Lo Doc loans – increased market access for lower income consumers, or the potential catalyst for a consumer credit meltdown[1]?

Keynote address:
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Introduction:

Financial counsellors have a keen interest in the establishment and maintenance of safe, fair credit markets. That interest is confirmed as a central focus in the national financial counselling peak body AFCCRA's objects, which commit the Association:

> To develop proposals for and to promote, solely from the perspective of consumer borrowers and consumer debtors, fair credit and debt related practices, laws and policies.[2]

The policy/law reform part of AFCCRA's role frequently involves comment on problems at the fringes of the credit market. It often appears the credit providers who populate the fringes exist for the primary purpose of exploiting the vulnerability and disadvantage of the borrowers they service. The growth of lo doc lending, particularly in the home loan market has however seen a potentially dangerous merging of the fringes with mainstream credit provision. It represents an inherently less careful and often more expensive form of credit and has become the fastest growing form of new home loan facility being written in Australia.

Whether it has been encouraged by, or grown in spite of pressures in the first home buyer lending market, the increase in the relative prevalence of lo doc lending is a phenomenon already presenting challenges for governments and regulators. If there is sustained negative economic pressure in the form of upward interest rate movements, or a return to the enormous increases seen in fuel prices in the middle months of 2006, we may find out whether the attention lo doc lending is now drawing is a case of too little too late.

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[1] A speech presented at the Financial Counselling Association of Western Australia (FCAWA) Conference, Perth, 23 October 2006.
[2] This is the third of AFCCRA's Objects, detailed at Clause 3.3 of the Association's Constitution. The Constitution can be accessed on AFCCRA's website www.afccra.org.

The increasing prevalence of lo doc loans:

Lo doc, or non-conforming lending are the terms most regularly used to describe a form of credit provision that makes a positive out of softer credit assessment methods. Traditional loan application processes include detailed questions about income and expenditure, with supporting documentation often required, including pay slips, tax returns, even the provision of references. Lo doc lenders have reduced the scope of the information gathered and rarely seek verification. It is also frequently the case that applications for lo doc loans are made through mortgage brokers, with the added potential for already minimalist information to be misinterpreted or misrepresented.

Originally targeted at the self employed, those on lower or less regular incomes or the credit impaired, lo doc lending originally established a niche by claiming to assist those that the traditional home loan market was ignoring. There is considerable evidence that lo doc lenders have been the real beneficiaries of intense competition in the mortgage market in recent years, expanding to compete with traditional products, whilst at the same time further stretching the boundaries of safe, fair lending practices. By asking fewer questions of prospective borrowers, lo doc lenders in part shift the responsibility for ensuring affordability to the consumer. With the vast majority of lending of this type secured by real property assets, it is hard as a consumer advocate to separate much of the current lo doc lending from what used to be called asset lending. In other words, if there is an asset that can be sold to cover indebtedness, such that the lender is unlikely to lose, less attention is paid to whether the borrower can actually afford the payments.

Marketing of lo doc options presses the claim that less scrutiny in the application process is a positive for borrowers. Although not exclusively a message being peddled by lo doc providers, even the benefits of saving a deposit prior to trying to purchase a home have been undermined in the scramble for market share.

The growth in lo doc lending has been considerable. In a speech to a Retail Financial Services Forum in August 2006, Reserve Bank Assistant Governor Ric Battellino noted that in the last decade, the relative share for lo doc lending in the home mortgage market had risen from below 1 per cent in 1996 to 9 per cent in 2006.[3] A little over a year earlier than Mr Battellino's speech, the Reserve had estimated the non-banking/lo doc share of the mortgage market at 4 per cent.[4] Industry commentators not only acknowledge the rate of growth as dramatic, they apparently expect it to continue. For example, a report in the Australian Financial Review on 5 September 2006, indicated some industry players thought that the

> $10 billion non-conforming market is growing by up to 40 per cent per year.[5]

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[3] Battellino, Ric, *Address to Retail Financial Services Forum,* Reserve Bank of Australia, Sydney 22 August 2006 (in particular Table 1: Housing Loan Market). The speech is available at www.rba.gov.au/Speeches/2006/sp_ag_220806.html).
[4] Reserve Bank of Australia, *Financial Stability Review*, Sydney, March 2005, page 41.
[5] Oldfield, Stewart, *Big banks flirt with riskier loans*, Australian Financial Review, Tuesday 5 September 2006.

The Market Intelligence Strategy Centre indicated in a media release dated 15 August 2005, that lo doc loans had passed through $2 billion in the preceding quarter, with 80 to 90 per cent of those loans originated through brokers. The Centre predicted the lo doc share of the total housing market would grow to 22 per cent by 2008[6].

Ric Battellino's paper suggests that at least some of the growth in the lo doc/non-conforming market may be at the expense of the big banks. Over the same ten years from 1996 to 2006, the relative share of the home mortgage market for the big four Australian banks fell from 67 per cent to 55 per cent.[7]

Returning to the Australian Financial Review report of 5 September 2006, it would appear that the banks are determined to fight for that share not only by trying to do better with traditional products and services but by developing and expanding their own lo doc offerings. Many banks, big and small, have been offering lo doc products for some time.[8] The banking industry has clearly stated its view that the lack of appropriate regulatory oversight for its lo doc competitors requires attention[9] and I will explore that regulatory disparity later in this paper.

Where is the problem and why does it concern financial counsellors?

There has been much comment regarding the increasing amount of credit and debt being carried by Australian consumers. Over the last 10 years, the movement upwards in the amount of outstanding consumer credit has been dramatic.[10] For all of that increase, the credit industry is quick to point out that relative levels of default are extremely low. That is of course different to saying over-commitment and genuine hardship do not exist, but there is considerable evidence being presented in support of the view that such hardship is not widespread and that the incidence of financial stress may be short-lived[11]. Whether research of this type is reflecting the picture entirely accurately is not clear. For example, there may be better ways to frame and track financial stress indicators than those currently utilised. For financial counsellors and consumer advocates working with a target group who are invariably amongst those faring the worst in making ends meet,

[6] Market Intelligence Strategy Centre Pty Ltd, *Low-document Loans in Broker Channel reach $2.2 billion in one quarter suggesting $9.8 billion in Low-doc lending might be achieved by brokers this year,* Melbourne, 15 August 2005.
[7] Battellino ibid (Table 1: Housing Loan Market).
[8] Oldfield, AFR 5 September 2006 ibid.
[9] Australian Bankers' Association, *Submission to the Senate Inquiry into possible links between household debt, demand for imported goods and Australia's current account deficit,* Sydney, 4 April 2005.
[10] Reserve Bank data for the amount of credit and charge cards is amongst the most dramatic. The most recent data to end July 2006 sees that total at $36.7 billion. By way of comparison, at end July 1996, the total was around $7 billion. (www.rba.gov.au/Statistics/Bulletin/C01hist.xls)
[11] For a discussion of this perspective see Marks, Gary N, *Dynamics of Financial Disadvantage,* Agenda, Volume 12, Number 4, 2005, pages 309-322.

industry representations regarding the affordability of current debt levels conflict with the experience of daily service demands.

The lo doc market has however been bucking the trend in relation to low levels of default on consumer credit facilities. Finding out precisely how much higher the incidence of default is across the lo doc/non-conforming sector is less straightforward than might be the case for mainstream credit providers. One need go no further than the disturbing trends in enforcement and mortgage foreclosure activity through State and Territory Supreme Courts to get a sense of the differences between classes of lenders.

The most recent compilation of local enforcement data was released by the Consumer Law Centre of the ACT, co-located with my employer Care Inc Financial Counselling Service, in September 2006. Aptly named *'They want to take our house'*[12], the ACT Consumer Law Centre report tracked trends in actions taken by credit providers to enforce debts against real property security from 2002 to 2005. The report noted the following main findings:

- There was a 39% increase in the number of actions by lenders seeking possession of homes between 2004 and 2005 in the ACT.
- There was an increase of 60% in the number of writs issued and an increase of 67% in writs later executed between 2004 and 2005.
- Lenders acted faster in 2005 to obtain judgments, seek enforceable orders and to execute those orders than in any other year studied.
- Preliminary data for 2006 shows that this upward trend is continuing.[13]
- *68% of actions for possession from 2002-2005 were taken by non-bank lenders with this percentage increasing over this four year period. Most notably, non-bank lenders were largely responsible for the substantial increase in the numbers of actions initiated in 2005, taking 66 of 90 (or 73%).* (Emphasis added). [14]

It was not possible for the Consumer Law Centre researchers to look at the loan contracts to which the actions for enforcement against real property related. Not all would have been lo doc loans. Similarly, not all would have been loans to owner occupiers. Several other factors however, lead the Centre to draw links between the data and the acceleration in the lo doc home loan market, in particular the over-representation of non-traditional lenders in the list of those taking action and the Centre's casework experience over the same period of time.

Care's Annual Report 2004-2005 noted that the Consumer Law Centre's largest area of casework growth had been in mortgage foreclosure matters. The Centre reported acting in

[12] Kilpatrick, Amy (Principal Solicitor – Consumer Law Centre of the ACT), *'They want to take our house' – An investigation into House Repossessions in the ACT Supreme Court,* Care Inc Financial Counselling Service, Canberra, September 2006. (The report is available on Care's web-site www.carefcs.org.)
[13] Kilpatrick, ibid, page 5. The report notes that 55 actions were commenced in the 6 months, 1 January to 30 June 2006, compared to 40 in the first 6 months of 2005.
[14] Kilpatrick, ibid, page 2.

six such matters at the one time in the reporting year, all involving non-bank lenders and lo doc loans.[15] The situation continued to deteriorate, with the Centre's mortgage foreclosure practice reaching double figures in the first half of 2006.[16] For a legal service able to carry an active caseload of around 30 files, fully one-third of that service was engaged in dealing with consumers at risk of, or having already lost their homes.

The ACT mortgage market is small in comparison to other major Australian cities. So too are the numbers of actions for enforcement against real property much smaller in the ACT. It is a matter of considerable concern then that the experience described in the Consumer Law Centre of the ACT's research appears to be occurring in very similar ways in other much larger markets. In both NSW and Victoria, mortgage foreclosure activity is increasing, apparently being driven by non bank credit providers at rates well outstripping their share of the home loan market. [17]

I am not sure whether data of this type is readily available in Western Australia. If it has not already been compiled, there may be considerable benefit in either Government or an appropriate community agency approaching the Supreme Court Registry to ask for its assistance, or access to the public records of civil enforcement proceedings to get a sense of whether the emerging picture is the same in this jurisdiction as elsewhere in the country. The Western Australian economy is galloping along on the back of a resources boom and the rate of increase in values of property prices in this state is leading the country.[18] If there is not a problem here, which I very much doubt, it is a matter of when it will appear rather than whether.

These issues will naturally find their way to financial counselling agencies. In fact in the ACT, many of the matters that were referred to the Consumer Law Centre and eventually prompted its research report were originally received through Care's financial counselling information line. That is unsurprising given that financial counselling services are often in the front line of responding to consumer financial crisis. It does however point to a further shift in the demographic of the traditional financial counselling client base, which is undergoing some subtle but significant changes toward greater numbers of people previously considered financially secure.

A more dramatic expression of the changes was reported in the Age on 3 August 2006:

> Families struggling to pay off a mortgage are being forced to seek emergency food parcels in one of Melbourne's northern suburbs. Of the 2000 people seeking emergency relief at the Broadmeadows Uniting Care centre each year, more than

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[15] Care Inc Financial Counselling Service, *Annual Report 2004-2005,* Canberra November 2005, page 15. (The report can be accessed online at www.carefcs.org/publications/annualreports.html).

[16] Consumer Law Centre of the ACT, *Performance Reports to the ACT Department of Justice and Community Safety -1 January to 30 June 2006,* Canberra, July 2006 (Annexure A – Casework and Litigation Activities).

[17] For example see Burke, Kelly and Needham, Kirsty, *Houses falling down on high-risk mortgages,* Sydney Morning Herald, 19 August 2006.

[18] See Real Estate Institute of Australia, *(Media Release) One Country – But Three Distinct Markets,* Canberra, 6 September 2006.

> 300, or 15 per cent, are trying to pay off a mortgage. About 260, or 13 per cent, are public housing tenants. The centre's financial counsellor Gary Rothman, said rising interest rates, petrol prices and inflation had forced people to choose between repaying their mortgage or putting food on the table.[19]

Although not mentioned in the Age report, based on consistent enforcement data it seems a safe guess that lo doc loans would be over-represented amongst those in crisis and seeking emergency relief.

Options for responding to the regulatory challenges posed by lo doc lending:

Regulation is not the only or even necessarily the most effective way to deal with market failure or unfairness. For example industry self regulation, where the industry involved has a genuine interest in ethical conduct and maintenance and enhancement of quality, can achieve impressive results. The success of such endeavours involves a number of key pre-requisites – for me the most important being a real threat of consequence in the event of non-compliance with the relevant industry standard.

The question is how do you make self regulation work in a new and disparate market segment, where profit rather than reputation is the driver? What exists in the self regulatory space for the lo doc lenders is delivered largely through the Mortgage Industry Association of Australia with the option of referral of complaints to the relevant External Dispute Resolution Scheme, the Credit Ombudsman Service Limited. Both in my experience fail reliability and credibility tests because not enough of the burgeoning industry are covered, or take the processes seriously.

For these key reason and in the face of consistent and increasing mortgage foreclosure data across a number of jurisdictions, there must be some consideration of regulatory reform. Holding our collective breath and hoping against further interest rate rises or petrol price increases is not a strategy. In any event, the problems have emerged in some of the most favourable of economic times, so even an absence of predicted economic tightening is no guarantee of solution.

Home lending is a sub-set of issues in the broader housing market, where reductions in the affordability of appropriate housing, particularly for first home buyers have been prevalent in public discussion and debate. Sadly, much of that discourse has been undermined by the political tensions that dominate Commonwealth, State and Territory relations. If there is to be any meaningful understanding of and action in relation to dysfunction in home lending, it will require effective cooperation and coordination between various levels of government.

[19] Doherty, Ben, *Howard's dream believers living on hand-outs,* The Age, Melbourne, 3 August 2006.

Some of the possible layered responses are discussed in the following:

i) At a national level:

The big issue on the national stage is the level of regulatory oversight, or rather lack thereof, that applies to the lending decisions of non traditional credit providers. This theme was a central message in the Australian Bankers' Association's (ABA) submission to a Senate Inquiry investigating possible links between household debt, demand for imported goods and Australia's current account deficit, in April 2005.[20]

Some of the regulation banks comply with in the home loan market is common across classes of credit providers – most importantly the Uniform Consumer Credit Code (UCCC). Observations about the continuing effectiveness of the UCCC process are made in section iii) to follow. The ABA focused however on explaining the significance of the extra layer of regulation deposit taking institutions are subject to, via the supervision of the Australian Prudential Regulatory Authority (APRA).[21] In short, APRA sets and oversees a range of prudential standards, aimed at protecting the funds that customers have deposited with deposit taking institutions. APRA can demand information in undertaking its supervisory role and can act against institutions operating contrary to the standards.

The ABA suggests that the APRA role is significant because:

> In protecting the interests of depositors, APRA is particularly focussed on bank lending because it is on the lending side of the banking ledger that traditionally the largest risk to the banks' solvency reside. The most significant risk is known as 'credit risk'. This refers to the risk that a loan will default. If a large enough proportion of a banks' stock of loans default, this will place major stress on the bank to fulfill its promises to repay the banks' depositors.[22]

The ABA went on to bemoan the lack of competitive neutrality that exists for banks, building societies and credit unions, subject to the prudential supervision of APRA and the remaining class of credit providers not subject to that regulation, including the growth market of the non-conforming/lo doc lenders.[23] Quoting the Reserve Bank's Financial Stability Review, of March 2005, the ABA noted:

> Reflecting the riskiness of non-conforming loans, a relatively high proportion of non-conforming borrowers are behind schedule on their loan repayments. At the end of 2004, nearly 4 per cent of the value of securitised non-conforming loans were in arrears by at least 90 days, compared to only 0.2 per cent of both securitised and banks' housing loans.[24]

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[20] Australian Bankers' Association (ABA), submission 4 April 2005, ibid.
[21] ABA submission, ibid, page 6.
[22] ABA submission, ibid, page 7.
[23] ABA submission, ibid, page 7.
[24] ABA submission, ibid, page 9.

Having regard to the comments of the central bank, the fact that the non-bank lenders have become so heavily over-represented relative to market share in actions seeking enforcement against real property in the ACT and elsewhere, may have been predictable.

Consumer groups, AFCCRA included, are clear in expressing concerns about problems with banking conduct when observations of that type are warranted. On this issue however, it is hard not to have sympathy for the banks' position. As an industry banks have worked hard to improve self regulation through efforts like a much improved Code of Banking Practice, enforceable against those that adopt it, and what is often touted as the best External Dispute Resolution process - the Banking and Financial Services Ombudsman. On top of those efforts, prudential regulatory standards require banks to make more considered decisions on when and how to lend. They are however competing against providers that, if the experiences reported to the Consumer Law Centre of the ACT are anything to go by, will consider lending to anyone with a pulse and property that might be taken if they default. That has to impact on how banks present their offerings to the market.

The lack of policy comment linked to decisive action is therefore confusing. The Reserve Bank former Governor made a number of important public statements over several years reiterating the importance of maintaining proper standards in bank lending.[25] The Treasurer even called the Chief Executives of the four major banks to Canberra earlier this year to discuss their home lending standards.[26] Whilst there has been some evidence of panic in individual bank responses to drifting market share[27], by and large telling the banks to behave looks like a case of preaching to the converted. The real problem is a growing group of providers that do not have any effective industry self regulation and are not subject to prudential oversight.

My understanding is that when APRA has been asked for comment on the issue, it has noted that it has no regulatory responsibility for the lo doc/non-conforming providers. That bit we know. The question is should it? Perhaps we need to update our understanding of the need to appropriately protect 'depositors'. At both an individual and collective level, I would suggest that the stake consumers have in being able to finance the purchase of homes to live in on appropriate and fair terms, is at least as important as protecting the security of funds deposited in savings accounts. Equity in home ownership, spread more broadly and reliably across the community would certainly represent a greater expression of national financial security.

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[25] See for example Macfarlane I J, *Monetary Policy and Financial Stability,* Speech to CEDA Annual Dinner, Melbourne, 16 November 2004.

[26] For example, reported in Gordon, Josh, *Rate rise takes the shine off tax cuts,* The Age, 4 May 2006.

[27] For example, the National Australia Bank's reported intention to review previously rejected home loan applications to see whether they might be improved (Australian Financial Review, *NAB Stoops to compete on risk,* 12 December 2005). St George Bank was also advertising a no-deposit home loan earlier in 2006, although the marketing appears to have been dumped.

ii) Through the cooperative efforts of Commonwealth and State and Territory governments:

The theory of a cooperative approach to policy and law reform in specific areas like consumer protection, driven by a council of Ministers across all Australian Governments sounds fabulous. We have such a process – it just does not work, or at least does not deliver outcomes to obvious problems when the community needs them. In the context of a discussion of lo doc home lending there is no more compelling example of that failure than the absence of any effective regulation of the activities of mortgage brokers.

The issues in relation to finance brokers more broadly have been acknowledged by the Ministerial Council on Consumer Affairs. The Council's web-site notes the following:

> *Objective:* Develop a model for consistent national regulation of finance and mortgage brokers incorporating the following features:
>
> - Coverage extended beyond consumer credit to small business and investment credit, with capacity for exclusion from certain legislative requirements where appropriate;
> - Requirements for brokers to be licensed or registered, and as a condition of the licensing or registration to meet minimum competency or probity standards and to belong to an alternative dispute resolution scheme approved by ASIC or other nominated agency;
> - A contractual relationship with the broker based on refinements to the NSW *Consumer Credit Administration (Finance Brokers) Act;*
> - Broking clients being provided with appropriate remedies including a capacity to stay proceedings for the forced sale of their home where action is being taken against the broker that could result in the home being saved;
> - Brokers being required to hold professional indemnity insurance and/or contribute to a fidelity fund.[28]

The list does not exactly set the world on fire. For example, missing is any reference to clarifying the ongoing issue of agency, where credit providers still successfully avoid any consequence resulting from the poor, even dishonest conduct of brokers. The most disappointing aspect of the process is the glacial pace at which it has progressed. The Council first began reviewing these issues in 2003. A Regulatory Impact Statement was circulated in 2004 and the web-site reports an expected completion date of March 2006.[29]

In the context of the growing problems in the lo doc market, effective regulation of finance brokers is a matter of the most urgent priority. One would not get the sense from the Communique of the Council's most recent meeting on 15 September 2006 that this

[28] This item can be found on the Ministerial Council's web-site, under the Strategic Agenda dated September 2005, at www.consumer.gov.au/html/mcca_projects.htm.
[29] Again these timelines are noted on the web-site www.consumer.gov,au/html/mcca_projects.htm.

urgency has either registered, or encouraged Council members to find a way through their differences to deliver an outcome:

> *National Regulation of Finance Brokers*
>
> Ministers today discussed issues related to the national regulation of finance and mortgage brokers. The proposals have been the subject of on-going consultation with industry and consumers. A decision on the scheme will be announced after further consideration out of session.[30]

The failure of this process to deliver a reasonable outcome in anything approaching an acceptable timeframe is what happens when consumer protection is squashed into being a sub-priority in the competition law framework. Meanwhile, consumers continue to be duped by at best conflicted and at worst overtly dishonest brokers into facilities they could never afford and that were destined to fail from before the funds were advanced.

Take for example the nationally publicised case of Mr A J Biega, a client of the ACT Consumer Law Centre:

- A J Beiga was eighteen years old when he inherited $180,000. He thought buying a house would be a sound investment for the inheritance and secure his future.
- AJ approached a broker who lined up a $355,000 home loan with a non-bank lender. The monthly repayments were around $3000.
- AJ told the broker he was a self employed artist. In fact, he was receiving a Centrelink benefit and according to AJ, had been living on the street for much of his teenage years. Not surprisingly, when the inheritance ran out, AJ could not keep up payments. The broker *helpfully* organised a refinance.[31]

iii) By making the State and Territory regulation of consumer credit more effective:

The main vehicle for regulating consumer credit in Australia is the Uniform Consumer Credit Code (UCCC). Template legislation, introduced through the Queensland Parliament in 1996 delivers if not a uniform system, then a substantially compatible framework for the entire country. That is a good outcome and, because I am about to discuss an example of failure, it is important to be clear that national consistency remains a worthwhile goal.

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[30] Ministerial Council on Consumer Affairs, *Joint Communique – Ministerial Council on Consumer Affairs Meeting,* Melbourne, Friday 15 September 2006. Also available on the MCCA web-site at www.consumer.gov.au/html/download/DraftCommuniqueSept2006.pdf.

[31] This story first appeared on the World Today on 4 July 2006. Geoghan, Andrew, *Debt levels in Australia cause concern*, Australian Broadcasting Commission, The World Today, 4 July 2006. A transcript can be viewed at http://www.abc.net.au/worldtoday/content/2006/s1678401.htm.

As an advocate, working with vulnerable and disadvantaged consumers in crisis, a section of the UCCC that is referred to consistently is section 66. The section provides options for responding to consumers who report financial hardship.

In my experience this section has not been able to operate as it should. It provides an excellent example of the challenges we face in responding to problems in the lo doc lending market. Similarly it exposes weaknesses in the manner in which the nationally cooperative model of UCCC management functions.

<u>Section 66:</u>
For those involved in negotiating the form of the UCCC regime, delivery of a mechanism where consumers could raise financial hardship as an issue and seek some accommodation under their credit contract to take account of that hardship, could justifiably have been seen as a breakthrough. The cause of the hardship must be reasonable, the options for varying contractual obligations are limited to reducing payments, delivering breaks in payments, or a combination of the two and the consumer must reasonably expect to be able to meet their commitments if the variation requested is made. If the credit provider does not agree to the request, the consumer can ask the relevant Court or Tribunal in that jurisdiction to make orders.

There were two really important shortcomings inherent in the hardship framework from the date the UCCC commenced:

- limitation of the hardship relief options to a capped ceiling of $125,000 credit available or outstanding on the relevant facility and
- a lack of any obligation on the part of the credit provider as to how, when or even whether it would respond to a hardship request.

The first of the two shortcomings was addressed by amendment in 2004 linking the credit ceiling to average house prices, reviewed monthly and based on Australian Bureau of Statistics data[32]. The solution was way too slow coming and I have never seen any real logic in having a ceiling, but with the figure applicable at the time of writing $301 950, the vast majority of consumer credit facilities for consumers who might be potential clients of financial counsellors would now fall within the hardship framework.

The second problem has not been addressed and does not even appear to be on the radar screen. It is an issue prevalent when dealing with non-traditional lenders offering lo doc products and again I would contrast the drivers for that sector with banks – or at least those that have signed on to the most recent version of the Code of Banking Practice. Under Clause 25.2 of the Banking Code, subscribing banks make the following undertaking:

> With **your** agreement, **we** will try to help **you** overcome **your** financial difficulties with any credit facility **you** have with **us**. **We** could, for example, work with **you** to develop a repayment plan. If, at the time, the hardship variation

[32] Background on the hardship threshold and its current level is available at www.creditcode.gov.au.

> provisions of the Uniform Consumer Credit Code could apply to **your** circumstances, **we** will inform **you** about them.[33]

The Banking and Financial Services Ombudsman has also expressed clear views about what is expected of members when receiving requests for hardship relief[34], including basics like responding and giving reasons if requests are rejected. The existence of the Banking Code, or the issuing of views by the Ombudsman do not ensure that banks will always respond to hardship requests as they should, but a set of expectations has been created and articulated. If the expectations are not met, consumers can complain and have issues addressed in forums other than the significant hurdle of formal Court or Tribunal proceedings.

By way of contrast, the Consumer Law Centre of the ACT noted the following:

> Should the loan fall into arrears, consumers with loans from non-bank lenders face a number of practices that inhibit their capacity to defend a claim:
>
> - an inability to engage with consumers experiencing hardship, and a greater readiness to take court action;
> - lack of access to or dysfunctional internal complaint mechanisms;
> - lack of access to or respect for Alternative Dispute Resolution schemes (such as the Credit Ombudsman Service Limited); and
> - the haste with which court proceedings are brought and concluded (which, as noted earlier in the report, is happening with increased speed).[35]

The UCCC should require certain things of all credit providers receiving requests for assistance from consumers. Failures to deliver should attract sanctions.

Section 66 is not the only example in the UCCC that could benefit from close attention. Section 70, dealing with unconscionable conduct also needs considerable work – although perhaps the adoption of unfair contract terms legislation is a better course in this regard, providing a mechanism for inevitable hardship to be averted before it is delivered. In the lo doc space a good example of fundamental unfairness are clauses increasing interest rates that are usually already higher than market upwards by as much as 4 per cent in the event of default. For consumers in hardship, with the non-existent or unreliable hardship processes described in the discussion of section 66, failure is not just inevitable but a whole lot faster when such clauses kick in.

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[33] Australian Bankers Association, *Code of Banking Practice,* Sydney, August 2003.
[34] Banking and Financial Services Ombudsman Limited, *BFSO Bulletin 46,* Melbourne, June 2005. The relevant section is *Dealing with customers in financial difficulty including hardship variations,* pages 2 to 9.
[35] Kilpatrick, ibid, page 16.

Conclusion:

The Executive Summary of the ACT Consumer Law Centre's report '*They want to take our house'* begins as follows:

> Australians have traditionally seen the family home as the means of building a secure economic future for themselves and their children. For many people, being a fully participating member of Australian society is psychologically linked to owning property. Conversely, the risk of losing the family home can be emotionally devastating. Home loans that fail can bring financial disaster, eroding or eliminating the wealth held in what is often the only asset of significance a person or couple may have. This is especially the case where the failure of a loan ends in court action by a lender, and the lender takes physical possession of the borrower's home.[36]

My wife and I purchased our first home in 1998. We had the most spectacular blind luck in the process, buying just before the property market in Canberra exploded. In only two years following the property increased in value by almost 80%. We have always been careful and conservative in money matters and although we planned our purchase carefully, even made some improvements to our home, the surge in the value had little to do with us. It could equally have gone the other direction. The arrival of children has since meant a slightly larger home. It too has accumulated value but at nowhere near the pace that the first property did.

Why share this information in closing a discussion like this one? I believe it to be illustrative of the pressures that have caused the lo doc fire to burn so brightly. For example:

- If we were buying our current home now at its current value, and borrowing the same proportion that we needed to borrow to fund our first purchase, we would seriously struggle to keep up those payments.
- We would be unlikely however to have much trouble securing the necessary finance – probably being offered more than we asked for or needed in the process.

Property values have played no small part in sustaining the consumer credit boom in Australia. In the process, they given us what I believe to be a false sense of security that as individual consumers and as communities we will be able to adjust to changes in economic conditions. They have also fuelled new markets, or changed traditional ones like home lending – and our policy confidence in the ability of markets to self heal has caused governments to largely watch on, rather than to fully investigate, consider and take action where appropriate.

Mortgage foreclosure data is growing in a manner that cannot be ignored. Another interest rate rise before Christmas will only make the case for action more compelling and urgent.

[36] Kilpatrick, ibid, page 2.