LawRight Submission 30 July 2019

Submission to Australian Securities and Investment Commission's consultation paper on its product intervention power in Pt. 7.9A of the *Corporations Act 2001*

About LawRight

LawRight is an independent community legal centre and the leading facilitator of pro bono legal services in Queensland, directing the resources of the private legal profession to increase access to justice.

About the Homeless Person's Legal Clinic

The Homeless Persons' Legal Clinic was established in 2002 by LawRight to provide free legal assistance and representation to people experiencing or at risk of homelessness. Our outreach model has since expanded and we now also coordinate the Mental Health Civil Law Clinic and the Refugee Civil Law Clinic.

In the 2018/2019 financial year, Homeless Persons' Legal Clinic provided ongoing legal assistance in 434 matters and 186 advices to clients attending a drop-in clinic.

Many HPLC clients experience several forms of disadvantage including mental illness, severe financial hardship, addiction, physical or intellectual disabilities and complex family backgrounds.

Summary of submissions

Our experience in assisting clients with credit provided by Gold-Silver Standard Finance and its associate Cigno Loans Pty Ltd (collectively **Cigno**) poignantly demonstrates the need to restrict the operation of a short term lending model. Our submissions include direct insights into the impact short term credit can have on vulnerable members of our community.

Informed by the experiences of our clients, LawRight:

- considers the short term lending model causes detriment to consumers and that the detriment is significant;
- supports ASIC's proposal to make a product intervention order by legislative instrument under s1023D(3) of the *Corporations Act* 2001 in relation to short term lending models;
- recommends ASIC adopt Option 1 as outlined in Consultation Paper 316 Using the product intervention power: Short term credit (the **Consultation Paper**).

Submissions

1. Detrimental impact of the short term lending model

C1Q1: We consider the short term lending model causes detriment to consumers and that the detriment is significant.

C1Q2: We consider that ASIC has accurately indentified the detriment caused by the short term lending model as outlined in the Consultation Paper.

The detrimental impact of small amount, short term lending at high cost is well established. Counterintuitively, these types of loans often leave the borrower in a worse financial position[1]. Any influx of cash is short-lived, with consumers required to take on additional credit to meet the high costs of the loan, creating a cycle of hardship[2]. Unable to meet their obligations under the loan, borrowers can be left in substantial financial hardship, unable to pay for basic living expenses.

The negative financial impacts of small amount, short term credit is born out by both the research and our anecdotal experience assisting clients through the Homeless Persons' Legal Clinic.

The negative impacts are not limited to a person's financial circumstances. Financial pressures and debt can lead to poor health outcomes, including increases in depression, reduced psychological well-being, obesity and anxiety[3]. This is particularly true for unsecured debt, such as debt related to small amount, short term credit[4].

The short term lending model is designed to avoid the restrictions placed on lenders by the *National Consumer Credit Protection Act (2009)* (Act) and the Credit Code, deliberately circumventing protections afforded to vulnerable consumers, a point conceded by Cigno[5]. By evading these protections, the short term lending model causes additional detriment to vulnerable consumers, above and beyond the negative impact of other forms of small amount lending.

Specifically, the short term lending model avoids two key protections provided by the consumer credit legislation. The model allows a lender to:

- provide credit without assessing the borrowers capacity to meet their repayment obligations; and

[1] Financial Counselling Australia, Submission No 57 to the Senate Standing Committee on Economics, Inquiry into Credit and Financial Services Targeted at People in Financial Hardship (November 2018), 5; Paul Holmes, Legal Aid Queensland, cited in the Senate Standing Committees on Economics report '*Credit and financial services targeted at Australians at risk of financial hardship*', February 2019.
[2] J Gathergood, B Guttman-Kenney and S Hunt, 'How do payday loans affect borrowers? Evidence from the U.K market' (2018) 32 (2) *The Review of Financial Studies*, 496, 520.
[3] E Sweet, CW Kuzawa and TW McDadeT, 'Short-term lending: Payday loans as risk factors for anxiety, inflammation and poor health' (2018) 5 *SSM - Population Health,* 114, 114.
[4] Ibid, 115.
[5] In correspondence with our office, Cigno Pty Ltd stated the design of their service means 'the protections offered by the "Act" are not available to the client'.

- impose unreasonable fees and charges, above the amounts allowed by the Act.

By avoiding these protections, the short term credit model causes significant detriment to vulnerable consumers. We have discussed this in more detail below.

Failure to assess capacity to pay

Through our legal work, we have seen multiple clients provided with loans that would likely be considered unsuitable had an appropriate assessment of the consumer's capacity to repay been undertaken. The below examples illustrates this pattern of lending.

David* connected with LawRight through a homelessness support agency in a regional area. He had been homeless for a significant period, sometimes sleeping rough and sometimes staying in homeless hostels. Related to his period of homelessness and experience of trauma, David's physical and mental health was poor. Unemployed, David's only income was a basic Centrelink payment. He lived day-to-day and was in significant debt.

Cigno gave David $175 without completing an assessment of his capacity to repay the loan or its suitability under the Act. David defaulted immediately but made sporadic payments when he could.

By the time he saw LawRight, David had paid Cigno over $400. However, the various dishonour and account keeping fees amounted to over $1,400. David was asked to pay over $1,200 to finalise the debt, approximately 700% of the original loan.

A failure to adequately assess the suitability of a loan has two significant consequences:

- consumers can be provided loans for amounts they cannot repay or that do not meet their needs; and
- the repayment arrangements can be structured in inappropriate and unaffordable ways, without regard to a consumers ability to meet their repayment obligations.

The short term lending model limits the length of the loan to a maximum of eight weeks. The service provider is not required to consider whether the consumer is able to make these payments or if a different arrangement with a lower fortnightly repayment may be in the consumer's interest.

Cigno further limits the loan length to four weeks for new clients. This reduces the service fees but increases the individual payment amounts. Existing clients may choose six or eight week repayment options, but pay higher fees, which incentivises consumers to take shorter loans with higher fortnightly payments.

Higher individual repayment amounts increase the likelihood the consumer would be unable to meet their obligations, increasing the chance the consumer will incur additional costs for defaulting under the agreement. The costs charged for default ensure that consumers are unable pay down the loan, thereby incurring more fees and charges: the debt spiral begins.

Lesley* is a single mother with significant, multiple heath concerns. She was a survivor of domestic violence and raised her child on a NewStart allowance.

At the time Cigno gave her a loan of $175 it completed an assessment of her bank account that showed she was overdrawn for 30% of the prior three months.

Despite this, under her agreement with Cigno Lesley was required to make four fortnightly payments of $93. Unsurprisingly, Lesley defaulted immediately.

By the time she saw LawRight, Lesley had paid Cigno $175. However, the various dishonour and account keeping fees amounted to over $950, which Lesley was asked to pay to finalise the debt, approximately 550% of the original loan.

Without an appropriate consideration of a consumer's capacity to repay, there is an increase in the likelihood of an unsuitable loan and the significant detriment caused by that loan. This is consistent with our experience representing vulnerable consumers.

Unreasonable fees and charges

The Consultation Paper outlines the fees and charges imposed under Cigno's service agreement. These fees are consistent with the fees and charges we have seen through our casework.

The cost of these loans is significantly more than that charged by lenders regulated by the Act. For example, in the event of default, a consumer can be charged $50 for a default letter plus a $49 default payment fee. Consumers are charged fees for phone contact and payment rescheduling. Unlike other lenders, these fees are not capped at twice the amount of the original loan[6].

Kurt* is a young aboriginal man with a long history of homelessness. He had been accessing homelessness services since the age of 16 after leaving a historically disadvantaged Aboriginal community.

Cigno failed to provide any evidence it had completed an assessment of Kurt's capacity to repay the loan or its appropriateness.

Kurt was unable to make any payments under the agreement. By the time he saw LawRight, Cigno was asking Kurt to pay over $900 to finalise the debt, approximately 500% of the original loan.

The fees charged under the small term lending model are exorbitant. For clients unable to meet the high repayment costs, the amount owed under the agreement can increase significantly over a short period of time. A vulnerable consumer can very easily find themselves in significant debt, which exacerbates their existing social, legal and financial problems.

[6] *National Credit Code* section 39b.

When she connected with LawRight, Jenny* was over $8,000 in debt to a variety of non-traditional lenders including small amount credit providers, high interest lenders and pawnbrokers.

Her income was a Newstart allowance, she was supported by a women's support service and she spoke English as a second language. Her financial position had been dire for some time.

Cigno gave Jenny $120 without a formal assessment of her capacity to repay the loan or its suitability under the Act. Jenny defaulted immediately but made sporadic payments when she could.

By the time she saw LawRight, Jenny had paid Cigno $180. However, the various dishonour and account keeping fees amounted to over $1,200. Jenny was asked to pay over $1,150 to finalise the debt, approximately 900% of the original loan.

2. Alternative options: accessing other services

C1Q3: We agree with ASIC's proposal to make an intervention order by way of legislative intervention prohibiting credit providers and their associates from providing short term credit and collateral services except in accordance with a condition which limits the total fees that can be charged.

C1Q4: We consider the alternative options proposed by ASIC in the Consultation Paper would be unlikely to achieve the identified objectives of preventing detriment to vulnerable consumers.

Many of our clients access short term credit to fund everyday living costs such as food, accommodation, bills or outstanding accounts, and clothing. This is further supported by the research in this area[7]. When accessing credit to meet basic and immediate needs, a consumer's priorities are for easy and fast access to necessary funds. Given this, a consumer will preference arrangements that provide immediate relief over options on more favourable terms.

In our experience, the alternative options presented by ASIC in the Consultation Paper do not provide a genuine alternative for vulnerable people seeking small amounts of credit in times of emergency. Many of our clients will already have accessed a Centrelink advance when seeking additional credit to cover basic living costs. Consumers are unlikely to take other options, including the No Interest Loan Scheme (NILS), where they are unable to access funds immediately.

Consumers typically access small amount credit to meet an immediate need despite knowing these loans are expensive or that other, less immediate, options may be available. This is evident in the short term lending model: consumers elect a more expensive option that provides immediate relief despite being made aware of an existing service where they

[7] Glasgow Centre for Population Health, 'Public Health Implications of payday lending' (2016) *Briefing Paper 48*, 9.

can access credit for a minimal cost (5% of the loan amount). The existing disclosure documents provided by Cigno clearly identify a cheaper but slower option. When you need to meet immediate essential needs, a notification or warning is unlikely to dissuade you from entering into an agreement, even if that agreement will inevitably place you in greater financial hardship.

We consider the alternative options proposed by ASIC in Consultation Paper would be unlikely to achieve the identified objectives of preventing detriment to vulnerable consumers.

We support ASIC's proposal to make an intervention order by way of legislative intervention prohibiting credit providers and their associates from providing short term credit and collateral services except in accordance with a condition which limits the total fees that can be charged.

Submissions made on 30 July 2019 to:

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