

9 November 2018

Committee Secretary
Senate Standing Committees on Economics
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By email: economics.sen@aph.gov.au

Dear Secretary

Inquiry into credit and financial services targeted at Australians at risk of financial hardship

We welcome the current inquiry into credit and financial services that target vulnerable Australians. We are presently in the early stages of a major empirical investigation of harmful financial products. This project will investigate, document and analyse the impact of several potentially harmful financial products, such as payday loans, consumer leases, funeral insurance, budgeting services and 'buy now, pay later' schemes, with a focus on the impact of these products on disadvantaged and marginalised consumers.

Information about this project is available at

<https://law.unimelb.edu.au/centres/cclsr/research/major-research-projects/harmful-financial-products-project>. While it is too early to provide data from this project, we wish to draw attention to our earlier research in this area, which we have published with a number of colleagues at Melbourne Law School.

1. Outline of this submission

Our submission addresses the first and second terms of reference, with particular regard to the impact and current regulation of payday loans, consumer leases and credit repair services. These are discussed below, in sections 2, 3 and 4, respectively. In each section, we provide the details of our relevant publications, including a brief summary of each article, as well as a link to the full text via the Social Science Research Network (SSRN).

Our submission also addresses the third term of reference, concerning 'the present capacity and capability of the financial counselling sector to provide financial counselling services to financially stressed and distressed members of the community'. We see extremely high value in the work of financial counsellors, borne out by our empirical studies of Australian financial hardship schemes and the personal insolvency system. We discuss our findings regarding the role, value and present capacity of the financial counselling sector in section 5, below.

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2. Payday loans

To date, we have published two studies of payday lending in Australia:

- Paul Ali, Cosima McRae and Ian Ramsay, 'The Politics of Payday Lending Regulation in Australia', *Monash University Law Review*, 2013, Vol. 39, No. 2, pp. 412-451 (available at <https://ssrn.com/abstract=2402514>)

The regulation of payday lending in Australia has recently been reformed. The reforms followed a highly charged and polarised debate between the conflicting interests of consumer and welfare advocates — who argued for increased protection for payday loan borrowers — and the payday loan industry. The debate followed research findings of the adverse consequences of payday lending for low income and financially vulnerable borrowers. We analyse the political dynamic that unfolded and show how the protections proposed to be afforded to payday loan borrowers were reduced in several key respects. Our research highlights several concerns. First, key changes to the original proposals do not take account of the recommendations of consumer and welfare advocates and are more consistent with the views of the payday loan industry. Second, the increased complexity of the final form of the regulation of payday lending creates potential for regulatory avoidance and poses problems for enforcement. Third, policies to reduce reliance on payday loans have not been implemented. The result is new regulation of payday loans that may not achieve the key aim of protecting the most vulnerable borrowers from the harm that can result from these loans.

- Paul Ali, Cosima McRae and Ian Ramsay, 'Payday Lending Regulation and Borrower Vulnerability in the United Kingdom and Australia', *Journal of Business Law*, 2015, Issue No. 3, pp. 223-255 (available at <https://ssrn.com/abstract=2597393>)

The current debate in the United Kingdom about the appropriate regulatory response to payday lending involves the key issue of borrower vulnerability. There is compelling evidence in the UK that many payday lenders are deliberately making loans to financially vulnerable borrowers who cannot afford those loans. This article examines the evidence for borrower vulnerability in the UK and Australia and the regulatory responses in those two countries to payday lending. Payday loans in Australia are the same as those that are available in the UK and the concerns that are now being raised in the UK about payday lending formed the basis for recent regulatory intervention in Australia. This article also contains an empirical study of the location of payday lending businesses in Australia. We investigate whether payday lenders are more likely to locate their business operations in areas where larger groups of financially vulnerable people are living.

3. Consumer leases

We have published two studies of consumer leases, including one considering the particular impact of consumer leases on indigenous consumers in remote communities:

- Paul Ali, Cosima McRae, Ian Ramsay and Tiong Saw, 'Consumer Leases and Consumer Protection: Regulatory Arbitrage and Consumer Harm', *Australian Business Law Review*, 2013, Vol. 41, No. 5, pp. 240-269 (available at <https://ssrn.com/abstract=2402518>)

Consumer leases are regulated in Australia separately from credit contracts. This has created opportunities for regulatory arbitrage and has resulted in significant harm to consumers. Recent reforms, which commenced on 1 March 2013, have addressed this problem by applying to consumer leases many of the statutory protections available to consumers under credit contracts. However, the distinction between consumer leases and credit contracts has been retained. We argue in this article that the distinction is artificial and should be abandoned. We also examine how the uneven regulation of consumer leases and credit contracts has harmed consumers and we assess the recent reforms to the regulation of consumer leases. Finally, we investigate the practice of consumer leasing in Australia by reference to our survey of the consumer leasing industry, the cost of consumer leases, and selected "real life" case studies.

- Paul Ali, Steve Kourabas, Cosima McRae and Ian Ramsay, 'Consumer Leases and Indigenous Consumers', *Australian Indigenous Law Review*, 2017, Vol. 20, No. 1, pp. 154-177 (available at <https://ssrn.com/abstract=3089495>)

Consumer leases offer low-income consumers the option to hire household items that they do not have the money to purchase upfront. They are marketed by consumer lease providers as a cheap way to purchase important household items. However, recent studies illustrate that the price ultimately paid to hire goods under a consumer lease contract will generally exceed the retail value of the goods hired and that it is the most expensive form of finance available. Despite this, consumers are often persuaded to enter into consumer lease contracts as a result of predatory practices engaged in by providers. These predatory practices are most effective with low-income consumers who may be experiencing financial difficulties and who live in remote areas that make it difficult to shop for alternative goods or seek financial and legal advice.

The problems associated with consumer leases are particularly prevalent in remote and rural Indigenous communities where issues such as geographical isolation, financial hardship, and cultural practices make them vulnerable targets for providers. This article explores in detail the ongoing problems faced by Indigenous

consumers when entering consumer leases. After setting out some of the key aspects of consumer leases and the general problems associated with their use, the article explores the operation of consumer leases in Indigenous communities and enforcement actions relating to Indigenous consumers that have been undertaken by the Australian Securities and Investments Commission. The article also reports the results of interviews conducted by the authors that indicate that, despite regulatory reforms and enforcement actions, Indigenous communities continue to be vulnerable consumers. This vulnerability has led many Indigenous consumers to pay exorbitant amounts for household items that could be purchased more cheaply or through less costly credit products. As a result, Indigenous consumers entering into consumer leases often find they are unable to afford to pay for other essential items, which in turn forces them into even greater financial distress. The article concludes with observations regarding the potential negative effects of consumer leases in Indigenous communities and reforms that may address these problems.

4. Credit repair services

We have also published an article focussing specifically on credit repair services. To our knowledge, this is the only academic study of credit repair to have been published in Australia to date.

- Paul Ali, Lucinda O'Brien and Ian Ramsay, 'A Quick Fix? Credit Repair in Australia', *Australian Business Law Review*, 2015, Vol. 43, No. 3, pp. 179-205 (available at <https://ssrn.com/abstract=2616619>)

A poor credit history can preclude an individual from obtaining loans, credit cards and even access to basic utilities. Credit repair companies claim to assist people in this situation, by deleting adverse information from their credit histories. As financial hardship becomes more widespread, increasing numbers of Australians are turning to credit repair. Yet critics maintain that these companies charge high fees for services that are available for free through ombudsman schemes. In this way, they often increase their clients' financial hardship, while subverting the objectives of the ombudsman schemes. This article examines the Australian credit repair industry, including the regulatory context and the industry's attempts at self-regulation. It discusses several case studies from a Melbourne community legal centre, and describes the regulation of credit repair in the United States and the United Kingdom. It considers various law reform options that would address the problems posed by credit repair in Australia.

5. Financial counselling services

Our recently completed studies of financial hardship and personal insolvency have explored the nature of financial counsellors' work with financially distressed Australians. These studies have shown that financial counsellors perform a vital role. At the same time, they show that financial counsellors are currently unable to meet the demand for their services.

(a) Financial hardship

We have recently completed a research project, funded by an Australian Research Council Discovery Grant (DP140101031), entitled *The Legal and Social Dimensions of Financial Hardship in Australia: Implications for Legal, Regulatory and Policy Frameworks*. Our project involved an analysis of the legal protections available to Australians suffering financial hardship. It also entailed an empirical study of how these protections operate in practice. Between 2014 and 2018, we conducted surveys of, and focus group interviews with, financial counsellors and other professionals providing advice and advocacy services to consumers in financial hardship. We also carried out a survey of 1,100 Australians who recently found themselves unable to pay one or more debts when they fell due.

These studies yielded strong empirical evidence that financial counsellors play an important role in assisting low income consumers to exercise their rights under Australia's legal hardship protections. These protections allow consumers in financial hardship to negotiate repayment arrangements with creditors, with the aim of enabling them to avoid enforcement action, energy disconnection, and in the most serious cases, bankruptcy. Consumers who negotiate directly with their creditors often obtain less favourable outcomes than those who are represented by a financial counsellor. Many consumers are unaware of their right to seek hardship assistance. Even when they do contact their creditors to discuss their financial difficulties, they are frequently pressured into accepting inflexible and unaffordable repayment arrangements. A large part of financial counsellors' work involves renegotiating repayment arrangements after they have broken down, either because the consumer was unable to make scheduled repayments, or because the repayments have left the consumer with insufficient income to cover food, heating, medical care and other essentials.

The financial counselling sector needs more funding, so that more consumers in financial hardship — particularly those on low incomes — can receive timely, impartial assistance to resolve their existing debt problems and to avoid becoming further indebted. At present, many consumers — particularly Indigenous Australians and recent migrants and refugees from non-English-speaking backgrounds — are unaware that financial counselling services are available free of charge. Yet demand for these services continues to exceed supply, with consumers waiting weeks to secure face-to-face appointments with financial counsellors. Additional funding is also needed to allow financial counsellors to be integrated into community organisations providing mental health, family violence and other support services. Consumers presenting to these services are often dealing with debt problems.

These findings are discussed in detail in the following publications:

- Evgenia Bourova, Ian Ramsay and Paul Ali, 'The Experience of Financial Hardship in Australia: Causes, Impacts and Coping Strategies', *Journal of Consumer Policy*, online edition, 2018 (available at <https://ssrn.com/abstract=3275131>)

- Paul Ali, Evgenia Bourova and Ian Ramsay, 'The Role of the Legal Hardship Protections in Coping with Debt Problems: Insights from a Survey of Consumers', 2016, *Competition and Consumer Law Journal*, Vol. 24, No. 2, pp. 77-100 (available at <https://ssrn.com/abstract=2875555>)

(b) Personal insolvency

We have also recently completed a major empirical study of Australia's personal insolvency system, funded by an ARC Linkage Grant (LP130101022: *Evaluating Australian Personal Insolvency Laws in the Context of Changing Demographics and Increasing Financial Stress*). In the course of this project, we conducted an evaluation of on-site financial counselling services offered to self-represented debtors in the Bankruptcy List of the Federal Circuit Court, as part of a pilot project. This evaluation involved a formal partnership with the Federal Circuit Court and the Federal Court of Australia. It entailed a written survey of self-represented debtors, completed at the Court; an online survey of legal practitioners representing creditors in the Bankruptcy List; focus groups with financial counsellors and three Deputy Registrars of the Court; and the analysis of data and case notes compiled by Court staff.

This study found that the work of financial counsellors provided significant benefits to self-represented debtors. The financial counsellors at the Court helped some debtors to establish solvency, when they may otherwise have been made bankrupt. They also helped other debtors to identify bankruptcy as a positive step for them, in their circumstances, reducing the emotional distress that would otherwise have attended the process. Irrespective of the outcome, access to financial counselling enabled debtors to understand the nature of the bankruptcy proceedings and to participate meaningfully in the Court hearing. In this way, the financial counsellors significantly increased both the procedural fairness and the efficiency of hearings in the Bankruptcy List.

This study identified the need for greater support for self-represented litigants in the bankruptcy system, including greater access to on-site financial counselling services. It informed the Federal Circuit Court's decision to continue the project beyond the pilot stage and to implement on-site financial counselling in other courts around Australia.

The results of this study are reported in the following article:

- Paul Ali, Lucinda O'Brien and Ian Ramsay, 'Financial Counselling and the Self-Represented Debtor in the Federal Circuit Court Bankruptcy List: An Analysis of a Recent Pilot Service', *Insolvency Law Journal*, 2015, Vol. 23, No. 4, 161-180 (available at <https://ssrn.com/abstract=2732824>)

We hope that our research findings will be of assistance to the committee. Should you wish to discuss any aspect of this submission, or our research more generally, please do not hesitate to contact Lucinda O'Brien, Research Fellow, via email at

Yours sincerely

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