

Inquiry into credit and financial services targeted at Australians at risk of financial hardship

Legal Aid NSW submission to the Senate Standing Committee on Economics

November 2018

323 CASTLEREAGH ST
HAYMARKET NSW 2000 / DX 5 SYDNEY

Legal Aid 
NEW SOUTH WALES

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 and pro bono legal services. Our community partnerships include 29 Women's Domestic Violence Court Advocacy Services.

The Legal Aid NSW Civil Law Division focuses on legal problems that impact most on disadvantaged communities, such as credit, debt, housing, employment, social security and access to essential social services. Consumer issues constitute the largest category of service for our Civil Law Division, with over 8,000 services in the 2017-18 financial year.

The case studies in this submission have been drawn from the work of our consumer law teams. They have been de-identified to protect the privacy of our clients.

Legal Aid NSW welcomes the opportunity to make a submission to Senate Standing Committee on Economics regarding the *Inquiry into Credit and Financial Services Targeted at Australians at Risk of Financial Hardship*. Should you require any further information, please contact:

Rhiannon O'Donoghue
Solicitor
Combined Civil Law Specialist Team
Phone: 02 9219 5135
E: rhiannon.o'donoghue@legalaid.nsw.gov.au

or

Damien Hennessy
Senior Law Reform Officer
Strategic Law Reform Unit
Phone: 02 4629 2753
E: damien.hennessy@legalaid.nsw.gov.au

Introduction

Legal Aid NSW welcomes the opportunity to provide a submission to the *Inquiry into Credit and Financial Services Targeted at Australians at Risk of Financial Hardship*.

The recent growth of credit and financial services targeting vulnerable consumers at risk of financial hardship has had a significant impact on our work. The products are high cost, and our clients are often exploited by unscrupulous practices. Despite the relatively low value of the transactions, the impact of these credit and financial services on vulnerable and disadvantaged consumers has a significant and disproportionate effect on people experiencing financial hardship.

TOR (a) The impact on individuals, communities, and the broader financial system of the operations of:

(i) payday lenders and consumer lease providers

Legal Aid NSW has previously provided submissions to the Independent Review of the Small Amount Credit Contract Laws (**the SACC Review**),¹ which made a number of recommendations to strengthen protections for consumers accessing short term credit and consumer leases. In 2017, an exposure draft bill was released with provisions to implement the Government's response to the review.

Legal Aid NSW urges the Government to progress implementation of legislated consumer protections in response to the SACC Review as a priority.

Payday Lenders

Legal Aid NSW frequently assists clients in financial hardship who have debts arising from payday loans. In our experience, clients seek out payday lenders in periods of peak financial instability in the absence of other suitable small amount loan providers. Due to payday lenders' fees, clients repay far more than the principal, further entrenching financial hardship. For clients experiencing severe financial hardship, this can create a cycle of dependency on payday lenders. Legal Aid NSW frequently observes payday lenders taking advantage of this relationship in breach of responsible lending obligations, as shown by Rachel's case:

¹ Legal Aid NSW made submissions on the Final Report in May 2016 (https://static.treasury.gov.au/uploads/sites/1/2017/06/C2016-016_Legal_Aid_NSW.pdf) and the Interim Report in January 2016 (http://consumercredit.treasury.gov.au/content/downloads/SACC-submissions/Interim-Report/Legal_Aid_NSW.pdf).

Case Study – Rachel

Rachel is a young, single Aboriginal mother and Centrelink recipient from a remote community. She recently left a relationship during which she experienced domestic violence. Rachel entered seven payday loan agreements with the same provider within a 13-month period. The loan amounts ranged from \$300 to \$1,500. The majority of the contracts were entered the day Rachel completed payment of a previous contract. The majority of the contracts contravened responsible lending obligations. If Rachel had made all required repayments under each of the contracts, she would have paid more than \$2,500 above the total loan amounts.

Our clients' disputes are commonly settled with the lender agreeing to repayment of the principal loan only, with all other fees waived. While this is a positive outcome for our individual clients, we have yet to see any substantive change to lending practices in the industry. We are concerned that people in financial hardship who are not able to access legal advice or financial counselling services are being exploited, trapped in a cycle of high cost payday loans.

Consumer Leases

Legal Aid NSW considers that consumer lease providers should be excluded from Centrepay.

Consumer lease arrangements are common for our clients experiencing financial hardship, especially in regional and remote Aboriginal communities. In these communities, consumer lease providers are often the only source of basic household items, leaving clients at risk of unfair consumer practices by virtue of the providers' monopoly in the market.

Legal Aid NSW is concerned that consumer lease providers frequently engage in misleading and deceptive conduct, especially in relation to the suitability of the lease and the ownership of the goods at the end of the contract. The distinction between sale-by instalment contracts and consumer leases is often artificial, meaning consumer lease providers can draft their contract terms to circumvent the 48% interest cap imposed on sale-by instalment contracts.

The majority of Legal Aid NSW clients who enter into consumer lease agreements are Centrelink recipients and make payments to the consumer lease provider via a Centrepay arrangement. As a result, and as demonstrated by the experiences of Jackson and Rebecca below, our clients are unable to prioritise their immediate financial needs when

necessary, and consumer lease providers are not alerted to times in which clients may be experiencing financial hardship by observing missed payments.

Case Study – Jackson

Jackson is an Aboriginal man in receipt of the Disability Support Pension. He has low literacy levels and lives in a remote community. Jackson entered a consumer lease and paid almost \$11,000 in Centrepay instalments of \$140 per fortnight for household items worth about \$2,500. Jackson was often unable to afford his regular groceries after this payment was taken out. The consumer lease provider cited Jackson's compliance with his payment obligations as evidence that the consumer lease had not created a situation of financial hardship.

Case Study – Rebecca

Rebecca is a young Aboriginal woman with a history of abuse, trauma and disadvantage. She had to leave her housing situation and set up a new home. Rebecca entered into a consumer lease for a lounge set. She did not understand that she would not own the lounge at the end of the lease, or that she would end up paying nearly \$3,500 for goods worth substantially less. Rebecca was only receiving Youth Allowance payments and entered a Centrepay arrangement to pay for the lease. Although this prevented Rebecca from defaulting on her payments, it left her without enough money to meet her basic expenses.

- (ii) unlicensed financial service providers including 'buy now, pay later' providers and short term credit providers

Unlicensed financial service providers

Legal Aid NSW supports the introduction of strong anti-avoidance measures into the National Credit Law to strengthen protection for consumers.

Historically, it was common for the payday lending and consumer lease industry to structure products to circumvent consumer protection laws. While the incidence of this has decreased, particularly after the introduction of the National Credit Law, we continue to see business models designed to avoid consumer protections, in particular the costs cap and responsible lending obligations. Taylor's case study below provides an example of

this. This practice increases the vulnerability of customers and can compound financial hardship and the cycle of dependency on high cost payday loans.

Further, unlicensed financial service providers do not have to participate in external dispute resolution. This is a significant concern where, in the absence of a negotiated outcome, a consumer can only resolve their dispute by litigation. This is difficult and complex for the consumer, and not cost-effective for low value disputes.

Case Study – Taylor

Taylor was in an abusive relationship when her partner fraudulently applied online for a loan in her name. There was limited verification to confirm the identity of the applicant. The loan was for \$175. The loan was unusually structured: the funds were offered by one lender, but the transaction was arranged wholly through an unlicensed financial service provider who would charge a supply fee for their services.

Taylor's partner accessed and withdrew the money from her account while she was in custody. Taylor is now homeless. By the time Taylor had paid off the original loan amount, the fees which had been added to the loan totalled \$875, which is five times the original loan. This amount far exceeds the costs allowable under the National Credit Code. As the financial service provider is unlicensed, it is not a member of any external dispute resolution scheme.

'Buy now, pay later' arrangements

Legal Aid NSW considers that 'buy now, pay later' arrangements are effectively providing credit. We are encountering an increasing number of consumers having problems with 'buy now, pay later' providers, an example of which is Mary's case study below. The products are deceptively easy to obtain, without any need for the provider to verify repayment capacity or observe any other responsible lending obligations. Typically, our clients are financially vulnerable and have signed up to these arrangements at the checkout or online without appreciating the full implications. They later find themselves with large debts they cannot afford to repay and are then saddled with further fees.

Case Study – Mary

Mary is a single woman living in regional NSW with significant mental health issues. She receives the Disability Support Pension and is on the NDIS. Over just a couple of

days when she was very unwell she entered into 'buy now, pay later' arrangements with two different providers for multiple transactions. The total debts exceeded \$600.

Mary did not know how much she had borrowed, and only became aware of the problem when direct debits started coming out of her account, consisting solely of fortnightly social security payments. This left her without money for daily living expenses. Legal Aid NSW attempted to obtain relevant contract documents from the providers to assess the loans, but with no legislative requirement to be provided with such documents, only one provider was willing to provide the documents. Legal Aid was able to refer Mary to a financial counsellor who negotiated suitable repayment plans with the lenders.

In light of these concerns, Legal Aid NSW supports the extension of the National Credit Law to these products, or alternatively, regulation along the lines of existing laws, to require that providers:

- are licensed
- develop financial hardship guidelines
- develop formal dispute resolution processes, including external dispute resolution.

(iii) [debt management firms, debt negotiators, credit repair agencies and personal budgeting services](#)

The experience of our clients with debt management-type businesses has generally been poor. These businesses target consumers who are particularly vulnerable; often overwhelmed by debt, stressed from interactions with debt collectors and desperate for assistance with their finances. However, consumers do not usually appreciate that these high-cost services are provided for profit. Frequently, providers either cannot deliver the desired outcome, or charge for services that the consumer could have conducted themselves with minimal assistance. We have seen many examples of these businesses charging excessive fees for services, and misleading clients about their contracts and the services provided. Examples of this are shown in the cases of Craig and Melissa:

Case Study – Craig

John went to see a debt management company about a phone debt he had incurred. He was quite unwell with various medical conditions due to a recent work accident. His

friend signed the contract on his behalf. John believed that the company would help negotiate a lower debt, and did not understand that they only assisted with 'credit repair'. The company removed a default listing from John's credit report, but the original phone debt remained outstanding. The company also charged Craig for the removal of a negative credit listing from a payday lender, despite the client advising them that he had already repaid the debt and the default had been removed by him 12 months earlier.

The company then commenced legal proceedings against Craig to recover their fees of around \$2,000. Legal Aid NSW was able to assist the client to defend the proceedings in the Local Court, reducing the fees to the repair company to less than half the debt claimed. Legal Aid NSW also negotiated with his phone company to reduce the amount of the debt.

Case Study – Melissa

Melissa has a low level of literacy. She was receiving Newstart and signed up with a budgeting company. She did not read the contract and was just shown where to sign. She was initially told that she could pull out at any time and would not incur any fees. However, when she attempted to terminate the contract, the company refused, informing her that a deferred establishment fee of nearly \$2,000 had to be paid. Legal Aid NSW was able to negotiate a release from the contract without payment of any fees. On review of her documents, it was discovered that the budgeting company had failed to assess Melissa's obligation to repay a number of payday loan debts which should have been disputed.

Legal Aid NSW supports regulation of the debt management industry to address these systemic consumer concerns. This regulation would provide:

- A requirement that the industry be licensed, including standards to ensure services offer high quality advice from qualified staff
- A ban on upfront fees for services
- A requirement for external dispute resolution through the Australian Financial Complaints Authority
- A requirement that businesses inform consumers of free options which could assist a consumer, such as financial counsellors, hardship programs, and external dispute resolution.

The debt management industry is able to exploit financially vulnerable consumers because there is a high need for assistance that is currently not being met by the current number of free financial counselling services. Legal Aid NSW also supports further funding for these valuable, specialist services to meet the growing need for people in financial hardship.

TOR (b) whether current regulation of these service providers meets community standards and expectations and whether reform is needed to address harm being caused to consumers

We have outlined above where the current regulation of financial services and products the subject of this inquiry are inadequate, and have made recommendations for reform.

TOR (c) the present capacity and capability of the financial counselling sector to provide financial counselling services to financially stressed and distressed members of the community

Legal Aid NSW considers the current level of available financial counselling services is inadequate to meet the needs of financially stressed and vulnerable members of the community. We highlight below three areas in which this is apparent.

Aboriginal Communities

Legal Aid NSW currently employs a financial counsellor to work with clients of the Civil Law Service for Aboriginal Communities (**CLSAC**). CLSAC provides place-based outreach services to over 20 communities in New South Wales. Since the role was created in March 2016, the financial counselling service has resulted in a total waiver or reduction in debts of \$196,494.38. Where debts are unable to be waived, the financial counsellor assists clients to identify suitable repayment arrangements, as seen in the case of Michelle:

Case Study – Michelle

Michelle is a single Aboriginal mother who escaped from a domestic violence relationship. Michelle experienced severe financial hardship as a result of a number of debts to various bodies including telecommunications providers, utility providers, payday lenders and consumer lease providers. The CLSAC financial counsellor was able to secure waivers totalling over \$12,500 for Michelle, and negotiate suitable payment plans for other outstanding debts.

However, the number of clients to whom we can provide this service is necessarily constrained. With additional funding, Legal Aid NSW could provide this service to more clients in communities across the state. In our experience, clients in financial hardship benefit from a multidisciplinary approach to their problems. In CLSAC, the skills of the financial counsellor and lawyers are leveraged to obtain outcomes for clients in the most effective and efficient way.

In the majority of communities in which CLSAC works, no local financial counselling service is available. In some areas, the Rural Financial Counselling Service is available for local farmers and small business owners, but this does not extend to other members of the community. Financial counsellors working for this service have spoken with CLSAC to take client referrals, but they do not have the remit or resources to assist.

While the CLSAC financial counsellor visits most of the communities a few times per year, there is no capacity to provide the ongoing assistance many clients would benefit from, as can be seen in John's case:

Case Study – John

John is an Aboriginal man in a remote community with multiple debts arising from different electricity contracts. As some of these debts had entered collection stages with third party agencies, John was often uncertain about the source of his debts. On being contacted by debt collectors, John agreed to unsuitable repayment plans and experienced financial hardship. Although John met with the CLSAC financial counsellor, he was often difficult to contact by phone and unable to give a clear overview of his financial situation. Consequently, his financial distress escalated between the times he was able to meet with the financial counsellor in person.

Expanding the number and network of financial counsellors, particularly in regional and remote areas, would offer several benefits, including:

- Providing ongoing assistance to clients through regular contact and consistent relationship, allowing for early intervention in management of key debts
- Promoting awareness of alternative financial products, such as the No Interest Loan Scheme, minimising the risk of consumers engaging with payday lenders or consumer lease providers
- Identifying key financial issues within communities to deliver tailored financial literacy programs

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- Increasing access to the education and supports necessary to prevent financial hardship
 - Protecting vulnerable consumers from exploitation by the debt management industry.

Prisoners

Legal Aid NSW supports additional funding for financial counsellors to provide services in prisons, and greater access to those services for prisoners.

People currently in prison form an especially vulnerable segment of the community. Legal Aid NSW's Prisoners Legal Service (**PLS**) works exclusively with prisoners to address their criminal, family and civil law matters.

Many prisoners enter custody with debts that compound during their time in custody, and they then later leave in a worse financial position than when they entered. This is highlighted in the Financial Counselling Australia report, 'Double Punishment: How people in custody pay twice' (May 2018)².

The majority of clients assisted by the PLS are suffering financial hardship. There are a number of factors which contribute to financial vulnerability of prisoners, including:

- Lack of access to the internet and limited telephone access. Prisoners are unable to contact creditors to manage their debts and financial obligations, and if they can, they generally do not have the necessary reference numbers and paperwork to speak with the service provider
- Centrelink benefits are suspended when a prisoner enters custody, so prisoners quickly default on direct debits, resulting in dishonour fees and accumulating interest
- Lack of access to identification documents in custody so prisoners cannot apply for a copy of their credit report
- Prisoners are generally more likely to be excluded from mainstream financial products both prior to entering custody and upon release, and are more likely to be reliant on payday lenders and consumer leases.

Unfortunately, our experience is that the present capacity and capability of the financial counselling sector to provide services to this vulnerable group is significantly under-

² <https://www.financialcounselingaustralia.org.au/getattachment/Corporate/Publications/Reports/Double-Punishment-Final.pdf>

resourced. The PLS has found it very difficult for their clients to access financial counselling services while in custody.

Legal Aid NSW's Cooperative Legal Service Delivery (**CLSD**) Program has provided limited one-off funding to the Lifeline South Coast Financial Counselling Service to support outreach by a financial counsellor to the South Coast Correctional Centre. This outreach complements a civil law outreach service to the correctional centre that is provided by the Legal Aid NSW Nowra Regional Office. Regular outreach by a civil lawyer and a financial counsellor assists prisoners to address financial problems at an early stage and supports them to transition to life outside of prison. However, the CLSD Program is not in a position to provide ongoing funding for this service at the South Coast Correctional Centre, and it is likely that the service will not be able to continue without additional support. Financial counsellors from the Salvation Army attend other centres, primarily at the complexes at Windsor and Silverwater, but the vast majority of correctional centres are currently not being serviced by financial counsellors. The overall result is that financial and legal issues, which could be addressed at an early stage, compound and become more complex.

Debt and financial stress contribute to the risk of recidivism for an individual released from custody, and prisoners would benefit greatly from having access to financial counselling services while in custody. The nature of custodial settings and the various security and safety requirements that need to be met prior to entering a facility is a significant impediment to providing financial counselling services in custody. However, each correctional centre has opportunities to facilitate various services including the provision of financial counselling.

Work and Development Order recipients

In New South Wales, disadvantaged people with accumulated fines, including people in serious financial hardship, can clear their debts by undertaking certain approved beneficial activities, including seeing a financial counsellor. This is called a Work and Development Order (**WDO**), and must be approved by Revenue NSW and supported by an eligible sponsor organisation. Legal Aid NSW's specialist Fines and WDO Service helps clients with fine debts to obtain a WDO, and that also assists service providers to become approved WDO sponsors. The Service is dedicated to assisting clients with complex needs including people experiencing acute financial hardship, homelessness, mental illness, addiction, cognitive impairment or intellectual disability. It prioritises clients with limited capacity to self-help. Aboriginal clients consistently represent over 20% of all clients assisted as a result of targeted outreach to Aboriginal communities in partnership with other stakeholders.

Access to financial counsellors is of significant benefit to our WDO clients to help them budget and gain valuable financial literacy skills. However, we have found that, although many financial counselling services are approved sponsors, they are often overwhelmed

with requests. For example, western Sydney has the highest Indigenous population in NSW, yet as far as Legal Aid NSW is aware there is only one Indigenous financial counsellor for the whole area. This often means that financial counsellors must limit their assistance and not provide a program of complete assistance to a WDO client, making the assistance of limited benefit and appeal to the client.