Chapter 1

Committee view

The committee's approach to this inquiry

1.1 This inquiry occurred against the backdrop of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry. The matters were referred to the committee in October of last year while the Banking Royal Commission was conducting public hearings, and we are now reporting shortly after the Commissioner, the Hon. Kenneth Hayne AC QC, has delivered his final report.

1.2 The Banking Royal Commission provided a long overdue forum for the public and policy makers to hear what had gone wrong in Australia's mainstream financial sector, and the impact that misconduct had on ordinary people's lives.

1.3 However, it only considered some of the ways in which ordinary Australians interact with financial products. The Banking Royal Commission did not contemplate marginal credit service providers such as payday lenders, consumer leases, and debt advice firms. Although many Australians do not interact with these products, they loom large in the financial lives of lower income Australians and dominate the casework of financial counsellors and credit lawyers.

1.4 This inquiry aimed to address this gap. There are obviously differences between the resources, time and powers available to a royal commission and a Senate inquiry. Nonetheless, this inquiry provided an opportunity to shine a light on the conduct of those who target credit products and services at Australians who are at risk of financial hardship.

1.5 Throughout the course of this inquiry the committee has been conscious that the financial products it examined are not all alike. Like all financial products, they exist on a spectrum of risk and potential harm. The business models (and business practices) of different providers also differ considerably. Some products, such as consumer leases and payday loans, are clearly targeted at low income Australians who do not have access to other credit products. The evidence before this committee (as well as the public record of regulatory actions) shows that there are real issues with the business models and business practices of providers in this sector. That is plainly different from the risk posed by other providers, such as those in the buy now pay later sector, whose products are marketed to a much broader range of Australians.

1.6 What these products all have in common, however, is the oversized risk they pose specifically to Australians in financial hardship. The committee heard from financial counsellors and credit lawyers about the financial troubles that affect too many vulnerable Australians. The work that the financial counsellors and credit lawyers do is important, and the committee takes their evidence very seriously.

The reality of financial hardship in Australia

1.7 The committee received moving evidence about what financial hardship looks like in Australia. Financial hardship impacts more than just a person's finances.

> Sue and Bob live in Broadmeadows (20 km north of Melbourne's Central Business District), with their two children age 12 and 16.
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> Sue works full-time and earns $1030 per week. Bob is on Newstart and receives around $200 a fortnight. He is unable to work after he had a car accident while driving a company truck in September 2017 and injured his back. He is unable to work and not receiving WorkCover, as at the time of the accident, Bob was unlicensed.
>
> Bob took out payday loans from MoneyMe, Wallet Wizard and Sunshine Loans to pay for the registration of their two cars, as well as covering utility bills and rent when money was tight. They could not afford the loans but were desperate because they didn't want to be evicted or disconnected. Repayments on the three loans is around $550 per fortnight, with very high interest rates and fees meaning that they will be paying these loans for a significant period of time.
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> They have not sought support from family as they feel ashamed. Sue suffers from anxiety and Bob depression.
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> After paying rent and the loan repayments, the family is left with $635 per week, well below the 2018 poverty line of $742 a week disposable income.[1]

1.8 This is not an isolated instance. Independent research found that 2.1 million Australians are under severe or high financial stress.[2] For low and middle income earners, this stress can have an immense impact on the ability to service day to day living expenses such as rent, bills and maintenance of household goods.

1.9 Some have tried to paint those in financial hardship as victims of their own poor decisions. The evidence to this inquiry does not support this. As we have heard repeatedly from financial counsellors and legal advice services across the country, the average story of financial hardship is not that of someone with tastes beyond their means. It is the story of someone who has found themselves in a spiral of debt because they cannot bridge the gap between their income and their basic needs, or save enough to absorb the ordinary financial shocks that strike family budgets.

1.10 The intractable maths of low income earners' family budgets pushes them towards the marginal credit products that were examined over the course of this inquiry—products such as payday loans, consumer leases and, in the end, debt management firms. Government can and should improve the terms under which these products are offered. Products that are targeted at Australians at risk of financial hardship should not be allowed to take advantage of their financial vulnerability.

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1 UnitingCare, *Submission 49*, p. 12.

2 NAB and the Centre for Social Impact, *Financial Security and the influence of economic resources*, December 2018, https://www.csi.edu.au/media/2018-Financial-Resilience-in-Australia.pdf (accessed 19 February 2019), p. 6.

1.11 However, the longer term solution has to be found in (a) raising incomes and (b) expanding access to the mainstream financial products that offer better value to those who can afford them. Inclusion in Australia's financial system is critical for a successful and robust economy and social framework. Low income Australians should not be excluded from fair and appropriate access to financial services, and not be relegated to the use of high cost and potentially harmful products.

Recommendation 1

1.12 The committee recommends that the government should have a strategy to raise the incomes of low income Australians. This strategy should, at a minimum, include protecting penalty rates and reviewing the adequacy of government payments including Newstart.

Credit products targeted at Australians at risk of financial hardship

1.13 The worst case studies presented to this inquiry concerned marginal credit products such as payday loans and consumer leases.

1.14 Consumer leases ostensibly offer rented goods. The reality is consumers are often charged an inflated price to use the goods, and can pay the total cost of the goods multiple times during the course of the agreement:

> Unlike other credit providers, there is absolutely no cap on the amount consumer lease providers can charge. An ASIC [Australian Securities and Investments Commission] report on the cost of consumer leases for household goods found a clothes dryer cost a Centrelink recipient the equivalent of an 884% interest rate.[3]

1.15 The situation worsens for those who cannot repay their debts on time, with the lessor able to repossess the goods. As the agreement is not seen as a loan, there are limited protections for the individual under the National Credit Code. Repossession can cause immense stress:

> If the leased good is a car or an essential electrical item (like a fridge or washing machine), repossession can mean further costs like job loss, no stored food and visits to the laundromat.[4]

1.16 Despite being sold as quick and cheap credit, in reality payday loans are pushing people into a spiral of debt. Confusion around the operation of legislated caps has led to incredible rates of interest being charged to consumers.

> Due to the generous fee caps, these loans typically attract comparison annual interest rates of between 112.1% and 407.6%. The vast majority of payday lenders charge the maximum amount permitted by legislation, as competition is generally ineffective in bringing down prices in this market.[5]

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3 Consumer Action Law Centre, *Submission 37*, p. 6.

4 Financial Counselling Australia, *Submission 57*, p. 6.

5 Consumer Action Law Centre, *Submission 37*, p. 6.

1.17 Often these products appear not only to have been targeted at Australians in financial hardship—they seem to have been designed to take advantage of them. It is difficult to escape the conclusion that many providers' business models depend on vulnerable consumers who have limited awareness of other product options, limited negotiating power, and limited propensity to complain about improper or illegal behaviour.

1.18 This is not a revelation. Concern over high cost credit is a long standing one. The government commissioned a review of the Small Amount Credit Contract (SACC) industry in 2015. It found widespread problems throughout the industry. In relation to consumer leases it found that '…the current regulatory framework is not effective in promoting financial inclusion.'[6] The exposure draft of legislation was developed in 2017 and Treasury undertook a consultation process in relation to it.[7]

1.19 There has been no apparent action since then. There has been media coverage of the internal government tensions that may have contributed to this delay. Irrespective of the cause of the inaction, its consequences have been clear.

> Since the Government released the SACC Review report in April 2016, Digital Finance Analytics estimates that three million additional payday loans, worth an estimated $1.85 billion, have been taken out. This has generated a net profit of about $250 million for lenders. Around one fifth (about 332,000 households) were new payday borrowers.[8]

1.20 These providers have gone largely unchecked for too long. The delay in the introduction of the 2016 recommendations encapsulated in the exposure draft bill and the failure to pass the subsequently introduced private member's bill have allowed product providers to continue to offer products unsuitable to many of their consumers.

Recommendation 2

1.21 The committee recommends that the National Consumer Credit Protection Amendment (Small Amount Credit Contract and Consumer Lease Reforms) Bill 2017 exposure draft released by Treasury be introduced, and passage facilitated by the government.

1.22 The passage of the SACC legislation would address some but not all of the known problems in the sector. The committee received evidence about a number of discrete issues that also require remedy. Those issues include:

- breaches of the existing regulatory framework;
- the use of blackmail security;
- the regulation of medium amount credit contracts;

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6 The Treasury, *Review of the small amount credit contract laws, Final Report*, March 2016, p. 4, https://static.treasury.gov.au/uploads/sites/1/2017/06/C2016-016_SACC-Final-Report.pdf, (accessed 5 December 2018).

7 The Treasury, *Small Amount Credit Contract and Consumer Lease Reforms*, https://treasury.gov.au/consultation/c2017-t229374/ (accessed 21 February 2019).

8 Consumer Action Law Centre, *Submission 37*, p. 3.

- the role of sales staff in offering credit; and
- the need for effective anti-avoidance measures.

1.23 Each of these issues is addressed in turn below.

Noncompliance

1.24 The committee is concerned about ongoing noncompliance with the existing regulatory framework for consumer leases and payday loans. Although providers gave evidence that the issues in the sector were historic and not ongoing, that is not consistent with the case studies and experiences presented by financial counsellors and credit lawyers.

1.25 There are, for instance, real doubts about whether pay day lenders comply with responsible lending obligations. As one financial counsellor noted:

> I see loans issued where there's clearly no capacity to repay that loan. A lady I met last month had 30 Cash Converters loans in the last four years. Three of those loans were issued after a Cash Converters loan had been defaulted and not repaid, and 17 of those loans had been issued when she had two or more loans in the previous 90 days, and that would indicate that she has an incapacity to meet that loan, particularly when you look at her bank statements that show several overdrafts…[9]

1.26 It has been suggested that lenders push borrowers to accept shorter contract terms despite this being against their interests:

> It's about trying to get as many loans in as possible. The establishment fee is much higher than the monthly fee…also…a lot of the market is making its money on people falling into arrears and hardship, because it's the penalty fees where you actually make all the money. So, to try and push people into contracts that are very tough to service but that they don't fall over on is actually an optimal business model.[10]

1.27 The committee was provided with hundreds of examples of illegal behaviour in small and medium credit and consumer leasing, suggesting widespread non-compliance.

1.28 Greater scrutiny is needed as to how these products are sold, how they are policed and the recourse that consumers have to make complaints or inquire as to whether the product was inappropriately sold.

Recommendation 3

1.29 The committee recommends that the government provide additional funding to strengthen the capability of the Australian Securities and Investments

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9 Mrs Sandra Blake, Financial Counsellor, Financial Counselling Australia, *Committee Hansard*, 12 December 2018, p. 3.

10 Ms Corinne Proske, General Manager, Retail and Online, Good Shepherd Microfinance, *Committee Hansard*, 12 December 2018, p. 40.

Commission to police the small and medium credit contract sector and consumer leasing sector.

Recommendation 4

1.30 The committee recommends that the Australian Securities and Investments Commission, the Australian Competition and Consumer Commission and the Australian Financial Complaints Authority undertake a review to assess what systems and mechanisms would counteract the chronic underreporting of malpractice and how best to allow consumers to make complaints about the behaviour of consumer lease and payday lending providers.

Blackmail security

1.31 The committee is concerned by evidence that some providers would secure a loan against an asset such as a car that is worth less than the value of the loan but is essential for the borrower to have. As Legal Aid Queensland noted, this form of security is:

> …'coercive': the pressure's on them to continue to pay it, because without it they don't get to work and they don't keep their job.[11]

1.32 Lenders were able to circumvent restriction on blackmail securities by moving borrowers onto medium amount credit contracts:

> There is a prohibition in the current code around blackmail securities, because in the past one of the things that was added as security to these types of loans was—I think the classic we had was a Bananas in Pyjamas doona cover. When the credit legislation became national, that was prohibited. What was not prohibited was the taking of security on medium amount credit loans. Blackmail securities were prohibited, but they still could take security. What we've seen is people wanting to take a medium amount loan, which is between $2,001 and $5,000. There are companies out there who are working out if somebody has a car. The car is usually worth significantly less than the value of the loan. They're securing it to try to make sure that that becomes the priority loan to be paid, because usually people, particularly in regional areas of Queensland where the public transport isn't as good, are needing that car to get to work, so they'll pay that loan first, to the exclusion of anything else.[12]

Medium amount credit contracts

1.33 The regulatory regimes for small and medium amount credit contracts differ significantly in key areas. Evidence was presented of providers moving clients from SACC products to medium amount credit contract products, where regulation in some matters is less onerous:

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11 Mr Paul Holmes, Senior Lawyer, Civil Justice Services (Consumer Protection), Legal Aid Queensland, *Committee Hansard*, 22 January 2019, p. 26.

12 Mr Paul Holmes, Senior Lawyer, Civil Justice Services (Consumer Protection), Legal Aid Queensland, *Committee Hansard*, 22 January 2019, p. 26.

> **Mr Wood**: A lot of the lenders out there are pushing the applicant to go above the $2,000, because the regulations, in their opinion, are too tight on the small amount credit contract market. As Corinne said, over the last 12 to 18 months a number of lenders have stopped offering that product, and offer a line of credit because it's easier. It's less regulated, in their opinion. So they can get someone on the drip, basically, and they're just continually earning money that way.
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> **ACTING CHAIR**: As those businesses move into that market strategy, are they targeting particular demographics?
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> **Mr Wood**: It's the younger generation, if you look at their advertising. They're always down at the beach, they're relaxing, they're having a drink and stuff like that. It's very much targeted towards the younger generation.[13]

1.34 A consistent and robust regulatory framework is needed across these sectors to remove distortions between the different products and loan sizes.

Recommendation 5

1.35 The committee recommends that Treasury undertake a review to identify necessary reforms to regulatory arrangements for medium amount credit contract products.

Sales staff and credit

1.36 The role of frontline staff in promoting financial products in franchisee stores has the potential to lead to adverse consumer outcomes. There is no justification for retail dealers being carved out of the *National Consumer Credit Protection Act 2009*. Commissioner Hayne of the Banking Royal Commission made a recommendation in this regard.[14] It should be adopted.

Recommendation 6

1.37 The government should implement Recommendation 1.7 of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry removing point of sale exemptions from the *National Consumer Credit Protection Act 2009*.

Anti-avoidance

1.38 Witnesses told the committee that providers of pay day loans and consumer leases are structuring their businesses to avoid regulatory obligations:

> In the situation of Cash Converters, when Queensland introduced capping legislation, the Cash Converters outlet went from acting as an agent for Cash Converters to a broker for the customer. So I think there are reasons to be concerned that providers do take a very close and careful look at the

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13 Mr Richard Wood, Credit Manager, Good Shepherd Microfinance, *Committee Hansard*, 12 December 2018, p. 40.

14 Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, *Final Report*, vol. 1, pp. 86–87.

> legislation and work out how they cannot be bound by it. I think a broad based and substantive anti-avoidance provision that is clearly directed at schemes or arrangements, something broader than contracts, is necessary.[15]

1.39 The committee accepts this evidence and considers that the entire consumer credit architecture would benefit from more robust anti-avoidance mechanisms.

1.40 It is possible that the product intervention powers previously considered by the Senate Economics Legislation Committee may provide regulators with sufficient powers to achieve this. Government should work with ASIC to monitor the use of the product intervention powers and determine whether they need to be supplemented further.[16]

Recommendation 7

1.41 The committee recommends that the *National Consumer Credit Protection Act 2009* be amended to contain strong anti-avoidance provisions that are capable of capturing both new, emergent credit-like products, and attempts to disguise the nature of existing credit products.

Financial services targeted at Australians at risk of financial hardship

1.42 Unregulated provision of debt and credit repair services poses significant risks to vulnerable Australians.

1.43 While regulated debt agreements can provide administrative support to those who are going through the process of bankruptcy, the emergence of unregulated predatory debt negotiation and debt management firms are impacting those in financially vulnerable situations

1.44 There is limited data available about the size of the industry because most operators do not require a licence. The Consumer Action Law Centre also observes:

> Given the lack of regulation and oversight, it is difficult to maintain comprehensive information about this industry, with new practices and business models constantly emerging.[17]

1.45 Consumers are at risk of entering into agreements where the terms are not clear, often resulting in unexpected fees for service.

1.46 The Salvation Army reports a $1600 set-up fee for a debt agreement that involved only one debt.[18] Legal Aid Queensland offered the following example of a budgeting service:

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15 Ms Miranda Nagy, Principal Lawyer, Maurice Blackburn Lawyers, *Committee Hansard*, 12 December 2018, p. 38.

16 Senate Economics Legislation Committee, *Treasury Laws Amendment (Design and Distribution Obligations and Product Intervention Powers) Bill 2018 [Provisions]*, November 2018.

17 Consumer Action Law Centre, *Submission 37*, p. 22.

18 The Salvation Army, *Submission 9*, p. 12.

> The client and her friend signed the contract at the meeting without the fees and obligations under the contract being properly explained. These fees included a $45 charge to move their own money from the company's account back into their own accounts when they requested money for things such as paying car registration. The client was of the view that she and her friend had been pressured into signing a contract to purchase a product of no or little value to them. When she tried to withdraw from the contract, the budgeting service informed her that she was liable for a large establishment fee.[19]

1.47 The fee paid to the provider is often disproportionate to the service delivered and can leave consumers worse off. In many cases, the fees and contract structure are deliberately complex in order to mask the total cost of the service.

1.48 Financial Rights Legal Centre explained that debt negotiators often charge high fees for results which do not solve the consumer's problems:

> We've seen quite a few that are a percentage of the amount saved. If you have $150,000 in credit cards and they reduce it to $70,000, they'll take 50 per cent, 40 per cent or 80 per cent of the saving or whatever it is…[20]

1.49 Witnesses provided first hand evidence of firms making deliberate attempts to mislead consumers, or obscure the fees they will pay:

> At this meeting, I was told there was a problem with their printer, so I couldn't receive a hard copy of the contract. I was made to digitally sign it on a tablet. I wasn't able to read it before I signed because it was over 40 pages long…At this meeting I again asked about the fees, and I was told there are only two sets of fees: a fee to set up the agreement to liaise with the creditors and a fee to use the budget. On checking the budget, I found there were other fees embedded there.[21]

1.50 Low financial literacy among consumers means many are unaware they are dealing with a for-profit entity. Individuals who are using these types of services could receive help from financial counsellors or community legal services; and, again at no cost, they can have an independent ombudsman scheme help resolve disputes with lenders, telecommunications and utilities providers.

1.51 The Australian Financial Complaints Authority (AFCA) suggested that debt management firms prey on consumers' ignorance of the system:

> If consumers actually bring a financial hardship matter to AFCA then, whilst the matter is being considered by AFCA, the financial firm is not able to—is excluded from—enforcing that debt. Yet we see situations where debt management firms are actually charging fees, sometimes not

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19 Legal Aid Queensland, *Submission 3*, p. 11.

20 Ms Karen Cox, Chief Executive Officer, Financial Rights Legal Centre, *Committee Hansard*, 12 December 2018, p. 27.

21 Henry, *Committee Hansard*, 12 December 2018, p. 24.

> insignificant fees, to get the financial firm to stop the enforcement action…[22]

1.52 While debt agreements are regulated by the *Bankruptcy Act 1966*, debt services more broadly are largely unregulated.

1.53 The committee is concerned that a regulatory vacuum risks leaving consumers exposed.

Recommendation 8

1.54 The committee recommends that the government implement a regulatory framework for all credit and debt management, repair and negotiation activities that are not currently licensed by the Australian Financial Security Authority, including:

- **compulsory membership of the Australian Financial Complaints Authority, giving clients access to an External Dispute Resolution scheme;**
- **strict licensing or authorisation by the Australian Securities and Investments Commission or the Australian Financial Security Authority;**
- **prohibition of upfront fees for service;**
- **prescribed scale of costs;**
- **an obligation to act in the best interests of their clients; and**
- **banning unsolicited sales.**

Other financial products

1.55 The buy now pay later sector is one of Australia's fintech growth stories. Not only does the sector now account for a considerable proportion of consumer credit, but this credit is being taken up by new and young customers who have limited previous experience of managing credit.

1.56 This growth has largely outstripped the regulatory response.

1.57 Unlike other credit providers, these products are not covered by the *National Consumer Credit Protection Act 2009* (the National Credit Act) and providers have no obligation to undertake credit checks or appropriate measures to ensure their product is appropriate for the consumer's personal circumstances.

1.58 The committee considers that this regulatory gap should be filled.

1.59 Many Australians can use buy now pay later products with limited financial risk. It seems likely that, as providers have suggested, many people use their products as a budgeting tool. It is less likely, however, that the 23 per cent of people paying their buy now pay later account with a credit card are using the service for

22 Mr David Locke, Chief Ombudsman and Chief Executive Officer, AFCA, *Committee Hansard*, 24 January 2019, p. 9.

budgeting.[23] It is almost certainly not the case that individuals with multiple payday loans are using buy now pay later products to budget.

1.60 The evidence from financial counsellors and credit lawyers suggests that there is a real risk for a cohort of vulnerable Australians arising from adding buy now pay later products to a mix of other credit products. For people in a debt spiral responsible actions, even some protective design features, can lead to unintended consequences. The committee heard, for instance, that some individuals prioritise buy now pay later repayments over other forms of credit specifically to avoid being cut off from the service for missing payments.

1.61 There is also a unique risk that arises by virtue of the age and financial experience of the buy now pay later customer base. Eighty-five per cent of customers of one provider, Afterpay, use a direct debit card, and have a limited credit file.[24] For many people, a buy now pay later product is their first credit product. We should ensure that experience is a positive one.

1.62 The evidence by buy now pay later providers ZipCo and Afterpay to this committee suggested that both were alive to these risks and willing to strengthen the regulatory framework that applies to the sector. As Afterpay noted:

> We are confident the right regulatory balance can be struck for new products such as Afterpay to ensure customers get the best outcomes with the best protections.[25]

1.63 There is no guarantee, however, that future entrants to the sector will take a similar approach.

1.64 There is a clear role for regulators in ensuring that buy now pay later is subject to proper regulation that will provide consumers with the same protections they would enjoy with respect to products with a similar risk profile.

Recommendation 9

1.65 The committee recommends that the government consider, in consultation with the Australian Securities and Investments Commission, consumers and industry, what regulatory framework would be appropriate for the buy now pay later sector. This regulation should ensure that:

- **before credit is extended, providers appropriately consider consumers' personal financial situations;**
- **consumers have access to internal and external dispute resolution mechanisms;**

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23 ASIC, *Report 600: Review of buy now pay later arrangements*, November 2018, p.12, https://asic.gov.au/regulatory-resources/find-a-document/reports/rep-600-review-of-buy-now-pay-later-arrangements/ (accessed 20 February 2019).

24 Mr Nick Molnar, Chief Executive Officer and Co-Founder, Afterpay, *Committee Hansard*, 22 January 2019, p. 13.

25 Mr Nick Molnar, Chief Executive Officer and Co-Founder, Afterpay, *Committee Hansard*, 22 January 2019, p. 9.

- **providers offer hardship provisions;**
- **products are affordable and offer value for money; and**
- **consumers are properly informed, prior to entering into agreements, about their terms and conditions.**

Recommendation 10

1.66 The committee recommends that the buy now pay later sector develop an industry code of practice.

1.67 It is important that government get the regulatory settings working for consumers. Currently, ASIC does not have the powers to intervene as new products emerge in the market and make interventions if a financial product such as buy now pay later is not fit for purpose. Key players in the sector have agreed that a product intervention power would strengthen the regulatory regime for consumers.

Recommendation 11

1.68 The committee recommends that product intervention power currently proposed in the Treasury Laws Amendment (Design and Distribution Obligations and Product Intervention Powers) Bill 2018 legislation be extended to cover buy now pay later products.

Online and digital marketing of financial products

1.69 The products examined over the course of this inquiry do not exist in isolation. The interactions between consumers and the providers have become more complex as digital technology develops.

1.70 The committee recognises that the delivery method for financial products has changed since the advent of online and digital marketing. Consumers are increasingly at risk of targeting by providers through methods that create an imbalance between the consumer and the credit provider. For those who are financially vulnerable this is of particular risk.

1.71 Dr Paul Harrison of Deakin University provided evidence as to how providers are able to target those who are most likely to use these financial products:

> This is because the provider has significant data analytic capacity, they are able to adapt their offer as it virtually follows and tests consumer responses and, through technology such as neural networking, is able to anticipate consumer responses and intervene to lead the consumer to make choices that suit business.[26]

1.72 This form of advertising allows providers to target products to individuals for whom the product may not be suitable or to whom the features of the product are not transparent. In an age of continuous digital innovation, regulatory guidance should be updated in order to ensure consumers are protected.

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26 Dr Paul Harrison, Centre for Employee and Consumer Wellbeing, Deakin University, *Committee Hansard*, 22 January 2019, pp. 1–5.

Recommendation 12

1.73 The committee recommends that the Australian Securities and Investments Commission review how financial products and services (including credit) are advertised and issue an updated regulatory guide to how credit products interact with consumers in an online environment.

Centrepay

1.74 Centrepay is a government billing and budgeting tool for Centrelink recipients. It is intended to benefit Centrelink recipients.

1.75 The Department of Humans Services provided evidence of the quantum of consumer leases used through Centrepay payment system:

> ...out of the $2.6 billion in 2018 run through Centrepay, $255.5 million ran through consumer leases—so, about 9.8 per cent.[27]

1.76 The benefit to consumer lease providers of being registered through Centrelink is clear: automatic deductions reduce the default rate for companies, while also allowing them to continue to charge the consumer for products well above the cost of the product. Thorn Group, the parent company of Radio Rentals, noted that 52 per cent of Thorn Group's consumer leasing customers paid via Centrepay.

1.77 The benefits to recipients are less clear. ASIC noted that although Centrepay lowered the risk of default on rental payments, the companies still charged Centrepay customers more. Because Centrepay customers are on lower incomes, the terms of their loans are longer, which also increases the final cost.[28]

1.78 The committee understands that the purpose of Centrepay is to support recipients with payment of their expenses. Given the expensive nature of consumer lease products, the use of this service is not in line with the purpose of Centrepay. The payment structure of consumer leases can cost consumers more in the long run and further entrench individuals in a spiral of debt.

1.79 As the Salvation Army observed:

> This appears contrary to the original principles of Centrepay, which we understand were to help people on low incomes with money management. In our experience a consumer lease payment is more likely to cause money management issues.[29]

1.80 Far from helping Centrelink recipients budget, Centrepay deductions for consumer leases can impact an individual's ability to pay for essential goods:

> Financial Rights speak to many consumers who call us because they cannot afford essential expenses such as rent and energy. It is only upon delving

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27 Mr Gavin Matthews, General Manager, Older Australians, Department of Human Services, *Committee Hansard, 24 January 2019*,p. 21.

28 Mr Michael Saadat, Senior Executive Leader, Deposit Takers, Credit and Insurers, Australian Securities and Investments Commission, *Committee Hansard*, 24 January 2019, p. 13.

29 The Salvation Army, *Submission 9*, p. 9.

> into their financial situation that we discover a significant proportion of their Centrepay payments are being diverted to pay consumer leases.[30]

1.81 The impact is particularly severe on marginalised groups:

> Remote Aboriginal communities have been targeted by payday lending and consumer lease companies through the use of Centrelink's Centrepay system.[31]

Recommendation 13

1.82 The committee recommends that Centrepay should only be available to entities that can demonstrate historic and ongoing compliance with relevant regulations, and that provide products at a fair price and in a fair manner.

1.83 Centrepay is administered with little acknowledgement of the impact that these products can have on consumers. While the Department of Human Services acknowledges the impact of consumer lease products, they do not take into account the potential for hardship through the use of Centrepay.

> We do compliance audits on businesses to make sure that the customer is giving consent before entering into the Centrepay arrangement. We check to make sure that what the company is charging-the payment matches the contract they've got. But we're not a regulator, so we don't regulate whether, for example, they're in that circumstance.[32]

1.84 The department indicated that product providers were only removed from the system in limited circumstances including if ASIC had taken action to remove a product licence.

> The responsible lending obligations are really where the Centrelink action would come in. ASIC obviously will make a range of decisions. They may remove licences but they may not. So it may be that they find some behaviour in the organisation, the organisation remediates that behaviour and ASIC don't find any further behaviour. Then we wouldn't necessarily remove them from Centrepay for that, because there is action underway from the regulator to ensure that the business is complying.[33]

Recommendation 14

1.85 The committee recommends that the Department of Human Services develop the capability to review Centrepay data to identify clients who are at risk of serious financial hardship and develop appropriate interventions, such as referral to a financial counsellor.

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30 Financial Rights Legal Centre, *Submission 31*, p. 12.

31 Financial Rights Legal Centre, *Submission 31*, p. 13.

32 Mr Gavin Matthews, General Manager, Older Australians, Department of Human Services, *Committee Hansard*, 24 January 2019, p. 22.

33 Mr Gavin Matthews, General Manager, Older Australians, Department of Human Services, *Committee Hansard*, 24 January 2019, p. 23.

The need to support and expand financial counselling services

1.86 The committee recognises the important work of financial counsellors offering a free service to assist financially stressed households to manage their debts and avoid further financial hardship.

1.87 During the course of the inquiry financial counsellors provided evidence of the scale and impact of predatory financial products on their clients.

1.88 Financial Counselling Hunter Valley Project provided evidence that showed the impact of pay day loans on an individual's livelihood.

> These vulnerable consumers tend to develop relationships with payday lenders and develop a reliance on this type of credit usually to their detriment. While payday loans result in a short-term increase in funds, in the following months the person's financial position worsens.[34]

1.89 While financial counsellors across the country are delivering for their clients, the demand for services is increasing without the adequate resources or trained financial counsellors to meet demand.

1.90 Financial Counselling Australia highlighted that the demand for services is exceeding supply and is leading to many clients being turned away.

> This means that roughly 60% of people seeking assistance were able to be accommodated and 40% were not. Another way of putting this is that for every five who seek financial counselling, three people are able to access it and two are turned away.[35]

1.91 There is broad unmet need through the community for services. These services have real impact on the lives and finances of families. Funding for these services needs to be expanded.

1.92 The government response to tackling the effect of debt on consumers must include both a regulatory regime for providers and appropriate support for those impacted by provider conduct.

Recommendation 15

1.93 The committee recommends that the government increase the funding available to financial counselling organisations to enable a substantial increase in the number of full time employed financial counsellors across the country. The funding should be directed to ensure there are sufficient financial counsellors available in areas of need, including regional Australia.

Recommendation 16

1.94 The committee recommends that the government increase the funding available to community and financial rights legal centres.

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34 Financial Counselling Hunter Valley Project, *Submission 2*, p. 1.

35 Financial Counselling Australia, *Supplementary submission 57.1*, p. 14.

1.95 The committee recognises that financial counselling services are impacted by inconsistent funding processes.

1.96 Financial Counselling Australia argued for both adequacy in funding and consistency in the funding allocation process.

> The continued theme is that funding for financial counselling is almost always under threat. There is example after example of where governments either cut funding completely or reduce it substantially. Some State governments have defunded services in one budget and then reinstated it again one or two budgets (or more) later, once they've realised the original decision was short-sighted.[36]

1.97 The uncertainty in the sector makes it difficult for agencies to plan for and manage their services. Recent tender processes have continued to be implemented in a chaotic manner and to the detriment of those who are relying on financial counselling support.

1.98 Financial Rights Legal Centre and Consumer Action Law Centre highlighted their concerns with the recent tender process on the National Debt Helpline:

> …we consider the DSS tender process that has occurred this year suffered from serious flaws, and the outcome of the process will negatively impact the effective NDH service model. While the full outcomes of the tender process have not been made public, Consumer Action Law Centre and Financial Rights Legal Centre were informed in late October that our applications were unsuccessful.[37]

Recommendation 17

1.99 The committee recommends that future tenders for financial counselling be conducted in a manner and to a timetable that gives service providers confidence in the outcome, and allows them to continue their work without significant disruption.

Alternative financial products for financially stressed Australians

1.100 The committee considers the failure of trust in small amount credit providers to provide appropriate and affordable credit as an indictment on the poor practice in the sector. Excessive interest applied to, and predatory behaviour targeted at, vulnerable people is forcing consumers into spiralling debt.

1.101 The committee received evidence of alternative means of providing credit to those in need of financing through microfinance such as No Interest Loans Schemes (NILS) and Step-Up loans, which offer small loans at low interest. These products offer a fairer alternative to pay day loans and consumer leases. To date, the government has provided limited support to these credit facilities which could have far reaching benefits for financially stressed Australians in need of credit.

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36 Financial Counselling Australia, *Supplementary submission 57.1*, p 9.

37 Consumer Action Law Centre and Financial Rights Legal Centre, *Submission 42*, p. 3.

1.102 Good Shepherd Microfinance highlights the benefits of NILS:

> No Interest Loan Scheme (NILS) offers people on low incomes safe, fair and affordable loans for fridges, washing machines and furniture, as well as education and medical expenses. Loans up to $1,500 are available from 178 community organisation at 628 locations across Australia. In the 2017-2018 financial year 27,392 NILS loans were written.[38]

1.103 The provision of microfinance and low and no interest loans has scope for expansion in Australia. The government should explore the scalability and delivery potential of such programs.

Recommendation 18

1.104 The committee recommends that the government consider what tax and other incentives could be used to encourage mainstream credit providers to offer low interest products to vulnerable Australians.

Recommendation 19

1.105 The committee recommends that the No Income Loans Schemes and Step-Up grant programs should be expanded, with longer funding cycles that are aligned to the other grants in the Department of Social Services Financial Wellbeing and Capability funding stream.

Recommendation 20

1.106 The committee recommends that the government should actively promote the No Income Loans Schemes and Step Up programs through Centrelink offices, and other forums where there is contact with people at risk of financial hardship. The government should also consider whether information regarding these programs should be included alongside the information regarding the debt helpline on bills and other documents.

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38 Good Shepherd Microfinance, *Submission 50*, p. 1.