CURRENT DEVELOPMENTS IN BANKING LAW

Consumer Credit — The New Laws

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You have been a very dedicated audience, and the fact that you are still here, I hope, indicates that you are not all desperate to get to the bar or the Annual General Meeting. I will not tell you what Barbara said as I went by but she said basically to keep it down to half an hour. I think she wants me to finish by 5:30 and I will not quite do that, but I will do as closely as I can.

I want to make two main points, if I may. The first relates to the last point raised by David in relation to comparison rates which, he says, are basically a thing of the past if this legislation is to be enacted in the form likely to be agreed tomorrow. The second is to make one or two comments in relation to civil penalties which, as I understand it, have always been the most controversial aspect of the current credit legislation, which is now largely uniform throughout the mainland States with the exception of South Australia and the Northern Territory, and not, of course, in Tasmania.

The comparison rate first. There is obviously a great difficulty in prescribing a means of setting a comparison rate which will apply across as wide a range of products as is intended to be covered. The difficulty with not having a comparison rate is this, in my view. Pricing in this area is not transparent, nor is the nature of the product being purchased obvious to most purchasers - and I, perhaps like many others outside the industry, resisted the use of the term 'products' in relation to financial products for a long time, because it seemed to me that they were services. If I accepted that financial services were products, maybe legal services were too, and that seemed a horrific thought for me as a lawyer. But it is useful to use the term 'products' because it makes you try and distinguish what the difference is between a financial product and a physical product such as white goods. And one of them is that the product itself is defined by its contractual terms, and unless those terms are distinctly stated in simple English so that the purchaser knows what he or she is buying, they simply do not know what the product is. Secondly, I think it is important that the information be available, because the price of the product is extended over time and there are a number of variables which may alter the price from time to time. Each of those variables needs to be defined at the outset.

There are two other aspects in which I think it is fair to say that financial services, especially when available from banks, differ from most physical products. They are sold within a cultural context which, in relation to credit, often means that the purchaser sees that he or she is obtaining the grant of a privilege rather than purchasing something which is on the open market, and that is more true the further down the social and educational scale you go.

The other element which is important, although not so absolute, is that comparison of products may require a level of sophistication and education well beyond that obtained by the bulk of the population, and I include in that many people with tertiary education such as myself. Having said that, in relation to the philosophy behind the disclosure of a comparison rate, may I also say this: although there are difficulties in defining a comparison rate, there have to be compromises made in most situations, and

any attempt by Government to put forward a piece of legislation like this which entirely avoids the means for the ordinary consumer to make comparisons between products offered by an individual institution and products which are offered by different institutions, will only give rise to confusion and will increase the scope for later re-opening on the basis of unjustness. That, you may say, is a quid pro quo. But in days when legal aid is becoming less and less available to poor people in the community to challenge their contracts, I do not think it is a quid pro quo at all, and it is something which needs to be much more seriously considered rather than 'giving up' - which is what has happened so far. Governments have failed to agree on a means of establishing a comparison rate and have therefore given up. I might say that the Bill in its present form, which David says will not be accepted, effectively contains different rates for advertising and for pre-contractual disclosure, and that is an example of the sort of compromise which obviously has to be avoided. But do not throw out the baby with the bath water.

In relation to re-opening for unfairness, some of you may agree with David's comments that this is a major change. But for those of us from New South Wales, of course, it is not. Since 1980, we have lived with the *Contracts Review Act* which allows us to re-open virtually all relevant contracts - in fact, I should imagine every contract which is now going to be the subject of the credit legislation. We have lived with similar provisions in the *Credit Act*, we have lived with similar provisions in the *Consumer Claims Tribunals Act*, and it has caused no great social disruption; it is an entirely appropriate method of dealing with standard form contracts in this day and age.

The second thing I wanted to address was in relation to civil penalties and it was whether or not they are the appropriate way to go. There have been texts written on this, so I will restrict myself to a number of short comments. Firstly, I think that when one is comparing civil penalties with criminal penalties, one is really looking at a regime which does not require Government resourcing for enforcement. Secondly, where one is looking at an automatic civil penalty, one is looking at a regime in which the credit provider who makes the mistake bears the burden of rectifying it. Both of those principles, I would say, are quite appropriate and useful principles to work on. When you compare civil penalties with criminal penalties, you find that the Act has now left a number of matters in the area of criminal penalties only, including the disclosure of commission charges, and we have today the *Financial Review* saying that the life insurance industry is happy to disclose commission charges; the rest of the financial sector has apparently gone backwards.

If one has a criminal penalty regime, then it is useless to restrict that to the penalty unit which, although not defined in the legislation, is presumably a form of fine. The important use of criminal penalties is to ensure that things like community service obligations and compliance regimes can be enforced as a form of penalty on the company. And if that were done, as it is being done to some extent in the area of civil penalties, not by plan but by default, through agreements between credit providers and consumer representatives, and with the concurrence of tribunals, then one has a mixed system which I think is probably a desirable result. In addition to compliance regimes though, one also needs to have an education campaign which will ultimately have to be funded by somebody - industry funding has its own difficulties, Government funding is sparse, and consumer funding is non-existent. But what David said about competition is perfectly true. Competition in this area is undoubtedly restricted. Interest competition is known to be largely defunct. Until one has effective public education of what the cost of credit involves, I do not think competition will work effectively in this area and therefore the marketplace is insufficient in terms of traditional philosophy.

The final thing I want to say is that these regimes can be extremely expensive to operate under for credit providers who make mistakes and then have to rectify them. Hopefully that is a transitional problem which will tend to go away. We have now had eight years of working under the *Credit Act*, and in most jurisdictions national credit providers will all be familiar with the terms of truth-in-lending.

There are, however, five stages in remedying a problem. When one identifies the problem, it is important to know immediately, or as soon as one can, the extent of the contravention. Once the extent of the contravention is defined, it will be necessary to go through the process, whenever it is a systemic contravention, of notifying borrowers. The third stage is to put together the explanation of what has

occurred, and why it will never happen again. The fourth stage is to take the matters towards dispute resolution, and I can say from my experience, not only with Westpac and with Barbara's assistance in that area, but also in relation to other large credit provider cases with which I have been involved, that mediation does have an important role to play, and if it is necessary that a tribunal, such as the New South Wales Commercial Tribunal, be pulled into line by legislation, so be it. Tribunals have got to make it clear that they will accept mediated settlements which have properly been reached on the basis of public representation and consideration of all the facts, and that they will not place obstacles in the way of such a public interest. Expensive hearings after mediation, because the Tribunal believes it has a statutory obligation to consider everything that everybody else has already decided, is in nobody's interest.

And finally, may I say in relation to the imposition of civil penalties and the later reinstatement of credit charges where necessary, I think there is a warning to be given to banks and other credit providers in this area. To date, the legislation has, perhaps, been somewhat unknown. The recompense which might be authorised under such legislation is not within everybody's conception of legal remedies. It is not a compensatory jurisdiction at all, it is much closer to a forfeiture jurisdiction, as David said. But I think that banks and credit providers are tending to leave themselves, and I will duck as soon as I have said this, in some cases too readily in the hand of lawyers who tell them what to do. When one gets a reinstatement order it is, especially in New South Wales, almost invariable that the credit provider will end up paying the costs of the borrowers who have been represented. It is understood that those costs must be reasonable. It has also become virtually universal practice to seek and obtain a consideration of the costs they have incurred in bringing the case to hearing and finality in mitigation of the penalty they should pay. That penalty ultimately is a sum of money which will be distributed to consumers who have been the subject of the contravention.

I think it will need to be said in the very near future that such mitigation will not be permitted to be taken into account where it exceeds the reasonable costs which should have been incurred. If credit providers end up in incurring exorbitant legal costs then they will not be able to set off those against the penalty which is imposed in the Tribunal, and I think that is something that credit providers should keep in mind and keep their lawyers under rein.