7th October 2022

Senator Jess Walsh
Chair Senate Economics Legislation Committee
Parliament House
Canberra ACT 2600
By email: economics.sen@aph.gov.au

Dear Senator Walsh

The National Credit Providers Association (NCPA) is pleased to make a submission on the Financial Sector Reform Bill 2022.

For further information or if you have any questions, please don't hesitate to contact me on [redacted] or email me at [redacted]

Yours sincerely

Michael Rudd
Chairman

On 28 September 2022, the Senate referred the provisions of the Financial Accountability Regime Bill 2022, Financial Sector Reform Bill 2022, Financial Services Compensation Scheme of Last Resort Levy Bill 2022 and Financial Services Compensation Scheme of Last Resort Levy (Collection) Bill 2022, to the Economics Legislation Committee for inquiry and report by 20 October 2022**.** The National Credit Providers Association (NCPA) is pleased to make a submission to the Committee, focusing on the proposed reforms in the *Financial Sector Reform Bill 2022*[1].

About the National Credit Providers Association (NCPA)

The NCPA is the peak national body representing the Small Amount Consumer Lending Industry in Australia. NCPA represents companies that provide Small and Medium Amount Credit Contracts and are all holders of an Australian Credit License, who operate from retail and online platforms in Australia.

NCPA takes very seriously its role of driving self-regulation of the industry, by assisting and guiding lenders in the provision of fair and safe credit under the National Consumer Credit Protection Act 2009. Most importantly, NCPA strives to promote and protect the rights of customers by ensuring lenders are applying responsible lending practices.

About the Sector

The NCPA welcomes the opportunity to provide up-to-date information to the Committee on the consumer credit sector, in particular information on small amount credit contracts or SACCs. A small amount credit contract is defined as a credit contract that is not a continuing credit contract, where the credit limit is $2,000 or less and is repayable between 16 days and 12 months.

It is important to note, the proposed reforms in Part 1, Schedule 4 – Consumer Credit Reforms of the Financial Sector Reform Bill 2022 apply only to small amount credit contracts and consumer leases.

However, there is a range of small loan and credit products currently available in Australia (see table 1). These include continuing credit contract products such as those provided by Wallet Wizard (Credit Corp ASX: CCP) with annual interest rate charges of up to 47.8%. A credit card is also a continuing credit contract, which typically incurs interest rate fees of between 12 and 24%, depending on the lending institution. There is also a consumer credit product provided by Cigno, that is also a continuing credit contract but uses arrangements between Cigno and another party that includes high charges and fees to the consumer. This arrangement is the subject of appeal in the Courts, however, the product is still available to consumers, regardless of the efforts of the regulator ASIC, to ban the product.

[1] https://parlinfo.aph.gov.au/parlInfo/download/legislation/bills/r6909_first-reps/toc_pdf/22087b01.pdf;fileType=application%2Fpdf

Table 1

	Loan amount	Interest rate	Repayment period	Contract term	Establishment fee	Account keeping fee	Default fees and charges
A SACC loan	Up to $2,000		Monthly	The loan period minimum 16 days and up to 12 months	No more than 20% of loan amount	No more than 4% of loan amount monthly	
Cigno product	Up to $1,000 continuing credit contract	Fees charged based on payments made towards loan	5% immediate repayment upon receipt of funds	Up to 56 days (8 weeks)	Base amount of $13 plus 60% of loan amount	$23.80 a month	Dishonor fee $67 Additional default fee $20 Payment re-schedule fee $30
Wallet Wizard product	Up to $8,000 continuing credit contract	47.8% per annum	Options for weekly, fortnightly, and monthly repayments	Between 6 and 12 months for loans between $1201 and $2000 Between 4 and 9 months for lower amounts	20% establishment fee	2% of loan amount monthly	Direct debit reversal fee of $10
ANZ Low-Rate Credit Card	Minimum credit limit of $1,000	12.49% purchase rate per annum 0% balance transfer for 30 months, then 21.24%	Monthly, minimum repayment of 2% of closing balance or $25, whichever is greater	Ongoing	1% balance transfer fee	Annual fee of $58 ($0 for first year)	$20 late payment fee
NAB Low-Rate Credit Card	Minimum credit limit of $1,000	12.99% purchase rate per annum 0% balance transfer rate for 32 months, then 21.74%	Monthly minimum repayment of 2% of closing balance or $25, whichever is greater	Ongoing	-	Annual fee of $59 ($0 for the first year)	$15 late payment fee

The NCPA fully supports the actions taken by ASIC to remove from the market any consumer credit product that causes consumer harms, including the continuing credit contract product provided by Cigno. Most of these products, with the exception of a credit card, are all commonly referred to as payday loans. As the table above identifies, the range of consumer credit products available have varying rates of interest and fees attached. However, the proposed reforms in Part 1 of the Financial Sector Reform Bill 2022 focuses on small amount credit contracts but will do little to address the harm caused by some continuing credit contracts, such as the Cigno product.

The latest data[2] available (8,095 complaints) from the Australian Financial Complaints Authority (AFCA) records the number of complaints in the banking and finance sector for the period 1st July 2021 to 31 December 2021. You will note the banking and finance firms listed provide continuing credit contracts, including all the major banks and Credit Corp Services Pty Ltd (Wallet Wizard).

The providers of small amount credit contracts listed include Jacaranda Finance, Cash Converters, Ferratum and Cash Stop, who combined have a total of just 34 complaints during the 6-month period, out of a total of 8,095 complaints. And in 2019-20 SACCs made up less than 0.7% of the total complaints being 80,546. This is a trend in the data from AFCA that highlights the adherence to the already very stringent SACC laws together with very strongly customer focused licensed business in the SACC sector rather than an anomaly. This is an important point.

Further, it is a gross overreach to mandate a protected earnings amount that applies equally to all consumers, regardless of either their level of or where they derive their income from. Different consumers have differing financial requirements. For example, a consumer not in employment who has a net income of $20,000 per annum derived via Government Benefits when compared to a consumer employed full time with an income of $85,000 under this Bill are both subjected to the same protected earnings restrictions.

What is the problem the government is trying to fix, given the very low level of complaints received by AFCA? The proposed reforms are based in part on an omnibus style telephone survey conducted in 2015. The sector is now vastly different than it was almost 8 years ago. The proliferation of buy now pay later products has changed the sector significantly. You only have to look at the loan approval rates for small amount credit contracts which continue to fall (from 68% in 2017 to just 31% in 2021-22), largely due to the applicants gorging on the unregulated credit which is seen in the massive expansion and growth in the availability of buy now pay later products and the very accessible credit available from Cigno, having the effect of excluding many applicants from qualifying for a loan. The latest CoreData Industry Data Report is available upon request.

The NCPA has major concerns for the approximately 3 million financially excluded Australians who cannot obtain credit from a bank or mainstream financial institution but still need access to credit as much as anyone.

[2] https://data.afca.org.au/banking-and-finance

According to Good Shepherd Microfinance, *seventeen per cent of adults in Australia experience financial exclusion. That's 3 million people unable to access a small amount of credit, a transaction account or general insurance. This places them and their families at risk of poverty and poor social, emotional and health outcomes.*

The Bill

Protected Earnings Amount - *Schedule 4, Part 1, Subsection 133CC(1)*

The NCPA supports the vast majority of the proposed reforms in the Bill but does not support any change to the protected earnings amount in Schedule 4, Part 1, Subsection 133CC(1). The Government's Bill proposes to apply the protected earnings amount on a small amount credit contract to all consumers and lower the amount of their income that can be applied to loan repayments to 10% of a consumer's net income.

This is a significant shift in policy from the current regulations and deserves scrutiny. The National Consumer Credit Protection Act 2009 (NCCP Act) that regulates the small loans sector already includes a protected earnings amount, set at 20% for consumers in receipt of a government benefit, with no protected earnings amount in place for working Australians. These changes were introduced in the Enhancement Bill in 2013.

This is and continues to be fair and appropriate regulation and is working as intended for the approximately 3 million financially excluded Australians who need access to credit. To lower the protected earnings amount to 10% for all consumers, regardless of their employment status, is a very authoritarian form of income management for all Australians and is a significant over-reach which will have the effect of further excluding this cohort of Australians using the SACC product.

Experiences in other jurisdictions have resulted in negative outcomes for consumers. For example, the State of Colorado, in the United States in 2010 enacted a near identical PEA, with a review of the data in 2014 concluding that "Limiting the payment-to-income ratio would benefit fewer than 1% of borrowers by reducing the incidence of loans that are not paid off, but it would impose costs on 86% of current borrowers, who could not be offered the same credit on the same terms that they now obtain"[3]. The review concluded, "regulation that prohibits lending based on simple affordability criteria risks substantial reductions in credit availability to a population that often has few available alternatives".

Importantly, this change to regulation will also increase the cost of credit for consumers and extend the period of a loan. For example; a small loan of $500 over a 6 month period currently costs the consumer $720 fully repaid, including the principal. This is the original loan of $500, a 20% establishment fee ($100) plus a 4% monthly credit fee ($20 x 6 months) – total loan costs incurred over the term of loan is $220. This is under the current regulations.

[3] Beales, Howard & Goel, Anand. (2015). Small-Dollar Instalment Loans: An Empirical Analysis. SSRN Electronic Journal.

Under the government's new Bill, the protected earnings amount will be lowered to 10% of a consumer's net income. The same $500 loan now costs $340 (55% more expensive) and will take 12 months to repay, and now costs the consumer $840 fully repaid, including the principal. How is this helping already financially excluded Australians?

It's a form of income management for all Australians, which is the opposite to the government's recent stance taken on the abolition of the cashless debit card. This reform is being driven by consumer activists who are intent on pushing their views onto others.

Recommendation: The NCPA proposes the current protected earnings regime be retained as it is working as intended. Subsection 133CC(1) of the Schedule 4, Part 1 of the Financial Sector Reform Bill 2022 be removed.

Unsolicited Communications - *Schedule 4, Part 1, Subsection 133CF – Licensee not to make certain unsolicited communications in relation to a small amount credit contract*

The NCPA also has serious concerns about the proposed amendment to *133CF, prohibition on certain unsolicited communications.* The NCPA agrees that unsolicited communications for pre-approved products should not occur and will support reforms of that nature, but the NCPA does not support 133CF in its current form as it is unworkable and is effectively a prohibition on contacting your customers.

The NCPA is of the view that credit providers need to be able to communicate with their customers (essentially their database asset). Further and in regard to Subsection 133CF, we note that it may be that the value of the databases of all credit providers is substantially reduced due to this proposed amendment.

The current wording of the proposed amendments are not realistic and are unworkable and will be an administrative nightmare for lenders to have to determine whether a consumer has applied for or been previously given a SACC from other lenders. The NCPA is happy to work with the government to ensure:

- Providers must be able to communicate with their own customers
- Providers should not provide or assert to any pre-approvals
- Providers shouldn't be able to contact consumers not on their database, i.e. buying databases and marketing to them

Recommendation: The NCPA proposes some rewording for Subsection 133CF of the Schedule 4, Part 1 of the Financial Sector Reform Bill 2022, so as to not prevent providers from contacting their customers, and to remove unrealistic administrative burdens on providers.

Enforcement

SACC lenders who breach the disclosure provisions of the Credit Act are subject to the same Civil Penalty provisions as any other credit provider. This is fair. Likewise, any SACC lender who charges more than the amounts prescribed in sections 21A, 31B and 39B of the Credit Code must refund those charges back to consumers.

Breaches of the proposed Protected Earnings regime in section 133CC(1) of the NCCP can also be the subject of a criminal charge leading to a recorded conviction and fine. However, the current law provides for a fine of up to 2,000 Penalty Units and the Bill proposes increasing this to 5,000 Penalty Units.

NCPA does not dispute that compliance is important and should be the subject of enforceable sanctions. In the case of large corporations, the relevant individuals may receive no personal benefit from the mistakes they made in attempting to comply with the new regime. They were just doing their job. The extent that they were deficient in that task should be a matter of regulatory and commercial nature. It should not be a crime.

As the Australian Law Reform Commission has said:

In a regulatory context, criminal sanctions serve as a ***last-resort*** (emphasis added) *punishment after repeated or wilful violations.*[4]

The relevant sanctions should reflect the nature of the provisions to which they apply.

Recommendation: The NCPA proposes the government remove reference to criminal penalties in the Bill.

The Australian Research Council report on the small loans sector noted the following in their report in 2012: *Dr Marcus Banks, a Researcher from the School of Economics, Finance and Marketing at RMIT, published a report on the small loans sector entitled: Caught Short, an Australian Research Council funded report. This research was conducted prior to regulations that abolished payday loans in 2013. However, the key findings demonstrate the need that exists for a product aimed at those consumers who are not eligible to receive credit from banks – a gap that has been filled since 2013 by responsible lenders offering Small Amount Credit Contracts. In March 2015, Dr Marcus Banks also published an article in the Overland Journal referencing his report and ongoing media interest in small loans.*

He said: "The report's finding that most people get caught up in an expensive cycle of repeat borrowing has led to calls by the media and consumer advocates to further regulate the sector and even close it down. A financial counsellor interviewed for the study summed up what is wrong with this argument: 'It's very easy for a bunch of middle-class advocates, financial counsellors, whatever, to say this shouldn't be happening – but walk a mile in the shoes of the people who have no other access. I think our entire premise should sit around that Centrelink payments are inadequate for people to live with dignity in this community.'

"There is a knee jerk reaction by media and consumer advocates to frame small loans simply as a market problem that can be addressed by greater regulation and smaller fees. The short answer is no, it won't. It is expensive to be poor, and the higher risks associated with lending to those on a low income means that any tighter regulation will abolish this now- established

[4] Australian Law Reform Commission, *Principled Regulation: Federal Civil & Administrative Penalties in Australia*, ALRC 95 (2002), [2.40]–[2.44].

market and send it underground. "Secondly, ignoring the wider societal issues that drive casual and low-waged workers to online lenders and welfare recipients to street front lenders leaves the status quo unchallenged. "People borrowing these loans are portrayed in the media as passive, easy prey and financially illiterate. However, as the Caught Short report and other studies suggest, a person taking out a small loan is often making a highly rational choice to manage their credit and debt in small amounts over short periods of time rather than putting themselves at greater risk of being overwhelmed by a ballooning credit card debt.

"Narrowly moralising against one financial symptom of current society lets the Australian government off the hook, airbrushes away the real financial struggles of low-income earners and offers no viable strategy to resolve their financial problems.

Summary

The NCPA supports sensible reform that is supported by evidence and where there is a real need for greater consumer protections. This is why we support much of the Bill's amendments, but we do not support a form of income management for all Australians, telling them how much of their income they can use for the repayment of small loan, that doesn't apply to a continuing credit contract such as a credit card and they represent more than three quarters of all complaints to AFCA.

In addition, the NCPA also does not support Subsection 133CF which prohibits the lender from communicating with their customers together with a totally unworkable restraint on contacting a customer who may have engaged with another SACC provider during the past 2 years. This is essentially an act by the Commonwealth that will depreciate the value of databases of all credit providers.

Finally, the NCPA continues to support a robust compliance regime but considers criminal sanctions a step to far.

A lower protected earnings amount will not dampen demand. Without a viable alternative, this proposed change will only drive borrowers to unregulated lenders who provide products that cause real consumer harm and does nothing to assist those vulnerable Australians wanting access to credit when they need it most. Where is the real problem?