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IN BRIEF

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THE NATIONAL CONSUMER CREDIT PROTECTION AMENDMENT (CREDIT CARDS AND HOME LOANS) BILL 2011

Today the Treasury released for industry consultation an exposure draft of the National Consumer Credit Protection (Credit Cards and Home Loans) Bill 2011. The draft bill formalises a number of the key credit card and home loan reforms announced by the Treasurer in December last year.

A consultation period of just **3 days** has been allowed by Treasury for these important reforms. A consultation period of **3 weeks** has been allowed for draft disclosure documents proposed under the reforms.

CREDIT CARDS

If the provisions of the draft bill relating to credit cards become law, these reforms would:

- Require credit card application forms to include up-to-date Key Fact Sheets in accordance with regulations (a sample Key Fact Sheet has been released for consultation);
- Prohibit entry by a credit provider into a credit card contract unless the application is made using an application form which includes an up-to-date Key Fact Sheet (if the Key Fact Sheet is out of date, the applicant must have been provided with up-to-date information as prescribed);
- Prohibit credit providers from inviting cardholders in writing to increase credit limits without express consent (even if a customer is continuously incurring overdraft fees and the card issuers merely seeks to address this);
- Prohibit credit providers from approving the use of a credit card in excess of:
    - a default buffer being the lesser of $500 and 10% of the credit limit; or
    - the credit limit, if the account holder has elected not to have a default buffer;
- Prohibit the charging of fees or charges or a higher rate of interest because the credit limit was exceeded;
- Require card issuers to apply payments received in accordance with rules under which parts of the account balance which are subject to higher interest rates are repaid first. Provision is made for agreement to be reached on other payment allocation arrangements, but the account holder may withdraw from this at any time.

Regulations may be made which require the card issuer to notify the account holder upon becoming aware that the credit limit has been exceeded. However, it would not be permissible to charge a fee for this notice which means the cost will be subsidised by other customers.

Records of consents for credit limit increase invitations and elections not to have a default buffer must be retained by credit card issuers together with any withdrawal of these.

STANDARD HOME LOANS

The draft bill includes new rules relating to "Standard Home Loans". These are standard form credit contracts under which credit is provided to purchase a residential property or refinance credit wholly or predominantly for such purposes.

If the provisions of the draft bill relating to home loans become law, these reforms would require credit providers to ensure consumers who apply for or inquire about a standard home loan can obtain a Key Fact Sheet for the loan including on any web-site where an application can be made.

The contents of the Key Fact Sheet will be prescribed by regulations and a sample has been released for consultation. The regulations may require the Key Fact Sheets to be tailored for individual customers using information provided by them.

If more information is required from a customer to generate a Key Fact Sheet, the credit provider must tell the customer what information is required.

CONSIDERATIONS

Prohibition on allowing credit limits or default buffers to be exceeded

The prohibition incorrectly assumes that all transactions are routed to the card issuer for real time approval. For manual transactions (using traditional "click-clack machines" or transactions where communications are off-line, the issuer has no opportunity to prevent the provision of further credit).

The prohibition will also prevent card issuers from actively encouraging customers to increase their credit limits where they are frequently having bill payments declined.

Prohibition on charging fees or default interest for a credit limit being exceeded

This prohibition will even preclude a fee from being charged for a default notice notwithstanding that the customer will be in default and that it will be appropriate for a default notice to be sent. This position will apply even though the credit limit may have been exceeded as a result of manual or off-line transactions which denied the card issuer any opportunity to prevent the credit limit being exceeded.

Imposition of mandatory payment allocation rules

This is likely to generate resistance from the credit card industry because it interferes with pricing considerations relevant to differentiating product features and may require prohibitively expensive changes to account management systems.

Requirement for a home loan key fact sheet

At the simplest level, a range of lump sum loan products which amortise over a fixed term of say, 25 years, can be easily compared by reference to the interest rates, the establishment and ongoing fees and even key features (such as whether they have a redraw facilities or "mortgage off-set" facility).

However, even the most basic of product innovations can prevent a meaningful product comparison. For example, under a typical equity loan, the customer has a credit limit and the principal need not be repaid over a fixed term. In this case the cost of the product depends entirely upon how much the borrower chooses to use it and it will not be possible to calculate a comparison rate.

Even amortising loans have different repayment periods (ranging from 15 to 50 years) and these can have a significant impact on the total interest charges thereby complicating any meaningful comparison. This is further complicated by the fact that most loans are repaid well before the term thereby rendering information about total repayments meaningless.

Most mortgage loans have variable interest rates which means that any comparison will fail to take account of future changes to the rates being compared. Also, many of the costs associated with a mortgage loan are contingent on uncertain events such as late payment or the use of a redraw facility and these costs cannot be incorporated in a comparison unless a range of assumptions are made. The need to disclose such assumptions inevitably complicates the information being provided and undermines its utility as a comparison tool.

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