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NCP Review of the Consumer Credit Code

FINAL REPORT

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Contents

1 Executive summary 9
1.1 Introduction 9
1.2 Consultation process 9
1.3 The consumer credit industry 9
1.4 The Consumer Credit Code 10
1.5 Objectives of the Consumer Credit Code 11
1.6 Scope of the Consumer Credit Code 11
1.7 Consistency with competition legislation 12
1.8 Restrictions on competition 12
1.9 Reform options 13
1.10 Analysis of reform options 14
1.11 Conclusion 14

2 Introduction 15
2.1 Structure of the report 15
2.2 Scope of work completed 17
2.3 Vote of thanks 18
2.4 Warranties and disclaimer 18

3 National Competition Policy legislation review methodology 19
3.1 Background to National Competition Policy 19
3.2 Public interest test 20
3.3 Review process 21
3.4 Terms of reference 21
3.4.1 Object of review 21
3.4.2 Competition Policy issues to be addressed 21
3.4.3 Other considerations 22
3.5 NCP legislation review guidelines 23

4 The consumer credit industry 24
4.1 Overview of the credit industry 24
4.1.1 Key factors influencing credit trends 24
4.2 Consumer credit purposes 26
4.3 Supply of consumer credit 26
4.3.1 Industry structure 27
4.3.2 Consumer credit market share 28
4.4 Consumer credit product attributes and characteristics 29
4.4.1 Housing Loans 31

4.4.2 Personal Loans 32
4.4.3 Credit Cards 32
4.5 Pricing 32
4.6 Forces driving change in the consumer credit industry 33
4.6.1 Deregulation 33
4.6.2 Technological change 34
4.6.3 Product innovation 37
4.7 Summary 38

5 The Consumer Credit Code legislation 40
5.1 History of consumer credit regulation 40
5.1.1 The Credit Acts 42
5.1.2 The Consumer Credit Code 43
5.1.3 Key reforms under the Consumer Credit Code 43
5.2 Market theory and consumer protection legislation 45
5.3 How the Consumer Credit Code addresses failures in the consumer credit market 46
5.4 Description of the Consumer Credit Code 49
5.4.1 Part 1 – Preliminary 49
5.4.2 Part 2 – Credit contracts 49
5.4.3 Part 3 – Related mortgages and guarantees 50
5.4.4 Part 4 – Changes to obligations under credit contracts, mortgages and guarantees 50
5.4.5 Part 5 – Ending and enforcing credit contracts, mortgages and guarantees 51
5.4.6 Part 6 – Civil penalties for defaults of credit providers 51
5.4.7 Part 7 – Related sale contracts 52
5.4.8 Part 8 – Related insurance contracts 53
5.4.9 Part 9 – Advertising and related conduct 53
5.4.10 Part 10 – Consumer leases 53
5.4.11 Part 11 – Miscellaneous 54
5.5 Administration and differences across jurisdictions 54
5.6 Review of Consumer Credit Code consistency with part IV of the Trade Practices Act 1974 and the Competition Codes 56
5.6.1 Trade Practices Act 1974 56
5.6.2 Competition Codes 57

6 Post Implementation Review 59
6.1 Introduction 59
6.2 Summary of recommendations 59
6.3 Competition issues of proposed amendments 64
6.4 Summary 66

7 Public consultations and submissions 67
7.1 Introduction 67
7.2 Key stakeholders 67
7.3 Consultation process 67
7.3.1 Call for submissions 67
7.3.2 Targeted stakeholder consultations 68
7.4 Summary 68

8 Objectives of the Consumer Credit Code 69
8.1 Clarification of the objectives 69
8.2 Relevance and appropriateness of the objectives 69
8.3 Conclusion 71

9 Definitions and exemptions 73
9.1 Definitions 73
9.1.1 ‘Credit’ and ‘amount of credit’ 73
9.1.2 ‘Credit contract’ 74
9.1.3 ‘Mortgage’ and ‘guarantee’ 76
9.1.4 ‘Goods lease’ 77
9.2 Exemptions 77
9.3 Credit classes exempted by the regulations 81
9.4 Corporate Law Economic Reform Program (CLERP) 84
9.5 Summary 84

10 Identification and classification of restrictions 86
10.1 Identification of restrictions on competition 86
10.2 Classification of restrictions on competition 86
10.3 Summary of restrictions 87

11 Description of regulatory reform options 88
11.1 Option 1 – Status quo 88
11.2 Option 2 – Amended status quo 88
11.3 Option 3 – Industry deregulation 88
11.4 Option 4 – Mandatory Code of Conduct 89

12 Restriction 1: Part 2 disclosure requirements 93
12.1 Introduction 93
12.2 Nature of Restriction 1 93
12.3 Key issues raised in submissions and consultation 94
12.4 Classification of Restriction 1 95
12.5 Reform options for Restriction 1 96
12.5.1 Option 1 – Status quo / cost-benefit analysis 96

12.5.2 Option 2 – Amended status quo 101
12.6 Post Implementation Review Recommendations 103
12.7 Conclusions 104
12.8 Additional comments on Restriction 1 105

13 Restriction 2: Part 2 product innovation restrictions 106
13.1 Introduction 106
13.2 Nature of Restriction 2 106
13.3 Key issues raised in submissions and consultation 107
13.4 Classification of Restriction 2 107
13.5 Reform Options for Restriction 2 107
13.5.1 Option 1 – Status Quo / Cost-benefit analysis 108
13.5.2 Option 2 – Amended status quo 109
13.6 Post Implementation Review Recommendations 109
13.7 Conclusions 109

14 Restriction 3: Part 3 disclosure requirements 110
14.1 Introduction 110
14.2 Nature of Restriction 3 110
14.3 Key issues raised in submissions and consultation 111
14.4 Classification of Restriction 3 111
14.5 Reform Options for Restriction 3 111
14.5.1 Option 1 – Status quo / Cost-benefit analysis 111
14.5.2 Option 2 – Amended status quo 113
14.6 Post Implementation Review Recommendations 113
14.7 Conclusions 113

15 Restriction 4: Part 3 product innovation restrictions 114
15.1 Introduction 114
15.2 Nature of Restriction 4 114
15.3 Key issues raised in submissions and consultation 114
15.4 Classification of Restriction 4 115
15.5 Reform Options for Restriction 4 115
15.5.1 Option 1 – Status quo / Cost-benefit analysis 115
15.5.2 Option 2 – Amended status quo 116
15.6 Post Implementation Review Recommendations 116
15.7 Conclusions 117

16 Restriction 5: Part 4 disclosure requirements 118
16.1 Introduction 118
16.2 Nature of Restriction 5 118
16.3 Key issues raised in submissions and consultation 119

16.4 Classification of Restriction 5 119
16.5 Reform Options for Restriction 5 120
16.5.1 Option 1 – Status Quo / Cost-benefit analysis 120
16.5.2 Option 2 – Amended status quo 121
16.6 Post Implementation Review Recommendations 121
16.7 Conclusions 121

17 Restriction 6: Part 4 potential compliance costs 122
17.1 Introduction 122
17.2 Nature of Restriction 6 122
17.3 Key issues raised in submissions and consultation 123
17.4 Classification of Restriction 6 123
17.5 Reform Options for Restriction 6 124
17.5.1 Option 1 – Status quo / Cost-benefit analysis 124
17.5.2 Option 2 – Amended status quo 125
17.6 Post Implementation Review Recommendations 126
17.7 Conclusions 126

18 Restriction 7: Part 5 potential compliance costs 127
18.1 Introduction 127
18.2 Nature of Restriction 7 127
18.3 Key issues raised in submissions and consultation 128
18.4 Classification of Restriction 7 129
18.5 Reform Options for Restriction 7 129
18.5.1 Option 1 – Status quo / Cost-benefit analysis 129
18.5.2 Option 2 – Amended status quo 131
18.6 Post Implementation Review Recommendations 131
18.7 Conclusions 131

19 Restriction 8: Part 6 potential compliance costs 133
19.1 Introduction 133
19.2 Nature of Restriction 8 133
19.3 Key issues raised in submissions and consultation 135
19.4 Classification of Restriction 8 136
19.5 Reform Options for Restriction 8 136
19.5.1 Option 1 – Status quo / Cost-benefit analysis 136
19.5.2 Option 2 – Amended status quo 137
19.6 Post Implementation Review Recommendations 137
19.7 Conclusions 138

20 Restriction 9: Part 7 discrimination between credit providers 139
20.1 Introduction 139

20.2 Nature of Restriction 9 139
20.3 Key issues raised in submissions and consultation 140
20.4 Classification of Restriction 9 140
20.5 Reform Options for Restriction 9 140
20.5.1 Option 1 – Status quo / Cost-benefit analysis 141
20.5.2 Option 2 – Amended status quo 141
20.6 Post Implementation Review Recommendations 142
20.7 Conclusions 142

21 Restriction 10: Part 7 third line forcing restrictions 143
21.1 Introduction 143
21.2 Nature of Restriction 10 143
21.3 Key issues raised in submissions and consultation 143
21.4 Classification of Restriction 10 143
21.5 Reform Options for Restriction 10 144
21.5.1 Option 1 – Status quo / Cost-benefit analysis 144
21.5.2 Option 2 – Amended status quo 144
21.6 Post Implementation Review Recommendations 145
21.7 Conclusions 145

22 Restriction 11: Part 8 third line forcing restrictions 146
22.1 Introduction 146
22.2 Nature of Restriction 11 146
22.3 Key issues raised in submissions and consultation 146
22.4 Classification of Restriction 11 147
22.5 Reform Options for Restriction 11 148
22.5.1 Option 1 – Status quo / Cost-benefit analysis 148
22.5.2 Option 2 – Amended status quo 149
22.6 Post Implementation Review Recommendations 149
22.7 Conclusions 149

23 Restriction 12: Part 8 pricing restrictions 151
23.1 Introduction 151
23.2 Nature of Restriction 12 151
23.3 Key issues raised in submissions and consultation 151
23.4 Classification of Restriction 12 151
23.5 Reform Options for Restriction 12 152
23.5.1 Option 1 – Status Quo / Cost-benefit analysis 152
23.5.2 Option 2 – Amended status quo 153
23.6 Post Implementation Review Recommendations 153
23.7 Conclusions 153

24 Restriction 13: Part 9 conduct restrictions 154
24.1 Introduction 154
24.2 Nature of Restriction 13 154
24.3 Key issues raised in submissions and consultation 155
24.4 Classification of Restriction 13 155
24.5 Reform Options for Restriction 13 156
24.5.1 Option 1 – Status Quo / Cost-benefit analysis 156
24.5.2 Option 2 – Amended status quo 158
24.6 Post Implementation Review Recommendations 158
24.7 Conclusions 158

25 Restriction 14: Part 10 disclosure requirements 160
25.1 Introduction 160
25.2 Nature of Restriction 14 160
25.3 Key issues raised in submissions and consultation 160
25.4 Classification of Restriction 14 161
25.5 Reform Options for Restriction 14 161
25.5.1 Option 1 – Status quo / Cost-benefit analysis 161
25.5.2 Option 2 – Amended status quo 162
25.6 Post Implementation Review Recommendations 162
25.7 Conclusions 163

26 Restriction 15: Part 10 potential compliance costs 164
26.1 Introduction 164
26.2 Nature of Restriction 15 164
26.3 Key issues raised in submissions and consultation 164
26.4 Classification of Restriction 15 164
26.5 Reform Options for Restriction 15 165
26.5.1 Option 1 – Status quo / Cost-benefit analysis 165
26.5.2 Option 2 – Amended status quo 166
26.6 Post Implementation Review Recommendation 166
26.7 Conclusions 167

27 Fair trading outcomes 168
27.1 The need for the Consumer Credit Code 168
27.2 Summary 170

28 Conclusions 171

References 172

Glossary of terms 174

Appendix A – Overview of the Consumer Credit Code 178

Appendix B – Legislation by jurisdiction 192

Appendix C – Summary of submissions and targeted consultations 201

1 Executive summary

1.1 Introduction

The Competition Principles Agreement (the 'Agreement'), endorsed by members of the Council of Australian Governments in April 1995, commits the governments to undertake by the end of the year 2000 a review of all potentially anti-competitive legislation.

The Agreement requires that legislation should not restrict competition unless it can be demonstrated that the benefits to the community as a whole outweigh the costs of such restriction(s), and that the objectives of the legislation can only be achieved by restricting competition.

All States and Territories are party to the Australian Uniform Credit Laws Agreement 1993. The essence of the agreement is the introduction and maintenance of consumer credit laws, which apply equally to all forms of consumer lending, and which are uniform in all jurisdictions.

In accordance with each State and Territory's obligations under the National Competition Policy Package, this review will examine the case for reform of legislative and regulatory restrictions made under or in relation to the Consumer Credit Code.

KPMG Consulting (KPMG) were retained by the Standing Committee of Officials of Consumer Affairs (SCOCA) to conduct the National Competition Policy review of the Consumer Credit Code as an independent party and to prepare a report based on the assessment of the issues raised by the terms of reference.

1.2 Consultation process

An Issues Paper prepared by KPMG outlined the background to the review, detailed the restrictive provisions contained within the Consumer Credit Code, provided alternatives to the current regulatory framework and invited submissions from interest parties. This Issues Paper was forwarded to all known interested stakeholders and was made available online through the Consumer Credit Code's website. A number of targeted consultations were also conducted with key industry associations and consumer advocacy groups.

1.3 The consumer credit industry

The key features and characteristics of the market in which the Consumer Credit Code operates are:

- A wide range of products fall within the category of consumer credit, including housing loans, mortgages, personal loans, credit cards and leases;

- Household debt levels have increased significantly in the last 10 to 15 years, reflecting changing attitudes, financial deregulation, and low inflation and interest rates;
- Consumer credit is used predominantly for housing, which accounts for almost 80% of the value of credit provided;
- There are a large number of credit providers in Australia, including banks, building societies, credit unions and other financiers, such as finance companies;
- Banks are the main providers of consumer credit, accounting for more than 80% of consumer credit;
- A number of functional variables apply across the range of consumer credit products. That is, consumer credit may be revolving or fixed, secured or unsecured, loan or sale credit, and may have a combination of fixed and variable costs;
- The cost of credit comprises interest charges, which apply to all credit products, and non-interest charges, such as loan application fees and annual fees;
- Over the last decade, non-interest income has represented an increasing proportion of total income. However, fees represent less than 1% of the cost of consumer credit;
- Deregulation, technological change and product innovation are the key forces driving change in the consumer credit industry;
- Technological developments have significantly reduced transaction costs, but there are equity issues in relation to access to new technology;
- Electronic transactions legislation, which recognises electronic documents and digital signatures, is expected to be introduced in each jurisdiction; and
- Product innovation has led to a wide range of product attributes, rather than an increase in the main credit product categories.

1.4 The Consumer Credit Code

The Consumer Credit Code governs the provision of information and the conduct of credit providers in relation to the provision of consumer credit. In particular, the Consumer Credit Code governs:

- Information disclosure to debtors, guarantors and mortgagors at the pre-contractual stage, the contractual stage and throughout the life of the credit contract;
- Notification of any changes under the credit contract to the debtor;
- Redress mechanisms, where credit providers do not comply with the legislation;

- Linked credit providers;
- Related insurance contracts;
- Advertising; and
- Consumer leases.

The justification for government involvement (through legislation) in this particular case is two areas of market failure in the consumer credit industry, being:

- Inadequate disclosure of information or information asymmetries between credit providers and consumers; and
- Unfair or fraudulent conduct by market participants.

1.5 Objectives of the Consumer Credit Code

The objectives of the Consumer Credit Code, as stated in the Explanatory Memorandum of the Queensland Act, are:

- To provide laws which apply equally to all forms of consumer lending and to all credit providers, and which are uniform in all jurisdictions in Australia.
- The legislation is based on the principle of truth in lending that will allow borrowers to make informed choices when purchasing credit.
- The Consumer Credit Code applies rules that regulate the credit provider's conduct throughout the life of the loan, but without restricting product flexibility and consumer choice.
- The policy of the legislation is to rely generally on competitive forces to provide price restraint but to provide significant redress mechanisms for borrowers in the event that credit providers fail to comply with the legislation.
- The Consumer Credit Code is designed to apply in a deregulated credit market and provide standards for the provision of credit that will not be overtaken by changes in the financial marketplace.

The review has indicated that these objectives are still relevant and appropriate in today's marketplace.

1.6 Scope of the Consumer Credit Code

The scope of the Consumer Credit Code is delineated by the definitions and exemptions outlined in Part 1 of the Consumer Credit Code.

Overall, the definitions and exemptions are appropriate to the objectives of the Consumer Credit Code. There are, however, a number of instances where credit, which is for all intents and purposes consumer credit, is outside the scope of the Consumer Credit Code. These include:

- Pay day lending;
- Terms sale of land;
- Conditional sale agreement;
- Tiny terms contracts; and
- Solicitor lending.

While CLERP 6, as initially promulgated would capture credit contracts not within the scope of the Consumer Credit Code, the Commonwealth Government, after hearing submissions from industry, determined that CLERP 6 would not be covering credit products at all.

Given that transactions that are for all intents and purposes a form of consumer lending should be within the ambit of the Consumer Credit Code, it is recommended that consideration be given to bringing the above transactions within the scope of the Consumer Credit Code.

1.7 Consistency with competition legislation

Part IV of the *Trade Practices Act 1974* and the Competition Codes deal with restrictive trade practices, and prohibit practices that may restrict competition in a market, including the practices of exclusive dealing and resale price maintenance.

The Consumer Credit Code was found to be consistent with the competitive conduct rules in Part IV of the *Trade Practices Act 1974* and the Competition Codes of each jurisdiction.

1.8 Restrictions on competition

Restrictions on competition contained within the Consumer Credit Code were identified using the tests contained in the Western Australia and Victorian guidelines for legislation reviews. This revealed that a substantial number of individual provisions could potentially restrict competition. These were grouped as follows:

- Restriction 1 – Part 2 disclosure requirements;
- Restriction 2 – Part 2 product innovation restrictions
- Restriction 3 – Part 3 disclosure requirements;

- Restriction 4 – Part 3 product innovation restrictions;
- Restriction 5 – Part 4 disclosure requirements;
- Restriction 6 – Part 4 potential compliance costs;
- Restriction 7 – Part 5 potential compliance costs;
- Restriction 8 – Part 6 potential compliance costs;
- Restriction 9 – part 7 discrimination between credit providers;
- Restriction 10 – Part 7 third line forcing restrictions;
- Restriction 11 – Part 8 third line forcing restrictions
- Restriction 12 – Part 8 pricing restrictions;
- Restriction 13- Part 9 conduct restrictions;
- Restriction 14 – Part 10 disclosure requirements; and
- Restriction 15 – Part 10 potential compliance costs.

Using the WA guidelines, Restrictions 1, 3, 8 and 14 were identified as major restrictions requiring more detailed analysis compared to the balance of restrictions, which were identified as minor.

1.9 Reform options

The options originally presented in the Issues Paper were further developed and defined during the review process. The actual options analysed in this review were:

Option 1 Status Quo, which is the retention of the Consumer Credit Code in its current form.

Option 2 Amended Status Quo, which proposes to reform individual provisions of the legislation by amending it.

Option 3 Industry Deregulation, which proposes to repeal the entire Consumer Credit Code and rely on market forces to restrain prices and the conduct of credit providers.

Option 4 Mandatory Code of Conduct, which proposes to replace the Consumer Credit Code with a mandatory Code of Conduct.

1.10 Analysis of reform options

Option 1, which proposed retaining the status quo, was analysed for each of the identified restrictions. This was found to be the most appropriate reform option for most of the restrictions analysed.

Option 2, which proposed amending specific provisions, was analysed in relation to Restriction 1 (Part 2 Disclosure requirements). It was proposed to reduce and simplify the disclosure requirements of credit contracts. However, it was dismissed on the basis that research conducted during the PIR and this review suggested that the amount of information provided to consumers was not the key issue. Rather, it is the timing and format of the information provided that is the most critical aspect of information disclosure from a consumer's perspective.

In this respect we considered that the PIR recommendations associated with the inclusion of a 'Schumer Box' in the credit contract documentation provided for a better outcome in terms of consumer protection than reform Option 2 for this restriction. That is, the analysis conducted to examine the viability of adopting Option 2 in relation to Restriction 1 (Part 2 Disclosure requirements) in the context of this NCP review actually reinforced the PIR recommendations relating to the inclusion of a 'Schumer Box' in contract documentation.

Option 3, which proposed industry deregulation was discounted on the basis that it does not provide a feasible alternative to the Consumer Credit Code. There are a number of consumer protection provisions that are not necessarily anti-competitive, but which would be lost if the Consumer Credit Code was repealed in its entirety.

Option 4, which proposed industry co-regulation through a mandatory Code of Conduct was discounted on the basis that, as it mirrored the provisions of the Consumer Credit Code, there would be little, if any, net gains for consumers. However, this reform option entailed significant administrative costs for the Commonwealth, State and Territory governments in relation to repealing the existing legislation, developing the Code of Conduct and the appropriate legislation and the transfer of administrative functions from the State and Territory governments to the AFIC.

1.11 Conclusion

In conclusion, the key recommendations of this review are:

1. Maintain the current provisions of the Consumer Credit Code and, as per the PIR, review the definitions of the Consumer Credit Code to ensure that terms sale of land, conditional sale agreements, tiny terms contracts and solicitor lending are bought within the scope of the Consumer Credit Code; and

2. Adopt PIR Recommendation 1.1 in order to enhance the disclosure provisions within Part 2 of the Consumer Credit Code.

2 Introduction

KPMG Consulting has been appointed by the Standing Committee of Officials of Consumer Affairs (SCOCA) to undertake a National Competition Policy (NCP) review of the Consumer Credit Code, which is the legislation governing the provision of consumer credit.

The NCP review has been undertaken in accordance with the Competition Principles Agreement and the following guidelines:

- The Council of Australian Governments' *Principles and Guidelines for National Standard Setting and Regulatory Action*;
- The Western Australian *Legislation Review Guidelines*;
- The *Guidelines to the Review of Legislative Restrictions on Competition* published by the Victorian Government;
- The *Consultation Framework for Review of Anti-Competitive Legislation* published by the NSW Government; and
- The Commonwealth Treasury's *Guidelines to Cost Benefit Analysis*.

2.1 Structure of the report

The report is structured as follows:

- Chapter 3: National Competition Policy

  This chapter provides a general overview of National Competition Policy and details the methodology used in this review.

- Chapter 4: The consumer credit industry

  This chapter provides an overview of the consumer credit industry and provides the background information to identify if market failures exist within the sector.

- Chapter 5: The Consumer Credit Code legislation

  This chapter provides information on the regulation of the consumer credit industry in Australia and examines how the Consumer Credit Code addresses the market failures present. It also considers the Consumer Credit Code's consistency with Part IV of the *Trade Practices Act 1974* and the Competition Codes.

- Chapter 6: Post Implementation Review

  This chapter considers the recommendations of the Post Implementation Review that potentially restrict competition.

- Chapter 7: Public consultations and submissions

  This chapter presents an overview of the public consultation process, which included a public notice calling for written submissions and a subsequent round of targeted consultations.

- Chapter 8: Objectives of the Consumer Credit Code

  This chapter clarifies the objectives of the Consumer Credit Code and examines their relevance and appropriateness to the consumer credit industry.

- Chapter 9: Definitions and exemptions

  Chapter 9 reviews the key definitions and exemptions contained in the Consumer Credit Code and makes an assessment as to their appropriateness in relation to the objectives of the Consumer Credit Code.

- Chapter 10: Identification and classification of restrictions

  This chapter presents an overview of the process used to identify and then classify the restrictions on competition contained within the Consumer Credit Code.

- Chapter 11: Description of regulatory reform options

  This chapter presents an overview of the reform options considered in this review and outlines the assumptions underpinning each of these reform options.

- Chapter 12: Restriction 1: Part 2 disclosure requirements

  Chapter 12 presents the analysis of Restriction 1. More specifically, the relevant sections of the Consumer Credit Code are identified, the nature of the restriction is examined, relevant issues raised in the consultation process are noted and the restriction is classified as major or minor. The benefits and costs of the restriction are then assessed before the appropriate reform options are considered. The relevant Post Implementation Review recommendations are also considered.

- Chapter 13 – 26: Restrictions 2 – 15

  Chapters 13 to 25 present Restrictions 2 to 15, respectively. Each restriction is analysed in the same manner as noted above for Restriction 1.

- Chapter 27: Fair trading outcomes

  Chapter 27 examines the need of the Consumer Credit Code in terms of achieving fair trading outcomes.

- Chapter 28: Conclusions

  This chapter presents the conclusions with respect to each reform options and highlights the key recommendations made.

- Glossary of Terms

  The Glossary of Terms defines terms commonly used in relation to consumer credit.

The supporting appendices provide a detailed overview of the Consumer Credit Code, a summary of the consumer credit legislation in each State and Territory and a summary of the issues raised in the submissions and targeted consultations.

2.2 Scope of work completed

In completing the NCP review of the Consumer Credit Code, KPMG:

- Reviewed the legislation to identify anti-competitive restrictions;
- Prepared an Issues Paper, advertised the availability of the Issues Paper and called for written submissions;
- Reviewed submissions received in response to the Issues Paper, as well as those received during the Post Implementation Review process;
- Conducted targeted consultations with key stakeholders;
- Discussed options for reform with the Steering Committee;
- Using secondary sources, analysed the consumer credit industry in Australia;
- Considered the competition policy implications of the recommendation of the Post Implementation Review;
- Assessed the consistency of the Consumer Credit Code with Part IV of the *Trade Practices Act 1974* and the Competition Codes in each jurisdiction;
- Reviewed the relevance of the objectives of the Consumer Credit Code;
- Assessed the nature, benefits and costs of each of the identified restrictions;
- Analysed the relative merits of less restrictive options for reform for each restriction; and
- Made recommendations as to the most appropriate reform options for the Consumer Credit Code.

2.3 Vote of thanks

KPMG Consulting would like to take this opportunity to thank individuals and organisations for their assistance in the review process, especially:

- Members of the Uniform Consumer Credit Code Management Committee; and
- Individuals and organisations that contributed during the consultation process.

2.4 Warranties and disclaimer

The statements and opinions in this report are given in good faith but rely upon information from the source identified in this report and discussions with relevant stakeholders and industry experts. The report also draws upon the resources of KPMG.

KPMG Consulting does not have any pecuniary interest that could reasonably be regarded as being capable of affecting their ability to give an unbiased opinion in relation to the matter. KPMG Consulting will receive a professional fee for the preparation of this report.

3 National Competition Policy legislation review methodology

3.1 Background to National Competition Policy

Since the mid-1980's, all governments have concertedly pursued microeconomic reforms to improve the performance of their economies and the welfare of their citizens. Initially, major Commonwealth Government reforms centred on measures to make the economy more export focussed. More recently, governments at all levels have implemented measures aimed at improving the performances of government businesses, providing better services to the public and making labour markets more flexible.

Many reforms have been progressed through the Council of Australian Governments (COAG). In 1992, COAG established an independent committee of inquiry into a national competition policy – the Hilmer Committee – in an attempt to address problems that can arise from a fragmented State-by-State approach to reform. In response to the Hilmer Committee's report, all nine Australian governments agreed in April 1995 on the need for a more coordinated and systematic approach to reform. National Competition Policy therefore represents the national approach to competition policy reform.

The aim of National Competition Policy is not only to facilitate effective competition to promote economic efficiency, but also to accommodate situations where competition does not have that effect, or where it conflicts with social objectives. For example:

- A competitive market may not develop if there are market failures associated with a particular good or service; and

- Allowing a free market to operate in narcotics, or other substances open to abuse, is unlikely to be in the public interest.

The governments' National Competition Policy commitments are set out in three inter-governmental agreements:

- The Competition Principles Agreement;

- The Conduct Code Agreement; and

- The Agreement to Implement the National Competition Policy and Related Reforms.

The Competition Principles Agreement (CPA) sets out principles for prices oversight of government businesses, competitive neutrality, reform of public monopolies, legislation reviews and access to services provided by significant infrastructure facilities.

Under the CPA, each party agreed to review, and where appropriate reform by the year 2000, all legislation that restricts competition. Subclause 5(1) of the CPA provides the guiding principle for legislation reviews, namely that legislation should not restrict competition unless it can be demonstrated that the:

- Benefits of the restriction to the community as a whole outweigh the costs; and
- The objectives of the legislation can only be achieved by restricting competition.

Therefore, National Competition Policy generally places the onus on those seeking to retain legislative restrictions on competition to prove the wider community benefit of such restrictions.

3.2 Public interest test

The 'public interest test', as described in Subclause 1(3) of the CPA, is a pivotal element of competition policy and is used to determine whether competition policy reforms will be implemented (Standing Committee on Financial Institutions and Public Administration 1997). Subclause 1(3) describes the 'public interest test':

> *'Without limiting the matters that may be taken into account, where this Agreement calls:*
>
> *(a) for the benefits of a particular policy or course of action to be balanced against the costs of the policy or course of action; or*
>
> *(b) for the merits or appropriateness of a particular policy or course of action to be determined; or*
>
> *(c) for an assessment of the most effective means of achieving a policy objective*
>
> *the following matters shall, where relevant, be taken into account:*
>
> *(d) government legislation on policies relating to ecologically sustainable development;*
>
> *(e) social welfare and equity consideration, including community service obligations;*
>
> *(f) government legislation and policies relating to matters such as occupational health and safety, industrial relations and access and equity;*
>
> *(g) economic and regional development, including employment and investment growth;*
>
> *(h) the interests of consumers generally or of a class of consumers;*
>
> *(i) the competitiveness of Australian businesses; and*
>
> *(j) the efficient allocation of resources.'*

The public interest test is not confined to the specific matters listed above; that is, the above list is not exhaustive. Furthermore, the Standing Committee notes that the most important factor for a specific review may not even be on the list, nor may all listed factors be relevant. However, the Standing Committee also pointed that:

> *'The fact that a matter is specified on the list is an indication of its status as a key public policy consideration that cannot be ignored.'*

With respect to legislation reviews, the public interest test applies to the assessment of the costs and benefits of legislative restrictions by virtue of Subclause 5(1).

3.3 Review process

As part of the National Competition Policy reform process, and the broader Post Implementation Review (PIR), all State and Territory governments have agreed to review Consumer Credit Code legislation enacted in each Australian jurisdiction against the National Competition Policy principles.

Accordingly, the Standing Committee of Officials of Consumer Affairs (SCOCA) has appointed KPMG Consulting to conduct the National Competition Policy review as an independent party and to prepare a report based on the assessment of the issues raised by the terms of reference. SCOCA will then present this report to the Ministerial Council on Consumer Affairs.

The Uniform Consumer Credit Code Management Committee (the Management Committee), which comprises representatives of State and Territory Consumer Affairs and Fair Trading Departments, is responsible for oversighting the conduct of the review and ensuring the requirements of National Competition Policy are met.

3.4 Terms of reference

3.4.1 Object of review

All States and Territories are party to the Australian Uniform Credit Laws Agreement 1993. The essence of the agreement is the introduction and maintenance of consumer credit laws, which apply equally to all forms of consumer lending, and which are uniform in all jurisdictions.

In accordance with each State and Territory's obligations under the National Competition Policy Package, this review will examine the case for reform of legislative and regulatory restrictions made under or in relation to the Consumer Credit Code.

The guiding principle of the review shall be that legislation or regulation should not restrict competition unless it can be demonstrated that the benefits of the restriction to the community as a whole outweigh the costs and that the objectives of the legislation can only be achieved by restricting competition.

3.4.2 Competition Policy issues to be addressed

The key components of this NCP review include:

- Clarification of the objectives of the Consumer Credit Code;
- Identification of the nature of any restrictions on competition;

- Analysis of the likely effect of any restrictions on competition and on the economy in general;
- Assessment of the costs and benefits of each restriction;
- Consideration of alternative means of achieving the same result including non-legislative approaches; and
- Consideration of whether the legislation contravenes the competitive conduct rules in Part IV of the *Trade Practices Act 1974* (Cth) and the Competition Codes of each jurisdiction.

3.4.3 Other considerations

This review will consider Government and market activities relevant to the objectives of the Consumer Credit Code, and:

a) Review existing definitions and exemptions contained in the legislation to determine whether they are appropriate to the objectives of the Consumer Credit Code.

b) Assess the need for the Consumer Credit Code having regard to the following fair trading outcomes:

  - access to appropriate information to enable informed decisions to be made by participants;
  - appropriate post contractual protection for consumers;
  - provision of redress mechanisms for consumers;
  - minimal misleading, deceptive or unconscionable conduct by market participants;
  - minimal restriction on product flexibility and consumer choice; and
  - minimal compliance costs for business.

c) Consider future strategies that might influence those regulated by the Consumer Credit Code towards improved performance against fair trading outcomes.

d) Consider the recommendations of the Ministerial Council on Consumer Affairs (MCCA) relating to the report of the Post Implementation Review of the Consumer Credit Code.

3.5 NCP legislation review guidelines

The review has been carried out in accordance with the following guidelines:

- COAG's *Principles and Guidelines for National Standard Setting and Regulatory Action*;
- The Western Australian *Legislation Review Guidelines*;
- The Victorian Government *Guidelines to the Review of Legislative Restrictions on Competition*;
- The *Consultation Framework for Review of Anti-Competitive Legislation* published by the NSW Government; and
- The Commonwealth Treasury *Guidelines to Cost Benefit Analysis*.

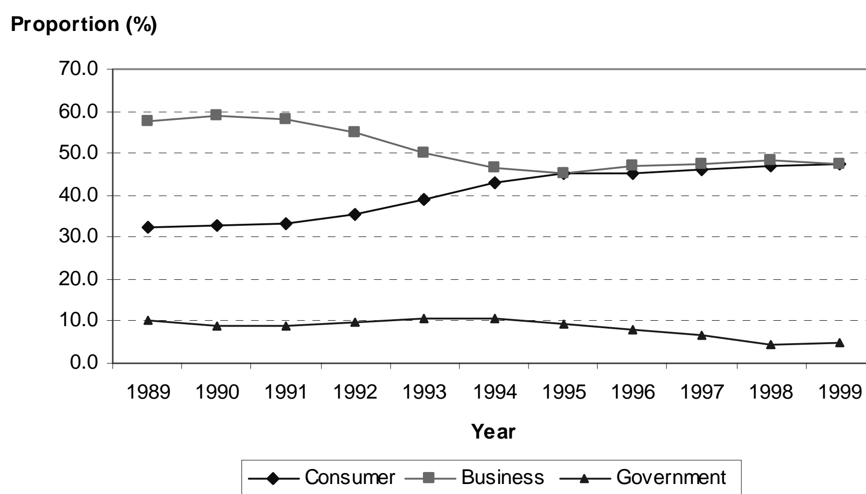
4 The consumer credit industry

4.1 Overview of the credit industry

Consumer credit is the provision of money under contract to individuals and residential strata corporations[1] which is predominantly for personal, household and domestic purposes (Duggan & Lanyon 1999). The Consumer Credit Code applies to consumer credit products including personal loans, mortgages, credit cards, guarantees, overdrafts, revolving credit, housing loans, goods leases and consumer leases[2]. The Consumer Credit Code does not cover credit for business purposes or investments such as rental properties.

Consumers represent a significant proportion of the lending market in Australia. As shown in Figure 4.1, consumer credit accounted for approximately 47.6% of all credit provided by Australian financial institutions (AFIs) in June 1999 (RBA 1999a).

Figure 4.1 Relative Credit Volumes, by Sector, June 1989 – June 1999



Source: Reserve Bank of Australia

4.1.1 Key factors influencing credit trends

The changing nature of credit throughout the 1990s reflects the changing attitudes of Australian households towards consumption spending and the acquisition of debt to fund this spending. Generally speaking, households have become more consumption orientated. This is illustrated by the rise in the level of household debt, which is now approaching 100% of

[1] 'Strata corporation' is defined in the Consumer Credit Code as a body corporate incorporated in relation to land subdivided wholly or mainly for residential purposes or a body corporate whose issued shares confer a right to occupy land for residential purposes.

[2] See Glossary of Terms for definitions and descriptions of each type of loan.

annual disposable income, up from a level of 50% a decade ago (RBA 1999c, 2000). In June 1999, the average debt per household was around $41,125 (RBA 1999a, ABS 2000).

Household debt to income ratios in Australia now reflect those in the US, the UK and Canada, whereas they were quite low by comparison to international standards a decade ago (RBA 1999d, 1999e). While total debt levels have increased, the low interest rates experienced in the 1990s kept debt servicing costs (in relation to income) relatively constant (RBA 1999c). However, the latest figures indicate that the recent increases in nominal interest rates increased the ratio of household sector interest payments to disposable income to 6.5% in the December 1999 quarter, up from the most recent low of around 6% in the March 1999 quarter (RBA 2000).

The growth in borrowing by households over the past 15 years has been facilitated by a number of key factors, including financial deregulation, low inflation and interest rates.

Deregulation of the Australian financial sector during the 1980s had a large impact on the consumer credit market. The dramatic rise in the number of credit providers in the economy (with the licensing of a number of banks and the rapid expansion of the non-bank financial institutions sector) opened lending channels to consumers never previously available. This increase in access to credit enabled the volume of credit provided to individuals and households to grow substantially.

Lending to consumers has become a commoditised and competitive business over the past decade[3]. Industry commentators have suggested that aggressive competition from banks, mortgage managers and finance companies in markets for housing and personal finance has resulted in the relaxation of credit standards, competitive lending rates and product innovation[4]. Financial liberalisation removed constraints that formerly prevented some people from having their finances arranged in the way they desired. In general, this has reduced the cost of access to finance increasing not only the number of loans taken out but also the average size of a loan.

Further, low inflation and low interest rates throughout the 1990s has also generally boosted household confidence in taking on new debt[5] (RBA 1999c). This combination has hastened the process of households incurring greater levels of debt in the aggregate by improving the accessibility of finance to consumers. Falling nominal interest rates have decreased the repayment burden of households relative to income, with households responding by increasing the amount of debt that they are carrying.

---

[3] The first area to see the benefits of financial liberalisation and innovation and competition was the corporate sector in the 1980s. The full benefits did not really reach households until the 1990s.

[4] Prior to deregulation, access to housing finance depended on a number of variables including the borrower's record of savings at the bank, even the individual branch, making the loan counted for a lot in getting access to a loan. The actual availability of funds was not well signalled by price. Interest rates are now the principal device for rationing credit.

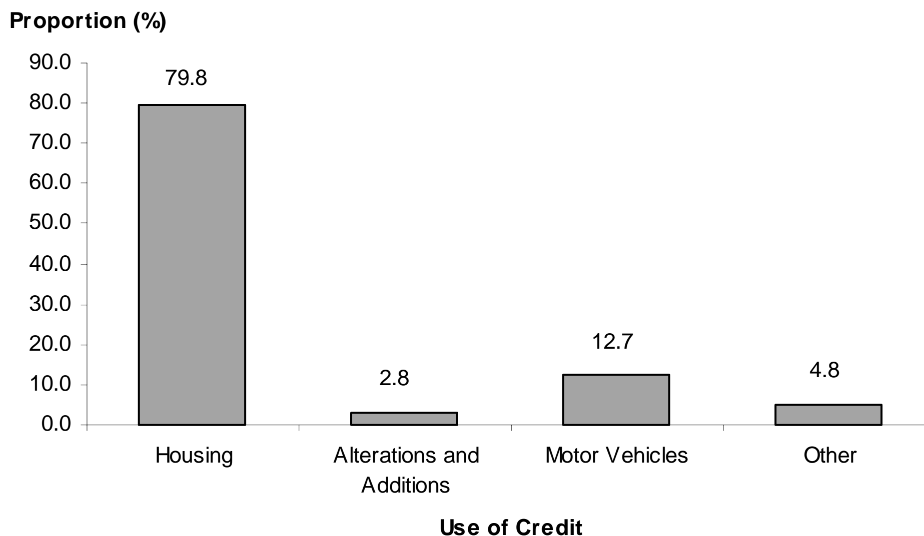
[5] Generally speaking, low inflation leads to lower nominal interest rates (RBA 1997).

4.2 Consumer credit purposes

Consumers use credit to obtain a variety of goods and services for personal, household and domestic purposes. Figure 4.2 illustrates the proportion of credit used by individuals and households for various consumption items. The types of credit included in this graph are secured housing loans, revolving credit (including credit cards), fixed loans and finance leases[6].

Housing, semi-detached housing, flats, home units, and town and terrace houses constitute the largest expenditure component, accounting for approximately 79.8% of credit usage as at June 1999. Housing alterations and additions account for a further 2.8% of total credit usage. Motor vehicles are another major item, representing 12.7% of total credit usage, while the purchase of whitegoods, furniture, computers and other items account for 4.8% (ABS 1999).

Figure 4.2 Purpose of Consumer Credit, as at June 1999



Note: Figures may not add to 100 due to rounding effects.
Source: ABS 1999

4.3 Supply of consumer credit

This section provides detail on the major financial intermediaries involved in the provision of credit to consumers.

[6] It is difficult to identify from the source (ABS 1999) whether this includes interest-free credit commonly provided through linked credit arrangements. However, the ABS refers to 'value of commitments', which KPMG interprets to include both interest-bearing and non-interest bearing commitments.

In Australia, the deposit-taking sector is the main provider of consumer credit products. Institutions within this sector comprise principally of banks and non-bank financial institutions (NBFIs) operating within the domestic market as there are no exports or imports of consumer credit services.

4.3.1 Industry structure

As at January 2000, there were 49 banks operating in Australia, of which 14 were Australian-owned (including 2 subsidiaries), 10 were foreign subsidiary banks and 25 were branches of foreign banks (APRA 2000). The credit providers included in the NBFI category consists of 229 credit unions and 19 building societies, as well as more than 150 finance companies, general financiers, cooperative housing societies, securitisation companies, and mortgage management companies.

As shown in the following table, the banking sector has the highest level of concentration, with the top four banks accounting for 68.3% of the loan market within the banking sector. This share of the market is relatively evenly spread amongst the top four banks, and ranges from 19.6% for the National Australia Bank to 14.3% for ANZ (IBIS 1999a).

Table 4.1 Industry Concentration

Sector	Number	Market Share[a] of Top Four
Banks	49	68.3%
Building Societies	19	48.9%
Credit unions	229	16.5%
Other Financiers	150+	30% – 35%

a. Share of total sector loan market (not total loan market).
Source: IBIS

As shown in the previous table, credit unions have a very low level of concentration, with the top 4 credit unions accounting for just 16.5% of the loan market within the credit union sector. The Australian Central Credit Union is the largest operator of this type in this market, yet accounts for only 5% of the market (IBIS 1999c).

Building societies are more concentrated than credit unions, but not as concentrated as banks, despite the small number of building societies in existence. The Newcastle Permanent Building Society is the largest, with 14.3% of the market (IBIS 1999b).

The market share of the top four other financiers is estimated to be between 30% and 35%. Macquarie Bank stands out in this market, with a market share of 20%, compared to the next largest other financier, RAMS Mortgage Corp, which holds just 6% (IBIS 1999d).

There is a degree of horizontal integration between other financiers and the banks, with some of the general finance companies wholly owned by banks. The most notable of these are:

- Australian Guarantee Corporation (AGC), which is wholly owned by Westpac; and
- Esanda, which is wholly owned by ANZ.

Some financing companies are associated with major manufacturers, most commonly car manufacturers. Examples of these include BMW Australia Finance Limited, Ford Credit Australia and General Motors Acceptance Corporation (associated with Holden).

4.3.2 Consumer credit market share

As shown in Table 4.2, banks are the major providers of consumer credit accounting for 81.8% of the total credit provided to consumers as at June 1999. NBFIs provided the balance of consumer credit of 18.2%.

Table 4.2 Consumer Credit Market Share, by Credit Provider, as at June 1999

Credit Provider	Market Share	
	$ billion	**%**
Banks	254.0	81.8
Building Societies	8.3	2.7
Credit Cooperatives	16.0	5.2
Finance Companies	21.5	6.9
General Financiers	10.8	3.5
Total	**310.6**	**100.0**

Source: Reserve Bank of Australia

Market share has changed considerably over the decade to June 1999, with banks increasing their share of the consumer credit market by 23%, from 66.4% in June 1989 to 81.8% in June 1999.

This has been at the expense of the market shares of the NBFIs, with the exception of credit cooperatives, whose market share has remained steady at 5.2% over the period. Building societies recorded the largest loss in market share over this period, falling from 11.2% in June 1989 to just 2.7% in June 1999.

4.3.2.1 Banks

Banks have taken advantage of their size and strength to penetrate consumer-lending markets and increase their dominance. Banks have sought to boost market share by increasing their competitive position through marketing initiatives and through interest rate reductions. According to Reserve Bank data, in the period between June 1993 and June 1998, interest rates on banks' standard variable home loans fell by 2.8% in absolute terms while the cash rate fell by only 0.2% (indicating a fall in margins over this period of around 2.6%)

4.3.2.2 Mortgage Managers and other Financiers

Similarly, mortgage managers and other financiers have been targeting household business more aggressively and have been competing effectively in the housing loan market through innovative products. Over this period, non-bank mortgage originators have gained market share in housing loan markets, funding loans through securitisation vehicles. The high level of growth in securitisation has largely been driven by an increase in securitised residential

mortgages. In the 3 years to 1997-98, securitisation vehicles with mortgage assets experienced real growth in total assets of 55% per year. While market share in this industry has declined from 16.3% to 10.3% over the past decade, mortgage managers and other financiers have become the main source of new competition for the banks and have captured a large portion of the traditional building society lending market.

4.3.2.3 Building Societies

Building societies have lost an increasing share of the housing finance market, primarily because of the conversion of building societies into banks. The conversion in July 1995 of the Bendigo Building Society to bank status saw Bendigo's asset base ($1.7 billion) reclassified out of this industry. Similarly in 1996-97 Suncorp Building Society also exited the industry. Consequently market share has declined from 11% to 2.6% over the ten years to 1999.

4.3.2.4 Credit Unions

Competition from banks, mortgage managers and finance companies in traditional markets of housing and personal finance has been strong, resulting in a loss of market share for credit unions. For example, the expansion of bank credit card products eroded credit union's market share in the personal loan market, a traditional credit union market. Loans to individuals declined from 61% of total assets in 1990 to 41% in 1999. Despite strong competition, housing loans increased to 39% of total assets, compared to 17% in 1990.

4.4 Consumer credit product attributes and characteristics

A number of functional variables apply across the range of consumer credit transactions. These principles or concepts provide the basis for the various consumer credit products and loans arrangements, and have been described by Duggan & Lanyon (1999) as follows:

- **Revolving credit facilities**, which generally have the following characteristics:
  - a commitment for a credit or borrowing limit is given for a specific period after which the commitment is reviewed;
  - the extent of the borrowing used at any time during the period may be for any amount up to the authorised limit. In other words the consumer need not use all the credit at the outset, but may draw on the facility as and when convenient. Accordingly interest is not pre-computed but accrues only with respect to utilised credit; and
  - repayments (other than of charges and interest) made during the period reduce the extent of the borrowing used and thereby increases the amount of unused credit available up to the authorised limit. In other words each drawing by the customer

will reduce the amount of available credit, but each payment will restore it (after allowing for payment for charges and interest).

Revolving credit facilities offer borrowers more flexibility than fixed loans as they have no maturity and no fixed repayment schedule.

- **Fixed loan facilities**, which is credit other than revolving credit, generally involve:
  - a commitment for a fixed amount for a fixed period for a specific purpose. A contract may provide for the credit to be made available in instalments;
  - a schedule of repayments over a fixed period; and
  - repayments which reduce the liability of the borrower but not act to make further finance available.

- **Secured and unsecured credit**.

A credit contract may be secured or unsecured. Secured credit confers to the credit provider rights by contract over property in the event of default by the customer. The contract relating to the security may be with the customer, the security may be given over the property acquired with the credit, or it may be given over other property belonging to the customer. The latter method will be the only available option in the case of a non-purchase-money[7] loan credit transaction, and also where the credit relates to the acquisition of services.

The main classes of securitisation are the mortgage and the guarantee. A mortgage will involve the transfer to the credit provider of possession of the relevant property.

A guarantee is a collateral contract to answer for the debt or default of another. A guarantee is provided at the request of the debtor and both the debtor and credit provider agree that the guarantor's liability is a secondary one, the debtor being primarily liable for the obligation guaranteed. Guarantees serve a number of functions in the context of consumer transactions:

- a guarantee signals to the credit provider creditworthiness of prospective debtor, particularly where this person has no substantial credit record;
- a guarantee can be used to supplement security offered by prospective debtor; and
- a guarantee ensures that the credit provider can take enforcement action in the event of loan default.

[7] A non-purchase-money loan is one in which the credit provider does not impose any restrictions on how the money may be spent. In contrast, a purchase-money loan is one with which there is a definite connection with the acquisition of particular goods, services or land (Duggan & Lanyon 1999).

- **Fixed and variable costs**

  An important feature in any credit contract is the cost of credit imposed by the credit provider. Various arrangements are available according to the type of loan facility taken. Costs include:

  - Fixed costs, which include establishment, annual, transactions and application fees; and

  - Variable costs usually in the form of interest rates that can be applied on a variable or fixed basis.

  The various components of costs are discussed further in a subsequent section.

- **Loan and sale credit**

  The key difference between loan and sale credit is that loan credit is the payment of money to or for someone on the condition that it will be repaid, while sale credit is the deferment of the price payable for goods or services. Loan credit thus comprises all credit provided in loan form, whether it is fixed sum credit or revolving credit. Instalment sales are an example of sale credit.

The concepts described above form the basis of the major loan products available to consumers. They allow for various loan arrangements and customer choice, as detailed in the following sections.

4.4.1 Housing Loans

Borrowers can choose between a variety of loan arrangements in a highly competitive housing loan market. However, housing loans, by definition are secured loans.

Secured housing finance comprises all secured commitments to individuals for the construction or purchase of dwellings for owner occupation. Securing a housing loan enables the borrower to take out a larger loan and also to reduce interest payment on the loan as the collateral offered on the loan reduces the credit risk and hence the risk premium on the interest rate.

Housing loans can be tailored to suit specific customer needs with choices between fixed and variable interest rates, or a combination of both, and low ‘honeymoon’ interest rates, redraw facilities and interest offset accounts. Refinancing arrangements are also available, and this may be with the original or an alternative lender. Where existing borrowers seek to refinance their loan to gain access to more favourable terms, banks may impose substantial refinancing costs, including loan establishment fees, mortgage stamp duty and exit fees on the existing loan facility.

4.4.2 Personal Loans

There are a wide variety of personal loans available to consumers, although the range of loan features is generally not as extensive as those applying to housing loans. Personal loans may be secured or unsecured, revolving (eg overdraft) or fixed, and may have variable or fixed interest rates.

Personal loans are generally taken out for a specific purpose, but this does not need to be the case. Bank overdrafts are a species of revolving credit and do not involve the provision of credit in connection with a particular purchase.

4.4.3 Credit Cards

Credit card schemes are often taken to typify revolving credit. Two types of credit cards are available to consumers, namely:

- Card with interest-free period and an annual fee. If a customer with this card repaid all of their credit card borrowings in full each month, they would pay no interest. In other words the only direct cost to such cardholders would be the annual fee.

- Card without interest-free period and no annual fee. This type of card usually has a lower interest rate, but interest accrues immediately upon using available credit.

Credit card arrangements are subject to application, annual and transaction fees and include minimum and maximum credit limits. As an incentive, cards often provide bonus schemes and rewards, such as flyer points.

4.5 Pricing

The cost of credit is comprised of interest and non-interest charges:

- Interest charges, which apply to all consumer credit. The interest rate varies across credit products according to risk, or the lender’s assessment of the likelihood of default by the borrower. Interest rates may be variable or fixed rates, with caps applying in certain circumstances.

- Non-interest charges, which are charges other than those resulting from the interest rate, and include loan application fees, annual fees, establishment fees and transactions fees.

Over the past decade, banks have earned a rising portion of their total income from non-interest income, with the increase largely coming from fees as opposed to other non-interest income. This has only partly offset the decline in income associated with the fall in interest rate margins. Therefore, banks have turned to either economies of scale or differentiated products to gain a competitive advantage (RBA 1999c).

For the six largest banks, the fees earned from consumer loans amounted to $650 million dollars in 1998, which represents about 46.1% of total bank domestic fee income from the household sector of $1.4 billion (RBA 1999b). Housing loans accounted for $350 million (or 53.8%) of the fees earned on consumer loans, while personal loans accounted for $190 million (29.2%) and credit cards accounted for $110 million (16.9%).

The fees earned from consumer loans by the major banks in 1998 increased by 27.5% over the previous year (RBA 1999b). Most of this increase resulted from the 55.6% increase in fees earned from housing loans. Fees earned from credit cards increased by 10.0% over the same period, while the fees earned from personal loans fell 2.6%.

On loans, fees add a total of about 0.2% to the cost of housing loans, 1.4% to the cost of credit cards, and 0.8% to that of other personal loans. Overall, these fees are estimated to add about 0.3% to the cost of household borrowing (RBA 1999b).

4.6 Forces driving change in the consumer credit industry

This section describes the major factors driving change in the financial system and thereby affecting the consumer credit market and identifies some of their implications. The financial system is undergoing continuous and rapid change, which is primarily driven by interlinked forces. In brief, there are three key forces driving change in the consumer credit industry:

- Deregulation;
- Technological change; and
- Product innovation.

This section also consider market implications of these factors driving change, including changes to wholesale markets, financial service providers, products and distribution channels.

While this section addresses these factors separately, they interact with and affect one another. For example, global competitors have emerged in Australian markets partly because of technological developments have enabled them to access Australian consumers. Similarly, consumer demand for certain financial products, such as securitised home mortgages, has been stimulated by technological developments that have made those products both feasible and accessible to consumers.

4.6.1 Deregulation

Following the Great Depression of the 1930s, a Royal Commission chaired by Justice Napier conducted the first major inquiry into the monetary and banking system in Australia in 1935 (Wallis et al 1997). The Royal Commission recommended that the financial system should be subject to wide ranging intervention including, amongst other things, direct control of interest rates and the volume of credit.

The tight controls on banks encouraged the growth of non-bank financial institutions (NBFIs) and a number of larger private banks established savings bank and finance company subsidiaries in an attempt to avoid some of the regulatory restrictions faced by banks (Wallis et al 1997).

Subsequently, the NBFIs increased their market share at the expense of banks (Kent & Debelle 1999). Life companies had substantial holdings of residential mortgages and finance companies were main source for hire purchase finance for household consumables. Building societies also benefited by picking up the excess demand for housing loans that banks could not provide cost-effectively (Wallis et al 1997).

The process of deregulation in the financial sector began in the early 1970s with the gradual removal of controls on interest rates, which was then followed by:

- Removal of other controls on banks (such as the controls on the types of products they were allowed to offer);
- Freeing up of interest rates on government securities;
- Floating of the exchange rate; and
- Opening the banking system to foreign competition (Battellino 2000).

Deregulation has affected the relative competitive advantages enjoyed by the various types of credit providers. For example, credit unions and building societies, which were not as heavily regulated, lost the relative competitive advantage they had enjoyed when the banks were deregulated (Battellino 2000).

Changes generally to legislation governing consumer credit and credit providers have implications for product development, especially in terms of pricing. That is, any product developments must comply with the relevant legislation, and any changes to the legislation may require changes to existing products.

4.6.2 Technological change

Technological change has been a constant factor affecting business decisions and the shape of markets in the financial sector and the economy as a whole. Technology is allowing innovation to occur in the financial services industry at an accelerating pace, leading to significant changes in financial relationships and market structures (Wallis et al 1997).

The *Financial Systems Inquiry* identified the key technological developments affecting the financial services industry, namely:

- Reduced cost of transmitting, storing, using and interrogating information;
- Increasing access to electronic networks;

- Increasing security across networks;
- Rapidly growing use of electronic channels for payments and financial services delivery;
- Access to financial information is improving;
- The physical location of customers and suppliers is becoming less important; and
- Reduced costs and reduced need for extensive physical representation has reduced barriers to entry into the financial industry.

In summary, technological innovation has led to a communications and processing infrastructure with declining costs, increased power and capacity, and greater accessibility. In relation to the financial system, these factors have manifested themselves in key areas:

- Emergence of new players in markets;
- Changing distribution channels; and
- New products.

Technology is challenging the cost and pricing structure of banks, and pressures for standardisation, ease of use and cost effectiveness of systems and distribution channels is increasing.

The introduction of new technologies has significantly reduced transaction costs. It is estimated that a branch transaction costs around $5; an ATM transaction cost around $0.70 - $1.30; a telephone banking inquiry $2.50; interactive telephone voice inquiry $0.50; and an EFTPOS transaction $0.40 - $0.70. In comparison, it is estimated that an Internet banking transaction costs between $0.10 and $0.20.

Fees and charges are structured to encourage consumers to use the more cost-effective, electronic distribution channels. That is, financial institutions are actively encouraging the use of ATMs, EFTPOS, the telephone and Internet rather than branches for financial transactions.

The growth in the use of the Internet is illustrative of the possibilities of wide spread delivery of financial services by telecommunication channels. Technological development has resulted in a proliferation of Internet financial services over the last couple of years, including online banking, online loan application facilities and online BPAY loan repayment facilities.

For the consumer, the technological developments that have occurred potentially make financial services more widely available, at lower costs and with more convenient access (Wallis et al 1997). However, there are certain equity issues to be considered as not all consumers have equal access to the technology required to access, for example, online banking. Furthermore, not all consumers are equally technologically literate or motivated.

4.6.2.1 Electronic commerce

There appears to be some uncertainty as to the extent that the Consumer Credit Code allows or recognises the use of electronic documents and signatures to facilitate consumer credit transactions.

The PIR noted that, on balance, the submissions felt that the Consumer Credit Code does not, or does not sufficiently, permit electronic commerce. It was concluded that 'there is strong argument that the Code is ambiguous as to whether it permits credit contracts to be formed electronically'.

On the other hand, McGill and Willmott (1999) conclude that the definitions within the Consumer Credit Code 'clearly leave the door open to electronic and other technological developments which may take place over the years to replace the traditional forms of contract documentation'.

However, any such uncertainties may be more temporary than real, as legislation now exists at both the federal and state levels to facilitate electronic commerce. The Commonwealth Government's *Electronic Transactions Act 1999* commenced by proclamation on 15 March 2000, New South Wales has enacted its *Electronic Transactions Act 2000*, although it is yet to come into operation, and the Victorian equivalent which came into operation on 1 September 2000.

The Commonwealth legislation applies specifically to Commonwealth laws and thus is not directly applicable to the Consumer Credit Code. It was nevertheless the precursor to the NSW and Victorian electronic transactions legislation, which apply to common and statute laws of their respective jurisdictions. We note that each jurisdiction would need to implement electronic transactions legislation to ensure that digital signatures would be accepted nationally.

Section 4 of the *Electronic Transactions Act 2000* (NSW) provides a simplified outline of the Act:

> *(a) For the purposes of a law of this jurisdiction, a transaction is not invalid because it took place by means of one or more electronic communications.*
>
> *(b) The following requirements imposed under a law of this jurisdiction can generally be met in electronic form:*
>
> > *(i) a requirement to give information in writing,*
> >
> > *(ii) a requirement to provide a signature,*
> >
> > *(iii) a requirement to produce a document,*
> >
> > *(iv) a requirement to record information,*
> >
> > *(v) a requirement to retain a document.*

The legislation sets out the circumstances where the above requirements will be taken to have been met electronically.

Section 12 of the Act provides for regulations to be made exempting specific requirements, permissions or laws. In the absence of any such regulations, electronic transactions under the Consumer Credit Code are legally recognised.

Although only NSW and Victoria have enacted electronic transactions legislation, the Commonwealth Government worked in close cooperation with the States and Territories to develop a uniform *Electronic Transactions Bill 2000*, to which each of the States and Territories gave their in-principle agreement. Hence, it is expected that the other States and Territories will also enact uniform electronic transactions legislation.

The PIR recommended harmonising the Consumer Credit Code with the *Electronic Transactions Bill* and adopting specific consumer protection measures, as necessary, to deal with issues specific to the consumer credit industry (Recommendation 2.19). Furthermore, it was recommended that the definitions within the Consumer Credit Code be amended so that the Consumer Credit Code explicitly recognises both electronic records and the electronic authentication of records (Recommendation 2.20).

The PIR also made a number of other recommendations regarding electronic transactions, especially in relation to minimum requirements for consumer protection (see complete list of recommendations in Chapter 6).

4.6.3 Product innovation

Product innovation in the consumer credit industry is evidenced primarily by changes in product attributes, rather than by product types. That is, the main credit product categories remain housing loans, personal loans and credit cards, but the choices available to consumers within each of these categories has changed significantly over the past two decades.

4.6.3.1 Housing loans

Prior to the 1980s, the main sources of housing loans – banks and permanent building societies – offered an average of two varieties of housing loans, with only basic attributes compared to the housing loans available today (Wallis et al 1997). Most providers of housing loans now have at least four types of housing loans, namely:

- Basic variable rate housing loan;
- Standard variable rate housing loan;
- Fixed rate housing loan; and
- Honeymoon rate housing loan.

The standard variable rate housing loan commonly has the most number of features / options, and these may include a redraw facility, offset facility, portability, repayment flexibility,

repayment holidays and parental leave. More details on the various housing loans available and their features are provided in the Glossary.

Product innovation in the housing loan sector has been facilitated by the introduction of mortgage indemnity insurance, which has allowed securitisers (and traditional mortgage lenders) to shift the risk of default to another party (Wallis et al 1997). This insurance protects the credit provider against potential loss in the event of default by the debtor, where the sale of the security held by the credit provider fails to cover the amount of debt outstanding. While mortgage indemnity insurance protects the credit provider and is taken out by the credit provider, the insurance premium is usually paid by the debtor.

4.6.3.2 Credit cards

Product innovation in credit cards has related primarily to the introduction of new cards with specific loyalty / reward programs, such as:

- Westfield Visa, which provides rewards for shopping at particular retailers; and

- GM Card, which allows the cardholder to (potentially) save on purchases of new Holden cars.

The standard loyalty program provides ‘points’ for each dollar spent using the credit card and ‘bonus points’ for each dollar spent at participating retailers. The points earned may then be redeemed for particular goods and services – most commonly airfares.

Other product innovation in this sector has been the introduction of the ‘Gold’ card, which offers additional benefits to the standard loyalty program (such as preferred seating at specific entertainment venues) and a higher credit limit, but also incurs additional fees and a higher interest rate.

4.7 Summary

In summary, the key features and characteristics of the market in which the Consumer Credit Code operates are:

- A wide range of products fall within the category of consumer credit, including housing loans, mortgages, personal loans, credit cards and leases;

- Household debt levels have increased significantly in the last 10 to 15 years, reflecting changing attitudes, financial deregulation, and low inflation and interest rates;

- Consumer credit is used predominantly for housing, which accounts for almost 80% of the value of credit provided;

- There are a large number of credit providers in Australia, including banks, building societies, credit unions and other financiers, such as finance companies;

- Banks are the main providers of consumer credit, accounting for more than 80% of consumer credit;
- A number of functional variables apply across the range of consumer credit products. That is, consumer credit may be revolving or fixed, secured or unsecured, loan or sale credit, and may have a combination of fixed and variable costs;
- The cost of credit comprises interest charges, which apply to all credit products, and non-interest charges, such as loan application fees and annual fees;
- Over the last decade, non-interest income has represented an increasing proportion of total income. However, fees represent less than 1% of the cost of consumer credit;
- Deregulation, technological change and product innovation are the key forces driving change in the consumer credit industry;
- Technological developments have significantly reduced transaction costs, but there are equity issues in relation to access to new technology;
- Electronic transactions legislation, which recognises electronic documents and digital signatures, is expected to be introduced in each jurisdiction; and
- Product innovation has led to a wide range of product attributes, rather than an increase in the main credit product categories.

5 The Consumer Credit Code legislation

This chapter provides information on the regulation of the consumer credit industry in Australia and examines how the Consumer Credit Code addresses the market failures present. It also considers the Consumer Credit Code consistency with Part IV of the *Trade Practices Act 1974* and the Competition Codes.

5.1 History of consumer credit regulation

The practice of lending money in return for the payment of interest was prohibited until the 16th Century, at which time legislation was passed to allow the lending of money at a prescribed interest rate. However, the laws were widely avoided, rendering them ineffective. In 1854, the legislation was repealed and moneylending practices were essentially left to market forces (Duggan et al 1998).

Prior to the turn of the 20th Century, the House of Commons Select Committee on Moneylending in the United Kingdom published a report that was highly critical of the unregulated industry. This report detailed various kinds of abuse occurring within the moneylending industry, including:

- Misleading advertising;
- Use of aliases to cover bad reputations;
- Charging of excessive interest rates;
- Inclusion of harsh penalty clauses on default;
- Keeping the borrower ignorant of the terms of the contract until the date fixed for repayment; and
- Exploitation of the young and ignorant (Duggan et al 1989).

The findings of this Committee led to the enactment of the Moneylenders Act 1900, whose three main consumer protection measures were:

1. The establishment of a registration system for money lenders, which restricted them to only one business name and required them to register each business address separately;
2. Formalisation of certain types of conduct as a criminal offence; and
3. Provision to the courts of the power to reopen contracts with moneylenders on the basis of excessive interest, and the transaction being harsh and unconscionable (Duggan et al 1989).

This legislation was extensively amended by the Moneylending Act 1927, which extended the consumer protection measures by:

- Substituting registration for licensing;
- Establishing detailed requirements for the conduct of moneylending; and
- Setting an interest rate limit of 48% as representing an excessive interest rate.

The English Moneylending Acts of 1900 and 1927 provided the basis of moneylending legislation in various Australian states (Duggan et al 1989).

The Australian consumer credit and money lending laws first came under examination on a national basis at conferences in 1953 and 1959 of State and Commonwealth ministers. An outcome of these conferences was the enactment of 'uniform' hire purchase legislation in each Australian State and Territory between 1959 and 1961 (Duggan & Lanyon 1999).

Following the success of this exercise, the Standing Committee of State and Commonwealth Attorneys-General was established. This Committee began examining moneylending laws in Australia, and subsequently referred the subject of consumer credit and moneylending to the Adelaide Law School in 1966. A committee of the Law School, chaired by Professor Arthur Rogerson, undertook the study and presented its report in February 1969 (Duggan & Lanyon 1999).

The recommendations of the Rogerson Committee included repealing the hire purchase and moneylending legislation and enacting new laws to regulate consumer credit transactions on a national basis. Specific recommendations of the Rogerson Committee relating to the consumer credit legislation included:

- Requiring persons carrying on consumer credit business to be licensed;
- Regulating the form and content of transactions;
- Requiring disclosure of the cost of credit both in dollars and cents and also as a rate per cent per annum according to a statutory method;
- Implying mandatory conditions and warranties in consumer sales;
- Regulating the rights of the parties to a security transaction between themselves; and
- Standardising the rules governing disputes between the holder of a security interest in goods and a bona fide third party purchaser (Duggan & Lanyon 1999).

The Victorian Attorney-General subsequently established a committee, known as the Molomby Committee, to report on the feasibility of adopting the Rogerson Committee recommendations in Victoria. The committee reported in 1972, agreeing with the basic

philosophy, but detailing in greater depth many of the reform proposals (Duggan & Lanyon 1999).

5.1.1 The Credit Acts

The South Australian Government identified a need for an early response to the broader issues raised by the Rogerson Committee, and subsequently enacted the Consumer Credit Act and the Consumer Transactions Act in 1972 (Duggan & Lanyon 1999).

Other States and Territories in Australia were slower to act. Victoria and New South Wales agreed on the text of a uniform statute, enacting the same legislation, the Credit Act, in 1984. This legislation closely followed the Molomby Committee recommendations, and was quite different in form from the South Australian legislation. Western Australia joined the uniform scheme in 1984, the Australian Capital Territory in 1985 and Queensland in 1987. Tasmania and the Northern Territory did not join the scheme, nor did South Australia, which elected to continue with is 1972 legislation (Duggan & Lanyon, 1999).

The Credit Acts attracted significant criticism in the years following their enactment, including criticisms such as:

- Poor drafting, to the extent that it was barely comprehensible in parts. This led to a proliferation of exemption orders (as a substitution for statutory amendments), which only made the comprehensibility problem worse;
- Being too prescriptive, to the extent that it inhibited the development of new credit products;
- Severity of penalties – a breach of the detailed and technical disclosure requirements resulted in automatic loss of credit charges;
- Limitation of coverage, particularly:
  - Credit unions and building societies were not covered in most states;
  - Bank and pastoral company overdraft lending was exempt;
  - Loans over $20,000[8] were generally not covered, which effectively excluded housing loan contracts; and
- Non-uniformity in that South Australia, Tasmania and the Northern Territory remained outside the scheme (Duggan & Lanyon 1999).

Upon directions from the Standing Committee of Consumer Affairs Ministers (SCOCAM), the Victorian Law Reform Commission prepared a plain English draft Credit Bill in 1989.

[8] The upper limit was $30,000 in the ACT and $40,000 in Queensland.

The main purpose was to redraft the legislation into plain English, but a number of reforms were also incorporated. However, only the first of the concerns noted above were addressed in the draft Credit Bill. It was subsequently criticised by both industry and consumer groups for not addressing the broader need for reform, and the Bill was never proceeded with (Duggan & Lanyon 1999).

5.1.2 The Consumer Credit Code

In 1993, the State and Territory governments entered into an agreement called the *Australian Uniform Credit Laws Agreement 1993*, which provided for the adoption of uniform credit laws throughout Australia based on template legislation to be enacted by the Queensland Parliament (Duggan & Lanyon 1999). The key features of the agreement were:

- A Ministerial Council for Uniform Credit Laws was established to consider and review the template legislation and its administration;
- The text of the template legislation and regulations required unanimous approval of Council, but future amendments would only require a two-thirds Council majority;
- Parties to the agreement would make reasonable endeavours to ensure that administration of the legislation would be uniform or reasonably consistent; and
- A state or territory would cease to be a party to the Agreement if it failed to pass either uniform or alternative consistent legislation, or if it introduced amendments contrary to the requirements of the Agreement (Duggan & Lanyon 1999).

In 1994, Queensland enacted the Consumer Credit (Queensland) Act. The Consumer Credit Code – the subject of this Review – is set out in an appendix to this legislation. Each State and Territory, with the exception of Tasmania and Western Australia, have enacted legislation applying the Consumer Credit Code as in force in Queensland as their own. Western Australia enacted alternative consistent legislation and Tasmania has a modified template system[9]. The Consumer Credit Code commenced operation throughout Australia on 1 November 1996 (Duggan & Lanyon, 1999).

5.1.3 Key reforms under the Consumer Credit Code

In general terms, the Consumer Credit Code was an improvement over the former Credit Acts in that it was written in plain English, simplified a number of processes and introduced a number of reforms. More specifically, the key reforms of the Consumer Credit Code over the earlier Credit Acts are:

- Rather than a monetary limit, the Consumer Credit Code uses a purpose test to determine coverage of the legislation to particular credit contracts. This effectively expands the scope, such that it can include housing loans. Furthermore, the Consumer Credit Code

[9] Section 5.5 of this Chapter further discusses the administration of the legislation across the jurisdictions.

does not distinguish between credit providers and, hence, credit unions and building societies are now covered;

- Under the Credit Acts, credit contracts were divided into three mutually exclusive categories, namely credit sale contracts, loan contracts and continuing credit contracts, and the application of the legislation varied between the three categories. With a few minor exceptions, the Consumer Credit Code treats all forms of credit contracts similarly;

- Previous restrictions on fees and charges a credit provider was allowed to impose were removed. However, the Consumer Credit Code does allow for specific fees and charges to be reviewed for unconscionability and to be prohibited by regulation[10];

- The Credit Acts generally prohibited the inclusion of more than one interest rate in a credit contract, as well as the use of variable interest rates. Multiple and variable rates are allowed under the Consumer Credit Code, subject to certain disclosure requirements; and

- The Consumer Credit Code contains a civil penalties regime that overcomes the criticisms of the civil penalties regime of the Credit Acts. In particular, the penalties are no longer automatic, apply only to breaches of ‘key requirements’, must consider the seriousness of the contravention and are capped at $500,000 (where the application is made by the credit provider or a Government Consumer Agency).

Compared to the previous Credit Acts, the Consumer Credit Code had the advantages of:

- Being *nationally uniform* – this is important given the national nature of the consumer credit market, the fact that many credit providers operate nationally, that consumers (and their assets and liabilities) move between States, and the expectation that all Australians should enjoy consumer protection in relation to credit matters;

- Regulating credit *processes*, rather than prescribing outcomes – the Consumer Credit Code requires disclosure of credit terms and conditions, rather than prescribing the nature of those terms and conditions;

- Being *comprehensive* – with some limited exceptions, the Consumer Credit Code covers all forms of consumer credit, including home loans, whereas previous legislation only applied to consumer credit up to a certain value, and therefore excluded housing loans; and

- Promoting *innovation and choice* in credit products – for example, under the old legislation, banks could not offer tiered rates whereby a variable rate applies to, say, the first $50,000 of a loan and the balance is at a fixed rate. With a greater choice of product attributes available, there are a wider range of possible products and, hence, greater choice for consumers.

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[10] There are currently no prohibited fees and charges specified in the regulations.

5.2 Market theory and consumer protection legislation

It is a fundamental principle of economics that the allocation of productive resources in a market economy, such as Australia's, is primarily determined by consumer preferences. Goods and services are demanded by consumers and supplied by producers. Producers in turn use the revenue obtained from the sale of these goods and services to hire workers, finance equipment purchases and pay rental on business premises. Markets are never static, since consumer preferences and their ability to pay are constantly changing, as are the costs of production and the prices of goods and services. Nevertheless, the system is generally regarded as effective in ensuring that economic resources are allocated to the production of goods and services which consumers require.

The theory of 'perfect markets' is based on the underlying assumption that consumers have equal weight and bargaining powers in negotiating transactions. However, consumers may not have all the information necessary to make a fully informed decision about products and services, nor about the legal rights and obligations that may arise from that transaction. Government intervention may be appropriate where governments can improve market outcomes and address market failure effectively.

Consumer protection legislation is generally developed in response to problems experienced by consumers when purchasing goods or services.

Markets may fail to operate competitively or efficiently for a number of reasons. Most commonly market failures arise in the presence of:

- ***Public goods*** The nature of these goods means that even though the benefits to the public are great, the private sector does not have the incentive to invest in them, or if it does invest it will be at less than the optimum level for society. The reason for private sector under-investment is typically that the supplier cannot prevent those not paying for the good or service from enjoying its benefits. Public goods can also be non-rivalrous so that no matter how many people enjoy them, the supply is not diminished.

  Examples of public goods are lighthouses, street lighting, defence and some kinds of research.

- ***Externalities*** These apply where an activity, good or service has unintended spill-over effects on others. They can be negative, for example a factory discharging waste and polluting a water course, or they could also be positive, such as an investment in agroforestry that also assists in the reduction of salinisation on an adjacent farm.

  An externality per se does not justify intervention, it is only justified where the benefits of intervention are greater than the costs.

- ***Natural monopoly*** These exist where capital costs are so high that it is not worthwhile for a competitor to duplicate the capital to enter the industry. The costs provide a natural barrier to entry and duplication of the capital can mean costs would be lowest under a single supplier.

  Examples of natural monopoly industries include gas and water pipelines and electricity grids.

- ***Information asymmetry*** In some markets there is a great difference between the seller's knowledge of the good or service being sold and the buyer's knowledge. There may be significant costs to consumers in adequately informing themselves about prospective purchases. Further, some consumers will be more proficient than others in assessing and interpreting information.

  For example, the used car salesman knows much more about the quality of the car being sold than the buyer. The result of this is that prices can be kept higher for a service or product that the quality of the product would bring if the buyer were better informed.

When market failure occurs it is necessary to firstly consider whether government action is required, or is it better left for the market to remedy itself. The role of government regulation in addressing market failures is generally concerned with promoting the more effective operation of markets in order to ensure an efficient allocation of resources. In determining the most appropriate government action to implement it is necessary to consider a range of interventions, identifying the one which imposes the least cost in return for the greatest public benefit.

5.3 How the Consumer Credit Code addresses failures in the consumer credit market

As noted previously, the primary purpose of the Consumer Credit Code is to assist in the efficient functioning of the credit sector. The types of arguments put in favour of an efficient credit provision sector are similar to those in favour of standard weights and measures. They are:

- Reduced transaction costs, particularly information search costs for consumers. That is, without the Consumer Credit Code consumers may not be provided with all the necessary information to allow them to make an informed choice about whether or not to initiate a credit contract in the first instance, and then which credit contract to accept. If the information required to be provided by the Consumer Credit Code were not, consumers are likely to occur both physical costs and opportunity costs in the seeking out of all the information they require;

- Increased transaction certainty. That is, consumers are likely to be more confident about entering into a credit contract where they are able to base their decisions on information provided directly from the credit provider; and

- Occurrence of transactions which would not otherwise have occurred. That is, the Consumer Credit Code specifically provides redress mechanisms for both pre- and post-contract disputes between consumers and credit providers. Without these redress mechanisms, consumers may be less confident to commit to a credit contract, thereby reducing the overall level of economic activity.

Further, it can be argued that a poorly performing credit sector has implications for the wider economy. That is, credit as an entity itself has limited value, rather the value that credit provides lies in its purchasing potential. The provision of credit facilitates demand for other products (such as houses, cars and whitegoods) which may otherwise not exist. Hence, the purchases made with credit have greater multiplier effects on the economy than the provision of credit itself.

While the above comments identify the known benefits of an efficient functioning credit sector, the Wallis inquiry into the banking industry found two areas of market failure in the consumer credit market, being:

- Inadequate disclosure of information or information asymmetries between credit providers and consumers; and

- Unfair or fraudulent conduct by market participants (Wallis et al 1997).

We note, however, that fraudulent conduct is a reflection upon the mismatch of information between parties to a transaction, and that this issue is really an outcome of information asymmetry existing in the marketplace. That is, it would be difficult for a credit provider to defraud a debtor who was as knowledgeable about the transaction as the credit provider. Nevertheless, regardless of information asymmetries, credit providers may act unfairly if the opportunity arises and they are inclined to do so.

Information asymmetries arise when buyers lack sufficient information to assess the competitiveness of service offerings. In the consumer credit market, the plethora of fees and charges, and the different ways of applying interest rates[11], mean that consumers are often not aware of the price they are paying for consumer credit. A number of adverse outcomes flow from this.

Firstly, the price mechanism may not be effective in promoting competitive market outcomes. Suppliers who offer credit at uncompetitive prices may be able to retain market share because consumers may not be aware that the prices being charged are uncompetitive. As a result, prices, profits and costs in the consumer credit market may be higher than if the market was more competitive. This contrasts with other markets where suppliers who charge excessive prices lose market share to lower-priced suppliers, and this competitive process encourages cost containment, efficient and competitive prices.

Secondly, consumers' lack of awareness of the cost of consumer credit may mean that they make inappropriate consumer credit package selections. Instead of selecting the consumer

[11] For example, interest rates may be fixed or variable, applied on daily or monthly balances.

credit package which provides the lowest cost credit given their circumstances (eg length of loan, repayment ability, flexibility to terminate the contract), consumers' inability to understand and compare packages may mean that they select a package that is less cost effective in their circumstances. This is another factor leading consumers to pay an excessive price for consumer credit.

In the context of differentiating consumers by income, we note the recent study, 'Taking Credit', which was completed by Mr. Justin Malbon of the Griffith University Law School for the Consumer Credit Code Post Implementation Review Committee. This study found that the behaviour of consumers when making decisions about purchasing credit is largely the same regardless of income category, gender or residential location. However, this research found that the lower income consumers might be more inclined to take the loan they are offered without question as they believe it is the only loan they will be offered.

The Consumer Credit Code seeks to address information asymmetry by requiring compulsory disclosure. The aim of disclosure is to increase awareness of the price of credit by requiring disclosure of the interest rate and all fees that might be expected to be charged during the life of the loan, as well as the term of the loan.

The Consumer Credit Code also provides for a formula to calculate a comparison rate enabling consumers to compare the price of credit provided by different providers. While the Consumer Credit Code mandates the formula for calculating a comparison rate, there is no requirement for credit providers to disclose the comparison rate. However, if the comparison rate is disclosed, it must be accompanied by the appropriate warning set out in Regulation 12. The purpose of the warning is to inform consumers that the comparison rate applies to an example of a particular loan and thus may not be directly comparable to comparison rates calculated for other particular loans.

In this regard, the Consumer Credit Code may be considered as a form of pro-competitive regulation. The Consumer Credit Code's provisions are designed to promote information in the consumer credit market, so that consumers can compare the prices of consumer credit offered by different suppliers, encouraging competitive behaviour and outcomes.

That is, the benefits of the Consumer Credit Code with respect to information disclosure, can be simply summarised in the following points:

- Information disclosure reduces information asymmetry for this complex product;
- With the availability of comparable information, consumers are able to shop around, compare products and select a product that is right for them; and
- There is an incentive for credit providers to differentiate their product, by price and other features, as consumers are able to compare benefits and costs between credit providers.

Even where consumers are fully informed, a credit provider may nevertheless act unfairly in certain circumstance, such as the instance where the debtor is 'desperate' for cash. For example, the low income debtor who is inclined to take the first loan they are offered, as

identified in the Malbon study, may provide an opportunity for an unscrupulous credit provider to act unfairly.

The Consumer Credit Code seeks to address unfair conduct through misconduct provisions, including:

- Reopening of unjust credit contracts, where unjust includes unconscionable, harsh or oppressive; and
- Civil penalties regime for contravention of 'key requirements' of the Consumer Credit Code.

In the absence of these particular misconduct provisions, some credit providers may act unfairly, as the profit motive provides the impetus for misconduct to occur. Hence the regulatory framework provides mechanisms to redress opportunism (or misconduct of credit providers).

5.4 Description of the Consumer Credit Code

The following sections provide a brief summary of the Consumer Credit Code, highlighting the key features of each Part. A more detailed overview is provided in Appendix A.

5.4.1 Part 1 – Preliminary

Part 1 of the Consumer Credit Code sets out the scope of the legislation, the definitions to be applied and the presumptions that may be made in relation to the application of the Consumer Credit Code. The key features of this part are that it:

- Defines credit, amount of credit and credit contract; and
- Sets out explicitly what credit the Consumer Credit Code regulates and what it does not regulate.

Both these aspects of the Consumer Credit Code are discussed in greater detail in Chapter 9.

5.4.2 Part 2 – Credit contracts

Part 2 of the Consumer Credit Code outlines key provisions governing contract formation and formalities, in particular:

- The form and content of the credit documentation;
- Pre-contractual disclosure requirements;
- The debtor's right of termination;

- Acceptance of early payments;
- Application of interest charges;
- Restrictions on fees and charges; and
- Frequency and content of periodic statements of account.

This Part of the Consumer Credit Code introduces consistency in the presentation of credit information and contract documentation as well as ensuring truthful disclosure of all relevant information about credit arrangements, including interest rates, fees, and commissions. The disclosure provisions within Part 2 allow debtors to more easily compare credit products and to make informed choices when purchasing credit.

5.4.3 Part 3 – Related mortgages and guarantees

Part 3 of the Consumer Credit Code outlines additional provisions governing contract formation and formalities relating specifically to mortgages and guarantees, in particular:

- Form of and content of mortgage documentation;
- Copies of mortgage documentation to be provided to mortgagor;
- Amount that may be secured;
- Prohibited securities;
- Process for assignment or disposal of mortgaged property;
- Form of guarantee documentation; and
- Copy of credit contract to be provided to guarantor.

This Part of the Consumer Credit Code contains a number of provisions designed to ensure the protection of mortgagors and guarantors by ensuring disclosure of relevant information and that credit providers cannot impose unreasonable obligations on the mortgagors or guarantors.

5.4.4 Part 4 – Changes to obligations under credit contracts, mortgages and guarantees

Part 4 of Consumer Credit Code is concerned with changes to obligations under credit contracts, mortgages and guarantees. It deals separately with changes made:

- Unilaterally by the credit provider;

- By mutual agreement of the parties to the credit contract; and

- Changes made on account of hardships and unjust transactions.

Regarding unilateral changes and changes by mutual agreement, the Consumer Credit Code sets out how and when debtors are to be informed of changes relating to interest rates, repayments, credit fees and charges and other changes.

The Consumer Credit Code allows a debtor, who is experiencing financial hardship, to make an application to the credit provider to make particular changes to the credit contract, where these changes would ensure that the debtor does not default on the credit contract. Furthermore, the debtor may apply to the courts if the credit provider does not change the credit contract in accordance with the application.

This Part of the Consumer Credit Code also contains provisions to allow the courts to reopen transactions giving rise to a contract, mortgage or guarantee or a change to such, if satisfied that, in the circumstances when it was entered into or changed, it was unjust. The court may also review unconscionable changes to the annual percentage rate, establishment fee or charge, termination fees and charges and prepayment credit fees and charges.

5.4.5 Part 5 – Ending and enforcing credit contracts, mortgages and guarantees

Part 5 of the Consumer Credit Code deals with ending and enforcing credit contracts, mortgages and guarantees, in particular:

- Ending of credit contract by a debtor through, for example, the early payout of the contract;

- Enforcement procedures following a default in relation to a credit contract, mortgage or guarantee;

- Debtor’s right to negotiate with the credit provider for a postponement of enforcement proceedings, or to apply to the courts for a postponement;

- Procedures for repossession of mortgaged goods; and

- Enforcement Expenses.

5.4.6 Part 6 – Civil penalties for defaults of credit providers

Part 6 of the Consumer Credit Code establishes the civil penalty regime and other remedies for breaches of the Consumer Credit Code by credit providers. The provisions within Part 6 are divided into two divisions:

- Division 1 deals with contraventions of ‘key requirements’, where these key requirements relate mainly to disclosure provisions and prohibited monetary obligations; and

- Division 2 deals with other contraventions of the Consumer Credit Code and allows for compensation to debtors who have suffered as a result of the breach.

The court may hear applications relating to breaches of key requirements and, if it declares that a credit provider has breached a key requirement, order the credit provider to pay a civil penalty. A credit provider who contravenes a key requirement of the Consumer Credit Code faces a number of possible sanctions, including:

- Loss of interest charges under the contract;

- A maximum civil penalty (or fine) of up to $500,000 per contravention; and

- Compensation to borrowers who have suffered as a result of the error.

Part 6 also introduces cross-vesting by allowing a credit provider or Government Consumer Agency to register with the court of one jurisdiction an order made by a court in another jurisdiction.

5.4.7 Part 7 – Related sale contracts

Part 7 of the Consumer Credit Code deals with related sale contracts and linked credit providers, in particular:

- Liability of credit providers for suppliers’ misrepresentations;

- Liability of credit providers in relation to goods; and

- Termination of related transactions.

A ‘linked credit provider’ is a credit provider who has an arrangement with a supplier of goods such that the supplier refers consumers to the credit provider, or the supplier signs customers up for the credit provider. For example, a consumer purchasing a television from a major retailer on credit or interest free will typically be provided credit with a finance company. In this example, the finance company is the linked credit provider.

Under the Consumer Credit Code, the supplier and linked credit provider are jointly and severally liable to the debtor for loss or damage suffered by the debtor as a result of misrepresentation, breach of contract or failure of consideration in relation to the contract.

5.4.8 Part 8 – Related insurance contracts

Part 8 of the Consumer Credit Code is concerned with related insurance contracts (which insure the obligations of the debtor under the credit contract), in particular:

- Formalities relating to the taking out of insurance;
- Financing of insurance premiums over mortgaged property;
- Limits on commissions for consumer credit insurance;
- Formalities for dealing with a rejection of a proposal for insurance; and
- Termination of a related insurance contract if the credit contract is terminated.

Furthermore, a credit provider may not:

- Force a debtor to take out a related insurance contract (unless it is a form of insurance approved by the Consumer Credit Code)
- Require the debtor to take out insurance with a particular insurer; or
- Require the debtor to take out insurance under unreasonable terms.

5.4.9 Part 9 – Advertising and related conduct

Part 9 of the Consumer Credit Code regulates credit advertising and related conduct involving the promotion of credit, in particular:

- Appropriate content for advertisements;
- Persons liable for advertisements (for redress purposes);
- False or misleading representations made by any party to a credit contract; and
- Harassment and canvassing of credit at residential premises.

No statement of interest charges or costs may be included in an advertisement unless it is the annual percentage rate, the comparison rate and/or a statement to the effect that other fees and charges are payable.

5.4.10 Part 10 – Consumer leases

Part 10 of the Consumer Credit Code governs consumer leases, in particular:

- Scope and presumptions relating to the application of the Consumer Credit Code;

- Form and content of consumer lease documentation;
- Application of other sections of the Consumer Credit Code; and
- Formalities for ending and enforcing consumer leases.

The Consumer Credit Code defines a 'consumer lease' as:

> *'... a contract for the hire of goods by a natural person or strata corporation under which that person or corporation does not have a right or obligation to purchase the goods'.*

This contrasts to a goods lease (where there is a right or obligation to purchase the goods) which is treated as any other credit contract under the Consumer Credit Code.

Although Part 10 brings consumer leases within the ambit of the Consumer Credit Code, the provisions within Part 10 are significantly less stringent than the consumer credit provisions within the Consumer Credit Code.

5.4.11 Part 11 – Miscellaneous

Part 11 of the Consumer Credit Code outlines additional general provisions relating to consumer credit, and deals separately with:

- Tolerances and assumptions relating to disclosure requirements;
- General requirements relating to credit documentation, including contracts and notices;
- General provisions relating to the assignment of rights and obligations under a credit contract;
- General provisions relating to the delivery of notices and other credit documentation; and
- Provisions relating to offences.

5.5 Administration and differences across jurisdictions

The description of the Consumer Credit Code provided in the previous section is based on the template consumer credit legislation passed in Queensland, namely the *Consumer Credit (Queensland) Act 1994* (the Initial Legislation). Under the *Australian Uniform Credit Laws Agreement 1993*, the other Australian States and Territories were required to enact either:

- Legislation enabling the Consumer Credit Code to take effect in their jurisdiction; or
- Alternative consistent legislation, which does not conflict with or negate the operation of the Consumer Credit Code.

With the exception of Western Australia (which enacted alternative consistent legislation), all States and Territories passed enabling legislation. The legislation in Tasmania, while being enabling legislation, is slightly different in that changes to the Consumer Credit Code are not adopted automatically. Rather, the *Consumer Credit (Tasmania) Act 1996* adopted the Consumer Credit Code as in force on the date the Tasmanian legislation commenced, and any future amendments have to be approved by both houses of parliament and be proclaimed by the Governor before applying as law in Tasmania.

The Western Australian legislation, while being 'alternative consistent legislation', has some differences with the Initial Legislation. These differences, which are presented in Appendix B, are not material in relation to the anti-competitive provisions of the Consumer Credit Code.

Although the aim is to provide for uniform national legislation, the *Australian Uniform Credit Laws Agreement 1993* specifically allows variations in legislation between jurisdictions to provide for:

- The fixing of maximum interest rates payable under consumer credit contracts;
- The establishment of trust funds with designated purposes into which forfeited interest charges may be paid;
- The establishment of a scheme for the licensing or registration of credit providers;
- The vesting in a Tribunal of jurisdiction which under the Initial Legislation is vested in a Court; and
- Such other matters as are approved by unanimous resolution of the Ministerial Council.

The *Australian Uniform Credit Laws Agreement 1993* also required the States and Territories to endeavour to ensure that the administration of the credit legislation is consistent. To facilitate national uniformity in administration, the Standing Committee of Officials of Consumer Affairs (SCOCA) established the Uniform Consumer Credit Code Management Committee (the Management Committee) in 1996.

The role of the Management Committee is to monitor and coordinate all activities relating to the Consumer Credit Code in order to ensure consistency in its implementation and administration across jurisdictions, and specifically to:

- Consider amendments to the Consumer Credit Code and regulations;
- Review the applications for exemption from the Consumer Credit Code;
- Develop and administer procedures, schemes and arrangements to ensure consistency in implementation of the Consumer Credit Code.

Details of the legislation passed in each jurisdiction, the variations in the legislation and the administrative arrangements are presented in Appendix B of this report.

5.6 Review of Consumer Credit Code consistency with part IV of the Trade Practices Act 1974 and the Competition Codes

The Terms of Reference require that consideration be given to whether the Consumer Credit Code contravenes the competitive conduct rules in Part IV of the *Trade Practices Act 1974* and the Competition Codes of each jurisdiction.

5.6.1 Trade Practices Act 1974

Part IV of the *Trade Practices Act 1974* deals with restrictive trade practices and prohibits practices that may restrict competition in a market, including the practices of exclusive dealing and resale price maintenance. More specifically, the provisions of Part IV are:

- **Sections 45 – 45C**, which render unenforceable provisions or covenants that have, or potentially have, the effect of substantially lessening competition. Provisions or covenants that have the purpose of fixing, controlling or maintaining prices, or a discount, in relation to goods and services are deemed to have the effect of substantially lessening competition;

- **Sections 45D – 45EB**, which deal with boycotts and prohibit two or more persons engaging in conduct that hinders or prevents trade between a third and fourth party, or causes substantial damage or loss to the fourth party. Furthermore, when the two or more persons engaging in the conduct are members of the same organisation of employees, that organisation is deemed to have participated in that conduct. Boycotts are permitted in certain circumstances, namely where the boycott relates to remuneration and employment conditions, environmental protection or consumer protection;

- **Sections 46 – 46B**, which prohibits the misuse of market power. That is, a corporation with a substantial degree of market power may not use that power to eliminate or damage a competitor, prevent entry into a market or prevent a person from engaging in competitive conduct;

- **Section 47**, which prohibits the practice if exclusive dealing, where this practice would have the effect of substantially lessening competition. It also sets out what constitutes exclusive dealing and the exclusions to the provision;

- **Section 48**, which prohibits the practice of resale price maintenance;

- **Sections 50 – 50A**, which prevent acquisitions of assets where that acquisition would have the effect of substantially lessening competition;

- **Section 51**, which notes that anything that is authorised by any Act or regulation of the Commonwealth or any State or Territory, is to be disregarded in determining whether a person has contravened Part IV; and

- **Section 51AAA**, which notes that it is the Parliament's intention that Part IV should be able to operate concurrently with any law of a State or Territory, unless it is directly inconsistent with Part IV.

Our analysis indicates that the Consumer Credit Code does not contravene any of the provisions of Part IV of the *Trade Practices Act 1974*; however, this analysis highlighted a number of provisions in the Consumer Credit Code which are similar to those in the *Trade Practices Act 1974*. These provisions are considered later as part of the analysis of the reform options.

5.6.2 Competition Codes

The *Conduct Code Agreement 1995*, which is one of the inter-governmental NCP agreements between the Commonwealth, State and Territory governments, required each of the jurisdictions to pass legislation to enable the Competition Code to apply as law in their jurisdiction. In each jurisdiction, the enabling legislation is the Competition Policy Reform Act of that jurisdiction.

As defined in s.1 of the *Conduct Code Agreement 1995*, 'Competition Code' means

> *'... the text in:*
>
> *(a) the Schedule version of Part IV of the Trade Practices Act;*
>
> *(b) the remaining provisions of that Act (except sections 2A, 5, 6 and 172), so far as they would relate to the Schedule version if the Schedule version were substituted for Part IV; and*
>
> *(c) the regulations under that Act, so far as they relate to any provisions covered by paragraph (a) or (b)*
>
> *applying as a law of a participating jurisdiction.'*

The 'Schedule version' of Part IV is set out in a schedule to the *Trade Practices Act 1974*. This version is almost an exact copy of Part IV, but for the following key differences:

- Where Part IV reads 'corporation', the Schedule version reads 'person' (although person is not defined in the *Trade Practices Act 1974*);

- Section 45D (relating to boycotts) has been reduced in scope relative to Part IV and other sections relating to boycotts (ss. 45DA, 45DB, 45DC and 45DD) have been omitted in the Schedule version;

- Sections 45E, 45EA and 45EB relating to the prohibition of contracts, arrangements or understandings affecting the supply or acquisition of goods and services have been omitted from the Schedule version;

- Sections 46A and 46B, which relate to misuse of market power in trans-Tasman markets, have been omitted from the Schedule version;

- Section 50A, which relates to acquisitions that occur outside of Australia, has been omitted from the Schedule version; and

- Section 51AAA, which relates to the concurrent operation of State and Territory laws, has been omitted from the Schedule version.

Consistent with the conclusion reached relating to any breaches of Part IV of the *Trade Practices Act 1974*, the Consumer Credit Code does not breach the Competition Code of any of the participating jurisdictions.

6 Post Implementation Review

6.1 Introduction

In August 1997 the Ministerial Council on Consumer Affairs (MCCA) agreed to undertake a Post Implementation Review (PIR) of the Consumer Credit Code to determine:

- Whether the objectives of the Consumer Credit Code are being achieved;
- The impact the Consumer Credit Code has had on the marketplace; and
- Opportunities for improving the national management structure of the Consumer Credit Code.

The three broad purposes of the PIR were:

- To inform and provide relevant input to the competition policy review;
- Pending full competition policy review, inform the Ministerial Council as to the practical effects of the Consumer Credit Code's implementation to date; and
- To make appropriate recommendations to the Ministerial Council for immediate improvements to the national management / administrative structure for the Consumer Credit Code (that is, matters identified as being able to be addressed without pre-empting the competition policy review).

Further, the terms of reference for the PIR were to address the following key areas:

- The impact of the Consumer Credit Code's 'truth in lending provisions' on borrowers;
- The relevance of the law to the current consumer credit marketplace; and
- The impact of the Consumer Credit Code's administrative structure on the achievement of uniformity between jurisdictions.

The PIR is now completed, with the PIR Project Team having presented to the MCCA a report outlining a series of recommendations and technical amendments to the Consumer Credit Code. A summary of the key recommendations is presented in the following section.

6.2 Summary of recommendations

The project team proposed that the Ministerial Council adopt the following recommendations.

Terms of Reference 1

1.1 Amend Regulation 13 to provide a simplified "Schumer Box" format containing essential financial information. Other essential information would be provided outside the "box" and would prominently indicate that other important information was contained in the contract document.

1.2 Amend the Consumer Credit Code to clarify which fees and charges are required to be:

- Disclosed in the simplified Schumer Box; or
- Otherwise disclosed/identified in the pre-contractual documentation but outside the Schumer Box.

1.3 Request the Management Committee to provide further detail on goods purchased with credit with which there is associated consumer detriment and make recommendations to the Ministerial Council for an interval or cooling off period in respect of those goods.

1.4 Require a comparison rate to be given for fixed term products in advertisements and in the "Schumer Box" on the proposed summary sheet.

Terms of Reference 2

2.1 Request the Management Committee to further examine and consult on the implications of Rafiqi and McKenzie v Smith to determine whether the decision is consistent with the Consumer Credit Code's policy in respect of "deferred debt".

2.2 Amend the provision of section 6 of the Consumer Credit Code to provide a clearer distinction between the "amount of credit" and "interest charges". This may be achieved by providing a definition of "interest" and making reference in this section to the Consumer Credit Code's definition of "cash price".

2.3 Amend the Consumer Credit Code's definition of "cash price" to ensure that it adequately applies to goods which are not normally sold for cash by including the concept of "reasonable value".

2.4 Amend the Consumer Credit Code so that the solicitor is the credit provider where consumer lending is organised by a solicitor on behalf of investors or from investment funds.

2.5 Revise the Consumer Credit Code's regulation of insurance to remove overlap and duplication between the Consumer Credit Code's regulation of insurance and the Insurance Contracts Act. The Consumer Credit Code should regulate insurance only where a specific need arises because of its relationship with the credit contract or where the policy of the Consumer Credit Code is to regulate an aspect of insurance

that is not otherwise regulated. Where there is a need to make reference to other regulation, this should be achieved by signposting the provisions in the Consumer Credit Code.

2.6 Amend section 133 of the Consumer Credit Code to:

(a) clarify the scope of this section;

(b) to ensure that this section more clearly expresses the Consumer Credit Code objectives in relation to third line forcing; and

(c) harmonise, where appropriate, the Consumer Credit Code's approach to "bundled products" with that taken by the ACCC under section 47 of the Trade Practices Act.

2.7 Review the advertising provisions contained in Part 9 of the Consumer Credit Code in the light of the Post Implementation Research Project.

2.8 Review the Consumer Credit Code's regulation of linked credit providers to determine whether there is unnecessary overlap and duplication between Part 7 of the code and the Trade Practices Act.

2.9 Amend section 66(3) of the Consumer Credit Code to remove doubt as to the application of this section of continuing credit contracts.

2.10 Revise the monetary limit of $125,000 on the application of sections 67-69 imposed by section 66(3) of the Consumer Credit Code to a level sufficient to cover most Australian home mortgages.

2.11 Amend the requirements for default notices under section 80(3) of the Consumer Credit Code to include additional information stating:

(a) that the notice is a default notice;

(b) the date after which enforcement action may commence;

(c) that repossession may not extinguish the debtor's liability; and

(d) the debtors right to make applications for hardship and postponement.

2.12 Request the Management Committee to monitor the level of new fees and charges that are unilaterally imposed by credit providers during the course of credit contracts.

2.13 Revise the monetary limit of $125,000 on the application of Division 3 of Part 5 of the Consumer Credit Code to a level sufficient to cover Australian home mortgages.

2.14 Amend Part 10 of the Consumer Credit Code (consumer leases) to require pre-contractual disclosure of the information detailed in section 152(1).

2.15 Amend section 155(1) of the Consumer Credit Code to include a reference to section 144 of the Consumer Credit Code.

2.16 Amend section 15(G) and 100 to ensure that contingency fees and charges are not key requirements.

2.17 Request the Management Committee to examine the level of compliance with section 15N(d) of the Consumer Credit Code.

2.18 Review existing state and territory laws relating to finance brokers to provide a consistent approach to the review of unconscionable broker fees and charges and standards for broker conduct.

2.19 Recognise electronic transactions, by harmonising the Consumer Credit Code, as far as possible, with the Electronic Transactions Bill 1999. In addition, adopt specific consumer protection measures to respond to the issues that arise specifically out of the consumer credit environment.

2.20 Amend the Consumer Credit Code's definitions of "writing" and "sign" to make it clear that the code recognises both electronic records and the electronic authentication of records.

2.21 Give further consideration to those types of contracts, such as real property mortgages, which need to be exempted from being able to be entered into electronically.

2.22 Permit electronic communications where the consumer has an electronic address, the means to notify a change of address, elects to receive communications electronically and has a right to cancel this election.

2.23 Prohibit documentation under the Consumer Credit Code that triggers an enforcement process being able to be provided electronically.

2.24 Implement points 1 to 7 below in relation to the storage and reproduction of information.

1. Ensure that the pre-disclosure statement and the contract is capable of being stored both before and after the transaction is completed.

2. Ensure that all electronic communications delivered electronically are capable of being retained and are accompanied by instructions on how to do so.

3. Ensure that the capacity to store or retain electronic communications includes both the capacity to copy them on a personal electronic file and make a paper print-out of it.

4. Ensure that any electronic communications so retained be able to be done in a manner that satisfies conditions of reliability and identification of place, time and date of origin and receipt of the information.

5. Ensure that electronic communications permit the display of text messages in a clear and readily understandable format.

6. Require that credit providers take reasonable steps to ensure that the pre-contractual information and the contract are complete and unaltered at the point at which a consumer receives them. Of course, this needs to be done in a way that does not prevent the electronic information from being stored by the consumer.

7. Give further consideration to the kinds of documentation of other information that would not be considered to be appropriate to post on a web site for the purposes of providing that information to the consumer.

2.25 Require that pre-contractual and contractual information is able to be scrolled though before any contract can be entered into. This documentation should be required to be sent in a form that enables consumers to download it or print it out if they choose.

2.26 Amend section 162 of the Consumer Credit Code or make a regulation under section 13 to ensure that important electronic communications are clearly and conspicuously expressed without distractions.

2.27 Ensure that the Consumer Credit Code's minimum requirement for font size for paper based documentation is also required for electronic communications.

2.28 Ensure that consumers are given the opportunity to challenge unfair presumptions concerning the sending and receipt of messages.

2.29 Ensure that consumers are given the opportunity to challenge unfair contractual terms concerning the attribution of a message to them.

2.30 Require credit providers to disclose a physical address in the context of electronic communications only.

2.31 Support a two-stage process by:

1. requiring the introduction of a multi-clicking process at the stage at which the consumer is considering the loan product and expressing their interest in proceeding to the formal contracting process; and

2. requiring the introduction of a mechanism that does not involve clicking at the stage at which they express their agreement to enter into legal relations. This mechanism would involve some kind of electronic signature, which is reliable in authenticating the identity of the consumer and of the intent of that person to

be associated with the message. The consumer ought to have the option at this stage to enter into the contract by other means.

2.32 Address the issue of currency disclosure in the electronic commerce context only.

2.33 In adhering to the objective of functional equivalence, the issue of a right of reflection ought not to be addressed in the context of electronic communication only.

2.34 Request the Management Committee to monitor the level of popularity of Internet transactions with overseas credit providers with a view to developing a targeted educational campaign on the potential problems associated with obtaining credit from overseas if any problems are identified.

2.35 Request the Management Committee to convey any concerns to the Federal Government via the National Office for the Information Economy.

Terms of Reference 3

3.1 Amend the Uniformity Agreement to require adoption of amendments to the Consumer Credit Code or Regulations by all jurisdictions within six months of the passage of those amendments in Queensland.

3.2 Continue the operation of the Management Committee until completion of the stage 2 competition policy review and any subsequent amendment of the Consumer Credit Code.

3.3 Provide a mechanism to legally link guidelines so that they can assist in interpreting the provisions of the Consumer Credit Code.

3.4 Establish a cross-vesting scheme under the code for relevant judicial and, where appropriate, administrative functions.

Technical Amendments

4.1 Defer further consideration of technical amendments until completion of both the PIR and the National Competition Policy Review, and consider these in any subsequent drafting process arising from these processes.

6.3 Competition issues of proposed amendments

Of interest to this National Competition Policy review are those recommendations that may be considered to potentially impact competition. That is, while the primary purpose of this study is to analyse current provisions within the Consumer Credit Code that have been identified as potentially impacting on competition, the terms of reference of this review has also identified that the PIR recommendations should also be considered in the light of competition policy.

The following PIR recommendations have been identified as potentially impacting on competition.

- **Recommendation 1.1**

  Amend Regulation 13 to provide a simplified 'Schumer Box' format containing essential financial information. Other essential information would be provided outside the 'box' and would prominently indicate that other information was contained in the contract document.

- **Recommendation 1.2**

  Amend the Consumer Credit Code to clarify which fees and charges are required to be:

  - Disclosed in the simplified 'Schumer Box'; or
  - Disclosed / identified in the pre-contractual documentation, but outside the 'Schumer Box'.

- **Recommendation 1.4**

  Require the comparison rate to be given for fixed term products in advertisements and in the 'Schumer Box' on the proposed summary sheet.

- **Recommendation 2.11**

  Amend the requirements for default notices under section 80(3) of the Consumer Credit Code to include additional information stating:

  - that the notice is a default notice;
  - the date after which enforcement action may commence;
  - that repossession may not extinguish the debtor's liability; and
  - the debtors right to make applications for hardship and postponement.

- **Recommendation 2.14**

  Amend Part 10 (consumer leases) of the Consumer Credit Code to require pre-contractual disclosure of the information detailed in Section 152(1).

These particular recommendations have been identified as potentially impacting on competition through additional information disclosure requirements, which increase compliance costs for credit providers. These potential compliance costs include once-off initial costs associated with amending existing document templates to accommodate the additional requirements, as well as ongoing (though incremental) costs associated with

printing, copying and delivery of documentation. Furthermore, these potential compliance costs may act as a prohibitive barrier to entry for small credit providers.

It should be noted that the objectives of recommendations 1.1 and 1.2 above are to simplify the disclosure documents that should result in a benefit to both consumers and credit providers. Overall, the benefits of these recommendations is that they allow consumers to be aware of the key elements of the credit arrangements.

The other PIR recommendations have not been considered as anti-competitive as they either:

- Have no immediate impact on the operation of the Consumer Credit Code, such as requests for further research to be undertaken on a particular issue;
- Clarify the terms and/ or scope of the Consumer Credit Code;
- Potentially reduce the level of regulation; or
- Relate to the management, rather than operation, of the Consumer Credit Code.

Some of the recommendations relating to electronic transactions (PIR Recommendations 2.19 to 2.35) would result in provisions that regulate the conduct of credit providers. However, they are considered to have minimal implications in competition policy terms (ie compliance costs and competition between credit providers).

6.4 Summary

The PIR recommendation which have been identified as potentially impacting on competition will be reviewed in the options for reform analysis, while the remaining PIR recommendations will be considered in the context of the broader restrictions of the Consumer Credit Code.

7 Public consultations and submissions

7.1 Introduction

A crucial component of the conduct of a legislation review is consultation with parties that have an interest in the legislation under review. This is required so as the views of all stakeholders are taken into consideration when assessing whether or not any restrictive provisions contained within the legislation or alternative options provide a net benefit.

This Chapter outlines the consultation process undertaken. Details of the submissions are presented in the analysis of each restriction (where relevant) and fully summarised in Appendix C of this report.

7.2 Key stakeholders

The key stakeholder groups identified were:

- Consumers, particularly debtors, mortgagors and guarantors;
- Consumer agencies, such as consumer credit legal services and consumer protection organisations;
- Consumer credit providers, including banks, credit unions, finance companies and other credit providers;
- Consumer credit insurance providers; and
- Government departments and agencies.

7.3 Consultation process

The stakeholder consultation was conducted in two stages:

- Calling for submissions from interested parties; and
- Conducting targeted face-to-face interviews with key stakeholders.

7.3.1 Call for submissions

A public notice calling for submissions from interested parties was published in nationally circulated newspapers, as well as the main newspaper in each State and Territory. To assist stakeholders in the preparation of their submissions, an Issues Paper was prepared which provided details of the review being undertaken, the potentially anti-competitive provisions within the legislation and the reform options under consideration.

This Issues Paper was sent out upon request from interested stakeholders and was also forwarded to key stakeholder groups.

There were seven written submissions received:

- Australian Bankers' Association (ABA);
- Australian Finance Conference (AFC);
- Commonwealth Consumer Affairs Advisory Council (CCAAC);
- Consumer Credit Legal Service (Vic), Consumer Credit Legal Centre (NSW) and Consumer Credit Legal Service (WA) (combined submission) (CCLS);
- Ms Denise McGill, Member of the Centre for Commercial and Property Law;
- Members of the Consumer Credit Subcommittee of the Banking, Finance and Consumer Credit Committee of the Law Council of Australia (the LCA-CCS); and
- Mr Randall Dennings, a member of the public who is a solicitor.

7.3.2 Targeted stakeholder consultations

KPMG conducted face-to-face interviews with various stakeholders, including:

- Australian Association of Permanent Building Societies;
- Australian Bankers' Association;
- Australian Finance Conference;
- Consumer Credit Legal Centre, New South Wales;
- Consumer Credit Legal Service, Victoria; and
- Legal Aid Queensland.

7.4 Summary

The consultation process revealed that, while there was general consensus that the Consumer Credit Code should be retained, there were quite a number of issues of concern to stakeholders. Issues most commonly raised were those relating to disclosure requirements, national uniformity, duplication with other legislation and civil penalties. As noted previously, the particular issues raised are considered in relation to the relevant restrictions and summarised in Appendix C.

8 Objectives of the Consumer Credit Code

A standard component of all legislation reviews is the clarification of the legislation's objectives and an examination of the relevance and appropriateness of those objectives.

8.1 Clarification of the objectives

The objectives of the Consumer Credit Code, as stated in the Explanatory Memorandum of the Queensland Act, are:

- To provide laws which apply equally to all forms of consumer lending and to all credit providers, and which are uniform in all jurisdictions in Australia.
- The legislation is based on the principle of truth in lending that will allow borrowers to make informed choices when purchasing credit.
- The Consumer Credit Code applies rules that regulate the credit provider's conduct throughout the life of the loan, but without restricting product flexibility and consumer choice.
- The policy of the legislation is to rely generally on competitive forces to provide price restraint but to provide significant redress mechanisms for borrowers in the event that credit providers fail to comply with the legislation.
- The Consumer Credit Code is designed to apply in a deregulated credit market and provide standards for the provision of credit that will not be overtaken by changes in the financial marketplace.

8.2 Relevance and appropriateness of the objectives

Objective 1: *To provide laws which apply equally to all forms of consumer lending and to all credit providers, and which are uniform in all jurisdictions in Australia.*

The following observations may be made in relation to this objective:

- Credit providers are not homogenous. Rather, they vary by size, type of institution, type of credit products provided, overall product range and customers. Hence, as written, the objective captures all credit providers. Furthermore, to specify specific credit providers may encourage particular credit providers to classify themselves so as to fall outside the scope of the Consumer Credit Code;
- Some credit providers operate branches nationally. Hence, uniform legislation facilitates administration and operational efficiencies in these organisations;

- The obligations of a debtor under a credit contract remain unaffected by any change in the debtor's State or Territory of residence; and
- Credit products are also not homogenous, as highlighted in Chapter 4. Hence, as written, the objective captures all consumer credit products. Furthermore, to specify specific credit products may encourage credit providers to develop products so that they fall outside the scope of the legislation.

Hence, Objective 1 is relevant and appropriate.

Objective 2: *The legislation is based on the principle of truth in lending that will allow borrowers to make informed choices when purchasing credit.*

The following observations may be made in relation to this objective:

- As noted previously, information asymmetry exists in the consumer credit market. This effectively places the consumer at a disadvantage in terms of comparing the cost of different credit products, determining the full cost of credit and relative bargaining power with the credit provider. Hence, it is appropriate that the Consumer Credit Code should aim to provide for truth in lending so as to assist consumers reduce the impact of information asymmetry on them;
- An ill-informed choice of credit product can have serious (negative) financial consequences for the debtor. Hence, the debtor should be able to make an informed decision about purchasing credit; and
- Information asymmetry in the marketplace allows a credit provider to act fraudulently when dealing with debtors. Hence, the provision of information to consumers limits the ability of credit providers to act fraudulently.

Hence, Objective 2 is relevant and appropriate.

Objective 3: *The Consumer Credit Code applies rules that regulate the credit provider's conduct throughout the life of the loan, but without restricting product flexibility and consumer choice.*

The following observations may be made in relation to this objective:

- Product flexibility allows the credit provider to differentiate their products in the marketplace, thereby facilitating competition;
- By providing a choice of credit products, consumers' needs may be better met, thereby adding to the level of consumer welfare; and
- As noted previously, credit providers generally have more bargaining power than consumers. This enables them to act unfairly in their dealings with debtors. Legislation can be used effectively to limit the ability of credit providers to act in this manner.

Hence, Objective 3 is relevant and appropriate.

Objective 4: *The policy of the legislation is to rely generally on market forces to provide price restraint but to provide significant redress mechanisms for borrowers in the event that credit providers fail to comply with the legislation.*

The following observations may be made in relation to this objective:

- Relying on competitive forces to set prices is generally efficient and ensures that debtors base their decisions on the correct price signals. In contrast, artificially setting a price (say the interest rate) may lead to an over-allocation of resources (if set too low) or an under-allocation of resources (if set too high) on behalf of the debtor; and

- Even if prices are generally efficient, there still exists the opportunity for unscrupulous credit providers to take advantage of some debtors. Hence, it is appropriate to provide redress mechanisms to deter this type of activity.

Hence, this objective is relevant and appropriate.

Objective 5: *The Consumer Credit Code is designed to apply in a deregulated credit market and provide standards for the provision of credit that will not be overtaken by changes in the financial marketplace.*

The following observations may be made in relation to this objective:

- As noted previously, technological developments will continue to impact the financial marketplace through cost reductions and product innovations. It is appropriate that credit providers be able to use these technologies to deliver low cost products to consumers; and

- The legislation attempts to manage for outcomes rather than being prescriptive on products and services. This allows the legislation to remain current in a changing financial marketplace.

Hence, Objective 5 is appropriate and relevant.

8.3 Conclusion

In summary, the stated objectives are still generally considered relevant and appropriate in today's marketplace. That is:

- The laws should apply equally to all forms of consumer lending and to all credit providers and they should be uniform in all jurisdictions;

- The legislation should be based on the principle of truth in lending;

- The legislation should not restrict product flexibility and consumer choice;
- The legislation should rely generally on competitive forces for price restraint and there should be appropriate redress mechanisms for credit providers that do not comply with the legislation; and
- The legislation should provide standards for the provision of credit that will not be overtaken by changes in the financial marketplace.

9 Definitions and exemptions

The Consumer Credit Code does not apply to all credit transactions; rather the definitions and exemptions set out in Part 1 delineate the scope of the Consumer Credit Code. The key definitions and exemptions are presented in the following sections.

As per the review requirements, each key definition and exemption is assessed in terms of their appropriateness to the objectives of the Consumer Credit. Of particular importance in this context is the objective of providing laws that apply equally to *all forms of consumer lending* and to *all credit providers*.

9.1 Definitions

9.1.1 'Credit' and 'amount of credit'

'Credit' and 'amount of credit' are defined in s.4 of the Consumer Credit Code as follows:

> *(1) For the purpose of this Code, "credit" is provided if under a contract–*
>
> *(a) payment of a debt owed by one person (the debtor) to another (the credit provider) is deferred; or*
>
> *(b) One person (the debtor) incurs a deferred debt to another (the credit provider).*
>
> *(2) For the purpose of this Code, the "amount of credit" is the amount of debt actually deferred.*
>
> *The "amount of credit" does not include–*
>
> *(a) any interest charge; or*
>
> *(b) any fee or charge–*
>
> *(i) that is to be or may be debited after credit is first provided under the contract; and*
>
> *(ii) that is not payable in connection with the making of the contract or the making of a mortgage or guarantee related to the contract.*

The Post Implementation Review (PIR) identified instalment sales as a category of product for which the above definition may need to be amended to clarify the application of the Consumer Credit Code. This product category includes:

- Terms sale of land, which is a sale of land under which the purchase price is payable by instalments. The vendor lets the purchaser into possession but retains title until conveyance following the final payment; and
- Conditional sale agreement, which is a sale of goods under which the purchase price is payable by instalments. The seller delivers the goods to the buyer but retains title until final payment (Batt 1999).

While *Rafiqi* and *McKenzie vs Smith*[12] both held that the Consumer Credit Code does cover these transactions, concern exists that a higher court may rule otherwise because these transactions do not necessarily incur a 'deferred debt' (Batt 1999). The PIR has recommended this issue for further consideration.

Given that one of the Consumer Credit Code's objectives is to apply to all forms of consumer lending, it would appear that terms sale of land and conditional sale agreements should be within the scope of the Consumer Credit Code, provided that the provisions of s.6 are also satisfied.

With the above exception, the definitions of 'credit' and 'amount of credit' are considered appropriate to the objectives of the Consumer Credit Code as they are broad enough to encompasses *all forms of consumer lending*. In addition, these definitions do not detract from any of the stated objectives.

9.1.2 'Credit contract'

Sections 5 and 6 combined set out the principal conditions necessary for the Consumer Credit Code to apply (McGill & Willmott 1999). A 'credit contract' is defined in s.5:

> *For the purpose of this Code, a "credit contract" is a contract under which credit is or may be provided, being the provision of credit to which this Code applies.*

A 'contract' is further defined in Schedule 1 of the Consumer Credit Code to include a series or combination of contracts, or contracts and arrangements. Schedule 1 also defines that a 'continuing credit contract' means a 'credit contract'.

The Consumer Credit Code defines a credit contract in simple terms that apply to all kinds of credit contract, irrespective of the form of the particular transaction (McGill & Willmott 1999). Furthermore, the broad definition provided in the Consumer Credit Code extends to a number of arrangements that would not constitute a 'contract' under common law (Bingham & Niven 1998).

Hence, the definition of 'credit contract' is also considered appropriate to the objectives of the Consumer Credit Code as it is broad enough to encompasses *all forms of consumer lending*. In addition, this definition does not detract from any of the stated objectives.

Section 6(1) sets out the provisions of credit to which the Consumer Credit Code applies:

> *This Code applies to the provision of credit (and to the credit contract and related matters) if when the credit contract is entered into or (in the case of pre-contractual obligations) is proposed to be entered into–*

[12] Rafiqi and Thomas v Wacel Investments Pty Ltd (1998) ASC 155-024. McKenzie v Smith, Lenehan v Smith (1998) ASC 155-025.

(a) the debtor is a natural person ordinarily resident in this jurisdiction or a strata corporation formed in this jurisdiction; and

(b) the credit is provided or intended to be provided wholly or predominantly for personal, domestic or household purposes; and

(c) a charge is or may be made for providing the credit; and

(d) the credit provider provides the credit in the course of a business of providing credit or as part of or incidentally to any other business of the credit provider.

Criteria (a) and (b) of s.6 of the Consumer Credit Code would capture what a reasonable person would consider to be *consumer lending* and, hence, they may be considered appropriate to the objectives of the Consumer Credit Code.

McGill & Willmott (1999) note that the purpose of restricting the application of the Consumer Credit Code to credit provided wholly or predominantly for personal, domestic or household purposes is that ‘persons who obtain credit for business purposes are more likely to be able to take of themselves and do not need the protection of the statute’.

Section 6(c) requires that a charge is or may be made for providing the credit. Thus if there is no charge for the provision of credit, the transaction is not covered by the Consumer Credit Code.

The PIR highlighted ‘tiny terms’ contracts as such a transaction. These are contracts where the cost of credit is incorporated into the cash price and the transaction is represented as a sale of goods by instalment (without any credit charges) (Batt 1999). Even though the amount under a tiny terms contract could be separated into a cash price component and a charge (or interest) component, the use of ‘cash price’ in the Consumer Credit Code is exclusive to s.10, which relates to goods leases. Hence, the definition of ‘cash price’ may not apply and this approach may not be able to be used to argue that a charge is payable (Batt 1999).

The PIR notes that this may be overcome by including a definition of ‘interest’ or providing a link to the Consumer Credit Code’s definition of cash price in s.6. However, this would not capture ‘exclusive products’, which are not otherwise available for cash. Hence, the PIR also recommends that the definition of ‘cash price’ be amended to include the concept of ‘reasonable value’.

While the inclusion of s.6(c) may be considered appropriate to the objectives of the Consumer Credit Code, the current wording and definitions allow for the Consumer Credit Code to be circumvented. Given that the Consumer Credit Code’s objective is to apply equally to *all forms of consumer lending*, it would appear appropriate to adopt the PIR’s recommendations.

Section 6(d) encompasses credit providers whose main business is that of providing credit, as well as those for whom the provision of credit is a secondary activity to their main business. Thus this definition would not capture a private loan between, say, two family

members. However, it was never the intention of the Consumer Credit Code to capture such transactions (Batt 1999).

The PIR highlighted that solicitor lending, whereby an investor provides funds to a solicitor, who then arranges for the funds to be lent to a consumer on behalf of the investor, was not necessarily captured by s.6(d). The reason for this being that the investor is the credit provider, but whether they were a 'credit provider' for the purposes of the Consumer Credit Code would have to be established in each case.

The PIR suggested that the Consumer Credit Code be amended so that the solicitor is the credit provider where consumer credit is organised by a solicitor. Solicitor lending would thus be captured and the consumer protection provisions of the Consumer Credit Code would then apply to those transactions.

With this exception and under the assumption that other elements of Part 1 are satisifed, the Consumer Credit Code applies to all credit providers and, hence, the definition within s.6(d) is appropriate to the objectives of the Consumer Credit Code.

9.1.3 'Mortgage' and 'guarantee'

Section 8 extends the coverage of the Consumer Credit Code to include mortgages, where the mortgage secures obligations under a credit contract or related guarantee. A mortgage is defined in Schedule 1:

> *"mortgage" includes:-*
>
> *(a) any interest in, or power over, property securing obligations of a debtor or guarantor; or*
>
> *(b) a credit provider's title to land or goods subject to sale by instalments; or*
>
> *(c) a mortgage taken to have been entered into under section 10(3);*
>
> *but does not include a consumer lease to which Part 10 applies.*

The Regulation specifically excludes any mortgages relating to perishable goods, livestock, primary produce and foodstuffs.

Similarly, s.9 extends the coverage of the Consumer Credit Code to include guarantees, where it guarantees obligations under a credit contract. The legislation defines 'guarantee' only to the extent that a guarantee 'includes an indemnity (other than one arising under a contract of insurance)'. McGill and Willmott (1999) note that 'in the context of the Code, the guarantee will be of a debtor's obligations under the credit contract, which consists principally of the payment of money owing to the credit provider'.

Similarly, an 'indemnity is a promise by the promisor to keep the promisee harmless against loss as a result of entering into a transaction with a third party' (McGill & Willmott 1999). In the context of the Consumer Credit Code, an indemnity is a promise by the guarantor to keep the credit provider harmless against loss as a result of entering into a credit contract with the debtor.

Given that mortgages and guarantees are an integral component of some forms of consumer lending, particularly housing loans, it would appear appropriate that those mortgages and guarantees are also governed by the Consumer Credit Code.

9.1.4 'Goods lease'

Section 10 of the Consumer Credit Code sets out the conditions under which a goods lease is to be regarded as a 'sale of the goods by instalment', and thus be covered by the Consumer Credit Code:

> *(1) For the purposes of this Code, a contract for the hire of goods under which the hirer has a right or obligation to purchase the goods, is to be regarded as a sale of the goods by instalments if the charge that is or may be made for hiring the goods, together with any other amount payable under the contract (including an amount to purchase the goods or to exercise an option to do so) exceeds the cash price of the goods.*
>
> *(2) A debt is to be regarded as having been incurred, and credit provided, in such circumstances.*
>
> *(3) Accordingly, if because of section 6(1) the contract is a credit contract, this Code (including Part 6) applies as if the contract had always been a sale of goods by instalments.*

Schedule 1 defines 'cash price' as the 'lowest price … that a cash purchaser might reasonably be expected to pay for [the goods or services] (either from the supplier or, if not available for cash from the supplier, from another supplier)'.

Where goods leases are, for all intents and purposes, a form of consumer credit, it would appear appropriate to extend the coverage of the Consumer Credit Code to goods leases, given that it is the Consumer Credit Code's intention to apply to all forms of consumer lending.

9.2 Exemptions

Section 7 of the Consumer Credit Code sets out a number of situations in which the provision of credit, which may otherwise fall within the scope of the legislation, will be excluded from the application of the Consumer Credit Code. While each of these exemptions may represent a departure from the objective of applying equally to all forms of consumer lending, they may nevertheless be appropriate.

Each of these exemptions is assessed against the objectives of the Consumer Credit Code below.

- **S.7(1) Short term credit.** This Code does not apply to the provision of credit limited by the contract to a total period not exceeding 62 days.

One type of situation envisaged by this exception is where a customer telephones their bank manager and asks for a temporary extension of credit, which is to be rolled over into a formal agreement within a given number of days, to pay for a deposit on a house.

While this is an appropriate exemption from the provisions of the Consumer Credit Code, this may not be so in the case of pay day lending.

Pay day lending, which is the ‘practice of a lender advancing to a consumer a relatively small amount of money until their next pay day in exchange for a fee’, is exempted from the Consumer Credit Code since pay day loans are generally for less than 62 days (Office of Fair Trading 2000).

In a recent report on pay day lenders, the Queensland Office of Fair Trading (2000) found that:

- Cash is lent in exchange for a fixed fee, which is usually in the range of $20 - $25 per $100 advanced;
- The effective annual percentage rates charged by pay day lenders ranges from 235% to over 1,300%;
- Pay day lending appeals most to those in need of urgent cash and those who are unable to access mainstream credit;
- A reasonable proportion of pay day borrowers would appear to be ‘vulnerable’; and
- Pay day lending lacks truth in lending and also raises concerns about over-commitment and unconscionability.

An amendment to s.7(1), which would bring pay day lending within the scope of the Consumer Credit Code, is currently being considered. This amendment would insert the following words at the end of s.7(1):

> *‘However, this Code applies to the provision of credit if, under the contract –*
>
> *(a) the total credit fees and charges exceed 5% of the amount of credit; or*
>
> *(b) the annual percentage rate exceeds 24% per annum.’*

This amendment would close a ‘loophole’ that has allowed pay day lenders to operate outside of the scope of the Consumer Credit Code despite providing what is for all intents and purposes consumer lending. Furthermore, the amendment will also address the truth in lending, over-commitment and unconscionability issues identified by the Queensland Office of Fair Trading.

Given that pay day lending is for all intents and purposes consumer lending, the current exemption is not considered appropriate. We note, however, that the proposed amendment will bring pay day lending within the scope of the Consumer Credit Code.

Hence, assuming that the proposed amendment will be incorporated into the Consumer Credit Code, the current exemption may be considered appropriate to the objectives of the Consumer Credit Code.

- **S.7(2) Credit without prior agreement**. This Code does not apply to the provision of credit without prior agreement between the credit provider and the debtor. For example, when a cheque account becomes overdrawn but there is no agreed overdraft facility or when a savings account falls into debit.

  Given that it would be difficult for the credit provider to comply with, for example, the disclosure provisions of the Consumer Credit Code in circumstances such as these, it would appear that this exemption is appropriate to the objectives of the Consumer Credit Code.

- **S.7(3) Credit for which only account charge payable.** This Code does not apply to the provision of credit under a continuing credit contract if the only charge that is or may be made for providing the credit is a periodic or other fixed charge that does not vary according to the amount of credit provided. However, this Code applies if the charge is of a nature prescribed by the regulations for the purposes of this subsection or if the charge exceeds the maximum charge (if any) so prescribed.

  Section 5 of the *Consumer Credit Regulation 1995* states that the prescribed maximum charge is $200 for the period of twelve months after the continuing credit contract is made and $125 for any subsequent period of twelve months.

  Duggan and Lanyon (1999) note that the main purpose of this provision is to take charge card schemes, such as American Express and Diner's Club, outside of the Consumer Credit Code. For these cards, the exemption is based on the fact that the fee does not vary according to the amount of credit provided and it is below the amount specified in the regulations. Furthermore, the courts have already established that the 'liquidation damages', which are charged when the balance owing on these cards become overdue, should not be considered 'interest'. Hence, this exemption is considered appropriate to the objectives of the Consumer Credit Code.

- **S.7(4) Joint credit and debit facilities.** This Code does not apply to any part of a credit contract under which both credit and debit facilities are available to the extent that the contract or any amount payable or other matter arising out of it relates only to the debit facility.

  In other words, the provisions of the Consumer Credit Code only apply when the facility is in debit. This would appear appropriate to the objectives of the Consumer Credit Code, as it is not the intention of the Consumer Credit Code to regulate debit accounts.

- **S.7(5) Bill facilities.** The Code does not apply to the provision of credit arising out of a bill facility, that is, a facility under which the credit provider provides credit by accepting, drawing, discounting or endorsing a bill of exchange or promissory note.

However, the regulations may provide for the application of the Code to the provision of all or any credit arising out of such a facility.

No such regulation exists. As noted by McGill and Willmott (1999), a bill facility does not involve the provision of credit. Hence, this exemption, while not necessary, is nevertheless appropriate to the objectives of the Consumer Credit Code.

- **S.7(6) Insurance premiums by instalments.** This Code does not apply to the provision of credit by an insurer for the purpose of the payment to the insurer of an insurance premium by instalments, even though the instalments exceed the total of the premium that would be payable if the premium were paid in a lump sum, if on cancellation the insured would have no liability to make further payments under the contract.

  Although monthly premiums are generally higher than annual premiums, this difference does not represent a charge for the provision of credit, but incremental administration costs reflecting 12 payment processes. Furthermore, the consumer obtaining insurance under this arrangement must be able to 'walk away' from the arrangement without incurring any further liabilities for this exemption to apply.

  Hence, this exemption is appropriate to the objectives of the Consumer Credit Code, as the payment of insurance premiums by instalments is not a form of consumer lending.

- **S.7(7) Pawnbrokers.** This Code does not apply to the provision of credit by a pawnbroker in the ordinary course of a pawnbroker's business (being a business which is being lawfully conducted by the pawnbroker). However, sections 70 to 72 (Court may reopen unjust transactions) apply to any such provision of credit.

  The PIR notes that the basic process of pawnbroking varies significantly from the general provision of credit and that 'considerable technical difficulty' would arise in trying to bring pawnbroking within the ambit of the Consumer Credit Code. Furthermore, State and Territory legislation governs the activities of pawnbrokers.

  Hence, the PIR recommendation to retain the status quo in relation to pawnbrokers is supported and the exemption is considered appropriate to the objectives of the Consumer Credit Code.

- **S.7(8) Trustees of estates.** This Code does not apply to the provision of credit by the trustee of the estate of a deceased person by way of an advance to a beneficiary of prospective beneficiary of the estate. However, section 70 to 72 (Court may reopen unjust transactions) apply to any such provision of credit.

  This exclusion relates to a long-standing practice whereby a beneficiary may be entitled to receive a large sum of money in 12 months time, but is currently in need of money. In such circumstances, trustees will make an advance to the prospective beneficiary out of the funds of the estate in anticipation of the legacy that the prospective beneficiary will receive. It is also usual practice to charge interest on this sum so that other beneficiaries

under the estate do not suffer a financial loss due to the funds being lent at no interest rather than being invested (Bingham & Niven 1998).

Unlike consumer credit generally, there is no obligation to repay the principal. Furthermore, the monies may be considered as an advance.

Hence, this exemption is considered appropriate to the objectives of the Consumer Credit Code.

- **S.7(9) Employee loans.** This Code other than this Part, Part 4 Div 3, Pat 5, Div 4 and 5, Part 7, Part 11 and Schedules 1 and 2) does not apply to the provision of credit by an employer, or a related body corporate within the meaning of the Corporations Law of an employer, to an employee or former employee (whether or not it is provided to the employee or former employee with another person). However, for a credit provider that provides credit in the course of a business providing credit to which this Code applies to employees or former employees and to others, this subsection only applies to the provision of credit on terms that are more favourable to the debtor than the terms on which the credit provider provides credit to which this Code applies to persons who are not employees or former employees of the credit provider or a related body corporate.

  The purpose of the exemption relating to employee loans is to encourage businesses to make loans to employees at a cost which is lower than market rates while retaining essential protection for those employees in the event of hardship or other difficulties. Thus this exemption benefits both employees (through lower cost loans) and employers (through reduced compliance costs), while maintaining the key consumer protection provisions.

  This exemption is considered appropriate to the objectives of the Consumer Credit Code.

- **S.7(10) Regulations may exclude credit.** The regulations may exclude, from the application of all or any provisions of this Code, the provisions of credit of a class specified in the regulations. In particular (but without limiting the generality of the foregoing), the regulations may so exclude the provision of credit if the amount the credit exceeds or may exceed a specified amount or if the credit is provided by a credit provider of a specified class.

  A number of classes of credit have been exempted from the provisions of the Consumer Credit Code in this manner. These are discussed in the following section.

9.3 Credit classes exempted by the regulations

The classes of credit exempted by the regulations are set out in sections 6 to 6E of the *Consumer Credit Regulation 1995*:

- **S.6 Additional exempt credit.** The Code (except Part 4, Div 3 and Part 5) does not apply to the provision of credit under a contract (other than a continuing credit contract)

if the amount of credit does not at any time exceed $200, there is no insurance financed under the contract, there is no mortgage or guarantee taken by the credit provider and the annual percentage rate for the contract rate does not exceed the maximum annual percentage rate (if any) for the contract if it were a contract to which the Code applies.

If the above conditions hold, then there is little risk on the behalf of either the debtor or the credit provider. Furthermore, the compliance costs associated with providing such a loan would surely outweigh the benefit to either the credit provider or the debtor. Hence, it appears that this exemption is appropriate to the objectives of the Consumer Credit Code.

- **S.6A GIO Finance Ltd's No Interest Loan Scheme.** The Code does not apply to the provision of credit under the No Interest Loan Scheme, which is operated by GIO Finance Ltd in accordance with the deed of agreement executed by the NSW Minister for Further Education, Training and Employment and GIO Finance Ltd.

  This No Interest Loan Scheme provides interest-free loans to people with disabilities in the workplace to assist them to purchase aids and appliances for their daily living needs.

  The MCCA granted this exemption on the basis that the provision of this credit was unintentionally caught by the Consumer Credit Code:

  - The debtor pays only the principal and would not ordinarily receive the protection of the Consumer Credit Code; and

  - The State Government, which pays the interest component of the loan, is not a person or a strata corporation and should not receive the protection of the Code.

  Given that the debtor does not incur a charge for the provision of credit, this provision of credit is not within the general meaning of consumer credit and there is limited need for the consumer protection provisions of the Consumer Credit Code. Furthermore, it is usual practice for governments to bear the risk rather than insure themselves. Hence, this objective is appropriate to the objectives of the Consumer Credit Code.

- **S.6B Queensland Government's Rental Purchase Plan.** The Code, other than section 70 to 74, does not apply to the provision of credit under the Queensland Government Rental Purchase Plan Scheme. This plan involves the acquisition by a consumer of a part-interest in a residence. Progressively, further shares can be purchased over time, at liberty, eventually leading to full ownership by the consumer. The consumer rents the Government's share of the property.

  The shares are acquired by an instalment purchase with interest and this is the component that is subject to the regulation by the Consumer Credit Code.

  The MCCA granted this exemption on the basis that:

  - The product had not been available to new customers since mid-1996;

- The product was unique to Queensland and did not contravene competitive neutrality principles; and
- Compliance burden, although this was a secondary factor.

The reasons provided by the MCCA are sound and we agree that the regulatory burden would be too great given that the product will be phased out. Hence, this objective is appropriate to the objectives of the Consumer Credit Code.

- **S.6C Partnership Loans.** This exemption extends the exemption provided for employee loans under s.7(9) of the Consumer Credit Code to professional partnerships.

  The MCCA granted this exemption on the basis that businesses structured as professional partnerships are warranted the same protection and opportunities as those captured by s.7(9) of the Consumer Credit Code.

  Hence, this exemption is considered appropriate to the objectives of the Consumer Credit Code for the same reasons as provided in relation to s.7(9) exemptions noted above.

- **S.6D Student loans.** The Code (other than s.56(1) and ss.70-74) does not apply to the provisions of credit by a higher educational institution, or by an association of students of the institution, to a student of the institution on the grounds of hardship or of an emergency. This is conditional on minimum precontractual disclosure.

  The MCCA granted this exemption on the basis that:

  - There was broad agreement that the nature of the loans was in the public interest. The small size of the loans, the generous terms offered and the importance of the provision of welfare programs to higher education students was considered;
  - Such loans would unlikely to be available in the general credit market;
  - The withholding of the schemes by some institutions (unable to meet the Consumer Credit Code's compliance costs and / or fear of penalties) impacted on the consumers' access to assistance; and
  - A partial exemption could ensure the schemes' viability whilst ensuring a minimum level of consumer protection and disclosure of information.

  For the reasons provided by the MCCA above and because these schemes are generally not-for-profit (thereby eliminating the commercial objectives that generally lead to harsh, unjust or unconscionable conduct by unscrupulous credit providers), this exemption is considered appropriate.

- **S.6E Loans for conservation of heritage items.** The Code does not apply to the provision of credit under the Heritage Acts of NSW, SA and Victoria, where the loan is to be used for the purpose of conservation of heritage items.

The MCCA granted this exemption on the basis that:

- The various Heritage organisations are non-profit;
- There is no question of the Heritage organisations acquiring an unfair advantage in the marketplace;
- The loans provided are not for business, but rather solely for the preservation of landmarks of significant historical value; and
- Compliance burden, although this was a secondary factor.

For the reasons provided by the MCCA above and because these schemes are generally not-for-profit (thereby eliminating the commercial objectives that generally lead to harsh, unjust or unconscionable conduct by unscrupulous credit providers), this exemption is considered appropriate.

In summary, in each of the classes of exemptions granted by the MCCA, sound reasons were provided for the granting of the exemption. Furthermore, key consumer protection provisions were retained as appropriate.

9.4 Corporate Law Economic Reform Program (CLERP)

In April 1999, the Minister for Financial Services and Regulation released a consultation paper on implementing CLERP 6. This paper proposes a regulatory framework for the 'licensing of financial product markets and service providers, conduct and disclosure of service providers and financial product disclosure'. This paper stated that credit contracts to which the Uniform Consumer Credit Code applies would be specifically excluded as there is already a regulatory regime applying to these arrangements. Hence, all credit contracts that fall outside of the scope of the Consumer Credit Code would fall within the scope of the new regulatory framework.

However, the Commonwealth Government, after hearing submissions from industry, determined that CLERP 6 would not be covering credit products at all.

9.5 Summary

Overall, the definitions and exemptions are appropriate to the objectives of the Consumer Credit Code. There are, however, a number of instances where credit, which is for all intents and purposes consumer credit, is outside the scope of the Consumer Credit Code. These include:

- Pay day lending;
- Terms sale of land;

- Conditional sale agreement;
- Tiny terms contracts; and
- Solicitor lending.

While CLERP 6, as initially promulgated would capture credit contracts not within the scope of the Consumer Credit Code, the Commonwealth Government, after hearing submissions from industry, determined that CLERP 6 would not be covering credit products at all.

Given that transactions that are for all intents and purposes a form of consumer lending should be within the ambit of the Consumer Credit Code, it is recommended that consideration be given to bringing the above transactions within the scope of the Consumer Credit Code.

10 Identification and classification of restrictions

This chapter of the report outlines the processes used to identify the anti-competitive provisions within the Consumer Credit Code and classify the identified restrictions as major or minor restrictions in accordance with the WA *Legislation Review Guidelines*.

10.1 Identification of restrictions on competition

Both the Victorian and Western Australian guidelines for NCP reviews pose a range of tests to help assess whether a legislative provision is a restriction on competition. These tests include:

- Does it create entry criteria affecting the ease with which new firms may enter and secure a viable market?
- Does it result in increased costs of production or compliance costs for those wishing to participate in the industry?
- Does it limit the number of firms which may participate in the industry, the locations in which they may operate, or affect the degree of market concentration?
- Has it given firms extra functions or reduced independence across the production chain?
- Does it constrain firms in terms of the business decisions they are free to make?
- Are incumbent firms provided with market information or research which may not be available to new entrants?
- Does it discriminate between firms or between consumers?
- Do existing arrangements limit the ability of firms to innovate, to introduce new technology, to differentiate between products or to advertise their products?

An analysis of the provisions of the Consumer Credit Code against these tests has revealed a number of provisions that potentially restrict competition, as summarised in Section 8.3.

10.2 Classification of restrictions on competition

In recognition that all restrictions are not of equal importance, the Western Australian *Legislation Review Guidelines* require the identified restrictions to be classified as follows:

- A major restriction, needing a detailed analysis and public benefit test; or
- A minor restriction, needing simple analysis and public benefit test which involves less effort weighing benefits and costs or advantages and disadvantages.

In classifying restrictions as minor or major, each restriction was assessed against the two criteria outlined in the Western Australian *Legislation Review Guidelines*. These two criteria are:

- *Is having versus not having this restriction likely to make a significant difference to the economy?* That is, will the restriction on the economic / financial objective potentially be more than, say, a million dollars per year (positive or negative)?

- *Is a detailed analysis of costs and benefits likely to be needed to decide whether and / or demonstrate whether the restriction is in the public interest?* That is, is a detailed analysis required in order to ascertain the net cost or benefit of the restriction, or is the net cost or benefit obvious, and demonstrably so?

If the restriction is likely to be 'significant' in economic / financial terms and a detailed analysis is required to ascertain the net cost or benefit of the restriction, then the restriction is considered a major restriction. That is, if the answer is 'yes' to each of the above questions, then it is a major restriction for analysis purposes. In all other cases, the restriction is considered a minor restriction for analysis.

10.3 Summary of restrictions

The following table provides a summary of the restrictions on competition within the Consumer Credit Code.

Summary of Restrictions on Competition			
Restriction	**Code Sections**	**Nature of restriction**	**Type**
1	14, 15, 18, 31-34	Part 2 disclosure requirements	**Major**
2	23(1), 29	Part 2 product innovation restrictions	Minor
3	39, 51, 52, 56(1)	Part 3 disclosure requirements	**Major**
4	46	Part 3 product innovation restrictions	Minor
5	59-63, 65, 67	Part 4 disclosure requirements	Minor
6	70, 72	Part 4 potential compliance costs	Minor
7	76, 78, 80, 83, 91, 94, 96	Part 5 potential compliance costs	Minor
8	102-106	Part 6 potential compliance costs	**Major**
9	118, 119	Part 7 discrimination between credit providers	Minor
10	130	Part 7 third line forcing restrictions	Minor
11	133	Part 8 third line forcing restrictions	Minor
12	135	Part 8 pricing restrictions	Minor
13	140, 143, 146	Part 9 conduct restrictions	Minor
14	152, 153, 155, 156	Part 10 disclosure requirements	**Major**
15	155	Part 10 potential compliance costs	Minor

Each restriction is discussed in turn, beginning with Restriction 1 in Chapter 12.

11 Description of regulatory reform options

Prior to examining each of the restrictions in detail, it is important to establish the proposed reform options so that a meaningful analysis of the restrictions may be conducted.

The reform options[13] considered and assessed in this review were:

Option 1 Status Quo

Option 2 Amended Status Quo

Option 3 Industry Deregulation

Option 4 Mandatory Code of Conduct

Details of each of these reform options are presented below.

11.1 Option 1 – Status quo

This option assumes the status quo is retained and there are no changes to the existing provisions of the Consumer Credit Code. For the purposes of analysis, the costs and benefits of retaining the Consumer Credit Code as a whole are considered in the context of the costs and benefits of retaining the provisions relating to the particular restriction.

11.2 Option 2 – Amended status quo

Even if a particular provision is found to be in the public interest and thus worth retaining, it may nevertheless be appropriate to consider amending the provision.

This option may be appropriate where the desired objectives and fair trading outcomes of the particular provision can be achieved through less restrictive means, but where reliance on market forces or alternative legislation is not appropriate or feasible. Details of any such amendments are considered in relation to specific provisions, where appropriate.

11.3 Option 3 – Industry deregulation

The Issues Paper noted that it could be argued that there is no particular reason for retaining the Consumer Credit Code, given that:

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[13] Although similar, these are not the reform options put forward in the Issues Paper. However, it was considered appropriate to amend the options for consideration in recognition of issues and matters arising out of the conduct of the review.

- Economic theory states that the demand and supply of goods and services, which is primarily driven by consumer preferences, will equalise over the medium to longer term; and

- Some of its provisions are duplicated in other legislation, such as the Trade Practices Act, Insurance Contracts Act and State Fair Trading Acts.

Furthermore, the question was raised as to whether the Consumer Credit Code should be repealed and reliance placed on market forces and provisions within other legislation. However, it was made clear by the written submissions[14] and the targeted consultations that deregulation was not considered appropriate or credible by either consumer protection agencies or credit providers.

Furthermore, the research and analysis conducted as part of this review has indicated that repealing the Consumer Credit Code in its entirety could have serious negative implications for consumers. There are numerous provisions within the Consumer Credit Code that act to protect consumers without placing onerous burdens on credit providers or imposing anti-competitive restrictions.[15]

For the above reasons, it has been determined that this option does not provide a feasible alternative to the Consumer Credit Code and, hence, will not be given any further consideration in this review.

11.4 Option 4 – Mandatory Code of Conduct

If it is found that some form of intervention is required to ensure the efficient functioning of the consumer credit market, it may be that industry co-regulation through a mandatory Code of Conduct may be considered to be more appropriate than the existing legislative framework.

Other existing legislation (such as Part IVB of the *Trade Practices Act 1974*) provides the regulatory power to prescribe mandatory Codes of Conduct in industries where problems exist. Mandatory codes prescribed under these legislative frameworks outline minimum standards of legal behaviour in respect to industry-specific or sector specific problems.

For the purpose of this review, the following assumptions have been made regarding reform Option 4:

- The existing Consumer Credit Code legislation would be repealed in all jurisdictions;

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[14] See Australian Finance Conference, Commonwealth Consumer Affairs Advisory Council and Consumer Credit Legal Service submissions in particular. The Australian Bankers' Association, Ms Denise McGill and Mr Randall Dennings made no comments in relation to the merits or otherwise of this option.

[15] See, for example, ss. 19, 24, 27, 53, 75, 99, 139, 144, 145, 162, 167, which are summarised in Appendix A.

- The existing Consumer Credit Code (with a few modifications) would be declared a mandatory Code of Conduct under s.51AE of the *Trade Practices Act 1974*, and a new regulation would be developed to give effect to the Code of Conduct;

- The mandatory Code of Conduct would be binding on all the participants in the consumer credit industry;

- The Code of Conduct would mirror the provisions of the Consumer Credit Code, with the exception of the civil penalties regime (Part 6), which would be replaced with a dispute resolution process (ie mediation); and

- Although the Australian Competition and Consumer Commission (ACCC) is the administrator of the *Trade Practices Act 1974*, the administration of the Code of Conduct would fall to AFIC in this instance.

The current civil penalties regime would be replaced by a dispute resolution process, in accordance with the importance the ACCC places on effective alternative dispute resolution mechanisms. Alternative dispute resolution mechanisms are often a quicker and less costly form of settling disputes (Lieberman 1998).

If the dispute resolution process does not resolve a particular issue, the parties to the credit contract would then be able to seek remedy under Part 6 (Enforcement and remedies) of the *Trade Practices Act 1974*, including injunctive relief (s.80) and damages (s.82).

This reform option should not impose any additional costs to credit providers and, as the disclosure requirements are effectively the same, there should be no difference in start-up costs for new entrants to the industry. However, there may be some benefits (in terms of cost savings) to credit providers where disputes are resolved through a dispute resolution process (ie mediation) rather than through the court system.

Although the provisions of the Code of Conduct would largely mirror those of the Consumer Credit Code, it is unlikely that the Code of Conduct would deliver the same level of consumer protection due to the replacement of the civil penalties regime by an alternative dispute resolution mechanism. The reasons for this include:

- The removal of the civil penalties regime would remove the incentive for credit providers to comply with the Code of Conduct, which could result in more breaches;

- Unlike the Consumer Credit Code, mandatory Codes of Conduct generally do not require credit providers to take action if a breach is discovered. The onus would then be placed on consumers to take action in these circumstances; and

- Alternative dispute resolution mechanisms are generally confined to disputes where a consumer can claim a loss. In contrast, the Consumer Credit Code provides redress for some breaches irrespective of whether the consumer has suffered a loss.

Hence, the mandatory Code of Conduct would be unlikely to offer the same level of protection as the Consumer Credit Code. Relative to the Consumer Credit Code then, benefits to consumers would then decrease, while costs to consumers would increase, under this reform option. Furthermore, consumers would need to be educated / informed of the new Code of Conduct and the dispute resolution process. There may be a period of uncertainty and reduced confidence after the changeover, where the length of this period may be influenced by the quality of the education program.

The Commonwealth government would incur costs associated with:

- Developing and implementing the new legislation, specifically the relevant regulation and the dispute resolution process under the Code of Conduct;

- Educating the industry and consumers about the Code of Conduct and the dispute resolution process; and

- Administration of the Code of Conduct and the dispute resolution process.

The State and Territory governments would incur costs associated with repealing the existing Consumer Credit Code legislation, but there may be costs savings as they would no longer be responsible for administering the legislation.

In summary, there would no material (negative or positive) impacts on credit providers relative to the existing Consumer Credit Code. However, consumers would face additional costs due to a reduction in the level of consumer protection. Furthermore, it is anticipated that there would be significant administrative costs incurred by the Commonwealth, State and Territory governments in the changeover to a mandatory Code of Conduct in net terms. Hence, the overall impact of this option is likely to be a negative income impact, which would fall mostly on consumers and the Commonwealth government.

This option does not meet all the objectives of the Consumer Credit Code, specifically that of providing a significant redress mechanism for borrowers. Furthermore, it is no less restrictive on competition nor does it offer any net public benefits. Based on this assessment, it has been determined that this option does not provide a feasible alternative to the Consumer Credit Code and, hence, will not be given any further consideration in this review.

This conclusion is consistent with the views presented in the written submissions[16], particularly that of the:

- Australian Finance Conference, who doubted that there existed credible ground to support this option;

[16] Australian Bankers' Association, Ms Denise McGill and Mr Randall Dennings did not comment on the merits or otherwise of this option.

- Commonwealth Consumer Affairs Advisory Council, who believed that there would be little point in moving from the legislated Consumer Credit Code to a mandatory code; and

- Consumer Credit Legal Service, who oppose regulation by a mandatory code on the basis that they are often too general and ambiguous.

12 Restriction 1: Part 2 disclosure requirements

12.1 Introduction

Part 2 of the Consumer Credit Code has been identified as potentially impacting on competition through disclosure requirements, which increase compliance costs and may act as a prohibitive barrier to entry for small lenders. Specific anti-competitive provisions are:

- Section 14, which requires disclosure of important terms and conditions of the proposed credit contract prior to entering into a credit contract;
- Section 15, which requires the contract documentation to contain detailed information on the credit to be provided;
- Section 18, which requires a copy of the contract documentation be provided to the debtor; and
- Sections 31 to 34, which require credit providers to generally provide periodic statements of credit accounts showing, amongst other things, how much the borrower has repaid, the amount of interest charged and the outstanding balance.

12.2 Nature of Restriction 1

The disclosure provisions in the Consumer Credit Code are prescriptive and have in some cases led to lengthy and complex[17] credit contracts that are costly for credit providers to prepare and produce. Therefore, the disclosure provisions increase the compliance costs imposed on credit providers.

A concern with respect to the cost of compliance is that some provisions of the Consumer Credit Code may actually impact on the efficient operation of the credit market itself. That is, while all credit providers are subject to the Consumer Credit Code, it has been suggested that the associated compliance costs potentially act as a prohibitive barrier to entry for small lenders.

While these sections of the Consumer Credit Code have been identified as impacting on competition within the context of increasing compliance costs, they are also the mechanism by which the truth in lending objective and the information asymmetry issues are addressed.

As noted in the Second Reading speech of the *Consumer Credit (Queensland) Bill*, by ensuring truthful disclosure of all relevant information about credit arrangements, 'a consumer can make an informed choice between credit providers as to the nature of the credit being offered, as well as the comparative costs between credit providers'.

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[17] It was also suggested that the complex nature of some credit products contributes to the complexity of some credit contracts.

The aim of the statement of account is to reinforce the debtor's understanding of the key elements of the credit arrangements and to provide an opportunity for consumers to periodically review their credit arrangements. Duggan & Lanyon (1999) note that the purpose of periodic statements of account vary with the type of credit product:

- In the case of variable interest rate credit contracts, the main purpose is to inform the debtor of interest rate changes and allow the debtor to see how interest rate changes affect the interest payable; and
- In the case of continuing credit contracts, the purpose is three-fold:
  - To give the debtor a record of account transactions during the statement period;
  - To inform the debtor of the outstanding balance of the account and the minimum payment due; and
  - To allow the debtor to see how the terms of the contract work in practice.

In addition to addressing the objective of truth in lending, the disclosure requirements also contribute to fair trading outcomes, specifically that of access to appropriate information to enable informed decisions to be made by participants.

12.3 Key issues raised in submissions and consultation

Australian Bankers' Association (ABA):

The emergence of 'infomediaries', who assist consumers to identify and evaluate the suitability of financial products, has been a significant factor in reducing information asymmetries in the consumer credit market. 'Infomediaries' include organisations such as the Australian Consumer Association, which often provides commentary on issues related to the purchase of consumer credit, particularly through its *Choice* magazine. Other 'infomediaries' in the Australian consumer credit market are *eLoan*, *Quicken*, *Cannex*, *Your Mortgage* and *LoanNet*.

The ABA notes that there is little evidence that the current disclosure requirements address information asymmetries, and indeed create a number of competitive distortions as the information presented under current disclosure requirements are complex, excessive and often confusing.

The ABA therefore agrees with Recommendation 1.1 (simplified Schumer Box) of the PIR, but notes that, if there is to be mandatory disclosure, then this should be directed towards key information that consumers are likely to use.

The ABA does not agree with disclosure of a comparison rate (Recommendation 1.4), noting that this would shift the focus to price rather than allowing competition to be based on a bundle of price and other features. Furthermore, the disclosure of a comparison rate may mislead consumers as the comparison rate published in the advertisement is likely to be

different from the rate noted in the pre-contractual disclosure because the comparison rate is specific to each credit contract.

Australian Finance Conference (AFC):

The AFC considers that disclosure requirements are important; however, the amount of information required, its relevance at the time and the way it is regulated are of concern.

The AFC provides the example of purchasing a car to support its argument that the amount of information is too great in the context of all the material a consumer receives, resulting in the information not being sufficiently assimilated at the pre-contractual stage. In this example, there may be a number of documents involved, including car purchase order and contract, credit contract documentation, insurance documentation and vehicle registration documentation.

The AFC notes that Recommendation 1.1 and Recommendation 1.2 (clarification of which fees and charges are to be disclosed) of the PIR generally reflects their concerns. However, the AFC strongly opposes Recommendation 1.4 because it cannot be made to work without market distortion, inequities and without misleading consumers.

The AFC asserts that what is missing from the disclosure requirements is the education of consumers on how to use the information, and that the development of such an education program is the responsibility of the government, with input from industry.

Consumer Credit Legal Service (CCLS):

The CCLS argues that the truth in lending objectives have not been fulfilled, as disclosure currently occurs in a way which allows credit providers to avoid proper truth and lending requirements.

Mr Randall Dennings:

Mr Dennings asserts that further research needs to be undertaken to ascertain what information the consumer actually finds useful and also to determine the best method of delivering that information to the consumer. Only then will it be possible to accurately assess the public benefit that the existing provisions provide.

Mr Dennings believes that there will be practical difficulties created by Recommendation 1.4 and questions whether this recommendation would deliver any public benefit.

12.4 Classification of Restriction 1

Restriction 1 has been classified as a major restriction on the basis that having versus not having this restriction is likely to make a significant difference to the economy and a detailed analysis of the costs and benefits is needed to demonstrate that this restriction is in the public interest.

12.5 Reform options for Restriction 1

The reform options considered most appropriate for Restriction 1 are Option 1 (Status quo) and Option 2 (Amended status quo). These are discussed in turn in the following sections.

Option 3 (Industry deregulation) and Option 4 (Mandatory code of conduct) have been discarded for the reasons previously outlined in Chapter 11.

12.5.1 Option 1 – Status quo / cost-benefit analysis

The requirements of Restriction 1 add to the administration costs of credit providers and thus to the price paid for credit by consumers. However, the disclosure requirements benefit consumers by assisting them to make informed credit decisions. These provisions address the information asymmetries in the market and the objective of truth in lending.

Furthermore, Malbon (1999) notes that more informed choices by consumers leads to greater efficiency in the consumer credit market. The easier it is for consumers to compare products, the more they shop around. This in turn leads to more transactions, which increases competition amongst credit providers and thus lowers prices.

In the absence of mandatory information disclosure provisions in the Consumer Credit Code, the provision of information to consumers would be governed by:

- Codes of Practice, which currently exist for the banking sector, building society sector and credit union sector. While the Codes of Practice have provisions covering disclosure of information, these codes do not cover all credit providers, do not have the force of law, nor do all the provisions have to be abided by, even if the credit provider has 'adopted' the code. In particular, credit providers who 'adopt' their particular code of practice are not bound by the provisions relating to disclosure of terms and conditions, pre-contractual disclosure or guarantees.

- Contract law, which requires that the terms of a contract must be certain (and not vague) for an agreement to amount to an enforceable contract. In this respect, considerable disclosure is required (irrespective of the Consumer Credit Code) to establish a legally binding contract.

  This is evident in the current level of disclosure in a commercial contract, which is not covered by the Consumer Credit Code. A comparison of a consumer credit contract and a commercial contract (both from the same credit provider) has indicated that there may be very little difference. Furthermore, all requirements as set out in s.15 of the Consumer Credit Code were covered in the commercial credit contract.

- Alternative information sources, such as infomediaries, printed media and the Internet. As noted by the ABA in their written submission, infomediaries assist consumers to identify and evaluate the suitability of financial products, and have been a significant factor in reducing information asymmetry in the consumer credit market.

However, access to these alternative information sources is not equal between all consumers. In particular, a consumer with access to the Internet can more readily access a wider range of information than a consumer who does not (and must then call or visit credit providers to obtain this information.

Thus, the benefits to consumers from having mandatory information disclosure provisions within the Consumer Credit Code are:

- Reduced information search costs;
- Awareness of the implications and financial obligations prior to entering into a credit contract, which potentially protects a consumer from entering into an inappropriate or unsuitable credit contract; and
- The periodic statement reinforces the debtor's understanding of the credit arrangements and provides them with an opportunity to periodically review their credit arrangements

However, the potential benefits to consumers may not be fully realised. Submissions made to the PIR noted that:

- Information provided as a result of the pre-contractual disclosure requirements was given too late in the process and was too complex to be useful in comparing lenders and products;
- The process of accessing information from different credit providers was costly and arduous;
- The information provided did not assist at all in making comparisons or influence the selection process; and
- The amount of information provided is too great to read at a pre-contractual stage if the information is only obtained after making an application to a credit provider.

Malbon (1999) noted that 'lenders were unanimous in their belief that the majority of consumers do not fully read the loan documentation before signing it, and if they do, few understand it'. In contrast, Malbon's survey of debtors indicated that a significant proportion of debtors do read the information provided to them by the credit provider (see Table 12.1 below).

Table 12.1 Use of Pre-contractual Disclosure				
Proportion of respondents who …	**Credit Contract Type**			
	Housing Loans	**Personal Loans**	**Credit Cards**	**Linked Credit**
Read the pre-contractual documentation	90%	88%	78%	77%
Read it at least				
- a week before signing	51%	15%	57%	15%
- a day before signing	28%	32%	19%	19%
- an hour before signing	5%	11%	5%	11%
- just before signing	16%	41%	19%	55%
Source: Malbon 1999				

Furthermore, in the case of housing loans and credit cards, most respondents indicated that they read this information at least a week before signing the credit contract. Hence providing sufficient time to digest the information and make comparisons with other credit products / providers.

In the case of personal loans and linked credit, more than half of those who read the contract documentation did so an hour or less before signing the credit contract. This is unlikely to be sufficient to fully understand all the terms and conditions of the loan, or to make meaningful comparisons with other credit products.

Of those who read the pre-contractual documentation, approximately two-thirds indicated that they found it 'mostly helpful' (see Table 12.2 below).

Table 12.2 Helpfulness of Pre-contractual Disclosure				
Proportion of respondents who believed the…	**Credit Contract Type**			
	Housing Loans	**Personal Loans**	**Credit Cards**	**Linked Credit**
Information was mostly useful	66%	62%	67%	68%
Information was helpful because it:				
- made clear what the loan involved.	55%	51%	46%	49%
- made the information easy to understand.	21%	17%	17%	16%
- explained the repayments.	17%	24%	19%	24%
- explained the fees and charges.	13%	8%	19%	10%
- explained the interest rates.	10%	12%	27%	18%
Documentation was:				
- too long and difficult.	22%	14%	15%	13%
- difficult to understand.	19%	16%	14%	13%
- difficult to make sense of.	11%	9%	9%	9%
Source: Malbon 1999				

Of those respondents who indicated it was helpful, approximately half said it was helpful because it made clear what the loan involved. However, a significant proportion also indicated that it was too long and detailed, difficult to understand or difficult to make sense of.

Malbon (1999) also found that the pre-contractual disclosure documents influenced a small, though not insignificant, proportion of debtors (see Table 10.3 below).

Table 12.3 Influence of Pre-contractual Disclosure

Proportion of respondents who believed the…	**Credit Contract Type**			
	Housing Loans	**Personal Loans**	**Credit Cards**	**Linked Credit**
Information influenced their decision.	11%	9%	14%	13%
Information was influential because it made the debtor:				
- more confident about the transaction	78%	72%	31%	80%
- hesitate about entering the transaction.	4%	4%	37%	5%
- enter into further discussions with the credit provider.	17%	17%	11%	25%
- consider other credit providers.	10%	3%	--	--

Source: Malbon 1999

Generally, the information provided made the debtor more confident about entering into the credit contract. Except in the case of credit cards, the information provided caused only a small proportion to hesitate about entering into a credit contract. In the case of credit cards, 37% of those who indicated that the pre-contractual disclosure affected their decision, said that it made them hesitate.

Therefore, it would appear that consumers do value the information disclosure aspects of the Consumer Credit Code as the research presented above indicates the majority of consumers read the information provided and find it helpful. While the Malbon research provides no quantitative values, it is considered that the consumer benefit associated with information disclosure would be substantial from a market efficiency viewpoint.

Most of the costs stemming from these provisions are borne by credit providers, but may be passed on to consumers through higher prices (through, for example, application fees). These costs are:

- Preparation, printing, copying and delivery of contract documentation, which is generally a once-off cost for each of the pre-contractual disclosure and the credit contract documentation; and

- Preparation, printing and delivery of the periodic statements of account, which are ongoing costs for the term of the credit contract.

In relation to periodic statements of account, it would be in the credit provider's own interest to provide these statements (as they do for credit contracts not governed by the Consumer Credit Code) even in they were not required by the Consumer Credit Code, as the alternative is to provide extra resources to address inquiries from consumers for information relating to their credit accounts.

It was suggested during the consultations that the compliance costs associated with this restriction are significant enough to have the potential to act as a barrier to entry for small credit providers.

The Wallis Inquiry noted that the one-off implementation cost as a result of the Consumer Credit Code was $16 million at one of the big four banks. Furthermore, additional operating costs were close to $3 million per annum. This is consistent with the Australian Bankers' Association's (ABA) estimates of the compliance costs of the Consumer Credit Code. The ABA estimated that the banks spent a combined $100 million to ensure systems compliance and a further $50 million per annum in ongoing costs (Boreham 1998).[18]

The costs noted above reflect total cost of the Consumer Credit Code and, as such, costs associated with disclosure requirements would be a subset of these costs. However, from an economic efficiency viewpoint, the costs associated with establishing the Consumer Credit Code should be considered as a 'sunk cost', and therefore excluded for consideration within an NCP context.

While we appreciate that, as a major restriction, a quantitative analysis should be conducted for this restriction, stakeholders did not provide any quantitative information regarding costs in the submissions or during the consultation phase. A survey was forwarded to credit providers in an attempt to gather quantitative information; however, the responses received were insufficient to conduct a meaningful quantitative analysis.

In the absence of these disclosure provisions from the Consumer Credit Code, it is likely that consumer confidence would fall if consumers felt they had lost the protection of the Consumer Credit Code (despite the possible continued use of comprehensive contracts). This would reduce the number of consumer credit transactions and, as noted previously, this has flow-on implications for the wider economy as the multiplier effects of those purchases that would have been made are foregone.

Thus, while credit providers do incur most of the costs associated with this restriction, they also derive a number of benefits from the existence of these provisions within the Consumer Credit Code:

- The promotion of consumer confidence potentially generates consumer credit transactions that otherwise would not have occurred;
- Increasing efficiency with regard to business administration; and
- The promotion of flexibility in product development, which allows for competition based on product differentiation.

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[18] While these costs appear significant industry experts have suggested that they represent a lower level of cost than those incurred under the former Credit Acts.

Governments also face costs in relation to these provisions, namely those associated with administration of the legislation and coordination of national uniformity[19]. However, there is a corresponding benefit to governments through reduced requests to government consumer agencies for information relating to consumer credit products.

Under the Consumer Credit Code, civil penalties imposed by the courts in relation to breaches of key requirements (such as information disclosure) as a result of an application by the credit provider or a Government Consumer Agency are required to be paid into a fund established for such purposes or to the Government Consumer Agency (s.106). This provides a further benefit to government as it is essentially a source of funds for service provision.[20]

In summary, while the provisions of Part 2 do add to the compliance costs for credit providers, these costs are ultimately recoverable from the debtor. Furthermore, these annual compliance costs represent only a fraction of the total consumer debt outstanding.

Hence, it may be concluded that this restriction provides a net benefit to consumers and thus should be retained within the Consumer Credit Code. Furthermore, it addresses the objective of truth in lending and the fair trading outcome of providing access to appropriate information to enable informed decisions to be made by participants.

12.5.2 Option 2 – Amended status quo

Based on the PIR of the Consumer Credit Code, the major concern of industry participants with respect to the current legislation appears to relate to the regulatory requirements of compulsory disclosure. This is particularly the case with those sections of the legislation relating to pre-loan and loan documentation, that is:

- Section 14, which sets out the form and content of pre-contractual disclosure; and
- Section 15, which sets out the content that must be disclosed in the credit contract documentation.

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[19] The following cost estimates have been provided by the States and Territories:

State / Territory	Cost ($)
Australian Capital Territory	5,000
New South Wales	800,900
Northern Territory	14,100
Queensland	220,000
South Australia	55,500
Tasmania	33,250
Victoria	190,000
Western Australia	164,000
Source: KPMG 2000	

Based on the information provided by various States and Territories, it is estimated that the total cost to government in administering the Consumer Credit Code is in the order of $1.5 million. The cost that may be attributed to each particular restriction is a small component of this total cost.

[20] The amount of penalties currently paid into such funds as a result of applications under Part 6 is not known, but believed to be relatively small. Hence, these potential benefits may be relatively minor.

The Issues Paper suggested that an option for reform is to simplify the disclosure requirements within the existing legislation, given that disclosure requirements are still considered to be required, such that only 'standard' fees and charges are required to be detailed in the credit documentation.

It was also suggested that disclosure obligations could also be strengthened through the adoption of a code of practice that stipulates principles of disclosure, similar to that of the Code of Banking Practice. However, this suggestion has been discarded on the basis of the shortcomings of codes of practice identified in the analysis of Option 1 in relation to this restriction (see Section 12.5.1).

For the purposes of this review, Option 2 assumes a level of mandatory disclosure that is less than the current level under the Consumer Credit Code. That is, disclosure will be mandated by the Consumer Credit Code and therefore subject to civil penalties, for only key information that immediately affects the operation of the loan.

Further research and/or consideration of existing research (such as the PIR or Malbon report) is required to determine what this 'key information' should be.

The reduction of the disclosure requirements under the Consumer Credit Code will potentially impose the following costs on consumers:

- Information search costs will be higher relative to the status quo. That is, the effort and/or monetary outlay required on behalf of the consumer to obtain all the information currently provided under the Consumer Credit Code will increase under this option;

- Inappropriate credit choices stemming from possible lack of information, which may have significant financial implications for some consumers; and

- A reduction in confidence, which may mean that some transactions are not entered into even if they would have been appropriate.

Credit providers may benefit in terms of reduced administration costs related to disclosure requirements, but may also incur additional costs. Specifically, consumer confidence may fall, which in turn may reduce the number of credit transactions entered into by consumers. Therefore, credit providers may incur additional public relations and marketing costs to be able to maintain the same level of business.

State and Territory governments would face one-off costs associated with amending the Consumer Credit Code legislation.

Option 2 requires the provision of 'essential' information to consumers, rather than all information as currently required. The submissions and consultations have highlighted that the amount of information provided to consumers is not the key issue with respect to disclosure, rather it is the timing and format of the information that is provided.

In this context the PIR has recommended that Regulation 13 be amended to provide a simplified 'Schumer Box' containing essential information (for summary purposes), while other essential information would be provided outside of this box, but still within the credit contract. This essential information in the Schumer Box would likely include:

- Amount of credit;
- Annual percentage rate;
- Term of loan;
- Repayment amount;
- Upfront and monthly fees;
- Comparison rate; and
- Total amount repaid.

Therefore, Option 2 is really a subset of PIR Recommendation 1.1, as essential pre-contractual information would still be required to be provided, although the provision of other information would be up to the discretion of the credit provider under Option 2. While the provision of this other information would not be mandatory under Option 2, it is considered that credit providers would still disclose much of the information currently disclosed as it would be required in the contract for the contract to be legally binding and enforceable (as discussed in relation to Option 1 in Section 12.5.1).

Given this, we consider the marginal cost of adopting the PIR Recommendation 1.1 would be negligible in comparison to adopting reform Option 2 as the difference between the administrative costs of these two reforms would be minor.

In conclusion, while there is merit in adopting Option 2, we consider that it provides only marginal incremental benefits to credit providers in terms of costs savings in comparison to the consumer benefits likely to be gained through the adoption PIR Recommendation 1.1. Therefore, we consider PIR Recommendation 1.1 would provide a better outcome over Option 2 in terms of consumer protection and, as such, we recommend amending the Consumer Credit Code consistent with PIR Recommendation 1.1.

12.6 Post Implementation Review Recommendations

As mentioned above, the PIR recommendations relevant to this restriction include 1.1, 1.2 and 1.4. The objectives of these recommendations reinforce one of the objectives of the Consumer Credit Code, which is to allow consumers to make informed choices when purchasing credit. Further, they also provide for ensuring fair trading outcomes, specifically that of access to appropriate information that enables consumers to make informed choices.

12.7 Conclusions

The analysis of the costs and benefits of the Consumer Credit Code and those of the alternative options has indicated that the level of disclosure in the absence of these particular provisions within the Consumer Credit Code may remain relatively high due to:

- The need for certain terms and comprehensive disclosure in order to have a credit contract that is legally enforceable;
- Services provided by infomediaries, which are generally free of charge; and
- Information published by credit providers.

The information provided by infomediaries and the credit providers tends to be comprehensive, particularly in relation to housing loans. However, access to this information is not equal between all consumers. A consumer with access to the Internet can more readily access a wide range of information than a consumer who does not (and must then call or visit credit providers to obtain this information).

Under the Consumer Credit Code (and the situation generally today) the rational consumer has a number of potential sources of information regarding consumer credit, including the media (eg newspapers), Internet, info-mediaries and the credit providers themselves. However, this has not always been the case in the past and, while the advent of new technology should continue to ensure the current levels of information available, there is no guarantee that it would continue to do so in the absence of the Consumer Credit Code.

The Consumer Credit Code acts as a safety net to ensure a minimum level of information disclosure, and because there are no certainties about what would happen in the absence of the legislation, it should at least be retained in its current form with respect to this restriction.

Furthermore, while it is probable that those credit providers who are at the top end of the market (banks, credit unions, building societies and most finance companies) would provide an adequate level of disclosure in the absence of the Consumer Credit Code (for the reasons outlined previously), the same cannot be assumed for other credit providers.

On balance, the costs associated with Restriction 1 are outweighed by the benefits it generates. We note that reform Option 2 appears to provide a potential alternative to the status quo; however, for reasons already discussed, the PIR Recommendation 1.1 enhances the efficacy of the pre-contractual disclosure requirements of the Consumer Credit Code more appropriately than does reform Option 2.

Therefore, we recommend that Restriction 1 remain and PIR Recommendation 1.1 be adopted to enhance the disclosure requirements nominated by Part 2 of the Consumer Credit Code.

12.8 Additional comments on Restriction 1

While there was general consensus in the written submission regarding the importance of the disclosure requirements within the Consumer Credit Code, there were also a number of issues raised about the specifics of the disclosure provisions, namely:

- There is little evidence that the current disclosure requirements address information asymmetries;
- The information presented under current disclosure requirements are complex, excessive and often confusing;
- The amount of information required and its relevance at the time – the information may not be sufficiently assimilated at the pre-contractual stage;
- If there is mandatory disclosure, it should be directed at key information that consumers are likely to use;
- Further research is required to ascertain what information the consumer actually finds useful and also to determine the best method of delivering that information to the consumer;
- Credit products are still not well understood by consumers;
- The Consumer Credit Code fails to provide consumers assistance in comparing credit products; and
- Consumers need to be educated on how to use the information.

These comments above reflect many of the concerns raised during the PIR process. In response to these earlier concerns, the PIR Project Team recommended amending Regulation 13 to provide a simplified 'Schumer Box' format containing essential financial information (PIR Recommendation 1.1). As noted in the previous sections, this response appears to be an appropriate mechanism by which to better enable consumers to understand and digest the information provided to them during the process of sourcing credit.

13 Restriction 2: Part 2 product innovation restrictions

13.1 Introduction

Part 2 of the Consumer Credit Code has also been identified as potentially impacting on competition through provisions that limit a credit provider's ability to innovate, specifically:

- Section 23(1), which requires the credit provider to provide the credit amount in cash or money's worth.[21]
- Section 29, which provides for regulations that specify prohibited fees and charges.

13.2 Nature of Restriction 2

Section 23(1) restricts product innovation by requiring that the loan amount be provided in cash or money's worth. That is, the credit provider may not supply goods or other property instead. This ensures that the consumer receives the full value of the loan amount and protects the consumer from being provided with goods that have been overvalued by the credit provider (Duggan & Lanyon 1999).

Section 29 states that the regulations may specify credit fees and charges that are prohibited for the purposes of the Consumer Credit Code. While the regulations currently do not specify any such fees and charges, this provision nevertheless has the potential to restrict product innovation. For example, a credit provider may be hesitant about introducing any new fees or charges in case they are considered inappropriate by the legislators. While this potentially restricts product innovation in the consumer credit industry, it also protects consumers from being charged with unreasonable fees and charges.

Although this potential restriction exists, the extent to which it has impacted on product innovation in practice may be minimal, as there are currently a wide range of fees and charges in existence, some of which have been introduced since the introduction of the Consumer Credit Code.

Both these provisions contradict the policy objective of regulating conduct without restricting product flexibility; however, they do contribute to fair trading outcomes, and specifically that of minimal misleading, deceptive or unconscionable conduct by market participants.

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[21] Section 23(1) also requires that the loan amount be paid in full without deducting an amount for interest charges, except in the circumstances set out in s.23(2). This is not considered to be a restriction on competition.

13.3 Key issues raised in submissions and consultation

Australian Bankers Association:

There is no clear reason for the price controls contained in s.29 of the Consumer Credit Code and hence it should be removed.

13.4 Classification of Restriction 2

Restriction 2 has been classified as a minor restriction on the basis that having versus not having this restriction makes little difference to the economy. That is, the costs associated with this restriction relate to decreased product choice and the subsequent profit generated by the new product for credit providers, while the benefits associated with this restriction include:

- Maintaining and enhancing consumer confidence through ensuring consumers receive the full face value of their credit contract;
- Establishment of a 'level playing field' between consumers and credit providers.

It is anticipated that the net outcomes of these costs and benefits would be less than $1 million per annum to the Australian economy.

We note that consumer confidence is a critical component of an efficiently functioning financial market and, as such, it would be appropriate to suggest that, on face value, the benefits associated with this restriction are greater than its corresponding costs.

In the first instance, there are unlikely to be many consumers who would accept the loan amount in other than cash or money's worth. Secondly, the net benefits that s.23 provides in terms of consumer protection appear obvious. Thirdly, there are currently a wide range of fees and charges in existence despite s.29, and there are no fees and charges currently prohibited under this section. Furthermore, alternative mechanisms exist to protect against excessive fees and charges (see Section 13.5 below).

Therefore, it is our opinion that the benefits and costs associated with this restriction are obvious and do not require detailed analysis to enable individuals to consider the competition issues associated with it.

13.5 Reform Options for Restriction 2

The reform options considered most appropriate for Restriction 2 are Option 1 (Status quo) and Option 2 (Amended status quo). These are discussed in turn in the following sections.

Option 3 (Industry deregulation) and Option 4 (Mandatory code of conduct) have been discarded for the reasons previously outlined in Chapter 11.

13.5.1 Option 1 – Status Quo / Cost-benefit analysis

In the absence of s.23(1), credit providers would be able to provide the loan consideration in something other than cash or money's worth, thus potentially placing the debtor in the position of accepting goods or property as loan consideration. While this would be of little concern where it was the intention of the debtor to use the credit to purchase those particular goods or property, the same cannot be said if the debtor intended to use the loan for other purposes.

For example, if the debtor intended to use the loan for other purposes, the debtor would first have expend time and effort to sell those goods or property before being able to apply the loan to the intended purpose. Furthermore, if the debtor had overvalued the goods or property, the debtor would face an additional cost equivalent to the difference between the realised value of the goods or property and the loan amount.

Thus the existence of s.23(1) in the Consumer Credit Code protects the consumers from potential misleading, deceptive or unconscionable conduct by the credit provider. More specifically, s.23(1) benefits the consumer by ensuring that the consumer receives the full value of the loan amount and protects the consumer from being provided with goods that have been overvalued by the credit provider. However, this comes at a cost of reduced product choice.

The consumer also benefits from having confidence in the transaction, which in turn may benefit the credit provider by generating transactions that would otherwise not have occurred, as well as benefiting the economy through its flow-on effects.

Section 29 potentially prevents a credit provider from introducing a new product that may give the credit provider a competitive advantage over competitors. That is, in the absence of s.29 credit providers could develop credit products based on new fees and charges that gave them a basis for differentiating their products in the market place. Hence the cost to credit providers of having s.29 in the Consumer Credit Code is potentially the income foregone by not introducing that new product. These costs are likely to be minimal given that the impact of s.29 on product innovation appears to have been minimal since the introduction of the Consumer Credit Code.

However, credit providers do incur additional legal costs when developing new products to check compliance with the provisions of the Consumer Credit Code.

Section 29 protects consumers from being charged with unreasonable fees and charges. In its absence, credit providers would be free to impose any fee or charge as there is no alternative existing mechanism for providing the direct restraints on fees and charges imposed by s.29 of the Consumer Credit Code.

This further benefits consumers as they can have confidence in the transaction, which in turn also benefits the credit provider.

Governments also face costs in relation to these provisions, namely those associated with administration of the legislation and coordination of national uniformity[22].

In summary, the Consumer Credit Code clearly provides a net benefit to consumers in relation to s.23(1), while the impact of s.29 has been minimal to date (as the provision has not been used). While both these provisions have the potential to contradict the policy objective of regulating conduct without restricting product flexibility, they do contribute positively to the fair trading outcomes, specifically that of minimal misleading, deceptive or unconscionable conduct by market participants. Hence, both these provisions should be retained within the Consumer Credit Code.

13.5.2 Option 2 – Amended status quo

The review team did not identify any amendments that could be made to ss. 23(1) and 29 to make them less restrictive, while at the same time meeting the objectives of the Consumer Credit Code and the required fair trading outcomes.

13.6 Post Implementation Review Recommendations

PIR Recommendation 2.12 requests 'the Management Committee to monitor the level of new fees and charges that are unilaterally imposed by credit providers during the course of credit contracts'. This recommendation is consistent with s.29 of the Consumer Credit Code.

As noted previously, this section of the Consumer Credit Code has not formally been utilised to restrict the introduction of fees or charges by credit providers. However, regulators do keep an eye on fees and charges and, from time to time, consider the use of s.29 to prohibit particular fees and charges. Section 29 is considered a fallback position to control unscrupulous behaviour, should the need arise.

13.7 Conclusions

In the context that s.23(1) essentially provides protection to those in society who are most at risk from unscrupulous credit providers, and there has been no objections from industry in maintaining this provisions, we believe that the benefits of retaining s.23 in the Consumer Credit Code outweigh the (potential) costs that may arise if it were to be removed.

In relation to s.29, the analysis has indicated that there has been little (positive or negative) impact stemming from this provision to date. That is, s.29 has not been used to prohibit any specific fees or charges, and new fees and charges have been introduced despite its existence. However, s.29 is considered a fallback position to control unscrupulous behaviour, should the need arise. Hence, it may be assumed that there is a need for this provision within Consumer Credit Code and we recommend that the status quo be retained in relation to s.29.

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[22] See footnote 19.

14 Restriction 3: Part 3 disclosure requirements

14.1 Introduction

Part 3 of the Consumer Credit Code has been identified as potentially impacting on competition through disclosure requirements, which increase compliance costs and may act as a prohibitive barrier to entry for small lenders. Specific anti-competitive provisions are:

- Section 39, which requires that a copy of the mortgage documentation be provided to the mortgagor by the credit provider.

- Section 51, which requires disclosure of the credit contract and the rights and obligations of the guarantor prior to the credit contract being secured by the guarantor.

- Section 52, which requires that a copy of the contract documentation and guarantee documentation to be provided to the guarantor by the credit provider.

- Section 56(1), which states that, if the terms of a credit contract are changed to increase or allow for an increase in liabilities, the liabilities of a guarantor under a related guarantee are not increased unless the guarantor has been provided written notice and subsequently provided written acceptance of those changes.

14.2 Nature of Restriction 3

The provisions of Part 3 of the Consumer Credit Code are similar to those of Part 2, but extend the coverage to mortgagors and guarantors. As such, their impact on competition is similar to that of the disclosure provisions within Part 2. That is, the compliance costs associated with meeting these disclosure provisions may act as a barrier to entry for small lenders.

However, the disclosure provisions are the mechanism through which the objective of truth in lending and the issue of information asymmetries are addressed. Specifically, these provisions ensure that the mortgagors and guarantors are fully informed of their financial commitments, while protecting them from unreasonable obligations.

The specific policy objective of s.51 (pre-contractual disclosure) is to place the guarantor in a stronger position to make a determination about whether to become a guarantor of the debtor's obligations (McGill & Willmott 1999).

In addition to the policy objectives noted above, the disclosure requirements also contribute to fair trading outcomes, specifically those of access to appropriate information to enable informed decisions to be made by participants and, in the case of a guarantor, appropriate post-contractual protection.

14.3 Key issues raised in submissions and consultation

There were no comments made specifically in relation to the Part 3 disclosure requirements. However, the comments in relation to Part 2 disclosure requirements (Restriction 1) may be considered relevant in the context of this restriction.

14.4 Classification of Restriction 3

Restriction 3 has been classified as a major restriction on the basis that having versus not having this restriction is likely to make a significant difference to the economy and a detailed analysis of the costs and benefits is needed to demonstrate that this restriction is in the public interest.

14.5 Reform Options for Restriction 3

The reform options considered most appropriate for Restriction 1 are Option 1 (Status quo) and Option 2 (Amended status quo). These are discussed in turn in the following sections.

Option 3 (Industry deregulation) and Option 4 (Mandatory code of conduct) have been discarded for the reasons previously outlined in Chapter 11.

14.5.1 Option 1 – Status quo / Cost-benefit analysis

These requirements add to the administration costs of credit provider and thus to the price paid for credit by consumers. However, the disclosure requirements benefit guarantors and mortgagors by assisting them to make informed decisions. These provisions address the information asymmetries in the market and the objective of truth in lending.

In the absence of these disclosure provisions from the Consumer Credit Code:

- The mortgagor or guarantor may not have a copy of the mortgage or guarantee in their possession, even after they have signed the mortgage or guarantee. Thus, their awareness or knowledge of obligations and rights under the mortgage or guarantee may fall, potentially placing the mortgagor or guarantor in a position of making a sub-optimal choice in relation to their obligations.

- Potential guarantors would lose their right to pre-contractual disclosure of the contents of the credit contract and notice of their rights and obligations. This potentially places guarantors in the position of providing a guarantee when they have little knowledge of the potential financial commitment they may face.

  It should also be noted that guarantors are more vulnerable than other parties to a contract for various reasons, including:

- There are usually no direct benefits accruing to the guarantor from the contract, but the costs can be very high. For example, the cost may include loss of the guarantor's home if a mortgage is given to secure obligations arising under a guarantee; and

- In cases where the debtor and guarantor are family members, the guarantor is often put under considerable emotional pressure to enter into the transaction (whether or not to the knowledge of the credit provider) (Duggan & Lanyon 1999).

■ The guarantor could have their obligations under a guarantee increased without their direct consent, particularly if there is a 'principal debtor clause' in the guarantee. McGill & Willmott (1999) note that it is common for guarantees to contain 'principal debtor clauses', which allows the credit provider to increase credit to a debtor without releasing the guarantor from the liability. If such a clause does not exist, the guarantor can only be held responsible for the obligation that they initially guaranteed.

Thus, the benefits to guarantors and mortgagors from having these information disclosure provisions within the Consumer Credit Code are:

■ Reduced information search costs;

■ Guarantors and mortgagors are fully informed of their financial commitments;

■ Awareness of the implications and financial obligations prior to entering into a guarantee, which potentially protects a guarantor from entering into an inappropriate or unsuitable guarantee; and

■ Protection from an increase in obligations without consent from the guarantor.

The Review team was unable to obtain any quantitative data on the use of these disclosure documents by guarantors or mortgagors. Nevertheless, it may be assumed that these persons place similar value on these documents as do the debtors identified in Malbon's study. That is, it may be assumed that a significant proportion of guarantors and mortgagors read the pre-contractual information provided to them and that a significant proportion of these persons find this information mostly helpful. If this were the case, it would follow then that this information also influences the decisions of a small, but not insignificant, proportion of guarantors and mortgagors.

Credit providers incur the cost[23] of preparing, printing, copying and delivering the required mortgage and guarantee documentation, but may pass these costs on to consumers through higher prices. Furthermore, these costs may act as barriers to entry for small lenders. However, these provisions also deliver a number of benefits to credit providers:

■ Mortgagors and guarantors may be more confident about entering into a mortgage or guarantee, thereby potentially generating consumer credit transactions that otherwise would not have occurred;

[23] See Section 12.5.1

- Increase efficiency with regard to business administration; and
- The promotion of flexibility in product development, which allows for competition based on product differentiation.

Governments also face costs in relation to these provisions, namely those associated with administration of the legislation and coordination of national uniformity[24]. However, the government benefits through reduced requests to government consumer agencies for information relating to consumer credit products.

If it is assumed that the results of the Malbon study may be extrapolated to guarantors and mortgagors, then it may be concluded that these persons place significant value of the information provided to them under Part 3 of the Consumer Credit Code.

The provisions of Part 3 do add to the compliance costs for credit providers, but these costs are ultimately recoverable from the debtors. Furthermore, these annual compliance costs represent only a fraction of the total consumer debt outstanding.

Hence, it may be concluded that this restriction provides a net benefit to consumers. Furthermore, it addresses the objective of truth in lending and the fair trading outcome of providing access to appropriate information to enable informed decisions to be made by market participants.

14.5.2 Option 2 – Amended status quo

The review team did not identify any amendments that could be made to the disclosure provisions within Part 3 to make them less restrictive, while at the same time meeting the objectives of the Consumer Credit Code and the required fair trading outcomes.

14.6 Post Implementation Review Recommendations

There were no recommendations contained within the PIR that have an impact on this restriction or its associated reform option.

14.7 Conclusions

The analysis of the costs and benefits of the reform options relative to the Consumer Credit Code has indicated that there are no alternative mechanisms for achieving the particular objectives of the disclosure requirements within Part 3.

Hence, KPMG recommends the retention of ss.39, 51, 52 and 56(1) of the Consumer Credit Code.

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[24] See footnote 19.

15 Restriction 4: Part 3 product innovation restrictions

15.1 Introduction

Part 3 of the Consumer Credit Code has been identified as also potentially impacting on competition through provisions that limit a credit provider's ability to innovate, specifically:

- Section 46, which limits the securities over which a mortgage may be created.

15.2 Nature of Restriction 4

Section 46 states that a mortgage may not be created over employees' remuneration or employment benefits or benefits under a superannuation scheme, nor may an obligation under a credit contract be secured by a cheque, bill of exchange or promissory note, where this is endorsed by the debtor or guarantor.

This provision restricts competition in the consumer credit industry by limiting the product innovation ability of firms and restricting the potential range of competing products in the market.

The policy objective appears to be:

- To protect mortgagors from entering into agreements that may impose unreasonable obligations;
- To ensure that the Government's social security policy in relation to superannuation is not undermined; and
- To ensure that securities provided are realisable by the credit provider in the event of a default.

Duggan & Lanyon (1999) note that this restrictions stem from recommendations made by both Rogerson and Molomby.

We note that while this provision contradicts the policy objective of regulating credit provider conduct without restricting product flexibility it does however contribute to fair trading outcomes, and specifically those of minimal misleading, deceptive or unconscionable conduct by market participants and providing appropriate post-contractual protection for consumers.

15.3 Key issues raised in submissions and consultation

There were no comments made in relation to Restriction 4 in either the submission or consultation process.

15.4 Classification of Restriction 4

Restriction 4 has been classified as a minor restriction on the basis that, while not having this restriction has the potential to make a significant (negative) difference to the economy, we believe that a detailed analysis of costs and benefits is not likely to be needed to demonstrate that the restriction is in the public interest.

That is, the cost of this restriction relates to a loss of income for credit providers who are unable to satisfy total lending demand due to turning down applicants who do not have sufficient collateral to meet the prudential lending rules and who cannot access other forms of collateral, such as superannuation.

In contrast, the benefits of this restriction relate to:

- Minimising over-commitment to credit in the community; and
- Reducing the potential exposure to Governments who have a social responsibility to provide funding to the aged who do not have adequate superannuation.

The potential to create problems in society, both today (in terms of over-commitment) and into the future (in terms of decreasing a consumer's future wealth), by allowing access to a person's superannuation as collateral is significant.

Therefore, it is our opinion that the benefits and costs associated with this restriction are obvious and do not require detailed analysis to enable individuals to consider the competition issues associated with it.

15.5 Reform Options for Restriction 4

The reform options considered most appropriate for Restriction 1 are Option 1 (Status quo) and Option 2 (Amended status quo). These are discussed in turn in the following sections.

Option 3 (Industry deregulation) and Option 4 (Mandatory code of conduct) have been discarded for the reasons previously outlined in Chapter 11.

15.5.1 Option 1 – Status quo / Cost-benefit analysis

Section 46(1) benefits mortgagors by preventing them from committing to potentially unreasonable financial obligations. For example, if a mortgage were allowed over a person's remuneration, the (extreme) situation may arise whereby the credit provider claimed 100% of a mortgagor's wages or salary. The mortgagor could then be left without a means for providing for everyday necessities.

Prohibiting mortgages to be made over superannuation benefits not only protects consumers from potentially committing to unreasonable obligations, but also protects the integrity of the

Government's superannuation policy, which is central to reducing the reliance on social security as the Australian population ages.

Industry experts note that there is a long history of consumer credit law in relation to the undesirability from a public policy perspective of allowing people to put up superannuation assets as security. We also note that no commentary has been provided by either industry participants or consumer associations as to this provision's ability to actually restrict competition, particularly product innovation, in the market place.

Section 46(2) prohibits securing an obligation under a credit contract by a cheque, bill of exchange or promissory note that is endorsed by the debtor or guarantor. While this potentially limits product innovation and the range of competing product in the credit market, it also protects the credit provider in the event of a default by a debtor, by ensuring that securities provided are realisable.

The costs to credit providers is the income foregone by not being able to offer these types of products. However, these costs are likely to be minimal compared to the benefits delivered to consumers.

Governments also face costs in relation to these provisions, namely those associated with administration of the legislation and coordination of national uniformity[25]. However, the government possibly benefits through reduced dependence on social security.

Hence, it may be concluded that this provision of the Consumer Credit Code delivers a net benefit to the community. Furthermore, it contributes positively to achieving fair trading outcomes, and specifically those of minimal misleading, deceptive or unconscionable conduct by market participants and providing appropriate post-contractual protection for consumers.

15.5.2 Option 2 – Amended status quo

The review team did not identify any amendments to s.46 to make it less restrictive on competition, while at the same time meeting the objectives of the Consumer Credit Code and the required fair trading outcomes.

15.6 Post Implementation Review Recommendations

There were no recommendations contained within the PIR that have an impact on this restriction or its associated reform option.

[25] See footnote 19.

15.7 Conclusions

In the absence of Restriction 4, there would be increased opportunity for market participants to engage in misleading, deceptive or unconscionable conduct may increase, especially towards those consumers who are most at risk.

Therefore, while s.46 of the Consumer Credit Code does not meet all the stated objectives of the legislation, the benefits of keeping the legislation are likely to exceed the benefits of repealing this section of the Consumer Credit Code. Hence, KPMG recommends the retention of s.46 of the Consumer Credit Code.

16 Restriction 5: Part 4 disclosure requirements

16.1 Introduction

Part 4 of the Consumer Credit Code has been identified as potentially impacting on competition through disclosure requirements that result in increased compliance costs for credit providers, specifically:

- Sections 59 to 63, which require the credit provider to notify the debtor in writing of interest rate changes, repayment changes, credit fees and charges changes, and other unilateral[26] changes by the credit provider. In the case of interest rate changes and changes to fees and charges, this written notice may be in the form of a notice in a newspaper circulating throughout the relevant jurisdiction;[27]

- Section 65, which requires written notice of changes agreed by all parties under a credit contract to be provided to the debtor by the credit provider; and

- Section 67, which requires written notice of changes to a credit contract, where these changes are based on grounds of hardship, to be provided to the debtor by the credit provider.

16.2 Nature of Restriction 5

The disclosure requirements in Part 4 of the Consumer Credit Code add to the administration costs of credit providers. As noted previously, the concern with compliance costs is that they potentially act as a barrier to entry for small lenders.

The objective of this provision is to inform consumers about changes to contractual obligations and to provide them with an opportunity to amend their credit arrangements to suit the new terms.

In addition to the above objective, the disclosure requirements also contribute to fair trading outcomes, specifically:

- Access to appropriate information to enable informed decisions to be made by participants;

- Appropriate post-contractual protection for consumers; and

- Minimal misleading, deceptive or unconscionable conduct by market participants.

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[26] The use of the term 'unilateral' is unfortunate as it suggests that credit providers may make any changes they desire. However, credit providers can only make changes where the contract stipulates they may do so. In this respect, they are mutually agreed changes.

[27] These sections do not apply to unilateral changes that are ascertainable from the contract.

16.3 Key issues raised in submissions and consultation

Consumer Credit Legal Service (CCLS):

Since credit providers are not required to individually notify rate changes before the change occurs, the consumer may receive this information some time after the change has occurred when they receive their statement of account. This in turn affect's a consumer's decision to leave or stay with a credit provider and does not allow the consumer to adjust repayments with the interest rate changes.

The CCLS considers the practice of allowing unilateral changes by the credit provider and anti-competitive and suggests that the Consumer Credit Code needs to strike a better balance between the ability of a credit provider to vary the contract and the need for a consumer to be able to rely upon 'the bargain they have struck'.

There is minimal application of the hardship provisions in practice as the debtor and credit provider generally deal directly with each other to reach a compromise and, hence, it is difficult to say that this provision has imposed any cost upon credit providers.

Consumer Credit Subcommittee of the Banking, Finance and Consumer Credit Committee of the Australian Law Council (LCA-CCS):

The LCA-CCS believes that there are ambiguities in Part 4, which should be resolved in the interests of both consumers and credit providers. These ambiguities in the Consumer Credit Code provisions are likely to create differing impacts on credit providers, which may adversely affect an even competitive environment.

16.4 Classification of Restriction 5

Restriction 5 has been classified as a minor restriction on the basis that having versus not having this restriction makes little difference to the economy. That is, the compliance costs relating to this restriction are incremental to other compliance costs, such as the Part 2 disclosure requirements, and are unlikely to be greater than $1 million per annum in net terms.

For example, most notices under ss.59-62 can be dealt with by an advertisement in a widely circulating newspaper, followed by a notice included within the next statement of account. Where the change reduces the debtor's obligation under the credit contract, the notice generally only needs to be provided with the next statement of account. On a per credit contract basis, these costs are likely to be negligible.

In the case of notices under ss.65 and 67, these are required to be provided within 30 days of the change (which may or may not coincide with a statement of account). However, as these are changes affecting a particular debtor (as opposed to, for example, a general interest rate change, which may affect many debtors), there are not likely to be many such notices incurring a significant cost to credit providers during any given year.

16.5 Reform Options for Restriction 5

The reform options considered most appropriate for Restriction 1 are Option 1 (Status quo) and Option 2 (Amended status quo). These are discussed in turn in the following sections.

Option 3 (Industry deregulation) and Option 4 (Mandatory code of conduct) have been discarded for the reasons previously outlined in Chapter 11.

16.5.1 Option 1 – Status Quo / Cost-benefit analysis

These requirements add to the administration costs[28] of credit providers and thus to the price paid for credit by consumers. However, the disclosure requirements benefit consumers by assisting them to make informed credit decisions. These provisions address the information asymmetries in the market and the objective of truth in lending.

In the absence of the Part 4 disclosure provisions from the Consumer Credit Code the credit provider would not have to provide the debtor with written notice of changes to the credit contract, irrespective of whether the changes are unilateral, mutually agreed or based on grounds of hardship.

Thus, the benefits to consumers of having these disclosure provisions within the Consumer Credit Code are:

- Reduced information search costs;
- Debtors are fully informed of their financial commitments; and
- Debtors have the opportunity to adjust their credit arrangements to suit the new terms of the credit contract.

Furthermore, given that importance is placed on the provision of contract documentation, it follows than that providing written notices of changes to that contract is also important. It would also follow then that consumers place significant value on such notification.

Credit providers incur the costs of informing the debtors of the relevant changes to their credit contracts. As noted previously, however, these costs may be only incremental as the notice may be included in the periodic statement of account, or take the form of an advertisement in a newspaper which circulates in the relevant jurisdiction. Furthermore, the costs may be offset through higher fees and charges.

Again, the benefits to credit providers are those associated with increased consumer confidence. That is, increased confidence in the consumer credit market may generate transactions that would other wise not occur.

[28] See Section 12.5.1.

Governments also face costs in relation to these provisions[29], namely those associated with administration of the legislation and coordination of national uniformity. However, the government benefits through reduced requests to government consumer agencies for help relating to changes in credit contracts. Section 66, which sets out the general principles to be followed for changes on the grounds of hardship and the changes the debtor must seek to make to the credit contract in such circumstances, in particular potentially reduces the burden on government consumer agencies.

Given that the costs to credit providers are incremental and the costs to the government are only a small component of the overall cost of administering the Consumer Credit Code, it may be concluded that the disclosure benefits to consumers outweigh any such costs. Hence, the disclosure provisions within Part 5 of the Consumer Credit Code provide a net public benefit.

16.5.2 Option 2 – Amended status quo

The review team did not identify any amendments that could be made to the Part 4 disclosure requirements to make them less restrictive on competition, while at the same time meeting the objectives of the Consumer Credit Code and the required fair trading outcomes.

16.6 Post Implementation Review Recommendations

There were no recommendations contained within the PIR that have an impact on this restriction or its associated reform option.

16.7 Conclusions

The analysis of the costs and benefits of the Part 4 disclosure requirement of the Consumer Credit Code has indicated that there are net benefits to consumers from this restriction. Furthermore, the disclosure provisions meet the objectives of the Consumer Credit Code and deliver on fair trading outcomes, especially:

- Appropriate post contractual protection for consumers; and
- Minimal misleading, deceptive or unconscionable conduct by market participants.

In the absence of an appropriate alternative mechanism for delivering these outcomes, it is recommended that the status quo be maintained for this restriction.

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[29] See footnote 19.

17 Restriction 6: Part 4 potential compliance costs

17.1 Introduction

Part 4 of the Consumer Credit Code was also identified as potentially impacting on competition through potential costs associated with legal costs and loss of potential income as a result of a change in contract obligations, specifically;

- Section 70, which allows the court to reopen a credit contract, guarantee or mortgage on the basis that at the time it was entered into or changed, the contract, mortgage guarantee or change was unjust.
- Section 72, which allows the court to review unconscionable annual percentage rate changes, establishment fees and charges, termination fees and charges and prepayment of credit fees and charges.

17.2 Nature of Restriction 6

Sections 70 and 72 potentially increase costs for credit providers, especially administration, legal costs and potential loss of income as a result of a change in contract terms.

A potential effect of Section 70, and in particular subsection 70(2)(l), is that credit providers, especially mainstream credit providers, view loan applications more cautiously and more readily refuse finance to high risk and low-income borrowers. These borrowers are therefore forced to borrow from other credit providers at higher interest rates, or in some case lenders of last resort. However, we note that this may be a normal market phenomenon – higher risk borrowers tend to borrow funds from non-mainstream lenders at higher interest rates.

While subsection 70(2)(l) was incorporated into the Consumer Credit Code in an attempt to minimise the likelihood of debtor over-commitment, it was also incorporated to discourage the practice of 'asset based lending' in the consumer credit market. Asset based lending occurs where credit is provided by lenders without any regard to the debtor's capacity to pay, but rather is based on the debtor's ability to provide sufficient security. This is confirmed by the second reading speech of the *Consumer Credit (Queensland) Bill*, which states that s.70(2) is:

> *…intended to deal with those lenders who consciously lend without making proper inquiries into the debtor's ability to pay rather than those lenders and borrowers who have gone down this path and made a conscious decision based on the best information available.* (Queensland Government 1994)

McGill & Willmott (1999) note that these provisions were included to provide relief from the general operation of contract law, which failed to develop a general doctrine for the relief against unconscionable contract.

In addition to addressing the objective of providing a redress mechanism for consumers in the event of unjust credit contracts, mortgages, guarantees or unjust changes to such contracts, these provisions also contribute to the following fair trading outcomes:

- Appropriate post-contractual protection for consumers; and
- Provision of redress mechanisms for consumers.

17.3 Key issues raised in submissions and consultation

Ms Denise McGill:

Ms McGill argues that s.70(2)(n) may have an adverse impact on competition because of the difficulty in ascertaining when interest rates are excessive. Interest rates are based partially on the risk involved in the transaction, and this risk is unique to each transaction.

However, if there are any adverse impacts on competition stemming from s.70, these are outweighed by the public benefits. This provisions benefits both consumers and credit providers and strikes a fair balance between their interests.

Furthermore, the alternative mechanisms available are all much narrower in scope than s.70 of the Consumer Credit Code, and hence s.70 is more likely to fulfil the objectives of the Consumer Credit Code.

Ms McGill notes also that the restrictions on competition in s.70 are appropriate as restricting the use of unjust contracts can only serve to preserve fair competition. It does this by discouraging practices which would give an unfair competitive advantage to credit providers willing the exploit the weak negotiating position of vulnerable consumers.

Mr Randall Dennings:

Mr Dennings agrees that the anecdotal evidence suggests that the provision relating to the matters to be considered by the court (s.70(2)) causes mainstream credit providers to view applications more cautiously, but that more research is required to determine the actual effect on mainstream credit providers.

17.4 Classification of Restriction 6

Restriction 6 has been classified as a minor restriction on the basis that having versus not having this restriction makes little difference to the economy. That is, the compliance costs relating to this restriction are incremental to other compliance costs, such as the Part 2 disclosure requirements, and are unlikely to be greater than $1 million per annum in net terms.

Further, this restriction is not a restriction in the purest sense, rather it reflects normal business risk. That is, this risk exists irrespective of whether or not this provision occurs within the Consumer Credit Code. In the absence of these provisions, the credit provider

who engages in unconscionable, harsh or oppressive behaviour in relation to a credit contract, mortgage or guarantee or a change to such a contract, potentially faces penalties under common and statute law.

More specifically, consumers can pursue redress under:

- Contract law;
- *Trade Practices Act 1974* (Part IVA); or
- *Contracts Review Act 1980 (NSW)*, from which s.70 is derived.

However, as noted in Ms McGill's written submission, the alternative mechanisms available under common law are narrower in scope than s.70. This is discussed further in the analysis of regulatory reform options, specifically Option 2 (see Chapter 9).

17.5 Reform Options for Restriction 6

The reform options considered most appropriate for Restriction 1 are Option 1 (Status quo) and Option 2 (Amended status quo). These are discussed in turn in the following sections.

Option 3 (Industry deregulation) and Option 4 (Mandatory code of conduct) have been discarded for the reasons previously outlined in Chapter 9.

17.5.1 Option 1 – Status quo / Cost-benefit analysis

These provisions generally benefit consumers in two ways:

- By requiring lenders to consider the debtor's ability to repay (and not just their ability to provide security), consumers are protected from over-committing themselves under a credit contract; and
- Consumers are protected from unjust or unconscionable credit contract terms.

In the absence of ss. 70 and 72 from the Consumer Credit Code, a consumer could seek redress through:

- Contract law and doctrines of equity;
- *Contracts Review Act 1980 (NSW)*; and
- Part IVA of the *Trade Practices Act 1974.*

However, these mechanisms are generally much narrower in scope than s.70 and are less likely to fulfil the objectives of the Consumer Credit Code than s.70 currently does.

We note that s.51AB of the *Trade Practices Act 1974* and the equivalent sections in the fair trading legislation of each of the States and Territories that deal with unconscionable conduct are similar in scope to s.70 of the Consumer Credit Code, being the operations of credit providers are covered under the nominated legislative frameworks.

However, the practicalities of s.70 are such that the specific circumstances by which a credit contract may be reopened appear to be greater than under either the *Trade Practices Act 1974* or fair trading legislation, such as the over-commitment provision (s.70(2)(l)). We also note that s.70 and 72 are explicitly identified as being relevant to pawnbrokers and trustees of estates, who are generally exempt from the normal operations of the Consumer Credit Code.

These provisions potentially increase costs[30] for credit providers, especially administration expenses, legal costs and potential loss of income as a result of a change in contract terms. Furthermore, these provisions may cause mainstream lenders to view credit applications more cautiously and may refuse credit to high risk and/or low income borrowers. These potential borrowers may then be forced to borrow from high interest lenders.

Governments also face costs in relation to these provisions, namely those associated with administration of the legislation and coordination of national uniformity[31].

Given that the costs to credit providers are incremental and the costs to the government are only a small component of the overall cost of administering the Consumer Credit Code, it may be concluded that the benefits of these consumer protection provisions outweigh any such costs. Hence, the disclosure provisions within Part 5 of the Consumer Credit Code provide a net public benefit.

Furthermore, this restriction addresses the objective of providing a redress mechanism for consumers in the event of unjust credit contracts, mortgages, guarantees or unjust changes to such contracts and also contributes to the following fair trading outcomes:

- Appropriate post-contractual protection for consumers; and
- Provision of redress mechanisms for consumers.

17.5.2 Option 2 – Amended status quo

The review team did not identify any amendments that could be made to s.70 or s.72 to make them less restrictive on competition, while at the same time meeting the objectives of the Consumer Credit Code and the required fair trading outcomes.

[30] See Section 12.5.1.

[31] See footnote 19.

17.6 Post Implementation Review Recommendations

There were no recommendations contained within the PIR that have an impact on this restriction or its associated reform option.

17.7 Conclusions

In conclusion, while it appears that there are alternative legislative frameworks from which to seek redress from contractual conditions, such as the *Trade Practices Act 1974* and fair trading legislation in each State and Territory, we note that these mechanisms are not as specific as those incorporated within the Consumer Credit Code. Hence, it would be fair to suggest that these alternative legislative frameworks would not be able to fully satisfy the objectives of the Consumer Credit Code, nor the fair trading outcome of appropriate post contractual protection for consumers.

Given that the status quo provides a net benefit to consumers and existing alternative legislative mechanisms are unable to provide similar consumer protection outcomes, it is recommended that the status quo be maintained for this restriction.

18 Restriction 7: Part 5 potential compliance costs

18.1 Introduction

In general, the provisions of Part 5 of the Consumer Credit Code impose restrictions on the way a credit provider can enforce or end a credit contract. While there are general restrictions within this Part of the Consumer Credit Code in terms of requirements that must be met, the key competitive issues primarily relate to the potential administration and legal expenses imposed on credit providers.

Those sections of the Consumer Credit Code that have been identified as potentially impacting on compliance costs include:

- Section 76, which requires that a written statement of the pay out figure must be provided upon the written request of the debtor or mortgagor;
- Section 78, which places obligations on both the debtor and credit provider to provide written notices in relation to the voluntary return of mortgaged goods by the debtor or mortgagor to the credit provider, and subsequent sale of those goods;
- Section 80, which requires that a written default notice generally be provided to the debtor or mortgagor prior to beginning any enforcement procedures against a debtor or mortgagor;
- Section 83, which requires that a credit provider obtain court approval before taking possession of mortgaged goods, where the amount owing under the credit contract is below a given threshold;
- Section 91, which requires that a credit provider obtain court approval or written consent from the occupier of the premises, before entering residential premises for the purpose of taking possession of mortgaged goods;
- Section 94, which requires that written notice be provided to the mortgagor after the credit provider has taken possession of the goods. The notice must provide the mortgagor with details of the estimated value of the goods and enforcement expenses incurred, as well as details of the mortgagor's rights and obligations; and
- Section 96, which requires the credit provider, upon sale of repossessed goods, to provide the mortgagor with a written notice of the sale details, including any amounts still outstanding under the credit contract or guarantee.

18.2 Nature of Restriction 7

These sections of the Consumer Credit Code restrict the conduct of credit providers in relation to repossession of mortgaged goods, add to the administrative and legal costs

potentially imposed on credit providers, and thus may act as a barrier to entry for small lenders.

These provisions address the objective of truth in lending so that debtors are informed of their financial commitments and, in the event that they default on their loan, their options and obligations. Furthermore, these provisions facilitate the fair trading outcomes, specifically those of:

- Access to appropriate information to enable informed decisions to be made by participants; and
- Appropriate post-contractual protection for consumers.

18.3 Key issues raised in submissions and consultation

Australian Finance Conference (AFC):

State/territory property laws have similar requirements when it comes to the enforcement of mortgages given to secure either payment to the credit provider under a credit contract or a related guarantee, particularly in relation to default notices, and this is reflected in the current combined default notices allowed under the legislation. The AFC argues that there needs to be greater consistency between these different pieces of legislation.

Consumer Credit Legal Service (CCLS):

The importance of the provision relating to payout figures (s.76) is often understated. Consumers need to be able to obtain a statement of the early termination penalty if they are to have the capacity to make meaningful decisions about early repayment.

Ms Denise McGill:

Sections 78(6) and 96(1) imposes obligations on a credit provider when selling returned and repossessed goods. Ms McGill notes that, in the absence of these provisions, a duty would be imposed on a credit provider by the *Property Law Act 1974* (Qld) and by the general law in other states.

Ms McGill argues that the Consumer Credit Code goes further than necessary to protect consumers and concludes that the alternative mechanisms are less restrictive while still delivering the objectives of the Consumer Credit Code.

Ms McGill argues that s.80 does not provide the redress mechanism for borrowers that they need for it to be an effective restraint upon credit providers and to that extent fails to meet the objectives of the Consumer Credit Code. This stems from the fact that proceedings may still be valid even if the credit provider fails to produce a default notice. However, there is no alternative mechanism for the giving of default notices, and s.80 should therefore be retained to meet the objective of the Consumer Credit Code.

In the case of mortgages of land, the general conveyancing statutes and Torrens legislation impose alternative mechanisms, and for this reason, it seems unnecessarily restrictive on competition for the Consumer Credit Code to impose duplicate requirements.

There are ambiguities in Part 5 which should be resolved in the interests of both consumers and credit providers. These ambiguities in the Consumer Credit Code provisions are likely to create differing impacts on credit providers, which may adversely affect an even competitive environment.

18.4 Classification of Restriction 7

Restriction 7 has been classified as a minor restriction on the basis that having versus not having this restriction makes little difference to the economy. That is, these provisions generally impose only potential costs to most debtors as they generally apply only in cases where the debtor defaults leading to repossession of mortgaged goods and, as such, are likely to be less than $1 million per annum in net terms. Cases where the credit provider enforces the contract and realises security are few in number (Duggan & Lanyon 1999).

These costs may also be mitigated by diligence and care on behalf of the credit provider when assessing a credit application. That is, by taking all reasonable steps to ensure that a potential debtor is able to meet the obligations under a proposed credit contract, a credit provider can minimise the likelihood of a default.

Furthermore, similar obligations are imposed by hire-purchase and property law legislation of the States and Territories.

In the case of a statement of pay out amount, this cost is incremental on a per credit contract basis.

18.5 Reform Options for Restriction 7

The reform options considered most appropriate for Restriction 1 are Option 1 (Status quo) and Option 2 (Amended status quo). These are discussed in turn in the following sections.

Option 3 (Industry deregulation) and Option 4 (Mandatory code of conduct) have been discarded for the reasons previously outlined in Chapter 11.

18.5.1 Option 1 – Status quo / Cost-benefit analysis

These requirements add to the administration costs of credit providers and thus to the price paid for credit by consumers. However, the disclosure requirements benefit consumers by assisting them to make informed credit decisions.

In the absence of these provisions from the Consumer Credit Code:

- Credit providers would not be required to provide statements of pay out amount to debtors. However, they would still be entitled to pay out the contract early, as this right is conferred specifically by s.75 of the Consumer Credit Code;
- The requirements to provide written notices in relation to voluntary return of mortgaged goods and enforcement under default would fall to State and Territory property laws[32] and hire-purchase laws. However, this legislation does not provide the same level of coverage as it overlaps, rather than duplicates, the provisions of the Consumer Credit Code.

Thus, the benefits to consumers from having these provisions within the Consumer Credit Code are:

- Reduced information search costs;
- Debtors are fully informed of their rights and obligations and the repossession process; and
- Debtors have the opportunity to remedy the default prior to action being taken against them;

As there are also obligations on debtors to provide written requests in some instances, debtors potentially also incur administration expenses to prepare such requests.

The potential costs[33] imposed on credit providers are:

- Administration expenses associated with preparing and delivery of statements of payout figure, default notices and details of the repossessed goods; and
- Legal costs associated with obtaining court approval to enter residential premises and to repossess goods.

However, as noted previously, the instances in which these costs apply are relatively few in number and, hence, may not be significant on a per contract basis.

Governments also face costs in relation to these provisions, namely those associated with administration of the legislation and coordination of national uniformity[34].

Given that the costs to credit providers are incremental and the costs to the government are only a small component of the overall cost of administering the Consumer Credit Code, it

[32] Property Law Act 1974 (QLD), Land Title Act 1994 (QLD); Property Law Act 1958 (VIC), Transfer of Land Act 1958 (VIC); Property Law Act 1969 (WA), Transfer of Land Act 1893 (WA); Real Property Act 1886 (SA); Real Property Act 1900 (NSW); Land Titles Act 1980 (TAS); Land Titles Act 1925 (ACT); Real Property Act (NT).
[33] See Section 12.5.1.
[34] See footnote 19.

may be concluded that the benefits of these consumer protection provisions outweigh any such costs. Hence, the disclosure provisions within Part 5 of the Consumer Credit Code provide a net public benefit.

Furthermore, these provisions address the objective of truth in lending so that debtors are informed of their financial commitments and, in the event that they default on their loan, their options and obligations. These provisions also facilitate the fair trading outcomes, specifically those of:

- Access to appropriate information to enable informed decisions to be made by participants; and
- Appropriate post-contractual protection for consumers.

18.5.2 Option 2 – Amended status quo

The review team did not identify any amendments that could be made to these provisions to make them less restrictive on competition, while at the same time meeting the objectives of the Consumer Credit Code and the required fair trading outcomes.

18.6 Post Implementation Review Recommendations

PIR Recommendation 2.11 impacts this restriction in the sense that it requires additional information to be provided to the debtor or mortgagor prior to beginning any enforcement proceedings against them (s.80). This recommendation has no competition policy implications, as the incremental net costs associated with this recommendation are likely to be negligible in real terms. Further, the analysis presented above with respect to reform options is consistent with the intent of the PIR recommendation.

18.7 Conclusions

The analysis of the costs and benefits of Restriction 7 has indicated that there are no effective alternative mechanisms for requiring a credit provider to provide a statement of the pay out amount. That is, in the absence of this particular provision in the Consumer Credit Code, consumers would be faced with increased information search costs.

This statement of pay out amount is required by consumers in order to make informed decisions regarding early pay out of credit contracts. The Consumer Credit Legal Service noted that the importance of this provision in this regard is often understated.

Hence, KPMG recommends the retention of s.76 of the Consumer Credit Code to ensure that consumers are able to make informed decisions throughout the life of their credit contract.

With respect to written notices relating to voluntary surrender of mortgaged goods and enforcement under default, there exists alternative legislation that govern mortgages of real

property and, in some States, hire-purchase agreements. However, the alternative legislation overlaps, rather than duplicates, the provisions of the Consumer Credit Code.

Therefore, these alternative mechanisms do not provide the same protection for consumers, particularly in jurisdictions without hire-purchase legislation and also in relation to goods mortgages. Hence, KPMG recommends the retention of these provisions within the Consumer Credit Code, but notes the concern raised by the Australian Finance Conference that there needs to be greater consistency between the various pieces of legislation.

19 Restriction 8: Part 6 potential compliance costs

19.1 Introduction

Part 6 of the Consumer Credit Code has been identified as potentially impacting on competition through provisions which potentially increase the compliance costs for credit providers, specifically:

- Section 102, which requires a court, on an application being made, to determine whether or not a credit provider has contravened a key requirement (listed in s.100). The court may order the credit provider pay a civil penalty (ie an amount of money) if it is of the opinion that such a breach has occurred. This section also notes the matters that the court must take into account in determining the imposition of a civil penalty;

- Section 103, which sets out the maximum penalty if the application is made by a debtor or guarantor, namely an amount equivalent to the interest charges over the period of the breach. The court may impose an additional penalty if it is satisfied that the debtor or guarantor has suffered an additional loss;

- Section 104, which states that a civil penalty imposed as a result of an application by a debtor or guarantor may be offset against any amount payable under the credit contract, or to the debtor or guarantor if there is no such amount owing;

- Section 105, which sets the maximum penalty (at $500,000) if the application is made by a credit provider or the Government Consumer Agency; and

- Section 106, which states that a civil penalty imposed as a result of an application by a credit provider or Government Consumer Agency must be paid into a fund established for the purposes of this section or, if no such fund exists, to the Government Consumer Agency. With the exception of Western Australia and Tasmania, each State and Territory has established such a fund.

19.2 Nature of Restriction 8

While the individual provisions within Part 6 are (strictly speaking) not anti-competitive, industry commentators have suggested that, overall, the civil penalty regime may impact competition in the following context:

- Whether the severity of the potential penalty for a breach has caused some credit providers, particularly smaller credit providers, to decide that the risk of being subjected to a civil penalty is such that they leave the market; and

- Whether the costs of defending a civil penalty application, which is a form of compliance cost, are that great that the civil penalty regime is imposing unjustifiable costs on credit providers. The following table highlights the significant legal costs associated with recent civil penalty legal proceedings. However, it has also been noted by some industry

commentators that the penalties associated with these proceedings have been minor, or none at all, reflecting that the defence of an application is often seen as penalty enough.

Table 18.1 Consumer Credit Code
Part 6 Related Legal Cases

State	Credit Provider	Costs	Result
NSW	Macquarie Credit Union	$70,000	No civil penalty
QLD	Suncorp-Metway	>$100,000	No civil penalty
QLD	Stafford Parish Credit Union	$38,000	Nominal penalty - $198
QLD	Sunstate Credit Union	$133,000	No civil penalty

Source: Queensland Department of Equity and Fair Trading

While it is acknowledged by the industry that the civil penalty regime may impact on competition, it is worthwhile considering the Molomby Committee's rationale for the inclusion of civil penalty provisions within a legislative framework.

> *The committee regards civil sanctions as an important means of ensuring compliance with the legislation. If a party knows that a breach may lead to his facing financial loss at the instance of the other party to the contract, he has a strong economic incentive to comply with the law. This policy runs through the Money Lenders Acts, the Hire-Purchase Acts, and the Uniform Consumer Credit Code[35]. In some cases amounts under the contract are rendered irrecoverable; in other cases the party can sue to recover amounts. An advantage of civil sanctions is that they are enforceable by the other party to the contract who has a direct economic incentive (particularly when sued) to raise breaches of the legislation. The enforcement does not depend upon action by any public official.*

In other words, the purpose of the civil penalties regime is to encourage compliance by avoiding penalties for a breach or an imposition of sanctions. A secondary purpose is to compensate debtors for loss suffered as a consequence of contraventions (Duggan & Lanyon, 1999).

The civil penalties apply to breaches of 'key requirements', which cover, amongst others, most of the provisions within s.15. In this regard, the civil penalty regime facilitates the objective of truth in lending, as well as that of providing a significant redress mechanism for borrowers. The fair trading outcomes facilitated are:

- Appropriate post-contractual protection for consumers;
- Provision of redress mechanisms for consumers; and
- Minimal misleading, deceptive or unconscionable conduct by market participants.

[35] Refers to the United States Uniform Credit Code (1968).

19.3 Key issues raised in submissions and consultation

Australian Bankers' Association (ABA):

The current civil penalties regime fosters over-compliance by credit providers as it has the potential to penalise a credit provider in a way that is disproportionate to the gravity of the offences, and hence is inefficient.

Australian Finance Conference (AFC):

The AFC asserts that the provision of consumer credit is not sufficiently special to warrant the attention it uniquely attracts through the civil penalties regime. Credit providers are subject to the normal range of laws, including Trade Practices Act, Fair Trading Acts and Credit Administration Acts (where they exist). These Acts provide an armoury to officials and a raft of remedies to consumers

The AFC recommends the removal of the civil penalties, and notes that this would not remove the compliance culture amongst the credit providers.

Consumer Credit Legal Service (CCLS):

Consumer groups continue to strongly support the role of civil penalties under the Consumer Credit Code. The CCLS argues that these provisions assist competition in the credit market and have been fundamental in ensuring a compliance culture amongst credit provider.

Consumer Credit Subcommittee of the Banking, Finance and Consumer Credit Committee of the Australian Law Council (LCA-CCS):

There are unresolved conflicts and tensions between the objective (to encourage compliance) and certain features of the civil penalty provisions. In particular, the civil penalty provisions are also relied upon in varying degrees to perform a number of other functions in particular the provision of compensation to debtors, enforcement of the Consumer Credit Code generally, and licensing.

The LCA-CCS believes that, in one sense, the process itself has become the penalty. This is because the costs incurred by the credit provider in a civil penalty application and the damage to the credit provider's reputation, can be substantially more significant than the actual civil penalty imposed.

Furthermore, there are a number of other factors which also encourage a compliance culture amongst credit providers, and which are presumably considered to be a sufficient compliance incentive in relation to other consumer financial services products, including potential criminal penalties under the Consumer Credit Code and provisions under other legislation (for example, *Trade Practices Act 1974*).

The civil penalty regime has to potential to encourage excessive disclosure and a distortion in the allocation of available resources in that more extensive consideration and analysis may be directed to the key requirements than to other provisions of the Consumer Credit Code.

If a need is perceived to retain some form of civil penalty mechanism in order to encourage compliance, this should be a sanction which encourages compliance by providing an alternative means of punishment in the serious instances of misconduct.

The LCA-CCS believes there would be significant advantages for both credit providers and debtors in introducing a self-rectification mechanism which would permit credit providers to remedy certain types of errors without incurring the significant costs involved in bringing a civil penalty application. Any such procedure should balance the public interest in reducing the cost to credit providers (which is ultimately passed on to debtors), the protection of the interests of debtors and guarantors, and in ensuring public scrutiny of compliance breaches and the provision of relief. ()

Mr Randall Dennings:

The high costs associated with civil penalty legal proceedings act as a barrier to entry. Mr Dennings suggests that an appropriately drawn self-rectification regime will remove this barrier.

19.4 Classification of Restriction 8

Restriction 8 has been classified as a major restriction on the basis that having versus not having this restriction may make a significant difference to the economy and a detailed analysis is required to demonstrate the net benefits of these provisions.

19.5 Reform Options for Restriction 8

The reform options considered most appropriate for Restriction 1 are Option 1 (Status quo) and Option 2 (Amended status quo). These are discussed in turn in the following sections.

Option 3 (Industry deregulation) and Option 4 (Mandatory code of conduct) have been discarded for the reasons previously outlined in Chapter 11.

19.5.1 Option 1 – Status quo / Cost-benefit analysis

As noted previously, the legal costs associated with an application under Part 6 of the Consumer Credit Code can be quite high, and may be disproportionate to the gravity of the offences. The potential cost of being subjected to the civil penalty regime may be high enough to act as a barrier to entry for small firms and may cause small firms to leave the industry.

However, these provisions also reinforce consumer confidence in consumer credit contracts, thereby potentially increasing the number of credit transaction over what would have occurred in the absence of these civil penalties.

Part 6 of the Consumer Credit Code protects consumers by deterring contraventions of the law and, as the civil penalties apply mostly to contraventions of disclosure requirements, these provisions also facilitate the truth in lending objective.

In the absence of civil penalties regime within the Consumer Credit Code the dispute mechanisms associated with the banking, credit union and building society Codes of Practice may potentially provide a process by which to deal with consumer complaints. However, as noted previously, the Codes of Practice do not cover all credit providers, do not have the force of law nor do all the provisions have to be abided by, even if the credit provider has 'adopted' the code. In particular, credit providers who 'adopt' their particular Code of Practice are not bound by the provisions relating to disclosure of terms and conditions, which are the focus of the civil penalties regime.

Governments also face costs in relation to these provisions, namely those associated with administration of the legislation and coordination of national uniformity[36].

The civil penalty regime facilitates the objective of truth in lending, as well as that of providing a significant redress mechanism for borrowers. The fair trading outcomes facilitated are:

- Appropriate post-contractual protection for consumers;
- Provision of redress mechanisms for consumers; and
- Minimal misleading, deceptive or unconscionable conduct by market participants.

19.5.2 Option 2 – Amended status quo

The review team did not identify any amendments that could be made to Part 6 to make it less restrictive on competition, while at the same time meeting the objectives of the Consumer Credit Code and the Required fair trading outcomes.

19.6 Post Implementation Review Recommendations

The PIR recommendations relating to the civil penalties regime are Recommendations 2.16 and 2.17:

- Amend sections 15(G) and 100 to ensure that contingency fees and charges are not key requirements (PIR Recommendation 2.16); and
- Request the Management Committee to examine the level of compliance with section 15N(d) of the Consumer Credit Code (PIR Recommendation 2.17).

[36] See footnote 19.

PIR Recommendation 2.16 impacts this restriction in that it removes contingency fees[37] from the list of key requirements, so that they are no longer subject to the civil penalties regime. This recommendation has minimal competition policy implications, as the incremental costs and benefits associated with this recommendation are likely to be negligible in real terms.

While PIR Recommendation 2.16 has minimal competition impacts, it nevertheless has significant positive practical implications. More specifically, this recommendation, in conjunction with a Schumer Box, will significantly clarify and simplify disclosure requirements. Furthermore, this should also result in fewer breaches since a major uncertainty in respect of disclosure will be eliminated.

PIR Recommendation 2.17 does not have any immediate impacts on the civil penalties regime or any competition policy implications.

19.7 Conclusions

There appears to be two divergent points of view with this restriction, one held by the industry (being that the civil penalty regime is excessive) and the other held by the consumer protection advocates (being that the civil penalties regime provides appropriate behavioural incentives).

Based on the analysis of the costs and benefits of this restriction, as well as the commentary provided by industry participants and stakeholders, it appears that the maintaining of the status quo is the most appropriate for achieving the objectives of the Consumer Credit Code (particularly redress mechanisms) and fair trading outcomes, particularly:

- Appropriate post contractual protection for consumers;
- Provision of redress mechanisms for consumers; and
- Minimal misleading, deceptive or unconscionable conduct by market participants.

Therefore, it is recommended that the status quo be maintained for this restriction.

[37] Contingency fees are those fees and charges that ‘may become payable’ (Batt 1999).

20 Restriction 9: Part 7 discrimination between credit providers

20.1 Introduction

Part 7 of the Consumer Credit Code has been identified as potentially impacting on competition through provisions that discriminate between firms, by imposing potential costs on linked credit providers that other credit providers are not exposed to, specifically:

- Section 118, which attaches liability on the linked credit provider in relation to any statements or representation made by the supplier to the debtor; and

- Section 119, which states that the supplier and linked credit provider are jointly and severally liable to the debtor for any loss or damage suffered by the debtor as a result of misrepresentation, breach of contract or failure of consideration in relation to the sale contract. This section also provides defences for the linked credit provider.

20.2 Nature of Restriction 9

The provisions of Part 7 attach liability to the credit providers for misrepresentations, breach of contract or failure of consideration by the supplier of the goods and services being purchased by credit.

These provisions stem from the Molomby Committee, which considered that a credit provider who had a commercial link with a supplier should carry some responsibility for breach of the terms of the sale contract (Duggan & Lanyon 1999). The rationale behind this was that the decision to buy was often influenced by the availability of credit, such that both the credit provider and supplier benefit.

While the provisions contained within Part 7 of the Consumer Credit Code themselves are not strictly anti-competitive, it could be argued that this Part broadly gives rise to additional costs and risks, such as legal costs, legal liability and administrative costs, to linked credit providers that other sectors of the market, namely credit providers who deal directly with borrowers, are not subjected to. However, in this situation it could be argued that the supplier is essentially acting as an agent of the credit provider and this may balance any additional cost incurred by the credit provider by providing greater market exposure.

This objective is contrary to the stated objective of providing laws which apply equally to all credit providers, as these provisions are specific to linked credit providers. It does, however, facilitate the fair trading outcomes of appropriate post-contractual protection for consumers and provision of redress mechanisms for consumers.

20.3 Key issues raised in submissions and consultation

Australian Bankers' Association (ABA):

The ABA suggests that Part 7 should be simplified by removing those provisions which are duplicated in other legislation. This would reduce the potential for a divergence in administrative approaches.

Australian Finance Conference (AFC):

AFC notes that the provisions in Part 7 relating to joint and severally liability of linked credit providers are superfluous as they are mirrored in the Trade Practices legislation.

Consumer Credit Legal Service (CCLS):

If s.118 did not exist, there would be an even greater lowering of competition as credit providers would be at an advantage in selling through suppliers as their liability for unjust behaviour would be reduced.

20.4 Classification of Restriction 9

Restriction 9 has been classified as a minor restriction on the basis that having versus not having this restriction makes little difference to the economy. That is, the compliance costs relating to this restriction are incremental to other compliance costs, such as the Part 5 potential compliance costs, and are unlikely to be greater than $1 million per annum in net terms.

Further, we also note that, this restriction is not a restriction in the purest sense, rather it reflects normal business risk. While it is appreciated that the linked credit provider potentially faces additional risks relative to other credit providers (by virtue of joint liability), the linked credit provider is able to mitigate this risk by consideration of their choice of supplier and the contract they have with the supplier. More specifically, s.118(2) provides that a 'credit provider is entitled to be indemnified by the person who made the representation, warranty or statement, and any person on whose behalf it was made, against any damage suffered by the credit provider through the operation of this section'.

Further, any additional costs potentially faced by the linked credit provider (by virtue of being a linked credit provider) is offset by the greater market exposure gained by being a linked credit provider.

The *Trade Practices Act 1974* contains similar provisions relating to related sale contracts and these are discussed further in the analysis of reform options, particularly Option 4.

20.5 Reform Options for Restriction 9

The reform options considered most appropriate for Restriction 1 are Option 1 (Status quo) and Option 2 (Amended status quo). These are discussed in turn in the following sections.

Option 3 (Industry deregulation) and Option 4 (Mandatory code of conduct) have been discarded for the reasons previously outlined in Chapter 11.

20.5.1 Option 1 – Status quo / Cost-benefit analysis

Sections 118 and 119 set out the conditions under which a supplier and linked credit provider are jointly and severally liable to the debtor for any loss or damage suffered by the debtor as a result of misrepresentation, breach of contract or failure of consideration in relation to the sale contract.

The costs and benefits of this restriction fall primarily on the linked credit providers who potentially incur legal costs as the result of the actions of a supplier. However, any such costs are considered to be offset by the benefit of greater market exposure the linked credit provider obtains by virtue of being linked to a particular supplier.

We note that these costs and benefits are not exclusive to the Consumer Credit Code. That is, similar provisions exist within the *Trade Practices Act 1974* and, hence, similar costs and benefits would apply in the absence of the Consumer Credit Code.

The definitions of 'linked credit provider', 'tied continuing credit contract' and 'tied loan contract' are utilised in the same terms in both the Consumer Credit Code and the *Trade Practices Act 1974*. Furthermore, these provisions associated with these definitions are generally in the same terms in both pieces of legislation.

Therefore, any difference between the Consumer Credit Code and the *Trade Practices Act 1974* stem from the difference in the definition of 'credit provider', which appears to be broader under the Consumer Credit Code than the *Trade Practices Act 1974*.

Governments also face costs in relation to these provisions, namely those associated with administration of the legislation and coordination of national uniformity[38].

Given that any cost imposed on credit providers is likely to be offset by the benefits of greater exposure, and that the costs to government of this particular restriction is only a component of the overall cost of administering the Consumer Credit Code, it may be concluded that this restriction provides a net public benefit. Furthermore, this restriction facilitates the fair trading outcomes of appropriate post-contractual protection for consumers and provision of redress mechanisms for consumers.

20.5.2 Option 2 – Amended status quo

The review team did not identify any amendments that could be made to ss.118 and 119 to make them less restrictive on competition while at the same time meeting the objectives of the Consumer Credit Code and the required fair trading outcomes.

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[38] See footnote 19.

20.6 Post Implementation Review Recommendations

PIR Recommendation 2.7 relates to Restriction 9 in the context that it recommends reviewing if there is unnecessary overlap between Part 7 of the Consumer Credit Code and the *Trade Practices Act 1974*, which was essentially considered in the cost-benefit analysis presented above.

This analysis concluded that there are differences, albeit definitional, between the Consumer Credit Code and the *Trade Practices Act 1974* that suggest that the scope of the *Trade Practices Act 1974* is narrower than the Consumer Credit Code in this area.

20.7 Conclusions

As noted above, the provisions associated with linked credit providers appear to be almost the same between the Consumer Credit Code and the *Trade Practices Act 1974*, with the exception that the definition of a credit provider is broader under the Consumer Credit Code than the *Trade Practices Act 1974.*

This suggests that the Consumer Credit Code provider broader consumer protection than does the *Trade Practices Act 1974* with respect to credit contracts, specifically in relation to coverage of credit providers.

Further the Consumer Credit Legal Service observes that duplicate provisions within the Consumer Credit Code should not be deleted as the jurisdiction, coverage, statutes of limitation, redress options and simplicity may vary between legislative frameworks.

Given these issues, it is our recommendation that the status quo be maintained for this restriction. Further, our analysis has effectively implemented PIR Recommendation 2.8, with the outcome being no change to Part 7 of the Consumer Credit Code.

21 Restriction 10: Part 7 third line forcing restrictions

21.1 Introduction

Part 7 of the Consumer Credit Code has also been identified as potentially impacting on competition through provisions that limit a supplier's ability to force a consumer into taking a credit contract from a particular credit provider, specifically:

- Section 130, which prohibits a supplier from requiring the buyer to apply for, or obtain, credit from a particular credit provider.

21.2 Nature of Restriction 10

Section 130 prohibits a supplier from requiring the buyer to apply for, or obtain, credit from a particular credit provider. In terms of the competition guidelines, this restriction has the ability to constrain firms in terms of the business decisions that they are free to make. While this is true, the objective of this provision is really to maintain consumer choice in terms of the choice of credit provider. In this respect, the legislation may be considered pro-competitive as it allows for increased consumer choice rather than increased market concentration.

Thus, this provision addresses the objective of maintaining consumer choice, which is also a fair trading outcome.

21.3 Key issues raised in submissions and consultation

There were no issues raised specifically in relation to this restriction in the submissions or consultation process. However, the comments noted in Restriction 9 in relation to duplicate provisions may be relevant to this restriction also, specifically *Trade Practices Act 1974* overlaps.

21.4 Classification of Restriction 10

Restriction 10 has been classified as a minor restriction on the basis that having versus not having this restriction makes little difference to the economy. That is, the compliance costs relating to this restriction are incremental to other compliance costs, such as the Part 5 potential compliance costs, and are unlikely to be greater than $1 million per annum in net terms.

We also note that, although this provision restricts the conduct of the credit provider through their linked associated with a supplier, it may be considered pro-competitive because it allows for increased competition rather than increased market concentration.

Furthermore, this conduct is also prohibited under s.47 of the *Trade Practices Act 1974* and is discussed further in the analysis of regulatory change options, particularly Option 1 (see below).

21.5 Reform Options for Restriction 10

The reform options considered most appropriate for Restriction 1 are Option 1 (Status quo) and Option 2 (Amended status quo). These are discussed in turn in the following sections.

Option 3 (Industry deregulation) and Option 4 (Mandatory code of conduct) have been discarded for the reasons previously outlined in Chapter 11.

21.5.1 Option 1 – Status quo / Cost-benefit analysis

Section 130, which prohibits suppliers to force consumers to apply for, or obtain, credit from a particular credit provider, potentially restricts competition by constraining firms in terms of the business decisions they are free to make.

Specifically, the costs associated with this restriction include the loss of potential economies of scale and scope between credit provider and supplier, especially with respect to administration costs. Further, this restriction impedes on the facilitation of faster transactions between suppliers and consumers. However, this cost to suppliers can also be argued as a benefit to consumers as without this restriction consumers may feel pressured to take the products immediately, rather than deliberating over the purchasing decision further.

In the absence of s.130 from the Consumer Credit Code, consumers could seek protection from this conduct by s.46(7) of the *Trade Practices Act 1974*. However, as already noted previously, the Consumer Credit Code is wider in scope and coverage than the *Trade Practices Act 1974* and, as such, provides for greater consumer protection specifically with respect to securing credit.

Governments also face costs in relation to these provisions, namely those associated with administration of the legislation and coordination of national uniformity[39].

Hence, it is likely that this restriction provides a net public benefit, with most of the benefit falling to consumers. Furthermore, this restriction addresses the objective and fair trading outcome of maintaining consumer choice.

21.5.2 Option 2 – Amended status quo

The review team did not identify any amendments that could be made to s.130 to make it less restrictive on competition, while at the same time meeting the objectives of the Consumer Credit Code and the required fair trading outcomes.

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[39] See footnote 19.

21.6 Post Implementation Review Recommendations

As with Restriction 9, this restriction is impacted by PIR Recommendation 2.8 that suggests that Part 7 of the Consumer Credit Code be reviewed in the context of potential overlap with the *Trade Practices Act 1974*. This recommendation has essentially been completed within this NCP review, given that the intent of PIR Recommendation 2.8 was considered in the cost-benefit analysis.

21.7 Conclusions

In analysing this restriction we made note of its impact on the promotion of faster transactions and economies of scale between suppliers and consumers.

While we make this point, it is useful to restate some of Malbon's (1999) findings with respect to consumer purchases of linked credit. His research revealed that consumers' main motivation with respect to taking credit is the desire to purchase the underlying good. Secondary motivational factors included terms (such as fees and charges). This suggests that consumers may not give sufficient consideration to a credit contract at the time of purchasing a good as they possibly should.

Therefore, it would appear justifiable to maintain some level of consumer protection against these activities. While the *Trade Practices Act 1974* provides such protection, the Consumer Credit Code provides protection for consumers against a wider range of credit providers. That is, the scope of the Consumer Credit Code is broader in terms of its coverage of credit providers than is the *Trade Practices Act 1974*. In this sense, we have recommended that Restriction 10 remain, and the status quo be retained.

Further, our analysis has effectively implemented PIR Recommendation 2.8, with the outcome being no change to Part 7 of the Consumer Credit Code.

22 Restriction 11: Part 8 third line forcing restrictions

22.1 Introduction

Part 8 of the Consumer Credit Code has been identified as potentially impacting on competition through provisions which restrict third line forcing, specifically:

- Section 133, which prevents a credit provider from requiring a debtor to take out some types of insurance, or to take insurance out with a particular insurer; and

22.2 Nature of Restriction 11

At first glance, it appears that s.133 restricts the credit provider from providing bundled insurance and credit products and, more generally, has the potential to impact the credit market with respect to product innovation.

However, as noted in the *Consumer Credit Code Guideline 2000/1*, issued by SCOCA in June 2000, product bundling is permissible provided that, if the prospective debtor or guarantor declines to take out the insurance or to take out that insurance with a particular insurer, the credit is still available (regardless of whether that credit is then offered at the same or a higher price).

The primary purpose of s.133 is to prevent ‘insurance forcing’ (or third line forcing, as it is known more generally), which is the situation where credit is made available on the condition that insurance is also taken out and/or taken out with a particular insurer.

Therefore, this provision effectively prohibits insurance forcing but does not limit product innovation. The objective of this provision is therefore to maintain consumer choice (in terms of choice of insurer) and to protect consumers from taking out unnecessary insurance.

Hence, this restriction achieves the objective of applying rules that regulate the credit provider’s conduct without restricting product innovation and consumer choice. In addition, this restriction also facilitates the following fair trading outcomes:

- Minimal misleading, deceptive or unconscionable conduct by market participants; and
- Minimal restrictions on product flexibility and consumer choice.

22.3 Key issues raised in submissions and consultation

Australian Bankers’ Association (ABA):

Section 133, which prohibits requiring insurance to be taken out or to be taken out with a particular insurer, acts as an impediment to the development of innovative product bundles.

Furthermore, there is added confusion due to the inconsistencies with the regulatory approach (towards third line forcing) adopted in the *Trade Practices Act 1974*. The ABA contends that all insurance matters should be regulated within one regulatory environment.

The provisions of Part 8 overlap with those in the Insurance Contracts Acts 1984 (Cth). This not only adds compliance costs for the credit provider, but also adds to the bulk of information provided to the consumer (without necessarily adding to the quality of information).

Australian Finance Conference (AFC):

The AFC sees considerable merit in, and justification for, removing from Part 8 of the Consumer Credit Code the provisions that regulate insurance or that require insurance related disclosure, and notes that there should be no adverse implications for consumer protection due to the comprehensive regulation at the Commonwealth level.

Furthermore, the AFC argues that this area of regulation needs rationalisation, where this is best achieved by placing all regulation of insurance in one regulatory environment, or at least removing overlaps and duplications.

Consumer Credit Legal Service (CCLS):

The CCLS notes that deleting duplicate provisions in Part 8 (Related insurance contract), as per the PIR Recommendation 2.5, would have the effect that consumers will no longer be able to use low cost Consumer Tribunals to determine some insurance disputes (as the Tribunals do not have jurisdiction over insurance legislation).

Mr Randall Dennings:

Mr Dennings questions whether there are any consumer benefits delivered by ss.133(2) and 135 because of the practical difficulties created by those sections.

22.4 Classification of Restriction 11

Restriction 11 has been classified as a minor restriction on the basis that having versus not having this restriction makes little difference to the economy. That is, the compliance costs relating to this restriction are incremental to other compliance costs, such as the Part 5 potential compliance costs, and are unlikely to be greater than $1 million per annum in net terms.

Although this provision restricts the conduct of the credit provider, it is actually pro-competitive because it allows for increased competition through increasing consumer choice, rather than increased market concentration.

Furthermore, this conduct is also prohibited under s.47 of the *Trade Practices Act 1974* and is discussed further in the cost-benefit analysis (see below).

22.5 Reform Options for Restriction 11

The reform options considered most appropriate for Restriction 1 are Option 1 (Status quo) and Option 2 (Amended status quo). These are discussed in turn in the following sections.

Option 3 (Industry deregulation) and Option 4 (Mandatory code of conduct) have been discarded for the reasons previously outlined in Chapter 11.

22.5.1 Option 1 – Status quo / Cost-benefit analysis

Section 133, which prohibits forcing debtors to purchase some types of insurance or to take out insurance with a particular insurer, potentially restricts product innovation within the consumer credit industry, as well as limits firms' ability in terms of business decisions they are free to make. Credit providers wishing to introduce bundled (credit and insurance) products are restricted by the current legislative framework.

As with Restriction 10, the costs associated with this restriction include:

- The loss of potential economies of scale and scope between credit providers and insurers (ie administration costs); and

- Impedes the facilitation of minimising credit risk for the credit provider by ensuring that not all credit risk is mitigated by some form of insurance.

In contrast, the benefit of this provision is that it doesn't allow for the inappropriate transfer of risk from one party to another. That is, there are basic levels of risk that exist in any given transaction, be it credit related or otherwise.

S.133 of the Consumer Credit Code ensures that one party to the transaction, being the credit provider, does not, through their position of influence, shift the responsibility, and costs, of all the transactions risk to the other party, being the consumer.

In the absence of s.130 from the Consumer Credit Code, consumers could seek protection from this conduct by s.47 of the *Trade Practices Act 1974*. However, as already noted previously, the Consumer Credit Code is wider in scope and coverage than the *Trade Practices Act 1974* and, as such, provides for greater consumer protection specifically with respect to securing credit.

Consistent with the commentary provided for Restriction 10, we note that the Consumer Credit Code has a broader coverage than does the *Trade Practices Act 1974*, and as such provides for greater consumer protection over credit providers.

The *Insurance Contracts Act 1984* was also noted in the submissions as being overlapping legislation. However, on review of this piece of legislation it appears that the concept of 'forcing' from another party (being the credit provider) is outside its scope or coverage.

Governments also face costs in relation to these provisions, namely those associated with administration of the legislation and coordination of national uniformity[40].

Given that the costs to credit provider are incremental and the costs to government are only a small component of the overall cost of administering the Consumer Credit Code, it may be concluded that the benefits of these consumer protection provisions outweigh any such costs. Hence, s.133 of the Consumer Credit Code provides a net public benefit.

22.5.2 Option 2 – Amended status quo

The review team did not identify any amendments that could be made to s.133 to make it less restrictive on competition, while at the same time meeting the objectives of the Consumer Credit Code and the required fair trading outcomes.

22.6 Post Implementation Review Recommendations

PIR Recommendations 2.5 and 2.6 specifically relate to s.133 of the Consumer Credit Code, being the regulation of insurance associated with credit contracts. The key issues associated with these recommendations include:

- The deletion of provisions in the Consumer Credit Code that overlap with the *Insurance Contracts Act* (Recommendation 2.5); and
- Harmonising the approach taken by the Consumer Credit Code to that of s.47 of the *Trade Practices Act 1974* for 'bundled products'.

While the key issues of these PIR recommendations do relate to the practical operation of s.133, they do not influence the competition restrictions associated with s.133, being third line forcing. In this respect, the PIR recommendations are not inconsistent with the analysis completed above, nor are they anti-competitive in nature themselves.

22.7 Conclusions

The objective of s.133 of the Consumer Credit Code is to ensure that consumers are not taken advantage of by credit providers through the unnecessary purchase of insurance, or the purchase of over-priced insurance from linked insurance providers. That is, the emphasis of this restriction is the forcing of insurance, not what is incorporated within an insurance contract per se.

Given this, the key issue with respect to the reform option is whether or not alternative regulatory frameworks provide the same, or enhance, levels of consumer protection in comparison to the Consumer Credit Code. We have already noted in this review that the

[40] See footnote 19.

Consumer Credit Code has a broader scope in terms of defining a ‘credit provider’ than does the *Trade Practices Act 1974*.

In this instance, it is only the *Trade Practices Act 1974* that provides an alternative legislative framework to ensure consumer protection with respect to ‘forcing’. Therefore, it is recommended that the status quo be retained for this restriction.

23 Restriction 12: Part 8 pricing restrictions

23.1 Introduction

Part 8 of the Consumer Credit Code has also been identified as potentially impacting on competition through provisions that restrict pricing, specifically:

- Section 135, which limits commissions earned by credit providers for introducing customers to a particular insurer to 20% of the premium, excluding government charges.

23.2 Nature of Restriction 12

Section 135 of the Consumer Credit Code sets a limit of 20% on a commission paid (to a credit provider, supplier or agent thereof) by an insurer in connection with consumer credit insurance taken out by the debtor. This provision restricts competition by limiting the business decisions credit providers may make, especially in terms of pricing.

This provision contradicts the objective of relying on market forces to provide price restraint. However, s.135 protects consumers from paying high insurance premiums, which may result from reverse competition within the credit insurance industry (that is, insurers bidding against each other for access to credit providers, who effectively act as agents for the insurer).

23.3 Key issues raised in submissions and consultation

Australian Finance Conference (AFC):

There is no clear reason for the price controls contained in s.135 of the Consumer Credit Code and hence it should be removed.

Consumer Credit Legal Services (CCLS):

The CCLS noted in the consultation phase that industry practice prior to the introduction of the Consumer Credit Code was such that a price cap was necessary to ensure consumer protection against unscrupulous operators.

Mr Randall Dennings:

Mr Dennings questions whether there are any consumer benefits delivered by ss.133(2) and 135 because of the practical difficulties created by those sections.

23.4 Classification of Restriction 12

Restriction 12 has been classified as a minor restriction on the basis that a detailed analysis is not likely to be needed to demonstrate that this restriction is in the public interest. That is, the benefits of this restriction relate to prohibiting credit providers and insurance companies

colluding to set commissions that are ultimately funded by the consumer. The value of these benefits would match equally the costs of this restriction, being the additional revenue to credit providers. However, we note that the competition issue relates to the transfer of funds from consumers to credit providers that may otherwise have been put to more productive or efficient uses.

Past experience has shown that, in the absence of an upper cap on commissions, insurance commissions can be excessively high. For example, from our survey of industry participants it was revealed that commissions were around 25% prior to the introduction of the Consumer Credit Code.

Furthermore, this provision applies only to consumer credit insurance, which is an optional insurance. Hence, this provision only applies to a subset of all consumer credit contracts.

23.5 Reform Options for Restriction 12

The reform options considered most appropriate for Restriction 1 are Option 1 (Status quo) and Option 2 (Amended status quo). These are discussed in turn in the following sections.

Option 3 (Industry deregulation) and Option 4 (Mandatory code of conduct) have been discarded for the reasons previously outlined in Chapter 11.

23.5.1 Option 1 – Status Quo / Cost-benefit analysis

Section 135 of the Consumer Credit Code sets a limit of 20% on a commission paid (to a credit provider, supplier or agent thereof) by an insurer in connection with consumer credit insurance taken out by the debtor.

The benefit of this provision is that it protects consumers who choose to take out consumer credit insurance from paying high insurance premiums, which could result from reverse competition within the credit insurance industry (that is, insurers bidding against each other for access to credit providers, who effectively act as agents for the insurer).

Past experience has shown that, in the absence of a cap on consumer credit insurance commissions, reverse competition has resulted in (excessively) high insurance commissions for credit providers. Industry sources have indicated that the average commissions were about 25% prior to the introduction of the Consumer Credit Code.

For illustration purposes, if we assume that credit providers currently receive that maximum commission allowable (ie 20%), and that in the absence of this provision:

1. Credit providers would receive commissions (as a percentage of the insurance premium) similar to those levels previously experienced prior to the introduction of the Consumer Credit Code (ie 25%); and

2. The commissions increase would be reflected in the total premium payable, rather than the insurer reducing the net amount they receive;

then consumers would face an increase in premiums of 6.7%, with no corresponding increase in the benefits they would receive from the insurer.

Furthermore, high commissions may provide an incentive to credit providers and dealers to sell unnecessary or overpriced insurance (Duggan & Lanyon 1999). Consumers are therefore also protected from potentially being encouraged to take up unnecessary insurance.

The main cost to credit providers of this provision is that they are potentially missing out on higher commissions from insurers.

Governments also face costs in relation to these provisions, namely those associated with administration of the legislation and coordination of national uniformity[41].

23.5.2 Option 2 – Amended status quo

The review team did not identify any amendments that could be made to s.135 to make it less restrictive on competition, while at the same time meeting the objectives of the Consumer Credit Code and the required fair trading outcomes.

23.6 Post Implementation Review Recommendations

There were no recommendations contained within the PIR that have an impact on this restriction or its associated reform option

23.7 Conclusions

This restriction provides clear consumer protection outcomes in that it intervenes in situations where two parties agree on commercial terms to a transaction, although it is a third party who is the ultimate funder of this commercial relationship. That is, this provision protects the third party, in this case being a consumer taking out credit insurance, from being taken advantage of by other participants to the contract, being the insurer and credit provider.

In conducting the cost-benefit analysis, we considered the situation that would arise in the absence of s.135 of the Consumer Credit Code, and we have found such an action creates the opportunity for consumer exploitation. Therefore, it is recommended that the status quo be maintained for this restriction.

[41] See footnote 19.

24 Restriction 13: Part 9 conduct restrictions

24.1 Introduction

Part 9 of the Consumer Credit Code has been identified as potentially impacting on competition through provisions which restrict the conduct of credit providers, specifically:

- Sections 140 and 143, which regulate the content of advertisements; and
- Section 146, which restrict credit providers from visiting a person at home for the purpose of inducing them to apply for credit.

24.2 Nature of Restriction 13

These provisions restrict the conduct of credit providers, and it could be suggested that s.146 of the Consumer Credit Code limits the entrepreneurial ability of credit providers to seek out customers.

Sections 140 and 143[42] regulate the content of advertisements in relation to disclosure of annual percentage rates, comparison rates, and fees and charges. While an annual percentage rate is generally not required to be included in an advertisement, where it is included the advertisement must comply with the requirements set out in ss.140 and 143. Furthermore, if a comparison rate is included in the advertisement, it must be calculated in accordance with the legislation and be accompanied by specific warnings.

These provisions effectively extend the truth in lending principle to advertisements, ensuring that, if the advertisement makes a statement about the cost of credit, all the costs are noted or referred to in the advertisement and that they are referred to 'truthfully'.

Section 146 stems from the Molomby Committee recommendation that new credit legislation prohibit the hawking (ie. offering from door-to-door) of credit as 'the consumer in his home should not have to resist persuasions to accept a commodity of such universal appeal as money' (Duggan & Lanyon 1999, p.122).

In addition to addressing the objective of truth in lending, these provisions also facilitate fair trading outcomes, specifically:

- Access to appropriate information to enable informed decisions to be made by participants; and
- Minimal misleading, deceptive or unconscionable conduct by market participants.

[42] Both ss.140 and 143 are to be amended by ss.54 and 55, respectively, of the *Consumer Credit (Queensland) Amendment Act 1998*, which commenced on 28 October 1998. The discussion in this chapter is based on the amended versions of ss.140 and 143.

24.3 Key issues raised in submissions and consultation

Australian Bankers' Association (ABA):

The ABA notes that there is significant duplication between sections of the Code and the provisions within the *Trade Practices Act 1974*, ss.140 and 144 (which are partly mirrored in ss.52 and 53 of the *Trade Practices Act 1974*).

Australian Finance Conference (AFC):

The Trade Practices Act 1974 and state and territory fair trading legislation regulate credit advertising and prohibit harassing conduct in connection with the supply or possible supply of goods and services, as well as payment thereof.

The AFC therefore sees merit in research being undertaken to delineate the extent of overlap to ensure the Consumer Credit Code only deals with matters not addressed elsewhere. Furthermore, there appears to be no justification for any provision within the Consumer Credit Code to deal with harassment and thus s.145 does not need to be retained.

Consumer Credit Legal Service (CCLS):

The CCLS argues that the provisions relating to advertising have failed in creating a competitive market as they have little impact on forcing credit providers to advertise the cost of credit. Home loans are an exception.

Ms Denise McGill:

Ms McGill notes that this section facilitates competition by informing consumers, the benefits outweigh the costs, and there are no alternatives for achieving the objectives of the legislation.

Mr Randall Dennings:

Mr Dennings questions whether there are any consumer benefits delivered by the provisions of Part 9 of the Consumer Credit Code because of the practical difficulties created by those provisions.

In addition to the above specific comments, the comments regarding the comparison rate noted in relation to Restriction 1 (See Section 12.3) are also relevant here.

24.4 Classification of Restriction 13

Restriction 13 has been classified as a minor restriction on the basis that having versus not having this restriction makes little difference to the economy. That is, the compliance costs relating to this restriction are incremental to other compliance costs, such as the Part 5 potential compliance costs, and are unlikely to be greater than $1 million per annum in net terms.

Further, the Australian Finance Conference note in their written submission that the *Trade Practices Act 1974* and the fair trading legislation in each State and Territory also regulate the advertising of credit.

In the case of canvassing of credit at residential premises (relating to s.146), this may be dealt with by the harassment and coercion provisions in the above legislation. Alternatively, s.70 of the Consumer Credit Code may be relevant. More specifically, s.70(2)(j) allows the court to set aside a credit contract on the basis of the exertion of unfair pressure, undue influence or unfair tactics.

These alternative mechanisms are discussed further in the cost-benefit analysis below.

24.5 Reform Options for Restriction 13

The reform options considered most appropriate for Restriction 1 are Option 1 (Status quo) and Option 2 (Amended status quo). These are discussed in turn in the following sections.

Option 3 (Industry deregulation) and Option 4 (Mandatory code of conduct) have been discarded for the reasons previously outlined in Chapter 11.

24.5.1 Option 1 – Status Quo / Cost-benefit analysis

Part 9 of the Consumer Credit Code facilitates the truth in lending objective while also providing for consumer protection.

In the absence of ss.140 and 143, reliance would be placed on other provisions within the Consumer Credit Code, existing duplicate legislation or, where neither of those are available, on market forces for delivering the same consumer protection and information disclosure outcomes as under Part 9 of the Consumer Credit Code. More specifically:

- Section 144 (False and misleading representations) of the Consumer Credit Code potentially provides an alternative mechanism which consumers could rely upon to deliver the truth in lending objectives of ss.140 and 143;

- Section 53 of the *Trade Practices Act 1974*, which prohibits the making of a false or misleading representation with respect to the price of goods or services, and the equivalent provisions in the State and Territory fair trading legislation could also be relied upon. Where a consumer would be required to rely on these alternative frameworks, it appears that they would have similar remedies, and applications would be heard in similar courts and tribunals, particularly under the State and Territory fair trading legislation, as would be available to them currently under the Consumer Credit Code provisions; and

- With respect to s.146 of the Consumer Credit Code, it appears that s.70(2)(j) provides similar consumer protection outcomes on the basis that door-to-door selling of credit falls within the ambit of unfair pressure, influence or tactics. While this is true, the

reliance on s.70(2)(j) would not however allow the original recommendation of the Molomby Committee to be achieved. This recommendation was that 'the consumer in his home should not have to resist persuasions to accept a commodity of such universal appeal as money'. Further, this argument was not contested by any stakeholder through the submission or consultation process.

Thus having ss.140, 143 and 146 within the Consumer Credit Code potentially benefit consumers by:

- Reducing information search costs (ss.140 and 143);
- Providing for some uniformity in advertising, thereby reducing the potential for confusion and potentially making it easier to compare credit products (ss.140 and 143); and
- Protecting consumers from having to attempt to resist credit whilst within the comforts of their own home (and potentially purchasing credit that they may not need and would otherwise not purchase) (s.146).

In relation to advertisements, ss.140 and 143 do not require compulsory disclosure of interest rates or comparison rates. Hence, these benefits only apply to advertisements that contain either an interest rate or a comparison rate.

While not imposing any administrative or similar costs on credit providers, these provisions potentially limit the entrepreneurial ability of credit providers. By restricting the ways in which credit providers are allowed to entice consumers into purchasing credit, the credit provider is potentially foregoing additional sales of consumer credit.

Governments also face costs in relation to these provisions, namely those associated with administration of the legislation and coordination of national uniformity[43]. However, the government benefits through reduced requests to government consumer agencies for information relating to consumer credit products.

Given that this provision imposes only incremental costs on credit providers and the cost to the government is only a component of the total cost of administering the Consumer Credit Code, it may be concluded that this restriction provides a net public benefit, with most of the benefit falling to consumers.

Further, this restriction addresses the objective of truth in lending and facilitates fair trading outcomes, specifically:

- Access to appropriate information to enable informed decisions to be made by participants; and
- Minimal misleading, deceptive or unconscionable conduct by market participants.

[43] See footnote 19.

24.5.2 Option 2 – Amended status quo

The review team did not identify any amendments that could be made to ss.140, 143 or 146 to make them less restrictive on competition, while at the same time meeting the objectives of the Consumer Credit Code and the required fair trading outcomes.

24.6 Post Implementation Review Recommendations

The PIR recommendations relevant to this restriction are Recommendations 1.4 and 2.7.

PIR Recommendation 1.4 impacts this restriction in that it requires credit providers to include a comparison rate in all advertisements for fixed term products. This recommendation has competition policy implications since it increases compliance costs and reduces independent decision making by credit providers. However, the incremental costs associated with this recommendation are likely to be negligible in real terms.

The objective of this recommendation reinforces one of the objectives of the Consumer Credit Code, which is to allow consumers to make informed choices when purchasing credit. Further, it also provides for ensuring fair trading outcomes, specifically that of access to appropriate information that enables consumers to make informed choices

This being said, we also appreciate the industry concerns regarding the use of comparison rates. However, the Consumer Credit Code Regulation do stipulate that where a comparison rate is presented, it must be accompanied by a warning outlining the shortcomings of using the rate for comparative purposes.

PIR Recommendation 2.7 does not have any immediate impacts on the advertising provisions within Part 9 of the Consumer Credit Code or any competition policy implications.

24.7 Conclusions

Based on the arguments presented above, it appears that ss.140 and 143 of the Consumer Credit Code could be repealed with minimal loss of consumer protection as an outcome. Rather, consumers are able to rely upon:

- Section 144 of the Consumer Credit Code;
- Section 53 of the *Trade Practices Act 1974*; and
- Various consumer protection provisions of State and Territory fair trading legislation;

to achieve the same level of consumer protection as currently enjoyed under ss.140 and 143 of the Consumer Credit Code. However, these alternative mechanisms do not deliver the same direct restraints on credit providers and, hence, may not be as effective in practice as ss.140 and 143.

With respect to s.146 of the Consumer Credit Code, it appears that no alternative reform option would enable consumers to achieve the same objectives and fair trading outcomes as they currently achieve, as under any alternative consumers may become subject to the selling of credit at their door.

In conclusion, we recommend that the status quo be retained for this restriction.

25 Restriction 14: Part 10 disclosure requirements

25.1 Introduction

Part 10 of the Consumer Credit Code has been identified as potentially impacting on competition through disclosure requirements that result in increased compliance costs for credit providers (lessors), specifically:

- Section 152, which requires the consumer lease to contain certain information relating to the consumer lease;
- Section 153, which requires a copy of the lease documentation be provided to the debtor (lessee);
- Section 155, which applies s.67 of the Consumer Credit Code to consumer leases. Section 67 requires written notice of changes to a credit contract, where these changes are based on grounds of hardship; and
- Section 156, which requires the credit provider (lessor) to generally provide 30 days' written notice of an intention to repossess goods.

25.2 Nature of Restriction 14

The objective of Part 10 is to discourage the use of consumer finance leases as a way of avoiding regulation, although the consumer lease provisions in Part 10 have been identified as being significantly less stringent than the consumer credit provisions within the Consumer Credit Code.

In this respect, the concerns relating to restrictions on competition in Part 10 are similar to those relating to the disclosure requirements in Part 2 of the Consumer Credit Code. That is, the compliance costs (although not as significant) may act as a barrier to entry for small lessors.

These provisions address the objective of truth in lending in relation to consumer leases, and allow consumers to make informed choices regarding consumer leases. In addition, these provisions also facilitate fair trading outcomes, specifically those of:

- Access to appropriate information to enable informed decisions to be made by participants; and
- Appropriate post-contractual protection for consumers.

25.3 Key issues raised in submissions and consultation

Australian Finance Conference (AFC):

In relation to consumer leases, the AFC has no objections to the PIR's recommendations to require pre-contractual disclosure of consumer lease information (Recommendation 2.14).

25.4 Classification of Restriction 14

Restriction 14 has been classified as a major restriction on the basis that having versus not having this restriction may make a significant difference to the economy and an analysis is required to demonstrate the net benefits of the provisions.

25.5 Reform Options for Restriction 14

The reform options considered most appropriate for Restriction 1 are Option 1 (Status quo) and Option 2 (Amended status quo). These are discussed in turn in the following sections.

Option 3 (Industry deregulation) and Option 4 (Mandatory code of conduct) have been discarded for the reasons previously outlined in Chapter 11.

25.5.1 Option 1 – Status quo / Cost-benefit analysis

These requirements potentially add to the administration costs of lessors and thus potentially to the price for the lease by lessees. However, the disclosure requirements benefit consumers by assisting them to make informed leasing decisions. These provisions address the information asymmetries in the market and the objectives of truth in lending.

In the absence of these disclosure provisions from Part 10 of the Consumer Credit Code, consumers are able to access a wide variety of information sources that detail the fees, charges, terms and conditions associated with consumer lease transactions, albeit from a smaller pool of sources than for other credit contracts as they are a specialised credit product. However, given that concern was had to the ability of consumers to access information for much more common credit products from a larger pool of information providers, it follows that the alternative information sources would be adequate to fully inform lessees.

Thus, the benefits to lessees of having these disclosure provisions within the Consumer Credit Code are:

- Reduced information search costs;
- Lessees are fully informed of their financial commitments; and
- Protection of the general provisions of the Consumer Credit Code.

The Review team was unable to obtain any quantitative data on the use of these disclosure documents by lessees. Nevertheless, it may be assumed that these persons place similar value on these documents as do the debtors identified in Malbon's study. That is, it may be assumed that a significant proportion of lessees read the information provided to them and

that a significant proportion of these persons find this information mostly helpful. If this were the case, it would follow then that this information also influences the decisions of a small, but not insignificant, proportion of lessees.

Lessors incur the cost of preparing, printing, copying and delivering the required lease documentation. These costs may act as barriers to entry for small lenders. However, these provisions also deliver a number of benefits to lessors:

- Lessees may be more confident about entering into a lease, thereby potentially generating lease transactions that otherwise would not have occurred;
- Increase efficiency with regard to business administration; and
- The promotion of flexibility in product development, which allows for competition based on product differentiation.

Governments also face costs in relation to these provisions, namely those associated with administration of the legislation and coordination of national uniformity[44]. However, the government benefits through reduced requests to government consumer agencies for information relating to consumer lease products.

If it is assumed that the results of the Malbon study may be extrapolated to lessees, then it may be concluded that these persons place significant value of the information provided to them under Part 10 of the Consumer Credit Code.

The provisions of Part 10 do add to the compliance costs for lessors, but these costs are ultimately recoverable from the lessees.

Hence, it may be concluded that this restriction provides a net benefit to consumers. Furthermore, it addresses the objective of truth in lending and the fair trading outcome of providing access to appropriate information to enable informed decisions to be made by market participants.

25.5.2 Option 2 – Amended status quo

The review team did not identify any amendments that could be made to the Part 10 disclosure requirements to make them less restrictive on competition, while at the same time meeting the objectives of the Consumer Credit Code and the required fair trading outcomes.

25.6 Post Implementation Review Recommendations

PIR Recommendations 2.14 and 2.15 impact on this restriction through:

[44] See footnote 19.

- Requiring lessors to undertake pre-contractual disclosure with consumers prior to their entering into a consumer lease (Recommendation 2.14); and

- Explicitly linking the consumer lease provisions in the Consumer Credit Code to s.144 of the Consumer Credit Code, which relates to false and misleading representations (Recommendation 2.15).

In both these instances, the recommendations increase the current levels of consumer protection associated with consumer leases, while at the same time imposing minor (if any) costs to the lessors – assuming these lessors are currently operating in a 'best practice' manner. Therefore, while it could appear on face value that these recommendations may be anti-competitive in nature, in real terms they are unlikely to create significant incremental costs to lessors.

In contrast, the benefits to consumers through the strengthening of pre- and post-contractual redress mechanisms for consumer leases are considered to be substantial. Specifically, these recommendations, if implemented, would reduce any reservations consumers may have to utilising consumer leases, over other forms of credit, thereby improving consumer confidence in the process.

25.7 Conclusions

In conclusion, the cost-benefit analysis reveals that no feasible alternative exists by which the objectives of the Consumer Credit Code could remain fully realised.

Therefore, we recommend that the status quo be maintained for this restriction.

26 Restriction 15: Part 10 potential compliance costs

26.1 Introduction

Part 10 of the Consumer Credit Code was identified as also potentially impacting on competition through potential costs associated with legal costs and loss of potential income as a result of a change in contractual obligations, specifically:

- Section 155, which applies s.70 of the Consumer Credit Code to consumer leases. Section 70 allows the court to reopen a credit contract, guarantee or mortgage on the basis that at the time it was entered into or changed, the contract, mortgage or guarantee was unjust.

26.2 Nature of Restriction 15

Section 70 applies to credit contracts generally and has previously been identified as a potential restriction. Hence the same concerns expressed previously also apply here. That is, s.70 potentially:

- Increases costs for lessors, especially administration, legal costs and potential loss of income as a result of a change in contract terms; and
- Cause mainstream lessors to view lease applications more cautiously and more readily refuse finance to high risk and low-income lessees.

As noted previously, the objectives of s.70 are to discourage the practice of 'asset based lending' and provide a redress mechanism for consumers in the event of unjust consumer leases or unjust changes to consumer leases. In addition, this provision also contributes to the following fair trading outcomes:

- Appropriate post-contractual protection for consumers; and
- Provision of redress mechanisms for consumers.

26.3 Key issues raised in submissions and consultation

There were no comments made specifically in relation to this restriction. However, those comments made in relation to Restriction 6 are relevant.

26.4 Classification of Restriction 15

Restriction 15 has been classified as a minor restriction on the basis that having versus not having this restriction makes little difference to the economy. That is, the compliance costs relating to this restriction are incremental to other compliance costs, such as the Part 10

disclosure requirement, and are unlikely to be greater than $1 million per annum in net terms.

Further, this restriction is not a restriction in the purest sense, rather it reflects normal business risk. That is, this risk exists irrespective of whether or not this provision occurs within the Consumer Credit Code. In the absence of these provisions, the lessor who engages in unconscionable, harsh or oppressive behaviour in relation to a consumer lease or a change to such a contract, potentially faces similar redress under common and statute law.

More specifically, consumers can pursue redress under:

- Contract law;
- *Trade Practices Act 1974* (Part IVA); or
- *Contracts Review Act 1980 (NSW)*, from which s.70 is derived.

However, as noted in Ms McGill's written submission, the alternative mechanisms available under common law are narrower in scope than s.70. This is discussed further in the cost-benefit analysis below.

26.5 Reform Options for Restriction 15

The reform options considered most appropriate for Restriction 1 are Option 1 (Status quo) and Option 2 (Amended status quo). These are discussed in turn in the following sections.

Option 3 (Industry deregulation) and Option 4 (Mandatory code of conduct) have been discarded for the reasons previously outlined in Chapter 11.

26.5.1 Option 1 – Status quo / Cost-benefit analysis

These provisions generally benefit consumers in two ways:

- By requiring lessors to consider the lessee's ability to repay (and not just their ability to provide security), consumers are protected from over-committing themselves under a consumer lease; and
- Consumers are protected from unjust or unconscionable consumer lease contract terms.

In the absence of ss. 70 and 72 from the Consumer Credit Code, a consumer could seek redress through:

- Contract law and doctrines of equity;
- *Contracts Review Act 1980 (NSW)*; and

- Part IVA of the *Trade Practices Act 1974*.

However, these mechanisms are generally much narrower in scope than s.70 and are less likely to fulfil the objectives of the Consumer Credit Code than s.70 currently does.

We note that s.51AB of the *Trade Practices Act 1974* and the equivalent sections in the fair trading legislation of each of the States and Territories that deal with unconscionable conduct are similar in scope to s.70 of the Consumer Credit Code, being the operations of lessors are covered under the nominated legislative frameworks.

However, the practicalities of s.70 are such that the specific circumstances by which a consumer lease contract may be reopened appear to be greater than under either the *Trade Practices Act 1974* or fair trading legislation, such as the over-commitment provision (s.70(2)(l)).

These provisions potentially increase costs for lessors, especially administration expenses, legal costs and potential loss of income as a result of a change in contract terms. Furthermore, these provisions may cause mainstream lessors to view lease applications more cautiously and may refuse leases to high risk and/or low income lessees. These potential lessees may then be forced to borrow from high interest lessors.

Governments also face costs in relation to these provisions, namely those associated with administration of the legislation and coordination of national uniformity[45].

26.5.2 Option 2 – Amended status quo

The review team did not identify any amendments that could be made to s.155 to make it less restrictive on competition, while at the same time meeting the objectives of the Consumer Credit Code and the required fair trading outcomes.

26.6 Post Implementation Review Recommendation

PIR Recommendation 2.15 impacts on this restriction through requiring lessors to undertake pre-contractual disclosure with consumers prior to their entering into a consumer lease.

The recommendation increases the current levels of consumer protection associated with consumer leases, while at the same time imposing minor (if any) costs to the lessors – assuming these lessors are currently operating in a 'best practice' manner. Therefore, while it could appear on face value that this recommendation may be anti-competitive in nature, in real terms it is unlikely to create significant incremental costs to lessors.

In contrast, the benefits to consumers through the strengthening of redress mechanisms for consumer leases are considered to be substantial. Specifically, this recommendation, if

[45] See footnote 19.

implemented, would reduce any reservations consumers may have to utilising consumer leases, over other forms of credit, thereby improving consumer confidence in the process.

26.7 Conclusions

In conclusion, while it appears that there are alternative legislative frameworks from which to seek redress from contractual conditions, such as the *Trade Practices Act 1974* and fair trading legislation in each State and Territory, we note that these mechanisms are not as specific as those incorporated within the Consumer Credit Code. Hence, it would be fair to suggest that these alternative legislative frameworks would not be able to fully satisfy the objectives of the Consumer Credit Code, nor the fair trading outcome of appropriate post contractual protection for consumers. Hence, it is recommended that the status quo be maintained for this restriction.

27 Fair trading outcomes

The Terms of Reference requires consideration of the need for the Consumer Credit Code having regard to the following fair trading outcomes:

- Access to appropriate information to enable informed decisions to be made by participants;
- Appropriate post contractual protection for consumers;
- Provision of redress mechanisms for consumers;
- Minimal misleading, deceptive or unconscionable conduct by market participants;
- Minimal restriction on product flexibility and consumer choice; and
- Minimal compliance costs for business.

Each of these fair trading outcomes is considered below.

27.1 The need for the Consumer Credit Code

Fair Trading Outcome 1 Access to appropriate information to enable informed decisions to be made by participants.

The Review has indicated that, in the absence of the Consumer Credit Code, consumers would be able to obtain information on consumer credit products from a number of alternative sources, including infomediaries, printed media and credit providers. However, there is no guarantee that the same level of information would be provided in the absence of the Consumer Credit Code.

The Consumer Credit Code also provides for some uniformity and consistency in the information presented and this may also be lost in the absence of the Consumer Credit Code. Furthermore, not all consumers have equal access to these alternative information sources.

Therefore the Consumer Credit Code is required in order to ensure access to appropriate information to enable informed decision to be made by participants.

Fair Trading Outcome 2 Appropriate post contractual protection for consumers.

The Review has indicated that, in the absence of the Consumer Credit Code, there may be opportunities for credit providers to engage in unjust, harsh or unconscionable conduct, even if the entering into of the credit contract was fair and just. For example, the Consumer Credit Code currently provides consumer protection provisions in the event that:

- The financial position of the debtor changes during the term of the contract, so that they are provided an opportunity to continue with the credit contract; and

- The credit provider imposes a unilateral change to the interest rate, so that the debtor is informed of the change and are able to adjust their credit arrangements accordingly.

These standard post-contractual consumer protection provisions are implied into the credit contract, whereas they may not be included if it were not for the Consumer Credit Code. Hence, the Consumer Credit Code is required in order to provide appropriate post-contractual protection for consumers.

Fair Trading Outcome 3 Provision of redress mechanisms for consumers.

The Review has indicated that, in the absence of appropriate redress mechanisms such as ss.70 and 72 and the civil penalties regime, credit providers would have less incentive to comply with the provisions of the Consumer Credit Code. This could lead to situations whereby, for example:

- Credit providers act unconscionably in inducing debtors to enter into a credit contract;

- Debtors may not be sufficiently informed when purchasing credit, thereby making inappropriate credit choices; and

- Credit providers may impose unreasonable unilateral changes to the credit contract.

In the absence of the Consumer Credit Code, consumers may be able to seek redress for such behaviour on behalf of the credit provider through alternative legislation such as the *Trade Practices Act 1974* or the Fair Trading Acts. However, whereas the Consumer Credit Code is proactive in its application of redress mechanisms, the alternative mechanisms are generally reactive and place the onus on the consumer to make an application. Furthermore, the scope of the alternative legislation is not as extensive.

Therefore, the Consumer Credit Code is required in order to provide effective redress mechanisms for consumers.

Fair Trading Outcome 4 Minimal misleading, deceptive or unconscionable conduct by market participants.

The Review has indicated that, in the absence of the Consumer Credit Code, unscrupulous credit providers may act misleadingly, deceptively or unconscionably in their transactions with debtor. For example:

- Without the protection of s.23(1), credit providers may attempt to provide the loan amount in other than cash or money's worth;

- Without the protection of s.46, credit providers may attempt to create a mortgage over a debtor's remuneration or superannuation benefits; and

- Without the notification provisions of Part 4 of the Consumer Credit Code, credit providers could change credit terms, such as the interest rate, without notifying the debtor.

Hence, the Consumer Credit Code is required to reduce the potential for market participants to engage in misleading, deceptive or unconscionable conduct.

Fair Trading Outcome 5 Minimal restriction on product flexibility and consumer choice.

The Consumer Credit Code currently restricts product flexibility and consumer choice in a number of ways (see discussions on s.23(1) in Chapter X and s.46 in Chapter Y). Hence, it may be argued that there would be greater product flexibility and consumer choice in the absence of the Consumer Credit Code.

However, the benefits of these restrictions should also be taken into consideration. That is, greater product flexibility and consumer choice may not also be in the public interest.

Fair Trading Outcome 6 Minimal compliance costs for business.

The Consumer Credit Code currently imposes compliance costs on credit providers through, for example, the disclosure provisions that credit providers must comply with. Hence, it may be argued that compliance costs would be minimised in the absence of the Consumer Credit Code.

27.2 Summary

In summary, the Consumer Credit Code is required to deliver on the following fair trading outcomes:

- Access to appropriate information to enable informed decisions to be made by participants;
- Appropriate post contractual protection for consumers;
- Provision of redress mechanisms for consumers;
- Minimal misleading, deceptive or unconscionable conduct by market participants;

In contrast, restrictions on product flexibility and consumer choice, and compliance costs would be minimised in the absence of the Consumer Credit Code. However, the benefits associated with these restrictions have been shown to outweigh their costs.

Hence, it may be concluded that overall the Consumer Credit Code is required to deliver the stated fair trading outcomes.

28 Conclusions

Our analysis of the benefits and costs of the Consumer Credit Code has indicated that there are few alternative mechanisms for achieving the stated objectives of the Consumer Credit Code and the required fair trading outcomes than that currently employed.

Option 1, which proposed retaining the status quo, was analysed for each of the identified restrictions. This was found to be the most appropriate reform option for most of the restrictions analysed.

Option 2, which proposed amending specific provisions, was analysed in relation to Restriction 1 (Part 2 Disclosure requirements). It was proposed to reduce and simplify the disclosure requirements of credit contracts. However, it was dismissed on the basis that research conducted during the PIR and this review suggested that the amount of information provided to consumers was not the key issue. Rather, it is the timing and format of the information provided that is the most critical aspect of information disclosure from a consumer's perspective.

In this respect we considered that the PIR recommendations associated with the inclusion of a 'Schumer Box' in the credit contract documentation provided for a better outcome in terms of consumer protection than reform Option 2 for this restriction. That is, the analysis conducted to examine the viability of adopting Option 2 in relation to Restriction 1 (Part 2 Disclosure requirements) in the context of this NCP review actually reinforced the PIR recommendations relating to the inclusion of a 'Schumer Box' in contract documentation.

Option 3, which proposed industry deregulation was discounted on the basis that it does not provide a feasible alternative to the Consumer Credit Code. There are a number of consumer protection provisions that are not necessarily anti-competitive, but which would be lost if the Consumer Credit Code was repealed in its entirity.

Option 4, which proposed industry co-regulation through a mandatory Code of Conduct was discounted on the basis that, as it mirrored the provisions of the Consumer Credit Code, there would be little, if any, net gains for consumers. However, this reform option entailed significant administrative costs for the Commonwealth, State and Territory governments in relation to repealing the existing legislation, developing the Code of Conduct and the appropriate legislation and the transfer of administrative functions from the State and Territory governments to the AFIC.

In conclusion, the key recommendations of this review are:

1. Maintain the current provisions of the Consumer Credit Code and, as per the PIR, review the definitions of the Consumer Credit Code to ensure that terms sale of land, conditional sale agreements, tiny terms contracts and solicitor lending are bought within the scope of the Consumer Credit Code; and

2. Adopt PIR Recommendation 1.1 in order to enhance the disclosure provisions within Part 2 of the Consumer Credit Code.

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Glossary of terms

The following glossary was compiled using sources previously identified in the report, as well as *eLoan* (http://www.eloan.com.au), *Choice* (http://www.choice.com.au) and *Your Mortgage* (http://www.yourmortgage.com.au).

All-in-one loan — A variable rate *housing loan* that allows you to deposit all of your income into the loan account and then withdraw money from the loan account for all your day-to-day purchases and transactions. The longer spare funds stay in the account, the greater the interest savings.

Amortisation — The progressive reduction of the outstanding amount of a loan by regular payments that include a principal and interest component.

Application fees — Fees charged by a credit provider to partially or full cover the credit provider's internal costs of setting up the loan approval for the debtor.

Bank bill rate — An index rate that is used to determine interest rate changes for some variable rate housing loans.

Basic variable rate housing loan — A *housing loan* that has a lower *variable interest rate* than a *standard variable rate housing loan*, but which has fewer features. That is, there is generally no *offset facility* or *redraw facility*.

Capped interest rate — An interest rate that can fall but not rise above a stated rate (the cap). Most frequently offered as a honeymoon rate for first home buyers.

Collateral — An asset (such as a car or home) mortgaged to a credit provider to secure the repayment of a loan.

Collared rate — A variable rate with a set upper and lower limit beyond which the interest rate cannot move past.

Construction loan — A housing loan for financing the cost of construction. The borrower draws down the loan periodically (rather than in one lump sum) to make payments to the builder and usually only makes interest payments while the house is built. Once the construction is completed, repayments comprise both principal and interest.

Consumer lease — A contract for the hire of goods under which the lessee does not have a right or obligation to purchase the goods.

See also: *Finance lease.*

Credit card — Form of *revolving credit* whereby authority is given to borrow up to a set limit and any repayments (other than of charges and interest) made reduce the extent on the borrowing and increase the amount of unused credit available (ABS 1999).

Credit cards may have an interest-free period (up to 55 days) and / or a loyalty or other reward program (such as Frequent Flyers).

Early termination fees — Fees associated with paying out a loan in full early or before the term is up. May also be referred to as a prepayment fee.

Equity The difference between the fair market value of the property and the amount still owing on any debts secured by a mortgage of the property. It is the home owner's financial interest in the property.

Equity loans A loan secured by the equity a debtor has in their property. Also referred to as an equity mortgage.

Finance lease The leasing or hiring of tangible assets under an agreement, other than a hire-purchase agreement, which transfers from the lessor to the lessee substantially all the risks and benefits incident to ownership without transferring legal ownership (ABS 1999). Leases are often taken out on cars.

See also: *Consumer lease.*

First mortgage A mortgage that gives the holder of the mortgage (the mortgagee) first claim on the proceeds of the sale of the property.

Fixed costs Costs which do not vary with the size of the loan, and may include establishment, annual, transaction and application fees.

Fixed interest rate An interest rate which is fixed for an agreed term.

Fixed loan A credit facility generally having the following characteristics:

- a commitment for a fixed amount for a fixed (maximum) term for a specified purpose;
- a schedule of repayments over a fixed period; and
- repayments which reduce the liability of the borrower but do not act to make further finance available.

Fixed rate housing loan A *housing loan* with a *fixed interest rate* (usually for 1 to 10 years), after which a new fixed interest rate may be set or a variable interest rate applied. Exit penalties are usually higher than under *variable rate housing loans*. Additional repayments usually attract a penalty.

Goods lease A contract for the hire of goods under which the hirer has a right or obligation to purchase the goods where the charge that is made for hiring the goods, together with any other amount payable under the contract, exceeds the cash price of the goods.

See also: *Hire-purchase agreement*

Guarantee A collateral contract to answer for the debt or default of another.

Guarantor A party who agrees to be held responsible for the payment of another party's debt (in the event of a default).

Hire-purchase agreement Traditionally defined as an agreement for the letting of goods under which there is an option to buy, but also includes a conditional sale agreement where possession of the goods is given to the hirer and there is agreement to buy, but the property in the goods is not to pass until all instalments of the purchase price have been paid (McGill & Willmott 1999).

See also: *Goods lease*

Home equity loan A loan secured by a first mortgage on the debtor's home, which is generally only available to debtors with a high level of equity in their home. Unlike a line of credit attached to a mortgage, a home equity loan is a one-off loan. The repayment schedule is generally flexible.

Honeymoon rate housing loan A housing loan with a low interest rate (usually only for the first year), which then converts to a *variable interest rate*. The honeymoon rate may be a *fixed interest rate* or a *capped interest rate*.

Also referred to as an introductory loan.

Housing loan Finance to individuals for purchase or construction of dwellings for owner occupation, and for alterations and additions to existing owner-occupied dwellings (ABS 1999). This form of credit is generally secured (usually by the property being purchased) and for a maximum term (usually up to 30 years). Interest may be variable or fixed, or a combination of both.

See also: *All-in-one loan, Basic variable rate housing loan, Construction Loan Fixed rate housing loan, Honeymoon rate housing loan, Split rate housing loan, Standard variable rate housing loan*

Interest What the credit provider charges the debtor for the use of the money lent.

Interest rate The rate of *interest* on a loan, expressed as a percentage per annum.

Line of credit A form of *revolving credit*, which is usually secured by a mortgage over a residential property. .

Linked credit Finance to consumers provided on behalf of a linked credit provider via a supplier (who supplies the goods to which the credit applies). Linked credit is often offered on loans for major household purchases such as furniture, whitegoods, car tyres and computers. This type of credit often has an interest free period (of up to 30 months), after which a variable interest rate applies (usually higher relative to other credit). Linked credit provided by a finance company is often essentially a *credit card.*

Mortgage A legal document that gives a credit provider an interest in a security property and allows the credit provider to sell the property if the loan is not repaid.

Offset facility A savings account run in conjunction with a housing loan. The interest 'earned' on the account is applied to the interest paid on the loan to reduce the interest payable on the housing loan. A 100% offset is where the interest rates earned and paid are the same. A partial offset account is where the interest rate earned on the offset account is only a portion of the rate paid on the housing loan.

Overdraft A facility attached to a deposit account which allow funds to be drawn in excess of the balance available. The amount of any negative balance is the credit provided. Overdrafts may be secured or unsecured, and generally have a variable interest rate.

Personal loan Finance provided to individuals for their personal, non-business use. Generally used for purchases of consumable goods such as cars, whitegoods and computers. Personal loans may be secured or unsecured (which attracts a higher interest rate), and generally have terms up to 7 years

Principal Amount of debt, not including interest.

Redraw facility A loan facility whereby you can make additional repayments on your loan and then access these extra funds when necessary. Usually only available with a *standard variable rate housing loan*.

Revolving credit A credit facility generally having the following characteristics (ABS 1999):

- a commitment for a credit or borrowing limit is given for a specific period after which the commitment is reviewed;
- the extent of the borrowing used at any time during the period may be for any amount up to the authorised limit; and
- repayments (other than of charges and interest) made during the period reduce the extent of the borrowing used and thereby increase the amount of unused credit available up to the authorised limit.

Examples include credit cards, lines of credit and approved overdrafts. The Consumer Credit Code refers to revolving credit as 'continuing credit'.

Secured credit Confers to the credit provider rights by contract over property in the event of default by the customer. The security may be over the property acquired with the credit, or it may be given over other property belonging to the debtor. The main classes of securitisation are the mortgage and the guarantee. Housing loans are commonly secured credit.

Securitisation The process of taking a pool of diverse assets such as different home loans and converting them into a tradeable security, such as a bond, which investors can then purchase and trade.

Split rate housing loan A housing loan where part of the loan is treated as fixed rate housing loan and the other part is treated as a variable rate housing loan.

Standard variable rate housing loan A *housing loan* with a maximum term (usually 30 years), regular repayments and a variable interest rate. This type of credit generally has more features than a *basic variable rate housing loan*, and may include a *redraw facility* and an option to switch to a fixed interest rate for a period of time. Additional payments usually do not incur any penalties.

Term The period over which the loan is to be repaid. The maximum length of the term varies with the type of credit, and may be up to 30 years for a housing loan. Revolving credit does not have a term.

Unsecured credit No collateral is offered on the loan. This increases credit risk and the premium on interest rates.

Variable costs Costs that vary with the size of the loan, usually in the form of interest rates.

Variable interest rate An interest rate that may change over time. The rate is usually set relative to a reference rate.

Appendix A – Overview of the Consumer Credit Code

Part 1 – Preliminary

Part 1 of the Consumer Credit Code sets out the scope of the legislation, in particular:

- Short title and commencement;
- Interpretation;
- Scope; and
- Presumptions relating to the application of the Consumer Credit Code.

The short tile (s.1) and commencement (s.2) are self-explanatory, and the scope of the legislation (ss.4 – 10) has been discussed in detail previously.

Section 3 states that the principal definitions of words and expressions used in the Consumer Credit Code are provided in Schedule 1 and other miscellaneous provisions relating to interpretation of the Consumer Credit Code are provided in Schedule 2. The definitions provided in both Schedule 1 and 2 are not universal, and their application may be displaced by a contrary indication in the Consumer Credit Code (McGill & Willmott 1999).

Section 11 sets out the presumptions relating to the application of the Consumer Credit Code to credit contracts. The key provision within this section is 11(2), which states:

> *Credit is presumed conclusively for the purposes of this Code not to be provided wholly or predominantly for personal, domestic or household purposes if the debtor declares, before entering into the credit contract, that the credit is to be applied wholly or predominantly for business or investment purposes (or for both purposes).*

Furthermore, this declaration must be substantially in the form specified in s.10 of the Regulation.

Part 2 – Credit contracts

Part 2 of the Consumer Credit Code outlines key provisions governing contract formation and formalities, in particular:

- The form and content of the credit documentation;
- Pre-contractual disclosure requirements;
- The debtor's right of termination;
- Acceptance of early payments;
- Application of interest charges;
- Restrictions on fees and charges; and
- Frequency and content of periodic statements of account.

Section 14 governs pre-contractual disclosure and requires that, prior to entering into a credit contract, the debtor be provided with a pre-contractual statement setting out the matters required by s.15 to be included in contract document, as well as an information statement of the debtor's rights and obligations. Furthermore, s.13 of the Regulation requires 'relevant financial information' to be set out separately in the pre-contractual statement in a financial table. Through the pre-contractual statement, the debtor is provided with all the relevant financial information before entering into the credit contract.

Section 15 sets out the information that must be included in the credit contract, including:

(a) Credit provider's name;

(b) Amount of credit;

(c) Annual percentage rate;

(d) Calculation of interest charges;

(e) Total amount of interest charges payable;

(f) Repayments;

(g) Credit fees and charges;

(h) Changes affecting interest and credit fees and charges;

(i) Statement of account;

(j) Default rate;

(k) Enforcement expenses;

(l) Mortgage or guarantee;

(m) Commission;

(n) Insurance financed by contract; and

(o) Other information.

Many of these requirements are 'key requirements' under s.100 (Part 6) of the Consumer Credit Code, reflecting the importance of information closure to consumers (McGill & Willmott 1999). Part 6 deals with civil penalties for breaches of a serious nature, such as breaches of 'key requirements'.

Section 18 requires the credit provider to provide to the debtor a copy of the credit contract. This is consistent generally with consumer protection legislation (McGill & Willmott 1999).

Section 19 allows a debtor to terminate a credit contract provided that no credit has been obtained under the contract and the interests of the credit provider are not prejudiced (McGill & Willmott 1999). This provision provides the debtor with a 'cooling off' period.

Section 24 requires a credit provider to accept early payments (unless the credit contract prohibits its early payment) and credit each payment made under a credit contract as soon as is practical after the receipt of the payment.

Section 26 sets out the maximum interest charge that may be imposed under a credit contract. This section of the Consumer Credit Code itself does not specify a maximum rate, but rather sets out a formula that provides the maximum interest charge which may be imposed given the annual percentage rate in the credit contract (McGill & Willmott 1999).

Section 27 prohibits a credit provider from charging interest in advance.

Section 29 provides that the regulations may specify certain classes of credit fees and charges that are prohibited; however, the regulations currently do not specify any such credit fees or charges.

Sections 31 to 36 govern the credit provider's obligation to account to the debtor, namely:

- The credit provider is required to provide the debtor with a periodic statement of accounts containing details of the account;
- The credit provider is obliged, upon request of the debtor, to provide the debtor with a statement containing various matters as set out in the Consumer Credit Code; and
- Formalities for dealing with disputed accounts (McGill & Willmott 1999).

Periodic statements of account are not required for fixed interest rate credit contracts.

Part 3 – Related mortgages and guarantees

Part 3 of the Consumer Credit Code outlines additional provisions governing contract formation and formalities relating specifically to mortgages and guarantees, in particular:

- Form of and content of mortgage documentation;
- Copies of mortgage documentation to be provided to mortgagor;
- Amount that may be secured;
- Prohibited securities;
- Process for assignment or disposal of mortgaged property;
- Form of guarantee documentation; and
- Copy of credit contract to be provided to guarantor.

Section 39 requires the credit provider to provide the mortgagor with a copy of the mortgage documentation. Again, this would be expected under any consumer protection legislation.

Section 40(1) sets out the content of the mortgage documentation by rendering void any mortgage which does not describe or identify the property to which the mortgage applies, while **s.40(2)** renders void a provision in a mortgage that charges all property of the mortgagor. The latter provision prevents the credit provider taking a blanket security over all the property of the mortgagor (McGill & Willmott 1999).

Section 41 renders void any provision in the mortgage that creates a mortgage over property that the mortgagor is to, or may, acquire in the future (with the obvious exception of the case where the property is to be acquired with the credit provided). McGill & Willmott (1999) note that this provisions protects the mortgagor by restricting the extent to which property acquired in the future will become part of the property to which the mortgage applies.

Section 44 prohibits third party mortgages, so that a credit provider may not enter into a mortgage to secure obligations under a credit contract unless each mortgagor is a debtor

under the contract or a guarantor under a related guarantee. This provision protects a person from providing a mortgage without being fully appraised of the implications of doing so (McGill & Willmott 1999).

Section 45 specifies the maximum amount which may be secured under a mortgage, namely the amount of any liabilities of the debtor under the credit contract plus the reasonable enforcement expenses of enforcing the mortgage.

Section 46 states that a mortgage may not be created over employees' remuneration or employment benefits or benefits under a superannuation scheme, nor may an obligation under a credit contract be secured by a cheque, bill of exchange or promissory note, where this is endorsed by the debtor or guarantor.

Section 47 allows the mortgagor to assign or dispose of the property that is subject to the mortgage subject to the credit provider's or court's approval. The credit provider may impose conditions on such an assignment or disposal, such as payment of reasonable costs, as outlined in **s.48**.

Section 51 requires that a copy of the credit contract documentation and a document outlining the rights and obligations of the guarantor be provided to the guarantor prior to any obligations under the credit contract being secured by the guarantee.

Section 53 allows the guarantor to withdraw any time before the credit is first provided under the credit contract, or after the credit is first provided if the credit contract made differs materially from that disclosed under s.51. McGill & Willmott (1999) note that, if the guarantor withdraws before the credit is first provided, the guarantor does not need to have a specific reason for wishing to withdraw.

Section 55 specifies the maximum amount which may be secured under a guarantee, namely the amount of any liabilities of the debtor under the credit contract plus the reasonable enforcement expenses of enforcing the mortgage.

Part 4 – Changes to obligations under credit contracts, mortgages and guarantees

Part 4 of Code is concerned with changes to obligations under credit contracts, mortgages and guarantees. It deals separately with changes made:

- Unilaterally by the credit provider (Division 1);
- By mutual agreement of the parties to the credit contract (Division 2); and
- Changes made on account of hardships and unjust transactions (Division 3).

Section 58 limits the application of Division 1 to changes made unilaterally by the credit provider, and to changes which are not ascertainable from the credit contract and which do not fall under Division 3.

Sections 59, 60, 61 and 63 set out the formalities for notifying debtors of unilateral changes relating to interest rates, repayments, credit fees and charges and other changes, respectively. The credit provider is generally required to provide notice of such unilateral changes before or on the day the change takes effect. However, where these changes reduce the debtor's obligations under the credit contract or extends the time for payments, the credit provider is only required to advise of such a change before or when the next statement of account is sent to the debtor.

Section 65 sets out the notification procedures for changes made by agreement between all parties to the credit contract. With the exception of changes that reduce the obligations of the debtor under the credit contract or changes to the amount of credit provided under the credit contract, the procedures are the same irrespective of the type of change. This is the only section dealing with changes made by agreement of the parties to the credit contract.

Section 66(1) states:

> *A debtor who is unable reasonably, because of illness, unemployment or other reasonable cause, to meet the debtor's obligations under a credit contract and who reasonably expects to be able to discharge the debtor's obligations if the terms of the contract were changed in a manner set out in subsection (2) may apply to the credit provider for such a change.*

The types of changes allowed under s.66(2) are:

- Extension of the period of the contract, with the amount of each payment reduced;
- Postponement during a specified period the dates on which payments are due; and
- Extension of the period of the contract and postponement during a specified period the dates on which payments are due.

Section 67 requires that a written notice setting out the particulars of the change be provided to the debtor and guarantor (if applicable) by the credit provider within 30 days after the date of the agreement.

Section 68 allows the debtor to apply to the courts if the credit provider does not change the credit contract in accordance with the application. If credit contract is changed by an order under s.68, the credit provider may then apply (under s.69) to the courts to for an order varying or revoking the order.

Section 70(1) allows the court to reopen transactions giving rise to a contract, mortgage or guarantee or a change to such, if satisfied that, in the circumstances when it was entered into or changed, it was unjust. **Section 70(2)** sets out the matters the court is to take into consideration when determining whether a contract, mortgage or guarantee was unjust.

Section 72 allows the court to review unconscionable changes to the annual percentage rate, establishment fee or charge, termination fees and charges and prepayment credit fees and charges. Furthermore, the court may annul or reduce the change or fee or charge and make ancillary or consequential orders.

Part 5 – Ending and enforcing credit contracts, mortgages and guarantees

Part 5 of the Consumer Credit Code deals with ending and enforcing credit contracts, mortgages and guarantees, in particular:

- Ending of credit contract by debtor (Division 1: ss.75 – 79);
- Enforcement of credit contracts, mortgages and guarantees (Division 2: ss.80 – 85);
- Postponement of enforcement proceedings (Division 3: ss.86 – 89);
- Enforcement procedures for goods mortgaged (Division 4: ss.90 – 98); and
- Enforcement Expenses (Division 5: s.99).

Section 75 entitles a debtor or guarantor to pay out the credit contract at any time and sets out the amounts which may make up the pay out figure.

Section 76 requires that a written statement detailing the amount required to pay out a credit contract must be provided to the debtor (upon request from the debtor) within 7 days of the request. Alternatively, the courts may determine the amount payable if the credit provider does not provide such a statement (s.77).

Section 78 sets out the formalities to be followed by a credit provider and a debtor where the debtor wishes to return, and have the credit provider sell, goods bought under a sale of goods by instalments or subject to a mortgage (McGill & Willmott 1999). This section provides a means for the debtor or mortgagor to initiate a termination of a credit contract and mortgage of goods and is offered as an alternative to s.75.

Section 80 sets out the formalities that must be followed by the credit provider before enforcement procedures may be commenced against the defaulting debtor or mortgagor. The credit provider must provide the debtor with a default notice outlining the default and the action necessary to remedy the breach.

Section 82 sets out the formalities that must be followed by a credit provider before the credit provider can enforce a guarantee against the guarantor. There is no requirement to provide a default notice first, as this would have been provided to the guarantor under s.80.

Section 83 prohibits the credit provider from taking possession of mortgaged goods if the amount currently owing under the credit contract is less than 25% of the amount of credit provided under the contract or $10,000, whichever is the lesser. Circumstance under which this provision does not apply includes where court approval has been obtained, urgent action is required to protect the goods and continuing credit contracts.

Section 85 sets out the conditions under which a credit provider may enforce an ‘acceleration clause’, which provides that, under certain circumstance, the credit provider becomes entitled to immediate payment of all, or part, of an amount that would otherwise not be immediately payable.

Section 86 entitles a debtor, mortgagor or guarantor, who has been provided with a default notice, to negotiate with the credit provider for a postponement of the enforcement proceeding or application of any acceleration clause. McGill & Willmott (1999) note that this provision is meaningless by itself, as the parties to the contract are always free to negotiate.

If the credit provider does not grant a postponement, the debtor, mortgagor or guarantor may apply to the courts under **s.88** for such a postponement. Under s.89, the credit provider may apply to the courts for variation of the order.

Sections 91 and 92 set out the conditions under which the credit provider may enter residential property for the purpose of taking possession of mortgaged goods. Alternatively, the credit provider may apply to the courts under **s.93** for a court order requiring the person who is in possession of the mortgaged goods to deliver those goods to the credit provider.

Section 94 sets out the procedures to be followed by the credit provider after taking possession of the mortgaged goods. The credit provider must give the mortgagor a written notice outlining the estimated value of the goods, the enforcement expenses incurred and a statement of the mortgagor's rights and obligations. Furthermore, the credit provider must not dispose of the goods within 21 days of that notice, so as to allow the mortgagor an opportunity to rectify the default.

Section 96 requires the credit provider to sell the goods, as soon as is reasonably practical after the 21 day period has passed, to either the buyer nominated by the mortgagor under s.95 or for the best price reasonably attainable. The credit provider must provide written notice to the mortgagor of the details of the sale, as well as the balance of the proceeds of the sale after allowable deductions. These allowable deductions are set out in s.97:

- The amount required to discharge the related credit contract;
- The amount payable to discharge any prior and subsequent mortgages to which the goods were subject; and
- The credit provider's reasonable enforcement expenses.

Section 98 allows the mortgagor to apply to the court for an order that the credit provider credit the mortgagor with a payment, exceeding the net proceeds of the sale, if the court is not satisfied that the credit provider sold the goods as soon as reasonably practical for the best price reasonably obtainable. This may apply for any previous or subsequent mortgages also.

Section 99 prohibits a credit provider from recovering, or seeking to recover, enforcement expenses in excess of those reasonably incurred by the credit provider.

Part 6 – Civil penalties for defaults of credit providers

Part 6 of the Consumer Credit Code establishes the civil penalty regime and other remedies for breaches of the Consumer Credit Code by credit providers. The provisions within Part 6 are divided into two divisions:

- Division 1 deals with contraventions of 'key requirements'; and
- Division 2 deals with other contraventions.

Sections 100 sets out those provisions within the Consumer Credit Code that are 'key requirements'. These key requirements cover most of the provisions within s.15 (matters that must be in a credit contract), as well as s.21(1) (prohibited monetary obligations), s.32(E) (information to be contained in the statement of accounts) and s.33 (opening balance not to exceed closing balance). McGill & Willmott (1999) note that these provisions are fundamental to the underlying policy objective of the legislation, namely information disclosure.

Section 102 states that the court must, on an application being made under s.101 by a party to the credit contract, guarantor or Government Consumer Agency, by order declare whether or not the credit provider has contravened a key requirement. Furthermore, the court may make an order requiring the credit provider to pay a civil penalty. In doing so, the court must take into consideration the matters set out in s.102.

Sections 103 to 107 identify the maximum civil penalties associated with contravening a key requirement of a credit contract. That is, a credit provider who contravenes a key requirement of the Consumer Credit Code faces a number of possible sanctions, including:

- Loss of interest charges under the contract;
- A maximum civil penalty (or fine) of up to $500,000 per contravention; and
- Compensation to borrowers who have suffered as a result of the error.

The maximum civil penalty that may be imposed depends on which party makes the application. Where the application is made by the debtor or a guarantor, the maximum civil penalty that may be imposed is an amount equivalent to interest charges payable under the contract, or the debtor's loss resulting from the contravention, whichever is the greater. On the other hand, where the application is made by the credit provider or a Government Consumer Agency, the maximum civil penalty should not exceed $500,000.

Furthermore, a civil penalty order made on the application of the credit provider or Government Consumer Agency does not prevent a debtor or guarantor from applying for compensation in respect of loss suffered as a result of the contravention.

Section 108 allows a credit provider or Government Consumer Agency to register with the court of one jurisdiction an order made by a court in another jurisdiction. The purpose of this is to introduce a single system for the determination of civil penalty applications Australia-wide (ibid, pp.430, 431). However, the court may refuse to register the order if it believes it is more appropriate for the application to be heard in another jurisdiction.

Section 114 (Division 2) provides that a credit provider who breaches one of the other requirements of the Consumer Credit Code faces sanctions in the form of compensation to borrowers who have suffered as a result of the breach.

Part 7 – Related sale contracts

Part 7 of the Consumer Credit Code deals with related sale contracts and linked credit providers, in particular:

- Interpretation and application (Division 1: ss.115 – 117);
- Liability of credit providers for suppliers' misrepresentations (Division 2: s.118);
- Liability of credit providers in relation to goods (Division 3: ss.119 – 123);
- Termination of related transactions (Division 4: ss.124 – 131); and
- Other provisions (Division 5: ss.130 – 131).

A 'linked credit provider' is defined in **s.117** of the Consumer Credit Code and is a credit provider who has an arrangement with a supplier of goods such that the supplier refers consumers to the credit provider, or the supplier signs customers up for the credit provider. For example, a consumer purchasing a television from a major retailer on credit or interest free will typically be provided credit with a finance company. In this example, the finance company is the linked credit provider.

Section 118 makes a linked credit provider liable to a debtor for any representations, warranties or statements made by the supplier. However, the credit provider is entitled to be indemnified by the person who made the representation, warranty or statement against any damage suffered by the credit provider through the operation of this section.

Section 119 makes the supplier and linked credit provider jointly and severally liable to the debtor for loss or damage suffered by the debtor as a result of misrepresentation, breach of contract or failure of consideration in relation to the contract. However, the credit provider is not liable to the debtor if the circumstances set out in s.119(2) are satisfied.

Sections 120 is concerned with limits on debtor's right of action against the linked credit provider, specifically:

- The debtor may offset the credit provider's liability against the debtor's liability;
- Proceedings must be against both the supplier and linked credit provider;
- The credit provider's liability is limited to the amount of credit, interests and costs awarded by the court; and
- A judgement may not be enforced against a credit provider unless attempts have been made to enforce it against the supplier.

Division 4 deals with termination of related credit and sale contracts and the rights and obligations of the debtor, supplier and credit provider in relation to such a termination.

Section 124 gives the debtor the right to terminate the sale contract if the debtor is unable to obtain the credit required to purchase the goods, while **s.125** entitles the debtor to terminate the credit contract if the sale contract is rescinded or discharged.

Section 130 prohibits a supplier from requiring the buyer to apply for, or obtain, credit from a particular credit provider.

Section 131 prohibits a supplier from demanding or accepting, as payment from the buyer, a postdated bill of exchange or promissory note if the face value of the bill or note exceeds the cash price of the goods or services. This provision aims to prevent suppliers from providing credit to purchasers, thereby benefiting from the interest, without being subject to the all the provisions of the Consumer Credit Code (McGill & Willmott 1999).

Part 8 – Related insurance contracts

Part 8 of the Consumer Credit Code is concerned with related insurance contracts, in particular:

- Formalities relating to the taking out of insurance;
- Financing of insurance premiums over mortgaged property;
- Commissions for consumer credit insurance;
- Formalities for dealing with a rejection of a proposal for insurance; and
- Termination of a credit related insurance contract if the credit contract is terminated.

Part 8 does not apply to all private insurance financed under a credit contract; rather, it applies only to a 'credit-related insurance contract', which is defined in s.132 of the Consumer Credit Code as:

> *"… a contract for insurance of any of the following kinds in connection in connection with a credit contract-*
>
> *(a) insurance over mortgaged property;*
>
> *(b) consumer credit insurance;*
>
> *(c) insurance of a nature prescribed for the purposes of this section by the regulations.'*

Furthermore, the Consumer Credit Code only applies where the insurance contract insures the obligations of the debtor under the credit contract.

Section 133 prohibits a credit provider from requiring a debtor to take out insurance unless that insurance is compulsory insurance (ie personal injury insurance), mortgage indemnity insurance, insurance over mortgaged property or another form of approved insurance. Furthermore, a debtor may not be required to take out insurance with a particular insurer (s.133(2)(a)), or to take out insurance under unreasonable terms (s.133(2)(b)). Section 133(2)(a) is consistent with s.47 of the *Trade Practices Act 1974*, which prohibits the practice of exclusive dealing (McGill & Willmott 1999).

Section 134 prohibits a credit provider from knowingly providing credit to the debtor to finance insurance taken out by the debtor over the mortgaged property for a period of insurance exceeding one year. Furthermore, any such premium may not be debited from the debtor's account more than 30 days before the beginning of the period to which the insurance applies. This provisions prevents the credit provider from benefiting from the interest accruing from the beginning of the contract on amounts of insurance premiums not due until after one year (McGill & Willmott 1999).

Section 135 limits the amount of commission that may be accepted by the credit provider or supplier (in the case of a linked credit contract) to 20% of the premium (excluding government charges).

Sections 138 and 139 govern the formalities for termination of consumer credit insurance and insurance over mortgaged property if the credit contract is terminated. Specifically, the insurance contract is terminated upon the termination of the credit contract and the debtor is entitled to a proportionate rebate of the insurance premium, where the rebate is calculated in accordance with the method outlined in the regulation.

Part 9 – Advertising and related conduct

Part 9 of the Consumer Credit Code regulates credit advertising and related conduct involving the promotion of credit, in particular:

- Appropriate content for advertisements;
- Persons liable for advertisements (for redress purposes);
- False or misleading representations; and
- Harassment and canvassing of credit at a person's home.

Section 140 prohibits advertising of credit unless the advertisement complies with the provisions set out in this section. In particular, no statement of interest charges or costs may be included unless it is the annual percentage rate, the comparison rate and/or a statement to the effect that other fees and charges are payable. This is further reinforced by **s.143**, which states that a person must not disclose an interest rate unless it is the annual percentage rate or the comparison rate.

Section 144 prohibits the making of false or misleading statements in relation to a matter that is material to entry into a credit contract or a related transaction or in attempting to induce another person to enter into a credit contract. McGill & Willmott (1999) point out that this provision is not limited to false or misleading statements by the credit provider, but also to such statements made by debtor, guarantors and suppliers.

Section 145 prohibits harassment by a credit provider or supplier to induce a person to apply for credit or enter into a credit contract or a related transaction. Furthermore, **s.146** prohibits a credit provider from visiting at residential premises for the purpose of inducing a resident to apply for obtain credit, except by prior arrangement.

Part 10 – Consumer leases

Part 10 of the Consumer Credit Code governs consumer leases, in particular:

- Interpretation and application (Division 1: ss.147 – 150);
- Form an content of consumer lease (Division 2: ss.151 – 154); and
- Other provisions (Division 3: ss.155 – 157).

The objective of Part 10 is to discourage the use of consumer finance leases as a way of avoiding regulation, although the consumer lease provisions in Part 10 have been identified as being significantly less stringent than the consumer credit provisions within the Consumer Credit Code.

Section 147 of the Consumer Credit Code defines a 'consumer lease' as

> *'... a contract for the hire of goods by a natural person or strata corporation under which that person or corporation does not have a right or obligation to purchase the goods'.*

This contrasts to a goods lease (s.10) where there is a right or obligation to purchase the goods.

Section 148 limits the application of Part 10 to consumer leases where the goods are hired wholly or predominantly for personal, domestic or household purposes, and the total charge under the consumer lease exceeds the cash price of the goods. **Section 149** specifically excludes short term or indefinite period and employment related leases from application of Part 10 of the Consumer Credit Code.

Section 150 sets out the presumptions relating to the application of the Consumer Credit Code to credit contracts. This is similar to s.11, in that it allows the lessee to make a declaration that the goods to which the lease apply are not to be hired wholly or predominantly for personal, domestic or household purposes. This protects protect the credit provider where the consumer lease appears to be primarily for business purposes, but where the lessor may not be certain that it is so (McGill & Willmott 1999).

Section 152 sets out the disclosure requirements for consumer leases. Matters that must be disclosed include:

- Description of the goods;
- Amount of consideration to be provided by the lessee before delivery of the goods;
- Stamp duty and other government charges payable under the lease;
- Description of any other charges not included in the rental payable;
- Amount of each rental payment to be made by the lessee and due dates for payments;
- Total number of payments and total amount of rental payable;
- Statement of conditions under which the lease may be terminated; and

- Statement of liabilities of the lessee on termination of the lease.

Section 155 sets out the other provisions in the Consumer Credit Code that apply to consumer leases, including:

- Division 3 of Part 4, which governs changes to contracts on the grounds of hardship and unjust transactions);
- Sections 90 to 93, which governs formalities relating to repossession of goods); and
- Part 11, which governs miscellaneous provisions.

Section 156 requires the lessor to provide written notice of an intention to take possession of goods subject to the lease. This notice must be given 30 days prior to exercising any such rights in order to provide the lessee with an opportunity to rectify the default. However this 30 day period may be waived under certain circumstances, such as the expiry of the lease and lessee insolvency.

Alternatively, **s.157** allows the lessee to return the goods at any time before the end of a consumer lease, and thus end the consumer lease. However, the lessee may be required to pay an amount upon termination as set out in the consumer lease.

Part 11 – Miscellaneous

Part 11 of the Consumer Credit Code outlines additional general provisions relating to consumer credit, and deals separately with:

- Tolerances and assumptions relating to disclosures (Division 1: ss.158 – 160);
- Documentary provisions (Division 2: ss.161 – 164);
- General provisions (Division 3: ss.165 – 177); and
- Provisions relating to offences (Division 4: ss.178 – 184).

Section 158 sets out the tolerances and assumptions relating to the disclosure requirements of the Consumer Credit Code. McGill & Willmott (1999) note that these provisions assist credit providers to comply with the disclosure requirements, especially pre-contractual requirements.

Section 161 requires that any notices under the Consumer Credit Code must comply with the requirements set out in the regulations and reiterates that these notices must be in writing. Furthermore, **s.162** requires that a credit contract, guarantee or notice given under the Consumer Credit Code must be easily legible, not less than 10 point font and clearly expressed.

Section 163 requires a credit provides to provide, upon written request of a debtor, mortgagor or guarantor, a copy of any credit contracts or credit related documentation, including notices to the debtor, mortgagor or guarantor.

Sections 166 and 167 deal with the effects of an assignment of the rights and obligations under the credit contract, mortgage or guarantee by the credit provider, debtor, mortgagor or guarantor.

Sections 172 and 173 set out formalities dealing with the delivery of notices and other documents. Specifically, it sets out the conditions under which a notice or other document will be deemed to be provided and the date on which the notice or other document is provided.

Section 169 protects the rights of the consumer by nullifying any provisions within a contract which seeks to avoid or modify the effect of the Consumer Credit Code.

Section 176 deals with the conduct of agents of the credit provider and other related matters, specifically:

- The conduct of an officer, agent or employee of the credit provider will be imputed to the credit provider and taken to be the conduct of the credit provider; and
- A person may not authorise a credit provider, or a person associated with the credit provider, to enter into a contract, mortgage or guarantee on the person's behalf.

Section 177 provides for the regulations to give effect to any cross-vesting scheme whereby the administrative and judicial powers conferred by the Consumer Credit Code may be exercised by the administrative and judicial authorities of any other jurisdiction.

Section 178 reiterates that a penalty specified within the Consumer Credit Code is punishable on conviction by a penalty, up to the maximum penalty specified. Where this penalty is stipulated in penalty units, each penalty unit is equivalent to $100 (s.179).

Section 182 states that a person who aids, abets, counsels or procures an offence against the Consumer Credit Code or the regulations is taken to have committed that offence and is liability to the penalty for the offence. Furthermore, a person who attempts to commit an offence is punishable as if the offence had been committed.

Appendix B – Legislation by jurisdiction

This appendix contains two tables:

- Table B1, which outlines the differences between jurisdictions in the administration of the Consumer Credit Code and general differences in their regulatory approaches; and

- Table B2, which details the differences between the template Consumer Credit Code and the alternative consistent legislation adopted in Western Australia.

Table B1. Consumer Credit Legislation and Administration, by State / Territory				
State	**Legislation**	**Administrative Agency**	**Court**[a]	**Key variations**[b]
Queensland	Consumer Credit (Queensland) Act 1994	Office of Fair Trading	Courts (jurisdiction determined by monetary limit) Small Claims Tribunal (included in definition of court for the purposes of the Consumer Credit Code)	Enacted the template legislation.
New South Wales	Consumer Credit (New South Wales) Act 1995	Department of Fair Trading	Commercial Tribunal Consumer Claims Tribunal Courts (jurisdiction determined by monetary limit)	Enacted enabling legislation. Maximum annual percentage rate allowed is 48%.
Victoria	Consumer Credit (Victoria) Act 1995	Consumer and Business Affairs Victoria	Civil and Administrative Tribunal Courts (jurisdiction determined by monetary limit)	Enacted enabling legislation. Credit providers must register with the Credit Authority in Victoria. Limitations are placed on who may be a finance broker, and what fees a finance broker may accept or charge. Maximum annual percentage rate allowed is 48%. Mortgage is void if the annual percentage rate under the credit contract exceeds 30%.
South Australia	Consumer Credit (South Australia) Act 1995	Office of Consumer and Business Affairs	District Court of South Australia.	Enacted enabling legislation, with no major differences.

Table B1. Consumer Credit Legislation and Administration, by State / Territory

State	Legislation	Administrative Agency	Court[a]	Key variations[b]
Tasmania	Consumer Credit (Tasmania) Act 1996	Office of Consumer Affairs	Small Claims Division of the Magistrates Court. Courts (jurisdiction determined by monetary limit)	Enacted enabling legislation, but changes to the template legislation are not automatically adopted in Tasmania. Rather, amendments must be approved by approved by parliament and proclaimed by the Governor.
Northern Territory	Consumer Credit (Northern Territory) Act 1995	Department of Industries and Business	Courts (jurisdiction determined by monetary limit)	Enacted enabling legislation, with no major differences.
Australian Capital Territory	Consumer Credit (Australian Capital Territory) Act 1995	ACT Consumer Affairs Bureau	Credit Tribunal Courts (jurisdiction determined by monetary limit)	Enacted enabling legislation. Maximum annual percentage rate allowed is 48%.
Western Australia	Consumer Credit (Western Australia) Act 1995	Ministry of Fair Trading	Commercial Tribunal Courts (jurisdiction determined by monetary limit)	Adopted alternative consistent legislation, whereby the Consumer Credit Code is an appendix to the Consumer Credit (Western Australia) Act 1995

a. In some cases, jurisdiction for a particular section of the Consumer Credit Code is conferred exclusively on a particular court.
b. Variations other than those that would normally be specific to each jurisdiction, such as transitional provisions, conferral of judicial and administrative functions, and provisions relating to each jurisdiction’s credit fund.

Table B2. Key Differences Between Queensland Template Legislation and Western Australian Legislation		
Code Section	**Queensland**	**Western Australia**
1	This Code may be cited as the Consumer Credit Code.	This Code may be cited as the Consumer Credit (Western Australia) Code.
2	This Code commences as provided under section 2 of the Consumer Credit (Queensland) Act 1994 of Queensland	This Code commences as provided under section 2 of the Consumer Credit (Western Australia) Act 1996
4(2)	For the purposes of this Code, the "amount of credit" is the amount of the debt actually deferred. The "amount of credit" doe not include – (a) any interest charge under the contract; or (b) any fee or charge – (i) that is to be or may be debited after credit is first provided under the contract; and (ii) that is not payable in connection with the making of the or the making of a mortgage or guarantee related to the contract.	For the purposes of this Code, the "amount of credit" is the amount of the debt actually deferred.
15(F)(a)	If more than one repayment is to be made – (i) the amount of the repayments or the method of calculating the amount; and (ii) if ascertainable, the number of repayments; and (iia) if ascertainable, the total amount of the repayments, but only if the contract would, on the assumptions under sections 158 and 160, be paid out within 7 years of the date on which credit is first provided under the contract; and (iii) when the first repayment is to be paid, if ascertainable, and the frequency of payment of repayments.	If more than one repayment is to be made – (i) the amount of the repayments or the method of calculating the amount; and (ii) if ascertainable, when the contract is made – the number of the repayments, the period over whey they are to be paid and the total amount of the repayments; and (iii) when the first repayment is to be paid, if ascertainable, and the frequency of payment of repayments.
18(3)	Subsection (2) does not apply if the credit provider has previously given the debtor a copy of the contract document to keep.	Subsection (2) does not apply to a credit contract the terms of which are accepted by accessing or drawing down credit to incur a liability or by the debtor satisfying the conditions of an offer.
25(2)	A credit contract may specify, for the purposes of payments or any other purposes under the contract, when a day ends. Different times of the day may be specified for different purposes.	A credit contract may specify, for the purposes of payments under the contract, when a day ends.

Table B2. Key Differences Between Queensland Template Legislation and Western Australian Legislation

Code Section	Queensland	Western Australia
27(4)	This section does not apply to the debit of an interest charge under a credit contract before the end of the period to which the charge applies if- (a) the charge is debited on the last day of the period; and (b) the amount debited is not treated by the credit provider as part of the unpaid daily balance for that day for the purpose of calculating interest charges under the contract.	Subs (4) does not apply
31(4)	A separate statement of account may, but need not, be given in respect of each or any number of the credit facilities provided under a credit contract.	Subs (4) does not apply
34(1)	A credit provider must, at the request of a debtor or guarantor and within the time specified by this section, provide a statement of all or any of the following- (a) the current balance of the debtor's account; (b) any amounts credited or debited during a period specified in the request; (c) any amounts currently overdue and when each such amount became due; (d) any amount currently payable and he date it became due.	For s 34(1)(c) and (d) omit "currently"

Table B2. Key Differences Between Queensland Template Legislation and Western Australian Legislation		
Code Section	**Queensland**	**Western Australia**
36A	(1) For the purposes of this Code and the credit contract, a debit or a credit made by a credit provider to a debtor's account is taken to have been made, and has effect, on the date assigned to the debit or credit, not on the date on which it is processed. (2) A credit provider may subsequently adjust debits or credits to a debtor's account, and the account balances, so as to accurately reflect the legal obligations of the debtor and the credit provider. (3) However, subsections (1) and (2) do not permit a debit or a credit to be assigned a date other than the date on which it is processed, or the subsequent adjustment of a debit or a credit or account balance, if- (a) the assignment or adjustment is not consistent with the credit contract; or (b) the adjustment results in an interest charge that is more than the maximum amount permitted by the Code, as calculated on the basis of debits or credits to a debtors account consistent with the credit contract; or (c) the assignment or adjustment results in a contravention of section 24; or (d) the assignment of the date on which an interest charge is taken to be debited results in a debit taken to be done before a time permitted under this Code. (4) An adjustment by a credit provider under subsection (2) does not affect any liability of a credit provider under Part 6.	S 36A does not apply
39(2)	This section does not apply if the credit provider has previously given the mortgagor a copy of the mortgage document to keep.	Subs (2) does not apply
53(1)(a)	Withdraw from the guarantee at anytime before credit is first provided under the credit contract; or	Withdraw from the guarantee at any time before credit is first provided under the credit contract where the debtor also terminates or has terminated the credit contract in accordance with section 19 or where the debtor has not entered into a contract with another person in reliance on the availability of the credit subject to the guarantee; or

Table B2. Key Differences Between Queensland Template Legislation and Western Australian Legislation

Code Section	Queensland	Western Australia
60(1)	A credit provider must, not later than 20 days before a change in the amount or frequency or time for payment of, or a change in the method of calculation of, instalments or minimum repayments, under a credit contract takes effect, give to the debtor written notice setting out- (a) particulars of the change; and (b) any information required by the regulations.	For "20 days" read "30 days"
63A	The credit provider may, under section 59, 60, 61 or 63, give a person particulars only of a matter as changed instead of particulars of the change, but only if the credit provider- (a) makes it clear to the person that the matter has changed; or (b) issues to the person a new set of terms and conditions relating to the credit contract, mortgage or guarantee.	S 63A does not apply
65(5)	The credit provider may, under subsection (1), give a person particulars only of a matter as changed instead of particulars of the change, but only if the credit provider- (a) makes it clear to the person that the matter has changed; or (b) issues to the person a new set of terms and conditions relating to the credit contract, mortgage or guarantee.	Subs (5) does not apply
66(1)	A debtor who is unable reasonably, because of illness, unemployment or other reasonable cause, to meet the debtor's obligations under a credit contract and who reasonably expects to be able to discharge the debtor's obligations if the terms of the contract where changed in a manner set out in subsection (2) may apply to the credit provider for such a change.	Insert after s66(1) "66(1a) The Government Consumer Agency may, if requested in writing by a debtor, assist a debtor in applying for a change in the terms of a credit contract under subsection (1) and in any negotiations with the credit provider relating to the change."
67(2)	The credit provider may, under subsection (1), give a person particulars only of a matter as changed instead of particulars of the change, but only if the credit provider- (a) makes it clear to the person that the matter has changed; or (b) issues to the person a new set of terms and conditions relating to the credit contract.	Subs (2) does not apply
68(1)	If the credit provider does not charge the credit contract in accordance with the application, the debtor may apply to the Court to change the terms of the credit contract.	If the credit provider does not change the credit contract in accordance with the application, the debtor may apply to the Court to change the terms of the credit contract.

Table B2. Key Differences Between Queensland Template Legislation and Western Australian Legislation

Code Section	Queensland	Western Australia
100(1)(e)	Section 15(G)(a) and (b) – but only in respect of retained credit fees and charges;	100(1)(e) section 15(G)
100(2)(d)	Section 15(G)(a) and (b) – but only in respect of retained credit fees and charges;	100(2)(d) section 15(G)
101(2)	A debtor or guarantor may not make an application for an order under this Division in respect of a contravention under a contract if the contravention under that contract is or has been subject to an application for an order made by the credit provider or a Government Consumer Agency anywhere in Australia under this Code or a corresponding law of another jurisdiction.	A debtor or guarantor may not make an application for an order under this Division in respect of a contravention under a contract if the contravention under that contract is or has been subject to an application for an order made by the credit provider or the Government Consumer Agency under this Code.
108(2)	On registration of the order, the order is taken to be an order under sections 102 and 105 for the purposes of this Code in relation to the contraventions occurring in this jurisdiction.	On registration of the order, the order is taken to be an order under sections 102 and 105.
125(7)	This section does not apply if the credit is provided as a result of an approach by the debtor that was not induced by the supplier or credit provider.	Subs (8) does not apply
132(2)	This Code does not apply to insurance over mortgaged property that – (a) in insurance for an extended period of warranty for goods; or (b) is insurance over property that is not mortgaged to secure obligations under the credit contract.	Subs (2) does not apply
132(3)	This Code does not apply to consumer credit insurance in connection with a credit contract unless the contract for consumer credit insurance insures the obligations of the debtor under the credit contract.	Subs (3) does not apply

Table B2. Key Differences Between Queensland Template Legislation and Western Australian Legislation

Code Section	Queensland	Western Australia
169A	(1) An indemnity for any liability under this Code is not void, and cannot be declared void, on the grounds of public policy, despite any rule of law to the contrary. (2) The liabilities to which this section applies include the following– (a) a liability for any criminal or civil penalty incurred by any person under this Code; (b) a payment in settlement of a liability or alleged liability under this Code; (c) a liability under another indemnity for any liability under this Code. (1) This section is subject to section 169(2). (2) This section does not derogate from any other rights and remedies that exist apart from this section. (3) This section extends to any indemnity obtained before the commencement of this section.	S 169A does not apply
177(1)(a)	administrative and judicial powers conferred by this Code may be exercised by administrative and judicial authorities of any jurisdiction in which a law adopting this Code is in force; and	Administrative and judicial powers conferred by this Code may be exercised by administrative and judicial authorities of any jurisdiction in which a law is in force that adopts or substantially enacts this Code; and”
179	A reference in this Code or the regulations to a number of penalty units is to be read as a reference to an amount of money equal to the amount obtained by multiplying $100 by that number of penalty units.	S 179 is omitted.

Appendix C – Summary of submissions and targeted consultations

Australian Bankers' Association

The main points and issues raised in the Australian Bankers' Association (ABA) written submission are:

- **Market failure** exists in the consumer credit industry in the form of information asymmetries and negative externalities; however, externalities are more directly a result of information asymmetries.

  The ABA provides, as an example of negative externalities, the case where a transaction between a credit provider and a debtor impacts adversely on a third party. This may be the case where, for example, the debtor does not fully understand the risks associated with a loan and they may be unable to service the loan, and hence may become bankrupt. The ABA contends that any such bankruptcy is likely to have negative flow on impacts on innocent third parties.

- The emergence of **'infomediaries'**, who assist consumers to identify and evaluate the suitability of financial products, has been a significant factor in reducing information asymmetries in the consumer credit market.

  'Infomediaries' include organisations such as the Australian Consumer Association, which often provides commentary on issues related to the purchase of consumer credit, particularly through its *Choice* magazine. Other 'infomediaries' in the Australian consumer credit market are *eLoan*, *Quicken*, *Cannex*, *Your Mortgage* and *LoanNet*.

- The ABA contends that the general scope of the Consumer Credit Code (with minor amendments) is appropriate to address information asymmetries that may otherwise exist in the marketplace. That is, the public interest in such regulation outweighs the competitive restrictions inherent in the Consumer Credit Code.

- The ABA asserts that the **lack of uniformity** has the effect of substantially increasing uncertainty for consumers and business, and results in increased compliance costs in the form of unnecessary delays and acts as a barrier to interstate expansion.

  The ABA suggests it may be appropriate to consider the application of the mutual recognition principle to achieve some form of uniformity. Furthermore, the ABA supports the Post Implementation Review's Recommendation 3.4 to establish a cross-vesting scheme under the Consumer Credit Code for relevant judicial and, where appropriate, administrative functions.

- The ABA notes that there is little evidence that the current **disclosure requirements** address information asymmetries, and indeed create a number of competitive distortions

as the information presented under current disclosure requirements are complex, excessive and often confusing.

The ABA therefore agrees with Recommendation 1.1 (simplified Schumer Box) of the PIR, but notes that, if there is to be mandatory disclosure, then this should be directed towards key information that consumers are likely to use.

- The ABA does not agree with disclosure of a **comparison rate** (Recommendation 1.4), noting that this would shift the focus to price rather than allowing competition to be based on a bundle of price and other features.

  Furthermore, the disclosure of a comparison rate may mislead consumers as the comparison rate published in the advertisement is likely to be different from the rate noted in the disclosure because the comparison rate is specific to each credit contract.

- Section 133, which prohibits requiring **insurance** to be taken out or to be taken out with a particular insurer, acts as an impediment to the development of innovative product bundles.

  Furthermore, there is added confusion due to the inconsistencies with the regulatory approach (towards third line forcing) adopted in the *Trade Practices Act 1974*. The ABA contends that all insurance matters should be regulated within one regulatory environment.

- The ABA notes that there is **significant duplication** between sections of the Consumer Credit Code and the provisions within the *Trade Practices Act 1974*, in particular s.133 (as noted above), ss.140 and 144 (which are partly mirrored in ss.52 and 53 of the *Trade Practices Act 1974*) and those provisions within Part 7 of the Consumer Credit Code which are similar to ss.73 and 74 of the *Trade Practices Act 1974.*

  The ABA suggests that **Part 7 (Related sale contracts)** of the Consumer Credit Code should be simplified by removing those provisions which are duplicated in other legislation. This would reduce the potential for a divergence in administrative approaches.

- The ability of credit providers to deliver products and services **electronically** is hindered by a number of federal, state and territory legislative requirements.

  The ABA contends that the Consumer Credit Code needs to adopt a uniform approach to permit technological innovation in the areas of electronic signatures, electronic provision of notices and tendering of electronic evidence.

- The current **civil penalties** regime fosters over-compliance by credit providers as it has the potential to penalise a credit provider in a way that is disproportionate to the gravity of the offences, and hence is inefficient.

The ABA suggests that, if a civil penalties regime is to exist, then this regime should have the following features:

- Only a court of superior jurisdiction may impose a civil penalty;
- Only a government consumer credit agency or person authorised by the Minister should have standing to bring a civil penalty application; and
- The application standard of proof should be the criminal standards (ie, establishing a case beyond reasonable doubt).

- There is no clear reason for the **price controls** contained in ss.29, 30 and 135 of the Consumer Credit Code and hence they should be removed. Furthermore, s.30 should allow for the reasonable costs associated with the payment to the third party.

Australian Finance Conference

The main points and issues raised in the Australian Finance Conference (AFC) written submission are:

- The AFC agrees that the **objectives** of the Consumer Credit Code are still valid in today's marketplace, but not the methods those objectives are delivered through.
- **Information asymmetries** may also affect credit providers, as they are required to base their credit decisions on the information provided by the applicant (and this information may be incomplete). While there are credit references, credit reporting and credit scoring processes available, the *Privacy Act* restricts the extent and value of information available to credit providers.
- The AFC considers that **disclosure requirements** are important; however, the amount of information required, its relevance at the time and the way it is regulated are of concern.

  The AFC provides the example of purchasing a car to support its argument that the amount of information is too great in the context of all the material a consumer receives, resulting in the information not being sufficiently assimilated at the pre-contractual stage. In this example, there may be a number of documents involved, including car purchase order and contract, credit contract documentation, insurance documentation and vehicle registration documentation.

  The AFC notes that **Recommendation 1.1** (simplified Schumer box) and **Recommendation 1.2** (clarification of which fees and charges are to be disclosed) of the PIR generally reflects their concerns. However, the AFC strongly opposes **Recommendation 1.4** (disclosure of comparison rate) because it cannot be made to work without market distortion, inequities and without misleading consumers.

- The AFC asserts that what is missing from the **disclosure requirements** is the education of consumers on how to use the information, and that the development of such an education program is the responsibility of the government, with input from industry.

- The AFC argues that, due to the lack of **cross-vesting**, an application under the Consumer Credit Code can be both costly and inconvenient for a person who signs a contract and then moves interstate.

  Therefore, the AFC supports **Recommendation 3.4** of the PIR relating to the establishment of a cross-vesting scheme for relevant judicial and, where appropriate, administrative functions.

- Regarding **changes to obligations on grounds of hardship**, the AFC notes that it is in their members' commercial interests to accommodate customers who are experiencing financial difficulty. However, s.66 should be amended to require applicants for contract variations on the basis of hardship to be accompanied by information as to the customer's financial circumstances. This could avoid unnecessary expenses related to a formal court or tribunal proceeding.

- State/territory property laws have similar requirements when it comes to the enforcement of mortgages given to secure either payment to the credit provider under a credit contract or a related guarantee, particularly in relation to **default notices**, and this is reflected in the current combined default notices allowed under the legislation.

  The AFC argues that there needs to be greater consistency between these different pieces of legislation.

- The AFC asserts that the provision of consumer credit is not sufficiently special to warrant the attention it uniquely attracts through the **civil penalties** regime. Credit providers are subject to the normal range of laws, including Trade Practices Act, Fair Trading Acts and Credit Administration Acts (where they exist). These Acts provide an armoury to officials and a raft of remedies to consumers

  The AFC recommends the removal of the civil penalties, and notes that this would not remove the compliance culture amongst the credit providers.

- AFC notes that the provisions in Part 7 of the Consumer Credit Code relating to **joint and severally liability** of linked credit providers are superfluous as they are mirrored in the Trade Practices legislation.

- **Insurance:** The provisions of Part 8 (Related insurance contracts) of the Consumer Credit Code overlap with those in the Insurance Contracts Acts 1984 (Cth). This not only adds compliance costs for the credit provider, but also adds to the bulk of information provided to the consumer (without necessarily adding to the quality of information).

The AFC sees considerable merit in, and justification for, removing from Part 8 of the Consumer Credit Code the provisions that regulate insurance or that require insurance related disclosure, and notes that there should be no adverse implications for consumer protection due to the comprehensive regulation at the Commonwealth level.

Furthermore, the AFC argues that this area of regulation needs rationalisation, where this is best achieved by placing all regulation of insurance in one regulatory environment, or at least removing overlaps and duplications.

- The Trade Practices Act 1974 and state and territory fair trading legislation regulate **credit advertising** and prohibit **harassing conduct** in connection with the supply or possible supply of goods and services, as well as payment thereof.

  The AFC therefore sees merit in research being undertaken to delineate the extent of overlap to ensure the Consumer Credit Code only deals with matters not addressed elsewhere. Furthermore, there appears to be no justification for any provision within the Consumer Credit Code to deal with harassment and thus s.145 does not need to be retained.

- In relation to **consumer leases**, the AFC has no objections to the PIR recommendations to require pre-contractual disclosure of consumer lease information (Recommendation 2.14) or for applying the Consumer Credit Code's false or misleading representations prohibition (Recommendation 2.15).

- The AFC sees no reason to alter the **scope** of the Consumer Credit Code; however, the AFC does agree with Recommendations 2.1 and 2.4 of the PIR relating to clarification of the application of the Consumer Credit Code in relation to credit sale contracts.

- The AFC is not aware of any provisions of the Consumer Credit Code that contravene the *Trade Practices Act 1974*.

- The AFC is of the view that the **Consumer Credit Code should be retained**, as it offers and delivers to credit providers and consumers a national and competitively-neutral legislative base for the regulation of the consumer credit industry. However, there are still issues to be resolved relating to cross-vesting and bringing changes to Consumer Credit Code into law nationally and in a timely fashion.

- The AFC doubts that there exist credible grounds to support reform **Option 1** or **Option 2**.

- The AFC regards reform **Option 3** as having considerable merit, noting that this option is consistent with the recommendations of the PIR and that there is considerable scope for finetuning of the disclosure requirements.

- In relation to reform **Option 4**, the AFC believes that the issue of overlapping legislation is a prime factor to be considered in the context of the current NCP review. The AFC believes that overlapping regulation can present problems for compliance, administration

and enforcement. The problems may be overcome by exact duplications, but this raises the question as to why the duplication is necessary in the first instance.

Commonwealth Consumer Affairs Advisory Council (CCAAC)

- The CCAAC believes the Consumer Credit Code should not be amended or repealed, and that the **objectives of the Consumer Credit Code remain valid** in today's marketplace.

- The CCAAC argues that the crucial issue is **information asymmetry** and notes that credit products are still not well understood by consumers. The CCAAC believes that the objectives of the Consumer Credit Code relating to information asymmetry can only be achieved through restricting competition.

- Evidence suggests that more (or at least clearer) regulation rather than less regulation is required in the market. This evidence includes:

  - Pressure from consumer representatives and some in the Government sector for mandatory publication of a comparison rate because of the ongoing confusion amongst consumers as to the real cost of credit;

  - The recommendations of the PIR; and

  - An emerging problem with fringe credit providers and 'pay-day lenders', who are not covered by the Consumer Credit Code.

- The CCAAC argue that, while credit providers comply with the letter of the law, they do not comply with the spirit of the law. As evidence, the CCAAC provides an example of a notice to customers advising of changes to their continuing credit contract. This notice advises of changes to the interest rate and interest-free period, but does not indicate whether these have increased or decreased.

- The CCAAC believes some form of intervention is required to ensure the efficient functioning of the consumer credit market. Furthermore, as credit is becoming an increasingly fundamental issue for all consumers, a properly functioning consumer credit market provides a powerful community benefit.

- The CCAAC argues that, to be effective, a **mandatory code** (Option 1) would need to mirror the prescriptive provisions of the Consumer Credit Code. There seems little point in moving from the legislated Consumer Credit Code to a mandatory code.

  Therefore, the CCAAC believes it would be inappropriate at this time to adopt Option 1.

- The CCAAC does not believe the consumer credit industry should be **deregulated** (Option 2) for the reasons set out in its submission.

- Regarding **Option 3**, the CCAAC notes that disclosure 'goes to the heart of the problem in this market' and therefore the mandatory disclosure requirements should not be reduced, deleted or transferred to a code of practice.

- The CCAAC argues that it is difficult to see how the mere **duplication** of provisions in legislation is a competition issue. Furthermore, it is preferable for consumers to be able to obtain the information they need from the Consumer Credit Code, rather than having to consult a 'patchwork of Codes and legislation'.

  The CCAAC recommends that replicated provisions should not be deleted if they assist consumers in accessing relevant information about their rights and obligations.

Consumer Credit Legal Services (Victoria, NSW and WA)

- The CCLS argues that, given the pattern of the interest rate margins on credit cards over the last decade, it is difficult to conclude that consumers have benefited from competition in the area of credit card pricing. Similar conclusions may be made about personal loans from banks and finance companies.

- In the housing loan market, however, the advent of competition has resulted in significant benefits to consumers through reduced price of lending and the entry of new credit providers.

  The CCLS notes that the housing loan sector is one in which the level of regulation increased with the introduction of the Consumer Credit Code.

- A 1997 UK Office of Fair Trading study, *Consumer Detriment under Conditions of Imperfect Competition*, identified six signals of a problematic market:

  - Price dispersion amongst seemingly similar products;
  - Existence of focal points of competition;
  - Bundling of primary and secondary purchases after market;
  - Commission payments;
  - Complex products; and
  - Infrequent purchases of credit.

  In its submission, the CCLS provides examples of each of these in the Australian consumer credit market and concludes that at the very least, significant segments of the consumer credit market are not operating in a fully competitive way.

- The CCLS does not agree with the assertion Malbon (1999) made that there is no real differentiation between socio-economic groups with respect to the taking of credit, nor with Malbon's conclusion that interest rates were more influential in helping those on higher incomes to decide to obtain a linked credit loan than those on lower incomes.

- The CCLS argues that those segments currently outside of the scope (ie pawnbrokers, interest free lenders, pay day lenders and solicitor nominee lending) would operate more competitively if they were brought within the Consumer Credit Code's jurisdiction. The CCLS asserts that setting limits on coverage only encourages unscrupulous lenders to find ways to circumvent the Consumer Credit Code.

- **Deregulation** in the consumer credit market has not resulted in the benefits of competition flowing through to consumers and, as such, care should be taken in removing consumer protection on the basis of increasing competition.

- The **policy objectives** of the Consumer Credit Code remain valid and are consistent with competition policy.

- The CCLS argues that the **truth in lending** objectives have not been fulfilled, as disclosure currently occurs in a way which allows credit providers to avoid proper truth and lending requirements.

- The complex nature of credit transactions require detailed regulation, else the benefit of the regulation will be lost.

- Regarding **disclosure requirements**, the CCLS supports the use of the Schumer box and notes that the Consumer Credit Code currently fails to provide consumers assistance in comparing credit products.

- Since credit providers are not required to individually notify rate changes before the change occurs, the consumer may receive this information some time after the change has occurred when they receive their statement of account. This in turn affect's a consumer's decision to leave or stay with a credit provider and does not allow the consumer to adjust repayments with the interest rate changes.

  The CCLS considers the practice of allowing **unilateral changes** by the credit provider and anti-competitive and suggests that the Consumer Credit Code needs to strike a better balance between the ability of a credit provider to vary the contract and the need for a consumer to be able to rely upon 'the bargain they have struck'.

- The CCLS does not consider the provisions relating to **establishment fees and termination fees** themselves as anti-competitive, but notes that they do not redress the anti-competitive conduct of the credit providers in applying these provisions.

- There is minimal application of the **hardship provisions** in practice as the debtor and credit provider generally deal directly with each other to reach a compromise and, hence, it is difficult to say that this provision has imposed any cost upon credit providers.

- The importance of the provision relating to **payout figures** (s.76) is often understated. Consumers need to be able to obtain a statement of the early termination penalty if they are to have the capacity to make meaningful decisions about early repayment.

- Consumer groups continue to strongly support the role of **civil penalties** under the Consumer Credit Code. The CCLS argues that these provisions assist competition in the credit market and have been fundamental in ensuring a compliance culture amongst credit provider.

- If s.118 (Liability of credit providers for suppliers' misrepresentations) did not exist, there would be an even greater lowering of competition as credit providers would be at an advantage in selling through suppliers as their liability for unjust behaviour would be reduced.

- The CCLS notes that the avoidance of **commission disclosure** (Part 8) remains widespread, with credit providers using the provision that they are unascertainable at the time the contract was entered into.

- The CCLS argues that the provisions relating to **advertising** (Part 9) have failed in creating a competitive market as they have little impact on forcing credit providers to advertise the cost of credit. Home loans is an exception.

- The CCLS argues that the low level of disclosure on **leases** does not foster competition. For example, some consumers think that they have a car loan, when in fact it is a lease.

- **'Interest free'** lenders and **'pay day'** lenders were identified by the CCLS as credit providers who are not covered by the Consumer Credit Code. The CCLS argues that the practice of 'interest free' lending is anti-competitive because the consumer is not informed of the level of interest being charged, and there is no consumer protection. Furthermore, the objective of applying to all forms of consumer credit is not achieved.

- **Credit brokers** should also be covered under the Consumer Credit Code and treated as, for example, a car dealer who receives a commission from the credit provider.

- The CCLS notes that deleting **duplicate provisions** in Part 8 (Related insurance contract), as per the PIR Recommendation 2.5, would have the effect that consumers will no longer be able to use low cost Consumer Tribunals to determine some insurance disputes (as the Tribunals do not have jurisdiction over insurance legislation).

- The CCLS believes Recommendation 2.16, which amends the Consumer Credit Code to ensure that contingency fees and charges are not 'key requirements', is misconceived because such fees can be vital to the consumer's choice of product and the overall fairness of the transaction.

- The CCLS strongly supports the **retention of the Consumer Credit Code**, noting that virtually all provisions have a public benefit and pointing out that an ill-informed choice can financially destroy a consumer's life.

- The CCLS opposes regulation by a mandatory **Code of Conduct** (reform Option 1) because they are often too general and do not provide the detail required to avoid ambiguity.

- There is no basis for any argument for **deregulation** (reform Option 2); however, there is every indication that the recent lessening of regulation in the area of credit cards and personal loans has resulted in poorer practices and products.

- The CCLS argues that reliance on principles of disclosure (reform Option 3) would be 'disastrous', as the reduction in the detail of regulation between the Credit Act and the Consumer Credit Code has already resulted in a lessening of disclosure.

- The CCLS provides a number of reasons why the deletion of duplicate provision (reform Option 4) should not occur:

  - The jurisdiction of, for example, Consumer Tribunals may be affected;

  - Coverage of the Consumer Credit Code may be affected;

  - Relevant Statutes of Limitations may vary;

  - Redress options may vary; and

  - The relative simplicity of having all the rules in one place.

Ms Denise McGill (Member, Centre for Commercial and Property Law)

- Ms McGill submits that the provisions relating to **unilateral changes** by the credit provider and **changes by agreement** of the parties to a credit contract promote competition, as this is an improvement over the previous legislation which provided for very complex notification procedures. Furthermore the Consumer Credit Code simplified the contents of the notice.

- **Part 4 Changes to obligations:** Ms McGill argues that s.70(2)(n) may have an adverse impact on competition because of the difficulty in ascertaining when interest rates are excessive. Interest rates are based partially on the risk involved in the transaction, and this risk is unique to each transaction.

  However, if there are any adverse impacts on competition stemming from s.70, these are outweighed by the public benefits. This provisions benefits both consumers and credit providers and strikes a fair balance between their interests.

  Furthermore, the alternative mechanisms available are all much narrower in scope than s.70 of the Consumer Credit Code, and hence s.70 is more likely to fulfil the objectives of the Consumer Credit Code.

Ms McGill notes also that the restrictions on competition in s.70 are appropriate as restricting the use of unjust contracts can only serve to preserve fair competition. It does this by discouraging practices which would give an unfair competitive advantage to credit providers willing the exploit the weak negotiating position of vulnerable consumers.

- **Part 5 Ending and enforcing credit contracts:** Sections 78(6) and 96(1) imposes obligations on a credit provider when selling returned and repossessed goods. Ms McGill notes that, in the absence of these provisions, a duty would be imposed on a credit provider by the *Property Law Act 1974* (Qld) and by the general law in other states.

  Ms McGill argues that the Consumer Credit Code goes further than necessary to protect consumers and concludes that the alternative mechanisms are less restrictive while still delivering the objectives of the Consumer Credit Code.

  Ms McGill argues that s.80 does not provide the redress mechanism for borrowers that they need for it to be an effective restraint upon credit providers and to that extent fails to meet the objectives of the Code. This stems from the fact that proceedings may still be valid even if the credit provider fails to produce a default notice. However, there is no alternative mechanism for the giving of default notices, and s.80 should therefore be retained to meet the objective of the Consumer Credit Code.

  In the case of mortgages of land, the general conveyancing statutes and Torrens legislation impose alternative mechanisms, and for this reason, it seems unnecessarily restrictive on competition for the Consumer Credit Code to impose duplicate requirements.

- **Part 7 Related sale contracts:** Ms McGill notes that there are no additional anti-competitive provisions (other than those identified in the Issues Paper), that the benefits of the existing restrictions outweigh the costs, and there are no alternative methods of achieving the objectives.

- **Part 8 related insurance contracts:** Ms McGill argues s.138 (termination of consumer credit insurance contract) is not effective when the debtor returns the goods voluntarily because this terminates the credit contract and hence the insurance contract. The credit provider is then deprived of the insurance as a means of recovering the outstanding debt. A similar argument is provided for s.139 (termination of insurance contract over mortgaged property).

  Ms McGill concludes that there are no net public benefits from these provisions, but notes also that there are no alternative mechanisms for achieving the objectives of the Consumer Credit Code. Therefore, ss.138 and 139 should be amended to provide for termination of insurance contracts only if no part of the credit remains to be paid by the debtor.

- **Part 9 Advertising and related conduct:** Ms McGill notes that this section facilitates competition by informing consumers, the benefits outweigh the costs, and there are no alternatives for achieving the objectives of the legislation.

- Ms McGill asserts that **Romalpa agreements** are not necessarily a way of avoiding the Consumer Credit Code. This is because a contract under which the seller retain title and the buyer has an obligation to purchase the good and to pay an amount which exceeds the cash price, is deemed by s.10 of the Consumer Credit Code to be a credit contract, provided the provisions within s.6 are also satisfied.

- Ms McGill believes that **Recommendation 2.3** of the PIR, which recommends amending the Consumer Credit Code's definition of 'cash price' to ensure that it adequately applies to goods which are not normally sold for cash by including the concept of 'reasonable value', will promote fair competition.

- Ms McGill argues that **Recommendation 2.4** (that solicitors be covered by the Consumer Credit Code) may actually restrict competition by causing the practice to end and thus removing an important source of competition to more conventional and large financial institutions.

- **Recommendations 2.10 and 2.13** (revision of the $125,000 limit) may restrict competition, but the benefits would outweigh any such restrictions.

- **Option 4:** Ms McGill notes that Part 7 Division 3 of the Consumer Credit Code is wider than the corresponding provisions in the *Trade Practices Act 1974* because the Consumer Credit Code applies to a wider range of credit providers. However, the *Trade Practices Act 1974* covers a wider range of consumers. The Consumer Credit Code therefore complements, rather than reinforces, the *Trade Practices Act 1974*.

  Sections 130 and 133(2) are unnecessary as they replicate ss. 47(1) and 47(6) of the *Trade Practices Act 1974* and should be deleted.

  Ms McGill argues that s.136(1) of the Consumer Credit Code is invalid under s.109 of the Constitution as it is inconsistent with Part IX of the *Insurance Contracts Act 1984*, and thus this provision should be deleted.

Members of Consumer Credit Subcommittee of the Banking Finance and Consumer Credit Committee of the Law Council of Australia

- The LCA-CCS contends that **national uniformity** benefits the consumer through lower transactional costs and greater regulatory certainty. Uniformity in legislation is only one part of the picture; judicial and administrative consistency is also desirable.

- There are currently eight laws and the challenge is thus to provide as far as possible a seamless **administration** in the national interest. The LCA-CCS suggests that the

Consumer Credit Code Management Committee be given statutory support to reinforce its presence and to provide a clear direction for its functioning. Furthermore, this would provide a national repository of policy knowledge, official views and guidelines, case law and history.

- Existing **cross-vesting** arrangements under the *Jurisdiction of Courts (Cross-Vesting) Acts* of 1997 are complex, expensive and cannot be used in all cases, as they apply between jurisdictions of the Supreme Courts, while jurisdiction in respect of many Consumer Credit Code issues at first instance is conferred exclusively on state and territory tribunals or falls outside the monetary thresholds of Supreme Courts' jurisdictions.

  The cross-vesting that does exist within the Consumer Credit Code are specific to applications for civil penalties.

  The LCA-CCS recommends 12 principles in relation to cross-vesting, the main principles being that:

  - Each Consumer Credit Code to expressly confer jurisdiction concerning civil or criminal matters (as appropriate) arising under it on the courts or tribunals (as appropriate) of each other participating state and territory.

  - Each state and territory to vest in its appropriate courts or tribunals power to hear matters arising under the Consumer Credit Codes of any other participating state or territory, which confer jurisdiction on that court or tribunal.

- The LCA-CCS believes that the uncertainty about the extent to which **electronic commerce** is permitted under the Consumer Credit Code may be inhibiting the development of products, and recommends that a number of principles be recommended, including:

  - That the Consumer Credit Code be amended so as to facilitate electronic commerce (Wallis Inquiry Recommendation 91); and

  - That the Consumer Credit Code, as far as possible, should adopt appropriate internationally recognised standards for electronic commerce (Wallis Inquiry Recommendations 92 and 93).

- There are ambiguities in **Part 4** (Changes to obligations) of the Consumer Credit Code which should be resolved in the interests of both consumers and credit providers. These ambiguities in the Consumer Credit Code provisions are likely to create differing impacts on credit providers, which may adversely affect an even competitive environment.

  Section 66 (Changes on account of hardship) is provided as an example. The LCA-CCS believes that the benefits to consumers outweigh any effects on competition; nevertheless, some ambiguities ought to be resolved. For example, how may the

threshold test (unable reasonably because of illness, unemployment or other reasonable cause to meet the debtor's obligations) be satisfied? While it does not need to be prescriptive, there should be uniform procedures for making application under s.66.

- There are ambiguities in **Part 5** (Ending and enforcing credit contracts) of the Consumer Credit Code which should be resolved in the interests of both consumers and credit providers. These ambiguities in the Consumer Credit Code provisions are likely to create differing impacts on credit providers, which may adversely affect an even competitive environment.

  Section 86 (Postponement of exercise of rights) is provided as an example. The LCA-CCS believes that the benefits to consumers outweigh any effects on competition; nevertheless, some ambiguities ought to be resolved. For example, the court is given no guidance as to the exercise of its jurisdiction nor the orders it might make.

- There are unresolved conflicts and tensions between the objective (to encourage compliance) and certain features of the **civil penalty** provisions. In particular, the civil penalty provisions are also relied upon in varying degrees to perform a number of other functions in particular the provision of compensation to debtors, enforcement of the Consumer Credit Code generally, and licensing.

  The LCA-CCS believes that, in one sense, the process itself has become the penalty. This is because the costs incurred by the credit provider in a civil penalty application and the damage to the credit provider's reputation, can be substantially more significant than the actual civil penalty imposed.

  Furthermore, there are a number of other factors which also encourage a compliance culture amongst credit providers, and which are presumably considered to be a sufficient compliance incentive in relation to other consumer financial services products, including potential criminal penalties under the Consumer Credit Code and provisions under other legislation (for example, *Trade Practices Act 1974*).

  The civil penalty regime has to potential to encourage excessive disclosure and a distortion in the allocation of available resources in that more extensive consideration and analysis may be directed to the key requirements than to other provisions of the Code.

  If a need is perceived to retain some form of civil penalty mechanism in order to encourage compliance, this should be a sanction which encourages compliance by providing an alternative means of punishment in the serious instances of misconduct.

  The LCA-CCS believes there would be significant advantages for both credit providers and debtors in introducing a self-rectification mechanism which would permit credit providers to remedy certain types of errors without incurring the significant costs involved in bringing a civil penalty application. Any such procedure should balance the public interest in reducing the cost to credit providers (which is ultimately passed on to

debtors), the protection of the interests of debtors and guarantors, and in ensuring public scrutiny of compliance breaches and the provision of relief.

- The **linked credit** provisions (Part 7) are inconsistent and ambiguous in scope and this is likely to have anti-competitive effects. One issue is the wide definition of linked supply in s.117, which may catch providers even if they are unaware that credit will be used for an acquisition. The LCA-CCS contends that this may inhibit competition, especially by raising barriers against smaller players.

- The LCA-CCS believes that publishing a **comparison rate** is of limited utility to the consumer and departs from national uniformity.

Mr Randall Dennings (Member of the public and solicitor)

- Some of the objectives of the Consumer Credit Code are not being met by regulation, especially in relation to **national uniformity**:

  - There are still state and territory differences in the legislation and the methods of its enforcement; and

  - The lack of a uniform cross vesting provision could lead to a divergence of judicial views on key aspects of the Consumer Credit Code.

- Regarding **disclosure requirements** under Part 2 of the Consumer Credit Code, further research needs to be undertaken to ascertain what information the consumer actually finds useful and also to determine the best method of delivering that information to the consumer. Only then will it be possible to accurately assess the public benefit that the existing provisions provide.

- **Part 4 Changes to obligations:** Mr Dennings agrees that the anecdotal evidence suggests that the provision relating to the matters to be considered by the court (s.70(2)) causes mainstream credit providers to view applications more cautiously, but that more research is required to determine the actual effect on mainstream credit providers.

- The high costs associated with **civil penalty** legal proceedings act as a barrier to entry. Mr Dennings suggest that an appropriately drawn self-rectification regime will remove this barrier.

- **Part 8 Related insurance contracts:** Mr Dennings questions whether there are any consumer benefits delivered by ss.133(2) and 135 because of the practical difficulties created by those sections.

- Mr Dennings questions whether there are any consumer benefits delivered by the provisions of **Part 9** (Advertising and related conduct) of the consumer Credit Code because of the practical difficulties created by those provisions.

- Mr Dennings believes that there will be practical difficulties created by **Recommendation 1.4** (Mandatory disclosure of the comparison rate) of the PIR and questions whether this recommendation would deliver any public benefit.

- From a compliance perspective, the deletion of **replicate provisions** is to be welcomed, particularly in circumstances where the replicant is somewhat different between the two sets of legislation.

Targeted consultations – industry

- The introduction of the Consumer Credit Code was a significant cost to the industry, especially to smaller players within the industry. As the initial costs have now been sunk, industry is prepared to live with the current legislative framework.

- Continuing on-going costs associated with the Consumer Credit Code are difficult to identify as they are now just part of general business costs, however it is accepted that they are decreasing over time as the Consumer Credit Code becomes settled within normal operating procedures within the industry.

- The Consumer Credit Code was also seen as a cultural shock to many industry participants, especially smaller operators.

- The Consumer Credit Code is acknowledged as a significant improvement over the previous State based Credit Acts as it is a much clearer legislative framework. The Consumer Credit Code delivers where it should.

- Industry has always been happy with the ‘intent’ of the Consumer Credit Code, just some concerns about particular aspects of it, especially its inflexibility.

- One industry body specifically noted concerns about the lack of uniformity across jurisdictions, especially in context of Western Australian legislation. These comments were tempered by another industry body who suggested that the exceptions within the Western Australian legislation were manageable.

- In the context of lack of uniformity, there are current concerns with the New South Wales government proposal for the introduction of a mandatory comparison rate, as this requirement is not currently in the Consumer Credit Code. This stance being proposed by the New South Wales government was seen as ‘political grandstanding’, rather than providing benefits to consumers due to the ‘flaws’ associated with constructing the comparison rate.

- With respect to the documentary requirements of the Consumer Credit Code, it is considered that:

  - They don’t help with customer relations;

- The average person is not sophisticated, and doesn't understand the contracts;
- The customer focus is on the repayment amount, not the fine print; and
- The industry hasn't gained any additional business due to the introduction of the documentary requirements.

- Documentation and information is considered to be most helpful to consumers where it is relevant and able to be easily digested. The civil penalty regime within the Consumer Credit Code drives credit providers to be cautious, with the outcome being providing more information than less in order to satisfy any potential legal actions in the future.
- The largest complaint about the introduction of the Consumer Credit Code is that credit providers are now taking a more conservative approach to lending, with an outcome being some credit providers have stopped providing credit to historical customers as they now don't meet the new lending criteria.
- Industry generally accepts the current Consumer Credit Code, and have indicated that the status quo reform option is there preferred choice. However in saying this the industry have certainly indicated that there are opportunities for the fine-tuning of the legislation, which has been already considered through the PIR process.

Targeted consultations – consumer associations

- While the credit industry has become 'deregulated', it has essentially remained uncompetitive in terms of pricing credit, with the exception of the housing loan sector.
- The civil penalty regime associated with the Consumer Credit Code provides the right incentives to credit providers to ensure disclosure requirements of the Code are properly administered. There would be serious concern if the costs associated with the civil penalty regime were to be reduced, as it would likely follow that the level of disclosure currently being enjoyed would decline.
- Having clear disclosure at the beginning of any credit contract process avoids litigation, and is therefore should be considered as a cost saving mechanism.
- The length of the documentation associated with a credit contract is a feature of the complexity of the terms and conditions and charging regime now being offered by credit providers, and does not reflect the Consumer Credit Code.
- The Consumer Credit Code is considered to provide pro-competitive incentives, and actually tries to redress many of the anti-competitive practices within the credit industry.
- Increasing concerns about the amount of consumer lending occurring 'outside' of the scope of the Consumer Credit Code, especially by finance brokers such as 'pay day' lenders. They are the primary cause of market distortions in the finance industry as the

contracts associated with these activities provide for poor consumer outcomes. Activities promoted by these finance brokers should be brought within the scope of the Consumer Credit Code.

- Believe the proposed outcomes of the PIR are generally positive.
- Have concerns regarding the option for deleting overlapping provisions as the outcomes may be different under alternative legislative frameworks. Further, alternative legislative frameworks will require different forums in which to hear any action, and therefore will be a different cost structure from that currently enjoyed.
- In terms of reform options, there is clear support within the consumer association area for the status quo, with the requirement of also extending the scope of the Consumer Credit Code to incorporate activities promoted by finance brokers.
- With respect to deleting duplicate provisions, the consumer associations consider that the Consumer Credit Code should be a 'one-stop-shop' for consumer credit protection, and that consumers should not have to access other legislation in a piece-meal manner in order to ensure statutory protection.