Australian Finance Conference Level 7, 34 Hunter Street, Sydney, 2000. GPO Box 1595, Sydney 2001
ABN 13 000 493 907 Telephone: (02) 9231-5877 Facsimile: (02) 9232-5647 e-mail: afc@afc.asn.au

23 October 2011

Mr Tim Bryant
Committee Secretary
Parliamentary Joint Committee on Corporations and Financial Services
PO Box 6100
Parliament House
CANBERRA ACT 2600 via: corporations.joint@aph.gov.au

**INQUIRY INTO CONSUMER CREDIT AND CORPORATIONS LEGISLATION AMENDMENT (ENHANCEMENTS) BILL 2011**

Further to, and as noted in, our submission of 14 October, the Australian Finance Conference (AFC) would appreciate the Committee's consideration of the following more detailed analysis of key concerns identified for our Members in relation to the Consumer Credit & Corporations Legislation Amendment (Enhancements) Bill 2011 [the Bill] is attached.

We reiterate our general concerns in relation to policy and commencement timeframes expressed in our submission of 14 October 2011.

We thank the Committee for its consideration of the issues we have raised and would be pleased to assist with additional information, as required.

Yours truly

RON HARDAKER
Executive Director

Attachments:
1. Enhancements Bill: AFC Key Issues – Detailed Comments
2. Letter to NSW Consumer Affairs Minister – Interest Rate Caps)

# SCHEDULE 1 – ENHANCEMENTS

## Part 1 - HARDSHIP VARIATIONS

**AFC GENERAL COMMENTS**

The AFC is concerned that the proposed amendments to the hardship provisions that impact both the credit contract and consumer lease products are beyond the policy intent of the Government, fail to provide an appropriate off-set to compliance rigidity and operating risk for the financier to balance the greater accessibility and flexibility proposed for the consumer in financial hardship and may cause consumer detriment (eg through loss of value of secured assets to off-set outstanding debt) by imposing delay on enforcement proceedings.

The Phase 1 NCC Law reforms (including the changes introduced to the hardship provisions as part of the transfer of consumer credit regulation from the States to the Commonwealth and enactment of the NCC, together with the licensing obligations and compulsory membership of an ASIC-approved EDR Scheme) and the unfair contract terms provisions under the ASIC Act, are relevant to considerations of whether further enhancement of the hardship provisions is required.

We acknowledge that the Government's focus with these proposed reforms is to protect the vulnerable consumer or consumer in financial distress. However, given the majority of the NCC Law changes effectively commenced from 1 July 2010 (a little over 12 months ago), we submit that further amendment of the hardship provisions may be premature.

The **AFC recommends** that the Phase 1 reforms be given a chance to bed-down and following a reasonable time to take effect that empirical research should thereafter be undertaken to determine whether these reforms have achieved the underlying policy of protection of the vulnerable consumer and to identify areas where further reform may be required.

**SPECIFIC COMMENTS FOR CREDIT CONTRACT AMENDMENTS[1]**

**ISSUE 1: Types of hardship variations that can be requested & ISSUE 2: Monetary Threshold**

*Objective:*

We understand from the draft RIS (October 2010) that preceded the development of these reform proposals and the final RIS released by the Office of Best Practice (on 9 September 2011) that the objective of government action with Issue 1 is to "*support sufficient flexibility in the hardship variation provisions to enable the most mutually beneficial outcomes for lenders and consumers*" and for Issue 2: "*to facilitate consumers' access to mechanisms to request reasonable variations to their contracts when they are experiencing difficulty meeting their obligations*". Treasury sees that the key element of the reform on these Issues will be '*[making] it easier for debtors to apply for hardship variations by broadening the circumstances in which they can be requested*'.

*Proposed changes:*

As we understand there are two key areas to the proposed changes in Issue 1:

a. Potential change in form by which customer commences a hardship variation (ie. apply vs. notify).

[1] While these comments deal with the provisions for NCC-regulated credit contracts – they are equally applicable to the equivalent provisions for NCC-regulated consumer leases. This point is noted later in the part of this Submission relating to consumer leases also.

b. Broadening of circumstances in which hardship can be requested – to remove:
   (i) Need for customer to have a reasonable reason (ie illness or unemployment) that caused the financial hardship;
   (ii) Need for the customer to specify the contract variations that he/she believes would, if made, assist them continuing to meet their obligations while financially stressed;
   (iii) Need for the customer to have a reasonable expectation of being able to meet those obligations (as varied); and
   (iv) the threshold (currently $500,000).

*AFC Comments:*
Subject to our general comments, as a matter of policy, the AFC supports the Government's aims in relation to this reform consideration. As a matter of practice, AFC members aim to assist their customers to repay their credit obligations regardless of the amount borrowed and will endeavour to take into account customer's particular circumstances at any given point in time (eg. in the event of being made unemployed) to consider contractual obligations and possible variations to balance the customer and their situations.

However, the policy reforms need to be viewed in the context of their proposed implementation. Currently, the process of hardship variation under the NCC is prescriptive (eg. strict time-frames for response) and non-compliance raises risk of criminal/strict liability offences.

The proposed reforms are designed to facilitate flexibility by the consumer with the process of soliciting variation on the basis of hardship. Again, the AFC supports this. However, for it to be a mutually beneficial outcome in line with the Government's objective, similar flexibility needs to be adopted for the compliance obligations of the lender. In particular, **AFC recommends** that:

- strict timeframes should be replaced with concepts like "within a reasonable time;" and
- offence provisions should be removed.

This would have the benefit of allowing lenders to minimise regulatory risk while working with customers on a specific or targeted basis with the primary aim of assisting the customer to overcome their short-term financial difficulty while continuing to meet their contractual obligations.

a. Form – apply vs. notify

   The concept of a customer applying to a lender for a hardship variation is well known and understood. We therefore query the need for change from the current "application by a customer" approach – to what is a broader concept encompassed by the term "notify". We note that the change in method of request for variation appears to be beyond the parameters of what the Government was considering with this Reform in Issues 1 and 2 which were focused on broadening the types of hardship circumstances that a variation could be considered without restriction by a monetary threshold.

   We note the Government's objective of enabling the most mutually beneficial outcomes for lenders and customers together with the specificity of procedural requirements contained in the hardship provisions (eg. 21 days response after receipt of notification). We also note the risk non-compliance raises for lenders (eg. strict liability / criminal offences) and proposed restriction on enforcement action (under proposed NCC s 89A).

   **AFC Recommendation**: We recommend that a clear mechanism for commencement of these timeframes is a necessary and beneficial requirement for both lenders and customers. We therefore submit that the current term "apply" be retained or the term "notify" be qualified by "in writing."

We also note that the proposed substitution of ss. 72(1)(2) with the new s. 72(1) and consequent re-wording of s. 72(3) has the outcome that a customer is provided a means of alerting a lender of financial difficulty without any requirement to indicate an intention to also solicit variation of the contract to assist overcome that difficulty. Yet, within 21 days, the lender will be required to give written notice of whether it agrees to change the contract. Without a customer request triggering the need for change, we have difficulty understanding how this will work in practice. The **AFC recommends** that this gap should be addressed.

We also note the compliance difficulty the wording of s. 72 currently raises for lenders and the ASIC response (October 2010) to assist. In short, to address concerns expressed by lenders in relation to the timeframe for decision where insufficient information has been provided by the borrower, ASIC clarified its position in Information Sheet 105: Dealing with Consumers & Credit. In ASIC's view the 21 day period commences only after the borrower makes an application with sufficient information to allow the credit provider to make a final decision. Where insufficient, the credit provider will need to identify what further information is required and advise the borrower as soon as practicable. Until that information is provided, ASIC will not regard an application as having been made and the 21 days will not have commenced.

We submit that part of the reform process should be to clarify that NCC provisions so that the intention and operation of the law is clear and the need for ASIC Guidance removed.

b. Broadening of Circumstances

(1) *No reference to "for a reasonable cause" or "reasonable expectation of debtor meeting obligations as varied"*

We note the proposed omission of these concepts from the current provisions. We remain of the view that these elements are essential pre-cursors to a debtor approaching a financier to solicit variation of the contract on the basis of hardship and, in the interests of certainty, particularly for the debtor/lessee, the **AFC recommends** the re-inclusion of these words in redrafted s. 72.

Without their inclusion and in the context of the proposed rewording of the hardship process as contained in the Bill, it appears operationally difficult for a financier to decline an application should a customer have no reasonable expectation of meeting their obligations as varied, yet it would be to the customer detriment to agree to such a request for variation.

Should the Committee accept the AFC recommendation to retain the reasonable cause concept in s. 72, we also submit that the current wording of s. 72 should be used in preference to a more generic reference to "for a reasonable cause". The need for a change to the broader generic reference was considered by the UCCC Post Implementation Review Committee in relation to the UCCC equivalent of s. 72(1); namely UCCC s 66(1) as evidenced in the following extract:

> *Another respondent suggested that the current wording of section 66(1) may limit the reasons for which an application may be made on the grounds of hardship and expressed concern as to how the threshold test might be satisfied. For example, the respondent suggested that the current wording of the section may prevent an*

> *application which arises from circumstances relating to a child or a spouse of the debtor……*
>
> *While the project team notes the arguments about the grounds for applications under section 66(1), the words 'other reasonable cause' would appear to provide sufficient breadth to this section.[74]*
>
> [74] Section 66(1) of the Code states ' A debtor who is unable, because of illness, unemployment or other reasonable cause, to meet the debtor's obligations under a credit contract and who reasonably expects to be able to discharge the debtor's obligations if the terms of the credit contract were changed in a manner set out in subsection (2) may apply to the credit provider for a change.
>
> [UCCC Post Implementation Report December 1999 at pages 75 & 76]

In line with the view expressed above, the **AFC recommends** that the current wording of NCC s. 72(1) should be retained in preference to a generic terms as it is sufficiently wide to allow a customer to solicit variation in a broad range of circumstances (including circumstances of third parties associated with the debtor that impact of the debtor's financial position). The current specification in s. 72 of concepts of illness and unemployment together with the generic reference to other reasonable cause is useful to assist a consumer to understand what types of situations may fall within the general concept and should be maintained.

(2) *Omission of types of variation customer may request*

We note the proposed omission of NCC s. 72(2) which details a range of variations that a customer may request. We also note comments in the RIS that acknowledges the general provision (NCC s. 71) that might be used by lenders and customers to reach agreement for types of variation other than those specified in NCC s. 72(2). We therefore query the need for the omission of NCC s. 72(2) and submit for the reasons given earlier in relation to the need for certainty of application of these provisions given the regulatory risk for breach that it is necessary that NCC s. 72(2) in its current or a similar form be maintained. This provides clear parameters of the hardship process while still acknowledging that the lender and their customer are able through the process to negotiate variation beyond that contemplated by NCC s. 72(2) under the general variation provision of NCC s. 71.

Also, as noted earlier, to give the proposed re-wording of s. 72(3) effect, we think it essential for a customer to include in the written notice of inability to meet their obligations the contractual variation that they are soliciting. This then provides a starting point from which the negotiations with the lender can proceed.

(3) *Removal of Threshold*

As noted in the AFC response to the Green Paper and responses to Treasury on Exposure drafts of the Bill, in practice the current threshold for the hardship provisions is largely irrelevant to AFC members. Their aim is to assist their customers to repay their credit obligations regardless of the amount borrowed. However, as noted above, while the potential regulatory risk for breach remains, the threshold assists provide parameters of regulated-compliance and consequently operating risk. Further, as noted in Treasury's RIS (September 2011) - *This threshold is also relevant to the right to request a postponement of enforcement proceedings*. Removal of the threshold has compliance and operational implications for lenders beyond hardship variation considerations.

We again note the range of changes to the hardship provisions that only took effect with the NCC's commencement. In particular, as noted by Treasury,..... *as part of Phase 1 of the national credit reforms, the threshold for contracts entered into after 1 July 2010 was increased to $500,000 (or higher as specified in regulations). This was a significant increase* *and simplification of the threshold which applied to contracts entered into before 1 July 2010 [Treasury's RIS October 2010].*

Before further amendment to the monetary threshold for hardship and stay of enforcement provisions is finalised and implemented, the **AFC recommends** that the impact of the significantly increased threshold on transactions since 1 July 2010 be assessed to determine whether this has resolved concerns about limitation of access by customers in the pre-1 July 2010 environment. In the context of best practice regulation principles, this assessment should take into account the commercial self-regulation practices of lenders, including AFC members, which see consideration of hardship variation requests for monetary amounts in excess of the threshold.

Should Treasury remain committed to reform of the monetary limit, we submit an off-setting amendment should also be omission of the offence provisions relating to the processes of hardship and postponement.

**ISSUE 3: Enhancements to the postponement of enforcement provisions**

*Objective:*

The objective of government action is to "*provide balanced opportunities for consumers to rectify defaults and lenders to enforce their right to collect repayments while minimising unnecessary enforcement action*" [*Treasury draft RIS (October 2010)*] though we note this objective appears to have been omitted from the RIS as presented and considered by the Office of Best Practice. Treasury sees that the key element of the reform on Issue 3 will be that "*credit providers will be required to finalise an outstanding application for a hardship variation before being able to commence enforcement proceedings*".

*Proposed changes:*

As we understand key areas proposed to change in Issue 3 are:

a. That lenders will be prevented from commencing (or continuing) enforcement proceedings while a hardship variation is being considered;
b. The monetary threshold (currently $500,000) for stay of enforcement proceedings is to be removed.

*AFC Comments:*

In theory, the AFC supports the Government's aims in relation to this reform consideration. However, in practice, is should be acknowledged that enforcement proceedings are generally the result of ongoing contact between the credit provider and the customer which may have included many contractual variations to deal with hardship and other situations. Enforcement is traditionally taken after these agreements have not been honoured by the customer rather than a first response to a customer being unable to meet their repayment obligations for whatever reason.

The 1 July 2010 NCCL Phase 1 amendments to contracts, default notices and hardship decline letters mean customers are provided with information on EDR numerous times. The licensing requirements under the NCCL mean that lenders of NCC-regulated credit/consumer leases have to be a member of an ASIC-approved EDR scheme. Information from these EDR schemes indicates that current processes appear to be working. ASIC has significant powers to address non-compliance by lenders involved with NCC-regulated products that are not EDR members.

In addition, the current postponement provisions and financiers' practices of trying to proactively manage customers who are in difficulty mean there is ample opportunity for customers to seek assistance before proceedings are commenced.

The AFC therefore opposes the introduction of NCC s. 89A. We are advised by our Members that it would be operationally extremely difficult to implement a process to comply with its requirements. They also submit that the customer may be disadvantaged through the process; an outcome that should be avoided. We also fail to understand where the current law has failed to provide adequate consumer protection since commencement of the NCCL Phase 1 compliance obligations that requires the proposed regulatory response.

### TRANSITIONAL ISSUES – Schedule 6 Application Provisions - Hardship Amendments & Stay of Enforcement

We note the intention is for the new hardship provisions to be available for credit contracts/consumer leases entered into on or after commencement of the relevant amended provisions (eg s. 72). However, the outcome would appear to result in a financier having to follow two different compliance frameworks dictated by date of entry into the contract. While practically this might be avoided effectively by the financier choosing to comply with the requirements under the amended provisions, as a matter of law they would potentially face risk of breach by doing so. The AFC recommends therefore that a further provision be included to allow compliance with the new provisions to be regarded as meeting compliance for the purposes of contracts in existence pre-Bill No. 2 commencement. The transitional provision approach with the UCCC and contracts subject to the pre-UCC Credit Acts might be considered in this regard.

### HARDSHIP/ENFORCEMENT “ENHANCEMENTS” – MARKET BEHAVIOURAL RESPONSES

AFC supports the Government’s policy intention of assisting vulnerable consumers and those suffering financial distress. We would assert that all mainstream lenders, including our Members, via their processes and procedures already have in place mechanisms to constructively deal with the range of circumstances implicit in the proposed changes. As has been previously noted, AFC is concerned that the “enhancements” have been put forward without any consideration of whether there was a demonstrable need in the light of the new NCC regime including responsible lending, and compliance and enforcement activity of the regulator (ASIC) and the quasi-regulators (EDRs). Moreover, AFC is concerned that such “enhancements” conceived for vulnerable consumers when available in the wider market, may lead to a re-jigging of the starting point of ordinary negotiations between borrowers and lenders, thereby adding delays and costs to be borne by the entire market.

Obviously such added system costs are conjectural at this stage. Depending on its final form, ‘notification of’ rather than ‘application for’ hardship, might only add a small number of days (compared to present) to the process, but each added day is an added cost, and if repeated a number of times during the course of a contract, and if interspersed with Ombudsman applications, and if taken up by a greater number of borrowers, the overall cost increase could be significant. Our point is that we won’t know until broader market behavior responds to any finalized regime. Likewise we won’t know until then whether the position of the credit vulnerable have been enhanced.

## DOOR-TO–DOOR SELLING PROHIBITION

We note that the broader prohibition on the unsolicited canvassing of credit at a consumer’s home as part of the sale of goods or services included in an earlier version of the Bill, has been removed and is the subject of further consultation; given that the Government has only recently revamped the regulation of direct or door-to-door selling under its Australian Consumer Law and that the NCC already prohibits credit hawking, AFC commends the Government on this decision. The AFC looks forward to providing responses to the Discussion Paper on this issue with a view to ensuring a regulatory response that appropriately identifies and addresses market failure and consumer risk in this area.

## SCHEDULE 1 – Part 3 - REPRESENTATIONS ABOUT ELIGIBILITY TO ENTER CREDIT CONTRACTS, CONSUMER LEASES ETC. WITHOUT ASSESSING UNSUITABILITY

*AFC Comments*

The AFC believes that the proposed amendments to the Chapter 3 NCA responsible lending provisions to address concerns with representations are beyond the policy intent of the Government and introduce additional compliance obligations and regulatory risk in the credit assessment process which are not justified. We further submit that existing regulation (including NCC s. 154 – broad prohibition on a person making false and misleading representations to induce a person to enter into a credit contract or consumer lease) are adequate to address consumer risk concerns.

## SCHEDULE 2 – REVERSE MORTGAGES

*AFC Comments*

We acknowledge the significant consultation on the Reverse Mortgage aspect of the NCCL Phase 2 reforms through the Treasury Working Group that preceded the development of Schedule 2 of the Bill. We understand that the proposed amendments reflect the negotiated outcomes of that consultation and have no specific concerns with the provisions in this Schedule.

## SCHEDULE 3 SMALL AMOUNT CREDIT CONTRACTS & SCHEDULE 4 CAPS ON COSTS etc FOR CREDIT CONTRACTS

*AFC Comments*

**POLICY VS REGULATORY RESPONSE**

By way of context, consultation on short term, small amount, high cost lending commenced and was addressed, at least in part, through Phase One of the NCCL reforms (ie from 1 July 2010). The reforms included a number of measures to improve consumer protection and deter predatory lending practices; namely: licensing (including mandatory EDR scheme membership); responsible lending obligations; enactment of the NCC to replicate and enhance the UCCC including by tightening exemptions (eg. for low cost short term credit); mandating further requirements on credit providers in information statements and notices to disclose to consumers their rights to apply for hardship variations and stays of enforcement, access to EDR mechanisms, and the existence of financial counsellors and legal aid; and power for the court to re-open unjust contracts and review unconscionable interest and other charges. Further, ASIC has been appointed as the national regulator and been given extensive powers including the ability to ban people from the industry and impose a range of penalties in enforcing the regime. ASIC also has standing to make an application to the Court to re-open an unjust transaction or challenge unconscionable interest or certain charges where it is in the public interest.

Also, running parallel with these reforms was the enactment and 1 July 2010 commencement of national unfair contract terms reforms. We understand that while these provisions do not apply to upfront fees and interest rates, they do provide some further safeguards in the area of high cost credit as far as they cover contingent fees (eg default fees). The Commonwealth Government has also agreed to, and is in the process of, developing legislation as part of its privacy reform initiative to move to a more comprehensive credit reporting regime on the basis that increasing the range of information available through the credit referencing process may encourage improved lending practices and make it easier for some people on low incomes to obtain finance. We understand the Government remains committed to finalising and commencing these provisions and the balance of the reformed privacy laws at the earliest opportunity.

However, the Commonwealth Government also recognised that in order to address predatory lending concerns some States and Territories had over the years unilaterally put in place mechanisms to regulate consumer credit in addition to the UCCC, including the imposition of interest rate caps. There is variation both in the approach adopted by those that have them and the fact that not all have enacted a cap at this stage. As a consequence, the Government committed to an examination of the approaches to interest rate caps during Phase Two of NCCL reforms and has agreed that those jurisdictions with caps can retain them, pending the outcome of the review. The basis of that examination, as we understood it was, that (1) there is divergence in the views of stakeholders between whether the measures put in place in Phase One outlined above provide sufficient consumer protections to prevent indebtedness as a result of using small amount, short term, high cost loans and (2) there is concern that the lack of availability of appropriate 'mainstream' alternatives to short term, small amount, high cost loans though it was recognised that a reduction in their available may exacerbate this.

It is on this basis that we have participated in consultation on this area of reform. We therefore understood that, in line with Government's commitment to best practice regulatory reform principles and red-tape reduction that any reform proposals would be contingent on an identified market failure or consumer risk and this consideration would take into account the significant and broad-ranging measures adopted (as outlined above) as part of Phase One. We have yet to see any detail of analysis conducted by the Government on whether those reform proposals have achieved their underlying policy objectives and consequently whether there is a market failure or consumer risk in the short term, small amount, high cost lending market sector that requires a regulatory response. Nor have we seen any evidence that the caps, where enacted, have been enforced with any demonstrable consumer benefit.

Without these analyses it is consequently extremely difficult for the AFC to understand, let alone comment, on a proposal by the Government to introduce what are effectively price control measures on providers of short term, small amount, high cost credit that will see that segment of the market vacated on the basis of it no longer being commercially viable and without any real alternate yet proposed by the Government for current consumers of that product. For the Commonwealth to make national some States' (variously defined) APR caps because of COAG dynamics, does little service to the policy objectives espoused.

As has been the view expressed by the AFC over a number of years including the pre-NCC management of consumer credit regulation by the States through to recent consultation following transfer to the Commonwealth, the real policy issue with short term, small amount, high cost credit is one of social and income inequality. This is because some consumers are forced to borrow to meet pressing basic needs, not because the poorest consumers pay more for credit or face the prospect of over-commitment through the use of credit as often alleged. Consumers with limited income and resources have no choice other than to borrow to meet basic needs. No amount of regulatory responses to credit provision will change this situation. The unintended outcome will be to make credit more difficult or expensive to get, thereby resulting in the exclusion from the credit market of low income earners or those with poor credit ratings. As a result, these consumers may resort to other sources of credit, including unregulated sources. In effect, the outcome of the regulation will be to harm rather than protect consumers and to cause a market failure. We submit that this is not intended by the Government and recommend that COAG agree to extend the timetable for consideration of the short term, small amount high cost lending issue to enable further consultation on this issue in a timeframe that enables real consultation to occur with a view to ensuring the market continues to function in a way that appropriately protects consumers.

**INTEREST RATES CAPS – APPROPRIATE POLICY TOOL?**

As has been noted in a variety of commentaries, imposing a ceiling on the price of credit is one of the oldest policy tools available, along with prohibiting credit provision altogether. However, as was recognised by the Victorian Government in the report published on conclusion of its Small Amount Lending Inquiry 2008[2]:

> *Given inconsistent evidence that a ceiling significantly ameliorates the high cost of credit and, the difficulty in determining the appropriate ceiling, a more nuanced policy approach combining more established regulatory tools is preferred.*

As a consequence they recommended

> "*Recommendation 16 - that regulatory options, other than an inclusive fees and charges cap, be trialled including: a Code of Practice, membership of an external dispute resolution scheme, and application of Part 2B of the Fair Trading Act (unfair contract terms)*".
>
> *Recommendation 17 - that legislation (or equivalent policy) to impose an interest rate cap be considered if unacceptable consumer detriment is not ameliorated by the policy actions recommended by this Inquiry".*

As noted earlier, these other regulatory options (eg. Registration/licensing, mandatory EDR-scheme membership, unfair contract terms) have been implemented by the Government through the enactment of the Phase 1 NCA reforms and the Australian Consumer Law initiatives. The AFC recommends that Government either undertakes research, or releases details of research undertaken, to identify where those options have failed to justify the need for consideration of the adoption of a national interest rate cap.

Further, again, as noted in the Victorian Government's Report and in the context of Treasury's proposal that the NSW cap has been used as the basis for the draft provisions in Schedule 4:

> *Australia's experience of inclusive interest rate caps largely centres on NSW, where the Government implemented a 48 per cent p.a. cap on the total cost of credit in 2006. .....The NSW Office of Fair Trading has not evaluated the effectiveness of its capping legislation and is still working to close loopholes and to ensure lenders are compliant. However, the NSW experience is useful in highlighting some of the problems and challenges associated with this regulatory option.*

Since release of this Report, as Treasury is aware, contrary to industry and Commonwealth Government expectations, in 2010 the NSW Government amended the legislation to maintain the interest rate cap but also changed the method of calculating it. In particular, a significantly broader and ambiguous range of charges, including payments to third parties, as well as in some situations payments for insurance and other services, were to be included in the calculation. The officially stated intention was to ensure 'unscrupulous lenders cannot avoid the cap by artificially separating their business into a broker plus lender structure so that they can hide their exorbitant fees'. The AFC raised concerns with this development with the [then] NSW Minister for Consumer Affairs. The focus was on the potential for unintended consequences for some AFC members created by the modification of the calculation and the entire lack of consultation prior to enactment. Because Treasury has sought to base the draft provisions on the 2010 NSW model, we reiterate the concerns raised in the AFC submission to the NSW Government and have attached a copy rather than repeating the detail in this submission (Attachment 1).

For these reasons, the **AFC recommends** that further consideration of:

2 http://www.consumer.vic.gov.au/CA256902000FE154/Lookup/CAV_Publications_Credit_and_Debt/$file/consumer_credit_report_of_the_small_amount_lending_inquiry_2008.pdf

- whether interest rate caps are the appropriate policy response to address high cost lending; and
- if so, the appropriate formula for the cap to achieve a targeted outcome to address predatory lending and minimise unintended consequences for the consumer credit industry

is required on this issue in a timeframe that enables real consultation to occur as a pre-cursor to the development of draft legislation to implement the determined policy.

**INTEREST RATE CAP – TIME FOR CALCULATION – PROPOSED REQUIREMENT TO ASSESS THROUGH LIFE OF CONTRACT**

We note that in the original Exposure Draft of the Bill provided by Treasury that there was a proposal to further modify the NSW approach to interest rate caps in s. 32A. As we understand, this provision would require a credit provider to undertake an interest rate calculation not just at the outset or prior to entry into a credit contract (other than a small amount credit contract) but potentially on a dynamic basis throughout the life of the credit contract (ie. cap must not be exceeded **at any time**). In effect, a credit provider would need to adopt a process that individually flags and calculates each change in a credit contract on a portfolio basis to automatically run a calculation to determine whether the 48% cap would be exceeded. We appreciate that this provision has not been included in the present Bill to allow further consultation. We also note that this has commenced with the release of an Options Paper by Treasury. However, we note that an option has not been proposed to omit inclusion of this dynamic requirement rather proposed modification f how it might operate. Again, without evidence of market failure or consumer detriment to justify this significant, operationally difficult and costly compliance requirement, the AFC opposes its enactment and will be responding to this effect to Treasury.

**EXEMPTIONS**

Should the Government remain committed to introduction of an interest rate cap for all regulated credit we recommend that an exemption to address unintended consequences of this policy prescription is required. In particular, we submit continuation and expansion of the current exemption for ADIs to also encompass regulated credit provided by registered financial corporations (RFCs) as defined under the Financial Sector (Collection of Data) Act 2001. The policy basis for inclusion of the exemption for ADIs would equally be applicable for RFCs. Further we submit the exemption should be of general application for credit products offered by these entities because of the broad-application of the interest cap calculation proposed and consequence broad potential for unintended consequences and application to a range of products offered by AFC members (including credit card products).

We also acknowledge and support the proposed inclusion of an exemption for bridging finance on the lines as proposed. The concerns expressed for AFC members involved in bridging finance were incorporated in the submission to the NSW Government on interest rate caps referred to earlier and attached (Attachment 1). These concerns remain valid and the AFC recommends inclusion of the proposed exemption for providers of bridging finance to address those concerns.

## SCHEDULE 5 CONSUMER LEASE AMENDMENTS

*AFC Comments*

By way of background, in the mid-1980s in the policy development phase of the UCCC, AFC being aware of the consumer lease product in overseas jurisdictions, suggested that provision be made for it in Australia. As a consequence, a consumer leases regime, modelled on the then South Australia Consumer Credit and Consumer Transactions Act was incorporated. 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.

As practices and compliance generally in relation to consumer leases have been affected by the Phase 1 NCC law reforms including the responsible lending provisions and by the new unfair contract terms provisions (UCT) under the ASIC Act, what may have been a concern pre-NCC may no longer be. Given that the NCC and UCT only commenced on 1 July 2010 and full implementation of the responsible lending and hardship provisions is likewise near term – comments made earlier in relation to hardship and stay of enforcement provisions reiterate in the context of the equivalent provisions proposed for consumer leases.

However, we note that evidence of consumer detriment in relation to certain providers of consumer leases who are avoiding the operation of the NCC by offering leases for an indefinite term has been put forward but thatt the Bill does not seek to address this avoidance practice on the basis that referral of powers legislation at the state level is required as a pre-cursor to its enactment. While acknowledging the work the Government through Treasury is undertaking in this regard and the proposed inclusion of an anti-avoidance mechanism through a further Enhancements Bill next year, we note the somewhat anomalous situation which sees providers of consumer lease products complying with the NCC provisions potentially subject to additional compliance obligations with attendant costs without a clear basis of need for regulatory change while instances of consumer detriment are allowed to continue.

*Specific Provisions*

(a) Hardship & Stay of enforcement proceedings – We reiterate our concerns identified with equivalent provisions to the credit contract products as being equally valid with the proposed changes to the hardship and stay of enforcement provisions with consumer leases.

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

(c) 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.

*******************

# AFC MEMBER COMPANIES

Advantedge Financial Services
Advance Business Finance
Alleasing
American Express
ANZ t/as Esanda
Automotive Financial Services
Bank of Queensland
BMW Australia Finance
Branded Financial Services
Capital Finance Australia
Caterpillar Financial Australia
CNH Capital
Collection House
Commonwealth Bank of Australia
Credit Corp Group
De Lage Landen
Dun & Bradstreet
FlexiGroup
Ford Credit
GE Capital
Genworth Financial
GMAC
HP Financial Services
HSBC Bank
Indigenous Business Australia
International Acceptance
John Deere Credit
Kawasaki Finance
Key Equipment Finance
Komatsu Corporate Finance
Leasewise Australia
Liberty Financial
Lombard Finance
Macquarie Equipment Rentals
Macquarie Leasing
Max Recovery Australia
Members Equity Bank
Mercedes-Benz Financial Services
Nissan Financial Services
Once Australia t/as My Buy
PACCAR Financial
Pepper Australia Pty Ltd
Provident Capital
Profinance
RABO Equipment Finance
RAC Finance
RACV Finance
Resimac Limited
Ricoh Finance
RR Australia
Service Finance Corporation
Sharp Finance
SME Commercial Finance
Solar Financial Solutions
St. George Bank
Suncorp
Suttons Motors Finance
The Leasing Centre
Toyota Financial Services
Veda Advantage
Volkswagen Financial Services
Volvo Finance
Westlawn Finance
Westpac
Wide Bay Australia
Yamaha Finance

Professional Associate Members:
Allens Arthur Robinson
CHP Consulting
Clayton Utz
Dibbs Barker
EDX Australia
Henry Davis York

08/11 V2.0