

**Submission – Senate Economics Legislation Committee
Inquiry into the National Consumer Credit Protection Bill 2009 and related bills**

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This submission makes the following recommendation. There should be clarification of the time at which consumers must be given a Credit Guide and a credit assistance provider must enquire about the consumer's requirements and financial situation.

This submission is restricted to general comments on the importance of regulating the consumer credit market; supporting the obligation to provide a new Credit Guide when a debt is assigned; and querying the timing sequence of the obligations to give a Credit Guide, and to enquire and make a Preliminary Assessment.

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In a recent 101 page article on the US credit market Professors Oren Bar-Gill and Elizabeth Warren of New York University Law School and Harvard Law School, "Making Credit Safer" (2008) 157 *University of Pennsylvania Law Review* 1, have argued, with extensive evidence, that the chief problem in the credit market is product design. They argue that credit products are designed to be exploitative.

Bar-Gill and Warren argue that credit providers know more about how an individual consumer will use credit than that individual himself. They say that lenders can predict the individual's future use and particular weaknesses. They say that products can be constructed to take account of these weaknesses and in response to the consumer's imperfect information and imperfect rationality.

Bar-Gill and Warren say that there are minimum product safety standards for nearly all physical products. Such standards, they say, are noticeably absent for credit products.

The complexity of credit products, deficits in financial literacy, and growing knowledge of consumer behaviour and irrational decision-making make safety in credit as important as safety in physical products such as cars and children's toys.

The proposed National Consumer Credit Protection Bill 2009 does not prescribe credit products. Nor, generally, does it regulate the construction features of particular credit products to ensure that they are safe.

The National Consumer Credit Protection Bill 2009 combines a disclosure model with a suitability model to protect customers for consumer credit.

The disclosure model is well established, based on the existing "truth in lending" Credit Code. This is augmented by some modifications to the Code and new provisions. The new provisions assimilate towards financial services regulation by providing that consumers should receive information about who they are proposing to deal with, costs of the service, commissions and the like. Consumers must also receive the suitability assessment in some circumstances. These obligations fall on credit assistance providers and credit providers.

A further disclosure obligation falls on the person to whom “any rights or obligations of a credit provider under a credit contract” have been assigned. The assignee must give the debtor its credit guide. The debtor will then have the prescribed information about that licensee, including information about dispute resolution. There have been some objections to this provision. It should be remembered that in the US sub-prime crisis, many debtors and other with a legitimate interest in the debt have been unable to discover who actually holds the debt.

The suitability requirements are new for Australia. Nevertheless there are long standing obligations in Australian law similar to suitability. The market for goods requires goods to be fit for the purpose. Financial services providers must provide advice that is appropriate. The suitability obligation will be a move towards safer credit.

At various points in a proposed and prospective credit transaction the credit assistance provider and the credit provider must assess whether the proposed transaction is “unsuitable” for the consumer. To do this, the credit assistance provider or credit provider must elicit information about the consumer’s requirements, objectives and financial situation. The provider must verify the consumer’s financial situation. The provider is on constructive notice of the consumer’s financial situation.

With this information, the provider must assess if the suitability of the credit contract. The provider must take into account the whether it will meet the consumer’s objectives and requirements and whether the consumer will be able to comply with the financial obligations under the contract without substantial hardship. There are civil and criminal sanctions if the provider proceeds with an unsuitable recommendation or contract.

The credit assistance provider must provide a Credit Guide (which must set out the fees and charges for the assistance, commissions and six credit providers with whom the credit assistance provider does business) to the consumer and a Quote for credit assistance (with fees and charges).

According to the Explanatory Memorandum the purpose of the Credit Guide is to provide the consumer with information to enable the consumer to decide whether to use the services of the credit assistant. The Quote might include the scope of the assistance to be provided or the type of loan the consumer is looking for.

There may be a timing problem with these obligations. Logically the obligation should arise prior to gathering information for a Preliminary Assessment. Indeed the sequence of the provisions in the Bill indicates this.

However the point at which the obligation to provide the Credit Guide arises is as soon as practicable after it becomes apparent to the licensee that it is likely to provide credit assistance. When is this point in time?

Providing credit assistance is doing a number of things with respect to a “particular credit contract with a particular credit provider.” The earliest point of time at which the Credit Guide obligation arises is as soon as practicable after it becomes apparent

to the licensee that it is likely to suggest that the consumer apply for a particular credit contract with a particular credit provider.

Until there is a likelihood of a suggestion that the consumer apply for a particular credit contract there is not yet an obligation to give the Credit Guide.

This suggests:

Either the likelihood of suggesting an application for a particular credit contract, triggering the Credit Guide, will arise before the enquiries or preliminary assessment – in which case how has the likelihood of suggesting a suitable particular credit contract arisen?

Or,

The enquiries and preliminary assessment take place before the likelihood of suggesting an application for a particular credit contract, in which case the obligation to give the consumer a Credit Guide has not arisen and the consumer may be dealing with someone prior to receiving the mandatory information to help them decide whether or not to deal with such a person.

Under the FSR rules, the Financial Services Guide which is similar to the Credit Guide, must be given before the financial service will be or is likely to be provided. Thus if the service is personal advice, the Financial Services Guide must be given before personal advice is likely to be provided.

There is a difference between the likelihood of providing personal advice and the likelihood of suggesting (or advising) that a person apply for a particular product with a particular provider. The latter is, self evidently, more particular and the possibilities narrowed to the particular contract not to credit in general as opposed to personal advice in general.

As a result of the enquiries to enable the preliminary assessment, consumers will have to provide personal and sensitive information about their financial situation to a prospective credit assistant. This potential timing issue should be clarified.

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