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Dear Sir/Madam

Re: Discussion Paper "Reforms in Relation to Small Amount Credit Contacts"; and Exposure Drafts of Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011

We write to you in response to the release of the Discussion Paper "Reforms in Relation to Small Amount Credit Contacts" ("Discussion Paper"), and the Exposure Drafts of *the National Consumer Credit Protection Amendment (Enhancements) Bill 2011* ("Exposure Drafts"), in April 2012. The reforms proposed under the Discussion Paper and the Exposure Drafts impose operational restrictions and prohibitions on credit providers to offer small amount credit contracts, and provide further policy developments on caps on costs for both "small amount credit contracts" and the 48% national credit cap for all "other" contracts.

As you are aware, the release of the latest Discussion Paper and Exposure Drafts follows the extensive inquiry into the *National Consumer Credit Protection Amendment (Enhancements) Bill 2011* conducted by the Parliamentary Joint Committee on Corporations and Financial Services and the Senate Economics Legislation Committee in October 2011 ("Committee Inquiry"). The key recommendation of the Joint Committee's Report concerning the short-term small amount contracts proposals was that:

> *"Further consultation with stakeholders should be undertaken to address the concerns identified throughout the inquiry and to develop measures that will ensure cohesive and consistent national consumer credit legislation and an appropriate balance between consumer protection and industry viability."*[1]

Cash Doctors will demonstrate in this submission that the proposed measures in the Bill fail to provide an appropriate balance between consumer protection and industry viability.

[1] Parliamentary Joint Committee on Corporations and Financial Services Inquiry into Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011, December 2011, Recommendation 12, at paragraph 5.245

Instead, the proposed measures will have severe consequences for the sustainability of the industry and consequently inhibit consumers' choice of financial product.

Submission Synopsis

As you are aware, Cash Doctors has been an active stakeholder in the consultation process, having made written submissions on the first Exposure Draft of the legislation, the tabled legislation, the Parliamentary Joint Committee on Corporations and Financial Services and the Senate Economics Legislation Committee Enquiry (by attending the Joint Committee Enquiry to give oral testimony as well as written supplementary submissions to the Committee).

You will therefore be familiar of how Cash Doctors are differentiated in the market place, ***<u>offering a unique product for a unique customer base.</u>***

As previously submitted, ***<u>our customers are financially literate, in full-time employment, and are able to make fully informed decisions about their financial needs and commitments.</u>***

Our customers choose our credit product as a preferred alternative to traditional solutions. Our customers do not want to be tempted by taking up the available credit on a credit card, giving them more credit than they require, which they believe will perpetuate a long-term debt spiral. Cash Doctors customers are telling us that they do not want to be tied into a long-term financial product, and that they do not need or want to take on more credit.

We agree that there is need for reform in the industry to protect those who are vulnerable from the numerous unscrupulous players in the sector. However, given:

- the financial literacy of our client base;
- that our customers are fully PAYG employed with average net annual income of $40,000 (44% of clients earn between $35,000-$50,000 and 18% between $50,000-75,000);
- the strong credit history of our client base and their desire to engage with a short-term credit solution rather than the more traditional solutions;
- that we offer advances of between $100 to $600 for a period of 45 days with no roll-overs permitted; and
- we responsibly approve just 17% of total applications,

we contend that there is an emerging and growing demographic of consumer who also needs to be considered within the framework of these proposed reforms. These consumers are financially aware and want the ability to choose a short-term financial solution which suits them.

We are very concerned that certain of the proposed reforms, which will be discussed further, will result in the exit of responsible, small-amount short-term lenders from the sector, leaving our financially, full-time employed borrowers with few, if any, alternatives. **Our key submission is therefore that the proposed cap on costs, particularly compounded with the operational restrictions and prohibitions, continue to be unworkable and should immediately be revisited by the Government based on sound economic modelling with direct input from industry. In the alternative, should the Government choose to ignore the key recommendation of the Joint Committee in attempting to strike an informed balance between consumer protection and industry viability, we submit that to allow survival of this market and customer choice of product, albeit with a small profit margin, the maximum amount of permitted establishment fee for a small amount credit contract should be increased from 20% to 27.5%.**

About Us

Cash Doctors is a growing national brand in Australia and is the industry leader in online small-amount short-term lending. In 2005, the founders, Greg Ellis and Sean Teahan, identified a need in the small-amount short-term lending sector and saw an opportunity to provide a responsible, transparent service to the Australian working community that was neither available in the mainstream credit market nor the incumbent fringe/short-term lending and pawnbroking market.

Since its inception in 2005, Cash Doctors has grown rapidly in staff and customer base, now representing nearly 70 personnel, with some 27,000 customers, providing more than 201,000 cash advances under its continuing credit facility. We offer advances of between $100 to $600 for a maximum period of 45 days with **no roll-overs** permitted. Repayments are typically over 1-3 pay cycles. The average advance is $421 over a period of 21 days. We only offer loans to **fully PAYG employed** customers, and as such, only 17% of total applications are approved.

The low approval rate is the result of an extremely rigorous selection and approval process, which includes prudent credit checks and other responsible lending checks, accompanied by technically sophisticated data-driven underwriting measures to carefully assess capacity to repay and maximise the chance of customer repayment and satisfaction.

In response to the demands of this new financially-aware, computer-literate demographic, application is made purely online. If accepted, funds are deposited into the customer's account within an hour during business hours (with existing members paid within seconds of a request 24 hours a day, 7 days a week). Offering a loan product online is exactly what our customers are telling us is their preferred approach. Customers can log on to their PCs or mobile handsets and apply for a Cash Doctors cash advance any time of the day, any day of the week, in the privacy of their own homes. Transparency of fees and required documentation is not compromised by our innovative online model, and the customer has all the relevant information upfront in order to make an informed decision about accepting a Cash Doctors cash advance. We offer a simple solution allowing customers to move on with their lives without overcommitting to lengthy repayment schedules and the temptation of more credit than they need. Cash Doctors also offers financial tips and online budgeting tools to promote good financial health, and ultimately to help our customers avoid deeper financial issues in the first instance.

Cash Doctors is, and has always been a responsible lender. We are continually fine tuning our application and approval process by the development and use of sophisticated automated systems and tools for testing the reliability of information provided by a customer, which in turn produces a more accurate assessment of the customer's suitability of the contract for responsible lending purposes.

In the new online economy, unethical customer experiences spread very fast via online blogs and social media which forces extreme accountability and receptiveness to customer needs. Therefore, profiting from late fees is inconsistent with our company mission and values and the fact we apply a loss-making fee structure to those few accounts that fall overdue is designed to strongly incentivise our organisation to continually make correct initial lending decisions. That's in our interests and those of our customers.

Our Customers are different

The recent Department of Treasury Discussion Paper "Strategies for Reducing Reliance on high-cost, short term, small amount lending" released April 2012[2], states that:

> *"Australian research has shown there is a significant level of use of* ["high-cost small amount short-term loans"] *by consumers who are unable to access mainstream credit products and who may experience financial exclusion. In summary, the data suggests:*
>
> - *approximately 40 to 49 per cent of small amount loan customers have annual incomes of less than $24,000;*

[2] Cash Doctors supports the publication of this paper. It appears Treasury are now looking to expand government initiatives to address the issue of financial stress and reliance on small amount short term loans. This is a positive step as Treasury has historically, and rather openly, attempted to eliminate the entire payday market, as the sole solution to the problem. We are happy that the Government's focus has now shifted to addressing the needs of the intended group - the "vulnerable" low-income consumer.

- *between 50 and 74 per cent of small amount loan customers have annual incomes of less than $36,000;*
- *50 per cent of small amount loan customers are partially employed or unemployed; and*
- *between 46 and 50 per cent of small amount loan customers are in receipt of government benefits."*[3]

As has been previously submitted, Cash Doctors customers differ greatly from users of so-called "payday loans". Cash Doctors customers are fully PAYG employed with average net annual income of $40,000 (44% of clients earn between $35,000 - $50,000 and 18% between $50,000 - $75,000). These figures are *net* of tax, so the salary levels of our customers are, in fact, a lot higher.

Further, almost 65% of our customers have clear credit records. This illustrates that this customer demographic have most mainstream financial options available to them, yet a small-amount short-term cash advance, such as the Cash Doctors product, is freely chosen over all of the traditional lending options.

Clearly, our client base is very different. This has been accepted by the Joint Committee:

> *"The committee* [ ] *notes evidence that there is a growing number of middle income earners accessing the short-term loan market. The committee agrees with views of industry representatives that this growing client base cannot be considered to have the same vulnerabilities as lower income earners and, in particular, consumers whose income is substantially derived from Centrelink benefits."*[4]

Accordingly, our customers should not be disadvantaged by being included in the same group that the Government is, rightly, seeking to protect.

We also note the stated intent of the policy of the Discussion Paper is to address "financial exclusion" which means that:

> *"individuals are less able to participate fully in social and economic activities and financial hardship is increased. For this reason, increasing financial inclusion is a key policy goal of the Government."*[5]

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[3] At page ix
[4] Parliamentary Joint Committee on Corporations and Financial Services Inquiry into Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011, December 2011, at paragraph 5.222
[5] At page ix

This Discussion Paper suggests alternatives to short-term loans such as further developing advances on Centrelink payments, no or low interest loans, seeking hardship relief with a utility provider, along with new possible Government initiatives. These suggestions are clearly aimed at those low/no income consumers who have been wrongly subject to the predatory behaviour of many of the traditional players in the sector.

Given the employment status of our customers, most, if not all of the no interest and low interest loan scheme alternatives suggested have restrictive qualifying criteria thereby rendering many individuals, and certainly our customers, **ineligible.**

Additionally, customers with higher incomes are unlikely to satisfy the hardship criteria of utility providers as there is an assumption that higher paid individuals should be able to repay without qualification.

Exposure Draft - the "Small Amount Credit Contract" – Establishment fee

In section 31A(2) of the tabled Bill, Treasury introduced a cap on costs for small amount credit contracts ("SACCs") which had set the maximum permitted establishment fee as 10% of the adjusted credit amount, and a maximum permitted monthly fee of 2% of the adjusted credit amount. Cash Doctors, in its submission on the tabled Bill (dated 14 October 2011) explained that this figure was not commercially viable and that to continue to operate within the market, albeit with a very small margin, the establishment fee must be increased to at least 27.5%[6].

The Joint Committee, to whom the proposal was referred, agreed that this original suggested cap on costs was unworkable and recommended that:

> *"the restriction on fees and charges for small amount credit contracts should be set at a level that will ensure the ongoing viability of the small amount credit contract sector.* [7]

Coalition Members and Senators went further to comment:

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[6] Note, Cash Doctors previously did not make a submission to make any changes to the 2% monthly fee. Cash Doctors continues to not seek any changes to the proposed 4% monthly fee in this submission. As Cash Doctors advances are for an average of 21 days, Cash Doctors believes that the application of the monthly fee on a pro rata basis will be difficult to administer. We note however that, as the monthly fee is the "maximum" fee that can be charged, and therefore not compulsory to charge, there is no need to make any submissions on this issue.

[7] Parliamentary Joint Committee on Corporations and Financial Services Inquiry into Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011, December 2011, at paragraph 5.2.33

> *"We question why government should be setting a cap on the prices that* [short-term small-amount] *lenders – or any other kind of lender – may charge… we are sceptical of the wisdom of outlawing prices above a certain level."* [8]

Certainly the UK experience should be closely examined as an example of successful regulation without the use of "caps" on costs. The UK Office of Fair Trading conducted an extensive review of high-cost consumer credit and in its final report published in June 2010 provides some useful regulatory logic <u>against</u> the imposition of price controls. We have provided the relevant excerpt here:

> *"We have concluded that introducing price controls would not be an appropriate solution to the particular concerns that we have identified in these high-cost credit markets. We are aware that price controls can represent an efficient way to address concerns around high profits among suppliers and could, initially, limit the headline prices paid by consumers in the high-cost credit sector. We are, however, also aware that the strategic responses by suppliers to price controls may lead to an outcome in these high-cost credit markets which is* ***unlikely to be of benefit for consumers****.*
>
> *The imposition of price controls in high-cost credit markets creates a risk for suppliers that they would generate lower profit levels. It would be reasonable to expect these suppliers to respond to the imposition of a price control by* ***seeking to regain such lost profit by restricting the type and risk of consumers that they are willing to supply****. In an extreme case of a highly restrictive price control for high-cost credit,* ***some suppliers could cease offering a particular product or exit the market entirely****.*
>
> *This potential for reduced access to high-cost credit would be of concern for the following reasons:*
>
> - *The supply of high-cost credit is already constrained, with many consumers having limited options and in some cases few practical, alternatives to high-cost credit (particularly in the short term).*
> - *Many consumers using high-cost credit are using this for non-discretionary expenditure.* ***Any reduction in access to this would have a significant impact on their ability to manage their finances effectively****."* [9]

The UK OFT suggests that in lieu of price controls, the Government should focus its attention on:

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[8] As above, at paragraph 1.21

[9] See Executive Summary

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- development of a consumer education program, and helping consumers to make informed decisions;
- helping consumers establish a good credit history record;
- promoting best practice for lenders in a code of conduct covering issues such as rollovers, better customer communication concerning disputes and advice etc.[10]

We submit that, following the UK experience, there are clearly other alternatives to imposing price controls (or rate caps) and in the first instance we request that Treasury focus on exploring those options. As noted above, we welcome the publication of the Discussion Paper "Strategies for Reducing Reliance on High-cost, Short term, Small Amount Lending" as a first step to exploring other solutions to the issue.

We now will move on to our alternate submission concerning the raising of the "permitted establishment fee". As you are aware, section 31A provides an exhaustive list of the costs that can be charged for "small amount credit contracts". It specifies that, a "permitted establishment fee" can be charged if it:

> *"reflects the credit provider's reasonable costs of determining the application for credit and the initial administrative costs of providing the credit under the contract."*

The recent Exposure Draft has now increased the permitted establishment fee to an amount not exceeding 20% of the adjusted credit amount. We note that new section 31A(4) will allow an independent review of the caps after 2 years of its operation. Although we welcome this independent review, we submit that there will be no industry to review after 2 years, as the 20%+4% cap is simply not viable for commercial sustainability of the sector. The Government has recently stated that:

> "[It] *recognises the value of this small amount lending sector as it fills an important gap in the market place*"[11],

yet the Government still has chosen to ignore the valid economic figures submitted by Cash Doctors, those of other credit providers in the small amount short term lending market, as well as the Joint Committee's recommendations, to demonstrate a mutually acceptable position.

Accordingly, we request that the Government revisit its caps on costs for SACCs once again. We submit that a fee of 20% is still not reflective of "the reasonable costs of determining the application for credit and the initial administrative costs of providing the credit under

[10] As above

[11] Discussion Paper "Strategies for Reducing Reliance on high-cost, short term, small amount lending" at page vii

the contract". We believe that the Government has not considered the true costs of determining an application for credit, and associated administrative costs in its setting of the cap. In order to provide full transparency to consumers, the industry and legislators alike, we invite Treasury to provide its economic modelling to substantiate its position that 20% (+4%) will allow a continued industry presence. Without such modelling to back up Treasury's recommendation, it would appear that Treasury has simply chosen to "double" its earlier 10%+2% without any justification based on real-world facts, leaving an arbitrarily-rounded figure that clearly does not represent any real costs of credit providers.

Treasury is not only failing to listen to the stakeholders in the debate, it has failed to acknowledge the comments made by the Committee Members in the Committee Report:

> *"before we could support the imposition of such a law, we would need to be satisfied that the caps had been carefully developed based on a study of the business models of industry participants and their costs. We recommend that the Productivity Commission or a similar agency be tasked to carry out this study and recommend pricing which would permit* [short term small amount] *lenders to achieve a reasonable return on capital."*[12]

As previously submitted, we are willing to assist Treasury in their economic modelling by providing an economic analysis of our costs against the proposed model in this submission.

Cash Doctors incurs a range of costs for each loan including the cost of a credit report, labour costs in carrying out responsible lending assessments, office costs including rent, interest on borrowed funds, telephone and internet, marketing and the cost of complying with Government requirements imposed by ASIC, the ATO, AUSTRAC and statutory EDR's, including licensing fees, taxes, professional indemnity insurance premiums, and the indirect costs of compliance of IT software development for product compliance, and staff compliance training.

For Cash Doctors the current average cost for processing each advance is $116. The below scenario shows our costs if we charge as per the rates currently being proposed:

Amount Borrowed	$420
Loan Period	21 days
Establishment Fee	$84 (20%)

[12] Parliamentary Joint Committee on Corporations and Financial Services Inquiry into Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011, December 2011, Comments of the Coalition Members and Senators at paragraph 1.22

Monthly Fee (30 days)	$11 (2.8% which is 4% pro-rate for 21 days)
Gross Revenue	$95
Cost of Loan	$116
Loss per Loan	$21

It is clear that applying the 20%+4% rate cap on the average cash advance of $420 would result in a loss of $21 per advance. Thus the costs Cash Doctors incur in processing an advance exceed this 20%+4% margin. We contend that the proposed cap on costs for these short term credit contracts have, again, not had any due consideration of the true costs of a loan for short-term lenders.

We therefore submit that the Government's proposed cap on costs in the first instance is unworkable, and should immediately be revisited based on sound economic modelling with direct input from industry. In the alternative, we submit that the maximum amount of permitted establishment fee in proposed section 31A(2) of the Code be increased from 20% to 27.5%, allowing businesses to continue to operate, albeit with very small margins. The result would be as follows:

Amount Borrowed	$420
Loan Period	21 days
Establishment Fee	$115.50 (27.5%)
Monthly Fee (30 days)	$11 (2.8% which is 4% pro-rate for 21 days)
Gross Revenue	$126.50
Cost of Loan	$116
Profit per Loan	**$10.50**

As you can see, at the submitted rate of 27.5%, Cash Doctors would only profit $10.50 from an average advance of $420. This is no "super profit", this is merely a small margin. This is in sharp contrast to the returns generated by the big banks and large financial institutions. Therefore, creating a climate which will allow reasonable returns for players in our sector is not an unreasonable request. In fact, this is the only way that the Government can stand true to its statement that the small amount lending sector fills an important gap in the market – it must allow us to continue to fill that gap. This gap is a sizeable section of the community (the Cash Doctors customer base in itself representing some 27,000 customers and growing) which would be left without access to their product of choice. Anything less than 27.5%, and particularly at 20%, would force us and other industry participants to cease operating, as a loss per average loan of $21 is clearly not sustainable.

Exposure Draft - the "Small Amount Credit Contract" caps on default fees

Section 39B specifies the amount of default fees that may be recovered under a SACC. In the tabled Bill, the section specified it was an amount that did not exceed "twice the adjusted credit amount". The recent Exposure Draft has deleted "twice the adjusted credit amount" and replaced it with an amount not exceeding "the amount prescribed by the regulations". Without seeing the regulations and what Treasury proposes as the cap on default fees, we are prohibited from commenting on the viability of this proposal, as tested against an existing operating model. For example, we are curious to see whether Treasury will increase or decrease the cap on default fees, or maintain the cap that exists in the tabled Bill, and would appreciate reasoning or economic analysis as to why this should change or not, as the case may be.

Exposure Draft - the Annual cost rate must not exceed 48% "at any time"

In the first instance, we submit that the 48% cap for all other contracts, is equally as unworkable as the "permitted establishment fee" outlined above. The proposed national cap of 48% particularly received damaging feedback from the Joint Committee:

> *"The committee acknowledges that fees should reflect the cost of lending. However, the committee does not consider that it is best practice to impose a fee ceiling that is calculated using an APR. This method distorts the actual cost to the borrower, and the cost to the lender, and is therefore not the appropriate regulatory tool.*[13]

We see from the latest Exposure Draft that not only has the 48% cap been retained, the Government has further compounded the potential damage to the sector as it has made it even more difficult for credit providers to calculate with any precision or certainty, as we will explain further.

Historically, the first Exposure Draft of the Bill included in section 32A a provision which provided that the "annual cost rate" could not exceed 48% "at any time". The tabled Bill then omitted this provision. The latest Exposure Draft now includes the provision once again in the form of 32A(1A). This provision has the effect of imposing the 48% cap on costs over the life of the loan (ie "at any time").

[13] Parliamentary Joint Committee on Corporations and Financial Services Inquiry into Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011, December 2011, at paragraph 5.235

Another change proposed in the recent Exposure Draft has been the removal of the definition of the "credit cost amount" for the purpose of the calculation of the annual cost rate in section 32B. Instead, the definition will be moved to "regulations" (which are yet to be published). So as it stands, there is no certainty from Government as to what costs are to be included in the 48% cap.

Further, section 32A(8) had certain assumptions in relation to continuing credit contracts that were to be used for the purpose of calculating the cap. This section has now been removed from the recent Exposure Draft. Will Treasury deal with the continuing credit contract assumptions in the regulations? The latest Exposure Draft does not indicate that they will.

As Treasury noted in the October 2011 Discussion Paper "Maximum Annual Cost Rate":

> *"The application of the annual cost rate to continuing credit contracts creates different issues. The ongoing nature of these contracts and the uncertainty as to how consumers will use the credit provided or the timing and amount of repayments makes its application more complex."*[14]

It is true that for continuing credit contracts, there is uncertainty as to the amount of credit that the customer will draw down, and the timing of repayments. The previous section 32B(8) aimed to overcome this by making certain assumptions about continuing credit contracts that could be relied on for the purpose of the 48% cap calculation. Therefore the removal of the assumptions for continuing credit contracts, with no indication as to what Treasury intends to do with continuing credit contracts, makes it difficult to make an informed submission on this point.

In its discussion about whether the section should be included in the Bill, Treasury stated in the October 2011 Discussion Paper that:

> *"The primary concern was whether* [the section] *would, in practice, require credit providers to check whether or not they exceeded the annual cost rate each time they charged a contingent fee or varied the interest rate."*[15]

To address Treasury's concern, Cash Doctors submits that the inclusion of section 32A(1A) would indeed force credit providers to re-calculate the costs of the loan each time a contingent fee is charged, or if a variation is made to the repayment arrangements during the contract (i.e. if the customer wishes to repay all or part of the loan early), or even when a default fee is charged. These practical difficulties may lead to inadvertent breaches of the 48% cap during the life of the loan, even though the credit provider had been compliant

[14] At page 3
[15] October 2011 Discussion Paper "Maximum Annual Cost Rate" at page 2

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with the cap at the outset of the contract. This inevitably will cause administrative complexities to credit providers' systems and processes leading to a burden on resources, as well as an uncertainty as to the contract's compliance with the legislation at any point in time**.** This provides an additional complexity with the 48% cap calculation, and for completion of feedback on proposals, we would suggest that the 48% rate cap is calculated only once during the life of the loan, and that is, at the time the contract is entered into. At the very least, this is maintaining the status quo with the existing State rate cap provisions upon which section 32 has been modelled, and with which credit providers have become accustomed since the introduction of the caps in 2008.

Also, as we have no commitment from Government as to what costs are to be included in the calculation of the cap, we are unable to provide any valuable submission on the operation of this section, as the parameters of the formula need to be detailed in the said "regulations" in order to test our operating model. Our submission on this section is therefore reserved pending publication of regulations that will define the relevant fees and costs.

Discussion Paper "Reforms in Relation to Small Amount Credit Contacts"

Treasury has said that this Discussion Paper:

> *"discusses potential reforms in relation to the regulation of small amount credit contracts* [ ]*, where it is proposed that the detail of the reforms will be implemented through regulations, rather than by amendments included in the Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011."*[16]

We note in the first instance that it is Treasury's intention to propose detail of the reforms in "regulations", however not all provisions the subject of these reforms have enabling provisions whereby the detail can be dealt with in regulations. For example, of sections 133AA – 133CD (relevant to credit providers) only section 133AA has an enabling provision whereby the detail can be prescribed by regulation. Further the proposals in relation to the use of direct debit payment options do not appear to stem from any principal section. We therefore query Treasury's statement here, and therefore the entire intention of the Discussion Paper and Treasury's overall strategy with the submitted results.

Notwithstanding the omitting enabling power that we have highlighted here, we have nonetheless addressed the "focus" questions raised in the Discussion Paper, and you can find answers to them in Annexure A of this submission.

[16] At page 1

As an overall observation, the Discussion Paper raises some overly intrusive operational restrictions and prohibitions on credit providers who offer small amount credit contracts, which alone, or in combination with the caps on costs, will severely affect the viability of the industry, and will considerably inhibit the customer's freedom of product choice. For example:

- The suggestion that repayments by direct debit be banned will immediately increase the rate of default and the charging of default fees. This will only compound existing debt and the customer will continue on a downward spiral of indebtedness. It is also an abject failure to recognise the continuing modernisation and reform of how the financial services sector now operates.
- The suggestion that successive loans be capped after the customer has filled a statutory quota fails to take into account that the customer, who may have never defaulted on a loan, and who may be happy with that loan product, will be forced into the market again to search for an alternative product, running the risk that it may be an inferior or even illegal product that is clearly not suitable for the customer's needs.
- The suggestion that all single repayment loans should be banned applies blanket assumptions about the customer's financial situation and ability to repay. Further, the customer may in fact choose to repay in a single repayment by the customer's own motivation to incur less fees, or because the customer simply wants the debt retired enabling them to move on.

In relation to the existing prohibitions that appear in the tabled Bill, such as multiple concurrent loans and increasing credit limits, we note the Coalition Members and Senators comments in the Committee Report that:

> *"The measures in the Bill involve highly detailed and prescriptive interventions in the business practices of* [small amount short term] *lenders. …**We believe these measures are undesirable in principle and unworkable in practice.**"*[17]

We submit that the Government should take stock of the comments made in the Committee Report, and consider removing these restrictions and prohibitions in their entirety. Alternatively, the Government should follow the UK OFT suggestion that these be developed into codes of conduct, reflecting best practice[18]. Accordingly, we are of the belief that the policy underlying these restrictions and prohibitions would be best dealt with

[17] Parliamentary Joint Committee on Corporations and Financial Services Inquiry into Consumer Credit and Corporations Legislation Amendment (Enhancements) Bill 2011, December 2011, at paragraph 1.20
[18] At page 7-8

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by providing detailed best practice in Regulatory Guide 209 – Responsible Lending Conduct, as opposed to mandating blanket rules in legislation or regulations.

In Closing

Cash Doctors customers already have the protection they need to make an informed decision about the loan product they want: they are subjected to a rigorous and responsible assessment of their financial capacity to repay a loan; they have control over how and when they apply for a Cash Doctors cash advance; and they receive an advance that is an appropriate amount with an appropriate repayment schedule for their individual financial situation and purpose.

These fully employed, IT savvy, and financially literate customers deserve to be listened to, and their needs catered for. We have demonstrated in this submission that the proposed cap on costs for both short term credit contracts and all other contracts under the 48% cap are unworkable. These caps on costs, compounded with the intrusive operational restrictions and prohibitions, will inevitably create a mass exit in the industry, leaving our fully employed, financially literate customers with little financial choice – thereby creating "financial exclusion" for a large section of the community - the very thing that Treasury have stated they wish to address. We have requested that the caps on costs should immediately be revisited based on sound economic modelling with direct input from industry.

We have demonstrated, in the alternative, that to allow survival of this market and customer choice of product within the confines of what we believe to be an ill-conceived policy of caps on costs, the maximum amount of permitted establishment fee for a small amount credit contract should be increased from 20% to 27.5%, allowing for a small profit margin which, by way of survival of the market, could just result in achieving the "financial inclusion" the Government so desperately seeks.

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Yours sincerely

Sean Teahan,
Co-Chief Executive Officer
CASH DOCTORS

Greg Ellis
Co-Chief Executive Officer
CASH DOCTORS

Enc – Annexure A

Annexure A

Responses to Discussion Paper "Reforms in relation to small amount credit contracts"

WEB-BASED DISCLOSURE STATEMENTS

Focus Questions:

(a) What information should the disclosure notices include, given that it should be short and succinct to maximise its impact?

Treasury has suggested that a high impact statement feature on credit providers websites such as the following:

> *'A short-term, high cost loan may not be your best option or appropriate for your needs. There are cheaper borrowing options and/or other assistance available to you. This statement is an Australian Government requirement under the National Consumer Credit Protection Act 2009''*

This would also include an explanation of the relevance of the ASIC MoneySmart website, and a link to that website (called hereafter the "Statement").

Treasury also suggests that the disclosure include:

- information on alternative sources of assistance and cheaper finance (for example, NILS, LILS or Advance Centrelink payments);
- a statement encouraging those with problems managing their finances to seek assistance from a financial counsellor; and
- appropriate links and/or phone numbers for financial counselling, welfare or legal assistance organisations.

Cash Doctors supports the promotion of financial literacy and the use of disclosures to assist consumers who are under financial stress. The Cash Doctors client-base has permanent employment and accordingly would not be eligible to access alternative sources of assistance and cheaper finance (for example, NILS, LILS or Advance Centrelink payments). Cash Doctors therefore submits that it is potentially misleading for Treasury to presume that every person that visits websites of credit providers offering SACC's and in particular the Cash Doctors website, firstly, "need" the assistance that the Statement suggests, secondly, are "eligible" for such assistance, and thirdly, that the options are "cheaper" than the product on offer in that particular website. It would be dangerous to apply such blanket presumptions to all recipients of SACC's, and also to all the credit providers of SACCs - the financial situation of each website visitor will be different, and the costs of each credit provider will be different. For these reasons, Cash Doctors is of the opinion that this prescribed information is not relevant to its customer base, and has the potential to confuse and mislead the customer about its options and about the Cash Doctors product. Accordingly, Cash Doctors does not support a requirement to include this particular information.

Cash Doctors is of the opinion that information for customers to seek assistance from a financial counsellor, with appropriate links and/or phone numbers for financial counselling, welfare or legal assistance organisations, should be detailed in the MoneySmart website rather than include such information on credit provider websites.

In keeping with our promotion of financial literacy, however, Cash Doctors would happily mandate the provision of a direct link to the MoneySmart website, as it already features on the cashdoctors.com.au website (see link http://www.cashdoctors.com.au/articles/free-financial-advice). As suggested by Treasury, the disclosure should be short and succinct to maximise its impact, and therefore not be overburden with prescribed statements when there is no guarantee that it would be read by a consumer in any event.

Further, it would be administratively burdensome for credit providers to continually update their website disclosures once details of a new alternative finance scheme or financial counsellor has been introduced (or ceased for that matter). Similarly, it is a costly exercise for Government to continually update the regulations for each new addition/cessation (for example, having to go through a regulatory impact analysis and producing an RIS, consultation process etc).

(b) Should the website and the shopfront disclosure have the same content?

Cash Doctors is of the opinion that for competitive neutrality between online and storefront credit providers, it is imperative that both mediums have the same disclosures.

(c) What is the appropriate placement for the storefront notice – for example, immediately next to the entry door, or on the door if no window or glass placement is available?

This question is not relevant to the Cash Doctors business as it operates solely online. However the effectiveness of the placement should be no more or less equivalent to the effectiveness of the placement of the disclosure on a credit provider's website. However, Cash Doctors cannot suggest how the "effectiveness" of both disclosures can be measured.

(d) What timing/placement would be most effective in providing information to consumers in relation to the website disclosure? For example, should it be displayed on every webpage, say as a banner on top of each page (this would allow for consumers to see the information irrespective of their entry page to the website), or should it be a pop-up box that must appear on the application page before the consumer can commence a loan application ?

Cash Doctors are of the opinion that the disclosure should not appear on every webpage (ie in a banner at the top of each page). This would be administratively burdensome to resources as the Cash Doctors website contains approximately 400 webpages. Cash Doctors suggests that the disclosure should appear, in order of preference:

(i) in the credit guide, which Cash Doctors has combined with the customer contract and information statement. This option is beneficial in that it provides that all the statutory disclosures are given at the same time, and in the same document. Upon reading the disclosures and contract, the customer is given the option to accept or reject the Cash Doctors offer, so the customer still has the power to make an informed decision as to whether to proceed based on the information disclosed prior to accepting the contract.

(ii) as a stand-alone disclosure document, to be given at the same time as the credit guide. It should also have the ability to be given in combination with the other disclosure documents (refer to the enabling provision in reg 28L(9)).

(e) What is the likely impact of requiring information about alternative options to be included in the Credit Guide? In particular, is the timing of the provision of this document likely to be helpful to consumers?

See response (i) in question (d) above. Please note, Cash Doctors does not have the means to measure whether the disclosure via the credit guide prior to the contract being entered into (or via any other means for that matter) would achieve its objective of being helpful to consumers.

(f) Are there any other alternatives to the delivery or method of disclosure that should be considered?

In order of preference, refer to options (i) and (ii) in question (d) above.

PROHIBITIONS ON MULTIPLE CONCURRENT CONTRACTS, REFINANCING AND INCREASING CREDIT LIMIT

Focus Questions:

(a) What would be the practical implications of requiring lenders to consider the borrower's best interests? It this approach was adopted, how would the content of the obligation be defined?

Cash Doctors considers in the first instance that for competitive neutrality in the marketplace, any changes that impose additional restrictions on lending should be applied to all credit providers (including ADIs) not just to those that offer SACC's. In this respect, we refer to the comments of the Coalition Members and Senators in the Committee Report that:

> *"The restrictions in the Bill specifically carve out Authorised Deposit-taking Institutions (such as banks and credit unions.) We cannot understand why. Competitive neutrality ought to be a core public policy principle. If you are going to intervene heavily in marketplace activity, you ought to take care to do so in a way which is neutral as between market participants. The government has failed to do this."*[19]

Cash Doctors considers that it would not be wise to introduce another subjective test of "best interests", as stakeholders as a whole are already having to grapple with the interpretation of the responsible lending terms such as making "reasonable enquiries and verification" and the double-negative term of "not unsuitable" for the customer. Generally, the Government should consider refining the responsible lending provisions, possibly by updating Regulatory Guide 209, or introducing prescriptive/proscriptive obligations rather than introduce more "open" terms such as the above. This would create clarity around these obligations with fixed requirements, such as introducing specific rules as to the "enquiries" to be made to determine whether the customer has any existing loans with other credit providers, as well as the rules to "verify" such information (for example, a credit check). (Note that Government has yet to introduce comprehensive or "positive" credit reporting, and therefore making these enquiries is limited to what the customer is willing to disclose at the time of application). In theory, once this information is in the credit provider's knowledge, it will need to be considered in the "suitability" test in order to satisfy s133.

(b) If exceptions are to be defined by a category of transaction (for example, by the characteristics or circumstances of the borrower), how are these categories to be defined? In particular, can these transactions be defined in a way that is clear and unambiguous as to when the exception applies?

Cash Doctors has submitted that the responsible lending requirements should be refined rather than introduce any new concept of "best interests". It has also submitted that a presumption of "unsuitability" currently exists and is used in the Cash Doctors lending model to achieve what is essentially already the "best interests" of the customer. Cash Doctors does not believe that creating exceptions defined by category of transaction will

[19] At 1.17

achieve with any more certainty that the contract is "unsuitable" or not in the "best interests" of the customer. Accordingly, Cash Doctors cannot provide any comment on the "categories" to be defined, and whether they can be defined with clear and unambiguous certainty.

(c) If the approach of providing for an unsuitability presumption was adopted, what circumstances or transactions should the presumption apply to?

As above.

REPEAT LENDING/SUCCESSIVE LOANS

Focus Questions

(a) To what extent is the repeated use of SACCs indicative of a class of consumers who may be experiencing psychological or social barriers to seeking advice or assistance? Where this is the case, will repeated disclosure (under Option 1) overcome or lower these barriers?

Cash Doctors makes the following observations in relation to Treasury's summary of the issue of repeat lending/successive loans.

Again, for competitive neutrality, it will be necessary to apply any changes here across the board so that ADIs and other non-SACCs providers are subject to the same rules. Treasury need to understand that a customer's financial stress could equally have stemmed from one, or a combination, of say, a $400k mortgage, a $10k personal loan, and/or $10k credit card issued by an ADI, rather than from a series of small loans for a few hundred dollars. Cash Doctors customers are financially literate and fully employed, 65% of whom have a clear credit history. This is not the customer type which Treasury are attempting to protect here ("financially vulnerable consumers"), yet credit providers will be required to comply with these rules just because they provide a SACC product? Surveys of our customers indicate that they choose to opt for the Cash Doctors product over the use of credit cards for short-term cash shortages because they feel it gives them more control over their finances without the long term commitment. It is with this feedback from our customers that we reject the proposition that multiple short term loans are inherently damaging to the consumer. Unlike other forms of credit, the consumer is not accumulating unsustainable levels of debt and, to their benefit, they are building up a positive credit history.

The Cash Doctors business model relies on the consumer being able to repay debt and in fact only recovers around a third of costs incurred when the consumer makes late payments or fails to repay some or all of the advance. This is a fundamental market mechanism that will ensure that credit is withdrawn for customers that no longer are able to repay.

Treasury needs to be concerned with the dangers of taking average data, as it has from the quoted research reports, and formulating policy to the “average”. In this case we have customers where unlimited loans may be quite “suitable” whereas on the other hand a single loan for another customer may be more “suitable”. The market should be unfettered to determine the appropriate loan practices based on the consumer experience and behaviour.

Notwithstanding the above, Cash Doctors supports a level of control on rollovers so that credit providers do not unduly profit from the customer’s difficult financial position. Rollovers are not permitted in the Cash Doctors business, and default fees are capped after a fixed period of time. However Cash Doctors believes that the solution is in refining the responsible lending provisions and/or guidance as suggested above.

In relation to the first question here, Cash Doctors can only answer from a reflection of its own customer experience derived from internal customer service surveys. The feedback received from our customers is that the Cash Doctors product provides a valid alternative to mainstream finance, and therefore there does not appear to be a correlation between the use of the product with any type of psychological or social barrier to seeking advice or assistance. In relation to the second question, Cash Doctors is also not in a position to state whether the repeated disclosure will overcome or lower these barriers.

(b) What are the advantages and disadvantages of the options considered above to address repeated use of SACCs? What should be the appropriate trigger for each such option?

Treasury has suggested the following options:

- an additional disclosure requirement;
- a presumption that the SACC is unsuitable (for example, the fifth loan if the trigger is four SACCs in a row within a specified period); or
- specific responsible lending obligations (for example, a requirement to conduct more detailed inquiries into the borrower’s financial circumstances to ensure the provision of credit meets their requirements or objectives).

Cash Doctors, again, are not in a position to state whether additional disclosure has any effect on customer’s intentions to borrow. Although if it is the Government’s view to proceed with the disclosure discussed in focus question 1 (the Statement), Cash Doctors would generally support that the Statement should also be given after a prescribed number of loans that are taken in succession within a prescribed time period with the same credit provider. Another alternative to the disclosure in the Statement, is to introduce the provision of a new statutory "Warning" stating that the customer appears to be in financial difficulty and that he or she should reconsider taking out a new loan. But from a compliance perspective, this disclosure would pose yet another disclosure document to be given at a different time period and unless automated, would be difficult to administer.

Cash Doctors does not consider that a "presumption of unsuitability" should be imposed after a prescribed number of loans are taken in succession within a prescribed time period with the same credit provider, as this is simply reversing the test in the responsible lending requirements. The same responsible lending requirements would apply to the test, so it is arguable whether reversing the test, having "unsuitability" as a starting point in the loan assessment, will produce any different result.

Further, if a financially literate customer who is not a "centrelink" recipient (which is the Cash Doctors customer) has a genuine short-term need for a 5th loan why should the Government intervene in the customer seeking to address that need? Consider the case where a customer is happy with the choice of product (and accepts the fees and understands the structure of the product, the fees, their repayment obligations etc) – why should they be forced to discontinue its use and be forced to spend time in the market looking for another suitable alternative? What if that suitable alternative does not exist? This proposal would in effect cause the restriction of credit available to consumers who can, and have proven to, afford to repay the credit, most of whom have chosen this type of short term credit from a number of mainstream alternatives. For those without valid alternatives, the outcome could be the cash economy, or at worst bankruptcy.

To put this into context, the US Federal Reserve's Report "Payday Holiday: How Households Fare after Payday Credit Bans"[20] highlights the effect of a total ban on "payday lending" in 2 US States (Georgia and North Carolina) by comparing the financial situation of households of States that are subject to a ban on payday lending against those which have payday lending available in the market. The Report's findings are that compared with households in States where payday lending is permitted, households in the banned states have bounced more cheques, complained more to the equivalent US office of fair trading about lenders and debt collectors, and filed for bankruptcy at a higher rate[21]. If we are to learn anything from the US experience it would be that a mass exit of the small amount short term lending market would have dire consequences for the financial health of consumers, and indeed compound "financial exclusion" – the very objective Treasury are seeking to address.

[20] "Payday Holiday: How Households Fare after Payday Credit Bans", Donald P. Morgan and Michael R. Strain Federal Reserve Bank of New York Staff Reports, no. 309, November 2007; revised February 2008

[21] As above, Abstract

We note that with other financial products, such as a credit card, there is no limit in the number of times a customer can make drawdowns, so we question whether it is appropriate policy to have such inconsistent rules across credit products.

Finally, we would suggest that imposing a cap on successive loans would create inconsistency within the SACC industry. What would be considered a "loan" - would it include refinanced loans, or rolled-over loans? For example, would the cap apply on a loan that has been rolled-over 5 times totalling a period of 6 months? How would this equate with 5 successive loans that totalled 6 months? We suggest Treasury employ a level playing field here and be mindful of possible avoidance that would inevitably result from such a restrictive proposal.

(c) What additional responsible lending obligations could apply, if that was required, in relation to repeat borrowers?

Refer to answer to focus question 2(a) above –introducing specific rules as to the "enquiries" to be made to determine whether the customer has any existing loans with other credit providers, as well as rules to "verify" such information (for example, a credit check). However, as stated above, there are limitations to these changes such as reliance on the customer's own disclosure of other existing loans without a positive credit reporting system allowing proper verification of the customer's disclosure. In theory, this will produce additional knowledge for the purposes of establishing the customer's financial situation and the suitability of the loan.

(d) Are there any other options that should be considered to regulate repeated use of SACCs?

No further suggestions other than above.

RESTRICTIONS IN RELATION TO SMALL AMOUNT CREDIT CONTRACTS WITH A SINGLE REPAYMENT

Focus Questions

(a) What effect will the introduction of the proposed cap on SACCs and other proposed reforms have on single repayment SACCs? Could it be expected that it will result in a reduction in this type of lending?

It will depend on what legislation is eventually settled in respect of the amounts of the cap, the disclosure in Item 1 (the Statement), and the changes in responsible lending, to determine if single repayment lending is reduced, although Cash Doctors expects it will have *some* effect on this type of lending. Cash Doctors notes that the responsible lending requirements presently in place should already have this effect - clearly, if the customer has no discretionary spending after the repayment is made, the contract should not have been deemed “suitable” in the first place.

(b) What would be the impact of introducing a ban on contracts with single repayments? How would this compare with the impact of a presumption in relation to suitability?

Before any ban is imposed on single repayments, consideration should be made to each individual’s circumstances. For example, if responsible lending checks reveal that the customer has no other loans and has income that leaves more than adequate discretionary spending after the repayment is made, there is no detriment to the customer in requiring a single payment. The responsible lending requirements already suggest that the amount and timing of repayment should always be relative to the customer’s income and expenditure. Further, the customer may opt to pay the loan off in one repayment, so that the customer can move on from the debt. Not all customers want to be indebted over a longer period of time with a drawn-out repayment schedule, which only incurs more fees to the customer and more costs to the credit provider. The customer’s needs must be taken into account, and this is also a fundamental principle to the current responsible lending requirements, and therefore should be considered a key principle in this debate.

(c) Are there any other options that should be considered to address SACCs with single repayments?

As stated above, refining the responsible lending requirements is an option. For example, RG 209 could provide guidance that a loan with a single repayment “may suggest” that the loan is unsuitable, and that adequate enquiries should be made into the customer’ financial situation. Cash Doctors does not consider as a valid option, an outright ban on single repayment loans (for the reasons given in focus question in 4(b)), or imposing a presumption of unsuitability (for the reasons given in focus question in 3(b)).

USE OF DIRECT DEBIT REPAYMENT OPTIONS

Focus Questions

(a) What are the likely outcomes from banning direct debits? In particular would it be expected to result in an increase in the rate of defaults?

Cash Doctors does give the customer the option to pay via direct debit or via other payment means, and a direct debit is therefore not a “take it or leave it” option for the Cash Doctors product.

Generally speaking, the Cash Doctors customer base is technologically savvy appreciating the ease from which electronic direct debits can be used to satisfy their loan commitments. Cash Doctors considers that introducing a ban on direct debits would hugely disadvantage the customer as they do not have the convenience of repayment that is available in the form of electronic direct debits. Customers would be forced to remind themselves of the loan repayment dates, and if missed, inadvertently place themselves in default, exposing them to increasing transaction costs and default fees which may have not occurred if the obligation to repay rest with the credit provider. Cash Doctors therefore considers removal of this option would increase the instances of default.

To overcome the problems anticipated by Treasury, customers should always have the option of payment method and therefore a ban on *mandatory* repayment by direct debit (or other repayment method) could be a proposal.

Cash Doctors also notes that to ban direct debits just for SACCs would create an unfair disadvantage amongst SACC credit providers and other debt providers (including ADI’s, gas, electricity, phone providers). A level playing field is required here.

A direct debit can always be cancelled and the direct debit authority expresses this. Therefore, it does not necessarily operate as “priority” payment as suggested.

(b) Should consumers always be provided with choices for making repayments (for example, a minimum of three options)? If so, what other payment options would be considered appropriate?

Cash Doctors does not think it is necessary to prescribe by regulation the available repayment choices for the customer, however, a requirement that other repayment means *are disclosed* (say in the credit contract, and this can be achieved by amending section 17 of the Code) may be a viable alternative. Overall, good practice would indicate that credit providers do suggest other means of repayment during the loan application process, including Bpay and by electronic transfer, but over-regulation of the disclosure here is not necessary.

(c) What would be the impact of suspending the use of a direct debit request where it has been rejected three times because of insufficient funds in the borrower’s account?

Cash Doctors believes that intervention with the customer after a failed direct debit (enquiring into why the direct debit failed) is good practice, and policy around this concept would be welcomed (as opposed to the credit provider "sitting on its hands", allowing the customer to continually default in payments). There are often many reasons why a direct debit fails and it is not always indicative that the customer is in financial stress so Cash Doctors would not generally support an outright suspension without understanding the reason for the failed direct debit. Cash Doctors considers that it would only be reasonable to suspend a direct debit request where intervention with the customer reveals that the customer is in financial hardship and cannot make repayment. Treasury should consider mandating intervention rather than automatic suspension without reason.

(d) What would be the impact of increasing the triggers for credit providers to provide a Form 11 direct debit default notice (for example, when the consumers signs a direct debit authority)?

Cash Doctors supports giving a Form 11 at the time it signs a direct debit authority, or alternatively, incorporate the terms of the Form 11 into the direct debit authority. A prescribed form of the direct debit authority would also assist and ensure consistency amongst credit providers and transparency for customers.

INTRODUCTION OF A PROTECTED EARNINGS AMOUNT (PEA)

Focus Questions

(a) What are the likely outcomes from the introduction of a PEA? In particular, information is sought on the level of repayments charged to borrowers under SACCs, both currently and under the foreshadowed 20/4 cap, and whether they would ordinarily be less than 35% of the borrower's income?

The PEA is a reasonable concept and as discussed above in relation to single payment loans, should already underpin current lending assessments in line with responsible lending requirements. For the Cash Doctors customer, 97.5% of scheduled payments are under 35% of the customer's gross income, and about 95% of scheduled payments are under 35% of the customer's net income.

Cash Doctors are of the opinion that the PEA principle should be detailed in Regulatory Guide 209, stating that a repayment amount of 35% percentage is generally good practice for assessing whether any credit contract is suitable for a customer, not just for SACCs.

(b) What are the advantages and disadvantages of each of the models considered above?

Cash Doctors agrees with the issues anticipated by Treasury (ie definition of centrelink recipient, fluctuations in income etc) would pose problems with administering a prescribed PEA. As suggested above, Cash Doctors considers that it may be beneficial to set a PEA as guidance to the responsible lending requirements in RG209, which would apply equally to all customer credit contracts, and not just SACCs.

(c) How would the PEA interact with existing responsible lending obligations?

See above.

(d) Are there any particular categories of borrower who would particularly benefit from the introduction of a PEA requirement?

As above, the principle should apply to all customers, at least as a starting presumption in determining "suitability" of contract, but clearly, customers who are solely centrelink recipients (with no other income source) would benefit from this requirement.