

ASIC Consultation Paper 330 –
Using the product intervention
power: Continuing credit
contracts

Legal Aid NSW submission to
ASIC

3 August 2020

About Legal Aid NSW

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

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

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

services and 27 Women's Domestic Violence Court Advocacy Services.

The Civil Law Division provides advice, minor assistance, duty and casework services from the Central Sydney office and 20 regional offices. It focuses on legal problems that impact on the everyday lives of disadvantaged clients and communities in areas such as housing, social security, financial hardship, consumer protection, employment, immigration, mental health, discrimination and fines. The Civil Law practice includes dedicated services for Aboriginal communities, children, refugees, prisoners and older people experiencing elder abuse.

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

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Introduction

Legal Aid NSW welcomes the opportunity to contribute to the Australian Securities and Investments Commission's (**ASIC**) Consultation Paper 330 (**CP330**) regarding ASIC's proposed use of the product intervention power in relation to continuing credit contracts.

Legal Aid NSW strongly supports that ASIC use its product intervention power under Pt 7.9A of the *Corporations Act 2001* (Cth) to impose a cost cap on the total fees that can be charged in relation to continuing credit contracts.

Legal Aid NSW considers that this is the most effective means of addressing the issues of the continuing credit lending model as identified in CP330 and the detriment it is causing consumers, on an industry wide basis.

This submission outlines Legal Aid NSW's casework experience in respect of the continuing credit lending model and answers the consultation questions in CP330.

Legal Aid NSW's experience

Recent rise in clients seeking assistance with continuing credit contracts

Since ASIC issued their product intervention order for short term credit on 12 September 2019, Legal Aid NSW has seen vulnerable clients seeking legal assistance after entering into continuing credit agreements with high fees and subsequently experiencing increased financial hardship. These agreements are in the form of the continuing credit lending model described by ASIC in CP330.

Key concerns from our casework

In our experience, continuing credit lenders, of the type described at paragraphs 16-22 of CP330, lend to some of our community's most vulnerable consumers, many of whom are already experiencing financial difficulty. These include consumers with low levels of literacy, young people, Aboriginal and Torres Strait Islander people, people experiencing homelessness, people with disability and people whose only source of income is Centrelink payments.

Common themes with this lending model that emerge in our casework include:

1. Clients have low incomes and very little or no capacity to repay the loan.
2. Clients generally default on repayments quickly and are charged high fees.
3. Clients frequently do not understand the extent of fees and charges levied under the agreements. Clients are surprised when told that their total debt is several times the original small principle sum.
4. Where clients do not have sufficient funds for the direct debit, the withdrawals result in negative account balances, additional bank dishonour fees and we see debt spirals where clients seek to obtain new loans to repay existing debts.

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5. The lender continues to debit clients' accounts even after loan amounts and fees are repaid in full.
 6. Some continuing credit contracts ask that the consumer warrant that he/she was "of sound mind and judgement and able to make decisions regarding [their] finances". It appears counter intuitive to ask consumers to self-assess these criteria.
 7. The lender does not always provide credit documents upon request. Legal Aid NSW has received inconsistent and incomplete responses. In some cases, no credit contract is ever provided so we cannot advise our clients about the terms of their contract, including the relevant fees and whether the client has entered into a continuing credit contract or an alternative lending model.
 8. In our experience, the lender's Internal Dispute Resolution (**IDR**) responses appear formulaic and often don't address the specific issues raised in each dispute.
 9. Debt collectors operating on behalf of the lender continue to take steps to enforce debts including, in some cases, where debts are settled through IDR and no amount is owing.

The continuing credit lender and service provider that we are aware of, BHF Solutions Pty Ltd (BHFS) and Cigno, state in their Disclosures and Authorisations document (**D&A document**) that while not covered by the National Credit Code (**NCC**) "*they both have adopted the protections afforded by the [National Consumer Credit Protection Act 2009 (Cth)] they believe to be best practice and where practicable have sought to manifest those principles in their service*". It is not clear what 'protections' and 'best practice' have been adopted, aside from having an internal dispute resolution policy.

This same D&A document includes a misleading and incorrect fact that fees are fixed at a flat fee of 5%. This is inconsistent with the fees set out in the loan agreement. In the loan agreement, fees are calculated per draw down, up to a maximum fee in a 12-month period, the total of which exceeds 5%.

Examples of our clients' experiences

The below case studies are a portion of Legal Aid NSW's experience assisting clients with disputes relating to continuing credit contracts. They demonstrate the lender's practice of giving high cost loans to vulnerable people who are already experiencing financial difficulty and difficulties with IDR leading to significant consumer detriment.

Case Study 1

A 21-year-old homeless women with a mild intellectual disability, hearing loss and multiple psychosocial disabilities including depression, anxiety, panic attacks and PTSD obtained a continuing credit contract from BHFS through Cigno for \$200 in August 2019. She had limited literacy skills and had difficulty understanding the details of the contract she was entering.

By the time she saw Legal Aid NSW, less than two months after obtaining the loan, she had repaid \$106 but the remaining debt ballooned to \$412.65 and she was experiencing ongoing financial hardship.

She was charged financial supply and lender fees of \$160, priority transfer fee of \$16, weekly account keeping fees of \$41, a change of payment schedule fee of \$22 and \$78 in dishonour and default fees.

The consumer's bank account, provided to Cigno at the time of entering the contract, was in a negative balance for 71 out of the 90 days that it covered.

The continuing credit contract asked the consumer to warrant that she was "of sound mind and judgement and able to make decisions regarding [their] finances".

The 'Disclosures and Authorisations' document included a misleading and a false statement of the true cost of the loan, in that it referred only to a 5% flat fee. This is inconsistent with the fees set out in the loan agreement. The loan contract itself was expressed as a continuing credit contract with a fee of \$15.00 for each draw down, up to a maximum of \$120 per each 12-month period.

Legal Aid NSW assisted the client with preparing and submitting an IDR request for a compassionate waiver due to client's dire financial and personal circumstances.

Cigno's IDR response appeared to be a formula response, rather than a response which specifically considered our client's situation, and the issues we had raised. This response failed to address issues we raised and included responses to legal claims we had not made.

Cigno defended the decision to lend to this client, claiming that she met their criteria and they deemed the loan "suitable" but agreed to finalise this matter on terms favourable to our client.

Case Study 2

We assisted a 47-year-old female client who was homeless, a victim of family and domestic violence, and wholly dependent on social security benefits. She struggled with mental health issues making employment difficult. She used Cigno services to apply for and obtained a continuing credit contract from BHFS for a loan of \$100 in August 2019.

By December 2019 \$600 in fees had accrued including \$96 in upfront fees (same day fee, lender fee and financial supply fee), \$95 in ongoing account keeping fees and over \$375 in default fees in approximately four months since the loan was taken out.

At the time Cigno made the decision to advance \$100 to our client:

- there had been six dishonours in her bank account in the 90 days prior
- some of the dishonours related to loans provided via Cigno
- a Small Amount Credit Contract (SACC) loan had been taken out within the last 90 days
- the client was clearly within the period of a Debt Agreement
- the client had no income other than social security benefits.

The 'Disclosures and Authorisations' document included a misleading and a false statement of the true cost of the loan, in that it referred only to a 5% flat fee. This is inconsistent with the fees set out in the loan agreement. The loan contract itself was expressed as a continuing credit contract with a fee of \$15 for each draw down, up to a maximum of \$120 per each 12-month period.

Cigno agreed to finalise these matters on terms favourable to our client.

Case Study 3

A young Aboriginal man used Cigno services to apply for and obtain 10 credit contracts from BHFS over a period of just over 18 months from March 2018. Despite multiple requests to the lender for access to credit documents, Cigno only provided the final loan agreement which was confirmed as a continuing credit contract. We were unable to confirm how many of the earlier nine contracts were also continuing credit contracts.

At the time of the account statement from Cigno, he had paid \$2382.12 in fees and charges on top of the principal amounts borrowed totalling \$1,250. Deductions continued until IDR was initiated.

Legal Aid NSW prepared an IDR letter on the client's behalf, but we are yet to receive a response that engages with the substance of our client's complaint and the matter remains unresolved.

Case Study 4

An Aboriginal woman from a remote community in NSW used Cigno's services to apply for and obtain six continuing credit contracts from BHFS totalling \$1,750 between January 2017 and November 2019. She was dependent on social security benefits and had a history of credit defaults and financial hardship.

Loan no	Date	Loan Amount	Fees and Charges	Total Paid
1	Jan-17	\$250.00	\$257.65	\$507.65
2	Jul-18	\$250.00	\$195.75	\$445.75
3	Oct-18	\$250.00	\$251.70	\$501.70
4	Dec-18	\$250.00	\$399.00	\$649.00
5	Aug-19	\$350.00	\$349.55	\$699.55
6	Nov-19	\$400.00	\$369.65	\$769.65
Total		\$1,750.00	\$1,823.30	\$3,573.30

During the course of the contracts she paid Cigno almost \$3600 – more than twice the amount she borrowed.

When requested by Legal Aid NSW, Cigno failed to provide any documentation regarding the suitability and affordability of the loan.

Legal Aid NSW prepared an IDR letter on the client's behalf. In the course of negotiation, the client ended up accepting a lesser offer to what we believe she may have been entitled to obtain.

Case Study 5

A 60-year-old woman receiving the Disability Pension from regional NSW used Cigno's services to apply for and obtain a continuing credit contract from BHFS totalling \$250 in November 2019.

In the 12 months prior she had had two prior short-term credit contracts with Cigno and Gold-Silver Standard Finance Pty Ltd.

Upon entering the continuing credit contract, the client disclosed to Cigno that the loan was for a bond for a new house as she was homeless and sleeping at a shelter.

At the time she spoke with Legal Aid NSW about this loan two months later, the client had paid \$60. The client had been charged \$241 for financial supply fees and account keeping fees and had \$281 in default fees, leaving a total of \$726 outstanding.

Legal Aid NSW assisted the client to initiate IDR. Cigno agreed to finalise these matters on terms favourable to our client.

ASIC's proposal and feedback questions

D1Q1 Do you consider that continuing credit contracts, when issued to retail clients in the way described in paragraphs 16–22, have resulted in, or will or are likely to result in, significant detriment to retail clients? If so, please provide any relevant evidence which supports your views.

The model described in paragraphs 16 - 22 is largely accessed by vulnerable consumers who require small amounts of credit to meet basic expenses and are unable to access mainstream credit. The impact of this financial product on those vulnerable consumers is significant and entrenches financial hardship.

Financial stress can cause mental and physical harm to consumers and their families. A study by researchers from the University of Melbourne found that financial hardship has negative impacts on consumer's physical and mental health and overall quality of life. It also found that its impacts are experienced with greater severity by people who are Centrelink recipients and people with long-term debt problems.¹

¹ Evgenia Bourova et al, 'The Experience of Financial Hardship in Australia: Causes, Impacts and Coping Strategies' (2019) Vol 42, No. 2, *The Journal of Consumer Policy*, 26.

D1Q2 Do you consider that continuing credit contracts, when issued to retail clients in the way described in paragraphs 16–22, have resulted in, or will or are likely to result in, significant detriment other than, or to a greater or lesser extent than, that identified by ASIC? If other or greater detriment, how should the proposed product intervention order be expanded to address this detriment? Please provide any evidence which supports your views.

Legal Aid NSW does not consider that the proposed product intervention order needs to be expanded.

D1Q3 Are you aware of entities other than Cigno and BHFS that are issuing, or likely to issue, continuing credit contracts in the way described in paragraphs 16–22?

No.

D1Q4 Do you agree with our proposal to make an intervention order by legislative instrument prohibiting credit providers and their associates (including directors of such entities) from issuing continuing credit contracts in circumstances where total fees exceed the maximum permitted under the continuing credit exemption and reg 51 of the National Credit Regulations? Please provide details of why, or why not.

Yes. Legal Aid NSW considers that the current product causes financial harm to vulnerable consumers by charging high fees and administrative costs to consumers who are already in acute financial hardship. The proposed intervention aims to reduce the fees and costs that can be charged and would therefore prevent exacerbating debt levels of consumers who are in financial hardship.

D1Q5 What alternative approaches could ASIC take that would achieve our objectives of preventing the detriment to retail clients identified in this paper?

Legal Aid NSW considers this proposal is an efficient approach to meet the objectives of preventing the detriment to consumers identified in this paper.