LAW AND CHANGE

THE 1992 SCOCAM CREDIT BILL

On 31 July 1992, the Standing Committee of State Consumer Affairs Ministers ('SCOCAM') released draft consumer credit legislation for public comment. Preparation of the draft, known as the Credit Code, by New South Wales Parliamentary Counsel, followed a resolution by SCOCAM to repeal existing credit legislation in each jurisdiction[1] and enact a uniform scheme.

There has been some criticism of SCOCAM for publishing the Credit Code despite the failure of the Ministers formally to adopt it.[2] Two important issues have been the subject of dispute. First, whether and to what extent the Code should permit credit providers to charge fees in addition to interest (such as establishment fees and line fees) and secondly, the extent of automatic civil penalties, for example whether interest charges should be automatically forfeited where the credit provider fails to comply with disclosure requirements. In the light of the failure to resolve these fundamental policy matters, it is perhaps surprising that consumer and industry groups were invited to make detailed submissions on technical drafting points. There was also a mood of scepticism before publication. This is the second bill considered by SCOCAM in 12 months.[3] Some 12 months before that, the Victorian Law Reform Commission also published a draft bill under the direction of SCOCAM.[4] Given the fate of its predecessors, there must therefore be a question of how seriously the Code ought to be regarded.

Since the publication of the Credit Code, the Prices Surveillance Authority ('PSA') has published its report on credit card fees.[5] In that report, the Authority recommended that the restrictions on credit card pricing imposed by the credit legislation ought to be lifted subject to adequate disclosure of charges. SCOCAM has not yet responded to the PSA's recommendations, but they have been endorsed by the Federal Treasurer who has indicated that Commonwealth legislation may be introduced. The extent of this circumvention of the SCOCAM process is unknown, and it is unclear whether the Commonwealth's constitutional powers would support legisla-

1 In Victoria, the relevant legislation is the Credit Act 1984 (Vic.). There is corresponding legislation in New South Wales, the Australian Capital Territory, Queensland and Western Australia. In South Australia the legislation to be replaced is the Consumer Transactions Act 1972 (S.A.) and the Consumer Credit Act 1972 (S.A.). Moneylending legislation will be repealed in Northern Territory and Tasmania. In this Note all references are to the Credit Act 1984 (Vic.) unless otherwise indicated.

2 Edwards, S., 'Credit Law: An Industry Update' in *Credit Law 1992* (1992) Vol. I, 109, 112.

3 The Credit Bill 1990 was drafted by the South Australian Parliamentary Counsel for SCOCAM. It has been criticized by both industry and consumer groups.

4 Victorian Law Reform Commission, *Draft Credit Bill 1989* (1989).

5 Price: Surveillance Authority, *Enquiry in Relation to Credit Card Interest Rates*, Report No. 45 (1992).

tion with the breadth of the Credit Code.[6] Further policy shifts within SCOCAM itself are likely because of changes of government of member States. The Victorian Liberal Government's pre-election Fair Trading Policy Statement referred with approval to uniform national credit legislation, implying support for the SCOCAM process, but as yet the Minister has not made any public comment on outstanding policy issues or the latest draft.

Despite calls for national credit legislation, it would seem unlikely that this would occur in the near future because it is unclear that the Commonwealth's constitutional powers would encompass the whole field of consumer credit regulation. For this reason, the SCOCAM process needs to be taken seriously. In comparison with the preceding attempts which were the subject of quite trenchant criticism, this draft has received a measure of support both from finance industry and consumer groups.[7] Its publication has further developed the debate concerning reform of the existing legislation which, from an industry perspective, is generally agreed to have become almost unworkable. It is also useful to consider the implications of the Code so that changes can be suggested before agreement is made at the political level.

1. *LEGISLATIVE SCHEME*

The enactment of credit legislation in Victoria, New South Wales, Western Australia and the Australian Capital Territory during 1984 and 1985 was intended to presage a uniform scheme. However, from the outset it was clear that this would not be achieved. South Australia retained its consumer credit legislation enacted in 1972, and Northern Territory and Tasmania retained their antiquated moneylending legislation. Those dissidents declined to enact the credit legislation, especially as problems began to emerge with the drafting of the Act.[8] Queensland brought in legislation in 1987 which is similar to the Credit Act but different in some notable instances. These range from the minor — such as section numbering, text of notices and statements prescribed for use under the regulations — to the fundamental — such as the sections governing the scope of the Credit Act,[9] and the absence of a formal licensing regime for credit providers.[10]

The uniformity of the scheme began to break down even in those jurisdictions which had substantially enacted the same legislation. This occurred in several ways. First, the Credit Act permits transactions or organizations to

6 *E.g.* the banking and corporations powers would presumably not support regulation of terms sales by individual retailers.

7 Edwards, *op. cit.* n. 2, 105 (Australian Finance Conference); Niven, D., 'Consumer Update' in *Credit Law 1992* (1992) Vol. I, 103, 105 (Consumer Credit Legal Service, Victoria).

8 These included the failure of the legislation to address some kinds of open-ended credit arrangements, particularly those with daily calculations of interest: see Noblet, M., 'Consumer Credit Law and Uniformity: Implementation' (1986) 10 *Adelaide Law Review* 131.

9 See Duggan, A. J., Begg, S. W. and Lanyon, E. V., *Regulated Credit: The Credit and Security Aspects* (1989) para. 2.1.54.

10 Instead, a credit provider may be disqualified from carrying on business: Credit Act 1987 (Qld) s. 147.

be removed from some or all of its provisions by Exemption Order. There has been a proliferation of these orders but they are not uniform across all jurisdictions. For example, Victorian exemption orders exclude credit provided by stock and station agents for livestock dealing and from parts III-VIII provide for the acquisition of farms on a 'walk in walk out' basis.[11] These orders have not been adopted in the Australian Capital Territory.[12] Secondly, there have been statutory amendments concerned with procedures for relief from civil penalties and validating credit contracts which do not properly disclose insurance commissions, but these are not uniform. For instance, New South Wales has established a Financial Counselling Trust Fund to which the Credit Tribunal may direct credit providers to pay credit charges lost under s. 42 in lieu of requiring them to post refunds.[13] This initiative has not been adopted in any other jurisdiction. Lastly, courts and tribunals have diverged in their interpretation of certain essential features of the legislation.[14] All this has led to a most unsatisfactory commercial environment for credit providers, one in which the large legal and operational expenses are ultimately passed on to the consumer.

The Credit Code uses the 'template approach' to achieve uniformity.[15] The procedure is as follows. As a preliminary, all participating jurisdictions enter into a formal agreement which sets out the terms of the scheme. Pursuant to this, one jurisdiction, in this case Queensland, will enact the substantive legislation and promulgate the regulations. All other jurisdictions will pass short enacting legislation adopting by reference the terms of the Queensland legislation in force from time to time, repealing their own credit legislation and making any other necessary legislative changes referable to their own jurisdiction. There may also be non-uniform provisions, by agreement, such as vesting of jurisdiction in courts or specialist tribunals. From time to time, Queensland will pass amending legislation approved by at least a majority of SCOCAM members[16] which is then automatically applicable in each participating jurisdiction by virtue of the enacting legislation.

As a corollary, the legislation will deal with statutory interpretation (for example calculation of distance, time and age) which at present differs between jurisdictions. The current approach is to append a section to the Code dealing with these matters. Of course the template technique will not

11 That is, the provision of credit for the acquisition of goods being a commercial vehicle or farm machinery, or land where the land is acquired primarily for the purposes of a farming undertaking and the goods are intended for use in that connection.

12 See Duggan, Begg and Lanyon, *op. cit.* n. 9, paras 2.1.51-52.

13 See generally Cockburn, A., 'Consequences for Failure to Comply with the Credit Act: Some recent examples' in *Credit Law 1992* (1992) Vol. II, 169, 195.

14 *E.g. Australian Guarantee Corporation Ltd v. Faint* (1992) A.S.C. 56-153 (N.S.W. Commercial Tribunal); *Custom Credit Corporation Ltd v. Gray* (1991) A.S.C. 56-096 (Full Court of Victorian Supreme Court); *Westpac Banking Corporation v. Donald-Murrell* (1992) A.S.C. 56-151 (Victorian Supreme Court); *Westpac Banking Corporation v. Various Respondents* (1992) A.S.C. 56-176.

15 This is the same approach as that adopted in the Australian Financial Institutions Commission legislation and in the case of the Corporations Law.

16 Whether there must be unanimity has not yet been disclosed.

overcome the problem of conflicting judicial decisions. Hopefully this will be alleviated by the less prescriptive approach of the Code which accords credit providers more latitude in the contracting process. It remains a matter of considerable concern, however, that consistency across jurisdictions, which is so vital for credit providers operating on a national basis could be threatened by differing judicial interpretations. It is also not desirable for an individual debtor to have different rights under the same piece of legislation in different jurisdictions.

2. *APPLICABLE LAW*

Under the Code the credit legislation to be applied is that of the place in which the debtor resides when the contract is made.[17] Under the Credit Act, by contrast, the relevant law is that of the jurisdiction where the debtor signed the credit contract.[18] The current approach reflects the recommendations of the Molomby Committee.[19] The different test adopted by the Code may derive from the point of view that the most important consideration in a consumer transaction is the debtor's place of residence, because that is where the social consequence will ensue.[20] This consideration, however, should be balanced against the need for the credit provider to know with certainty which legislation will govern the initial contracting process. This policy concern will be effectively resolved if the legislative scheme, including the regulations which dictate the contents of prescribed forms, operates in a truly uniform way. If this were the case, the contract between the credit provider and the debtor could not be impugned simply because of the choice of jurisdiction.

3. *SCOPE OF THE CODE*

The apparent purpose of the Code is to regulate virtually all consumer transactions of a functionally similar nature, regardless of the identity of the credit provider or the debtor, or the form of the transaction.

(a) *Credit Providers*

The Credit Code encompasses all types of credit providers[21] so that, for example, credit transactions by credit unions, building societies and other co-operative societies will be regulated. These institutions are exempted from most of the provisions of the Credit Act on the assumption that the relationship between the members made specific legislative protection unnecessary. Also, they are already subject to regulation, albeit of a more

17 Cl. 5(1).
18 Ss 3(1), 5(1), 17.
19 Law Council of Australia, *Report to the Attorney-General for the State of Victoria on Fair Consumer Credit Laws* (1972) para. 9.2.3.
20 See Duggan, A. J., *Regulated Credit: The Sale Aspect* (1986) 348, n. 13.
21 Except pawnbrokers or trustees of estates who advance to beneficiaries: cls 6(8), 6(9). Note, however, Division 2 of Part 6 which allows for variation on the grounds of hardship and re-opening of unfair contracts.

limited kind.[22] The belief that specific protection is not necessary no longer enjoys wide support. Secondly, the prohibition of variable rate loans in the existing legislation presented a major obstacle to their inclusion, since such loans are one of the principal products offered by those societies. Variable rate lending is now permitted under the Code subject to certain safeguards.

Although banks are *prima facie* covered by the Act and indeed bank personal loans and Bankcard are regulated by the statute, many significant bank products such as housing loans, overdrafts and some types of term loans are exempted from its operation.[23] The Code applies to these transactions. Overdrafts, except where a cheque account is overdrawn without prior arrangement,[24] will be regulated by the Code as a credit contract. The initiatives referred to above have the major benefit of removing a competitive disadvantage from finance companies who are now vying directly with the banks and societies in the consumer credit market. They also ensure that debtors enjoy the same protection regardless of the institution from whom they obtain credit.

(b) *Debtors*

The Code affords protection to individual debtors but, like the Credit Act, does not extend to corporations.[25] The Act presently contains a monetary ceiling which, subject to the exceptions mentioned below, limits the scope of its application.[26] A credit sale contract involving a commercial vehicle, farm machinery or a loan contract secured by a mortgage relating to those types of equipment will be regulated irrespective of the amount of credit involved. There is no similar extension in the case of continuing credit contracts. Under the Code these special categories will disappear. There is also presently special limited protection in New South Wales for home buyers under the Credit (Home Finance Contracts) Act 1984 (N.S.W.). The Code assimilates housing loan contracts with other credit contracts but there are concessions to existing practices. For example, only housing loans can have interest charged at a higher rate reducible to a lower rate if payment is made on time.[27]

(c) *Transactions*

The Code abandons the Byzantine drafting which characterizes the provisions that define the scope of the Credit Act. The new draft employs a radically simplified definitional structure by making 'credit' and in turn 'credit contract' central. Species of credit contracts are not separately regulated except in the case of consumer leases (Part 10).[28] The Code

22 *E.g.* Co-operation Act 1981 (Vic.).
23 See s. 18 and by way of example, the Term Loans Exemption Order.
24 Cl. 6(3).
25 Except strata corporations, that is, strata title and company title companies: cl. 5(1).
26 In Queensland, $40,000; in other jurisdictions $20,000.
27 With some safeguards: cls 24(3), 25.
28 There is some special treatment of housing loan contracts but this does not disturb the definitional structure.

attempts to deal with single advance and multiple advance transactions within one set of provisions. On the one hand this avoids many of the pitfalls inherent in the existing separate treatment of continuing credit contracts.[29] However, it does disguise the functional difference between these types of transactions which may cause different problems such as the imposition of the requirement to give a statement of account[30] in inappropriate circumstances.

For the purpose of the Code, credit is provided 'where one person ... allows another ... to defer payment of a debt, or to incur a debt and defer its payment,'[31] a definition drawn from the United States Truth in Lending Act.[32] The adoption of the U.S. precedent ought to occasion no surprise or concern since debt deferral must underpin the notion of 'financial accommodation' by which credit is defined in the Credit Act.[33] What is open to criticism is that the Code insufficiently addresses the issue raised by the concept of deferral. That is, if deferral turns on the contractual date for provision of the benefit relative to the payment date, how does this apply to transactions like leasing, hire purchase and lay-by sales? These three categories were dealt with expressly by the Credit Act. The Code is silent as to lay-by sales. It defines hire purchase as a sale by instalments for the purposes of the Code[34] and assimilates them in that way to other credit contracts. 'Consumer leases' are dealt with separately in Part 10. There is, however, no clear answer as to whether a mortgage securing a consumer lease is one 'which secures obligations under a credit contract' and is thus regulated. This needs to be clarified.

(d) *Exclusions*

Some credit transactions are expressly excluded from the Code. These include credit for the purposes wholly or predominantly of investment by the debtor or for participation by the debtor in any other profit-making venture,[35] short term credit not exceeding 2 months,[36] overdrafts and other credit without prior arrangement,[37] credit provided under insurance contracts for funding payment of premiums,[38] and credit for which only an account charge is payable.[39] Joint debit and credit facilities are included to the extent only that credit is provided.[40] Although working drafts of the Code contemplated the regulation of bill facilities, they are now excluded.[41]

29 Duggan, Begg and Lanyon, *op. cit.* n. 9, para. 2.1.36.
30 *Cf.* Cl. 35 and s. 35.
31 Cl. 4(1).
32 *I.e.* Consumer Credit Protection Act 15 U.S.C. (1982 ed.) s. 1602 (e); see also Truth in Lending Regulations (Regulation Z) 12 C.F.R. s. 226.2 (a)(14).
33 S. 5(1).
34 Cl. 10.
35 Cl. 6(1).
36 Cl. 6(2).
37 Cl. 6(3).
38 Cl. 6(7).
39 Cl. 6(4).
40 Cl. 6(5); the Code does not apply if the charge for a transaction is the same whether or not there is a debit or credit balance.
41 Cl. 6(6).

All other transactions involving the provision of credit will be regulated, but only if that credit is 'provided wholly or predominantly for private purposes'.[42] This exclusion derives from the Queensland Credit Act,[43] which differs from other jurisdictions by including the words 'or predominantly'.[44] There is, however, an issue as to what 'predominantly' means: is this 50% or 75%? Is it the debtor's or the credit provider's purpose which is to be taken into account?[45] It is provided that the Code is presumed not to apply where the debtor signs a certificate in which he or she declares that the credit is to be applied wholly or predominantly for business purposes before entering into the contract.[46] This concession will not apply if the credit provider has actual or constructive notice of the private use of the credit. Use of the certificate, therefore, will not solve the hard case where an employee has knowledge or suspicions which are then imputed to the credit provider. Certainty as to the application of the Code ought to be a paramount objective and to this end, a certain arbitrariness should be tolerated. It is desirable that a definition of 'predominantly' be inserted to achieve this.

The Code envisages the possibility of other exclusions, including a monetary ceiling, being contained in regulations.[47] As yet, none have been publicly mooted. It is to be hoped that the Ministers will resist the temptation to follow the unfortunate precedent of the Credit Act where significant general exceptions have been made through Exemption Orders by the executive. It is most unsatisfactory both for credit providers and debtors that the scope of protection offered by the legislation can only be ascertained by reference to government gazettes.

4. *SUBSTANTIVE PROVISIONS*

(a) *Disclosure*

One of the most important features of the Code is that it identifies certain 'key requirements' in relation to the provisions and operation of a credit contract which must be disclosed accurately to the debtor.[48] The Code is otherwise far less prescriptive about the contents of the contract than the Credit Act. The key requirements generally relate to the total amount of credit provided and the amount of interest charges or means by which those charges are to be calculated. In contrast, the Credit Act requires the detailed itemization of the credit provided and applies a civil penalty for breach.[49] The innovations contained in the Code are highly

42 Cl. 5(1)(b).
43 Credit Act 1987 (Qld) s. 7(1).
44 In other jurisdictions the concession is contained in the Business Finance Exemption Order, and this only excludes such transactions from Parts III-VIII of the statute.
45 See Robinson, T., 'The Scope of the SCOCAM Credit Code, 1992' in *Credit Law 1992* (1992) Vol. I, 119, 124-5.
46 Cl. 11(2).
47 Cl. 6(10).
48 Cl. 131.
49 Loss of credit charges (s. 42) subject to reinstatement (s. 85).

desirable in the light of the difficulties faced by credit providers in complying with the Credit Act. The Credit Act has proved very expensive both because of lost credit charges and in terms of checking procedures, expenses which are ultimately passed on to the consumer.

The narrowing of disclosure requirements to those judged most essential to the decision to enter into the contract, or fundamental to its operation, represents a sensible compromise between the need to protect debtors and the desire to facilitate the business of providing credit. Further, the Credit Act has been justly criticized for its provision of civil penalties such as the loss of credit charges in all cases where error has occurred, even if this does not disadvantage the debtor or can be rectified by the credit provider. The Code provides that interest charges will be restored if, within six months of its occurrence, the credit provider rectifies the error and notifes the debtor and the relevant government consumer department or agency.[50] The error must be inadvertent and not first brought to the attention of the court or tribunal by the debtor. The concept of 'self rectification' has been the subject of some adverse criticism from the consumer lobby on the basis that it may encourage credit providers to slacken their emphasis on initial compliance by their officers. It is likely, however, that the six month limitation will be sufficient to prompt credit providers to maintain their current procedures.

(b) *Interest Rates*

The principal feature of the Code is that it permits both fixed and variable rates in the case of fixed sum contracts, unlike the Credit Act which only permits the former. The credit provider will not be able to switch between types of rates unless the contract permits this at the outset. The credit contract must include a statement of the 'means by which the debtor will be informed of the variation' and, if the interest rate is increased during the term of the contract, prior notice of the variation must be given.[51] If the debtor's instalments increase as a consequence, prior notice of 14 days must be given.[52] For this reason floating rates (such as those tied to a bank bill rate or overdraft rate), although ostensibly permissible, may be prohibited.[53]

A fixed rate contract cannot be varied even by agreement to provide for a variable rate.[54] It is unclear what the precise intention is as regards higher and lower rates, described as differential rates. Clause 15(4) refers to a housing loan contract 'under which a higher rate of interest may be charged when payments are in default', and cl. 25(2) provides: 'A housing loan contract may provide for a differential rate of interest, but the higher rate may be charged only in the event of default.' If the legislative intention is to preserve the *status quo* in respect of interest rate provisions in housing

50 Cl. 136.
51 Cls 15(7), 85.
52 Cl. 85(4).
53 Robinson, *op. cit.* n. 45, 137.
54 Cl. 87.

loan contracts, then that object appears not to have been achieved. Currently, such provisions are drafted to ensure that they are not struck down by courts as a penalty. This is achieved by making the higher interest rate applicable to the whole of the principal for the term of the loan. A concession is, however, made so that if the borrower is not in default, interest at the lower rate is accepted in lieu of the higher rate.[55] Requiring the credit contract to be drafted so that the higher rate is applicable only in the event of default (as the Code provisions seem to do) would infringe the doctrine of penalties. If it is intended to abrogate that doctrine in this manner, it is highly desirable that the abolition be done expressly.

Payment of interest in advance is not permitted.[56] This extends to housing loan contracts which in an unregulated setting often provide for this.

(c) *Forms of Transaction*

The intention behind the Code seems to be to permit the credit provider and debtor to select any form of credit transaction subject to compliance with disclosure requirements, and not to require them to fit their dealings into particular legislative categories. Currently, a hire purchase agreement falling within the scope of the Credit Act is deemed to be a credit sale contract. The likely rationale behind this was that in the view of the drafters, hire purchase was an intrinsically artificial transaction invented to overcome the bills of sale legislation and buyer in possession rules, and would wither into disuse if a more straightforward form was readily available. Unfortunately, hire purchase has been effectively prohibited because of the impossibility of drafting a complying document. Similarly, leases where there is an implied right of the lessee to purchase the goods are deemed to be credit sale contracts, with similar results. By contrast it is provided that 'for the purposes of [the] Code', goods leases with an option to purchase are 'to be regarded as' a sale of goods by instalments.[57] Part 10 deals separately with consumer leases. No element of deeming is involved and the disclosure and other requirements of the Code would seem to allow the documentation of lease and hire purchase.

(d) *Generally*

Many provisions derived from the Credit Act have been carried over into the Code, but have been revised and streamlined. One example is the sections dealing with variation of credit contracts.[58] All provisions relating to variation, including relief on the grounds of hardship or reopening unjust transactions have been collected together in Part 6. The intractable prob-

55 *Astley v. Weldon* (1801) 2 Bos & Pul 346; 126 E.R. 1318; *Protector Endowment Loan & Annuity Co. v. Grice* (1880) 5 Q.B.D. 592, described as a 'long-standing anomaly': see Duggan, Begg and Lanyon, *op. cit.* n. 9, 634.

56 Cl. 26(1).

57 Cl. 10.

58 See Lanyon, E., 'Variation of Credit Contracts' in *Credit Law 1992* (1992) Vol. II, 209.

lems of the current provisions have been solved by focussing on the two modes, namely unilateral and consensual variation, rather than the purpose of variation. Interest rate variations are dealt with separately. Instead of a detailed prescription as to the contents of the variation agreement, the sections require the credit provider to give the debtor written notice of the actual variation and 'the way in which the variation affects the obligations of the other party'.[59] There are straightforward guidelines as to when variation is not permitted and when new contracts must be entered into. Parties may also choose instead to consolidate agreements or to redocument.

Hopefully the recent changes of government will not mean that serious consideration of the Code is deferred. It contains too much that is of value to become a weapon in the political combat. To the extent that it has deficiencies, it requires careful appraisal so that the sins of its predecessors are not visited upon it.

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59 Cls 84, 85.

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