



**SMALL
BUSINESS
DEBT HELPLINE**
1800 413 828

CHOICE



**financial
counselling
australia**



**consumer
action**
law centre



Financial Rights
LEGAL CENTRE

Joint Response to Treasury on the Small Business RLO Exemption

19 August 2024

About Us

FCA

Financial Counselling Australia (FCA) is the national voice for the financial counselling profession in Australia. We are a not-for-profit organisation which provides resources and support for financial counsellors and works to raise awareness about the availability and value of financial counselling. FCA advocates for a fairer marketplace for consumers and aims to improve hardship processes for people in financial difficulty. We coordinate the National Debt Helpline and manage the Small Business Debt Helpline. Our vision is for an Australia with fewer people in financial hardship.

SBDH

The Small Business Debt Helpline (SBDH) is a national service providing financial counselling support to small businesses. Originally established as the Small Business Bushfire Financial Counselling Support Line in March 2020, SBDH supports any small business owner experiencing financial difficulty. SBDH is the only nationally available financial counselling service for all Australian small businesses. SBDH also provides training and information to other financial counselling agencies and secondary consultations to generalist financial counsellors whose clients operate a small business. SBDH is managed by FCA.

FRLC

Financial Rights Legal Centre (FRLC) is a community legal centre that specialises in helping consumers understand and enforce their financial rights, especially low income and otherwise marginalised or vulnerable consumers. We provide free and independent financial counselling, legal advice and representation to individuals about a broad range of financial issues. Financial Rights operates the National Debt Helpline, which helps NSW consumers experiencing financial difficulties. We also operate the Insurance Law Service which provides advice nationally to consumers about insurance claims and debts to insurance companies, and the Mob Strong Debt Help services which assist Aboriginal and Torres Strait Islander Peoples with credit, debt and insurance matters.

CALC

Consumer Action Consumer Action (CALC) is an independent, not-for profit consumer organisation with deep expertise in consumer and consumer credit laws, policy and direct knowledge of people's experience of modern markets. We work for a just marketplace, where people have power and business plays fair. We make life easier for people experiencing vulnerability and disadvantage in Australia, through financial counselling,

legal advice, legal representation, policy work and campaigns. Based in Melbourne, our direct services assist Victorians and our advocacy supports a just marketplace for all Australians.

CHOICE

CHOICE is the leading consumer advocacy group in Australia. CHOICE is independent, not-for-profit and member-funded. Our mission is simple: we work for fair, just and safe markets that meet the needs of Australian consumers. We do that through our independent testing, advocacy and journalism. To find out more about CHOICE's work visit

www.choice.com.au/campaigns

Response to Consultation

We welcome the opportunity to provide feedback on the proposal to extend the small business responsible lending obligations (RLOs) exemption.

There is an appendix on page 7 of this response with a comprehensive case study, written by a financial counsellor.

We believe the small business RLOs exemption should expire, for the following reasons:

1. Lending that should be subject to RLOs can fall outside them under the exemption

The exemption's wording enables lending that should be subject to RLOs to fall outside the regime.

The consequences of loans falling outside the RLOs are significant. It means the borrower takes on all the responsibility for assessing their ability to make repayments. And partial business purpose loans can be for large sums of money.

Consumers who are particularly vulnerable include casual rideshare drivers, e-commerce delivery drivers, student delivery drivers, and those who are running their small business as a second form of income in response to cost of living pressures.

A financial counsellor told us:

"The exemption ... fails people who are doing a second job in order to make ends meet."

The attached case study is an indicative example in which a financial counselling client had a small kitchen renovation company. He was seeking a business loan of \$5,000 to pay suppliers and he was in arrears \$10,000 on his mortgage, so he requested to borrow \$15,000. This loan was predominately personal. Were it not for the exemption, it would not have been a business loan.

He was then upsold a loan of \$30,000 by the creditor. In about a year, this loan had escalated into a debt of more than \$74,000.

The financial counsellor who supported him said:

"It was very distressing to work with this client, his financial literacy was low, and things progressed quite quickly."

Please read the full details of this case study in the appendix, to understand how people can be harmed by this exemption.

2. The exemption opens the door to poor lending practices

We understand the exemption was introduced after lenders argued it was too difficult to assess whether a loan was “wholly or predominantly” for business purposes.

Placing the onus on lenders to ensure a loan fits this description is not a big ask. Lenders should conduct inquiries into the reasons for a loan, to maintain protections for people who need them.

Without these deeper inquiries from lenders, problematic practices arise. Financial counsellors have come across loan companies that prompt people to simply tick a box online declaring a loan is for business purposes.

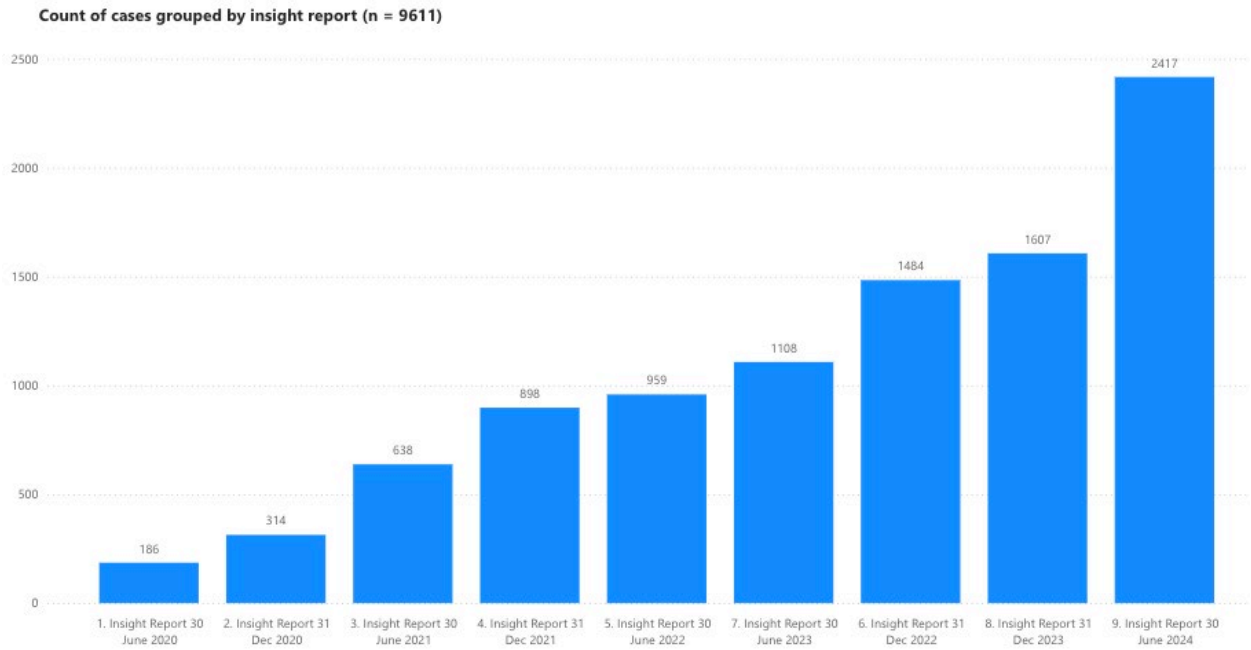
If the consumer ticks the box, the loan gets approved. If they don't tick the box, the loan won't be approved. It's clear what many people seeking a loan would do in this situation.

3. Small business operators experience many of the same vulnerabilities as consumers

The exemption is founded on the premise that small business operators are somehow less vulnerable than typical consumers. But we have vast amounts of evidence to show otherwise.

The Small Business Debt Helpline (SBDH) receives calls from people impacted by mental health illnesses, high levels of distress, low levels of financial/business literacy, and domestic and family violence. Some callers face language and cultural barriers. There are also situational considerations which may make a borrower vulnerable, such as desperation.

Demand for the SBDH's financial counselling services has been rapidly increasing. In July 2024, demand was up 77 per cent from the same month in 2023. As the graph below shows, demand has been steadily rising since the service was established in 2020.



We believe if the exemption were to be extended, it would exacerbate some of the financial issues facing small business operators.

In the case of dual-purpose loans, the one borrower is just wearing two hats of small business operator and consumer. RLOs and the protections they afford are still needed to protect these individuals.

Appendix

Case Study - Written by a Financial Counsellor

Some details have been changed, including the client's name, to protect his identity.

Business Loan Provided for Non-Business Use

Gary was married and had two young school-aged children. He owned a small kitchen renovation company.

Some of his work was delayed in late 2021 due to a second round of COVID lockdowns. In the meantime, the cost of supplies increased.

Gary completed the work in early 2022 but lost money on the jobs he had quoted six months earlier. As a result, Gary was unable to pay himself and he had a small amount of supplier debt. Although he had more work ready to start, he was unable to purchase supplies until he cleared the debt owing to his suppliers.

Gary had mortgage arrears of \$10,000 and needed \$5,000 to pay his suppliers.

In July 2022, Gary sent an enquiry to an online business lending broker. The online lending platform was an AFCA member and had a credit license.

In response to his enquiry, a broker representative contacted Gary to discuss his requirements. He explained that he needed \$10,000 for mortgage arrears and \$5,000 for supplier debt.

The broker recommended First Cash Flow Solutions as a lender who would be able to assist. Gary gave consent for the broker to pass his information on to First Cash Flow Solutions. He was told "These are the best guys for you." He wasn't given any other options.

Gary was contacted by First Cash Flow Solutions and was told that they could assist with a business loan, but a condition of the loan was that he would need to use part of it to pay his mortgage arrears. Even though Gary had only requested a loan of \$15,000, he was offered a loan of \$30,000.

The product was offered as a business line of credit which was secured by a second mortgage on his property. At the time of the loan, his property was valued at approximately \$650,000 with a mortgage of \$380,000.

A second condition of the loan was that as guarantor of the loan, Gary could not be in arrears with the primary mortgage holder (a major bank) or council rates. This would be an act of default.

“The borrower is required to ensure that the 1st mortgage repayments and council rates with respect to the Secured Property referred to in item 11 of the Schedule are up to date and do not fall into arrears. The lender may request evidence of the same during the term of the First Cashflow facility and upon such a request, the Borrower must provide the evidence requested within (3) business days. Non-compliance and/or if a payment due and owing to the first mortgagee or if council rates are in arrears will constitute an Event of Default pursuant to this Deed.”

Gary explained that he was in a very dark place mentally and experiencing major depression when he signed the loan contract.

He stated, “I had never done anything like this before, I didn’t really understand what I was signing.”

Gary was approved for the \$30,000 business line of credit. The facility initiation fees and charges were added to the account making the Facility Limit \$33,124.50.

First Cash Flow Solutions paid the ANZ Mortgage arrears of \$10,500 and council rates arrears of \$638.28 directly from the account and sent receipts to Gary by email.

The email stated:

“Please ensure your mortgage repayments and council rates don't fall into arrears which will put the First cashflow facility in default.”**

Although Gary was so relieved to clear his mortgage and rates arrears in July, unfortunately he was not able to make the August mortgage payment due to insufficient income, because he had no income.

Gary was already in default of his First Cashflow Solutions contract only 16 days after signing it.

Perhaps if the broker or the lender had been required to make enquiries about Gary's capacity to repay the loan and not fall into arrears on the primary mortgage as required by the contract, Gary would not have been approved for a business loan to repay mortgage arrears.

At first, the minimum line of credit repayments was affordable for Gary, only about \$140/week in interest and a \$33.00/month loan administration fee. Direct debits were successfully paid from his account for about eight months before he had a few failed payments. Each time a \$144.84 payment failed, Gary was charged a Direct Debit rejection fee and a Repayment Default fee of \$1,100.00. This happened ten times in a three-month period. On top of this, he was also charged a monthly Facility Default Management Fee of \$440.00 and an additional monthly Facility Risk Fee of \$828.11.

When First Cashflow Solutions realised that Gary's primary mortgage was in arrears, they sent him a default notice calling in the full loan plus another default fee of \$1,100.00. When Gary was unable to pay the debt in full by the due date, First Cashflow Solutions obtained a judgment and was granted an order for possession by the Supreme Court. With penalties, fees and legal costs added, Gary's \$30,000 line of credit grew to a debt of \$74,706.45 - including \$12,990.00 in legal fees.

"Things have gotten much worse, I have received a notice from the Sheriff's office for me and my family to vacate the property early next month. Looks like they have won and there is not much I can do," Gary said.

"The worst thing is that the stress of this has caused me to lose my job which makes things very hard. I'm looking for another job, it has to be full-time so we can find a place to rent.

"The only good news is that I don't have to deal with First Cashflow Solutions anymore."