

Chapter 1

Introduction

The Reference

1.1 The Australian Securities and Investments Commission (Fair Bank and Credit Charges) Amendment Bill 2008 (hereafter the ASIC bill) was referred to the Senate Economics Committee on 19 March 2008 on the recommendation of the Selection of Bills Committee. An earlier version of the bill had been referred to the committee in 2007, but the committee was unable to present a final report on that bill because the 2007 general election intervened. The Committee presented an interim report to that effect on 11 February 2008.

The Bill

1.2 The ASIC bill is a private senator's bill that was introduced by Senator Fielding on 14 February.

1.3 The bill proposes to amend the Australian Securities and Investments Commission Act 2001 to: limit banking and credit card penalty fees by ensuring fees are for cost recovery only; prevent fees being charged for third party dishonoured cheques; and enhance the powers of the Australian Securities and Investments Commission to monitor penalty fees and investigate customer complaints.¹

Submissions and Conduct of the Inquiry

1.4 The reference was advertised in the press on 26 March 2008 and on the Committee's website. The Committee also contacted a number of organisations to notify them of the inquiry and to invite them to make submissions. The Committee received several form letters and twenty-nine submissions in relation to the bill. The Senate also authorised the Committee to take account of the evidence submitted in relation to the 2007 bill.² A list of submissions may be found at Appendix 1.

1.5 The committee conducted a public meeting on the reference in Sydney on 12 June 2008. Witnesses who gave evidence at the hearing are listed in Appendix 2.

Acknowledgements

1.6 The Committee thanks those who assisted with its inquiry.

1 *Senate Bills List*, at: http://parlinfoweb.parl.net/parlinfo/view_document.aspx?id=1444&table=BILLSLST (accessed 18 June 2008).

2 *Journals of the Senate*, 20 March 2008, p.310.

Fees and charges

1.7 The bank fees and charges that are subject to this inquiry are described in the bill as *default charges*. A *default charge* is defined in the bill as follows:

default charge means a pre-determined fee or charge of any kind in a contract between a financial service provider and a consumer where that fee or charge is payable by the consumer in the event of a consumer default.³

1.8 These fees and charges may also be described as *penalty fees* or (by the banks) as *exception fees*. In this inquiry witnesses used all these terms interchangeably, but wherever possible in this report the Committee has used 'default charges'. Default charges include account overdrawn or honour fees, credit card over limit fees and late payment fees, cheque inwards and outwards dishonour fees and direct debit dishonour fees.

Background

1.9 Bank customers who have defaulted on their contracts with the banks by, for example, exceeding limits on credit cards or not having sufficient funds in an account to cover a direct debit payment, have expressed concern for some time about the application and quantum of default charges levied by the banks.

1.10 CHOICE and the Consumer Action Law Centre in a joint submission to the inquiry informed the Committee that the organisations had identified default charges as a significant issue for consumers several years ago and that they had campaigned on this matter since 2004.⁴

1.11 Also in 2004 concerns relating to default charges were examined in detail in a report published by the Consumer Law Centre Victoria (the Rich report).⁵ That report concluded that:

Cheque and direct debit dishonour fees are penalties at law. If Australian banks continue to assert that dishonour fees are enforceable as liquidated damages, they should release the data that proves this to Australian consumers.

Penalty charges are disproportionately borne by those who can least afford to pay them, namely, low-income consumers.

It is difficult for low-income consumers to avoid penalty charges.

Penalty charges contribute to preventing low-income consumers escaping their state of financial hardship.⁶

3 ASIC (Fair Bank and Credit Card Fees) Amendment Bill 2008, Clause 12FAA Definitions.

4 CHOICE and Consumer Action Law Centre, *Submission 18*, p. 1.

5 Nicole Rich, *Unfair fees: A report into penalty fees charged by Australian Banks*, Consumer Law Centre Victoria, December 2004.

1.12 The Rich report observed that while the lack of transparency on the part of the banks made it difficult to assess whether penalty charges were in fact penalties at law the failure of the banks to demonstrate the genuine losses involved in defaults made it difficult for the banks to assert that the default charges they charged were not penalties at law.⁷

1.13 The evidence on costs submitted at the Committee's inquiry drew heavily on the work done by the Rich report and also on anecdotal evidence, because there is still no more recent information on the costs to financial institutions of customer defaults.

Quantum of default charges

1.14 Data for income earned from default charges by Australia's financial service providers are not available.

1.15 The Reserve Bank of Australia (RBA) routinely publishes aggregate figures on banking fees in Australia which show that in 2007, total income from fees grew by 8 per cent to \$10.5 billion, with fee income from households growing faster than fee income from businesses.⁸ In relation to fees earned from credit cards, for which more disaggregated data are published, the RBA reported that fee income had grown by 170 per cent over the past five years and that this mainly reflected strong growth in unit fees (particularly annual fees, over-limit and late payment fees and foreign currency conversion fees), but also a 30 per cent increase in the number of credit card accounts and a 20 per cent increase in the value of cash advances.⁹

1.16 Ms Elissa Freeman, Senior Policy Officer, CHOICE, informed the Committee that CHOICE had approached the RBA to request that additional information on categories of fees should be published. She stated that the RBA had indicated that this might possibly be done in the next annual survey, which will not be published till May 2009.¹⁰

1.17 Choice and the Consumer Action Law Centre, relying on the figures that are published by the RBA, submitted that:

Penalty fees have been steadily increasing since 2002. In the case of credit card over-limit fees, the rate of growth has been exponential. These fees did not exist in 2000 and now average \$30 each (and can be as high as \$35.)¹¹

6 Nicole Rich, *Unfair fees: A report into penalty fees charged by Australian Banks*, Consumer Law Centre Victoria, December 2004, pp 21, 45.

7 Nicole Rich, *Unfair fees: A report into penalty fees charged by Australian Banks*, Consumer Law Centre Victoria, December 2004, p. 21.

8 Reserve Bank of Australia, *Banking Fees in Australia*, *Reserve Bank Bulletin*, May 2007, p. 79.

9 Reserve Bank of Australia, *Banking Fees in Australia*, *Reserve Bank Bulletin*, May 2007, p. 82.

10 Ms Elissa Freeman, Senior Policy Officer, CHOICE, *Committee Hansard*, 12 June 2008, p. 6.

11 CHOICE and consumer action law centre, *Submission 18*, p. 5.

1.18 Recently, default charges have trended downwards, and new products with low or no charges have been marketed. The great majority of these changes has occurred since a CHOICE campaign against unfair fees began in June 2007 and the 2007 version of the ASIC (Bank Fees and Charges) Bill was presented to the Senate.

1.19 The Australian Bankers' Association Inc. (ABA) submitted data that show a range of the lowest default charges, described as 'exception fees' by the banks, imposed on transaction accounts and credit cards. The data show that most banks no longer impose inward dishonour fees on regular transaction accounts. One product offered by a major bank does not impose any 'exception fees'. With that one exception, honour fees range from \$20 to \$45 and outward dishonour fees range from \$35 to \$45. There is a range of lower charges on transaction accounts offered for low-income earners and concession card holders. Banks charge late payment fees on credit card accounts and, with one exception for a concession account, also impose overlimit fees on those accounts. The quantum of default charges on credit card accounts is similar to those on transaction accounts.¹²

1.20 The ABA also submitted a copy of a 'Fact Sheet' published by the Association which includes information for potential bank customers about how to avoid or reduce default charges.¹³

Regulation of default charges

Australian Securities and Investments Commission

1.21 The Australian Securities and Investments Commission (ASIC) informed the Committee that the principal measure for regulating fees for financial services is the mandating of disclosure. The extent of disclosure depends on the product, with some products requiring Product Disclosure Statements (PDS). Basic deposit products and credit cards do not require a PDS, and ASIC's role is limited to ensuring that product providers do not engage in misleading, deceptive or unconscionable conduct. ASIC does not have the jurisdiction to prohibit or prevent the charging, or regulate the amount of, any properly disclosed default fees.¹⁴

1.22 ASIC also observed that:

The common law doctrine of penalties, which renders some contractual provisions in relation to damages for breach of contracts unenforceable, affects the rights and obligations of the parties to a contract. Such rights can only be enforced by individual consumers seeking relief under the common law ...¹⁵

12 Australian Bankers' Association Fact Sheet, 'Exception Fees November 2007', Submission 17.

13 Australian Bankers' Association Fact Sheet, 'Exception Fees November 2007', Submission 17.

14 Australian Securities and Investments Commission, *Submission 12*, pp 1-2.

15 Australian Securities and Investments Commission, *Submission 12*, p. 2.

Uniform Consumer Credit Code

1.23 Specific disclosure requirements for credit products exist at state level under the Uniform Consumer Credit Code (UCCC).¹⁶ The UCCC imposes certain requirements for credit contracts for individuals, but there is little scope under the Code to challenge the quantum of fees and charges under those contracts. Under section 72 of the UCCC establishment fees and early termination fees may be challenged by a debtor or guarantor on the grounds that they are 'unconscionable', but there is no definition of 'unconscionable' in the Code. Government consumer agencies do not have standing to make applications relating to section 72, or more generally under the UCCC, and the cost and uncertainty of litigation in relation to the sums involved might militate against individual consumers taking action.¹⁷

1.24 ASIC informed the Committee that proposals for reform of the law include amendment of section 72 of the UCCC to make all fees reviewable, to replace 'unconscionable' with 'unreasonable' and to give government agencies standing to represent the public interest or individual debtors or groups of debtors.¹⁸

Other State laws

1.25 Victoria has enacted legislation in relation to unfair contract terms. Evidence submitted to the Committee indicated that the *Fair Trading Act 1999* [Vic.] may apply to financial services but that the Victorian authorities have not pursued the banks under the legislation.¹⁹

1.26 The Committee was informed that, in New South Wales, Section 10 of the *Contracts Review Act 1980* [NSW] provides for that State's Attorney-General to seek declarations that a particular term of a contract is unfair. This has not been done since the legislation was enacted.²⁰

Proposed National Generic Consumer Law

1.27 A recent Productivity Commission report on a *Review of Australia's Consumer Policy Framework* recommended that there should be a new national generic consumer law and that unfair contract terms should be incorporated in that law.²¹ ASIC submitted that as default charges are in all cases contingent charges they

16 Australian Securities and Investments Commission, *Submission 12*, p. 2.

17 Australian Securities and Investments Commission, *Submission 12*, p. 4.

18 Australian Securities and Investments Commission, *Submission 12*, p. 7.

19 Mr Gerard Brody, Director, Policy and Campaigns, consumer Action Law Centre, *Committee Hansard*, 12 June 2008, p. 15.

20 Mr Ben Slade, Member, Consumer Law Committee, Law Council of Australia, *Committee Hansard*, 12 June 2008, p. 27.

21 Productivity Commission 2008, *Review of Australia's Consumer Policy Framework*, Final Report, Canberra, p. 72.

would appear to fall within the scope of the Productivity Commission's recommendations.²²

Council of Australian Governments

1.28 The Council of Australian Governments (COAG) has agreed in-principle that the Commonwealth should assume responsibility for regulating mortgage credit and advice, margin lending and lending by non-deposit taking institutions. COAG has also asked its Business Regulation and Competition Working Group to identify any other areas of financial services activities that best sit within the Commonwealth's regulatory responsibility.²³ More recently, the report of a COAG meeting held on 3 July 2008 indicates that the COAG has agreed that the Federal Government should take over all forms of consumer credit.²⁴

1.29 The ABA claimed that the Ministerial Council on Consumer Affairs is:

... pursuing fringe credit provider legislation that, despite its original objective of regulating fringe credit providers, is drafted to apply to all credit providers including banks and other mainstream providers and to capture all credit fees and charges.

Like the Bill, the fringe credit provider draft bill proposed to limit default fees and charges to the reasonable estimate of the credit provider's loss arising from the default. However the draft MCCA bill is proposed to go further. With the price control genie out of the bottle, the notion is contagious so that there is the proposal to introduce a general test of 'unfairness' to limit the amounts of other credit fees and charges.²⁵

Regulation in the United Kingdom

1.30 In the United Kingdom, the Office of Fair Trading (OFT) has a broad role in relation to conducting market studies and ensuring compliance with the Unfair Terms in Consumer Contracts Regulations. These regulations prohibit unfair contract terms generally, rather than specifically prohibiting penalty fees, but default fees are covered. In April 2006, the OFT announced that its enforcement policy would be to assume that any default fee on credit card accounts above 12 GBP (\$A27) was likely to be unfair. The OFT has indicated that similar principles could apply in relation to default fees on other ADI accounts.²⁶

22 Australian Securities and Investments Commission, *Submission 12*, p. 7.

23 Australian Securities and Investments Commission, *Submission 12*, pp 7-8.

24 'A seamless national economy', Council of Australian Governments' Meeting, 3 July 2008, <http://www.coag.gov.au/meetings/030708/index.htm#economy> (accessed 9 July 2008).

25 Australian Bankers' Association, *Submission 17*, p. 3.

26 Australian Securities and Investments Commission, *Submission 12*, p. 8.

- 1.31 A recently-concluded test case in the UK High Court relating to the application of the Unfair Terms in Consumer Contracts Regulations in respect of unauthorised overdraft charges found that fees where no previous agreement had been made between customer and institution for an overdraft, yet an overdraft was provided to the customer, were fees for service. The common law of penalties therefore does not apply in those circumstances.²⁷
- 1.32 The possible implications of this decision for default charges and for the bill are discussed in Chapter 2.

27 Mr Ben Slade, Member, Consumer Law Committee, Law Council of Australia, *Committee Hansard*, 12 June 2008, p. 23.