



Abacus
Australian Mutuals

Association of Building Societies and Credit Unions

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Executive Manager
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Policy & Legislative Division
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Dear Executive Manager

Managing the cost of consumer credit in Queensland

Abacus – Australian Mutuals appreciates the opportunity to contribute to the *Managing the cost of consumer credit in Queensland: Discussion Paper*.

Abacus welcomes the focus the Office of Fair Trading has placed on the cost of consumer credit in Queensland and the focus on fringe markets. *Abacus* particularly appreciates the Minister's commitment that the focus is on "finding an outcome that balances consumer welfare with the continued financial viability of lenders."

Abacus is the peak industry association for mutual building societies and the majority of credit unions in Australia.

There are 146 credit unions and 9 mutual building societies across Australia with 16 of these based in Queensland. Over 20% of all Queenslanders belong to a credit union or mutual building society. Credit unions and mutual building societies play a critical role in the consumer credit market, which is a national market, and contribute to the continued growth and success of the Queensland economy.

Credit unions and mutual building societies are highly regulated Authorised Deposit taking Institutions (ADI) and Australian Financial Services (AFS) licensees. Credit unions and mutual building societies also enjoy the highest levels of customer satisfaction in the retail banking market. As member-focused mutual organisations, they make substantial contributions to their communities and have a strong record of acting in members' interests while promoting financial stability and access to affordable and quality credit services.

Although *Abacus* does not believe interest rate caps are the answer, credit unions and mutual building societies would welcome the opportunity to work with the Office of Fair Trading in Queensland, as well as other regulatory counterparts, to address poor lending practices among the fringe market. Responsible lending has always been a key feature of the credit union and building society sector and *Abacus* believes promoting this customer-minded ethos should be part of a broad set of responses to predatory lending practices.

1. Uniformity of consumer credit regulation

Abacus strongly supports a continued focus on nationally consistent credit regulation. Uniformity across State and Territory jurisdictions is critical to the credit sector, which is very much a national industry.

The Office of Fair Trading would be aware that the *Ministerial Council on Consumer Affairs* (MCCA) and the *Standing Committee of Officials of Consumer Affairs* (SCOCA) have been reviewing payday and other fringe lending since 2003, which has canvassed interest rate cap proposals. *Abacus* has made submissions to the *Fringe Credit Providers – Discussion Paper* as part of that consultative process.

In our view, MCCA's role "*to consider consumer affairs and fair trading matters of national significance and, where possible, develop a consistent approach to those issues*" provides the best forum for consideration of the cost of credit and for exploring ways to make credit more affordable and accessible. This national approach reduces the scope for jurisdiction shopping, ensures consistency for consumers across the nation and reduces the potential for expensive and duplicative processes in different State and Territory jurisdictions.

Abacus notes recent comments by Dr David Cousins, from Consumer Affairs Victoria, at the *Centre for Credit and Consumer Law's "Credit Matters"* seminar on 7 December 2006, where he observed that credit was a national market and therefore jurisdictions should strive for national market solutions. At the very least, Dr Cousins observed, jurisdictions should consider the same thinking and arguments before making decisions to regulate. In that context, Dr Cousins suggested that interest rate caps (among other measures) could be raised at a planned SCOCA roundtable in February 2007.

The mutual ADI sector is concerned at the trend for individual States and Territories to pursue separate credit reform initiatives, often over-lapping with each other or national reform proposals. Credit unions and building societies, as smaller, member-focused organisations, would be concerned were Queensland to pursue reforms to deal with the cost of credit outside the established Ministerial Council process. *Abacus* recently made similar comments to the Office of Consumer and Business Affairs (OCBA) in South Australia in respect of their recent *Payday lending in South Australia – Options to increase consumer protection* discussion paper as well as in response to the earlier *Consumer Credit Review* in Victoria.

2. *Abacus'* view on cost of consumer credit

While *Abacus* and the mutual ADI sector support nationally consistent responses to these policy issues, the following comments are provided to assist the Office of Fair Trading's examination of cost of credit in Queensland.

(a) Status quo

The contention that mainstream credit provides are moving away from low-income earners is not an accurate reflection of current practices, particularly within the mutual ADI sector. Many mutual ADIs have well-established relationships and continue to offer credit services to low-income earners. Historically, many credit unions and building societies were established on the basis of people coming together to form a co-operative

in order to provide financial services to consumers that were otherwise unable to access these services in the mainstream market.

However, *Abacus* agrees that the fringe lending market warrants greater scrutiny and should be subject to higher standards of accountability. Customers in this space are generally regarded as being more vulnerable and may have fewer choices as to their source of credit. In these circumstances, *Abacus* welcomes attempts to bring the concerning practices among fringe credit providers into alignment with the controls and responsibilities set out in the credit regulation applicable to the mainstream market.

(b) Self-regulation

Capacity to repay

Generally, *Abacus* supports measures designed to limit access to credit where a borrower does not have capacity to repay the loan. *Abacus* also supports a remedy that an inappropriate credit offering may be rendered unenforceable in these circumstances. Credit unions and building societies already apply robust assessment processes to their credit offerings – a requirement not just of UCCC provisions, but also of credit quality standards imposed by APRA under prudential regulation. It is not in the interest for credit unions or building societies to avoid rigorous assessment processes before offering credit.

The experience of the mutual ADI sector is that the provision of credit is based on behavioural scoring models that take into account not just the member's proven capacity to repay, but also their propensity to repay. *Abacus* understands this to be in line with industry best practice. For consumers, there is also a positive obligation to alert their credit providers when their circumstances change. This provides a good platform for creditors to understand the repayment capacity of their customers.

Abacus believes comparable lending criteria and best practice approaches should operate among non-ADI lenders in the consumer credit market. In these circumstances, *Abacus* notes various suggestions to consider positive or comprehensive credit reporting to improve the collection, accuracy and retention of credit data to assist in decision-making about credit worthiness.

The case for positive credit reporting is that it will improve the chances of low-income earners gaining access to mainstream credit, it will reduce defaults leading to lower cost of credit, it will promote competitive markets as consumers are less reliant on existing institutional relationships to obtain credit, it will provide more reliable identification of over-committed consumers, it will better identify under-served market segments and it will enhance predicability of scoring models. However, *Abacus* also recognises concerns about an increase in the amount of personal information held on consumers, which could lead to detailed customer profiling or poor data quality.

If these reforms occur, they represent an important input into a payday lenders' ability to assess a consumer's capacity to repay a loan. However, if payday lenders and other fringe credit providers gain access to Part IIIA information under the *Privacy Act 1988* (and 2001 amendments) then it must be subject to at least the same high standards and expectations as mainstream credit providers covered by s.11B(1) of that Act.

Any positive credit reforms should also be balanced against the continued protection of consumer information and privacy. The *Australian Law Reform Commission* (ALRC) is considering access to the Part III consumer credit reporting information as a feature of its extensive review of the *Privacy Act 1988*. *Abacus* encourages further discussion between the Office of Fair Trading and the Federal Privacy Commissioner as well as the ALRC in relation to what information should be considered when assessing a borrowers capacity to repay a loan and how that information should be safeguarded.

Fees and charges

Many credit union and building society customers choose their mutual ADI for their fairer fees and better services. Two thirds of credit union members do not pay any transaction or account fees at all. In 2006, CANNEX ascribed \$112 per year in extra member value in terms of lower interest rates and fees for mutuals ADIs. This approach is derived from their mutual structure, where members are both owners and customers and profits are returned to members in the form of lower fees and a commitment to the local community.

While *Abacus* agrees that default fees should, prima facie, align to cost recovery criteria, the focus in regulatory responses should be on the most effective and efficient means of delivering reasonable fee outcomes. Heavy handed price interventions will impose high costs on mainstream or conservative lenders, while encouraging market manipulation by other parties to avoid capture or jurisdiction. Additionally, mutual ADIs and already subject to the misleading and deception and unconscionability provisions of the ASIC Act 2001.

Abacus believes intervention in relation to fees and charges across the mainstream lending market require further discussion and detailed review. This is particularly the case as the discussion paper has not outlined any consumer detriment attributable to the fees and charges of mainstream providers. Additionally, any proposal to limit fees and charges to cost recovery should also consider the corollary pressure to increase interest rates on some products. Similarly, proposals to address excessive fees charged by certain providers or in certain product lines (e.g. fringe credit) could be more effectively dealt with via specific enforcement action of existing provisions and the unconscionability tests.

(c) Low and No Interest Loan Schemes

Mutual ADIs have a long-standing commitment to providing banking and financial services to low-income earners or people with financial difficulties. *Abacus* would welcome proposals to consider options for providing funding or other support for no and low interest loan schemes in Queensland. Additional support in the delivery of these services to their local community would certainly assist mainstream providers.

Abacus notes that a particular issue for ADIs is the need to ensure their capital provisions under the Banking Act 1959 satisfy APRA's prudential standards. This includes provisioning against NILS-type schemes, which will be a direct cost to individual providers.

Abacus supports further discussion to explore low cost credit, how it can be funded and to whom it should be delivered. *Abacus* would be pleased to support consultation with interested credit unions and building societies on such proposals.

(d) Consumer education

Abacus supports measures that provide relevant, useful and practical information to consumers. There is a wealth of existing work by credit unions and building societies in terms of life-event and other targeted financial literacy initiatives. Further, *Abacus* provides a series of award-winning financial literacy books called Take Control. Titles address a wide range of issues but include managing credit and dealing with debt. These publications were recognised with a Fair Trading Award in NSW in 2004 and were provided to the Financial Literacy Foundation (FLF) for their Understanding Money campaign.

Attention should also be given to financial literacy measures that address saving and budgeting and the responsible use of credit. Such messages are likely to be more effective in protecting vulnerable consumers by equipping them with information to protect their own interests than seeking to limit the activities of individual fringe providers. At any rate, these strategies should be undertaken concurrently.

Another key educative message is to encourage consumers to approach their mainstream lenders if or when they experience financial stress or difficulties. This is preferable to exposure to further debts or the sharp practices of opportunistic lenders.

(e) Government regulation

The particular option suggested is the introduction of an interest rate cap. *Abacus* has a number of reservations about the use of caps as a broad regulatory response to activities by fringe credit providers.

In NSW, the cap includes the total cost of credit, thus capturing payday lenders extending their terms beyond the 62-day threshold or loading costs into fees and charges. Importantly, the regime exempts temporary overdraft facilities and the overdrawing of a line of credit provided by mainstream ADI lenders. The sensible relief provided to mainstream ADI lenders is critical and should be introduced in Queensland if an interest rate cap were adopted. Additionally, Queensland should learn from the avoidance techniques fringe lenders adopted in NSW to bypass UCCC coverage.

Conversely, *Abacus* notes that on their own interest rate caps are no panacea. The *Report of the Consumer Credit Review* in Victoria observed that:

It is recognised that applying the Code and imposing an inclusive interest rate cap would not necessarily arrest the cost of this form of credit, since default and other contingent charges are a significant part of the problem.

Additionally, the Victorian review noted that the national fringe credit proposals opted against recommending a national uniform interest rate ceiling because interest rates are outside the *Uniformity Agreement*. Although interest rate ceilings in some jurisdictions will not offend the *Uniformity Agreement*, they can pose compliance challenges for small amount lenders that operate across State and Territory borders.

Further, the NSW model where the interest rate cap incorporates credit fees and charges is nevertheless a break from the UCCC. The UCCC is not a tool for imposing restrictions on credit fees and charges, though it does contain a power to prohibit particular fees or

charges. For credit unions and building societies, the prospects of several jurisdictions imposing a cap on the total cost of credit risks undermining the uniformity of the UCCC.

Conclusion

Credit unions and building societies are committed to protecting the best interests of their members and will assist members facing financial difficulties. But credit unions and building societies also believe that the provision of credit must be equitable to both parties and support the operation of an effective and competitive market.

Thank you again for the opportunity to comment. *Abacus* looks forward to being included in further consultations and to learning the outcomes of this review.

In the meantime if you would like further information about *Abacus* or the comments in this response then please contact me on (02) 8299 9033 or at jmoyes@Abacus.org.au.

Yours sincerely,



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