

WesleyVoice

CONSUMER CREDIT and Payday Lending

- 1/3 of SA households live on less than \$16,000 a year
- Australian Credit Card debt was to \$38.89 billion in November 2007
- Pay day loan interest (and fees) can be over 1,000% when annualised

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What's the Problem?

Consumer credit can be defined as any form of loan for personal or household use, as opposed to business or commercial lending.

Loans are often unsecured and carry more risk than secured loans for lenders, so a higher interest rate is charged. Payday lending typically provides small amounts, (\$200-\$300) short-term loans (between 2 - 4 weeks, i.e. to the next payday) charging borrowers a fee, say \$50 on a \$200 loan. When annualised, payday loans can equate to interest rates as high as 1000 percent. Numerous terms are currently employed to describe these loans, including the generic 'short-term loan', 'loan sharking', 'cash advance' and the industry-preferred term, 'micro-lending'.

The practice of payday lending is of considerable concern to consumer advocates, including financial counsellors, because interest rates (including fees and charges), become usurious; usury being the act of lending money at an illegal or exorbitant rate of interest.

The Australian payday lending industry says that micro lending provides a valuable service by facilitating emergency cash relief to people with no other credit options available to them. Furthermore, they have consistently argued that their rates are reasonable when the establishment and administrative costs of loans are taken into consideration. 1. (Payday Lending in Victoria - A research report . Dean Wilson Consumer Law Centre Vic. Ltd. July 2002).

While payday lending is currently very newsworthy, it is just one of a number of consumer credit issues of concern; other aspects include interest free loans, loan sharks, unsolicited credit cards and some store cards. The term 'Fringe Credit' is sometimes used as a generic description for this range of practices.

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Current Situation

While Australia has experienced a number of years of economic growth and more people are employed (part or full time) than a decade ago, financial stress levels remain high for a significant number of households.

A half of all South Australian households have an annual equivalised¹ income at or below \$24,000, while the poorest third of SA households have equivalised household incomes below \$16,000 pa. By comparison, an adult earning the average weekly wage takes home \$48,000 per year.²

This means that about a half of all South Australian households live on very modest incomes, while a third can be regarded as living with considerable financial stress.

There are a range of indicators for financial stress; the following compares various experiences for the poorest 30% of households with the remaining 70% of households³ in Australia:

Selected indicators of Financial Stress, Australia, 2003-04

	Poorest 30%	Remaining 70%
Unable to Raise \$2000 in a week	52.1	8.6
Couldn't pay energy or phone bills on time	37.8	11.5
Pawned or sold something wanted	11.7	3.5
Went without meals	11.8	1.8
Sought help from welfare agencies	14.7	1.2

Source: Australian Social Trends 2007, ABS

This information suggests that 5%, or 1 in 20 households go without a basic need, food, because they have no money, while 19% cannot afford essential services, including energy.

¹ When household income is adjusted according to an equivalence scale, the equivalised income can be viewed as an indicator of economic resources available to a standardised household

² Figures rounded, Source: Australian Social Trends 2007, ABS

³ More formally, low resource households (poorest 30%) are those in the lowest 3 deciles of both income and net worth deciles

⁴ For comparison, in January 2008 the Reserve Bank set official interest rate was 6.75%, the base rate lending on housing, a secured asset.

Credit is widely promoted as a response to financial stress.

The Reserve Bank of Australia reports that "Over the year to November 07, total credit rose by 16.2 per cent." The total value of credit card debt has increased significantly over the last decade. In November 1997, personal credit card debt for Australia was \$7.23 billion, which had increased, in nominal terms (not adjusted for CPI) to \$19.15 billion in November 2002 and then to \$38.89 billion in November 2007.

Credit cards attract higher interest rates (18-20% being common, Jan 2008) than personal loans (about 14%)⁴. When credit card limits are reached and banks have low interest in small personal loans, people dealing with a financial crisis consider short term loans from non-traditional lenders as their only option.

Consumer Protection

The Uniform Consumer Credit Code (the Code) is the major piece of legislation governing consumer credit in Australia and was introduced in 1996. .

The Code aims to have credit providers present credit information in a clear and easy to understand format. Credit providers such as banks, building societies, credit unions, finance companies and businesses, must tell consumers what their rights and obligations are in any credit arrangement.

For people experiencing financial problems, research and experience of financial counsellors shows that a one to one, timely and tailored approach to financial problems works best. However, financial counselling (not budget advice or commercially provided 'financial planning') is seriously under-funded.

The level of unmet need for financial counselling continues to be significant.

The Banking and Financial Services Ombudsman (BFSO), is an effective service for people who use the service, with satisfactory results often including reduction of debt.

In relation to consumer credit issues, the lack of capacity to meet demand is exacerbated by:

- South Australia not having a statewide accessible (even phone accessible) specialised consumer credit legal service, which operate in other states
- South Australian Financial Counsellors Association, the professional body for financial counsellors in SA, is unfunded.

Currently a very small scale service is provided one day a week but the worker is unable to cope with the demand.

UCW Adelaide has formally sought funding to establish a Consumer Credit Legal Service, and this has been refused. Currently a very small scale service is provided.

Financial counsellors believe they are seeing the tip of the iceberg in relation to consumer credit issues.

Case Studies

Payday Lending

A person, whose sole income was a Centrelink benefit, saw a financial counsellor after receiving a court summons for a pay day loan. He had borrowed \$300 from a payday lender. The interest rate quoted on the contract was 576.70% per annum and total amount repayable at the end of the fortnight was \$366.36. The three-page contract was detailed and protected the lender.

The person had repaid \$200 in two installments over the next 2 months. He could pay no more and four months later he received an investigation summons. The judgment debt was for an amount of \$617.09, which, with extra interest, court fees, and solicitors fees had risen to \$705.84 on the court summons, and was still rising with interest accruing.

Unsolicited Credit

A financial counsellor was recently seen by a young man with an intellectual disability, working in a sheltered workshop and under care of a Community Living Program. He had a store card with a limit of \$1,000 which was transferred to a finance company credit card and the limit was increased to \$6000. When the client had a balance of \$393 he was offered a limit increase of \$9250. Seven months after receiving this increase his balance owed had increased to \$8,000. He was then offered an increase to \$13,250. Three months later his balance was \$14,000, he presented for financial counselling with the manager of the Community Living program. The manager said that the client thought that money in his wallet was "my money", he used the account so he could save "his" money. Negotiations are underway with the company to bring the balance back to a manageable amount.

Aboriginal Communities

UnitingCare Wesley remains concerned at how difficult it can be for Aboriginal people to access appropriate financial counselling services and advice, especially where English is not the first language.

In remote communities it is not unusual for nearby stores to hold large numbers of their customers' 'key cards'. The stores may also hold the PIN numbers for these cards. This is a long-standing practice. Sometimes stores advance cash or items to Aboriginal people and then hold the cards as surety. In other cases, people may have asked the store to hold their card for safekeeping. Whatever the reason, current arrangements are ad hoc and not closely scrutinised.

Many Aboriginal people living in remote SA communities are highly mobile. Consequently they often make significant purchases or enter into long-term financial arrangements in other jurisdictions

(WA and NT). For example, an Aboriginal woman from a small WA community entered into a financial arrangement with a car-dealer in Adelaide. As part of the arrangement, the woman left her key card with the dealer. After returning home to WA, whenever the woman wanted to purchase food at her local store, the store manager had to arrange a cash advance from the car-dealer in Adelaide. The amount of the advance was then added to the total amount owing on the original car loan.

The incidence of these and other problems could be reduced by firm action, including:

- school-based financial literacy programs.
- the establishment of additional financial counselling services for Aboriginal people delivered in the clients' first language.
- a determination to enforce consumer protection and credit legislation by government and regulators
- the establishment of consistent, mandatory codes regulating consumer credit and investment scheme practices across States and Territories.

What is UCW doing?

UnitingCare Wesley has, for many years, provided services to assist people who are struggling financially.

UCW Adelaide Services

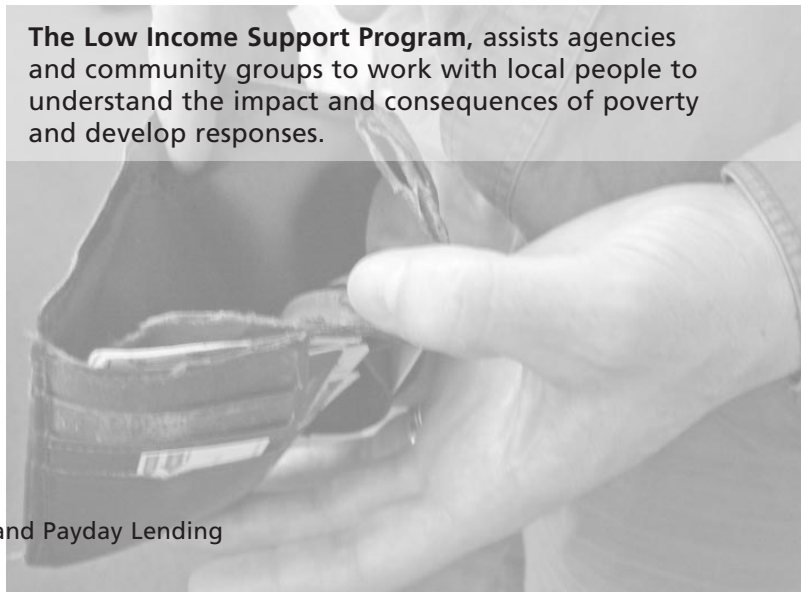
Financial Counselling is available to anyone, although the service focuses mainly upon low income and disadvantaged people. The service conducts an average of 80 interviews each month.

Financial counsellors regularly support clients with assistance to resolve financial difficulties including through options such as negotiating with creditors, bankruptcy, responding to court action, budgeting and dispute resolution.

The Central Community Legal Service is a program set up to provide FREE legal information, advice, referral and assistance. Advice is offered in areas including consumer issues, debt and tenancy.

In country areas, the service is available to people who live west of Whyalla, through the number - 1300 886 220 for the cost of a local call.

The Low Income Support Program, assists agencies and community groups to work with local people to understand the impact and consequences of poverty and develop responses.



What Needs To Be Done?

South Australian Government

In October 2007 the parliamentary Economic and Finance Committee inquiry into the provision of consumer credit and investment schemes in South Australia was released and made 24 recommendations, including the following:

- R1: Financial mediation services to be mandated ... to seek to resolve disputes outside the court system.
- R4: Consideration of capping annualised interest rates, fees and charges
- R5, 10: Licensing short term credit providers and mortgage and finance brokers with a 'fit and proper' character test.
- R7: Require short term credit providers to obtain more details as to customers capacity to repay a loan.
- R16: The creation of a dedicated credit tribunal to deal with credit matters not resolved by mediation.
- R21, 23: Creation of the offences of "Money Laundering" and "Loan Sharking"
- R24: Preventing credit card providers from offering pre-approved credit increases.

The South Australian Government can make significant advances in reducing financial stress from exploitative loan and credit providers, including 'pay day lenders' by implementing the recommendations from the Economics and Finance Committee. Further action to protect Aboriginal consumers is also urgently needed.

The South Australian Government also needs to be working with the Australian Government to establish a Consumer Credit Legal Service in South Australia that can assist people with specific consumer credit issues and advocate for policy change.

Further Reading

Ministerial Council on Consumer Affairs:
www.consumer.gov.au and www.creditcode.gov.

Payday Lending in Victoria - A research report Dean Wilson ...
www.consumersfederation.com/documents/

CHOICE - How to borrow at 972% (archived)
www.choice.com.au

Australian Government

A Ministerial Council on Consumer Affairs is currently active and has 5 strategy areas. National Credit policy and Fringe Credit providers are part of Strategy 1, Policy and Legislative Harmonisation.

Proposed amendments include:

- prohibition on taking security over household goods, for loans
- requiring credit providers to provide full information about direct debit authorities
- clarify disclosure of an annual percentage rate (though the oft mentioned 48% cap is not mentioned) measure to close the 'loop-holes' that many fringe credit providers use to avoid regulation.

The moves to strengthen the Consumer Credit Code to provide greater protections to consumers are significant and the desire to standardise consumer protections nationally is welcome. However it is critical that State governments continue to implement state based consumer protection as national agreement will take time and not all essential amendments will be made nationally.

Finance Industry

There are indications that financial institutions are becoming more aware of their responsibility to customers, including low income customers and the broader community. The ANZ bank, for example, has developed a Responsible Lending Commitment and promises to present annual audited statements on these commitments. ANZ has been a leader in understanding and responding to "Financial Exclusion". The National Australia Bank (NAB) has worked closely with community service organisations to develop No Interest Loan Schemes and other financial services for low income people.

Actions like these need to be followed by other financial service providers and a culture that is sensitive to low income customers needs to be 'mainstreamed' throughout the finance industry.

Community Service

Community service agencies have also responded to the financial stress that they witness on a daily basis, and in recent years have developed low cost, short term finance options for low income people.

In South Australia, Good Shepherd Youth and Family Services facilitated the establishment of No Interest Loan Schemes (NILS[®]), the largest micro credit program in Australia. South Australia has a limited NILS[®] coverage run by non-government organizations. In 2006 the NAB extended their commitment to capitalise NILS[®] nation wide. UCWs Adelaide, Bowden and Port Pirie provide a NILS[®] scheme and Wesley Adelaide's Julie McMahon is the State coordinator.

A second scheme called 'Step Up' (financed by the NAB) is being coordinated statewide by John Morris from Wesley Adelaide which provides low interest (currently 7.24%) loans for up to \$3,000 to people on low incomes for purchase of white goods, cars etc. Wesley Adelaide, Wesley Bowden, Wesley Port Pirie and in near future Wesley Port Adelaide, provide Step Up loan schemes.

The default rate on NILS, in particular, has been low, reinforcing the experience of financial counsellors that low income people generally, are very good managers of money - they have to be.

These community service / finance industry partnerships are vital.

