



**Money Centre Fortitude Valley
Brisbane**

SUBMISSION

to

Senator Nick Sherry
Minister for Superannuation and Corporate Law

Regarding the
**Draft National Consumer Credit Protection Bill,
2009**

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This Submission Addresses Only Those Sections of the Draft Legislation that Impact on the Small-Loans Industry

SUMMARY

The Federal Government's stated objective of having one law for lending throughout Australia has utterly and disgracefully failed. The resulting state-controlled hodgepodge for small lenders is the same shambolic mess it has always been. But now lenders are burdened with an additional layer of pointless, confusing and expensive Federal oversight.

The key points claimed by the Federal Government regarding the bill are:

- Delivers a single, standard, nationally consistent consumer credit law. (**Utter bullshit. The States are allowed to retain their old individual laws and also create new laws.**)
- Reduces duplication, red tape and compliance costs as eight sets of regulation are replaced with one national scheme. (**Crap. It increases duplication, red tape and compliance.**)
- Cuts up to 2,500 pages of inconsistent laws down to one comprehensive national regime. (**Lies. See previous comments.**)

Shame on our elected representatives who have succumbed to lobbying by biased and ignorant pressure groups. You had a golden opportunity to bring sanity to the small-loans industry throughout Australia but instead have abandoned your stated goal to appease a vocal minority.

I expected far better from the Rudd Government!

Why Australia Needs a Small Loans Industry

The banking industry is cumbersome and inefficient at doing small, short-term loans. Most personal loans offered by banks are a minimum of \$5000 repaid over 1 - 7 years.

People who need a small loan for unexpected expenses like car repairs, rental bonds and health emergencies shouldn't be forced to borrow far more than they need. The only alternative the banks offer is a credit card. But many people discover that cards are a credit trap that encourages impulse buying and may never be paid off. The banks profit from this entrapment.

A far better alternative for many consumers is to get a small loan with a defined repayment plan that will leave them debt-free within a few weeks or months.

The small-loans industry provides a vital service to ordinary Australians. The Federal Government should support it with sound, uniform legislation.

The K.I.S.S. principle

We've all heard of it: Keep It Simple Stupid! Its blunt but its very appropriate for legislation for the small loans consumer.

If the government wants to reduce the cost of small loans it should ensure that:

- a) there is ample competition amongst lenders. (i.e. consumers need to have a range of credit providers to choose from).
- b) that the rules of the transaction are kept simple, while providing adequate protection.

Consumers already have a lot of protection under the current Consumer Credit Code. Much of the proposed new legislation isn't applicable to small loans, and indeed will increase the cost of compliance. This cost will inevitably be passed onto the borrowers.

I believe there is an urgent need for a separate small-loans sub-category in the proposed Federal legislation.

Lenders Submissions Ignored

Lenders and their representative organizations the NFSF and FAA have for several years been lobbying Government for reform of the small-loans industry. They have been urging:

- Licensing of all lenders
- Mandatory external disputes resolution.
- Capping of total cost of credit.
- Legislation for Positive Credit Reporting.
- Federal Legislation so that the same rules apply in all states of Australia.

So far, the proposed Federal Government legislation has only addressed the first two. And let's face it, they're easy!

Positive Credit Reporting

The most frustrating thing for me and my staff is when we verify an applicant's identity, employment and income, check their last three months bank statements, verify their budget of living expenses, do a credit check on Veda, approve the loan, then quickly have it go bad. What more can we do?

Occasionally it's not the customer's fault; they've lost their job or had a serious health issue. But in most instances there are two factors over which we have no control:

1. The customer has lied to us in their written application and verbal interrogation.
2. Far too many other lenders don't use credit reporting agencies such as Veda for small loans. So how is the next lender to know the customer has defaults?

It's an unfortunate truth that the fees charged to honest borrowers subsidize the losses from dishonest borrowers. That's true of mainstream banking as well as the small loans industry.

- **Enlightened credit-monitoring legislation would significantly reduce the honest consumer's cost of borrowing.**

Credit Reporting Services

The Government has laid the onus squarely on Lenders and Brokers to ascertain that the loan is suitable for the customer's requirements and is affordable. But it has not provided the industry with the tools to thoroughly analyze a customer's financial status. e.g. Positive Credit Reporting.

Companies such as Veda and Charter Mercantile are geared towards servicing large and medium sized financial transaction reporting. They also provide a lot of useful ancillary services such as company searches. But they aren't really geared towards servicing the small, short-term loans providers.

- **The small loans industry needs a simpler and cheaper alternative.**

A proposal for a K.I.S.S. system for small loans reporting.

A simple solution could be borrowed from the food industry. It started in the UK, and is currently being mooted for compulsory use in Australia (& other countries). Processed foods will be rated according to their health benefits: But instead of complex charts showing kilojoules, sugars fats etc, the packaging will have a graphic of a **traffic light**. Green means good, orange means acceptable but with some negative factors, red light means the food is definitely bad for you. The beauty of the system is that everybody can see at a glance the health status of the food.

The small loans industry needs a similar system. The Federal Government should:

1. Establish a centralized credit monitoring agency with a traffic light system.
2. Make it compulsory for lenders to do a credit check of all loan applicants.
3. If the loan is granted, the lender records the amount and clicks onto the green button of the traffic light.
4. If the borrower goes into arrears, the lender changes the traffic light to orange.
5. If the borrower gets back on track with their loan, the lender would change them back to green.
6. If a lender issues a default notice, the borrower's traffic light is changed to red.
7. When a loan gets paid out, the lender switches off the traffic light and there is a notation of the date the loan was paid out.

Other benefits are:

- a. Because every lender would have to use it for every loan, the cost of operating the database would be amortized across the industry. It may be less than \$1 per loan, as compared to \$6 to \$7 per enquiry using the current monolithic service providers.

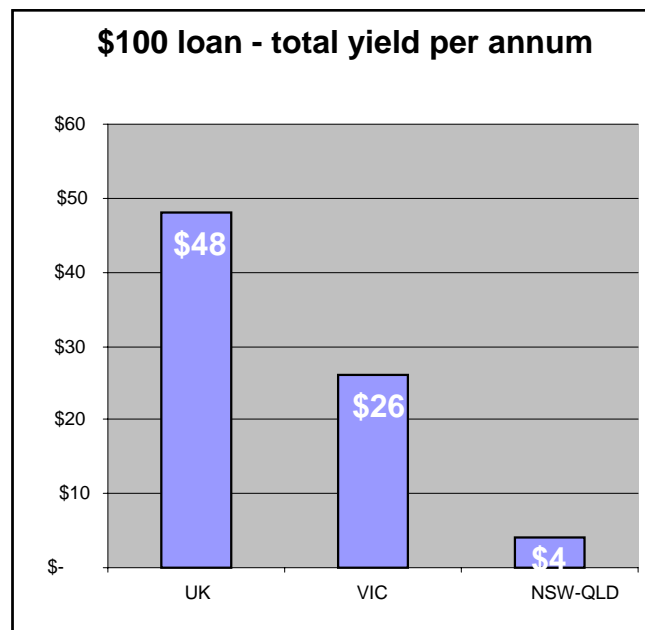
- b. In a snapshot it will deliver much more crucial data than any current credit reporting system.
- c. It will significantly reduce bad debts. Once this filters through to lenders, market competition will ensure that they reduce their charges to the deserving borrowers.
- d. It will give a much more accurate picture of the ongoing status of borrowers, thereby enabling the 'good' ones to build a positive credit rating.

Interest Rate Caps

This is undoubtedly the thorniest issue facing lenders. The 48% cap had its origins in England over a century ago. It was calculated at a flat rate: a \$100 loan for a year yielded interest of \$48. **England abandoned interest rate capping more than 30 years ago.**

When various Australian states introduced interest rate caps they followed the British lead. Except they sneakily changed the calculation to being 48% per annum **daily reducing** which is approximately **26% flat**.

Three years ago the do-gooders in NSW and ACT denounced all short-term lenders as crooks who had to be put out of business. In one foul swoop the legislators changed the formula so that the 48% cap became **inclusive of all fees and charges**. Queensland followed suit in August 2008. These actions made it totally uneconomical for lenders to do small, short-term loans. Never mind that the public need them!



It should be noted that the NSW-QLD column is the total yield to the lender before paying Rent, Wages, Electricity, Telephone etc.

- **Significantly Victoria, which has done by far the most exhaustive research and consultation on the small loans industry, has rejected the inclusion of fees and charges in their 48% cap.**

I don't intend to repeat the detailed evidence against the NSW/ACT/QLD cap. It has all been covered by me and numerous other parties in our previous submissions to both State and Federal governments.

But I am particularly alarmed at the Hon Nick Sherry's comments in an ABC interview in which he states, "Three states have a 48 per cent cap. That will be retained. Those states that don't have a 48 per cent cap, we're going to ask them not to impose a 48 per cent cap, and then we will assess the outcomes; we'll look at what has happened in the states that have a 48 per cent cap and those that don't, with a responsible lending provision that has come into force, and we'll look at what the outcomes are."

There is absolutely no excuse for waiting to compare how the various states perform; all the evidence is already available. NSW introduced the 48% all-inclusive cap three years ago and said it would be reviewed after one year. However they have failed to do the review, no doubt because it would have exposed the utter foolishness of their legislation.

Indeed one has to ask the question, why cap lenders fees and interest, but not other goods and services? Why didn't the government cap petrol prices when they went sky-high? Why doesn't it cap lawyer's fees? The answer is of course that in a free enterprise system, competition ensures that customers can get the best service to suit their needs. Why do we need a cap at all? There's heaps of competition amongst lenders.

Legality of Capping Fees Questioned

It's interesting to note that under current legislation the States are empowered to impose interest rate caps. But nowhere does it say they have the right to cap the fees charged for providing the service. Frankly I think we lenders should start a class action and sue the arses off NSW/ACT/Qld for the millions of dollars of losses we have incurred.

The Move to Uniform Federal Legislation

Personally I was looking forward to having lending come under the supervision of ASIC because I know I can justify what I charge my customers. I'm happy to defend myself in court as well, because I know the court has to examine the commercial reality of the evidence. But the Federal Government has bowed to pressure from a self-righteous minority in the NSW/ACT/Qld States who totally ignored the mountain of hard evidence about the true cost of providing small, short-term loans.

My customers deal with me because they're happy with the service I offer. What right has the State Government got to try and force me to lend to them at less than it costs me to do the loan?

Urgent Need for Standard Federal Legislation A.S.A.P.

If the Federal Government hasn't got the power to abolish State interest rate caps, then it should use whatever carrots or sticks it has available to get the States to agree to all adopt the most suitable State legislation. Clearly that is the Victorian legislation which has a 48% cap that is **not inclusive of fees and charges**. Lenders can live with that, and the consumers will have adequate protection.

The hard part will be forcing the recalcitrant states of NSW/ACT/Qld into line. But they're the ones who ignored economic reality by making their 48% cap inclusive of fees and charges so they deserve to have their heads banged together.

The Rudd Government is increasingly vulnerable as the recession deepens. Now is the time to demonstrate positive leadership by delivering on its promise of a level playing field for Consumer Credit legislation throughout Australia.

END