reconsider. There are also no consequences for failure to adhere to the principles, suggesting that the motivation for compliance may be less than adequate,

particularly in more challenging circumstances. Specifically, we are concerned that this approach will lead to an overly flexible approach to providing moratoriums to people with ample equity (to the borrower's ultimate detriment) at the same time as customer's with minimal or negative equity are not given sufficient flexibility, despite having perhaps a greater chance of getting back on track.

The Principles are being applied in an ad hoc manner

As demonstrated by the case studies above, banks appear to be finding a number of reasons to exclude the applicability of the principles. While the reasons for the apparent non-applicability of the principles are not always made clear, it would appear that the following factors may be at play:

- the amount of equity in the borrower's property;
- whether the borrower is unemployed, as opposed to in hardship for another reason (such as illness of family breakdown);
- whether the problem is recent (and therefore related to the global financial crisis) or more enduring (for example – borrowers are told they are not covered by the Principles because they fell into default before the date of the public announcement);
- the type of credit product (see Case Study 2); and
- whether the lender has already commenced legal proceedings, or obtained judgment.

These *ad hoc* and limited interpretations of when the principles apply completely undermine their effectiveness both as a fair and equitable process for borrowers in difficulty, and as a measure to minimize the impact of the global financial crisis. Two of these points are explored in more detail below.

Equity levels

The level of equity in a borrower's property, for example, while clearly relevant to a long term arrangement such as a 12 month moratorium on repayments, should not be a paramount consideration in determining whether they are eligible for a hardship variation *per se*. Neither the interests of the bank, the borrower, not the economy are served by taking a rigid approach to equity levels (such as in Case Study 5 above) if the borrower appears to have a reasonable chance of getting their repayments back on track. On the other hand, if the bank is offering a long term reduction in repayments to a borrower (usually because there is sufficient equity) the bank should be obliged to disclose to the borrower the impact of the arrangement on their indebtedness (for example the projected balance of the loan at the end of the agreement and the time to repay the debt if repayments remained the same, or the level of repayments required to pay off within the same period) and suggest the borrower gets independent advice.

Problems after the commencement of legal proceedings

CCLC currently receives a significant number of calls from borrowers who are already subject to legal action by their lender, including those who have had judgment entered against them for the amount of their mortgage plus enforcement costs and interest. Approximately 112 calls in 2009 to date have been from borrowers who have received a Statement of Claim, 67 of whom had already had judgment entered against them, and many of whom had been served with a Notice to Vacate. In some cases the lender had already entered into possession of the property or the Sheriff was in the process of taking possession at the time of the first call for advice or assistance.

Reliable percentages about the point in the process at which the debtor first sought assistance from CCLC are only available for the period 1 May to 15 June 2009. Analysis of this six-week period, however, reveals that 93 calls were made to the Hotline in relation to problems paying a home loan. 44% of these calls were received prior to the expiry of a default notice (29% prior to the issue of the default notice). 40% involved callers who had already been served with a Statement of Claim (signifying the first step in the legal process), including up to the point where the lender took possession of the property, 12% were in relation to post-sale issues and 3% were in relation to voluntary surrender of the property with or without enforcement proceedings. The Credit Ombudsman also noted at a recent event[32] that 90% of complaints about the lender's response to financial hardship are received after the borrower has received a default notice and 50% after a Statement of Claim has been served.

Our service is intervening more and more often at these late stages of the enforcement process, either because the borrowers have had a case for a hardship variation that the lender should have been aware of prior to issuing proceedings, or because the borrowers' financial position has improved to the point where they could repay the loan if given another chance. A significant barrier to these borrowers getting back on track is the addition of enforcement costs that begin to mount up quickly after legal proceedings commence.

We submit that if the principles are to have any real softening effect on the impact of the financial crisis, it must be made absolutely clear that they apply after legal proceedings have been issued, and even after judgment. Failure to do this will mean that:

- lenders can oust the applicability of the principles simply by taking legal action (and may take legal proceedings earlier than otherwise as a result) thereby defeating the purpose of the initiative
- borrowers who obtain employment, or otherwise improve their financial position after legal proceedings have commenced will often be denied the opportunity to remain in their homes (even though they can now pay their mortgage), placing an unnecessary further burden on the market for other forms of accommodation and social services, and downward pressure on property prices.
- Approximately 40% of callers to our service, for example, would find the Principles of no assistance whatsoever.

The Principles do not apply to other parts of the market

The Principles only apply to the major banks. Consumers with loans from other banks and non-bank lenders also need access to hardship. In the year 2009 to date (after removing as far as practicable repeat callers in relation to the same loan), only 27% of home repossession calls on average have been in relation to the major banks, despite their having the lion's share of the home loan market, although there has been an increase in these calls as the year has progressed (both in the number of calls per month and as a percentage of the total). Calls in relation to other banks make up 9% of total calls, 2 % concerned credit unions, and in 16% of calls the lender was not identified. By far the largest proportion of calls are about non-bank lenders at 45%, including but not limited to the so called "non-conforming" lenders and a number of lenders who have ceased to lend to new customers.

It has to be stated that even if non-bank lenders were interested in committing to the Principles, it is CCLC's experience that many non-bank lenders have such poor hardship policies and under-resourced hardship departments that any such commitment would be

[32] Reported by the Credit Ombudsman, Raj Venga, to the Financial Hardship Roundtable held at Melbourne Legal Aid on 15th May 2009.

illusory. Many of these lenders appear to take the approach of ignoring apparent financial difficulties on the part of their customers until a specific request is made in the language of the UCCC provisions. At that point forms are sent to the customer for completion detailing their financial position, but rarely resulting in a variation being given. Often it takes the intervention of the Court (or EDR scheme if they are a member) for the lender to agree to any form of variation. Lenders who have ceased to offer new loans have the added complication of not being able to extend the term of the loan, limiting the options available in the cases of hardship.

It should also be noted that many non-bank lenders are totally reliant on the international market for their funding and, as a result, have not lowered their interest rates in line with the Reserve Bank of Australia and the banks[33]. Many callers to CCLC have interest rates of 9-11% on their home loan with such lenders, with default rates of 15% or higher, while other lenders are offering rates of 5-6%. Not surprisingly, many of these borrowers are in default and incurring the higher rate of interest. The same loans often carry significant break fees and/or deferred establishment fees, making it expensive to refinance. Further, borrowers who are already in hardship as a result of unemployment or reduced employment, do not usually qualify to refinance to a loan with a cheaper rate. These consumers are also often in positions of insecure employment. These borrowers were encouraged to enter the market as part of the great *democratisation* of credit and home ownership. They have now been left high and dry.

The Principles do not address key issues raised by ASIC such as addressing the solution to the customer's circumstances

As indicated both in the press release and in the ASIC research, one of the main tools in assisting consumers with financial hardship is to offer a moratorium on payments. This is also consistent with reports CCLC receives from consumers experiencing financial hardship.

Offering a moratorium is a poor approach to financial hardship for a home loan. The home mortgage is often a large loan on which interest accrues and compounds very rapidly in the absence of repayments. It also represents a priority payment as it is for the home. If at all possible the consumer should be at least making part repayments on the home loan while arranging moratoriums on credit cards, for example. The major banks are failing to take this into account. Where a client has a medium term problem and they are given a 3 month moratorium, they are in a worse position in 3 months time when they are unable to resume normal repayments, particularly if they could have been making reduced repayments in the interim period. Further the bank is less sympathetic because the borrower has already been "given a chance". CCLC is finding that consumers are being given moratoriums with little or no regard to whether this makes any sense given the consumer's financial position.

Similarly, many callers to the Credit and Debt Hotline concede that the long term repayment of their loan has ceased to be a realistic possibility and are simply seeking time to sell their home. Lenders should be prepared to offer these borrowers a hardship variation in the form of significantly reduced repayments and a reasonable period in which to try to sell their home.

There is no audit process

The efficacy of the principles are very difficult to measure.

[33] Lenders who have ceased to lend and are simply winding down their loan book also have no incentive to lower interest rates as they are not trying to retain or attract business.

There is no audit process in place to ensure that the Principles are in fact delivering a discernible and real outcome for consumers and the economy.

It is possible that the principles are failing to deliver an outcome for consumers and the Government would be unaware of this. In fact, CCLC has real concerns about the efficacy of bank hardship assistance based on our experience with talking to callers to CCLC.

Appendix A

Extract from CCLC submission to Treasury

Avoidance practices over the years

The UCCC has a long history of being avoided. There have been a series of amending acts required to address these loopholes. This seems a very inefficient way of keeping up with a very creative industry. No sooner has one hole been closed and another appears.

- The use of short-term contracts (rolled over repeatedly);
- Interest expressed as fees to avoid interest rate caps and obfuscate the cost of credit;
- Split entities charging brokerage to inflate cost, avoid caps and the minimum credit charge to be caught by the UCCC;
- "Cheque cashing fees" and other means of avoiding minimum credit charge to be caught by the UCCC;
- False business or investment purposes declarations to facilitate predatory and exploitative asset-based lending;
- Promissory Notes;
- Bills of Exchange;
- Vendor terms contracts;
- "interest-free" lending , where the price of the goods is inflated to conceal the cost of credit;
- Goods rental contracts with "nudge, nudge, wink, wink" arrangements that the consumer can keep the goods which are not reflected in the written agreement;
- Exploitation of the pawn broking exemption; and
- Using "on demand", line of credit, home loan contracts to claim that default notice (s80) and hardship variation provisions (s66-68) do not apply.

More detail and examples are included below[34]. Many of these case studies date back some years because the particular loophole has been closed. Where the case is recent this is stated.

[34] These case studies were complied by CCLC for inclusion in a joint consumer organisation letter to the Commonwealth Government about the then proposed amendments to the UCCC in relation to fringe lending. The case studies are drawn from the casework experience of not only CCLC, but also Consumer Action Law Centre, Queensland Legal Aid and Wesley Community Legal Centre.

Short-term contracts (rolled over repeatedly)

Prior to amendment of the UCCC in 2001 to introduce a maximum charge for short-term loans in order for them to fall outside the Code, the "less than 62 days exemption" was used by short-term ("payday") lenders to avoid the Code entirely. Despite some suggestion that the law might deem rollover contracts to be covered by the Code under various other provisions, this was not tested and rollovers were common. The Wesley Community Legal Centre had a case in the CTTT only a few years ago where the loan was rolled over 11 times.

Interest expressed as fees to avoid interest rate caps and obfuscate the cost of credit

This has been addressed in NSW by a comprehensive cap on the cost of credit. Consideration of this issue has been delayed until Phase 2 of the Commonwealth government process. Unless these provisions of this nature, or another equally effective solution is introduced by the Commonwealth government, loans of the following type will once again proliferate.

How much?

Ms A needed to borrow $2,500 urgently and responded to an advertisement in the local paper that said "Easy Loans No Credit Checks". Ms A told the lender she was in receipt of Centrelink benefits as her only source of income. The loan she was given was $3,550, and included a flat fee of $1,050. A caveat was also taken over her home and lodged the next day. The loan was for 1 month and a default rate of interest of 10% per month applied if she did not pay the entire amount back within that time. Ms A was unable to pay on time and was threatened with bankruptcy shortly afterwards.

Split entities charging brokerage to inflate cost and avoid cap

Some lender have introduced a "brokerage charge", usually payable to a related entity which the borrower has nothing to do with and probably doesn't even know exists. This enables the lender to both avoid the comprehensive interest rate cap in NSW but also, in some cases to avoid the Code altogether for very short term loans. There were provisions aimed at addressing this issue in the Credit Code Amendment Bill 2007.

Brokers introduce borrowers to lenders – don't they? (recent)

Mr A needed a $500 loan to pay for basic necessities such as food and clothing. His sole source of income is the disability support pension, he is illiterate and has a heart condition. Mr A approached a small amount lender for a loan. The lender was aware at all times that Mr A was illiterate, but did not explain any of the terms and conditions of the loan. Mr A believed he was obtaining a $500 loan. Instead, he was put into a loan for $700 loan for 32 weeks at an interest rate of 48% per annum. $500 of the proceeds went to Mr A, however, unknown to him, a further $200 of the proceeds was paid to a brokerage company which Mr A did not deal with taking the actual cost of the loan well above the disclosed interest rate. The broker appears to have played no role in the transaction apart from enabling the overall cost of the loan to exceed the 48% cap on interest, fees and charges applicable in NSW. The lender also incorporated a bill of sale into the loan contract, so that it can take possession over Mr A's fridge and living room furniture in the event of default.

Mr A has fallen behind on his repayments. He is extremely concerned that the lender will repossess his household items, and that the stress may have a negative impact on his heart condition.

"Cheque cashing fees" and other means of avoiding minimum credit charge to be caught by the UCCC

This scheme applies the same principle as the brokerage fee above. The charge for credit under the contract may be less than the cap or the amount required under 7 to be caught by the Code, but the borrower is charged a separate "cheque cashing fee" if they want cash immediately. Of course, it is in the nature of this type of lending that all borrowers need the cash immediately. There were provisions aimed at addressing this issue in the Credit Code Amendment Bill 2007.

Whoops! The loans costs this much but if you actually want your money...........
Ms B has an intellectual disability and mental health problems. Her sole source of income was Centrelink disability benefits. Ms B borrowed $200 from a lender for a period of 7 days. The total credit fees and charges were about $80 and a significant proportion of these fees were made up of a "cheque cashing fee", and a membership fee, which were purportedly not credit charges for the purposes of the Consumer Credit Code. The lender did not explain any of the charges or the terms of the contract. Ms B did not understand that she had to repay the entire loan and charges in just 7 days.

False business or investment purposes declarations to facilitate predatory and exploitative asset-based lending

This is the most common way of avoiding the law in mortgage lending and facilitates the worst examples of predatory lending or equity stripping. Finance broker legislation in both NSW and Victoria is also dependent on attracting the jurisdiction of the Code and is therefore also avoided in the same manner.

The illusory mortgage stress solution (in CTTT 2008)

In Early 2006 Mr K lost his job in a flour mill. He was given a redundancy package and, as a result, he was excluded from Centrelink for a period of time. Mrs K was reliant on a partial Disability Support Pension. They had a mortgage with a bank over their home. Mr K found seasonal casual employment but this was disrupted during the floods and bushfires in NSW and Vic in late 2006. They fell behind in their mortgage to the bank and a default notice was issued. Mr K and Mrs K saw an advertisement on regional television offering "Bad Credit Mortgages". They were offered short term finance of $15,000, which included $10,000 to rectify their mortgage arrears and pay their water and land rates, $3,000 brokerage, $1,500 "prepaid" interest and $500 additional set up costs. They were told to sign a business purpose declaration and were assured this was just a "formality". A caveat was placed over the home.

The short-term credit was on the following terms **10% per month** interest, and **15% per month** in the event of default, the monthly repayments were approximately $1,500. They were told that this loan was only a stopgap measure and that a refinance of their entire home loan on better terms would be arranged. The refinance never eventuated and Mr and Mrs K were unable to meet the payments on the short-term finance or on their mortgage to the bank. Further, Consumer Credit Legal Centre has several clients who have used the

same broker and lender and the modus operandi is always the same – there is always a business purpose declaration and the promised refinance never occurs.

Narrow escape (recent)

Mr C is 70 years old. He has prostate cancer. He owns his home outright. He had a $30,000 credit card debt. He was using the whole of his pension to pay the minimum monthly repayments. His wife also pawned her jewellery to pay the credit card. He decided that he would obtain a mortgage secured over his property to pay out the credit card debt and to reduce the payments. He wanted additional credit so he could travel (probably for the last time) and take his three children to meet his wife's parents. He saw an advertisement on local television for "bad credit mortgages". Because of his large credit card bill he had fallen behind in his telephone and other debts. The broker said he could arrange a loan to consolidate his debts in a mortgage for $95,000. The broker said they could arrange a loan immediately for $50,000 if they sent the deed to the house.

Mr C sent the deeds and received a bundle of documents including a letter of offer to provide finance of $62,573. $50,000 to be paid to Mr C, the terms included **8% per month** interest, **10% per month** in the event of default. The loan included "prepaid" interest of $4,620 and **brokerage fee of $7,000**. The interest only repayments were $5,005 per month, well in excess of Mr C's income, and Mr C was told he had to sign a business purpose declaration. Mrs C was a registered nurse and during the course of her telephone conversations with the lender she was told that she had to state that loan funds were for the purpose of her being a sole trading registered nurse. Mrs C stated she had no intention of starting a business.

Signing a business purpose declaration not only takes the loan outside the jurisdiction of the Consumer Credit Code, but also relieves the broker of any obligations under applicable legislation in NSW and Victoria. Fortunately, Mr C went to see his solicitor, who told him not to go ahead. Mr C's solicitor got the deeds returned, and a mortgage was found for Mr and Mrs C that suited for their purposes.

Small loan, large cost

CCLC was approached by Ms. A, who had received a Statement of Claim (Equity Division of the Supreme Court) filed by a small fringe lender seeking possession of her home. Ms A was from a non-English speaking background and suffered from clinical depression at the time of seeking assistance. She had taken out a small loan of $5,000 to pay strata fees on her home unit. In fact the amount borrowed was for about $3,500 with the remaining $1,500 representing fees and charges added at settlement. The interest rate was 5% per month. The lender had taken a second unregistered mortgage over her home unit. The loan was described as being for business purposes even though it was for personal purposes. A first mortgage was held by a major bank. That loan was not in default. Ms A could not pay in accordance with the terms of the loan and the lender's first claim in order to stop the Supreme Court proceedings was for an amount in excess of $20,000.

CCLC filed a defence and a notice of appearance claiming that the loan was covered by the Consumer Credit Code. The matter was eventually settled to our client's satisfaction.

Promissory Notes

This commonly used loophole was closed by amending legislation in late 2007.

Home at risk (2007)

Borrower 3 is a male who suffers from schizophrenia. He borrowed $1000 under a promissory note secured by a bill of sale over his home unit. The amount repayable over 12 months is $2,476, an effective interest rate of almost 150%. The contract also disclosed a number of possible penalty charges including $48 for a dishonoured direct debit ($35-50 may also be payable to the borrower's bank for this dishonour), $20 for the reschedule of a payment, and a penalty service charge of 48% per annum payable on the remaining balance for any period during which the borrower is one or more repayments in arrears. Clearly Borrower 3's home unit is at serious risk for a $1,000 loan.

Hey big spender! (2007)

Borrower 68 year old woman on the Disability Support Pension. She has three loans from two different lenders, all taken out in late 2006 in order to simply survive. All three loans disclosed the purpose of the loan was to purchase white goods. Two of the three loans avoid the UCCC by using a Promissory Note and a Bill of Exchange arrangement. Two of the loans were secured over basic household necessities. The interest rates were approximately 163%, 224% and 44% respectively. The cheapest loan was UCCC compliant. The others were not. The client could not pay any of the loans as they fell due and the interest and charges began to accumulate.

Bills of Exchange

This commonly used loophole was closed by amending legislation in late 2007.

Set up to fail (2007)

Borrower 1 is 45 years of age. She has been on the Disability Support Pension for 3 years. She suffers from serious depression.

Borrower 1 pays rent of $180 per week, which is 69% of her pension payment. She fell into arrears with the repayment of her rent and was threatened with eviction if her rental arrears were not brought up to date.

Desperate to keep a roof over her head, she successfully applied to a specialist small amount lender for a $2000 loan. The loan was not regulated by the UCCC because it was extended under a bill of exchange. The amount payable 32 weeks after the date of the contract was $2,753. The majority of the borrower's necessary household items, including a fridge, microwave, lounge, dining table, washing machine, cloth dryer and a television, were mortgaged to secure the contract.

The contract does not disclose the amount of weekly or fortnightly repayments. If she was to repay the loan fortnightly, she would have to pay $172.06 per fortnight. Borrower 1's fortnightly pension is $525. She would have a shortfall of approximately seven dollars per fortnight just paying her rent and this loan. She would have no money at all with which to pay food, electricity, phone, transport or medication for example.

Not surprisingly, Borrower 1 has not been making any weekly or fortnightly payments and will not be able to repay the $2,753 on the termination date.

"Interest-free" lending, where the price of the goods is inflated to conceal the cost of credit

Amending legislation to address this loophole passed the Queensland parliament in the latter half of 2008.

Costly purchase (recent)

Ms D attended a car dealership in Western Sydney to purchase a car. She traded in a Gemini for approximately $1000 and entered into a contract to purchase a 1995 Commodore Holden Sedan with 270,000 km on the odometer for $14,385. The trade in of the Gemini was not taken off the price of the car. The repayments were 65 repayments of $220 per fortnight. She was also forced to take out an Extended Warranty

Ms D tried to get the car insured, but was informed the car was valued at only $4,500 – $5, 000.

Ms D changed the tyres and put in a new stereo. The car had a number of mechanical problems; she tried to use the Extended Warranty and was told that the problems were not covered. The cost of the repairs was $2000.

Ms D was no longer able keep up with the repayments and make repairs to the car. The car was repossessed. Ms D was happy to see the back of the car but the day after the repossession she attended the car dealership and demanded the return of the additional features she had installed at her own expense. This request was refused. The police were called. Mrs D attended the Local Court and got a Notice of Demand, returned to the dealership with the police and retrieved her goods.

Exploiting disadvantage (recent)

Mr J suffers from depression and schizophrenia and his sole source of income is a Disability Support Pension. He has a wife and three children. He has limited English language skills. In December 2006 he attended a car dealership and entered into an agreement to purchase a car for $14,985. The car was a 1990 Mitsubishi Wagon and had 276,638 kilometres on the clock. Mr J also traded in another vehicle but this is not noted on the contract or accounted for in any way apparent from the paperwork. The repayments were $220 per fortnight for 68 months. Subsequent valuations have indicated the car is worth only $3,000.

Exploitation of the pawn broking exemption

Amending legislation to address part of this problem was included in the Credit Code Amendment Bill 2007. Specifically that legislation proposed to limit the pawn broking exemption to contracts where the only recourse of the lender is to retain and sell the goods pawned. This would effectively prevent the sham transactions referred to in the press article below where articles worth less than a couple of dollars are "pawned" to avoid the UCCC. These amendments would not address the issue demonstrated in the case study below, whereby the arrangement involves an item worth considerably more than the amount of the loan.

Queensland loan laws fail most vulnerable

August 18, 2008 12:00am
http://www.news.com.au/couriermail/story/0,23739,24195915-13360,00.html

"Laws recently announced by Attorney-General Kerry Shine and effective from July 31 were designed to close down the cruellest of loan sharks known to charge up to 1600 per cent interest on short-term "payday" loans. The new laws emerged after years of complaints from victims of an unsavoury industry, yet the legislation still appears soft. With money lenders free to charge a still exorbitant 48 per cent interest rate, we wonder if this is lending or usury.

The Courier-Mail has exposed how some Queensland lenders apparently feel even this rate is unprofitable, with a few of the more familiar lending firms skirting the new law by offering loans as pawnbroker transactions. Companies such as Cash Converters and Fast Access Finance, for example, exploit legal loopholes – and their most vulnerable customers – by lending cash through the "sale" of diamonds or accepting CDs as collateral."

Pawning the car (2008)

In May 20007, Ms M borrowed $2,000 from a pawnbroker to cover rent arrears. She was unemployed. As security for the debt, the pawnbroker took a bill of sale over Ms M's car. The car was valued at $13,500. Repayments on the loan were $500 per month, representing an annualised interest rate of 300%. The provisions of the contract and their legal and practical effect were not explained to Ms M and there was no UCCC compliant disclosure. The repayments represented approximately 60% of Ms M's income.

Ms M repaid $3,000 between May and November 2007. In December however she contacted the pawnbroker requesting a deferment of that month's payment. The pawnbroker did not respond. Without notice, the pawnbroker took possession of Ms M's car. There was no court order and the car was on private property. The pawnbroker demanded the sum of $3,950. Despite requests, at no time has the pawnbroker provided any information as to how this amount was calculated.

The pawnbroker appears to be relying on the pawn broking exemption to the Consumer Credit Code, but the loan has few of the features of a typical pawn broking arrangement (where the goods are handed into the possession of the pawn broker and the loan is less or close to the value of the goods), and all the features of an unjust personal loan.