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Howell, Nicola (2009) *National consumer credit laws, financial exclusion and interest rate caps : The case for diversity within a centralised framework.* Competition and Consumer Law Journal, 17(2). pp. 212-233.

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National consumer credit laws, financial exclusion and interest rate caps: the case for diversity within a centralised framework

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Abstract

Australia is going through a major reform of consumer credit regulation, with the implementation of a proposal to transfer regulatory responsibility from the State and Territory Governments to the Commonwealth Government. While the broad policy approach is supported, the reform process has missed a significant opportunity to engage directly with issues of financial exclusion and with the potential role of regulation to reduce financial exclusion. The imposition of an interest rate cap can limit the impact of financial exclusion. However, the future of the existing interest rate caps is uncertain, given the diversity of approaches, and the heated debate that surrounds this issue. In the absence of support for regulatory initiatives to increase the availability of low cost, small loans, permitting regulatory diversity on this issue of interest rate caps, within an otherwise centralised regulatory framework., can minimise the impact of financial exclusion on consumers.

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1. Introduction

In 2008, the Council of Australian Governments (COAG) announced that responsibility for consumer credit regulation would be transferred from the State and Territory Governments to the Commonwealth Government.[1] This decision followed the Productivity Commission's recommendation earlier that year for such a shift in regulatory responsibility.[2]

The main impetus for the change was the desire for total uniformity and a 'seamless national regime'.[3] There is also an expectation that national regulation will lead to a more responsive regulatory regime, one that can respond quickly to changes in market practice and conditions. The slow pace of change in the current State and Territory based regime has been regularly highlighted as a serious failing of the regime.[4]

For the most part, this change from a State-based regime to a Commonwealth regime has been welcomed by commentators, industry and consumer groups, and the implementation of the proposals is proceeding relatively rapidly.[5] However, the proposals and the surrounding discussion have missed a significant opportunity to engage with the issue of financial exclusion, and the extent to which the regulatory framework can facilitate a reduction in financial exclusion. In this article, financial exclusion is defined as 'the lack of

[1] Council of Australian Governments, Council of Australian Governments Meeting 3 July 2008, at http://www.coag.gov.au/coag_meeting_outcomes/2008-07-03/index.cfm, viewed 22 April 2009.
[2] Productivity Commission, *Review of Australia's Consumer Policy Framework: Final Report*, Canberra, 2008, p 107 (Recommendation 5.2).
[3] Council of Australian Governments, above n 1.
[4] Productivity Commission, Final Report, above n 2, p 101.
[5] The National Consumer Credit Protection Bill 2009 was introduced into the Commonwealth Parliament on 25 June 2009.

access by certain consumers to appropriate low cost, fair and safe financial products and services from mainstream providers',[6] and the particular concern is of access to small loans.

This article therefore examines the extent to which the issue of financial exclusion might be addressed by the regulatory proposals for consumer credit. There is an absence of any consideration of regulatory initiatives that might encourage the availability of low cost, fair and safe small loan products. However, there are two aspects of the regulatory system that may operate in a more preventative sense. Obligations to lend responsibly can limit the extent to which consumers facing financial exclusion enter into unaffordable loans, and interest rate caps restrict the availability of loans that many regard as unaffordable and unsafe. In the absence of any initiatives to facilitate access to appropriate small loan products, I argue that the introduction and maintenance of these more preventative measures is critical if the risks of financial exclusion are to be minimised.

However, the fate of the current interest rate cap regulation in the new regulatory environment is, at the very least, uncertain. Currently, four jurisdictions (New South Wales, Victoria, Queensland and the ACT) impose an interest rate cap on consumer credit products,[7] and the remainder do not. However, as discussed later in this paper, some other jurisdictions had previously indicated some support for an interest rate cap.

[6] This is the working definition suggested in Chant Link and Associates, *A report on financial exclusion in Australia*, November 2004, p 58.
[7] See Consumer Credit (New South Wales) Special Provisions Regulation 2002, reg 7(1); Consumer Credit (Queensland) Special Provisions Regulation 2008, reg 3; Consumer Credit Regulation 1996 (ACT), reg 5; Consumer Credit (Victoria) Act 1995, ss 39, 40.

The merits of an interest rate cap or ceiling have been hotly debated both in Australia and in other jurisdictions for many years and there is little consensus about whether an interest rate cap is an appropriate regulatory tool, and if so, how such a cap should be structured.[8] The different approaches to regulating for an interest rate cap in the States and Territories will be 'examined' in Phase Two of the implementation plan for the transfer of credit regulation.[9] However, an agreed solution will not be easy to find, given the current diversity of regulatory approaches, and the political heat that accompanies this issue.

If a consensus view on the appropriate regulatory response is not able to be reached, I argue that there may be a case for permitting a level of diversity in the otherwise centralised regulatory framework. This would enable the retention of interest rate caps in those jurisdictions that support this regulatory approach, at least as an interim measure until a more definitive assessment can be made of the effectiveness of such measures.

[8] In the Australian context, see for example, N Howell, J Davidson and T Wilson, *Interest rate caps: Protection or paternalism?*, Centre for Credit and Consumer Law Research Paper, 2008 (summarising the views of some key stakeholders – consumer advocates, microlenders, mainstream lenders, and regulatory staff); Office of Fair Trading (Qld), *Managing the cost of consumer credit in Queensland*, Discussion paper, 2006; N Ashton, *Payday lending report – draft literature review*, Consumer Action Law Centre, 2008; T Wilson, 'The inadequacy of the current regulatory response to payday lending' (2004) 32 *Australian Business Law Review* 193; C Field, 'Pay Day Lending – An Exploitative Market Practice' (2002) 27(1) *Alternative Law Journal* 36. For overseas discussions, see for example, Department of Trade and Industry (UK), *The effect of interest rate controls in other countries*, 2004; I Ramsay, *Access to credit in the alternative credit market*, Paper prepared for the Office of Consumer Affairs, Industry Canada, and the Ministry of the Attorney-General, British Columbia, 2000; L Drysdale and K Keest, 'The two-tiered consumer financial services marketplace: the fringe banking system and its challenge to current thinking about the role of usury laws in today's society' (2000) 51 *South Carolina Law Review* 589; Michael Stegman 'Payday Lending' (2007) 21(1) *Journal of Economic Perspectives* 169; R Mann and J Hawkins (2007) 'Just Until Payday' (2002) *UCLA Law Review* 50; C Johnson, 'Payday Loans: Shrewd Business or Predatory Lending' (2002) 87 *Minn. L. Rev.* 1; T Durkin, 'An economic perspective on interest rate limitations' (1993) 9 *Georgia State University Law Review* 821.

[9] Australian Government, *National Consumer Credit*, undated, available at http://www.treasury.gov.au/documents/1381/PDF/NCC_Brochure_02102008.pdf, viewed 22 April 2009.

To set the scene, this article first summarises the current regulatory arrangements for consumer credit in Australia, and the history and rationale for the proposed transfer of regulatory responsibility from the State and Territory governments to the Commonwealth government. The proposals reflect a view that centralisation will provide benefits to consumers and businesses in the form of reduced compliance costs, increased interstate trade, ultimately leading to increased competition and welfare benefits for consumers, consistent consumer protection standards across Australia; and increase regulatory responsiveness to changes in the market.

While acknowledging the broad support for the proposal to transfer regulatory responsibility, the article next focuses on the extent to which the regulatory proposals have engaged with the issue of financial exclusion. Although the proposals have not expressly mentioned this issue, the regulatory approaches of a responsible lending obligation and interest rate caps regulation may be considered to have a positive impact on financial exclusion, in the sense of minimising the harm that can be caused by financial exclusion.

The article then focuses on the issue of interest rate caps as a regulatory approach, as the future of the current interest rate caps in the national regime is uncertain. I suggest that, given the divergent approaches to this issue, it is likely to be difficult to arrive at a consensus, or near consensus view on the appropriate outcome. I argue that the risk of interest rate caps being excluded from the national regime is a real one, and that this will have a negative effect on efforts to deal with financial exclusion.

Given this conclusion, the article then explores the case for permitting some regulatory diversity in the otherwise centralised national regime, specifically to deal with the issue of interest rate caps. Total centralisation of consumer regulation does pose some risks for consumers, by way of potentially reduced standards, and reduced opportunities for regulatory experimentation and local responsiveness. I argue that permitting regulatory diversity on interest rate caps to remain is both a pragmatic response in the face of diverse approaches, and a necessary response in the absence of more expansive regulatory initiatives to facilitate the availability of fair, safe and affordable small loans to those consumers at risk of financial exclusion.

2. The current and proposed regulatory framework for consumer credit law

Consumer credit transactions in Australia are currently regulated by the State and Territory Governments, with the Commonwealth Government only having a role in relation to the imposition and enforcement of generic fair trading standards on credit providers.[10]

The main regulatory instrument is the Uniform Consumer Credit Code ('UCCC'). The UCCC had its genesis in the Australian Uniform Credit Law Agreement 1993 ('the Uniformity Agreement'),[11] and operates in each State and Territory through a template legislation arrangement. The text of the UCCC is set out in a Schedule to the *Consumer Credit*

[10] See Australian Securities and Investments Commission Act 2001 (Cth), Part 2, Division 2.
[11] Available at www.creditcode.gov.au.

(Queensland) Act 1994 (Qld), and each of the other Australian States and Territories have passed legislation implementing the UCCC in the local jurisdiction.[12] The Uniformity Agreement and the UCCC were the result of many years of negotiations, and the history of credit law reform in Australia shows a long-held concern with achieving uniformity.[13]

Despite the considerable efforts involved in replacing the pre-existing and non-uniform State and Territory credit regulation with the UCCC, there has been regular criticism of the effectiveness of the State/Territory based regime. Of most concern has been the increasing diversity in the legislation applying to consumer credit,[14] and the significant delays in progressing amendments to the legislation. Transfer of regulatory responsibility for consumer credit from the States and Territories to the Commonwealth has often been cited as a solution to these and other problems with the current system. [15]

Most recently, criticisms of the current system were aired in the inquiry into the consumer policy framework, conducted by the Productivity Commission in 2007-2008. In relation to the regulation of consumer credit, the Productivity Commission agreed with many of the criticisms, and ultimately recommended that:

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[12] Consumer Credit (New South Wales) Act 1995 (NSW), s5; Consumer Credit Act 1995 (ACT), s4; Consumer Credit (Northern Territory) Act1995 (NT), s4; Consumer Credit (South Australia) Act 1995 (SA), s 5; Consumer Credit (Tasmania) Act 1996 (Tas), s5(1); Consumer Credit (Victoria) Act 1995 (Vic), s5; Consumer Credit (Western Australia) 1996 (WA), s5(1). Note that, in Western Australia and Tasmania amendments made to the UCCC do not come into force automatically, but must be proclaimed by the Governor after a draft of the proclamation is approved by both Houses of Parliament (see Consumer Credit (Western Australia) Act 1996 (WA), ss5(2), 5(3)); Consumer Credit (Tasmania) Act 1996 (Tas), ss5(2), 5(3)).

[13] See generally S Cavanagh and S Barnes, *Consumer credit law in Australia*, Butterworths, North Ryde, NSW, 1993, pp 7-11.

[14] Diversity occurs in the areas of permitted diversity (clause 12 of the Uniformity Agreement); and also due to individual jurisdictions passing additional legislation that applies to consumer credit contracts (eg s28 of the Fair Trading Act 1992 (ACT).

[15] For example, R Grady, 'Should Credit Go to the Commonwealth? Yes!' (2007) 23(6) *Australian Banking and Finance Law Bulletin* 82 at 83.

> Responsibility for the regulation of credit providers and intermediaries providing advice on credit products ('finance brokers') should be transferred to the Australian Government, with enforcement to be undertaken by the Australian Securities and Investments Commission (ASIC) (Recommendation 5.2).[16]

The Productivity Commission argued that implementation of this recommendation would:

- Reduce compliance costs for businesses, as there will be a uniform law governing credit transactions across Australia;
- Increase the responsiveness of the regulatory regime to changes in the market. Amending the UCCC has been notoriously slow, and the delays associated with amendment have sometimes been drivers for unilateral, and non-uniform, reform affecting consumer credit,[17] thus contributing to the problem of non-uniformity;
- Reduce consumer confusion about the laws that apply to them;
- Increase regulatory consistency between credit providers and other financial services providers (thus also reducing compliance costs); and
- Minimise the potential for regulatory gaps.[18]

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[16] Productivity Commission, *Final Report,* above n 2, 107.
[17] M Cowman, 'Out of Sync : Bringing Consumer Credit Regulation Back into Line' (2007) 81(1-2) *Law Institute Journal* 60 at 62-63. For example, in relation to the ACT credit card amendments introduced in 2002, the ACT Chief Minister and Attorney-General explained: 'Although foreshadowed changes to the consumer credit code are still on the ministerial council's agenda, the matter has not progressed as quickly or as well as the government had anticipated. Accordingly, as Ms Tucker has introduced this bill, we are prepared to support it as an interim measure.' Chief Minister, John Stanhope, ACT, *Parliamentary Debates*, ACT Legislative Assembly, 29 August 2002, 3083.
[18] Productivity Commission, above n 2, pp 100-101.

This recommendation was received positively by the Commonwealth, State and Territory governments. Subsequent to the Productivity Commission's report, the Council of Australian Governments (COAG) agreed to transfer regulatory responsibility for consumer credit from the States and Territories to the Commonwealth, by way of a referral of powers, to create a 'seamless national regime'.[19]

The proposal to transfer all responsibility for consumer credit regulation to the Commonwealth Government is consistent with the approach taken for the regulation of other financial services. The Australian Securities and Investments Commission (ASIC) is the sole agency responsible for the industry-specific consumer protection regulation of the banking, insurance and investment sectors,[20] with the States and Territories only having a concurrent role in relation to the economy-wide fair trading laws (for example, the prohibitions against misrepresentations and misleading or deceptive conduct).[21]

However, this is a different approach to that being pursued in the new Australasian Consumer Law. This will proceed by way of template legislation, with the State and Territory governments retaining enforcement powers in relation to the application of the legislation in their respective jurisdictions.[22]

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[19] Council of Australian Governments, above n 1.
[20] See chapter 7 of the Corporations Act 2001 (Cth).
[21] Fair Trading Act 1989 (Qld), Part 3, Division 1;Fair Trading Act 1990 (Tas), Part 2; Fair Trading Act 1992 (ACT), Part 2, Division 2; Fair Trading Act 1987 (NSW), Part 5; Consumer Affairs and Fair Trading Act 1996 (NT), Part 5, Division 1; Fair Trading Act 1987 (SA), Part 10, Division 2; Fair Trading Act 1999 (Vic), Part 2; Fair Trading Act 1987 (WA), Part 2, Division 1.
[22] Commonwealth of Australia, *An Australian Consumer: Law Fair markets – confident consumers*, Barton ACT, 2009, p 97.

The implementation of the COAG decision will take place in two phases.[23] Phase One is currently being progressed through the National Consumer Credit Protection Bill 2009. The Bill was introduced into the Commonwealth Parliament in June 2009, and a Senate Economics Committee report on the Bill recently recommended some minor changes to the text, and to the timing of implementation.[24] The Government has agreed to some, but not all, of the Committee's recommendations, including its recommendation to delay the commencement date of the legislation by a further six months, to 1 July 2010. [25]

If enacted, this legislation would see the text of the current UCCC re-enacted as the 'National Credit Code' in Commonwealth legislation. It would also result in the introduction of a new licensing regime for credit providers and intermediaries, responsible lending conduct obligations, additional sanctions and powers for ASIC, and improved access to dispute resolution and consumer remedies.[26]

The legislation will also require a referral of powers from the State and Territory governments,[27] however, at the time of writing, the referral legislation had not been released.

[23] Australian Government, *National Consumer Credit*, above n 9.
[24] The Senate Economics Legislation Committee, *National Consumer Credit Protection Bill 2009 and related bills [Provisions]*, 2009, available at http://www.aph.gov.au/senate/committee/economics_ctte/consumer_credit_09/report/report.pdf.
[25] The Hon Chris Bowen MP, *Consumer credit reforms – Senate amendments*, Media release No 017, 17 September 2009.
[26] The Hon Chris Bowen MP, *National Consumer Credit Protection Reform Package*, Media release No 002, 25 June 2009.
[27] See Ministerial Council on Consumer Affairs, *Joint Communiqué Ministerial Council on Consumer Affairs Meeting*, Friday 15 August 2008, pp 2-3, http://www.consumer.gov.au/html/download/MCCA_Meetings/Meeting_20_15_Aug_08.pdf viewed 22 April 2009.

Phase Two of the implementation program will involve extension of the legislation to cover small business and investment lending, and enhanced conduct obligations to stem unfavourable lending practices, including 'an examination of State approaches to interest rate caps'.[28] Phase Two legislation is due to be in place by mid-2010,[29] although given delays to the implementation of Phase One legislation (originally due to be implemented by mid-2009)[30] it may be that the timeframe for Phase Two legislation will also be amended. It is assumed that the form of referrals by the States and Territory governments will provide for continued legislative and enforcement authority in respect of the areas of current diversity that are to be considered in Phase Two (including interest rate caps legislation).

At the conclusion of this implementation plan, the total centralisation of consumer credit regulation in Australia will be complete, and the State and Territory governments will no longer have a role. In particular, COAG has agreed that the States and Territories will 'repeal all relevant legislation in line with phase two … of the implementation plan by mid-late 2010'.[31] At a broad policy level, these proposals have been welcomed by stakeholders, and the reform program is well underway. However, missing from the proposals appears to be any considered discussion of financial exclusion, and the respective roles of the regulatory framework and the market in addressing this issue. It is to this issue that I turn next.

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[28] Australian Government, *National Consumer Credit*, above n 9.
[29] Australian Government, *National Consumer Credit*, above n 9.
[30] Australian Government, *National Consumer Credit*, above n 9.
[31] Council of Australian Governments, *National Partnership Agreement to Deliver a Seamless National Economy*, Attachment A (Implementation Plan), items 11 and 27.

3. Financial exclusion and the new national consumer credit regime

The existence of financial exclusion in Australia should be of concern for governments and others interested in credit policy, and the proposed changes to the regulatory framework for consumer credit provide an opportunity for examining this issue and possible solutions.

In Australia, only a very small minority of consumers have no access at all to mainstream financial services or to the financial system more broadly. Data from 2003 suggests that only 0.8% of the adult population owned no financial products, and only 6% owned only a transaction product and no other financial product.[32] In part, this probably reflects the fact that welfare and other government payments are normally required to be paid into a bank account, rather than delivered by cash or cheque. If financial exclusion is defined as a lack of access to financial products and services, then it can be argued that there is a very low level of financial exclusion in this country.

However, in Australia, it seems more useful to understand financial exclusion by focusing on access to the relatively safe and affordable products and services that are available in the mainstream market. Thus, a 2004 report defined financial exclusion in Australia as:

[32] Chant Link and Associates, above n 6, p 120. This contrasts with some other jurisdictions, where small, but significant populations have no engagement with the financial system: Financial Services Authority (UK), *In or Out Financial exclusion: a literature and research review*, Consumer research report No 3, 2000, p 21.

> the lack of access by certain consumers to appropriate low cost, fair and safe financial products and services from mainstream providers.[33]

In the credit context, particular concern has been directed to the lack of availability of small, short term loans from mainstream lenders, or community providers, and the increasing availability of very high cost products from the fringe or micro lending market.[34] These latter products, including payday loans, are thought to be unsafe and exploitative by many consumer advocates and other commentators.[35]

A concern about safe and affordable products in credit markets reflects an understanding that, like utility services such as electricity and water, some financial services should be treated as essential services, and efforts should be made to ensure that they are accessible to all for a reasonable cost. For consumers on low incomes, small amount consumer credit that is used to cover emergencies and/or smooth out the costs of large purchases can be considered to be an essential financial services.[36]

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[33] Chant Link and Associates, above n 6, p 58.

[34] For example, Consumer Affairs Victoria, *The Report of the Consumer Credit Review*, Melbourne, 2005, p 72.

[35] For a summary of the views of a number of consumer advocates, see Howell, Davidson and Wilson, above n 8, p 113. See also D Wilson, *Payday Lending in Victoria- a Research Report,* Consumer Law Centre Victoria, (2002) p 83; C Bruch. "Taking the pay out of payday loans: Putting an end to the usurious and unconscionable interest rates charged by payday lenders" (2000) 69 *University of Cincinnati Law Review* 1257, especially Part V. For a comment on the 'upside' of payday lending, see S Ben-Ishai *Regulating Payday Lenders in Canada: Drawing on American Lessons* CLPE Research Paper No. 16/2008. Available at SSRN: http://ssrn.com/abstract=1128147, pp 5-7.

[36] Office of Fair Trading (UK), *Vulnerable consumers and financial services: the report of the Director-General's Inquiry*, OFT255, 1999, p 19.

The extent of financial exclusion in Australia is difficult to estimate.[37] However, the potential consequences for both individuals and the wider community are significant, and this warrants attention being given to the mechanisms – regulatory and non-regulatory – that can reduce the extent of financial exclusion. From the regulatory side, attention should be given to initiatives that facilitate or encourage the offering of fair, safe and affordable products, and to initiatives that limit the availability of unfair, unsafe, and unaffordable products, and therefore minimise the consequences of financial exclusion.

Despite considerable discussion of financial exclusion issues in recent years,[38] the issue has not been directly considered in the current credit reform proposals.

Financial exclusion is only obliquely raised in the Productivity Commission's report, in its discussion on the needs of vulnerable and disadvantaged consumers.[39] The Productivity Commission does not make any specific recommendations in this chapter of the report, explaining instead that some of the other recommendations in the report will be particularly beneficial for vulnerable and disadvantaged consumers. In relation to consumer credit, the Productivity Commission suggests that:

> Strengthening credit market regulation, including through requiring all finance brokers and credit providers to be members of an approved alternative dispute

[37] N Howell and T Wilson, 'Access to consumer credit: the problem of financial exclusion in Australia and the current regulatory framework' (2005) 5 *Macquarie Law Journal* 127, at 131-132.
[38] For example, Chant Link & Associates, above n 6; C Connolly and K Hajaj, *Financial services and social exclusion*, Financial Services Consumer Policy Centre, University of New South Wales, Sydney, 2001; Financial Services Authority (UK), *In or Out? Financial Exclusion: a Literature and Research Review*, Consumer Research Report 3 (2000); J Devlin, 'A Detailed Study of Financial Exclusion in the UK' (2005) 28 *Journal of Consumer Policy* 75; ANZ *Community Development Finance in Australia: A discussion paper*, May 2004: Howell and Wilson, Access to consumer credit, above n 37.
[39] Productivity Commission, *Final report*, above n 2, p 297.

> resolution scheme, is likely to be particularly beneficial to those most at risk in this area.[40]

There is also no explicit discussion of financial exclusion issues in the COAG agreement on consumer credit regulation, or in the explanatory memorandum for the National Consumer Credit Protection Bill. However, the proposed new obligation for responsible lending, and the existence of regulatory mechanisms to reduce the availability of loans with particularly egregious features (for example, very high cost loans, and loans secured by household goods) may have an impact on the extent to which unfair, unsafe and unaffordable products are offered to consumers who are financially excluded.

Responsible lending obligation

As noted above, the legislation will introduce a new responsible lending obligation on credit providers and credit advisers. The explanatory memorandum notes that:

> Responsible lending conduct regulation encourages prudent lending and leasing to continue and imposes sanctions in relation to irresponsible lending and leasing.[41]

As currently drafted, the new responsible lending provisions oblige credit providers, credit brokers, and other intermediaries to ensure that the loan offered is not unsuitable for the

[40] Productivity Commission, *Final report*, above n 2, p 299

[41] Explanatory Memorandum, National Financial Services Consumer Protection Bill 2009, p 81, para 3.16.

consumer; and to assess that the consumer has the capacity to meet the financial obligations under the loan without substantial hardship.[42]

There has been some strong criticism of the timing, effectiveness and workability of the proposed provisions, from both industry and consumer groups,[43] and amendments to address some of these concerns have been announced by the responsible Minister.[44] However, the broad parameters remain unchanged.

A responsible lending obligation does not necessarily facilitate the availability of 'appropriate low cost, fair and safe' credit products to consumers currently at risk of financial exclusion. However, neither should it prevent mainstream lenders from providing appropriately structured credit products to consumers on low incomes.[45] Imposing an upfront obligation on all credit providers and advisers to lend responsibly could go some way towards reducing the extent to which consumers enter into unaffordable loans, and where a more appropriate alternative is available, should facilitate a consumer taking out such a loan. However, on its own, a responsible lending obligation cannot ensure that an appropriate alternative is available.

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[42] See generally National Consumer Credit Protection Bill 2009, chapter 3.

[43] See for example, submissions on the exposure draft legislation made by the Australian Bankers Association, Consumer Action Law Centre, and Consumer Credit Legal Centre NSW. All submissions are available at http://www.treasury.gov.au/consumercredit/content/consultation/submissions/submissions.asp?round=1&subName=Exposure%20Draft:%20National%20Consumer%20Credit%20Regime%20Legislation.

[44] The Hon Chris Bowen MP, *Consumer credit reforms – Senate amendments*, Media release No 017, 17 September 2009.

[45] T Wilson, 'Values driven innovation or inadequate self-regulation?: The effective regulation of Australian banks as service providers to low income consumers' (2008) 21 *Australian Journal of Corporate Law*, 258 at 270.

Price regulation through interest rate caps

The responsible lending obligation discussed above is new to credit regulation in Australia. In contrast, imposing an interest rate cap on credit products is a regulatory approach that has existed for many years in some jurisdictions. There are currently three different approaches to interest rate caps regulation. In New South Wales, Queensland, and the ACT, a cap of 48% is imposed on credit contracts regulated by the UCCC, and the cap is calculated inclusive of fees and charges (although the formulas used are not completely consistent across the three jurisdictions).[46]

In Victoria, a cap of 48% is imposed on unsecured credit regulated by the UCCC, and a cap of 30% imposed on secured credit regulated by the UCCC. The caps are imposed on the interest component alone, and there is no regulation of the level of fees and charges that can be imposed.[47] The remaining jurisdictions have no cap or ceiling on the cost of credit, although some have previously considered the issue.

In South Australia, a 2007 report of the Parliamentary Economics and Finance Committee recommended "consideration of capping annualised interest rates and fees/charges", suggesting also that further research was needed.[48] At the time, the then Minister for

[46] Consumer Credit (New South Wales) Special Provisions Regulation 2002, reg 7(1); Consumer Credit (Queensland) Special Provisions Regulation 2008; Consumer Credit Regulation 1996 (ACT), reg 5.
[47] Consumer Credit (Victoria) Act 1995, ss 39, 40.
[48] Economics and Finance Committee, Parliament of South Australia, *Consumer Credit and Investment Schemes*, Sixty-fourth report, 2008, recommendation 4.

Consumer Affairs indicated that an interest rate cap would be introduced,[49] however, to date, only a Private Members' Bill has been introduced into the South Australian Parliament.[50]

In Tasmania in 2008, the Minister for Corrections and Consumer Affairs indicated that the government was looking at an interim measure to deal with fringe lending issues prior to the Australian Government taking over responsibility for credit regulation, however, no specific details appear to have been released.[51]

It has also been reported that West Australia was considering introducing an interest rate cap,[52] however, the West Australian government has not announced any decision in this regard.

No government has abolished an existing interest rate cap since the UCCC came into force. The recent Consumer Credit Review in Victoria did examine whether a cap on the total cost of credit be introduced in Victoria (similar to that in NSW), but was not convinced that such an approach was warranted.[53]

While some jurisdictions that do not currently have an interest rate cap may have previously indicated support for the introduction of an interest rate cap, it seems unlikely that these

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[49] The Hon Jennifer Rankine, Minister for Consumer Affairs, *Days are numbered for payday lending "rogues"*, Media release, 21 October 2007, available at http://www.ocba.sa.gov.au/assets/medicomms/mrelease_lawsrogues.pdf.
[50] Consumer Credit (South Australia) (Pay Day Lending) Amendment Bill, introduced by the Hon D.G.E Hood (Family First) on 18 February 2009.
[51] Parliament of Tasmania, Hansard, Legislation Council, Thursday 4 September 2008, p 35.
[52] Productivity Commission, Final Report, above n 2, p 449.
[53] Consumer Affairs Victoria, above n 32, p 117

jurisdictions will take any legislative action, pending the consideration of the issue in Phase Two of the implementation program.[54]

As with a responsible lending obligation, the role of interest rate caps in addressing financial exclusion is largely by way of minimising the risks of harm arising from financial exclusion. Interest rate caps play a preventative, rather than facilitative, role in improving access to fair, safe and affordable products.

As with a responsible lending obligation, an interest rate cap does not directly encourage the availability of affordable small loan products. Subject to the effectiveness of its coverage, an interest rate cap could reduce the availability of products that are unaffordable, or otherwise unsafe (for example, due to rollover facilities),[55] for consumers at risk of financial exclusion. This form of regulation therefore has the effect of excluding products from the market.

It may also be argued that an interest rate cap can play a more facilitative role. If credit providers are charging exorbitant fees (as some have suggested),[56] then the implementation of an interest rate cap may encourage these providers to restructure their products to comply with the cap. In turn, this could have the effect of increasing the availability of more affordable products. In practice, however, it is not always clear that this has been the effect of an interest rate cap. Instead, it is often suggested that some credit providers have

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[54] See also the then Minister's comments on this issue in Senator the Hon Nick Sherry, *Joint Press Conference with Tony D'Aloisio ASIC Chairman*, 27 April 2009, available at http://minscl.treasurer.gov.au/DisplayDocs.aspx?doc=transcripts/2009/021.htm&pageID=004&min=njs&Year=&DocType=2

[55] N Howell and T Wilson, 'The limits of competition: reasserting a role for consumer protection and fair trading regulation in competitive markets', in D Parry, A Nordhausen, G Howells and C Twigg-Flesner, *The Yearbook of Consumer Law 2009*, Ashgate, Surrey, 2008, p165.

[56] See, for example, the views of consumer advocates described in Howell, Davidson and Wilson, above 8, p 56.

responded by finding ways to avoid a cap, for example, by characterising the transaction as a pawnbroking transaction.[57] The argument that credit providers are making exorbitant profits, or that small loans can be profitable under the current interest rate caps regulation, is also strongly disputed by the industry.[58]

More optimistically, the existence of an interest rate cap may have the effect of opening a space in the market for mainstream institutions to develop and trial less exploitative forms of credit to serve the demand for small loans. Currently, a number of mainstream lenders offer low interest loans in partnership with community organisations,[59] and/or financially support no interest loan schemes operated by community organisations.[60] In addition, the National Australia Bank has been trialling, in partnership with Money Fast, a commercial small loan program. This program offers loans of between $1000 and $5000 with an annual interest rate of 15.95% and a comparison rate of 28.25%,[61] well below the rates offered by other fringe lenders,[62] and is reported to be operating on a break-even basis.[63] However, the reach and capacity of these initiatives is relatively low, and not comparable with the level of offerings in the commercial small loan sector.[64] If the existence of an interest rate cap had the effect of

[57] J Bryce, 'Trappings of easy money', Herald Sun, 6 April 2009, p 34.
[58] See, for example, submissions to the exposure draft National Consumer Credit Protection legislation made by City Finance Loans and Cash Solutions, and National Financial Services Federation. Available at http://www.treasury.gov.au/consumercredit/content/consultation/submissions/submissions.asp?round=1&subName=Exposure%20Draft:%20National%20Consumer%20Credit%20Regime%20Legislation
[59] For example, the ANZ Progress Loan (see http://www.anz.com/about-us/corporate-responsibility/community/financial-literacy-inclusion/programs/progress-loans/, viewed 12 October 2009), and the National Australia Bank Step Up Loan (see http://www.nab.com.au/wps/wcm/connect/nab/nab/home/about_us/4/3/4, viewed 12 October 2009).
[60] See, for example, National Australia Bank, 'NAB backs endeavour with $30m for affordable small loans', Media Release, 26 April 2006.
[61] See http://www.moneyfastloans.com.au/personal-loans, viewed 20 September 2009.
[62] A survey of micro-loans offered in Queensland in 2006 showed all inclusive annual percentage rates ranging from 107% to 3380%: see Howell, Davidson and Wilson, above n 8, p 48.
[63] J Bryce, 'Trappings of easy money', Herald Sun, 6 April 2009, p 34.
[64] For example, one lender, Cash Converters, reported making 280,000 payday loans in 2004, see Consumer Affairs Victoria, above n 34, p 37.

driving out of the market particular micro lenders, it might provide a greater market space for mainstream lenders to develop and invest in alternative business models and small loan products.

However, in the main, I argue that the role of interest rate caps regulation in the context of financial exclusion is to limit the availability of products that might be regarded as unfair, unsafe and/or unaffordable, and that this in turn minimises the potential effects of financial exclusion.

Other regulatory initiatives to address financial exclusion

While regulatory initiatives that are designed to reduce the likelihood of consumers taking out unaffordable loans, or to prohibit particular types of products from being offered in the market, are welcome, they will not be enough to solve the problem of financial exclusion. Addressing financial exclusion from a regulatory perspective also requires implementation of initiatives that facilitate and encourage the offering of small loans by mainstream credit providers. The voluntary initiatives of some lenders to offer small loans in partnership with other organisations are important, however, the reach and scale of these is insufficient. Greater incentives are needed. In particular, the imposition of more direct legislative obligations on mainstream providers to meet the needs of low income consumers is needed, perhaps along the lines of the Community Reinvestment Act in the United States, requires consideration.[65]

[65] See the discussion of this issue in Wilson, above n 45, at 270-273.

The Community Reinvestment Act was introduced in the United States in 1977, and was designed to encourage depository institutions to meet the credit needs of their communities, including the needs of lower-income consumers and neighbourhoods.[66] Among other things, the legislation provides for regulators to assess the performance of each institution in meeting the needs of their communities, and an institution's 'CRA' ranking will be taken into account when regulators determine applications for mergers, acquisitions, and opening and closing bank branches.[67] In this way, the Community Reinvestment Act creates a real incentive for banks and other deposit-taking institutions to address the credit needs of low-income communities. There is also the opportunity for individuals to comment on an institution's CRA record in the course of an application, and this too can increase the incentives for institutions to change lending practices, introduce new loan products, and partner with community groups.[68]

While the focus of activity under the Community Reinvestment Act was originally on home lending, Wilson has recently suggested that the model could be used to encourage the provision of small loans by mainstream lenders in Australia.[69]

Unfortunately, the examples of the Community Reinvestment Act and/or other regulatory initiatives[70] to address financial exclusion in a positive sense have not been part of the

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[66] W Apgar and M Duda, 'The Twenty-Fifth Anniversary of the Community Reinvestment Act: Past Accomplishments and Future Regulatory Challenges' (June 2003) Federal Reserve Bank of New York Economic Policy Review 169, at 172.

[67] M Barr, 'Credit where it counts: the Community Reinvestment Act and its critics (2005) 80 *New York University Law Review* 513 at 523.

[68] R Marsico, "Democratizing Capital: The History, Law, and Reform of the Community Reinvestment Act." *New York Law School Law Review*, Forthcoming. Available at SSRN: http://ssrn.com/abstract=651482, p 5.

[69] Wilson, above n 45, at 271.

current discussions on consumer credit reform.[71] In their absence, initiatives that address financial exclusion in a more preventative sense, by discouraging or prohibiting unsafe and unaffordable credit, become even more important. Although interest rate caps regulation is a somewhat blunt regulatory instrument, it can be a part of a package of initiatives designed to minimise the impact of financial exclusion. However, the fate of interest rate caps is uncertain, and in the next section, I discuss the likely future of interest rate caps in the new national framework.

4. Reconciling diversity: the future of interest rate caps in the national law

As noted above, there are currently divergent approaches in the States and Territories to the issue of interest rate caps. This diversity will need to be reconciled if the goal of a totally uniform and centralised regulatory system is to be achieved. In practice, this diversity is likely to be difficult to resolve. The merits or otherwise of an interest rate cap or ceiling has always been a hotly contested issue, both in Australia and overseas, and views are strongly polarised.[72] In summary, proponents of interest rate caps regulation argue that such controls protect vulnerable consumers from usury and exploitation, ensure that consumers pay fair rates, redress the imbalance in bargaining power between lenders and consumers, and compensate for a lack of practical choice for financially excluded consumers. In contrast,

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[70] Some other examples are discussed in Howell and Wilson, Access to consumer credit, above n 37, 141-142.

[71] A 2004 Parliamentary Committee report did consider the disclosure requirements of the CRA, and recommended that the banking industry and the Treasury consider whether there would be merit in imposing obligations on banks to disclose information on their role in providing finance and other assistance to disadvantaged communities: Parliamentary Joint Committee on Corporations and Financial Services, *Money Matters in the Bush: Inquiry into the Level of Banking and Financial Services in Rural, Regional and Remote Areas of Australia*, 2004, p 304 (recommendations 33 and 34).

[72] See references in n 8 above.

opponents argue that price controls result in credit shortages and credit exclusion, reduce diversity and competition in the market, affect the price of credit for low risk borrowers, do not address the identified problems, and are set at levels that demonstrate a lack of understanding of the true cost of providing small loans.[73]

As far as I am aware, there is nothing to suggest that the three jurisdictions with a comprehensive cap (New South Wales, the ACT and Queensland) are dissatisfied with their current arrangements. In contrast, Victoria's support for an interest rate cap now seems to be waning. In its 2005 review of consumer credit, Consumer Affairs Victoria suggested that:

> … there is not enough evidence to be confident that capping the total cost of credit is the best way to address the causes of the very high cost credit in the small amount sector, the non-conforming sector and in connection with default fees and charges in the mainstream market.[74]

In the same report, Consumer Affairs Victoria acknowledged that its form of price regulation, imposing a cap on interest rates alone, with no price regulation of fees and charges, has not been effective.[75]

The Commonwealth Government has announced that during the implementation period, those jurisdictions that currently impose interest rate caps will retain those caps,[76] and

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[73] For a summary of the main arguments, see N Howell, *High cost loans: A case for setting maximum rates?*, Centre for Credit and Consumer Law Background Paper, 2005, pp 22-31.
[74] Consumer Affairs Victoria, above n 34, p 117.
[75] Consumer Affairs Victoria, above n 34, p 110.

presumably the referrals from the State and Territory Governments will need to reflect this commitment in a practical sense.

Although the Commonwealth government has not disclosed its views in relation to interest rate caps, the trend of the Commonwealth government and its agencies in recent years has been to resist price regulation as a mechanism to provide consumer protection. For example, despite consumer dissatisfaction, the government has not introduced price regulation or other controls on bank fees, petrol prices, or grocery prices. In addition, while the Productivity Commission's report on the consumer policy inquiry did not specifically address price regulation in the credit market, it did consider examine price regulation in the context of utility services. Here, the Commission argued that:

> ... once full contestability [in utility service markets] is achieved, retail price regulation will have little role to play. As in other markets, competition amongst suppliers will best serve to keep prices in check.[77]

This approach by the Commonwealth is consistent with the empowerment and market model of consumer protection that has been adopted by the Commonwealth government in recent years, with a focus on information and self-regulation rather than prescriptive regulation.[78] In the context of high cost credit, an empowerment approach takes the view that high cost credit providers are meeting a particular market niche, and that effectively

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[76] See Senator the Hon Nick Sherry, *Joint Press Conference with Tony D'Aloisio ASIC Chairman*, 27 April 2009, available at http://minscl.treasurer.gov.au/DisplayDocs.aspx?doc=transcripts/2009/021.htm&pageID=004&min=njs&Year=&DocType=2.

[77] Productivity Commission, *Final Report*, above n 2, p 114.

[78] Howell and Wilson, *The Limits of Competition*, above n 57, p 169.

banning their operation would simply send consumers to 'loan sharks'.[79] Rather than imposing price regulation, competition between lenders should be encouraged, and consumers should be empowered to choose the most appropriate products for their needs. In contrast, others take what might be characterised as a more paternalistic approach, arguing that providers of high cost credit are preying on vulnerable and disadvantaged consumers, and the product should simply not be available.[80]

In public consultations on the current proposals for consumer credit regulation, Treasury officials appeared to be of the view that a responsible lending obligation will eliminate the need for interest rate caps. The then Minister also suggested, at the time of release of the exposure legislation, that a period of parallel operation of the responsible lending obligations and interest rate caps (in the jurisdictions that have them) would provide a basis upon which the need for interest rate caps regulation in the national law could be evaluated.[81]

There is therefore a significant divergence in approaches amongst the States and Territories to this issue. And from the Commonwealth Government's perspective, there seems to be a general resistance to price regulation as a regulatory tool, and a suggestion that, in any case, a responsible lending obligation might dispense with the need for interest rate caps regulation. There are therefore likely to be highly polarised views on what approach should be taken nationally on this issue.

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[79] For example, Department of Trade and Industry (UK) *Fair clear and competitive: The consumer credit market in the 21st century*, White Paper, 2003, p 63.
[80] Explanatory Notes, Consumer Credit (Queensland) and other Acts Amendment Bill 2008, p 1.
[81] See Senator the Hon Nick Sherry, *Joint Press Conference with Tony D'Aloisio ASIC Chairman*, 27 April 2009, available at http://minscl.treasurer.gov.au/DisplayDocs.aspx?doc=transcripts/2009/021.htm&pageID=004&min=njs&Year=&DocType=2.

In fact, it may not be possible to reconcile the divergent views during the 'examination of State approaches to interest rate caps' that is to take place in phase two.[82] This is even more so when it is considered that the proposed review of the impact of the responsible lending provisions on the need for a cap will not be clear, as the responsible lending provisions will not come into effect until 1 July 2010 (for some lenders), and 1 January 2011 (for the remainder),[83] while the Phase Two legislation is due to be in place by mid-2010.[84]

In light of the difficulties of achieving a uniform approach, the next section considers whether an interim response would be to continue to permit diversity on this issue, even within the proposal for centralised regulation.

5. Permitting some diversity in an otherwise centralised regime

The arguments for centralising consumer credit regulation through a transfer of responsibilities from the States and Territories to the Commonwealth are convincing. The failings of the current system, particularly in terms of improving uniformity and timeliness of reform, are summarised in the Productivity Commission report,[85] and the broad proposal for the transfer of regulatory responsibility has the support of most, if not all, stakeholders.[86] However, in order to deliver on the proposal, the current diversity in interest rate caps regulation will need to be resolved. As noted above, the recent position of the

[82] Australian Government, *National Consumer Credit,* above n 9, p 3.
[83] The Hon Chris Bowen MP, *Consumer credit reforms – Senate amendments*, Media release No 017, 17 September 2009.
[84] Australian Government, *National Consumer Credit,* above n 9, p 3
[85] Productivity Commission, *Final Report*, above n 2, pp 100-101, 448-450.
[86] Productivity Commission, *Final Report*, above n 2, p 101.

Commonwealth government towards price regulation suggests that it may be unlikely to support the imposition of interest rate caps. Depending on the scope of the referrals from the State and Territory governments, the Commonwealth may be able to impose such a preference, regardless of the views of the State and Territory governments. It is therefore not unlikely that uniformity in the future will mean the removal of interest rate caps regulation.

However, in the absence of other regulatory initiatives to address financial exclusion in a facilitative sense, removal of interest rate caps has the potential to increase the harm caused by financial exclusion. This highlights one of the potential risks of total uniformity and centralisation of laws: that of a reduction in consumer protection for some consumers.

For consumers, centralisation and uniformity in law is not necessarily always beneficial. Where there are different consumer protection standards across jurisdictions, it is unrealistic to expect that uniformity will result in the highest standards being imposed on all jurisdictions. In these circumstances, uniformity can result in standards dropping for consumers in those jurisdictions that previously imposed the highest standards. In the European context, Bourgoigne and Trubek note:

> Once again, it must be stressed that uniformity does not necessarily advance consumer interests …. There is a possibility that uniformity will be used to cut back consumer rights.[87]

[87] T Bourgoignie and D Trubeck, *Consumer law, common markets and federalism in Europe and the United States*, Walter de Gruyter & Co, Berlin, 1986, p 75.

In its recommendations, the Productivity Commission recognised the existing diversity in credit laws, and suggested that the requirements of the new national regime:

> Incorporate generally agreed provisions from state and territory credit legislation outside of the code, where these pass a benefit-cost test.[88]

However, the Commission provided no guidance in relation to provisions from state and territory legislation that are not 'generally agreed' (as is the case currently for interest rate caps). In addition, the benefit-cost test for regulation as it is currently framed has been cited as creating considerable problems for consumer credit reforms.[89]

The risk of a lowering of standards for some consumers if credit regulation is totally centralised has been acknowledged by some consumer advocates. For example, in its response to the Productivity Commission's inquiry, the Consumer Credit Legal Centre NSW noted:

> There are risks to this eventuality [transfer to the Commonwealth] from CCLC's perspective, including … above all, the potential loss of several consumer protections that are more stringent in NSW than in other states and in our view, very important.[90]

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[88] Productivity Commission, *Final Report,* above n 2, p 106.

[89] Choice, *A principled approach to the Review of Australia's consumer policy framework*, Submission to the Productivity Commission Inquiry into the Consumer Policy Framework, June 2007, pp 44 – 46. Available at http://www.pc.gov.au/projects/inquiry/consumer.

[90] Consumer Credit Legal Centre NSW, *Productivity Commission Review of the Consumer Protection Framework*, Submission, June 2007, pp 40-41. Available at http://www.pc.gov.au/projects/inquiry/consumer. See also the support for interest rate caps regulation in submissions to the Exposure Draft National Consumer Credit Protection legislation made by Consumer

The risk of losing the existing interest rate cap protections is one that is keenly felt.[91]

Another risk of centralisation is the loss of the potential for regulatory competition and regulatory experimentation in relation to interest rate caps specifically and potentially also in relation to other credit policy issues. In the context of Australian public health law, Opeskin suggests that:

> This is not to say that federal legislation may not itself embrace innovative solutions to particular problems, but that the possibilities of experimentation are significantly reduced when a matter is controlled by one legislature rather than nine.[92]

At a broad level, this is equally true for consumer law. However, there seem to be few proponents of this potential benefit of permitting a more decentralised approach. For example, in its draft report, the Productivity Commission was doubtful about the benefits of regulatory competition for generic fair trading laws. It suggested that 'the gains from experimentation are now unlikely to be large in the consumer area'. [93] The Commission's final report is perhaps less sceptical,[94] but the report's recommendations for centralisation

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Action Law Centre (p 1) and Consumer Credit Legal Centre (NSW) (p 1). All submissions are available at http://www.treasury.gov.au/consumercredit/content/consultation/submissions/default.asp.

[91] For example, see the support for the current regulation in submissions to the Exposure Draft National Consumer Credit Protection legislation made by Consumer Action Law Centre (p 1) and Consumer Credit Legal Centre (NSW) (p 1). All submissions are available at http://www.treasury.gov.au/consumercredit/content/consultation/submissions/default.asp.

[92] B Opeskin, 'The architecture of public health law reform: harmonisation of law in a federal system' (1998) 22 *Melbourne University Law Review* 337 at 364.

[93] Productivity Commission, *Review of Australia's Consumer Policy Inquiry: Draft report*, Canberra, 2007, p 50.

[94] Productivity Commission, *Final Report*, above n 2, p 50.

indicate that the Commission has taken a view that costs of the divergence that results from policy experimentation are too high.

However, there is still important scope for regulatory experimentation in consumer credit in Australia. For example, where there is not a consensus view (as is the case of interest rate caps), or it is not possible to identify the best regulatory approach, regulatory initiatives on a small scale (ie within a State or Territory) can ultimately help to develop and improve regulatory responses at the national level for the benefit of all consumers. Learnings from individual initiatives can be both negative and positive, and regulatory experimentation on a small scale can also reduce the risk of rolling out ineffective regulation nationally.[95] While not specifically referring to consumer regulation, Nahan's comments below seem particularly apt:

> in many, perhaps most, cases a diversity of solutions offers a better chance of finding the right one.[96]

Although the current regime allows for a level of regulatory experimentation in relation to interest rate caps regulation, resources have not yet been devoted to a comprehensive assessment of the different approaches. It is difficult to imagine that such an assessment can occur within the current timeframe for regulatory reform.

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[95] Victorian Government, *Submission to the Productivity Commission's Draft Report of the Inquiry into Australia's Consumer Policy Framework*, 2008, p 226; A Twomey and G Withers, *Federalist Paper 1, Australia's federal future: delivering growth and prosperity,* 2007, p 14.

[96] M Nahan, 'Competitive and uncompetitive approaches to microeconomic reform' in P Carroll and M Painter (eds), *Microeconomic reform and federalism'*, Federalism Research Centre, Australian National University, Canberra, 1995, p 236.

It is also important to note that a centralised system necessarily leaves no scope for responding to local issues and local conditions. Guerin suggests that:

> It is the ability to understand and respond to regional differences in needs, aspirations and priorities which remains the national government's biggest drawback in attempting any significant exercise of extended powers.[97]

In its final report, the Productivity Commission acknowledged the relevance of different needs in different jurisdictions.[98] However, it also noted that Australia's markets are becoming more national, that there are broad similarities in consumer demands across Australia, and that consumers' spending patterns are more influenced by factors other than the State/Territory in which they live.[99] In the context of the generic fair trading laws, the Productivity Commission implied that there is only limited need for local responses.[100]

In contrast, Nahan suggested (in 1995) that Australia was becoming a more diverse market, with the economies of different jurisdictions diverging rather than converging.[101] Nahan particularly referred to some of the southern states as being the 'rust belts', with Queensland and Western Australia becoming Australia's growth 'tigers'.[102] It is arguable that such

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[97] B Guerin,'The federal question – power or capacity' [2007, Jan-March] *Public Administration Today* 24 at 27.
[98] Productivity Commission, *Final Report*, above n 2, p 48.
[99] Productivity Commission, *Final Repor*t, above n 2, p 52.
[100] But see also the Productivity Commission's discussion in relation to vulnerable and disadvantaged consumers: Productivity Commission, *Final Report*, above n 2, p 304.
[101] Nahan, *Competitive and uncompetitive approaches to microeconomic reform*, above n 99, p 239.
[102] Nahan, *Competitive and uncompetitive approaches to microeconomic reform* above n 99, p 239.

economic and other differences might demonstrate a need for different regulatory responses.[103]

In the consumer credit sector, the market is largely national in its operation. However, there are some local factors that might influence the need for different regulatory responses. For example, variations in enforcement requirements under property legislation, and the level or type of competition in particular submarkets might suggest the need for different regulatory responses.

The need or otherwise for interest rate caps in an individual jurisdiction may also be influenced by other localised factors in the market, such as the extent of the availability of alternatives to payday loans and other short term, high cost loan products. For example, the various low and no-cost loan schemes that have been established to provide an alternative to payday loans often have limited geographic spread, and may have a greater presence in one jurisdiction than in others.[104]

There are therefore some potential risks for consumers if total centralisation of consumer credit regulation is introduced. In the context of interest rate caps, these risks, together with the fact that it is likely to difficult to find a consensus approach, or to conduct a comprehensive analysis of the relative merits of the different approaches within the reform timeframe, suggest that there may be some merit in permitting diversity on interest rate caps

[103] See also Twomey and Withers, *Federalist Paper 1*, above n 98, p 10.
[104] For example, in Queensland, the National Australia Bank's Step-Up Loan is only offered to residents of Cairns: see http://www.nab.com.au/wps/wcm/connect/nab/nab/home/About_Us/4/3/4/#6. See also Wilson, *Values driven innovation*, above n 45, at 268, for a discussion of barriers to the extension of such schemes in Queensland.

to remain, at least for an interim period. Among other things, this could minimise any expansion of levels of financial exclusion.

Achieving this outcome would clearly involve a change of tack in the reform proposals. In particular, it would involve the State and Territory governments retaining some legislative responsibilities for consumer credit. However, any such approach should occur within a largely centralised regime, where primary policy and enforcement responsibility is given to the Commonwealth government.

The current Uniformity Agreement provides a possible model for facilitating diversity in interest rate cap regulation, in that it specifically permits individual jurisdictions to adopt diverse approaches on clearly defined issues, including interest rate caps.[105] Moving into the new national regime, this approach could be supplemented by formal requirements to notify the Ministerial Council on Consumer Affairs (MCCA) of the intention to introduce new standards, and scope for MCCA to recommend that the changes not be proceeded with if they impose substantial compliance costs across the market as a whole, or if similar amendments can be progressed nationally in a timely manner.[106] Stakeholders could also be advised in advance of the intention of a State or Territory government to introduce or amend regulatory requirements in the limited areas of diversity, and will thus be better able to monitor the limited amount of regulatory diversity.

[105] See clause 12, Uniformity Agreement, available at www.creditcode.gov.au.
[106] For an example of a managed 'escape clause' along these lines, see Article 95(4) – (9) of the European Communities Treaty; S Weatherill, *EU consumer law and policy,* 2nd ed, Gloucester UK, 2005, pp 66-67.

If such a model were to be adopted, State and Territory governments would also have to retain some enforcement responsibilities. However, if State and Territory governments are only given enforcement responsibilities in relation to interest rate caps regulation, there is a considerable risk of that there will be insufficient resources to monitor and enforce compliance with the State or Territory legislation. This points to the need for the States and Territory governments to retain concurrent enforcement responsibility for the whole of the consumer credit regime.

Allowing for concurrent enforcement responsibilities is consistent with the proposals for the new Australian Consumer Law, where enforcement responsibilities will be shared between the Commonwealth, State and Territory regulators.[107] It will also address concerns about the ability of a federal regulator (in this case ASIC) to deal with local, one-off issues, that do not necessarily have a systemic nature, or do not otherwise have national implications.[108]

In its report, the Productivity Commission noted that:

> Provided that ASIC was proactive in addressing the full range of credit provision and intermediary issues, and appropriately resourced to do so, then such a shift in responsibility [for credit regulation and enforcement] has the potential to significantly improve the effectiveness of protection for consumers, and provide

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[107] Commonwealth of Australia, *An Australian Consumer: Law Fair markets – confident consumers*, Barton ACT, 2009, p 97.

[108] Department of Consumer and Employment Protection (WA) *Submission to the Productivity Commission's Draft Report on the Consumer Policy Inquiry*, 2008, pp 7-8.

> some cost savings to credit providers/advisors and their customers.[109] (emphasis added)

While funding support for ASIC's new role has been forthcoming,[110] and ASIC current motivation and determination to be proactive on consumer credit is quite clear,[111] it is not possible to anticipate ASIC's future motivation and willingness to be proactive. In the absence of internal drivers, it is not clear that motivation can be *imposed* on an agency. It is the motivation and willingness to act of the key players in an agency that are critical to an agency's success in a particular arena, and these can vary over time.[112] The operating environment is also crucial, including the level of support at Ministerial/Departmental level for a more or less active enforcement role.[113] Thus, while ASIC may have the necessary support and motivation at this point in time, there is no guarantee that this will remain. Providing the State and Territory governments with concurrent enforcement powers provides a back-up in the absence of a sufficiently motivated and resourced federal regulator.

A related issue is the fact that the state and territory agencies do have a geographical reach that ASIC (with offices only in the capital cities) does not. While contact by telephone or email is increasing, it is clear that face to face contact at a local level remains important for

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[109] Productivity Commission, *Final Report,* above n 2, p 102.

[110] The Hon Nick Sherry, *Australia to get world leading credit licensing regime*, Media Release No 040, 27 April 2009.

[111] ASIC explains (in relation to its limited credit jurisdiction) that it 'is already extremely active in the credit area …' See Australian Securities and Investments Commission, *Productivity Commission Review of Australia's consumer policy framework, Submission by the Australian Securities and Investments Commission*, 2007, p 46.

[112] For example, in the UK context, Ramsay refers to a life cycle theory of regulatory agencies: I Ramsay, *Consumer Law and Policy: Text and materials on regulating consumer markets*, 2nd ed, Hart Publishing, Oxford, 2007, p 456.

[113] A Fels, 'Regulating markets: marketing regulation' (2004) 63(4) *Australian Journal of Public Administration*, 29 at 34.

consumers. For example, in 2007-2008, Consumer Affairs Victoria reported almost 10,000 face-to-face advice sessions in its regional offices, and 3,000 telephone enquiries to regional offices.[114] Regional offices also facilitate delivery of specifically-tailored services to local communities, and regular compliance visits to local traders.[115] It is likely that local contact is particularly important for consumers who are vulnerable to financial exclusion, given that this group often has limited understanding of consumer rights and avenues for assistance.[116] A local presence is more likely to be accessible for these consumers than a national regulator accessible only by telephone or email. The need for a continued role for the state and territory governments is also highlighted by the fact that it is a state government agency, Consumer Affairs Victoria, that appears to be actively engaged in a discussion about how to meet the needs of financially excluded consumers.[117]

6. Conclusion

Australia is the middle of a major change in the regulation of consumer credit, with the implementation of a transfer of regulatory responsibilities from the States and Territories to the Commonwealth. While the proposals are broadly supported, this article has considered the proposals in light of the need to address financial exclusion in this country.

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[114] Consumer Affairs Victoria, *Annual Report 2007-2008*, p 69.
[115] Consumer Affairs Victoria, *Annual Report*, above n 117, p 69.
[116] See for example, Schetzer, L, *Drowning in debt: The experiences of people who seek assistance from financial counsellors*, Department of Justice, Victoria, 2007, p 51.
[117] Consumer Affairs Victoria convened an 'Affordable Credit Summit' in 2007, and reports the establishment of a Taskforce to progress issues raised at the summit, see http://www.consumer.vic.gov.au/CA256EB5000644CE/page/Credit+%26+Debt-Consumer+Credit+Review?OpenDocument&1=80-Credit+%26+Debt~&2=55-Consumer+Credit+Review~&3=~.

Despite a number of recent reports and discussions on financial exclusion in Australia,[118] the discussion on regulatory reform has failed to engage in any meaningful way with the potential for regulatory initiatives to reduce the level of financial exclusion. In particular, the discussion has missed an opportunity to consider the ways in which regulatory reform might better encourage mainstream credit providers to meet the needs of low income consumers, in particular, with respect to the need for appropriate low cost, safe and fair small loans. Regulatory alternatives that provide a real incentive for credit providers to engage with, and respond to, financial exclusion, such as a model based on the Community Reinvestment Act in the United States (discussed above) have not been given any serious attention in the reform process. This also reflects a lack of investment in research that can evaluate the broader economic impacts of financial exclusion and of a failure to provide safe and sustainable credit markets.[119]

While the regulatory proposals do not engage directly with the issue of financial exclusion, there are two facets within the current proposals that do have the potential to reduce access to unaffordable or unsafe products. In particular, the introduction of responsible lending requirements could limit the extent to which consumers enter into unaffordable loans. On its own, however, a responsible lending obligation does not ensure that an appropriate alternative is available.

Similarly, regulating the price of consumer credit through an interest rate cap can address financial exclusion in a preventative sense, rather than a facilitative sense. It does not

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[118] See the papers referred to in n 38 above.
[119] The Productivity Commission's report also noted a deficiency in the level of consumer research in Australia: Productivity Commission, *Final Report*, above n 2, pp 283-284.

necessarily create an environment where alternatives to the excluded products are offered to consumers at risk of financial exclusion.

I have argued that in a context where there is an absence of regulatory initiatives to encourage the provision of appropriate products to financially excluded consumers, the introduction or maintenance of regulatory initiatives such as responsible lending obligations and interest rate caps becomes critically important. However, the future of the interest rate caps is uncertain, given the current diversity in approaches, and the historical opposition to price regulation by the Commonwealth Government.

Given this concern, I have suggested that there is a case for permitting some limited diversity in the new national credit regime, specifically in relation to the regulation of interest rates. There are some consumer risks of total centralisation of regulation, and potential benefits from allowing diversity, at least in limited circumstances. To cap or not to cap is a controversial issue, and as others have suggested, '… controversial issues are not good topics for uniformity …'.[120]

I have therefore suggested that the current proposals for regulatory reform in consumer credit be modified so that they permit some regulatory diversity across Australia in limited and clearly defined areas (including interest rate caps), and provide that enforcement responsibility for consumer credit matters is shared between the Commonwealth, State and Territory governments. Clearly this model does not guarantee that broader financial exclusion issues will be addressed in the regulatory framework, now or in the future.

[120] Bourgoigne and Trubeck, above n 90, p 75. See also K Cseres, *Competition law and consumer protection*, Kluwer Law International, 2005, pp 233- 234.

However, it model could be a pragmatic way to ensure that interest rate caps are retained, at least in the jurisdictions that currently have them. In so doing, this approach can limit the impact that financial exclusion can have on low income and vulnerable consumers.