

**ASIC Consultation Paper 316 –
Using the product intervention
power: Short term credit**

Legal Aid NSW submission to ASIC
6 August 2019

About Legal Aid NSW

The Legal Aid Commission of New South Wales (**Legal Aid NSW**) is an independent statutory body established under the *Legal Aid Commission Act 1979* (NSW). We provide legal services across New South Wales through a state-wide network of 24 offices and 221 regular outreach locations, with a particular focus on the needs of people who are socially and economically disadvantaged.

We assist with legal problems through a comprehensive suite of services across criminal, family and civil law. Our services range from legal information, education, advice, minor assistance, dispute resolution and duty services, through to an extensive litigation practice. We work in partnership with private lawyers who receive funding from Legal Aid NSW to represent legally aided clients.

We also work in close partnership with LawAccess NSW, community legal centres, the Aboriginal Legal Service (NSW/ACT) Limited, pro bono legal

services and 29 Women's Domestic Violence Court Advocacy Services.

The Legal Aid NSW Civil Law Division focuses on legal problems that impact most on disadvantaged communities, such as credit, debt, housing, employment, social security and access to essential social services.

Should you require any further information regarding this submission, please contact:

[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

or

[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

Introduction

Legal Aid NSW welcomes the opportunity to contribute to the Australian Securities and Investments Commission's (**ASIC**) Consultation Paper 316 (**CP316**) regarding ASIC's proposed use of the product intervention power in relation to short term credit.

Legal Aid NSW strongly supports proposed Option 1 set out in CP316—that ASIC make a product intervention order by legislative instrument under s1023D(3) of the *Corporations Act 2001* (Cth) to prohibit 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. Legal Aid NSW considers that this is the most effective means of addressing the issues of the short term lending model as identified in CP316 and the detriment it is causing consumers, on an industry wide basis.

This submission outlines Legal Aid NSW's casework experience in respect of the short term lending model, and answers the consultation questions in CP316.

Legal Aid NSW's experience

Recent rise in clients seeking assistance with short term loans

Over the last 18 to 24 months, Legal Aid NSW has seen a rise in clients seeking legal assistance after entering into agreements with short term lenders and subsequently experiencing increased financial hardship. These agreements are in the form of the short term lending model described by ASIC in CP316.

We are aware of two companies that are currently using the short term lending model (**short term lenders**) described by ASIC in CP316. We are aware of two other companies that have previously used this model, which we understand are no longer operating.

Unsuccessful attempts to address conduct

Legal Aid NSW notes that the lending model used by the short term lenders attempts to avoid the safeguards prescribed in the *National Consumer Credit Protection Act 2009* (Cth) (**Credit Act**), which sets a cap on costs and a limit on fees that credit providers can charge consumers for small amount credit contracts. This is despite recent amendments to the *National Consumer Credit Protection Regulation 2010* (Cth) that sought to address particular gaps in the legislation.¹

Specifically, the amendments:

- Confirmed that credit providers (and third-parties) cannot rely on the provision for short-term credit in the Credit Act, which provides that the National Credit Code (Schedule 1 to the Credit Act) (**NCC**) does not apply to the provision of short-term credit contracts. This addressed the practice of some credit providers who remained

¹ *National Consumer Credit Protection Amendment (Small Amount Credit Contracts) Regulation 2014* (Cth).

unlicensed while levying fees and charges in excess of the cap on costs for small amount credit contracts.

- Ensured that where short-term credit is provided to consumers, no additional amounts can be charged above 5% of the amount of credit, and that interest is capped at 24%.²

Despite these amendments, the short term lenders continue to offer credit with a cost rate far in excess of what the NCC intended.³

Key concerns from our casework

In our experience, these short term lenders lend to some of the most vulnerable consumers, most of whom are already experiencing financial difficulty. These include young people, homeless people, people with disability and people whose only source of income is Centrelink payments.

Our clients commonly present with the following problems arising from this short term lending model:

1. They do not understand the full extent of fees and charges payable under the agreements, and are shocked when told that their small principal sums have escalated to debts that amount to hundreds of dollars.
2. They have low incomes and very little or no capacity to repay the loan.
3. They generally default on repayments quickly and are charged high fees.
4. The short term lenders continue to attempt to debit their accounts. This often results in negative account balances, additional bank dishonour fees and debt spirals if clients seek to obtain new loans to repay their debts.
5. Some people are repeatedly contacted by debt collectors demanding payments on behalf of the short term lenders.

In addition, Legal Aid NSW solicitors have encountered significant difficulty contacting the short term lenders, including long periods of time on hold (in one instance our solicitor waited on hold for four hours) only to have no one answer.

The short term lenders that we are aware of both state in their Disclosures and Authorisations document that while not covered by the NCC “*they both have adopted the protections afforded by the Act they believe to be best practice and where practicable have sought to manifest those principles in their service*”. It is not clear what ‘protections’ and ‘best practice’ have been adopted, aside from having an internal dispute resolution policy.

Examples of our clients’ experiences

The below case studies are a small portion of Legal Aid NSW’s experience assisting clients with loans from short term lenders. They demonstrate the short term lenders’ practice of giving high cost loans to vulnerable people who are already experiencing financial difficulty.

² Explanatory Statement on *National Consumer Credit Protection Amendment (Small Amount Credit Contracts) Regulation 2014* (Cth)

³ Schedule 1, *National Consumer Credit Protection Act 2009* (Cth)

Case Study 1

A 23 year old homeless male with Newstart as his sole source of income obtained a \$200 loan through the short term lenders after a friend told him how “easy” it was to get. The total repayment, including lender fees, a supply fee and account keeping fees, was to be \$291.90, provided he repaid the loan within two weeks.

Our client provided bank statements to the short term lenders to assess his loan application, which showed that he had a negative balance for one third of the 90 day statement period. The statements also showed that he was already in default on another small amount credit contract at the time of his application.

Our client defaulted on repayments and after the short term lender made numerous attempts to direct debit his account, the total debt rose to \$1,121.70, and his account had a negative balance.

By the time he saw Legal Aid NSW, around nine months after obtaining the loan, he had already repaid a total of \$490 and was experiencing ongoing financial hardship.

The short term lender defended the decision to lend to this client, claiming that he met their criteria and they deemed the loan “suitable”.

Case Study 2

An 18 year old Aboriginal female with an intellectual disability living in supported youth accommodation obtained a loan from the short term lenders just days after turning 18. Her only income was the disability support pension and after paying her rent and other deductions she received a net income of \$323.40 per fortnight.

The principal loan sum was \$150, and with the additional fees and charges sought by the short term lenders the total repayment came to \$237.90, which represented 72% of her total net income. Unaware that she had elected a once only repayment, the total was debited from her account, leaving her with a negative balance.

Legal Aid NSW contacted the short term lender and informed them that our client:

- had an intellectual disability
- could not afford to feed herself and was seeking food vouchers
- would not receive any further income for another two weeks and due to the negative balance would be left with only \$254.23 net income for the following two weeks.

The short term lender refused to refund any portion of the payment and four days after being notified of our client’s circumstances, the short term lender provided her with a further loan of \$120. Along with the fees and charges the total repayable amount was \$184.

The short term lender agreed to finalise these matters on terms favourable to our client.

Case Study 3

A 38 year old woman whose sole source of income was the Disability Support Pension for multiple mental health issues, and who had a history financial management orders, obtained a loan from the short term lenders of \$250. Added to this was a financial supply fee of \$187.50, a lender fee of \$12.50 and ongoing account keeping fees of \$5.95 per week for both companies operating the short term lending model.

The client missed her repayments on the loan almost immediately and the debt grew to a total of \$832.75 (including one repayment made by our client). Of that total, \$582.75 were fees. The account was then passed on to debt collectors.

Case Study 4

A 43 year old woman with significant health problems and whose sole source of income was the Disability Support Pension obtained a loan from the short term lenders for \$175. A lender fee of \$8.75 was added, plus a financial supply fee of \$78.75 and account fees of \$19.80. The total expected repayment was \$282.30 over 28 days.

Our client obtained this loan after receiving emails from the short term lenders telling her she could receive a "CASH loan TODAY". Under a heading "How it Works" she was told:

1. Complete the **3 minute application**.
2. We'll contact you with your APPROVAL and AMOUNT.
3. Receive funds in your account TODAY.

Approximately two hours after our client received this email, she received another email telling her "you have been Pre-Approved for a loan!" Within about four hours she had her final approval. Our client immediately defaulted on the repayments and within two months the total owing had risen to \$853.10.

While being pursued for the debt our client received correspondence with a heading that stated: "*THIRD AND FINAL NOTICE LEGAL ACTION: INVESTIGATION PENDING*" stating that: "*if you do not make contact with us, we have no alternative but to commence an investigation to determine whether the information you provided, including your financial situation, was correct and accurate at the time of taking the loan. Our decision was based on that information and misrepresentation will be regarded as extremely serious.*"

The same letter suggested that if "*you have multiple little debts and a consolidation loan would help you, then through our financial associate company Gold-Silver Standard Finance Pty Ltd or another lender we can apply for a consolidation loan of up to \$5000 to cover all of your debts.*"

Around two weeks later she received further advertising from the short term lender encouraging her to investigate further lending.

As a result of multiple debts our client entered into bankruptcy.

ASIC's proposal and feedback questions

C1Q1 Do you consider that the short term lending model causes detriment to consumers and that this detriment is significant?

Legal Aid NSW agrees with all of the reasons that are set out by ASIC 15 at paragraph [43] of CP316, that the short term lending model causes significant detriment to consumers, including severe financial hardship. This is also supported by the above case studies.

Financial stress can cause further deterioration in the sometimes already fragile state of our clients' lives and also negatively affects their families. For example, a largescale study by researchers from the University of Melbourne found that financial hardship negatively impacts on physical and mental health and overall quality of life. It also found that its impacts are experienced with greater severity by people who are Centrelink recipients and people with long-term debt problems.⁴

C1Q2 Do you consider that the short term lending model does or might cause detriment other than that identified by ASIC, or to a greater or lesser extent? If additional or greater, how should the proposed product intervention order be expanded to address this significant detriment?

Yes, Legal Aid NSW draws ASIC's attention to the debt collection activity conducted the short term lenders post default and in particular, the correspondence at Case Study 4 above.

This case study shows the short term lenders engaging in high pressure and intimidating collections activity. In this instance the short term lenders threatened a customer in default with "legal action" consisting of an "investigation" into whether they properly reported their financial details, and then suggested the client may need a larger loan to cope with their situation. This conduct increases pressure on already vulnerable consumers and encourages them to get further into debt as a way to resolve their situation.

However, Legal Aid NSW does not consider that the proposed product intervention order needs to be expanded. If the short term lending model is prohibited, we consider that there will be less risk of, and opportunity for, this type of conduct.

⁴ Evgenia Bourova et al, 'The Experience of Financial Hardship in Australia: Causes, Impacts and Coping Strategies' (2019) Vol 42, No. 2, *The Journal of Consumer Policy*, 26.

C1Q3 Do you agree with our 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? Please provide details of why, or why not.

Legal Aid NSW supports ASIC's proposal to make a product intervention order 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 to the maximum amount permitted under section 6(1) of the NCC. We consider this to be the most effective of all three proposed options. This approach is likely to be effective in prohibiting current short term lenders from using the short term lending model, and prevent other credit providers from adopting the same model.

Legal Aid NSW would ultimately prefer for short term credit to be covered by the NCC and therefore subject to responsible lending and small amount credit contract provisions. As well as preventing short term lenders from using the short term lending model, this would also extend consumer protections to all forms of short term credit. However, this would require legislative change and is unlikely to be supported across the industry. In our view, option 1 is a faster and more straightforward means of addressing the significant consumer detriment caused by the short term lending model.

C1Q4 What alternative approaches (including Options 2 and 3) could ASIC take that would achieve our objectives of preventing the consumer detriment identified in this paper?

In our view options 2 and 3 will not be effective in preventing the substantial consumer detriment caused by the short term lending model.

Option 2

In our experience, clients who use loans from short term lenders, and other forms of high cost credit, do so because they need funds quickly and generally cannot access other forms of mainstream credit. The alternative options listed, including the No Interest Loans Scheme (NILS), Centrelink advances and hardship arrangements, generally do not yield results as quickly as high cost credit. They can also be restricted in scope, making them less attractive to vulnerable consumers urgently in need of funds.

We are aware of one short term lender that already includes a standard warning about their loans and information about alternative options in its Disclosures and Authorisations document. This has not prevented consumers from using the short term lending model product, or the significant consumer detriment identified by ASIC.

We support raising consumer awareness of financial counselling and alternatives to high cost credit. However, we agree that disclosure, even if more prominent than the current

warning used by the short term lenders, would not materially reduce the number of consumers who are affected by the short term lenders' conduct.

Option 3

We do not support the status quo option and agree with the reasons provided by ASIC at paragraph [87] of CP316. This option would likely lead to an increasing number of consumers suffering significant detriment from the short term lending model used by short term lenders currently operating, and also risks other businesses adopting the same model.