



# Good Shepherd Microfinance

## Introduction

**Our submission is based on our experience delivering inclusive credit products designed for people on low and medium incomes across Australia. An average of 2,200 people apply for safe and affordable credit through Good Shepherd Microfinance every week, providing us with important insights into the impact of all of the products being examined in this Senate inquiry.**

**We have long advocated for changes to regulations for payday loans and consumer leases, and now extend that call to fintech companies that provide credit but are exempt from responsible lending obligations due to a regulatory loophole. We consistently see people with multiple debt liabilities they are struggling to afford, with buy-now pay-later services now usually part of a consumers' financial position.**

**To ensure consumers on low incomes are adequately protected we believe the following are required: regulations that are effective and that are enforced; availability of safe and affordable credit; and an adequately resourced financial counselling sector.**

**This inquiry is critical to ensuring protection for consumers, and we would welcome the opportunity to further discuss our services, our data, and client case studies to the Senate Economics References Committee.**

### *What is NILS and StepUP?*

The No Interest Loan Scheme (NILS) offers people on low incomes safe, fair and affordable loans for fridges, washing machines and furniture, as well as education and medical expenses. Loans up to \$1,500 are available from 178 community organisation at 628 locations across Australia. In the 2017 - 2018 financial year 27,392 NILS loans were written.

To be eligible for NILS you must have a healthcare or pension card or earn under \$45,000, have lived in your current residence for three months, and have a willingness and capacity to repay the loan. There are no credit checks.

The StepUP Loan program, delivered in partnership with NAB, brings low interest loans of between \$800 and \$3,000 to people on low incomes. Around 78 per cent of StepUP loans are used to purchase a second-hand car or to pay for car repairs.

NAB provides operational funding and loan capital for NILS and StepUP, with Federal and state governments providing operational funding to support microfinance delivery across Australia.

### *What is Speckle?*

Speckle is an initiative developed by Good Shepherd Microfinance and National Australia Bank (NAB). Speckle loans are issued by Good Shepherd Microfinance and are small loans from \$200 to \$2,000 with repayment options ranging from three months to one year. Interest rates and fees are half the cost of major payday lenders, and dishonour fees and default fees are far lower.

To be eligible, you need a minimum annual income of \$30,000 (excluding government benefits) before tax to apply. Speckle is an ethical, scalable and sustainable small amount credit contract alternative for people on low and medium incomes. Speckle lends responsibly, complying with the responsible lending obligations, current legislation and the majority of recommendations made in the 2017 review.

Our call centre staff are trained to identify financial hardship and abuse, and provide referrals to NILS, StepUP, financial counselling, emergency relief and any local community services that can assist people that are experiencing crisis where a loan may not be a suitable option for them.

Good Shepherd Microfinance does not share customer data with NAB and we do not have any introducer arrangements or obligations with NAB. Furthermore, to maximise protection of client data we require our vendors to store data in Australia only. We would welcome the opportunity to demonstrate how our systems, business model and our customer journey are built to support better financial inclusion and resilience.

### *What is Good Money?*

Good Money provides access to safe and affordable financial products via a high street retail store. Good Money was launched in Victoria in 2012 with stores in Geelong, Collingwood and Dandenong. It expanded to South Australia in 2015 with the opening of a store in Salisbury, and into Queensland in 2017 with stores in Cairns and Southport. In 2017, an additional Victorian store was also opened in Morwell.

## **Payday loans and consumer lease providers**

**Good Shepherd Microfinance continues to see people impacted by small amount credit contracts and consumer leases that they cannot afford to service. Regulatory reform is necessary to protect consumers, most urgently in the consumer lease market, for which NILS is a safe and affordable alternative.**

**To meet unmet demand for NILS, over the past 12 months we have commenced digitally transforming NILS delivery, increasing response times, increasing the capacity of the network and removing barriers to entry. As a result the number of NILS loans is steadily increasing, and NILS is available via telephone-based delivery from most places in Australia. Awareness and demand for our online cash loan Speckle is also rising.**

Since the review of the legislation, Good Shepherd Microfinance has observed the payday lending and consumer lease markets continue to operate as business-as-usual. This means that we and our network of over 200 community organisations across Australia regularly see people with payday loans that they cannot afford to repay, and consumer leases that offer poor value and lock them into years of high repayments.

Affordability of repayments for payday loans is a key issue. It is common for lenders to write large loans with short repayment schedules, resulting in borrowers being unable to meet their debt obligation without significant financial hardship, and increasing the likelihood of them needing a subsequent loan and entering into a debt cycle.

The bank statement of a recent applicant had \$2,250 payday loan repayments in one month on their bank statement, with a total income of \$5,000, totalling 45 per cent of her total income. This example highlights a number of issues:

1. The lender may have breached their responsible lending obligation to ensure that a borrower can 'comply without substantial hardship', regardless of whatever additional SACC regulations are in place.
2. This example may trigger the current SACC 'unsuitability' rule for any subsequent loans (presumed unsuitable if the borrower has had two or more SACCs in the past 90 days), but this may not have been adequately considered at the time of application for current loans.
3. The low likelihood of this lender being disciplined for irresponsible lending or breaching legislation (unless legal action is taken) due to inadequacy of resources for enforcement.

This example demonstrates the need for greater enforcement of responsible lending obligations on payday lenders, and regulation that requires reasonable repayment schedules to ensure that consumers are not placed into financial duress and as a result are at risk of being continuously indebted.

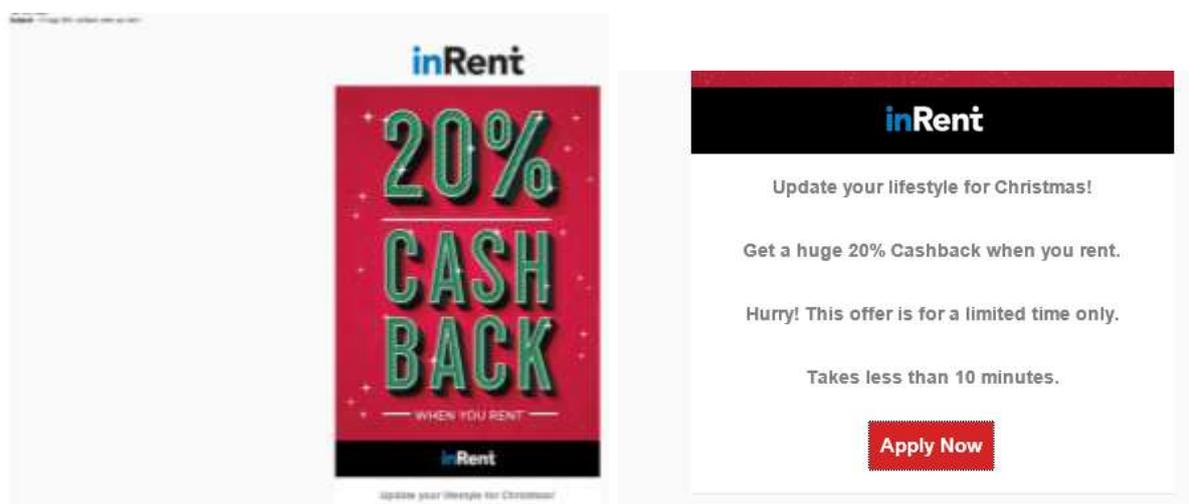
Another case study provided by our community partner Kyabra Community Organisation also demonstrates how unethical payday lending can exacerbate financial hardship:

*One service user took out a payday loan to purchase food for her family. She applied for the loan in person and when the staff member asked what she needed the loan for she was honest. The staff member responded that they were unable to give a loan for that purpose and asked the client to provide a different reason for the loan.*

*The client was then prompted by a friend to say car repairs (despite not owning a car), which satisfied the staff member's criteria and the loan was granted. The staff member was well aware that the loan would be used for basic living expenses and did not offer any referrals for financial assistance (e.g. financial counselling, emergency relief).*

For consumer leases, the key issues continue to be the low value of many consumer leases with no limitations on cost or contract length (as highlighted in previous submissions and in research undertaken by ASIC), lack of transparency for consumers and the aggressive marketing tactics used to target low income consumers.

As an example, a recent e-newsletter published by In Rent sent to consumers highlights the challenges for consumers to assess the value of an offer (see below):



The above example highlights a number of key issues that demonstrate the need for reform:

1. The advertisement lacks transparency about the value for the cashback offer, including whether it applies to the value of the item or the contract.
2. Consumer lease companies offer individualised pricing and do not provide detailed costs until a consumer makes an application, making it impossible for a consumer to assess the value of an offer without making an application.
3. Most people who use consumer leases do so because they have low incomes and cannot afford to purchase items outright. Therefore, offering 'cashback', targeted at Christmas time which is financially stressful especially for low income families, is a particularly aggressive marketing tactic.
4. Consumer lease companies have access to the Federal Government Centrepay system to assist people receiving Centrelink payments to manage their bills, and the majority of consumer lease users take up this payment method. We would question whether a 'cashback' offer would be allowable under this system.

A case study from Anglicare NT in Alice Springs demonstrates how consumer leases can take up a large proportion of a consumers' budget without adequate affordability assessment, and the challenge financial counsellors experience escalating matters:

*A client was referred to a financial counsellor in a very remote area due to the NLS worker seeing that 58.5% of her income was going towards consumer leases from two companies.*

*After doing timelines of the borrowings from these rent-to-buy places and what the client's Centrelink was at the time, it was found that at the date when her last item was rented, 27.75% of her Centrelink income was being taken up. She was also allowed to rent two televisions at once from each place (four televisions altogether) and a stereo from each place plus other household items.*

*27.75% of the client's income was at a time when she was receiving both the Disability Support Pension and Family Tax Benefit. Between the time when she arranged the rentals and when she came and first saw the financial counsellor, her family tax benefit stopped and this is what forced her repayments to these agencies to become 58.5% of her income.*

*After the client's payment had stopped to one company, they tracked her down again and re-signed her taking 28.62% of her Disability Support Pension. The financial counsellor believes this shows that the company did not do any financial assessment when re-signing the client and the counsellor reminded the company that it is against their responsible lending obligations.*

*The client has now stopped payments altogether as she will be on the Disability Support Pension for the rest of her life, can borrow through the No Interest Loan program and does not care about her credit file or rating. The rent-to-buy agencies have stopped chasing the client. The financial counsellor informed ASIC about the details of this case, however as far as they are aware this has not triggered investigation or enforcement action to date.*

In contrast, NLS offers a transparent, safe and affordable alternative to consumer leases that is increasingly available to people on low incomes across Australia.

Over the past 18 months Good Shepherd Microfinance and our national network of providers have implemented a range of changes designed to widen the availability of NLS and increase the capacity of our network to meet demand for NLS, and we are starting to see the results of this hard work.

These changes include digitising and centralising loan processing, to increase the efficiency of the loan application process, and in turn increasing the time available for client service providers to have financial conversations with loan applicants. These changes have also led to faster turnaround times (maximum 48 hours loan approval time, often much faster) and increased availability of phone applications<sup>1</sup>. In regions that have completed the transition to new systems, the changes have led to a significant increase in the number of applications being processed every week between January and October 2018.

We believe these changes are future-proofing NLS, and are working towards achieving our goal of 100,000 loans per year by 2020.

## **Unlicensed financial service providers including 'buy now, pay later' providers and short term credit providers**

**The biggest change in the fringe lending sector since the review was conducted has been the dramatic rise of buy-now pay-later providers, and other short-term credit providers, that take advantage of legal loopholes to avoid having to comply with responsible lending obligations.**

**Good Shepherd Microfinance estimates that 30 per cent of loan applicants are repaying a buy-now pay-later purchase, with around 10 per cent having a large debt, and it is rare that buy-now pay-later is the only form of credit that appears on an applicant's bank statement.**

**From a regulatory perspective, a key issue is that consumers can purchase items that cumulatively equal more than loan limits covered under SACC legislation with no assessment**

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<sup>1</sup> <https://goodshepherdmicrofinance.org.au/assets/files/2016/05/GSM-AR2017-180125-WEB.pdf>

**of affordability, even if they have no income. We advocate for consumer protections that include verification of income, assessment of affordability and photo ID check.**

Over the past 18 months, Good Shepherd Microfinance and our partners have observed the rapidly increasing use of unregulated buy-now pay-later sector by consumers across all income levels. These services can be used to purchase almost anything, from retail items like toys and clothing, to flights, alcohol<sup>2</sup> and essential food items such as meat<sup>3</sup>.

To understand this phenomenon better, the Melbourne Microfinance Initiative explored the use of these services by people under the age of 25 years old via 154 surveys and interviews<sup>4</sup>. Key findings relating to the users' most recent purchase include that:

- › 75% bought something that they did not need with their most recent purchase.
- › 54% bought something they wouldn't have bought otherwise with their most recent purchase.
- › 41% have paid at least one late fee, 19.2% due to lack of funds due to low income
- › 60% are spending more money than they were before buy-now pay-later was introduced
- › 10% made repayments by borrowing money (family, friends, cash loan or credit cards)
- › 80% had some form of existing credit (car loans and credit cards the most common)

However, the research also found that these financial services are valued by many consumers for their convenience and ability to smooth consumption, with examples of responsible consumption enabling very low income consumers to access items that improved their health and wellbeing that would otherwise be unattainable.

Case studies of buy-now pay-later provision that we have encountered can also inform this inquiry. One loan applicant recently provided us with a 90 day bank statement containing 288 buy-now pay-later transactions totalling \$5,600. This case study demonstrates the large amount of credit that can be accessed with no verification of income, credit check or assessment of capacity to repay.

Another recent loan applicant was a 21 year old woman, living in a shared house, receiving Youth Allowance as her only source of income (\$566 per fortnightly). At the point of application, the applicant had \$246 utility debt, a buy-now pay-later balance of \$1004 with one company, a payday loan of \$500 and \$612 balance with another buy-now pay-later company, with all debts totalling \$2,362, despite having very little money left over after living expenses had been taken into account. Buy-now pay-later had been used to buy a range of small to medium items from clothing and toy stores. The loan application did not proceed as the loan officer assessed that due to the debt the applicant was in severe financial crisis. This case study also demonstrates the large amount of credit, including credit that requires no assessment of affordability, which can be accessed from multiple lenders by people on very low incomes.

In addition, new fintech companies continue to emerge with business models that are reliant on regulatory loopholes. Most recently we have become aware of 'Defer it', offering consumers credit to defer bill payments (they recommending deferring household bills), for the cost of \$5 per month with repayments scheduled every fortnight for four weeks. However, our experience with people on low incomes is that those that are struggling with bill payments will find it difficult to catch up once they fall behind, even with the option to spread this deficit over four payments.

Our view is a more sustainable option for consumers struggling to afford their household bills would be to contact utility providers who can set-up affordable payment plans, arrange home energy assessments, refer to financial counsellors, provide information about state government utility grants and ensure concessional entitlements are being accessed (we know they often are not).

We believe that buy-now pay-later services and other credit products that operate functionally as credit products, should be required to lend responsibly via compliance with the responsible lending

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<sup>2</sup> <https://www.finder.com.au/afterpay-alcohol-food>

<sup>3</sup> <https://www.meysmeats.com.au/>

<sup>4</sup> Melbourne Microfinance Initiative (2018) Understanding the use of buy-now pay-later services by Millennial consumers

obligations. This would mean verifying a clients' income and identification, and adequately assessing their ability to repay the credit being sought.

**Debt management firms, debt negotiators, credit repair agencies and personal budgeting services, and financial counselling**

Through our work we observe companies offering for-profit debt management or budgeting services charge significant fees and over promise, particularly with regard to influencing the contents of a credit file. We also know that they clog up external dispute resolution channels without being members, and are quick to advise clients to go bankrupt or into debt agreement instead of just negotiating hardship and payment arrangements. We know that many of their clients are under 24, and may not understand the long term effect on their credit.

Yet, financial counselling provides the same service without any cost to the client. One of the reasons these businesses have grown exponentially is the serious shortage of free, independent, community-based financial counsellors. Face to face financial counselling agencies have long waiting lists, up to six weeks in many places. Calls to the National Debt Helpline, the phone financial counselling service, are at record levels. Current estimates point to a 5% increase this year, on top of 12% last year.

More funding for financial counselling is urgently needed, in addition to more funding for financial capability services that provide individual education and support that can reduce the need for intervention at the point of financial crisis.