

Chapter 4

Consumer leases

4.1 The National Credit Code and, by extension, the NCCP Act currently apply to certain consumer leases under which the consumer has the option or an obligation to purchase the goods that are the subject of the lease arrangement. These kinds of consumer leases are regulated in the same way as credit contracts, as the legislation classifies such arrangements as credit contracts.¹ However, the legislation does not provide the same protections for parties to consumer leases that do not provide the option to purchase or to consumer leases that, while providing the option to purchase, do not require the consumer to pay more than the cash price of the goods.

4.2 Statements in the Explanatory Memorandum contend that the dual regulatory framework 'may lead to avoidance behaviour and adverse competitive impacts on supplies of credit contracts relative to consumer leases.'² It is argued that the regulatory distinctions between credit contracts and consumer leases leave lessees 'particularly vulnerable to unscrupulous behaviour,' which reportedly includes:

- lessees mistakenly believing that they have an ability to buy the goods when they do not; and
- the amount paid under the lease may be significant (that is, greater than that paid under a credit contract to purchase similar goods) but the lessee has no right to the goods when the lease ends.³

4.3 It is understood that the current distinction mirrors regulation in state and territory legislation.⁴ As stated in the Second Reading Speech, and as reportedly intended by the development of a two-phased COAG consumer credit reform process,⁵ the reforms are designed to draw on the experience of state and territory regulations to rectify any weaknesses identified. At the introduction of the Enhancements Bill, Parliament was informed that state and territory experience demonstrates that the distinction between the regulation of certain forms of consumer

1 National Credit Code, s. 9.

2 Explanatory Memorandum, Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011, paragraph 6.8.

3 Explanatory Memorandum, Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011, paragraph 6.9.

4 The Hon Mr Bill Shorten, Assistant Treasurer, Minister for Financial Services and Superannuation, *House of Representatives Hansard*, 21 September 2011, p. 10954.

5 Explanatory Memorandum, Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011, paragraph 2.4.

leases and credit contracts facilitates lessors 'cherry picking what suits the lender not the borrower'.⁶

4.4 While this level of detail was not provided in the Explanatory Memorandum, further information is contained in Treasury's July 2010 *Green Paper*. The paper notes that the experience under state and territory legislation identified three issues with the regulatory approach to consumer leases, namely:

1. some providers of leases are offering a product where the consumer has no right or obligation to purchase the leased goods (rather than a credit contract or a lease where the consumer has this right or obligation), because of the lower regulatory burden under the Code;
2. consumers are being misled about whether or not they will own the goods, or have a right to purchase them, under the lease; and
3. the exclusion from the Code of short-term or indefinite leases results in some providers being able to avoid the Code entirely.⁷

4.5 The *Green Paper* also provides details of a 2007 study of consumer lease arrangements by the Micah Law Centre, which identified the following key concerns with the state and territory regulatory variations between consumer leases and credit contracts:

- the use of lease agreements instead of loan agreements by financiers as a means to avoid the stricter obligations that apply to credit contracts;
- complex or misleading clauses relating to final ownership of the goods;
- misleading and confusing marketing of lease agreements in stores;
- relatively high cost of lease agreements; and
- the impact of the marketing of these contracts to low-income consumers.⁸

4.6 To address these issues, under Schedule 5 of the Enhancements Bill it is proposed to align the regulation of consumer leases with the regulations applying to credit contracts under the NCCP Act and the National Credit Code.

6 The Hon Mr Bill Shorten, Assistant Treasurer, Minister for Financial Services and Superannuation, *House of Representatives Hansard*, 21 September 2011, p. 10954.

7 Treasury, *National Credit Reform: Enhancing confidence and fairness in Australia's credit laws – Green paper*, July 2010, pp 72–73.

8 Treasury, *National Credit Reform: Enhancing confidence and fairness in Australia's credit laws – Green paper*, July 2010, p. 70; citing Micah Law Centre, *A loan in lease clothing: Problems identified with instalment based rent/purchase contracts for household goods*, 2007.

Support for the proposed regulation of consumer mortgages

4.7 Of the six submissions commenting on the proposed changes to the regulation of consumer leases, five were strongly in favour of alignment between regulations for consumer leases and regulations governing credit contracts.⁹

4.8 While noting that its members do not provide consumer leases, Abacus – Australian Mutuals supported aligned regulations:

As a matter of general principle, except to the extent that the different product structures require a differentiated approach, we consider it appropriate for consumer leases to be regulated comparably with consumer loans where the lease contains a right or option to purchase. In our view, consumer leases are functionally identical with consumer loans in these circumstances. Generally comparable regulatory treatment is therefore appropriate from both a consumer protection and a level regulatory playing-field perspective.¹⁰

4.9 Submissions from consumer advocates supported the view that the current regulatory dichotomy creates loopholes that may be exploited to the detriment of the consumer.¹¹ The following statement by Redfern Legal Centre reflects the views of consumer advocates as depicted in evidence before the committee:

RLC is strongly supportive of creating rights and protections for lessees under consumer leases that substantially mirror the applicable rights and protections available for debtors under credit contracts...Addressing this gap in consumer credit laws is important to prevent unscrupulous industry participants from taking advantage of the loophole in order to bypass their obligations under the Act.¹²

4.10 The committee was provided with case examples of the effect of the regulatory distinction currently drawn between certain consumer leases and credit contracts. Cases include the following example submitted by the Consumer Credit Legal Centre (NSW) Inc as an example of the conduct that may be left unchecked due to regulatory loopholes:

A consumer wanted to buy her son an X-box for Christmas but did not have the cash and had voluntarily cut up her credit card. She knew she did not have time to replace the card before Christmas as it was only two days away. She was offered a consumer lease instead. The terms were very expensive – even compared to a credit card – the equivalent of between 30

9 Anglicare Victoria, *Submission 39*, p. 7; Consumer Action Law Centre, *Submission 20*, p. 14; Consumer Credit Legal Centre (NSW) Inc, *Submission 47*, p. 10; Redfern Legal Centre, *Submission 18*, p. 9.

10 Abacus – Australian Mutuals, *Submission 38*, p. 4.

11 Consumer Action Law Centre, *Submission 20*, p. 14; Consumer Credit Legal Centre (NSW) Inc, *Submission 47*, p. 10; Redfern Legal Centre, *Submission 18*, p. 9.

12 Redfern Legal Centre, *Submission 18*, p. 9.

and 40% interest after 12 months of payments. The salesperson said that for one extra payment the goods could be retained...The 12 monthly payments were made and then a 13th to secure ownership of the goods. The direct debit, however, continued to come out for a 14th month. The consumer contacted the lease company to complain. They said that contrary to what the salesperson had said it was necessary to contact the company and negotiate the amount of the final payment or the lease would continue indefinitely! This meant that the final cost of the goods could not be accurately estimated in advance and clearly exceeded the 30 or 40% per annum the consumer had reluctantly agreed to pay.¹³

4.11 Similarly, the Redfern Legal Centre provided the following case study as evidence of the deleterious effects of the regulatory dichotomy:

Lauren is a mother of five. When her car broke down, Lauren went to a well-known car dealership to buy a second hand car. After speaking with the sales representative, Lauren signed a contract and drive off with a second hand vehicle. Lauren soon ran into difficulties meeting her repayments. She came to Redfern Legal Centre for advice. Lauren was shocked to learn that she had in fact signed a consumer lease, and that at the end of the lease she would not own her vehicle. This had not been made clear to her when she went to the dealership with the intention of buying a car.¹⁴

4.12 Advocating that the amendments will offer appropriate and needed protections for consumers party to consumer leases, Anglicare Victoria drew the committee's attention to the merits of the following aspects of the proposed regulations.

A unilateral alteration of a lease by the lessor will be void without the lessee's agreement.

This alteration will allow consumers to continue to budget appropriately for the leased item, without variation. This will give the consumer the opportunity to maintain household budgets without unexpected hidden costs appearing six months into a signed contract.

Consumer leases can be changed under hardship grounds or on the basis the transaction is unjust.

This will allow consumers in the event of changed circumstances eg changed income, relationship breakdown or illness to alter the amount repayable without the difficulties faced previously.

A criminal penalty for harassment applies to the lessor or supplier.

Lessees with low incomes are particularly vulnerable because they tend to forego other essential expenses to maintain these repayments especially if they are leasing a car for work purposes or replacing broken whitegoods.

13 Consumer Credit Legal Centre (NSW) Inc, *Submission 47*, p. 11.

14 Redfern Legal Centre, *Submission 18*, p. 9.

These provisions address the current lack of legislation that has led to lessors pressuring lessees in financial hardship to enter into unrealistic repayment arrangements for arrears...heavy handed tactics are not beneficial in working towards an amicable resolution for either party. Reports of abusive phone calls, letters and upsetting collection procedures only deter consumers from communicating.¹⁵

4.13 Accordingly, it was argued that the proposed alignment of regulations between consumer leases and credit contracts 'is welcome and long overdue.'¹⁶

Additional measures proposed

4.14 While strongly supporting the proposed alignment, consumer advocates proposed additional measures for the regulation of consumer leases.

4.15 The Consumer Action Law Centre and the Consumer Credit Legal Centre (NSW) Inc argued that the regulations under clause 175D must require periodic statements of account to include a clause drawing the lessee's attention to the fact that the goods remain the property of the lessor at the end of the lease.¹⁷ In support of this recommendation, the Consumer Action Law Centre advised:

[o]ne of the most common complaints we hear from consumers regarding consumer leases is that they were misled or otherwise unaware that had entered into a consumer lease (rather than a credit contract) and that they would not own the goods at the end of the lease term.¹⁸

4.16 Proposals also included making lessees only liable for the market value of the goods as at the time the goods were lost or stolen.¹⁹

4.17 National Legal Aid (NLA) also noted that the proposed regulations do not include a cap on costs, as is proposed under Schedule 4 of the Enhancements Bill in relation to credit contracts excluding bridging finance arrangements and credit contracts provided by ADIs. In support of this recommendation, National Legal Aid submitted:

The National Credit Code now provides in s.9 that leases over goods on hire purchase are regulated loans and provides that the cost of credit is the amount payable over the term of the contract less the cash price of the goods (definition in Part 13).

This strengthened definition of cost of credit meant that some high cost lenders changed from offering goods on hire purchase to consumer leases,

15 Anglicare Victoria, *Submission 39*, p. 8.

16 Consumer Action Law Centre, *Submission 20*, p. 14.

17 Consumer Action Law Centre, *Submission 20*, p. 15; Consumer Credit Legal Centre (NSW) Inc, *Submission 47*, p. 11.

18 Consumer Action Law Centre, *Submission 20*, p. 15.

19 Consumer Credit Legal Centre (NSW) Inc, *Submission 47*, p. 11.

effectively meaning that they went from no regulation to “lighter-touch” legislation and were outside the ambit of 48% interest rate caps applicable to hire-purchase contracts.

In NLA’s view, there is no reason to artificially distinguish between goods that retain some value to the lender at the end of a consumer lease and goods which are paid for entirely by the borrower who takes ultimate possession.

The cost of credit for a consumer lease ought to be regulated by the interest rate caps. This could be done by amending the National Credit Code to ensure that the cost of credit is defined as the amount payable over the term of the lease less the cash price up-front using the Part 13 definition and the market value of the goods (if any) upon termination.²⁰

4.18 The Redfern Legal Centre questioned drafting differences between the provisions in the NCCP Act and National Consumer Code relating to credit contract and the provisions proposed as part of the Enhancement Bill. In particular, the Centre noted stylistic differences in terminology and language used and recommended greater consistency between the provisions.²¹

Concerns with the proposal to align consumer lease and credit contract regulations

4.19 The views of industry representative, the Australian Finance Conference (AFC), were in stark contrast to the approval provided by consumer advocates. The AFC questioned the need for regulatory alignment, arguing that existing regulations under the NCCP Act are sufficient to promote market integrity in relation to the provision of consumer leases.

AFC is not aware of evidence to substantiate regulatory or market failure in the provision of consumer leases that would justify additional regulation either under the newly enacted NCC law or elsewhere. We understand that a principal driver is concern of regulatory arbitrage, but remain concerned with the level of evidence-based research or empirical analysis that would give credence to this justification for change.²²

4.20 The AFC also submitted that the introduction of aligned regulations would be premature, given the relatively recent introduction of the NCCP Act and the Consumer Credit Code.²³ Were the alignment measures to be introduced, the AFC recommended the following amendments to the provisions:

Statements of account – we continue to question the need for the issue of a statement of account other than in response to a request from a customer.

20 National Legal Aid, *Submission 19*, p. 5.

21 Redfern Legal Centre, *Submission 18*, p. 9.

22 Australian Finance Conference, *Supplementary Submission 29a*, p. 12.

23 Australian Finance Conference, *Supplementary Submission 29a*, p. 2.

Given the static nature of the repayment amounts and period, this requirement appears to add compliance cost with no real customer protection benefit.

End of lease term – we submit that a provider should be able to contact a customer within 90 days of the end of the lease term to explore options rather than the current approach. This contact would, in the experience of our members, be far more meaningful to the customer given its relationship with the lease term and would therefore benefit both customer and financier.²⁴

4.21 In addition, and as canvassed in chapter two, the AFC were concerned with the provision allowing consumers to seek to vary consumer leases on hardship grounds and the proposed framework for enforcement proceedings.²⁵

Committee view

4.22 While noting the AFC's concerns with the timing of the introduction of the measures, the committee considers that the same protections should be afforded to consumers under all categories of consumer leases, and, therefore, between parties to all consumer leases and credit contracts. The committee notes that the provisions are intended to address problems for consumers that have arisen under state and territory consumer credit legislation. Evidence provided in the *Green Paper* and in submissions received for this inquiry strongly indicates that the dual regulatory system has created loopholes that allow unscrupulous lenders to avoid consumer protection requirements. This is neither conducive to prudent market regulation or to supporting a market in which vulnerable consumers can confidently participate.

4.23 The committee agrees with the view that periodic statements should clearly confirm that the arrangement does not transfer title to the lessee. This is an important clarification that will assist consumers to make informed credit choices. The committee also considers that there is merit to limiting the outstanding obligations on lessees to the market value of the goods where the goods are lost or stolen.

Recommendation 10

4.24 The committee recommends that the regulations under clause 175D require the statement of account to contain a clear statement that the lessee will not own the good at the completion of the lease.

Recommendation 11

4.25 That Schedule 5 be amended to restrict the liability of lessees under consumer leases for which the goods have been lost or stolen to the fair market value of the goods as at the time the goods were lost or stolen. This would not, however, apply in circumstances of fraud on the part of the lessee.

24 Australian Finance Conference, *Supplementary Submission 29a*, p. 12.

25 Australian Finance Conference, *Supplementary Submission 29a*, p. 12.

