



**Virgin Money
(Australia) Pty Ltd**

Level 4, 7 Macquarie Place,
Sydney NSW 2000
PO Box R1801
Royal Exchange
NSW 1225
tel: (02) 8249 8000
fax: (02) 8249 8001

Attention: Mr Peter Hallahan, Committee Secretary
Senate Economics References Committee
Suite SG.64
Parliament House,
Canberra ACT 2600

Re: Submission from Virgin Money Australia in response to invitation from the Senate Economics References Committee to provide comment on the inquiry into *Possible links between household debt, demand for imported goods and Australia's current account deficit*

ABOUT VIRGIN MONEY:

Virgin Money entered the Australian financial services market in May 2003 with its first financial services product, the Virgin Credit Card. Almost half a million cards were in circulation within 18 months, with the card's popularity the result of the low introductory and ongoing interest rates, no annual fee and an innovative reward program, Mates Rates.

The introduction of the Virgin Credit Card has sparked increased competition in the low-cost end of the credit card market in Australia. Indeed the Reserve Bank Governor, Ian Macfarlane, publicly acknowledged in December 2003 that the entry of non-traditional players in the credit card industry, like Virgin Money, "is very effective" in terms of applying competitive pressure on established financial institutions.¹

Since its entry into the Australian market, Virgin Money has been a strong advocate of overhauling the Australian financial services industry to make it more competitive and transparent for consumers, and to bring its practices into line with world's best practice. It is for this reason that Virgin Money has welcomed the opportunity to provide an industry perspective on some of the issues relating to household debt as part of this Committee's important inquiry.

The relatively niche range of Virgin Money products available in Australia has meant we have largely restricted our comments and suggestions to the specific parts of the industry in which we have expertise. However many of the principles remain the same and could indeed be applied further across the financial services industry as part of a holistic approach to addressing national concerns about household debt and its broader implications for the Australian economy.

Virgin Money would be more than willing to offer further industry insights to the Senate Economics References Committee, should the Committee wish to explore some of these issues further.

ROHAN GAMBLE
Managing Director

¹ Hansard, House of Representatives Standing Committee on Economics, Finance and Public Administration, 8 December 2003, Sydney.

EXECUTIVE SUMMARY:

The Federal Government's commitment to corporate governance reform and improved financial literacy during its third term of government has been welcomed by Virgin Money. We believe that each of these aspects is key to achieving an open and transparent economy which enjoys the confidence of Australian consumers.

As a relatively new but significant player in the Australian financial services industry, Virgin Money, like the Federal Government, believes that over-regulation is not in the best interests of either the industry or the broader economy.

We do however recognise that Australian household debt is at an unprecedented level and that this dubious 'record' carries with it the risk of serious implications for individual socio-economic disadvantage as well as for the broader health of the Australian economy. At the time of the 2003-04 Federal Budget total household debt had increased to 125 per cent of income, and 17 per cent of assets, and debt-servicing costs were around 6 per cent of income.²

Virgin Money submits that an important part of managing household debt levels, is ensuring Australian consumers adequately understand the terms and conditions of their credit, and therefore, ensuring that financial institutions are open and transparent in communicating interest rates, fees and charges for each of their products.

With so many different financial products on the market, Virgin Money further submits that the most appropriate way to deliver this transparency effectively for the consumer, without heading towards a "nanny-state" mentality, is through the implementation of a standardised mechanism for the publication of important product information.

Virgin Money has always had a strong record as an industry leader in consumer product disclosure. In late 2003 we introduced a concept known as the "Honesty Box" into all Virgin Credit Card print advertising.

Relatively simple, the Honesty Box presents the interest rates, key fees, and core terms and conditions of our card in a clear and easily understandable manner. However the value of the Honesty Box to consumers will only be realised if it – or a version of it – is required at a national level of all credit card providers. Australian consumers need to be able to easily compare the fees and charges associated with each credit product to ensure they select a product that best suits their financial means. As Virgin Money's own financial services product range expands, we intend to apply similar transparency principles to the rest of our consumer advertising.

Virgin Money believes the Federal Government has a role to play in introducing standardised marketing practices for financial services products – in the same way as their counterparts in the United States and the United Kingdom have already done. The approach is consistent with both the Federal Government's pursuit of greater financial literacy and its desire for constructive yet not overly onerous regulatory reform.

² 2003-04 Federal Budget Paper No. 1

SPECIFIC RESPONSES TO KEY TERMS OF REFERENCE:

a) current levels of household debt and whether these are historically high (as a proportion of household income or otherwise);

In terms of household debt, credit card debt comprises only a relatively small proportion of total debt and therefore in itself, is not as significant a factor in total household debt levels. According to the Reserve Bank of Australia (RBA) around three per cent of Australia's household debt is held on credit cards.

However, around 70 per cent of Australian households have at least one credit card³ and statistics released by the RBA in November 2004 show that there are over 11,358,000 credit and charge card accounts operating in Australia, representing an increase of well over 50 per cent since September 1996. On average, each credit card account holder owes \$2,520 with the nation owing a total debt of \$28.6 billion.

However it is not just the amount of money owed on credit and charge cards that has been rapidly increasing; the amount of fees and interest paid by Australian consumers to use their credit cards has also increased to record levels. According to the RBA, household credit card fees increased by almost 40 per cent in 2003 and on average by 30 per cent in each of the five previous years. Furthermore, while the official cash rate remains at 5.25 per cent, the average credit card interest rate is now 16.25 per cent, and one third of credit card holders are paying interest rates of 18 per cent or more. The Committee will appreciate that the average cost of servicing this credit card debt is significantly higher proportionately than the average 6 per cent for servicing total household debt.

Virgin Money submits that the level of penetration of credit cards into Australian households, and the increasing amount of fees and charges paid by Australians in servicing credit cards, is an important factor to consider against the wider context of household debt. There is no doubt that in the process of making monthly outlays from the household budget, that credit card debt is a contributing factor.

b) the factors, including the lending policies of banks and other financial institutions, that contribute to household debt levels;

Virgin Money believes there are two key aspects of lending policies that should be considered when gauging their contribution toward household debt levels in Australia.

The first is the overall the ease with which credit can be gained.

Whether it be a home loan, car loan, personal loan or a new credit card, loans have never been easier for consumers to acquire. Historically low interest rates have led to an era where it seems nearly everyone can get a loan.

With multiple lending institutions offering credit, consumers have a wide range of choice, comfortable in the knowledge that a suitable loan can be found. As the market becomes more competitive, in a bid to avoid the risk of losing market share, it would

³ RBA publication *Financial Stability Review*, September 2004

appear that some lenders have been downgrading their lending criteria.

The credit policies of one of Australia's biggest lenders recently came under scrutiny, when it was reported that the institution did not check the credit history of borrowers through an external agency. Similarly, last year, ASIC also warned borrowers against being duped into debt reduction loans where borrowers end up being worse off.

Virgin Money submits that a general lack of understanding by the borrowing public of how loans operate as well as the reportedly lax credit policies of lending institutions are exacerbating household debt levels.

The second important aspect to consider is that of misleading advertising practices employed by credit providers.

As a relatively new participant in the Australian industry, Virgin Money has been surprised at the low level of regulatory disclosure required in the Australian market. In particular, we feel that the incumbents within the industry have taken advantage of the lack of formal disclosure rules to reduce consumer awareness and understanding of the interest rates, fees, terms and conditions associated with a credit card offering.

Essentially the major problem faced by consumers lies in the disparate and disjointed nature of information presented by credit card providers. Generally speaking, consumers must currently trawl through numerous pamphlets, brochures, contracts and web pages to find all the relevant information about a credit card. In addition, critical information is often hidden in small print or buried in technical legalese, significantly reducing the consumer's ability to find and decipher information relating to fees and charges.

Many banks and financial institutions advertise their credit card offerings with low "honeymoon" introductory rates for the first six months, at the end of which period the interest rate often increases to an excessive level. Consumers who either don't possess an understanding of how credit cards operate, or who are time poor, tend not to delve into the fine print, especially since the introductory rates in bold, large print have been designed to be extremely appealing to consumers. As a result consumers risk accumulating significant debt, without truly realising how much interest they will be required to pay back once the introductory period has concluded.

Virgin Money submits that the high level of credit card expenditure in Australia – and therefore the high levels of credit card interest and fees paid by Australians each year – demands the need for more transparent marketing practices across the credit card industry. Australian consumers need to be able to easily compare the interest rates, fees and conditions associated with each credit card product to ensure they select the card that best suits their financial means.

Virgin Money – A responsible industry leader

For its part, Virgin Money has implemented a *Responsible Lending Policy* which contains three key components designed to reduce the risk of a customer accumulating unserviceable debt.

- Virgin Money has no pre-approved card offers. An assessment of every applicant's ability to meet card repayments is undertaken before approving a new Virgin Credit Card. As a result, **we do not market pre-approved Virgin Credit Card** offers to potential customers. This is in stark contrast to standard industry practice.
- Virgin Money believes in responsible credit limit increases. Virgin Money does from time to time offer some Virgin Credit Cardholders the opportunity to increase their credit limit but **no increase is automatic**. An assessment of the cardholder's ability to meet card repayments is undertaken before confirming the increase. Cardholders always have the right to decline the offer and retain their existing limit, or to request a smaller increase.
- Virgin Money has implemented a transparent pricing policy. **Virgin Credit Card print advertising includes an Honesty Box** clearly outlining the key fees and interest charges relating to the card. A full fee schedule is clearly set out on our website just one click away from the home page.

Virgin Money believes that its *Responsible Lending Policy* approach is consistent with that of a responsible industry leader, particularly given the increasing level of concern over national levels of household debt.

f) whether there is a case for addressing the lending policies of banks and other credit providers and if so, what practical options are available;

Virgin Money prides itself on a commitment to providing honest, upfront and straightforward information in all of our marketing literature. Our belief is that consumers must have all the critical information about a financial product at their disposal before an informed decision can be made. For Virgin Money, this means taking the information that is usually hidden in the fine print of marketing literature and bringing that information out into the open.

Unfortunately this is not an attitude that is generally shared within Australia's credit industry and therefore Virgin Money believes there is a case for addressing the lending policies of banks and other credit providers. It is not in Australia's economic interest for credit providers to be able to operate completely unfettered given the links between growing levels of credit and unprecedented household debt.

Reforming the credit card industry:

In December 2003, during his regular hearings with the House of Representatives Standing Committee on Economics, Finance and Public Administration, the Governor of the Reserve Bank was responding to a question about the increase in the costs of holding a credit card and said:

*"One of our (the Reserve Bank's) aims has actually been to try and make the true cost visible to the people who are making the decision as to whether or not to use a credit card."*⁴

⁴ Hansard, House of Representatives Standing Committee on Economics, Finance and Public Administration, 8 December 2003, Sydney.

Although this is but one relatively small aspect this Committee may choose to focus on, Virgin Money believes that there is a strong case for reforming and standardising credit card marketing practices. As a matter of public policy, Virgin Money believes credit card providers should be required to present vital information in a format that is transparent, user friendly and which enables comparisons to be easily made.

Other industries, such as the food and pharmaceutical industries, have already been required to standardise their marketing practices in the interests of full product disclosure for the consumer. The Federal Government introduced food labeling laws in 2003, which requires virtually all manufactured foods to carry a nutrition information panel. Likewise, the pharmaceutical industry, when promoting products in any form, must strictly adhere to a Code of Practice, otherwise the companies risk facing huge fines.

In each case these regulations have been introduced in recognition of the significance of the respective industries' products to Australian consumers – and Virgin Money suggests that at this time of unprecedented levels of household debt, that the financial services industry, particularly credit card providers, should be subject to the same kind of "labeling" regulations. We believe this can be achieved through the industry-wide adoption of what is known as an Honesty Box.

An Honesty Box brings together the most important information about a credit card and provides a means of comparing the costs and benefits of each card. It will create greater transparency and accountability in credit card marketing and in doing so, will assist consumers in better understanding the credit liabilities of the various products.

However for the Honesty Box to achieve its objectives on behalf of consumers it must be implemented right across the credit card industry. Industry-wide adoption of the Honesty Box will enable the consumer to effectively "comparison shop", ensuring consumers select a credit card most appropriate to their financial means.

Virgin Money submits that the introduction of new regulations to make it mandatory for credit card providers to include a standardised Honesty Box into all of their credit card marketing literature, as well as potentially other financial products, is a practical and easy option to implement, and one which has precedence in both the United States and the United Kingdom.

In 1988, United States Democrat Senator Charles Schumer authored a provision in the *Truth in Lending Act* requiring credit card providers to use Honesty Boxes or "Schumer Boxes" as they are known in that country. In the United Kingdom, credit card providers introduced Summary Boxes into pre-contract marketing materials from 31 March 2004, following an inquiry by the Treasury Select Committee into the types of improvements that could be made to provide clear and understandable information to consumers when obtaining a credit card.

The Honesty Box is fast becoming a feature of world's best practice and it is imperative that Australia ensures its regulatory framework similarly meets this standard. The new requirements could be phased in over a period of six to twelve months, thereby minimising the cost to industry in terms of their marketing materials production cycles.

#1. Check for high interest anxiety.

Plastic surgery
self assessment
test#1



Introductory rate	4.9% p.a. for the first 6 months
Ongoing interest rate	12.4% p.a.
Interest free period	Up to 55 days on purchases
Annual & rewards fees	None... ever
Rewards	Mates Rates™ rewards

Wondering whether you need plastic surgery? If you're paying any more than 12.4% p.a. ongoing interest on your current credit card or store card, go the chop. Virgin Credit Card cuts your interest rate down and slices off your annual fee completely... gone forever. You might also like to examine our 4.9% p.a. introductory rate for the first 6 months. Call 13 28 82 now or apply online at virgincreditcard.com.au



Shaping up credit cards.™

This information is current as at 1 March 2004. The Virgin Credit Card is issued by Westpac Banking Corporation ABN 33 007 457 141 and Westpac is the credit provider. Applicants are subject to Westpac's normal lending criteria. Fees and charges apply to the Virgin Credit Card. Full details of all terms and conditions are available on request. These may be varied, or new terms and conditions introduced in the future. The ongoing rate of 12.4% p.a. is a variable rate and therefore subject to change. Virgin Money (Australia) Pty Ltd ABN 75 103 478 807. 360XXXXXXX

g) whether there are other measures that might be taken in place of possible restrictions on lending practices which would be as effective;

Consistent with the Federal Government's general philosophical approach, Virgin Money does not believe it is in the interests of an open market economy to overly-regulate or restrict a particular industry's capacity to operate in the marketplace.

Virgin Money does however believe there is a role for the Federal Government to identify and implement regulatory means to ensure that consumers are in the best possible position to assess the various financial products on offer in the market, in an open and transparent manner.

As outlined above, Virgin Money submits that the mandatory introduction of a standardised Honesty Box in all printed marketing materials relating to credit cards will be an effective tool to ensure that consumers have the opportunity to compare the different credit cards that are available, both their introductory offers and their ongoing rates and fees. Similar regulatory reforms may also be appropriate across the broader Australian banking and credit industries.

h) whether any Commonwealth social and economic policy settings should be changed as a result of matters identified above;

Currently, responsibility for the Uniform Consumer Credit Code lies with the individual States and Territories. This in itself is somewhat of a peculiarity as the bulk of the financial services industry is regulated at a Federal level.

In seeking to address issues relating to household debt and options for managing debt better, Virgin Money submits that not only do consumers need to be provided with a set of standardised information relating to credit card products, but that this information should be a mandatory requirement regardless of the State or Territory in which they live and the financial institution with which they are dealing.

Interestingly, one of the few recommendations from the 1997 Wallis Report that remains outstanding is the review of the Uniform Consumer Credit Code. The Wallis Report recommended that:

"After (the Uniform Consumer Credit Code) has operated for two years, the UCCC should be subject to a comprehensive and independent review to consider what improvements are necessary and whether a transfer to the Commonwealth would be appropriate."

This recommendation has not yet been acted upon and as such provides this Committee with a strong rationale to investigate the procedures required for the Commonwealth to assume jurisdiction in consumer credit law. The case for this is supported by further comments in the Wallis Report, stating:

"A single market conduct and disclosure regulator for the financial sector should be established by the Commonwealth (the Corporations and Financial Service Commission (CFSC)). This new body should seek to establish a consistent and comprehensive disclosure regime for the whole financial system... The Inquiry would

in principle prefer that the CFSC assumed responsibility for the Uniform Consumer Credit Code..."⁵

Virgin Money submits that the industry-wide adoption of the Honesty Box can only occur if there is a national, uniform approach to this issue and as such would encourage this Committee to recommend a transfer of responsibility for consumer credit law from the States and Territories to the Federal Government.

SUMMARY RECOMMENDATIONS:

- Virgin Money submits that issues relating to household debt are significant for the Australian community, and therefore require and deserve national leadership.
- Virgin Money submits that an important part of managing household debt levels is ensuring Australian consumers adequately understand the terms and conditions of their credit, and therefore, ensuring that financial institutions are open and transparent in communicating interest rates, fees and conditions for each of their products.
- Virgin Money proposes this Committee recommends regulatory reform for the mandatory requirement for credit card providers to standardise the presentation of key rates, terms, fees and conditions in all written marketing materials.
- Virgin Money proposes this Committee recommends a transfer of consumer credit laws from State and Territory to Federal Government responsibility.

⁵ Wallis Inquiry Report pages 17 & 19