

# CONSUMER CREDIT LAW REFORM AND UNIFORMITY

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## IMPLEMENTATION

### OFFICIAL SOUTH AUSTRALIAN POSITION

Statement to Parliament by the Minister for Consumer Affairs on 7 May 1985:

- (1) "The Government has decided that the time has come to recognize that the Credit Act needs major overhaul, not simple tinkering. What is needed is credit legislation which is effective to protect all who borrow money, regardless of source, in a manner which does not advantage or disadvantage one group of lenders over another. The Government seeks legislation which is competitively neutral, which does not stifle innovation in the financial market place, which does not impose undue burdens or costs, and which provides effective protection for borrowers."
- (2) "The Government has therefore decided to withdraw the Bills presently before the House and proceed to substantially adopt the uniform legislation enacted in New South Wales, Victoria and Western Australia. The Government will prepare for the consideration of this Parliament a Credit Act, a Credit (Administration) Act and a Credit Home Finance Contracts Act, based upon the New South Wales equivalent of that legislation. So far as is practicable, the Government will adopt not only the spirit but also the letter of the uniform law; it will preserve the existing South Australian law wherever it represents a demonstrably superior regulation of a business practice. It will also advance a number of proposals for improvements on the model. Specifically, the reforms to be effected by the Bills the Government has decided to withdraw will be reflected in the new legislation which I hope can be put before this Parliament before the end of this year."

Government policy (Sir Humphrey Appleby: "It's not for me to comment on matters of Government policy; you must ask the Minister").

I am responsible for *administration* in this area.

H.A.: "While it has been Government policy to regard policy as the responsibility of Ministers and administration as the responsibility of officials, questions of administrative policy can cause confusion between the administration of policy and the policy of administration, especially when responsibility for the administration of the policy of the policy of administration conflicts, or overlaps with, responsibility for the policy of the administration of policy."

So on the basis of that admirably lucid explanation of the role of Minister and civil servant, I feel free to mention two major difficulties with which S.A. is faced in implementing uniform credit laws.

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## THE UNIFORM CREDIT LEGISLATION IS OBSOLETE

Let me take you back to 1972 when the Molomby Report was presented and the Standing Committee of Attorneys-General resolved to develop uniform State legislation based on the recommendations of that report. As most of you would know, the then Attorney-General for South Australia expressed the view that uniform legislation would take some considerable time to develop, probably at least five years, and he indicated that he regarded the matter as too urgent to be subjected to a delay of that order. He therefore proceeded to have legislation drafted in South Australia and this legislation was eventually enacted as the Consumer Credit Act and the Consumer Transactions Act, both of which come into operation in 1973.

History has proved that the Attorney-General's forecast was correct, although he was rather optimistic with his assessment of the time it would take to develop uniform legislation. It was exactly thirteen years from the presentation of the Molomby Report to the proclamation of the uniform legislation in New South Wales and Victoria. More importantly, I fear that much of the time spent during that thirteen years was devoted to endless drafts and re-drafts of legislation designed to implement the original recommendations and that those responsible for this exercise may have failed to recognise the extent to which the credit market was changing during that time.

In 1972, most significant consumer credit was provided by finance companies. Very little credit was provided by way of credit cards. Bankcard did not exist and banks were not substantially involved in the provision of consumer credit. The share held by credit unions of the consumer credit market was far smaller than it is today and building societies operated only in their traditional field of lending to those building or buying a home.

In 1972 then, the Molomby recommendations and the South Australian credit legislation that followed them, seemed to be on the right track. The exemptions in favour of banks, building societies, credit unions and the like were neither greatly unfair in any competitive market sense, nor were they significantly inappropriate in any consumer protection sense.

But look what has happened to the consumer credit market during that thirteen years. The market share held by finance companies has shrunk considerably; credit cards are now all pervasive — most of our wallets are now bulging with magnetised plastic rather than watermarked paper; the share of the market now occupied by bank personal loans has increased enormously, as has the share occupied by credit unions; and building societies are extending their operations far beyond the lending of money for housing. A series of advertisements appeared in the daily papers in Adelaide over the last few weeks by the Co-operative Building Society of S.A. for what it described as the "link account". The advertisement claims that this account "replaces all the others. It replaces your savings account. Your cheque account. Your creditcard. Your bankcard. And it even operates an automatic teller machine."

It is interesting to note that this sort of foray by a building society into a non-traditional area does necessitate some fancy footwork on its part, presumably because of the way in which the Building Societies Act is presently framed. The small print at the bottom of this advertisement reads: "Cheques are drawn by you on the National Australia Bank for whom the Co-op is acting as agent. The Co-op. is neither drawer nor

drawee of the cheques. The Co-op will also be acting as agent for you in provision of the cheque facility. Full details available on request." What those "full details" are and whether a consumer who requested them would be able to understand them, remains a matter for conjecture.

So the financial system is undergoing a period of major change. Not only are the distinctions between the various institutions involved in the field becoming more and more blurred, but those institutions are changing their methods of operation even within their traditional areas.

In 1972, almost all finance company lending was by way of fixed term loans, involving a separate transaction and separate documentation for each loan. If a consumer owed money to a finance company on a loan to purchase a motor vehicle and then wished to borrow further money for some other purpose before paying off the previous loan, the second loan would be documented as an entirely separate transaction. Finance companies are now moving away from this type of lending and encouraging the use of open-ended credit arrangements, particularly for loans of smaller amounts. They are establishing lines of credit against which a consumer may draw from time to time up to an agreed limit, with interest being charged on the outstanding balance from time to time.

This type of open-ended credit arrangement is, in terms of the uniform credit legislation, a continuing credit contract. However, the provisions in the legislation relating to these contracts were really designed to cover budget accounts and similar credit facilities offered by retail stores. There has been some tinkering with the original recommendations, but it seems that no-one has studied the way in which the market is actually operating at present and attempted to draft provisions which will apply sensibly and properly in that market.

For example, the uniform legislation provides that the annual percentage rate, in the case of a continuing credit contract, is the percentage rate applied to the chargeable amount for each billing cycle multiplied by the number of billing cycles in one year. That would have worked perfectly well in 1972, when retail stores operated on the basis of monthly billing cycles and monthly calculations of interest. However, some of the finance companies now offering continuing credit arrangements do so not on the basis of monthly billing cycles but *daily* calculations of interest. The legislation simply does not recognise this method of operation and the result is that some of these finance companies have been given a temporary exemption from some significant provisions of the legislation. (I certainly hope that this *will* be temporary, because the real answer to this problem is to amend the legislation.)

The States that have enacted the uniform credit legislation have agreed in principle that the legislation should be extended to cover the lending institutions that are presently exempt. However, they also indicated that they wanted to get their legislation "up and running" (hardly surprising, in view of the thirteen year delay) and that they would broaden the scope of the legislation by subsequent amendments. Although I can certainly understand this attitude, I cannot help wondering whether some tinkering with the uniform provisions, rather than a complete re-thinking of the whole legislation, will produce a satisfactory result.

Of course, there are those who oppose any expansion of the scope of credit regulation as being a "regulatory" move inconsistent with the

general "deregulation" of the financial system presently being pursued. I must emphatically disagree with that approach. It seems to me that two of the major recommendations of the Campbell and Martin Committee Reports were, first, that entry barriers to the financial market should be lowered, if not removed, and, secondly, that those controls (whether on entry or otherwise) that need to remain should apply equally to all participants in the marketplace. The catch-phrase for this second concept was "competitive neutrality". Others have described it as making sure that all players (even if there are more of them) play the game by the same rules. The expression used in the United States of America to describe this policy is "creating a level playing field".

No-one in Australia, to my knowledge has suggested that there is no need for regulation of the provision of consumer credit. Indeed, Mr. Justice Michael Kirby, when he was Chairman of the Australian Law Reform Commission, said:

"In our apparent enthusiasm to de-regulate the Australian financial system, it is important not to forget legitimate issues of community fairness — such as the proper preservation of banker/client privacy and adequate rules for consumer protection."

"Competitive neutrality" therefore demands that the regulation of the provision of consumer credit should apply across the board. The extension of credit legislation to cover banks, building societies, credit unions etc. would go a long way towards creating a level playing field and is entirely consistent with that concept.

As I have said, I can understand why those States that have just introduced consumer credit legislation for the first time are reluctant to make major changes to it at this stage. However, unless something is done in the very near future to extend the scope of coverage of this legislation, there is a grave danger that the practices of those institutions that are presently exempt from the legislation will become so firmly entrenched that it will become difficult to change them.

In today's credit market, the policy of concentrating the regulation of consumer credit on a sector of the finance industry whose market share is diminishing is quite indefensible. It is also quite illogical in the context of the Molomby Committee recommendations that credit regulation should have regard to substance rather than form. Anyone who suggested that the old hire purchase legislation should not apply to all those who provided credit by way of hire purchase would have been laughed at. Why, then, should the protection given to the consumer in today's market depend upon the legal character of the credit provider he or she deals with? And why should a building society which has diversified into consumer lending be permitted to behave in a manner which would be quite illegal for a retailer or finance company?

So, one difficulty facing South Australia is that the adoption of the uniform package as it now stands would not make any significant contribution to the levelling out of the credit playing field.

## **SIMPLICITY VERSUS UNIFORMITY**

I have previously quoted from Sir Humphrey Appleby who is regarded by some as the guiding inspiration for the civil service. In the interests of proper balance, I should quote also from the right Honourable James

Hacker, M.P., the Minister to whom Sir Humphrey is responsible in that admirable series "Yes Minister". The Minister observed, after his first twelve months in office, that the three articles of civil service faith were:

- it takes longer to do things quickly;
- it's more expensive to do things cheaply; and
- it's more democratic to do things secretly.

If the experience with credit laws is any guide, a fourth article might be added to that list:

- it is more complicated to do things uniformly.

The party presently in Government in this State has as part of its platform the objective "simplification of the laws"; an objective which is, not surprisingly, whole-heartedly supported by business interests. Part of the same platform is the policy objective to "establish uniform credit legislation", which is also strongly supported by business interests.

Of course, there is no inherent reason why there should be any conflict between these two policy objectives. The reality, however, is very different.

A new word was added to my vocabulary recently: oxymoron. Apparently this is the correct description for a "pointed conjunction of seemingly contradictory expressions", i.e. an expression involving a contradiction in terms. According to some of the more cynical members of our community, typical examples of oxymorons are: military intelligence, happily married, Government efficiency, honest politician, and even, perhaps, practical academic. Well it seems to me that the concept of simple and uniform credit legislation is positively oxymoronic.

It is easy to treat this lightly, but it really does bring into sharp focus a major difficulty facing South Australia in considering the adoption of the uniform credit laws package. We can make the credit laws simple, or we can make them uniform, but it does not seem possible to do both. If we simply adopt the uniform package we will be criticised by a large section of the business community, particularly small businesses which operate only within this State, for enacting legislation which is unnecessarily complicated, difficult to understand and to comply with and expensive to administer. However, if we decide to retain the concepts of the uniform package, but to re-draft the legislation so that it is much more simple and straightforward, we shall be criticised by another large section of the business community, particularly financial institutions which operate on a national basis, for failing to honour the commitment to uniformity.

As I mentioned earlier, the present policy is to go down the uniformity route, except where existing South Australian law represents a demonstrably superior regulation of a business practice. Present indications are that extremely few provisions would come within that exception. However, I must say that I am becoming increasingly concerned about the task facing small businesses in this State in attempting to comply with the uniform legislation and the task facing my officers in attempting to administer and enforce it.

Not only that, but events which have occurred since the New South Wales, Victorian and Western Australian Acts came into operation have demonstrated some fairly fundamental flaws in the drafting of that

legislation. Scarcely a day goes by without me receiving a letter or telex from one or more of those States proposing an exemption to be conferred by proclamation, regulation or order in council. I have no quarrel at all with any exemption designed to cater for some isolated situation which the Act has inadvertently caught and which does not need to be regulated. However, a great many of these exemptions have become necessary because of deficiencies in the legislation.

Since the Minister's statement on 7 May 1985, many businesses have found that the legislation does not deal appropriately (or at all, in some cases) with the method by which they conduct their business. Thus there have been exemptions proposed or conferred in relation to:

- continuing credit contracts for the supply of petrol or the hire of commercial passenger vehicles;
- continuing credit contracts providing for an insurance premium management account with a particular insurer;
- credit provided for the purchase of goods for the purpose of carrying on a business where the goods are to be incorporated into fixtures on land;
- credit provided by a particular company for the purpose of or in connection with the production of meat and wool for re-supply;
- credit provided for the purpose of contributing capital monies to the cost of producing a film;
- credit provided by a particular company for the purpose of a franchise offered by that company;
- credit provided in relation to the re-financing of an insurance premium or registration fee in respect of a hire purchase agreement entered into before the new legislation became operative;
- a transaction that commenced as an un-regulated contract but became a regulated contract by virtue of a variation;
- credit provided by way of factoring of book debts;
- credit provided in connection with a commodity futures clearing operation (this submission ran to 16 pages);

and many others which are far too complicated to attempt to summarise here.

The point I am making is the illusory dream of uniform credit legislation is in grave danger of becoming a nightmare. I only hope that all the exemptions that are granted because of some deficiency in the legislation will eventually be taken care of by appropriate amendments to the legislation. However, it seems that if the applications for exemption continue to pour in at the present rate, it could be some time before those responsible for the administration of this legislation are able to see the wood for the trees.

At least South Australia has one advantage over the other States and Territories in that it has had consumer credit legislation in operation here for some twelve years. The legislation is by no means perfect and it suffers from the same major deficiency that I mentioned earlier, namely a failure to recognise the changing nature of the consumer credit market. However, it does provide, in a relatively simple and straightforward way,

similar protections to consumers in this State as are provided by the far more complicated legislation comprising the uniform package. It is not for me to say whether the South Australian Government will proceed to enact the uniform package by the end of this year, as foreshadowed by the Minister. However, there is always a flurry of legislative activity in the period leading up to an election and it is quite possible that the priority presently given to this project will change over the next month or so. Speaking personally, I would prefer to wait until the uniform package has settled down, the teething problems have been taken care of, the exemptions granted to overcome deficiencies have been revoked and replaced by appropriate amendments, and uniform provisions have been agreed upon to extend the coverage of the legislation to those credit providers who are presently exempt from it.

I am therefore rather tempted to follow the example set by Sir Humphrey Appleby and to advise my Minister that the adoption of the uniform credit laws at this stage would comprise a courageous decision. This would undoubtedly result in the project being deferred for some time, at least until after the next election.