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The Australian Financial Counselling and Credit Reform Association Inc

1. Introduction

The Australian Financial Counselling and Credit Reform Association (AFCCRA) is pleased to provide this submission to the Financial System Inquiry. AFCCRA is the national peak body for financial counsellors and consumer credit solicitors in Australia and therefore represents the interests of low income and other disadvantaged groups in society in their dealings with the finance sector.

The deregulation of the financial system following the release of the Campbell Report in 1981 has had a significant effect on our constituents. This submission will firstly outline the issues arising from a deregulated financial system and then make recommendations.

2. Effect of Deregulation

The competitive forces at work in a deregulated financial services market place have resulted in a greater range of services and products for consumers to choose from. While this has meant that consumers in general have been able to purchase the best financial product or service to meet their particular needs at the best price, it has never the less worked to the disadvantage of some sections of our society.

Greater choice has resulted in a two tiered financial services market. At one end of the spectrum are financial institutions such as banks, credit unions and building societies while the other end of the spectrum is typified by finance companies.

Banks, credit unions and building societies typically provide:

- a wide range of services;
- relatively low interest rates on consumer credit;
- special discount rates to groups such as professional associations;
- access to independent dispute resolution mechanisms; and
- prudential security.

Finance companies typically provide:

- narrower range of products;
- relatively high interest rates on consumer credit;
- lack of independent dispute resolution mechanisms; and
- poorer prudential security.

Knowledge, ability and resources are required in order to access the appropriate and cost effective products offered by the banking end of the spectrum. Knowledge and skills enable consumers to discriminate between the many products offered in order to effectively match needs with products in a cost effective fashion. In a complex market place people who do not possess the required skills and knowledge purchase inappropriate products at a higher cost and this places them at a distinct disadvantage.

Access to consumer credit is often governed by economic resources such as level of income and availability of assets. Banks do not usually make consumer credit available to low income, assetless consumers unless a guarantee can be provided. In general AFCCRA does not support the use of third party guarantees as the consequences of default effect a wider section of the community (ie., family and friends) than just the debtor. The only viable option is often the finance companies who provide a narrower range of products at a higher cost to consumers.

An example may serve to illustrate the cost impact of accessibility issues. Due to its low level of income (eg less than $800 net per fortnight) Family A is not able to secure a loan through such sources as banks or credit unions. They are only able to secure a loan through a finance company. In contrast, Family B has a moderate to high level of income and is able to secure a bank loan. Both families need to replace an essential household item such as a refrigerator. The table below outlines the cost differences to each family.

Family	net fnly income	Purchase Price	annual interest rate	mthly payment for 12 mth loan period	total paid (including interest)	total interest paid
A	$800	$999	26.4%	$95.63	$1147.56	$148.56
B	$1625	$999	13.9%	$89.65	$1075.80	$76.80

While the overall interest cost to family A of $148.56 may not appear to be significant, it does represent 18.6% of their net fortnightly income. By comparison, the interest cost to Family B of $76.80 represents only 4.7% of their net fortnightly income. This lower relative cost of credit for family B is far easier to accommodate into a family budget than the cost of credit to family A. For family A, the relatively higher cost of credit could have an impact on the provision of other essential family expenses such as food, housing, electricity and medical needs. For families experiencing financial hardship resulting from low levels of income the extra $148.56 over the twelve months of the contract period could mean the difference between the payment of an essential utility account such as an electricity account or not.

A further consideration is the impact of new technology on groups such as the intellectually or physically handicapped, minority and marginalised groups such as remote aboriginal communities, and an aging population who find it difficult to adapt to new ways of carrying out their financial transactions. The introduction of new electronic technologies such as Automatic Teller Machines (ATMs), and internet access to financial services and products has in many cases resulted in the charging of a service fee for the use of traditional services such as over the counter assistance. These service fees are often not attached to the use of new electronic technologies such as ATMs. Consumers who do not have access to, or who are not able to use new technologies are therefore placed at a financial disadvantage. The ever increasing adoption of new technologies in the financial services industry means that this will become an escalating problem. This will effectively deny many consumers from disadvantaged groups in our society cost effective access to financial services.

The deregulation of the financial system has seen the adoption of a user pays principle in relation to provision of financial services. In particular fees and charges on retail transaction accounts (RTAs) have been introduced by most providers of financial services. While the loss of $5 per week in account charges may not be significant for a medium to high income family, it may have a significant impact on the budget for a social security recipient. Although the fees and charges may be calculated on a financially consistent basis, their impact on low income and disadvantaged consumers is inequitable.

In short, consumers from low income, minority, or marginalised groups in our society are often disadvantaged in their interactions with a deregulated finance market as they do not have the knowledge, skills, ability, or resources to access appropriate and cost effective products and services. They are often further financially disadvantaged with the introduction of new technology.

Those who can least afford it, often end up paying more for financial services and products through higher fees and charges, higher interest rates, and purchase of inappropriate products. They also lack effective means of redressing disputes arising from their dealings with the finance industry which can leave them further financially disadvantaged.

From our perspective two keys issues emerge from the deregulation of the financial system:

- **cost effective access to appropriate services for all members of society should be included as a key consideration, along with economic performance, and**
- **availability of greater choice does not necessarily lead to a fairer and more equitable market place for consumers.**

3. Recommendations

Many of the issues referred to above result from the adoption of inconsistent practices and the loss of a customer focus across the financial sector. These are therefore key issues needing to be addressed in any framework for the future of the financial system. This can be achieved with the adoption of:

- effective and appropriate regulation;
- consistent and industry wide codes of practice;
- consistent and industry wide dispute resolution mechanisms;
- ongoing monitoring and review of the financial sector;
- prudential supervision and security for the whole of the financial sector; and
- effective consumer feedback mechanisms and representation.

Effective and appropriate regulation is essential in the financial sector. This does not mean that the principle of competition is replaced with an overall requirement for regulation. It does mean that in areas of basic consumer protection regulation is still to be seen as essential. Consumer lending is an area where consumers are vulnerable to disadvantage associated with lack of essential information and vulnerable to exploitation. The adoption of the Consumer Credit Code will provide a degree of protection in this area. Compliance and effectiveness of redress available under the code will require ongoing monitoring by a central national body. It is not sufficient to leave such monitoring to each individual state or territory government as consistency in the application of the legislation was a principle underlying the development of this national uniform credit legislation.

Codes of Practice have already been developed and adopted by sections of the financial sector, an example being the Banking Code of Practice. Codes of Practice need to be developed and implemented for all sections of the financial sector under the oversight of a single body. In this way consumer needs and protections can be implemented consistently and the needs of particular sections of the financial sector can be accommodated. Ideally oversight should be placed with a central body such as the Australian Competition and Consumer Commission (ACCC) or equivalent body.

Consistent and industry wide dispute resolution mechanisms are essential if consumer rights are to be protected in their dealings with the financial sector. To be effective independent dispute resolution schemes need to:

- provide equity of access, particularly for NESB consumers, low income and other disadvantaged consumers, and isolated consumers;
- adopt processes which inform consumers of their rights under the scheme;
- ensue decisions which are not only fair and equitable but are seen to be fair and equitable;
- are accountable to consumers;
- are independent of industry and are seen to be independent of industry;
- are based on the principles of natural justice; and,
- are subject to performance review from a consumer perspective.

The Federal Bureau of Consumer Affairs (the Bureau) has been developing benchmarks for such schemes and the finalisation of these benchmarks should be proceeded with swiftly. Government should then actively promote, encourage the adoption of, and oversee the implementation of such dispute resolution schemes.

Ongoing monitoring and review of the financial sector needs to be undertaken by a centralised body such as the ACCC. Specific areas to be monitored include:

- introduction and setting of fees and charges on RTAs;
- examination of lending practices;
- impact of new technology;
- operation of Codes of Practice; and
- operation of independent dispute resolution mechanisms.

Prudential supervision and security for the whole of the financial sector is essential in a society where retirement saving is strongly encouraged. In an aging population security for long term savings is essential and these must be protected against failure of financial institutions. Prudential supervision and security for all financial institutions offering retirement or long term investments should be provided by a single body such as the Reserve Bank.

Effective consumer feedback mechanisms are essential if the financial sector is to be kept aware of consumer needs and requirements and if government is to be informed of the impact of its policies and directions. Consumer feedback should be sought specifically from those groups in society who would be most directly effected by changes to the financial sector and government policy. Disadvantaged and disempowered groups in society are often the most vulnerable to changes in the financial sector. It is the responsibility of government to ensure that such consumer representation processes are adequately funded and accountable to both the group being represented and to government.

In conclusion AFCCRA acknowledges that the effects of regulation are often undermined by the adoption of complex regulatory systems with multiple regulatory bodies. However we also believe that consistent and easily implemented regulation and supervision is possible which is not at odds with the benefits of a competitive and diverse financial systems market place.

We recommend that:

- regulation be retained in the areas of consumer protection;
- prudential requirements be broadened to include the whole financial sector under a single prudential supervisory body such as the Reserve Bank or other suitable body;
- the development and implementation of Codes of Practice and independent dispute resolution mechanisms be actively encouraged and supervised by a suitable body such as the ACCC;
- effective consumer representation be adequately funded by government; and
- ongoing monitoring and review of the financial sector be undertaken by a body such as the ACCC.

Further copies of this submission are available by contacting Ms Wendy Schilg at the AFCCRA office on (06) 281 4544.