Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry

Response to the Interim Report

Submissions by Consumer Credit Legal Service (WA) Inc.

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1 Introduction

CCLSWA previously provided substantive submissions to the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (**Royal Commission**) in July 2018 and supplementary submissions in relation to insurance in September 2018 and October 2018. Accordingly, CCLSWA now welcomes the opportunity to make a submission in response to the Interim Report released in September 2018.

The following organisations have contributed to and endorsed this submission:

- Financial Counselling Network (**FCN**)
- Financial Counsellors' Association of Western Australia
- Community Legal Centres Association (WA)

Details about each contributing organisation are contained in Appendix A.

2 About Us

CCLSWA is well placed to provide the Royal Commission with insight into, and information on, how Western Australian's engage with financial services entities (**FSE**).

CCLSWA is a not-for-profit specialist community legal centre based in the Perth metropolitan area. CCLSWA advises and advocates for consumers on consumer credit issues and Australian Consumer Law related problems.

CCLSWA operates a free telephone advice line service which allows consumers to obtain information and legal advice in the areas of banking and finance and consumer law. CCLSWA provides ongoing legal assistance to consumers by opening case files when the legal issues are complex and CCLSWA has capacity to do so.

CCLSWA also provides:

(1) assistance to financial counsellors and other consumer advocates who work closely with disadvantaged and low-income individuals for the resolution of their credit and debt related problems;

(2) community legal education programmes relating to credit and debt issues, and the Australian Consumer Law including financial literacy programmes to high school students and select groups within the community;

(3) contributions to relevant policy and law reform initiatives; and

(4) a training and supervision program for law students and graduate volunteer paralegals.

In providing these services, CCLSWA aims to create awareness, knowledge and understanding of consumer issues relating to FSE's, and the Australian Consumer Law. CCLSWA's mission is to support the community by educating people about, and advocating for, their consumer and financial rights.

CCLSWA also works in conjunction with a number of other consumer advocate groups in providing these services and also collaborates by sharing our clients' experiences of FSE misconduct. One such relationship is our relationship with **FCN**.

During the 6 months to June 2018 the FCN scheduled 4,224 appointments and worked with 3,219 clients across 2,742 cases.

Acts of bankruptcy remain a preferred option for many clients presenting to members of the FCN. This is reflected by the level of total presenting debt the financial counsellors are seeing, which increased to $318,434,366 (from $261,253,468) over the period. A majority of these debts consist of home loans, credit card debt, and personal loans. Clients continue to have an inability to meet basic living costs while servicing these debt repayments. Many clients seeking financial counselling are impacted by unforeseen changes to personal circumstances and loss of employment.

- 80% of clients presented with an issue relating to managing on a low, restricted or inadequate income
- 82% of clients presented with issues relating to debt (loans, payday lenders, credit cards)
- 27% of clients presented with an issue related to mortgages
- 11% of client presented about bankruptcy
- 8% of clients were referred by FSEs

We have incorporated case studies as examples of our experience. In most of the case studies we have not named the FSE's in order to protect our client's confidentiality. We have also made most of the FSE's anonymous as some matters are ongoing and others are subject to

confidentiality agreements. If the Royal Commission would like to know the name of or further detail on a particular case study, CCLSWA and FCN can approach the relevant agency and/or client and seek his or her permission for those details to be provided.

We have, however, consciously identified Sovereign Finance and Sovereign Insurance as a provider of particular concern in WA.

3 Consumer Lending

The following issues will be considered with a focus on the role as caryard intermediaries, as they are the predominant group of intermediaries on which CCLSWA provides advice. We will consider the role of other classes of intermediaries in consumer lending drawing on the experiences of clients from the FCN.

What duties does an intermediary owe to a borrower?

What duties should an intermediary owe to a borrower?

3.1 In our experience employees of car yards can act as intermediaries for both credit providers and for insurance providers.

3.2 Intermediaries are considered credit assistance providers under the *National Consumer Credit Protection Act 2009* (Cth) (**NCCP Act**).

3.3 The duties that an intermediary owes to a borrower are set out under the NCCP Act. These are the duties that an intermediary should owe to a borrower. Under the NCCP Act, credit assistance providers must:

(1) give a credit guide to a consumer (s 113 NCCP Act)

(2) give a quote to the consumer which must be signed and dated by the consumer before the intermediary can provide credit assistance to a consumer (s 114 NCCP Act)

(3) before providing credit assistance to the consumer, make a preliminary assessment as to whether the credit contract will be unsuitable for the consumer (s 115 NCCP Act)

(4) in determining whether a credit contract is unsuitable the credit assistance provider must make (s 117 NCCP Act)

(a) reasonable inquiries about the consumer's requirements and objectives in relation to the credit contract;

(b) reasonable inquiries about the consumer's financial situation; and

(c) take reasonable steps to verify the consumer's financial situation.

(5) provide the consumer with a proposal disclosure document which sets out details of any fees or charges and commission that the consumer will be required to pay to the intermediary (s 121 NCCP Act)

(6) the intermediary cannot provide credit assistance to a consumer in relation to a credit contract if the contract is unsuitable for the consumer (s 123 NCCP Act)

(7) the intermediary is prohibited from suggesting to a consumer that they remain in a particular credit contract that is unsuitable for the consumer (s 124 NCCP Act)

(8) the court is allowed to make orders to remedy unfair or dishonest conduct by credit service providers (s 180A NCCP Act).

3.4 The credit providers are then required to make a final assessment of unsuitability.

3.5 The Australian Securities & Investments Commission (**ASIC**) Consultation Paper 294 (**CP294**) notes that most sales of add-on insurance products are made by authorised representatives of the insurer located in car dealerships. Some car dealers refer consumers to finance brokers who can arrange the car loan and sell add-on products. These brokers may be located at or near the dealership, or may deal with the consumer by phone or email without face to face contact.[1]

3.6 Add-on insurance products sold by car-yard intermediaries are also typically sold using a 'no advice' or 'general advice' model which means that the intermediary seller is not obliged to select or recommend a product based on the needs of the consumer. Therefore, the intermediary can promote the sale of products based on the commissions they may earn. [2]

3.7 Even though an intermediary has made a preliminary assessment the lender is obliged to carry out their own assessment of suitability. However in our experience lenders regularly rely on the assessment of intermediaries in making their final assessments.

3.8 The case study below demonstrates how intermediaries in failing to make proper preliminary assessments are failing in their duties to both the lender and the borrower.

Case study: Catherine's story

Catherine and her ex-partner had a meeting with a financial counsellor (FC).

The ex-partner had bought a property in Wellard when Catherine was pregnant with their first child. When she fell pregnant with their second child they moved out and rented the Wellard property to tenants while they stayed in alternate accommodation.

As a couple, they took out an equity loan against the Wellard property to purchase a property in Success in 2014. When they got the equity loan they refinanced with another bank through a broker and ended up with a three tiered high interest structured loan.

The ex-partner is on the title for Wellard and the client and ex-partner are on the title for the Success property.

[1] https://download.asic.gov.au/media/4422973/cp294-published-24-august-2017.pdf
[2] Ibid, p 10.

The status of the three loans is as follows;

- No Fee Investment Home Loan Balance $200,000 - 2 months arrears
- Rate Saver Investment Home Loan Balance $57,000 - 2 months arrears
- No Fee home loan Balance $385,000 - 2 months arrears

All three are on interest only under hardship.

The relationship between the couple ended in May 2015.

The couple got divorced and the Family Court property settlement proceedings were concluded in 2016. Catherine got the Success property and the ex-partner got the Wellard property. The titles were not changed as they did not have the funds to do so.

The client and her father went to a real estate agent to check the current market value of both properties and were told the properties would be sold at a loss. The client does not want to declare bankruptcy but can see no other solution.

During the discussion with the FC it was revealed that the ex-partner's redundancy occurred two days before the new loan restructure was approved in 2014 and the broker was aware the couple no longer had capacity to make repayments but advised them not to inform the bank.

The loans are not being serviced, are in arrears by 60 days and there appears to be nothing in the short term future that will change their financial situation for the better. The FC received the documents relating to the loans, Landgate, Caveat and Family Court proceedings.

After seeking advice, FC found the actions of the broker were questionable and the broker should have notified the bank of the change in the couple's financial situation. The advice received indicated that the viability of the three-loan structure was certainly undermined by the ex-partner losing his job and the broker should have notified the bank. There were emails between the couple and the broker and FC discussed the client's options to make a formal complaint via the banks Internal Dispute Resolution process and then the Financial Ombudsman Service (FOS) if the outcome was in question.

As the bank was not made a third party to the Family Court order this meant the bank could act under its contract irrespective of the Family Court orders as the Family Court orders only bind the client and the ex-partner.

The client's first priority was to keep a roof over her and her children's heads, and food on the table. In the longer term, she may be able to make a claim against the bank for failing in its responsible lending obligations.

Considering where she began and her concerns of being homeless and having to go bankrupt, the information and options provided by the financial counsellor saw her in a significantly more powerful position. She was also referred to get independent legal advice.

Source: Financial Counselling Network

3.9 The following case study demonstrates how intermediaries often do not uphold their duties to the client in acting as a credit assistance provider.

Case Study: Sandra's story

An elderly client, Sandra, was new to the service and had self-referred after experiencing difficulties surviving on the Age Pension. Sandra had attempted to add to her income by seeking employment and after a number of unsuccessful attempts felt that she should look at other avenues to assist her living within her budget and remaining in her own home.

Sandra is paying a mortgage and all related costs for the property she resides in, however, the property is not considered her asset. After visiting a mortgage broker with her son and sinking all of her savings of $150,000 (proceeds of downsizing) into the property purchase, the ownership of the property is in her son's name only with the understanding that she covers all the costs directly for a $310,000 mortgage. Additionally, as the property is not in Sandra's name she is unable to claim any senior concessions surrounding council and water rates. On further advice from the broker, she does not claim or receive rent assistance from Centrelink as her mortgage payments would be classed as income for her son and he would have to claim this with the Australian Taxation Office. Sandra vehemently denied any wrongdoing on the part of her son and genuinely felt that together they had received and acted upon inadequate advice.

Although Sandra was vehement in her denial of any wrongdoing on her son's part, the FC had a delicate discussion around the reality of her financial circumstances and gently encouraged making contact with Advocare for information and resources on options available to someone in the client's position.

Source: Financial Counselling Network

3.10 The above case study is also illustrative of the failure of the 'not unsuitable' test protecting vulnerable consumers and ensuring that lenders and intermediaries turn their mind to the suitability of the credit contract rather than the limited definition of unsuitability. The test of 'not unsuitable' will be discussed later in these submissions.

How can entities' systems be improved to detect and prevent breaches of responsible lending obligations by intermediaries?

Who should be responsible for the intermediary's defaults?

3.11 We recommend applying the following:

(1) enhanced training and supervision by product providers;
(2) sale of products should be driven by consumer demand and need rather than the financial benefits that can be earned by the caryard intermediary;
(3) adequate arrangements to avoid conflict of interest;
(4) FSEs/ insurers should have reasonable controls in place to prevent car yard intermediaries engaging in unfair conduct at the point of sale and should be able

to effectively identify and compensate consumers who have been sold add-on products as a result of such conduct; and

(5) providers should adopt improved sales processes which take into account behavioural biases and other factors that currently inhibit or prevent consumers from making informed purchasing decisions.

What should be disclosed to borrowers about an intermediary's obligations to the lender and to the borrower?

3.12 We recommend the following disclosures by an intermediary about their obligations to the lender and to the borrower:

(1) whether they are an agent for the lender;

(2) what remuneration/commission is paid to the intermediary; and

(3) avenues for complaint for the borrower.

3.13 We would also recommend that providers of add-on insurance and their intermediaries disclose to the consumer:

(1) the likelihood of an insured event happening;

(2) the likelihood of a claim being accepted or rejected;

(3) the amount that may be paid in the event of the claim;

(4) the usual time the insurer takes to decide a claim;

(5) the usual time the consumer takes to respond to complaints; and

(6) the value of the product.

3.14 In our experience, the issue is often not the content of the disclosure that is made, but the way in which it is made.

3.15 Our experience shows that the process is often long and complicated, meaning that consumers often experience 'information overload'.

3.16 CCLSWA has a number of clients from culturally and linguistically diverse backgrounds who were not given adequate explanation and assistance taking into consideration their individual circumstances. (See Darren's story below, and Sue's story at para 3.59).

3.17 CCLSWA also has experience with clients who have a particular vulnerability or disability where information has not been disclosed in a manner that they would understand.

Case study - Darren's story - C992073

Darren comes from a culturally and linguistically diverse background. Darren is a Sudanese refugee and spent his childhood from age seven until 16 in a Kenyan refugee camp. He had no formal schooling, and cannot read or write in English, although he can communicate in spoken English. He has limited family support, with the sole family member in Australia being one older male cousin.

In 2012 Darren purchased a Jeep for about $32,000 from a Perth dealer with a loan from Carz 4 U. There is no evidence that Carz 4 U made their own final assessment of Darren's ability to repay the loan.

About 1 month later he returned the car in order to change it for a different colour. The dealership said that this would be OK and allowed him to exchange the car for a more expensive car. The second car was worth about $39,000.

On leaving the dealership Darren thought that the loan would be for 5 years for a total of $62,000. This was based on things he was told by employees of the dealership. There was nothing in writing to this effect. Darren was then told by Carz 4 U that he actually had a 7 year loan worth in total around $91,000.

Darren had a contract from the first loan, and he signed a new document for the second car but was not given a copy.

Darren told the dealership that he had trouble reading English and needed the loan explained to him. He only received advice from people at the dealership.

He was encouraged to obtain finance through the dealership and not independently.

CCLSWA obtained documents in relation to the loans and found the cost of the first loan was added to the second car loan without the client understanding what was happening.

CCLSWA was able to negotiate a reduced loan amount with the lender.

Source: CCLSWA

Financial Service Entities generally

What steps, consistent with responsible lending obligations, should a lender take to verify a borrower's expenses?

3.18 In line with ASIC Regulatory Guide 209 (**RG 209**) at 209.32 we believe that at a minimum lenders should take the following steps to verify a consumer's expenses:

(1) Fixed expenses

(a) cost of accommodation (rent/ home loan repayments/ board etc)

(b) repayment of existing debts

(c) child support

(2) Variable living expenses
    (a) food
    (b) utilities
(3) age and number of dependants
(4) any particular or unusual circumstances
(5) discretionary expenses
    (a) take-away food
    (b) gambling
    (c) telephone, internet, pay TV and media streaming subscriptions
    (d) medical and health
    (e) child care and education

3.19 In applications for credit where a consumer assesses their own expenses, if any of the required expenses are listed as being $0 by the consumer then the lender should require the consumer to give an explanation for that figure.

3.20 We would recommend at a minimum that lenders be required to obtain bank statements for the previous 90 days before the application was made for the bank account into which the consumer's income is deposited. This is in line with the obligations that are placed on small amount credit contract providers and would establish a minimum requirement for lenders in taking steps to verify a borrower's expenses.

Do the processes used by lenders, at the time of the hearings, to verify borrowers' expenses meet the requirements of the NCCP Act? Do the processes now used meet those requirements?

3.21 The requirements under the NCCP Act for lenders to verify borrowers' expenses are limited to Division 6 – Prohibition on suggesting or assisting with, unsuitable credit contracts which outlines that for the purposes of determining whether a credit contract will be unsuitable a credit provider can take into account information about the consumer's financial situation, requirements or objectives.

3.22 Verification requirements are therefore not onerous. The lender is only required under the NCCP Act to make 'reasonable inquiries' about a consumer's financial position. We believe that the requirements for 'reasonable inquiries' gives lenders unwarranted latitude as to what inquiries they need to make. We consider that it is not a scalable obligation depending on the level of credit being provided, as even small loans can put a borrower into financial hardship.

3.23 Much of the guidance on what steps the lenders need to take in order to verify a consumer's expenses are contained in ancillary documents and guidelines, and not within the NCCP Act.

3.24 For example, as cited above, RG 209 sets out what reasonable inquires about a consumer's financial situation will generally include. We submit that there needs to be a baseline by which to judge what is reasonable.

3.25 Whilst we advocate for a minimum requirement for what is 'reasonable inquiries', even where there are minimum requirements for lenders in verifying a consumer's expenses, they are not always complied with. Therefore, there also needs to be increased repercussions for lenders when they fail to make reasonable inquiries and comply with their responsible lending obligations.

3.26 For example, lenders who provide small amount credit contracts (**SACCs**) under s130 of the NCCP Act are required to obtain bank statements for the preceding 90 days. Whilst this guidance is useful in assisting lenders to comply with their responsible lending obligations, in CCLSWA's experience lenders still neglect these responsibilities.

3.27 Ryan's story shows how lenders have failed to comply with their responsible lending obligations under the NCCP Act, with little to no repercussions for the delinquent lenders. Although Ryan's story relates to SACC lending, it highlights that even where there is a minimum requirement for lenders to obtain statements, and follow responsible lending obligations, they are not, or are only partially, complied with.

Case study – Ryan's story – C995252

Ryan was a 25 year old electrician who suffered from a serious gambling addiction. Ryan underwent counselling for his addiction and granted his mother enduring power of attorney to deal with his legal and financial affairs.

Ryan instructed CCLSWA to obtain documents in relation to his various SACCs. CCLSWA provided Ryan with advice on our assessment of the documents provided which indicated the various SACC lenders failed to comply with their responsible lending obligations as follows:

SACC Lender 1

Account	Suitability Assessment	Verification of financial situation	Verification of objectives & requirements	Bank statements previous 90 days	No of defaults under other SACCs	Total no. of SACC in previous 3 months
1	X	✓	X	✓	0	2
2	X	✓	X	✓	1	10
3	X	✓	X	✓	1	11
4	X	✓	X	✓	2	10
5	X	✓	X	✓	1	12
6	X	✓	X	✓	2	15

SACC Lender 2

Account	Suitability Assessment	Verification of financial situation	Verification of objectives & requirements	Bank statements previous 90 days	No of defaults under other SACCs	Total no. of SACC in previous 3 months
1	✓	✓	X	✓	0	8
2	✓	✓	X	✓	1	12
3	✓	✓	X	✓	0	10
4	✓	✓	X	✓	0	16
5	✓	✓	X	✓	2	8
6	✓	✓	X	✓	4	8

SACC Lender 3

Account	Suitability Assessment	Verification of financial situation	Verification of objectives & requirements	Bank statements previous 90 days	No of defaults under other SACCs	Total no. of SACC in previous 3 months
1	✓	✓	X	✓	1	9
2	✓	✓	X	✓	2	12
3	✓	✓	X	✓	5	9
4	✓	✓	X	✓	2	7

SACC Lender 4

Account	Suitability Assessment	Verification of financial situation	Verification of objectives & requirements	Bank statements previous 90 days	No of defaults under other SACCs	Total no. of SACC in previous 3 months
1	✓	✓	X	✓	0	4
2	✓	✓	X	✓	0	8
3	✓	✓	X	✓	2	11
4	✓	✓	X	✓	2	9
5	✓	✓	X	✓	2	9
6	✓	✓	X	✓	1	10
7	✓	✓	X	✓	1	15
8	✓	✓	X	✓	4	10
9	✓	✓	X	✓	4	8
10	✓	✓	X	✓	5	11
11	✓	✓	X	✓	5	13
12	✓	✓	X	✓	3	7

SACC Lender 5

Account	Suitability Assessment	Verification of financial situation	Verification of objectives & requirements	Bank statements previous 90 days	No of defaults under other SACCs	Total no. of SACC in previous 3 months
1	✓	✓	X	✓	5	7

SACC Lender 6

Account	Suitability Assessment	Verification of financial situation	Verification of objectives & requirements	Bank statements previous 90 days	No of defaults under other SACCs	Total no. of SACC in previous 3 months
1	✓	X	X	X	3	7

SACC Lender 7

Account	Suitability Assessment	Verification of financial situation	Verification of objectives & requirements	Bank statements previous 90 days	No of defaults under other SACCs	Total no. of SACC in previous 3 months
1	✓	X	X	X (only 60 days)	0	0
2	✓	X	X	X (only 60 days)	0	6
3	✓	X	X	X (only 60 days)	5	9
4	✓	X	X	X (only 60 days)	5	14

SACC Lender 8

Account	Suitability Assessment	Verification of financial situation	Verification of objectives & requirements	Bank statements previous 90 days	No of defaults under other SACCs	Total no. of SACC in previous 3 months
1	✓	X	X	X	0	2
2	✓	X	X	X	0	7
3	✓	X	X	X	2	11
4	✓	X	X	X	1	11
5	✓	X	X	X	1	16

SACC Lender 9

Account	Suitability Assessment	Verification of financial situation	Verification of objectives & requirements	Bank statements previous 90 days	No of defaults under other SACCs	Total no. of SACC in previous 3 months
1	X	✓	X	✓	0	3
2	X	X	X	X	1	13
3	X	X	X	X	1	15
4	X	X	X	X	5	9

SACC Lender 10

Account	Suitability Assessment	Verification of financial situation	Verification of objectives & requirements	Bank statements previous 90 days	No of defaults under other SACCs	Total no. of SACC in previous 3 months
1	X	X	X	X	0	5
2	X	X	X	X	5	12

Source: CCLSWA

3.28 Additionally, the test of making 'reasonable inquiries' does not place any onus on the lender to make additional inquiries should any of the information raised in their initial inquiry appear inconsistent or raise any 'red flags' so long as the initial inquiry was 'reasonable'.

3.29 Furthermore, the information obtained by lenders ought to be assessed more thoroughly. That assessment may take the form of lenders 'double checking' their own assessments. There may be a system in which high risk circumstances are automatically flagged and this flag prompts the lender to make further inquiries of the consumer. High risk circumstances that may lead to a flag being raised include advanced age, low levels of savings or the consumer having a certain number of other credit products.

3.30 Beverly's story below demonstrates how if a 'red flag' had been investigated, unsuitable credit may not have been provided to a consumer.

Case study - Beverly's story – C993977

Beverly was 68 years old and self employed when she obtained a $650,000 home loan from Lender. The home loan was interest only for a term of 10 years, with a final lump sum payment of just over $650,000 due at the end of the term.

Beverly utilised approximately $400,000 of the home loan. The interest only repayments were made from the remaining "available funds" until insufficient funds remained whereupon she received a default notice.

Beverly did not understand why she received the default notice. She did not understand the concept of "interest only" and was not aware that she would be required to pay back the loan in one large lump sum.

The Lender knew, or ought to have known that Beverly could not repay the home loan without selling her home and accordingly the presumption of substantial hardship arises.

CCLSWA assisted Beverly to bring her dispute to the relevant Ombudsman scheme. The matter is ongoing.

Source: CCLSWA

Should HEM continue to be used as a benchmark for borrowers' living expenses?

3.31 It is our view that the Household Expenditure Measure (**HEM**) should not be used as a benchmark for borrowers' living expenses.

3.32 HEM does not accurately reflect the consumer's actual expenses and ability to service a loan. HEM is a measure that reflects a modest level of weekly household expenditure for various types of families.

3.33 HEM was not intended for use by FSE's to verify a borrower's living expenses. HEM is a benchmark that estimates household spending based on the ABS household expenditure survey.

3.34 HEM has previously been criticised for underestimating individual's expenses with Australian Prudential Regulation Authority labelling HEM as "too simplistic".

3.35 Therefore it is not an appropriate benchmark for FSE's to use in assessing a borrower's living expenses.

3.36 Responsible lending laws are designed to ensure that lenders have regard to all relevant information about a borrower and their financial situation before approving a loan.

3.37 Therefore, to comply with their responsible lending obligations, FSE's should be making material inquiries into the consumer's actual living expenses to see if the credit is suitable.

Is the offer of a credit limit increase, where the customer has consented to receive such marketing, consistent with the NCCP Act obligation not to provide credit that is not unsuitable for the customer, having regard to their requirements and objectives?

Is the offer of a credit limit increase based only on information held by the bank about a customer a breach of the NCCPA Act obligation to take reasonable steps to verify the consumer's financial situation?

3.38 It is our experience that consumers expect that FSE's will not suggest products to consumers that they cannot afford. In our view, if/when FSE's suggest such products to consumers they may be in breach of NCCP Act s 114(1).

3.39 The consequences of FSE's offering unsolicited credit, or increasing a credit limit based solely on existing information about a customer is outlined in Trish's story below.

Case study – Trish's story – C993805

Trish was employed as a management assistant on a full time basis. Despite her full time employment, Trish often found herself in a position of financial hardship and had previously utilised the services of a financial counsellor.

Personal Loan (Lender A)

In 2004 Trish and her then partner obtained a loan from Lender A.

This loan had been rolled over a total of 12 times as at May 2017. The most recent rollover CCLSWA was aware of occurred in November 2015 for the amount of $14,800 solely in Trish's name. This loan was secured over her car.

The balance of the rollover at May 2017 was about $13,400.

Credit card

In 2007 Trish obtained a credit card from Lender B with a limit of $3,000.00. Over the next few years, the credit limit of the card was gradually increased to $22,000.00 as at 24 December 2015.

Trish had overdue payments on her credit card since 4 May 2016. The balance at May 2017 was over $23,400, consisting mostly of interest.

With the assistance of a financial counsellor, Trish negotiated to pay off the remaining balance interest free over a seven year term.

Home loan

In or around November 2012 Trish approached Lender B to apply for a home loan. Trish cannot recall what specific enquiries Lender B made when assessing her home loan application, but she does recall Lender B asking about her expenses.

Trish was approved for the home loan in the amount of about $450,000. Under the home loan contract Trish was to pay interest only for the first 5 years with monthly repayments of approximately $1,900.

Trish used the proceeds of the loan to purchase a house and land package that she intended to rent out once construction was complete.

Trish was unable to find tenants for the property and without receiving rental income, she was unable to meet her repayments on the loan and fell into default on numerous occasions.

Each time Trish fell into default she was granted a temporary hardship variation but was never offered a long term repayment arrangement.

With the help of a financial counsellor, Trish eventually managed to negotiate time to sell the property in order to pay out the home loan. The house sold and the home loan was paid out.

Personal loan (Lender B)

In August 2014 Trish obtained a personal loan from Lender B. Trish was initially seeking $16,000 to buy a car. Lender B told her that she was eligible for up to $50,000 but that her credit card with Lender B might make it difficult for her to obtain the personal loan.

Lender B offered her the $50,000 personal loan on the proviso that part of the proceeds of the personal loan would be used to pay off her credit card debt, her credit card limit would be reduced and her personal loan with Lender A would be paid out. Trish agreed to this and received the $50,000 personal loan. $24,000 was used to purchase a car, $15,000 was applied to the credit card debt and the remainder was used to pay for a holiday.

At the time Trish was making repayments on her personal loan with Lender A of about $950 a month.

Outcome

CCLSWA made a complaint to FOS on behalf of Trish in respect of the personal loan with Lender A. The loan balance was amended to $7,500 and was payable without interest and fees over a term of three years.

CCLSWA lodged a claim for breach of responsible lending on the client's behalf with FOS in respect of the home loan, personal loan and credit card taken out with Lender B.

As a result Trish received a refund of approximately $90,000 for the home loan, however was still liable to repay the personal loan and credit card.

After all the accounts with Lender B were settled, Trish received a cash refund of over $45,000 from Lender B.

Source: CCLSWA

3.40 We suggest that FSEs be required to obtain more information from consumers prior to providing credit or credit assistance in order to ensure that the credit is suitable regardless of whether the consumer is a previous customer of the FSE and the FSE has previous information about the consumer. Relying on outdated information does not adequately discharge the FSE's responsible lending obligations as the consumer's situation may have significantly changed since the previous application for credit.

3.41 Updating the requirements to obtain updated information before offering new credit or an increase in credit may be achieved through an update to ASIC Regulatory Guide 209 Credit Licencing: Responsible lending conduct, or by incorporating requirements under ASIC RG 209 into legislation.

Should the test to be applied by the lender remain 'not unsuitable'? How should the lender assess suitability?

3.42 Under the current law, before providing or advising consumers, holders of Australian Credit Licences must:

(1) make reasonable enquiries about the borrower's financial circumstances;
(2) make reasonable enquiries about the borrower's requirements and objectives;
(3) assess the customer's capacity to repay the proposed loan without substantial hardship; and
(4) not suggest or offer products that are unsuitable.

3.43 There is a presumption that if the consumer could only comply with the terms of the loan by selling their principal place of residence, then the consumer could only meet the obligations of the loan under substantial hardship.

3.44 A loan must be assessed as 'unsuitable' if:

(1) the consumer will not be able to pay at all, or not without substantial hardship and/or
(2) the loan does not meet the consumer's requirements and objectives.

3.45 It is our experience that the phrasing of the credit as being 'not unsuitable' is confusing to the consumer.

3.46 Whilst we acknowledge that 'unsuitability' is easier to define than 'suitability'. It is our submission that suitability should be assessed in the consumer's individual

circumstances and in relation to the amount and type of credit sought, therefore making it a better test than a blanket test of 'unsuitability'.

3.47 It is CCLSWA's experience that FSE's do not always comply with the responsible lending obligations as set out under the NCCP Act and the National Credit Code (**NCC**). It is our submission that the negative phrasing of the obligation results in less stringent application of the test for responsible lending.

3.48 We would encourage a positive obligation for FSEs to find that credit is suitable for the individual using the established considerations.

3.49 Ryan's story below, and which we also refer to at 3.27 above, shows how responsible lending obligations are not being complied with, resulting in credit being provided which is unsuitable. There were a number of red flags in Ryan's case that if the test had been whether the credit was suitable, this may have meant that his application for credit was declined.

Case study – Ryan's story – C995252

Ryan was a 25 year old electrician who suffered from a serious gambling addiction. Ryan underwent counselling for his addiction and granted his mother enduring power of attorney to deal with his legal and financial affairs.

Between 2015 and 2017 Ryan obtained at least:

(a) 43 small amount credit contracts, and

(b) three credit cards,

from 10 different lenders in order to fund his addiction.

Many of these SACCs were approved concurrently, with some lenders aware that Ryan was already servicing up to 12 other SACCs, a credit card debt and a car loan at the time of approval.

The approval of these SACCs was in clear disregard of the presumption that a SACC will be unsuitable for the applicant if they have received 2 other SACCs in the 90 days preceding an application.

In addition to this, two of the credit cards (with combined credit facilities totalling $21,000) were approved by the lender despite Ryan and his mother requesting that the lender refrain from providing him with any further credit, as it would only be used for gambling.

Based on the documents CCLSWA managed to obtain, it appears that many of these SACC providers failed to conduct assessments of suitability or to take reasonable steps to verify Ryan's financial situation.

Despite Ryan managing to comply with his obligations under these credit contracts, save for the occasional default, CCLSWA is of the opinion that these practices still amount to the overprovision of credit.

This overprovision of credit has caused both Ryan and his mother considerable financial and emotional stress that could have been easily avoided by compliance with the responsible lending obligations.

Source: CCLSWA

3.50 We submit that in addition to requiring FSE's to be more vigilant in their assessment of suitability or unsuitability of a credit contract, consumers should be provided with the resources to make their own assessments of whether a credit contract is suitable and meets their requirements and objectives.

3.51 We are aware that financial literacy is a part of the Australian Curriculum and teachers draw on a range of material and programs to support an understanding of money and financial concepts.

3.52 Those resources are often produced by FSE's. Recently ASIC has announced a review of school banking programs.[3]

3.53 Allowing FSE's to provide financial literacy materials to schools, and promoting school banking raises an inherent conflict of interest.

3.54 Consumers at whatever age need to be able to make a considered choice about their financial product needs and this cannot be achieved while FSE's are providing financial literacy services.

3.55 Therefore, we submit that FSE's should not be able to participate in or promote financial literacy education and training. Instead, independent consumer advocates could provide these services as they are in a better position to provide independent information and training to consumers.

3.56 It is CCLSWA's mission to support the community by educating people about and advocating for their consumer and financial rights. Consumers who are financially literate will make positive financial decisions and be less likely to require our services.

[3] https://asic.gov.au/about-asic/news-centre/find-a-media-release/2018-releases/18-313mr-asic-announces-review-of-school-banking/

3.57 Therefore, we submit that further funding be made available to consumer credit legal services and financial counsellors to provide financial literacy training to the community.

When an employee or intermediary is terminated for fraud or other misconduct, should a licensee inform their clients of the reason for termination?

When an employee or intermediary is terminated for fraud or other misconduct, should a licensee review all the files or clients of that employee or intermediary for incidence of misconduct?

3.58 It is our view that if an employee or intermediary is terminated for fraud or other misconduct a licensee should inform the clients of that employee or intermediary of the reason for the termination.

3.59 It follows that we believe that a licensee should also review all of the files or clients of the employee or intermediary for incidence of misconduct.

Are certain types of add-on insurance, by their nature, poor value propositions for customers?

3.60 In our experience, the two forms of "add-on" insurance that are poor value for consumers are those of add-on car insurance including but not limited to GAP, extended warranty, tyre and rim insurance, mechanical breakdown insurance and consumer credit insurance; and Lenders Mortgage Insurance.

Add-on insurance in car yards

3.61 ASIC released a report in 2016[4] outlining the place of add-on insurance in the marketplace. It examined the experiences of consumers, the sales processes and practices of intermediaries and the outcomes for consumers.

3.62 It was found that some consumers would buy these products for reasons other than that they needed them and that customers often didn't know the cost of the product or what the policy covered when they purchased it.

3.63 The report found that most sales of add-on insurance products were made by intermediaries or authorised representatives of the insurer located at car dealerships. This amounted to approximately 75% of add-on products sold.[5]

3.64 These add-on insurance products are often sold to consumers by brokers or insurance providers as a result of referrals from car dealers. The brokers/insurance providers may

[4] https://download.asic.gov.au/media/4422973/cp294-published-24-august-2017.pdf
[5] Ibid, p 9.

then follow up and deal with the consumer by phone or email with no actual face to face contact.

3.65 Additionally, the car sales person as an intermediary is generally not under an obligation to select or recommend a product based on the needs of the consumer. As a result intermediaries tend to promote the sale of products solely based on the amount of commission they may earn.

3.66 Sue's story is illustrative of the negative consequences for consumers of commission driven sales.

Case study - Sue's story - C992142

Sue comes from a culturally and linguistically diverse background. Her partner at the time, who was abusive, wanted Sue to buy him a car and he took her to a car dealership.

Sue does not drive or have a driver's licence.

Sue signed various documents for the car loan, and also bought a warranty, gap cover and consumer credit insurance.

The dealer made no attempt to speak slowly or to explain the meaning of the credit and insurance documents or any other products. Sue could not understand what was being discussed between the car dealer and her partner and was instead simply told to sign various documents. She felt intimidated and pressured into signing.

Sue thought the loan amount was much less than it actually was.

She was charged $3,000 for the warranty and $4,200 for gap cover insurance and consumer credit insurance, which she did not know about or understand. Sue only learned of the extra amounts she had paid for the warranty and insurance products when she was advised by a CCLSWA lawyer, many months later.

Source: CCLSWA

Sovereign Insurance

3.67 John Hughes is a prominent motor vehicle dealer located in Victoria Park, Perth, Western Australia. As well as boasting some of the largest new and pre-owned car sales in Australia for particular makes and models on new and pre-owned vehicles, the John Hughes Group also includes a finance and insurance division known as Sovereign Credit and Sovereign Insurance.

3.68 In the period from 2004 to 2017 CCLSWA provided advice in over 50 instances to clients complaining about credit or insurance provided respectively by Sovereign Credit and Sovereign Insurance. In the majority of cases involving Sovereign Insurance/Sovereign Credit, our clients complained that the cost of the insurance was added onto their loans without their knowledge. Financing insurance in this way significantly increases the cost of the insurance to the consumer as they pay interest on the premium amount at the same rate as their loan over the life of the loan.

3.69 CCLSWA has also received numerous complaints about Sovereign Insurance unreasonably denying insurance claims (see Helen's story).

Case study - Helen's story - C989415

Helen bought a car from John Hughes. The salesperson obscured the sales and insurances contracts with his hand and Helen was unaware that she had applied for a car loan with Sovereign Credit or insurance with Sovereign Insurance until after the contracts were signed.

Helen thought she would pay $19,500, but was actually liable for $36,000.

Helen subsequently sustained an injury and could not work.

Helen submitted an insurance claim to Sovereign Insurance, which was supported by a medical certificate but Sovereign Insurance alleged that the injury existed before the contract was signed and denied her claim.

Source: CCLSWA

3.70 CCLSWA is also aware of instances of Sovereign Insurance failing to maintain regular repayments under their policies, even after approving claims (see Arianna's Story).

Case study - Arianna's story - C992394

Arianna had a car loan with Esanda Finance, with add on insurance provided by Sovereign Insurance.

Arianna required surgery and contacted Sovereign Insurance to make a claim on her loan protection insurance.

Sovereign Insurance sent out the paperwork, which Arianna had completed by her doctor and returned.

Arianna received a letter from Sovereign Insurance stating that her disability claim had been approved.

Every 4 weeks Arianna received another medical certificate from her doctor which she provided to Sovereign Insurance.

Esanda began to call Arianna every 2 weeks to inform her she wasn't making repayments on her loan.

Arianna repeatedly contacted Sovereign Insurance about this, and they confirmed that they had received her medical certificates and they had been making repayments to Esanda.

Arianna then received a default notice from Esanda and discovered that Sovereign Insurance had missed several repayments to Esanda, and that the payments Sovereign Insurance had made had been irregular and sporadic.

Source: CCLSWA

3.71 In CCLSWA's experience there is a distinct lack of knowledge about add-on insurance products, with many consumers not being aware that they are purchasing an add-on product or their entitlements under the policies (see Tristan's story).

Case study - Tristan's story – C993092

Tristan purchased a car from John Hughes for $60,000 financed by Sovereign Credit with fortnightly repayments of $500.

Tristan suffered from PTSD and depression as a result of workplace bullying.

At the time of signing his purchase and finance contracts, Tristan was not aware that insurance had been included in his loan. He later found out the insurance was included in his loan repayments and that Sovereign Insurance would continue to make repayments on his behalf in the case of disability.

Tristan made a claim on his insurance to pay the loan when he was on sick leave in 2012 and 2015. Tristan was under the impression that Sovereign Insurance would continue to pay his loan until the expiry of his medical certificate.

Debt collectors acting on behalf of Sovereign Credit came to Tristan's house while he was on sick leave and he was told that he was $8,000 in arrears, even though Tristan had not even received a default notice.

Tristan contacted Sovereign Credit to ask why the insurance payments had been stopped. Sovereign Credit said they were unable to help but could offer a $4000 per month repayment plan for the next 2 months; otherwise they would repossess the car.
Source: CCLSWA

3.72 Tristan's story is also illustrative of how Sovereign Credit and Sovereign Insurance operated cohesively to establish Tristan's credit and insurance contracts, but failed to communicate effectively through the claim and collection process.

3.73 Consumers have a reasonable expectation of effective communication and support between Sovereign Credit and Sovereign Insurance as they emanate from the same company group. However, our experience suggests that consumer expectations in this regard are consistently not met and there is a distinct lack of support to consumers between Sovereign Insurance and Sovereign Credit.

3.74 Our experience also suggests that consumers find it so difficult to make a claim that they are inclined to just 'give up' on their claims rather than pursue their rights and entitlements under the insurance contract.

3.75 The difficulties consumers experience in making claims means the process is often slow. The delays experienced mean that a consumer's credit contracts may fall into default while they await their insurance payout; and lenders may have commenced enforcement action in the meantime.

3.76 Boris' story illustrates how, even if a valid insurance claim is made, the difficulties and delays experienced making an insurance claim may mean that the consumer is unable to avoid repossession.

Case study - Boris' story – C984713

Boris had a car loan with Esanda Finance and was insured by Sovereign Insurance.

Boris' ex-wife suffered from bi-polar disorder and he was forced to stop working in order to look after their children. Boris lost all of his savings as his ex-wife took money from their joint bank accounts. Boris then went to Sovereign Insurance to claim on his policy. Sovereign Insurance made it very difficult, but eventually released one payment.

Sovereign Insurance asked Boris to complete the application process again to receive further payments. Boris said that he could not cope given the recent events in his life and failed to complete the re-application process.

Boris asked Esanda to contact Sovereign Insurance directly to seek payments on the loan. Esanda were unable to do this and so the loan went into arrears and the vehicle was repossessed. Boris was left with $12,000 shortfall debt after the vehicle was sold.

Source: CCLSWA

Lenders Mortgage Insurance

3.77 Lenders Mortgage Insurance (LMI) is insurance designed to protect the lenders in the event borrowers are unable to repay a home loan, and if the property is sold resulting in a shortfall.

3.78 LMI is usually required when a borrower's home loan deposit is less than 20% of the value of their home.

3.79 Consumers with a low deposit generally understand that they must pay for LMI otherwise they will not be approved for a home loan, however, in our experience; they do not understand the real purpose of LMI.

3.80 LMI comprises a one-off lump sum fee that is usually added to the consumer's home loan. So, even though it is obtained at the borrowers' cost, it only protects the lenders. We believe that this is where some of the confusion arises.

3.81 Borrowers are often under the misconception that as they have paid thousands of dollars for LMI, that they must benefit from it. That is not the case.

3.82 Consumers are often confused and fail to distinguish between LMI and Mortgage Protection Insurance. Many of our clients think that LMI protects them in the event that they cannot make their repayments due to illness or unemployment.

3.83 Sophie's story demonstrates this common misconception.

Case study - Sophie's story - C996104

Sophie and her now ex-partner obtained a home loan as joint borrowers with Big Bank. In October 2017 Sophie and her ex-partner agreed to the sale of their house two days before they received notice of Big Bank's intention to repossess.

The sale of the property resulted in a shortfall on the home loan of approximately $90,000.

Big Bank made a claim on its LMI. The terms of the LMI subrogated the right to collect the debt from Big Bank to the LMI insurer, which allowed the LMI insurer to pursue Sophie and her ex-partner directly. The LMI provider then sold the debt to a debt collection company. The debt collection company are now pursuing Sophie for the entire shortfall.

LMI was not explained to Sophie at the time the loan was taken out. However, Sophie understood that they needed it because they had a low deposit. She presumed that it was to cover repayments in the event that they could not pay the home loan due to unemployment or illness.

Sophie did not know how much she paid for LMI. She said she didn't think much more about it until they went to sell the property and Big Bank suggested that they get in touch with the LMI provider – but she didn't even know who they were.

After the property sale resulted in a shortfall debt, Sophie got a letter from the LMI providers asking her to complete a statement of financial position, which she did.

The next she heard was from the debt collectors saying that the LMI provider had assigned the debt to them.

Sophie questioned: what is she paying insurance for if it doesn't help her?

Source: CCLSWA

3.84 As Sophie's case above demonstrates, borrowers are often unaware of who the LMI provider is; and, as the borrowers are not parties to the insurance contract, they are unable to obtain a copy of the insurance contract in order to clarify its terms and their position.

3.85 The downturn in the WA economy, and the notable fall in house prices state-wide, has seen an increase in the number of calls CCLSWA receives in relation to properties sold with a resultant shortfall debt.

3.86 In CCLSWA's experience lenders do not hesitate to claim on LMI, and the LMI providers often ultimately assign the shortfall debt to debt collectors. It is often only at this point that consumers contact CCLSWA unclear on why they are being pursued and seeking advice on aggressive debt collection behaviour.

3.87 Tina's story is illustrative of a consumer pursued by a debt collector for the shortfall debt.

Case study - Tina's story – C994862

Tina and her ex-husband had a joint home loan with Big Bank. Family violence was prevalent in the relationship. Their property was repossessed and sold, resulting in a shortfall debt of approximately $58,000.

The shortfall debt was sold by Big Bank's LMI insurer to a debt collector.

All Tina knew about LMI was that it was very expensive but she thought it would give her some benefit.

The concept of LMI was not explained to Tina at the time she took out the loan. Tina did know that LMI was for the bank's benefit but thought that she would also have some protection under the policy.

Source: CCLSWA

3.88 As CCLSWA's cases demonstrate, consumers are paying for LMI but receiving no benefit. Consumers are confused about the nature of LMI. Consumers are also being aggressively pursued by debt collectors as a result of LMI.

3.89 Therefore it is our view that LMI is a clear example of an add-on insurance product that offers little to no value to consumers.

4 Small and medium enterprises

Should there be any change to the legal framework governing small and medium enterprise (SME) lending?

In particular, should any lending to SMEs come within the reach of the National Consumer Credit Protection Act 2009 (Cth) (the NCCP Act)?

4.1 It is our view that all small business lending should be captured by the same guidelines or legislation as those that govern the provision of consumer credit. Whether that is the NCCP Act, the Code of Banking Practice, requiring credit providers to hold an Australian Credit Licence, or being a member an external dispute resolution scheme (**EDR Scheme**).

4.2 We acknowledge that approximately 80% of lending to small businesses is by banks; however, it is our view that all lending to small businesses should be covered by the same guidelines or legislation.

4.3 Currently, those 20% of small business lenders who are not banks, are not bound by the Code of Banking Practice, are not required to hold an Australian Credit Licence, or be a member of an EDR Scheme.

4.4 It is also our experience that those business lenders who do not hold an Australian Credit Licence and are not part of an EDR Scheme often provide credit for consumer purposes, but have customers sign a business purpose declaration in order to circumvent the consumer protections available under the NCCP Act, NCC, and Code of Banking Practice.

4.5 Colin's story is illustrative of how small business lenders use the business purpose declaration to provide unsuitable credit with limited avenues for recourse for the consumer.

Case study - Colin's story – C992754

Colin was a recovering drug addict and was unemployed.

Colin got a loan from a small business lender to buy illegal drugs. At the time Colin applied for the loan, he was servicing many SACCs with seven lenders.

The application with the small business lender revealed a number of inconsistences and issues such as an incomplete ABN provided by Colin, the ABN did not match the business name, the small business lender only looked at Colin's personal bank statements and did not obtain a business bank statement.

Colin signed a business purpose declaration when he signed the loan contract with the small business lender.

As the small business lender was not a member of an EDR scheme, Colin's remedies were limited. CCLSWA lodged an ASIC complaint on behalf of Colin in relation to potential breaches by the small business lender of the NCCPA and NCC on the basis the loan was not for business purposes but was for personal use.

The small business lender sold its debt to another entity which settled the debt with Colin.

Source: CCLSWA

4.6 We suggest that like the small business provisions under the Australian Consumer Law, the NCCP Act provides thresholds for small business to be covered by the NCCP Act.

4.7 The Australian Consumer Law definition of 'small business' is that the business employs less than 20 people, including casual employees reemployed on a regular and systemic basis.

4.8 Alternatively, as a minimum, small business lenders should be required to be a member of an EDR scheme and to hold an Australian Credit Licence before being able to provide credit to small business borrowers.

Guarantees

If established principles of judge-made law and statutory provisions about unconscionability would not relieve a guarantor of responsibility under a guarantee, and if, further a bank's voluntary undertaking to a potential guarantor to exercise the care and skill of a diligent and prudent banker has not been reached, are there circumstances in which the law should nevertheless hold that the guarantee may not be enforced?

What would those circumstances be?

Would they be defined by reference to what the lender did or did not do, by reference to what the guarantor was or was not told or by reference to some combination of factors of those kinds?

Is there a reason to shift the boundaries of established principles, existing law and the industry code of conduct?

If the guarantor is a volunteer, and if further, the guarantor is aware of the nature and extent of the obligations undertaken by executing the guarantee, is there some additional requirement that must be shown to have been met before the guarantee was given if it is to be an enforceable undertaking?

Should lenders give potential guarantors more information about the borrower or the proposed loan? What information could be given with respect to a new business?

4.9 In our opinion there is inadequate consumer protection surrounding individuals who provide guarantees for small business loans. These individuals are consumers who are not connected with the business but are provided with no consumer protection under the NCC or NCCP Act. Individual consumers who provide guarantees for small business loans are inadequately protected under common law, equity and statute.[6]

4.10 As the current law stands, such individual guarantors may seek to deny liability on the basis they were unduly influenced into entering the contract as guarantors; or there was some form of unconscionable conduct when they entered into the contract as guarantor.

4.11 We would caution relying on the black letter of the law, particularly in relation to undue influence and unconscionable conduct, when protecting guarantors for small business loans.

4.12 Consumers need to be able to understand their rights in order to enforce them. However, it is difficult for consumers to understand the legal meaning of 'undue influence' and 'unconscionability' as distinct from what they may feel is

[6] *Australian Securities and Investment Commission Act 2001* (Cth).

'unconscionable'. Therefore, there should be greater protections under the NCCP Act for individual guarantors of small business loans outside of relying on the equitable principles of undue influence and unconscionable conduct.

4.13 CCLSWA has encountered many instances where a small business borrower was unable to meet repayments and defaulted on the loan, resulting in an individual guarantor being called upon to repay the balance of the loan.

4.14 A typical case would usually involve a parent being approached by their adult child to be a guarantor for a loan for the benefit of the child's business and the parent using the family home or other asset as security under the guarantee.

4.15 The Langdon's story below illustrates how the guarantor is usually unaware of the potential consequences of entering into the transaction and, over time, may even forget about the existence of the loan or guarantee. The guarantor is usually only reminded of their entry into the transaction once the FSE seeks to enforce the guarantee. The guarantor is usually shocked at receiving notices of demand or court documents, and may seek advice from CCLSWA.

Case study – the Langdon's story – 2015/090; C992267; C992266

Mr and Mrs Langdon owned their own home, Asset A. Their son, Adam, asked them to guarantee a loan. The loan was taken out by Adam's company as trustee for Adam's family trust and was used for the purposes of renovating Asset B. Adam intended to sell Asset B after renovations were completed to make a profit for Adam's family trust. The initial loan was for $600,000 and a 6 month term. Mr and Mrs Langdon agreed to be unlimited guarantors and provided a mortgage over Asset A as security.

After 6 months, Adam was unable to repay the loan and agreed with the Lender to extend the loan period and increase the loan amount by $500,000. The Lender did not communicate this to Mr and Mrs Langdon. At the end of the extended loan period, Adam was unable to repay the loan and the Lender commenced proceedings to enforce the loan including the guarantee provided by Mr and Mrs Langdon.

Mr and Mrs Langdon are currently challenging the guarantee in the courts.

When asked about their motivations for providing the guarantee, Mr and Mrs Langdon said that their concern for Adam and their wish to assist him because he was their son motivated them to become guarantors. They also indicated that they placed a significant amount of trust in Adam due to the fact that he was their son. Mr and Mrs Langdon did not focus on the financial aspects of the transaction and the potential implications for their family home if the loan was not repaid due to the level of trust they had in their son.

It would appear that the relative difference in wealth and assets between Adam and Mr and Mrs Langdon led Adam to request Mr and Mrs Langdon to be guarantors and Mr and Mrs Langdon's trust in Adam spurred them to be guarantors.

Mr and Mrs Langdon had received independent legal advice and the implications of entering into the guarantee were clearly communicated by the lawyer to Mr and Mrs Langdon. However, Mr and Mrs Langdon's trust and concern for Adam rendered the legal advice ineffective.

Mr and Mrs Langdon repeatedly cited their trust in Adam to the exclusion of legal advice. Mr and Mrs Langdon seemed eager to provide the guarantee notwithstanding the implications of default and their knowledge of Adam's lack of employment. Mr and Mrs Langdon also did not consider it likely that their guarantee would be called upon because in their opinion the sale of Asset B would pay off the loan. They even admitted to not reading the guarantee before signing it.

As the loan was for business purposes, the NCC did not apply, and there was no requirement for Lender to be a member of an EDR scheme. The Lender commenced proceedings in the Supreme Court of Western Australia for repossession of Asset A. CCLSWA acts for Mr and Mrs Langdon, with the assistance of pro bono counsel.

Source: CCLSWA

4.16 Stella and Yuki's stories below illustrates how loans for business purposes are exempt from being a member of an EDR scheme, therefore making it more difficult for consumers to lodge a dispute about the conduct of the FSP or the provision of the guarantee.

Case study – Stella's story – 2016/060; C993351

Stella was married to Alan for many years and they had a son together. After 30 years of marriage, the couple separated.

Shortly after Stella separated from Alan, Alan contacted Stella requesting that she guarantee a $30,000 loan. Alan assured Stella that the purpose of the loan was to pay off some of his debt, get up to date with his mortgage repayments and to cover travel expenses for a job he had lined up overseas. Stella felt guilty and was pressured into agreeing to sign the guarantee.

There was a meeting at Stella's home, attended by Alan and Mr Bamboo, Alan's solicitor. At this meeting Stella found out that the loan was actually for $100,000 and she did not want to guarantee the loan, however, once again Stella felt pressured to sign the deed of guarantee. Stella provided a mortgage over her own property as security for her guarantee.

Stella did not receive:

(1) independent legal advice before signing the documents,
(2) any benefit from the loan; or
(3) signed copies of the documents executed at the meeting.

Stella later found out that the loan was actually advanced to 'Upbeats Pty Ltd', Alan's company. Furthermore, the loan was actually a business kick-starter loan rather than a personal loan.

Alan defaulted on his repayments and has since disappeared leaving Stella to deal with the Lender.

When asked why she agreed to be guarantor, Stella stated that she felt guilty, and that they still had a child together who at the time was living with Alan. Ultimately, Stella succumbed to Alan's request and felt deeply pressured into signing the guarantee.

As the loan was for business purposes, the NCC did not apply to the loan or guarantee and the Lender was not required to be a member of an EDR scheme. The Lender commenced proceedings in the Supreme Court of Western Australia and the matter was transferred from CCLSWA to a private law firm.

If the NCC applied, more stringent rules would have applied to the credit provider and Stella would have:

(1) been provided with some protections such as being required to seek independent legal advice, and
(2) had the option of lodging a dispute with an EDR scheme.

Source: CCLSWA

Case study – Yuki's story – C987337; 2011/070

Yuki was born in Japan and immigrated to Australia in 2005. Her spoken English was enough to get by on a day to day basis, but her reading and writing skills in English were poor. In 2006, Yuki married Cooper and they had two children. In 2008 Cooper passed away, and Yuki had the home transferred to her name. The family home was and is Yuki's only significant asset.

In 2011, Yuki began dating Price. The couple had been dating for one year and in January 2012, Price suggested that they buy a business – a consulting firm. Yuki left it to Price to speak to Polo (broker), Marco (agent) and the FSE.

Yuki did not have any experience in consulting, or any business for that matter. Her usual employment was as a cleaner.

In July 2012, the FSE made an offer for the business loan and overdraft to 'Multi S'. Multi S was a company set up by Price in which Price was the sole shareholder, director and secretary. Yuki provided two forms of security for the business loan and overdraft. Yuki signed the Letter of Offer and Guarantee in Marco's office, in the presence of Marco and Price. Price also signed an individual guarantee and indemnity in favour of the FSE. However, Price did not provide any real or personal property as supporting security for his guarantee.

Yuki met with Marco only once, when she signed the guarantee in his office. The meeting lasted 15 minutes and Yuki had a stack of paperwork to sign. Marco only addressed Price, and Yuki felt very rushed. Further, Marco did not give Yuki an opportunity to read the guarantee (or take it home overnight to read), nor did he say that she could or should seek independent legal advice before signing it.

Yuki had never been a guarantor before and did not understand what giving a guarantee meant.

The consulting business was never profitable and in 2014, Price closed the business down. Price moved out of the family home and disappeared. Consequently, Yuki was left with paying off the loan.

It took CCLSWA two years to negotiate with the FSE to have the guarantee set aside on grounds of unconscionable conduct and undue influence. While CCLSWA was successful, it was an extremely lengthy process.

Had the NCC applied, the credit provider would have been bound by far more stringent rules, allowing Yuki to seek independent legal advice, and giving her at least 14 days to read over the guarantee. This would have allowed Yuki to understand what a guarantee was.

Source: CCLSWA

4.17 CCLSWA submits that the NCC should be extended to cover individual consumers who provide guarantees for small business loans, and who are not involved in the business. This is because the consumer is a volunteer, who is providing the guarantee without receiving a benefit from the business, and therefore, should be afforded consumer protection.

4.18 For the law to provide effective protection for such consumers, the NCC should:

(1) recognise such individuals as consumers; and

(2) encapsulate the entire span of the transaction -- from the formation of the contract, its operation, right up to the time of its enforcement or termination.

4.19 If the NCC were extended, it could be applied in the following ways:

(1) guarantors would be entitled to the statutory disclosures under s 55(3) of the NCC. That is a form 8 'warning box' placed immediately above, and on the same page as where the guarantor signs, or the guarantee would be unenforceable;

(2) guarantors would need to be given a copy of the credit contract before signing the guarantee;

(3) guarantors would need to be given a form 9 'information statement' under s 56(1)(b);

(4) guarantors would generally need to be given a signed copy of the guarantee within 14 days after signing;

(5) the guarantee would not automatically cover any increases in the liability under the underlying credit contract; and

(6) the 'unjust transactions' provisions under s 76(1) of the NCC could apply.

4.20 Extending the reach of the NCC to consumers who provide individual guarantees for business loans would provide these consumers with clear protections, and provide them with access to free EDR Schemes.

4.21 Furthermore, if the NCC were extended to include individual guarantors who are not connected with the business, it would be clear that CCLSWA would be able to provide legal advice to such consumers. Secondly, as case law illustrates, the legal doctrines in relation to third party guarantees are highly complex and expensive to litigate; therefore, by extending the NCC to individual guarantors of small business loans, it will be a step towards preventing guarantors from entering into unjust transactions, rather than simply relying on reactionary processes.

External dispute resolution

Should AFCA adopt FOS's approach of putting the borrower back in the position they would be in if the loan had not been made, but not awarding compensation for losses or harm caused?

Are there circumstances in with AFCA should waive a customer's debt?

4.22 Under AFCA's operational guidelines[7] the following remedies are available to complaints, other than a Superannuation complaint:

a) the payment of a sum of money
b) the forgiveness or variation of a debt
c) the release of security for debt
d) the repayment, waiver or variation of a fee or other amount paid to or owing to the Financial Firm or to its representative or agent including the variation in the applicable interest rate on a loan

[7] https://www.afca.org.au/custom/files/docs/20180913-afca-operational-guidelines.PDF

e) the reinstatement, variation, rectification, or setting aside of a contract
f) the meeting of a claim under an insurance policy by, for example, repairing, reinstating or replacing items of property
g) in the case of a complaint involving a privacy issue with an individual – that the Financial Firm should not repeat conduct on the basis that it constitutes an interference with the privacy of an individual or that the Financial Firm should correct, add to or delete information pertaining to the Complainant
h) in relation to a default judgment, not enforcing the default judgment
i) in relation to privacy-related complaints, to make an order that is generally consistent with the declarations available to the Information Commissioner when they make a decision under section 52 of the Privacy Act
j) an apology.

4.23 Whilst there is the option for AFCA to award a remedy of the forgiveness or variation of a debt, it does not have the same effect of putting the borrower back in the position that they would be in if the loan had not been made.

4.24 We recognise that the FOS approach to putting the borrower back in the position that they would be in if the loan had not been made balances the potential benefit that a consumer may have received with the losses/detriment they have suffered.

4.25 However, there are circumstances in which AFCA should waive a customer's debt such as:
(1) compassionate grounds - including circumstances of family violence;
(2) unconscionability; and/or
(3) where an initial unsuitable loan sets off a series of unsuitable credit contracts, causing the consumer substantial financial hardship.

4.26 We also advocate for AFCA to have the power to vary or set aside a contract. The ability to vary a contract is very different from the ability to forgive or waive a debt, or the power to rectify a contract. We believe it is an essential remedy to ensure fair outcomes for consumers.

4.27 One failure of the current EDR framework is in ensuring that consumers have fair and affordable arrangements after the determination of a complaint, particularly complaints about maladministration and responsible lending. The effect of EDR determinations can be to effectively accelerate repayment of amounts subject to the determination. In these types of disputes, we consider that the scheme should not leave the parties to come to agreement about repayment. Instead, AFCA should facilitate resolution of the complaint by determining fair arrangements for repayment, including the term of the repayment.

5 Regulation and the regulators

Is ASIC's remit too large?

- *If it were to be reduced, who would take over those parts of the remit that are detached?*
- *Why would detachment be better?*

5.1 It is our view that it would not be in the consumer's best interest to reduce the remit of ASIC or to split ASIC into different parts.

5.2 The suggestion that ASIC should have parts of its remit detached goes against the current logic in the sector which has resulted in the separate Financial Ombudsman Service, Credit and Investments Ombudsman, and Superannuation Complaints Tribunal, being amalgamated into one Ombudsman scheme: Australian Financial Complaints Authority (AFCA).

5.3 It is our experience that consumers often have enough difficulty in raising disputes with a single regulatory body, let alone a fragmented regulatory body. It is in the consumer's best interest to have one place to deal with all of their issues in relation to an FSE.

5.4 Consumers are often unaware of what both ASIC and the ACCC regulate and how to make a complaint to them. Further splitting up each of the regulators will make this process of determining where to complain even harder for consumers.

5.5 CCLSWA's substantive submission to the Royal Commission suggested:

(1) the reporting process be made simpler and more accessible;
(2) greater funding and resources be provided to the regulators; and
(3) regulators to take on more of an active role in identifying and taking action against FSE's that are in breach of their credit law obligations.

5.6 We are of the opinion that ASIC does great work as the regulator, considering the limited amount of resources in comparison to the scope of functions that ASIC is required to carry out as the regulator, and the abundance of resources that are available to the FSE's. We consider that instead of splintering the remit of ASIC, it would be more effective to enhance the powers ASIC has as regulator. This would include giving ASIC greater and more flexible powers of investigation, instigation of proceedings and enforcement in respect of misconduct in the sector.

5.7 In light of the Interim Report, we suggest that any reform to the regulators should focus more on resourcing the regulator and understanding how the different regulators

intersect rather than detaching or simplifying the regulator to the detriment of consumer rights.

6 Next steps

6.1 As a result of the Royal Commission, consumer credit legal services and financial counsellors have experienced greater demand for their services as a result of the Royal Commission shining a light on misconduct in the financial services industry.

6.2 As the statistics provided show, consumer credit legal services and financial counsellors are at capacity with the number of cases that they can take on.

6.3 As the Royal Commission concludes, CCLSWA expects that even more consumers will be seeking legal advice in respect of potential claims they make have against FSE's.

6.4 With consumer credit legal services and financial counsellors being currently at capacity, these consumers may face difficulties in being able to pursue legitimate claims they may have because of the lack of resources available to consumer credit legal services and financial counsellors.

6.5 Similarly, in order to effect change and implement any recommendations that come out of the Royal Commission, consumer advocates need sufficient resources and funding to be able to assist consumers.

6.6 Therefore we submit that there should be additional funding and resources made available to consumer credit legal services and financial counsellors in order to be able to assist individuals who have been affected by banking misconduct.

6.7 Further we suggests that any penalties imposed by the regulators be directed to consumer credit legal services and financial counsellors to help assist consumers' ability to access remedies in relation to FSE's. Without access to these legal resources, any changes implemented in the sector will have little to no effect on consumers as they still lack the resources to enforce their rights.

6.8 The findings of the Royal Commission warrant further investigation and consideration for increased funding for consumer credit legal services and financial counsellors. Generally, existing legal aid funding is typically reserved for criminal matters, yet a large proportion of court proceedings relate to financial matters.

6.9 In the 2017/2018 financial year, CCLSWA turned away 1517 people for legal advice. FCN data indicates that across the Perth metro area over 8,200 people annually contacted services wanting to make an appointment and were turned away due to appointment unavailability. Currently, demand outstrips capacity, and we believe that

the problem will only get worse with the release of the findings from the Royal Commission.

6.10 Outside of the ombudsman scheme's dispute resolution services, there are very few low cost options for victims of financial service misconduct. Underfunded consumer credit legal centres such as CCLSWA are unable to meet the high demand for services at the current funding level.

6.11 Independent Senator Tim Storer notes that there is a present power imbalance in legal representation. By creating a financial barrier to legal representation, it prohibits consumers and small businesses from taking civil action against financial service providers who are engaging in misconduct. Without the establishment and reinforcement of equality-based organisations in the sector, there will continue to be a power imbalance. Senator Storer states that consumer law centres need to have restrictions lifted and an increase in funding, which he suggests is funded through a bank levy. [8]

6.12 We welcome any suggestion that may assist consumer credit legal services and financial counsellors in gaining funding to be able to broaden the reach of their services to assist a greater proportion of the community in the wake of the findings of the Royal Commission.

7 Conclusion

CCLSWA is grateful for the opportunity to provide input to the Royal Commission.

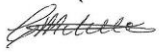
CCLSWA would be happy to be of assistance in providing further information or detail on CCLSWA's position or in relation to a case study.

[8] https://www.smh.com.au/politics/federal/calls-grow-for-banks-to-fund-legal-aid-in-cases-of-customer-disputes-20180930-p506xm.html

If you have any questions or would like to discuss these submissions further, please contact Gemma Mitchell on (08) 6336 7020.

Yours faithfully

Consumer Credit Legal Service (WA) Inc.



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Appendix A

Consumer Credit Legal Service (WA) Inc.

Consumer Credit Legal Service (WA) Inc. (**CCLSWA**) is a specialist community legal in Western Australia. In the 2017/2018 financial year, CCLSWA provided advice to 907 new clients, opened 121 case files, and closed 63 files. Of the 63 files closed:

- 98% were experiencing financial difficulty
- 53% were over 65
- 22% needed a translator as the main language spoken at home was not English
- 22% had a disability or mental illness

Community Legal Centres Association WA

The Community Legal Centres Association (WA) (**CLCA(WA)**) is the peak organisation representing and supporting 28 Community Legal Centres (**CLCs**) operating in Western Australia. Located throughout the state, CLCs are independent, non-profit organisations which provide legal services to disadvantaged and vulnerable people or those on low incomes who are ineligible for legal aid.

On behalf of our members, the CLCA (WA) is committed to the principles of human rights, social justice and equity, including the rights of Western Australians to equity in access to legal services. To do so, the Association also supports CLC's working together and with other organisations within the community.

Financial Counsellors' Association of Western Australia

The Financial Counsellors' Association of WA (**FCAWA**) represents financial counsellors who are practicing in WA, and we have a current membership of over 150 people. FCAWA also manages the National Debt Helpline, a 1800 number for people experiencing financial hardship in WA. All services provided by the Helpline and financial counsellors are free and independent and managed by a variety of not for profit organisations. FCAWA provides training, support, policy and advocacy advice to the financial counselling sector, government, key stakeholders and consumers.

Financial Counselling Network

The Financial Counselling Network (**FCN**) is a unique collaboration of 15 member organisations and provides a range of integrated and person centred services with the aim of reducing the drivers and impacts of financial hardship in the WA community. Member organisations of the FCN include community legal centres, family and domestic violence (FDV) centres, large not for profits, community service organisations and local government. This collaboration provides access to comprehensive referral pathways and expert knowledge whilst leveraging local expertise and relationships.