

Introduction

Super Nexus Pty Ltd (**Nexus**) welcomes the opportunity to comment on the reforms proposed by the *National Consumer Credit Protection Amendment (Credit Reform Phase 2) Bill (the Bill)*.

The principals of Nexus have operated a number of Cash Converter franchised businesses since 1989. Nexus currently operates 9 outlets throughout South Australia and Victoria.

In addition to trading in second-hand goods, the franchised businesses offer a number of consumer finance products including pawn broking loans, unsecured micro-loans and unsecured personal loans. With the exception of pawn broking loans these products are regulated by the *National Consumer Credit Protection Act 2009 (the Act)* and its subsequent amendments and associated regulations.

Nexus supports, in principle, the introduction of the phase 2 reforms contained in the Bill, however has concerns regarding application of the proposed anti-avoidance measures detailed in Schedule 6 of the Bill. It is these concerns which are the focus of this submission.

Pawn broking

A pawn transaction is an arrangement where a consumer pledges possession, but not ownership or title, of an item in exchange for cash, usually on a very short term basis. Pawn is a long established and well understood form of short term financial support. A fundamental feature of pawn transactions is they do not constitute a credit transaction for the purposes of the Act, and do not create a debt. The consumer has the right, *but no obligation*, to repay the any amount to the pawnbroker or to redeem their goods.

For these reasons, and due to the fact that pawn transactions are separately regulated by state based instruments, the Act does not consider pawn transactions to constitute credit¹, and the National Credit Code (**the Code**) explicitly excludes pawn transactions².

Proposed anti-avoidance provisions

The systematic anti-avoidance provisions proposed under Schedule 6 of the Bill aim to prevent a person from taking part in a scheme which, among other things, seeks to avoid

¹ See ASIC *Information Sheet 101*

([http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Does_the_new_credit_regime_apply.pdf/\\$file/Does_the_new_credit_regime_apply.pdf](http://www.asic.gov.au/asic/pdflib.nsf/LookupByFileName/Does_the_new_credit_regime_apply.pdf/$file/Does_the_new_credit_regime_apply.pdf))

² See section s6(9) of the Code

application of the Act. The definition of a *scheme* is exceedingly wide and encompasses almost all commercial undertakings a legitimate business could contemplate. It seems likely that any pawnbroker will, in the ordinary course of their business, engage in a “scheme” for the purposes of the proposed s323A. For the purposes of determining this scheme is wholly or partially for the purpose of avoiding application of the Act, a number of factors are required to be considered, including³:

- the change in financial position of the pawnbroker that has resulted, or may reasonably be expected to result, from the scheme;
- any similarities with a credit contract, mortgage, guarantee or consumer lease;
- any representation connected with the scheme made by the pawnbroker to a consumer;
- whether the pawnbroker considered the consumer’s ability to comply with the financial obligations of the contract;
- whether one party is operating at a loss under the transaction (for example, in the case of “diamond sale” transactions).

The exposure draft commentary indicates the intent of the Bill is to apply the factors without regard to the intention of the person potentially engaging in a scheme. This approach introduces a risk that activities which are not an act of avoidance, such as pawn broking, become subject to the Act despite clear current intention to the contrary.

There are material penalties for those who engage in a scheme which, in any way, seeks to avoid application of the Act is up to 2 years’ imprisonment as well as substantial fines.

While legitimate pawn transactions are clearly not avoidance behaviour, the characteristics outlined above include a number exhibited by pawn transactions, such as:

- Pawns are typically advertised or promoted as a “loan” transaction. While in conflict with the transactions underlying technical character this practice is consistent with long held consumer understanding.
- Consumer capacity to repay is typically not assessed in the case of a pawn transaction as the consumer has no obligation to make any payments whatsoever.
- A consumer may, in some cases, be considered to be operating at a “loss” where they elect to pawn an item for less than the market value of the goods.

Nexus is concerned pawn broking may inadvertently become subject to the Act due to application of the anti-avoidance provisions without regard to the intent of those potentially

³ See Schedule 6 of the Bill

engaging in a scheme under the Bill. This concern was also raised in the Regulation Impact Statement⁴. Currently the definition of a *credit contract* under the Act appropriately excludes pawn contracts, however the fundamental purpose of the avoidance provisions is to incorporate conduct which has a similar character to a credit contract (i.e. exhibits the characteristics set out in the Bill) but does not meet the technical definitions contained in the original Act. As such, the definition of a credit contract cannot continue to be relied upon to exclude transactions such as pawns from the Act.

Should pawn transactions become inadvertently subject to the Act via application of the proposed avoidance provisions it is likely to be commercially impracticable to simultaneously comply with both the Act and the separate state based legislation designed specifically to regulate pawn broking activity.

As an example, application of the *National Consumer Credit Protection Amendment Regulation 2012 (No. 4)* introduces a cap of total fees and charges on small amount credit contracts. This cap relies on application of an up-front fee (of 20%) and a maximum of 4% per month thereafter. Compliance with this approach is unreasonable for pawnbrokers based in Western Australia, who are prohibited from charging establishment fees under the *Pawnbrokers and Second-hand Dealers Act 1994 (WA)*.

A similar situation currently exists in New Zealand arising from the unresolved conflicts between the *Secondhand Dealers and Pawnbrokers Act 2004 (NZ)* and the *Credit Contracts and Consumer Finance Act 2005 (NZ)*. While the acts were intended to work harmoniously, subsequent application and enforcement of the *Credit Contracts and Consumer Finance Act* in respect to pawn transactions several years after drafting have created a situation where pawn brokers cannot practically comply with both acts. Additionally, the consumer is required to be provided with mandatory disclosure documents under both acts which, if complied correctly, describe the product differently. While such mandatory disclosure obligations are intended to assist consumer understanding, they in fact materially harm product comprehension in this instance.

Conflicting application of multiple legislative instruments creates significant uncertainty for an industry which is typically serviced by small business and, more importantly, creates confusion and hampers understanding for consumers who are seeking access to simple finance solutions.

⁴ See *Phase Two of the National Credit Reforms: Addressing Avoidance of the National Consumer Credit Protection Act 2009: Regulation Impact Statement*, pp25-26.

Recommendation

It is clear pawn transactions are not intended to be dealt with under the Act. State based legislation already exists to effectively regulate the industry and the character of the transaction is fundamentally different to credit regulated by the Act. Accordingly, Nexus recommends pawn broking be explicitly excluded from the Act in a similar manner to its treatment under the Code. This approach provides clarity to both the industry and consumers and avoids the uncertainty and cost associated with unclear application of the avoidance provisions.

Nexus would be pleased to provide further information or to discuss any matters raised in this brief submission which may assist Treasury. Questions can be directed to Andrew Kamp from Balance Professional Services at andrew.kamp@balanceservices.com.au or 08 8228 0500.

