Care inc financial counselling service

CONSUMER CREDIT LEGAL CENTRE (NSW) Inc

20 July 2007

House of Representatives Standing Committee on
Economics, Finance and Public Administration
Parliament House
Canberra ACT 2600

Attention: Andrew McGowen
Inquiry Secretary

& by email to: Andrew.Mcgowan@aph.gov.au

Dear Mr McGowan,

Re: Inquiry into Home Lending Practices and Processes used to deal with people in Financial Difficulty

Thank you for your recent correspondence inviting both our agencies to provide written comments to the Committee and to attend a roundtable on Friday 10 August 2007. As indicated, Care will not be able to attend the roundtable. CCLC has confirmed its attendance and will represent both agencies.

Care and the CCLC are separate organisations but provide similar services to similar clients. We communicate regularly, cooperating and sharing information to better understand the problems that our clients face at a structural level and to suggest systemic solutions. We have decided to provide this submission jointly to underline the similarity in experiences of a dysfunctional housing finance market being described daily to our front line staff. From our broader networking activities, we are aware the problems our clients are reporting to us are mirrored in consumer agencies around the country.

About our agencies:

Care Inc Financial Counselling Service and the Consumer Law Centre of the ACT:
Care Inc has been the main provider of financial counselling and related services in the ACT and region since 1983. It is host to the Consumer Law Centre of the ACT, a source of legal advice and advocacy for low to moderate income earners in relation to credit, debt, telecommunications and general fair trading matters. Care receives funding from a variety of sources, primarily ACT Government, the Commonwealth Financial Counselling Program and the NSW Credit Counselling Trust Fund.

Consumer Credit Legal Centre NSW Inc:
CCLC is an independent legal centre providing legal advice, representation, and education to NSW consumers in relation to credit, debt and banking matters. CCLC also operates the Credit and Debt Hotline, a financial counselling information and referral service, which is the first port of call for many debtors experiencing financial difficulty across NSW. CCLC receives funding from a variety of sources, primarily the NSW Office of Fair Trading.

Responses to specific questions:

Your correspondence posed several specific questions for us to consider. Those are dealt with briefly below. We have also prepared and annex a set of relevant recent materials our agencies have produced that we believe are relevant to the subject matter of the Inquiry.

1. *To what extent have credit standards declined in Australia in recent years?*
    - *Market share of non-conforming lenders; increase in low-doc products across the board.*

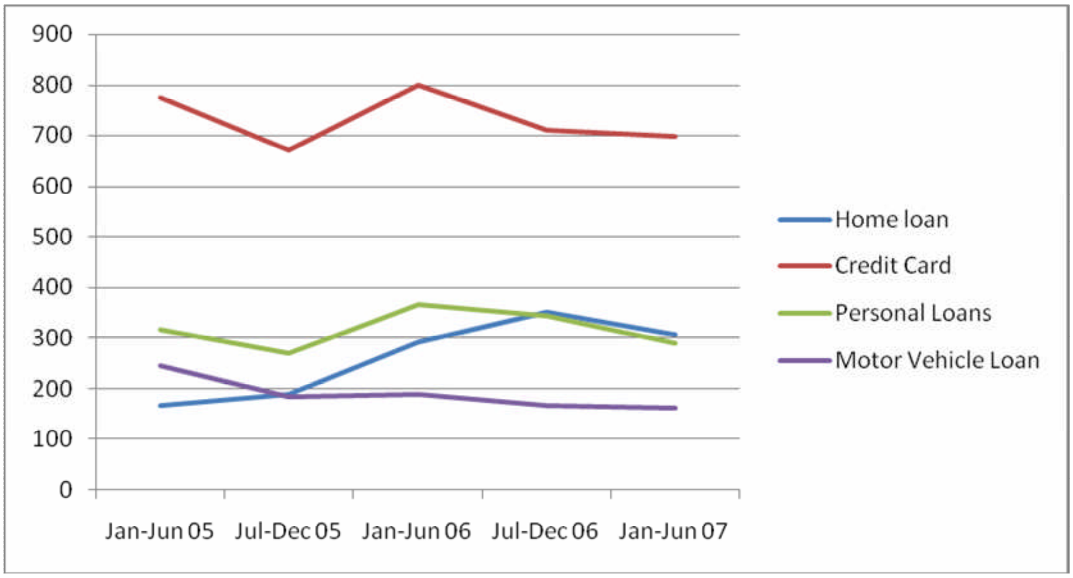
   We have noted a marked shift in the approach of all lenders in the consumer housing finance market in the last five years. There has been much public commentary on this shift, from the formal observations of the Reserve Bank of Australia and the Australian Prudential Regulatory Authority, through to media discussion of the growth in the market share of non-deposit taking lenders, specialising in low-doc and non-conforming loan products.

   The Committee is no doubt aware of much of that commentary and others can speak to it with more authority and familiarity than we are able. We would however make the following observations based on our case-work experience:

   - There has been a slow but noticeable increase in the proportion of new requests for assistance from consumers experiencing problems with their mortgages, the increase becoming more pronounced in the last two years (See graph based on CCLC data below);

- The proportion of mortgage difficulties that result in people seeking assistance from Care and the CCLC and that involve low-doc and non-conforming loan products is well in advance of the market share for products of that type (for example, 47 per cent of calls to the Credit and Debt Hotline in NSW in relation to home loans in the last 2.5 years related to loans with non-ADI lenders; and almost half of the Consumer Law Centre of the ACT's casework for the last 2 years related to mortgage foreclosures by non-ADI lenders);
- Non-bank/non deposit taking lenders are over-represented in the proportion of mortgage difficulties reported;
- There has been a noticeable increase in the proportion of mortgage products being written with the assistance of broker/intermediaries; and
- The majority of the mortgage problems reported to our services relate to loans that are within two years of their commencement, with a significant proportion resulting in payment problems for the borrowers from the date funds are advanced.

Calls to NSW Credit and Debt Hotline operated by CCLC by debt type[1]



2. *Have declining credit standards caused an increase in the number of loans in arrears and the number of repossessions?*
   - *Lack of accurate data on repossessions; 'agreed' sales hiding true rate of defaults.*

Yes. Generally mortgage defaults are on the increase. That increase in the mainstream market comes from a low base, but is still clear and rising. In the sub-prime market, default rates are much higher.

[1] This data is confined to those calls to the Credit and Debt Hotline about which specific details of debt types and creditors are taken. Many thousands of callers are given basic information and/or referred on to financial counselling and other services without such details being recorded.

Data sources that do exist confirm the escalating nature of the problems. For example our service delivery data confirms increasing problems for ‘mortgage belt’ consumers. No doubt other consumer agencies around the country are experiencing similar growth however coordinated and aggregated information from the financial counselling and consumer legal sectors nationally is not to our knowledge collated.

Information from the various state and territory Supreme Courts regarding mortgage foreclosure activity is already collected. It is not however coordinated, or easy to access. Further, it is not broken down into categories of loan type or lender, which can make it difficult to identify the source of apparent trends. There has nonetheless been a disturbing increase in mortgage repossession applications[2] in NSW in particular since about 2002, culminating in a 59% increase between 2004 and 2005.[3] Applications grew another 10% in 2006 to a record high of 5,368.[4] Other states have shown smaller increases but have also trended up. A copy of the research report prepared by the Consumer Law Centre of the ACT and released in 2006 is part of the annexure material. Follow up research is planned in the second half of 2007.

Bankruptcy information is readily available and regular. The most recent annual data for the 06-07 financial year indicates significant growth in bankruptcy activity, particularly in NSW.

Much of the information that is collected reports on the delivery of crises. Further information on how and where payment stress is being felt would be very useful. It may be that some of this data is also already being collected it just needs to be interrogated in a different way. For example the ABS Housing Affordability Index compares affordability as between cities. It may be an interesting and useful exercise to recalibrate the comparison between inner and outer city areas.

3. *Are borrowers in financial difficulty being treated appropriately by lenders?*
    - *Obligations under CBP and/or UCCC; access to superannuation for payments.*

No. Banks have noticeably improved their responses to reports of financial hardship, particularly amongst institutions that are signatories to the current version of the Code of Banking Practice. There are however still numerous examples where responses are too slow, inadequate, have failed to recognise a

---

[2] Applications do not necessarily relate to owner-occupier housing and may include investor housing and commercial properties.
[3] Statistics obtained from the Supreme Court of NSW “Announcements: Mortgage Defaults Stabilise”, 12/02/2007, http://www.lawlink.nsw.gov.au/practice_notes/nswsc_pc.nsf/pages/383
[4] Ibid, historical records attached to the Announcement reveal this number to be at least a 16 year high and much higher than the last peak of 3287 in 1991.

situation where financial hardship should have been clear or have insisted on repayments that are self-evidently unachievable. Some of the least appropriate responses are provided when banks outsource debts to commercial collectors or law firms, many of whom seem unfamiliar with the obligations that exist by virtue of the Code of Banking Practice or membership of the Banking and Financial Services Ombudsman scheme. Ironically, it often seems that more appropriate and reliable bank responses to reports of financial hardship can be found in relation to unsecured consumer credit products, rather than home lending where the lenders' risk is substantially covered by the secured asset.

There is no doubt however that the banking/deposit taking market sectors are well ahead of the non bank low-doc/non-conforming providers. The systems that exist within the non-bank sector are entirely inadequate and routinely fail. The focus is more clearly on collection activity and in many instances consumers who make contact with our services seeking assistance in relation to home loans written by the non-bank low-doc providers have already, or are about to lose their homes.

In 2006, CCLC conducted a survey of borrowers who had refinanced their home loan in response to financial difficulty. Some had done so multiple times in the last five years. The survey was a small qualitative survey including only 14 sets of borrowers. Significant details were taken about their refinancing experience. The majority of borrowers in the survey moved from "prime" loans to "sub-prime" or "non-conforming" loans as a result of their refinance(s). In undertaking the research we had expected to find that some borrowers had been driven into poor refinances as a result of inflexible hardship policies on the part of their original lender. This theory was not clearly supported by the research. Instead we found a consistent story of inflexible attitudes to hardship on the part of the sub-prime lenders in the period directly after the refinance, exemplified by the following comment by a survey participant:

> "*I didn't realize home lenders were so different from each other. I was only behind by one and a half payments and [the lender] took court action. A bank would not have done that. People ought to be warned about that."(Consumer Borrower – CCLC Refinance Survey for ASIC)*

At a more general level, requests to access early release of superannuation to address mortgage crises are increasing in frequency. For many lenders, it appears that their sole response to a report of financial hardship is to suggest the borrower attempt to dip into their superannuation. Often that provides only a temporary respite to collection activity because there is no consideration given to the cause of the financial hardship and the ongoing sustainability of the home loan. In such circumstances, borrowers risk forfeiting their superannuation withdrawal to interest and enforcement costs, without any guarantee of retaining their home.

The Uniform Consumer Credit Code's (UCCC) hardship relief mechanisms have been a source of enormous disappointment to consumer advocacy agencies. The provisions do not impose positive obligations on credit providers to respond to requests for variation at all, let alone within reasonable timeframes or providing reasons for rejection. It has been left for processes like the Banking and Financial Services Ombudsman and the Banking Code Compliance Monitoring Committee to develop informal jurisprudence regarding appropriate conduct for their subscriber lists. Although there have been recent case law developments (in particular the decision in Permanent Mortgages v Upston) that have raised the bar on how the UCCC will be interpreted, genuine access to the Court processes around the country is tiny in comparison to the scope of the problems being experienced.

4. *Are declining credit standards likely to have any long-term implications for the Australian financial system?*
    - *Lessons from the current situation in the United States.*

    Yes. It appears from our service experience that the depth and breadth of who experiences financial difficulty and how is changing. Moderate income households are struggling to make ends meet – and undoubtedly the cost of accommodation is a key part of that growing financial stress. We recognise that the deregulation of the mortgage market has encouraged the development of new products and services. What we do not know is how much those new products and services have actually *added* to the escalating costs of home ownership, by extending credit where it was unaffordable, encouraging more market churn when unaffordable loans fall over and so on. There is a complex array of policy challenges and those challenges will require complex and thoughtful responses. We are however heartened to see a developing national discussion of household affordability. Very low income households cannot do any better than they have been doing to maintain an acceptable standard of living, but there is clear evidence that the problems are reaching up income demographics.

We trust this information is of some assistance to the Committee in its deliberations and look forward to engagement with the Roundtable on 10 August 2007.

Yours sincerely,

David Tennant	Karen Cox
Director	Coordinator
Care Inc	CCLC NSW

Annexures:
- CCLC Submission – Productivity Commission review of Consumer Policy, June 2007
- Care Inc paper regarding lo-doc lending FCAWA Conference, October 2006
- Consumer Law Centre of the ACT, Research Paper ‘They want to take our house’, September 2006