

ACCESS TO CONSUMER CREDIT: THE PROBLEM OF FINANCIAL EXCLUSION IN AUSTRALIA AND THE CURRENT REGULATORY FRAMEWORK

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I INTRODUCTION

Many financial services, including the provision of short-term credit, have been acknowledged as essential services.¹ Exclusion from such services can be described as 'financial exclusion', which can itself lead to 'social exclusion', in the sense of being denied full participation in society. This article explores the term 'financial exclusion' in the Australian context and considers the extent to which the current regulatory structure for financial institutions in Australia assists in addressing it.

In Part II we describe the nature of financial exclusion in Australia, including the extent of exclusion, its causes and its consequences. We focus particularly on the consumer credit market. In Australia, there are not large groups of people who would be regarded as 'unbanked' with no engagement with the financial system whatsoever, as has been found to be the case in the UK. Financial exclusion in the Australian context can therefore best be defined in terms of lack of access to mainstream financial services. Those excluded from mainstream financial services may turn to alternative service providers, being either 'fringe' credit providers or the community sector. Organisations within the community sector offer fair financial products to those who cannot access the mainstream market; however, they are able to do so only on a limited scale. The financial products offered in the fringe market tend to be expensive and have been described as exploitative and 'unsafe'. While some mainstream institutions have started to extend their services to those previously excluded from mainstream short-term credit services, these pilot schemes have not been sufficient in terms of size or geography to satisfy the potential demand.

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¹ See eg Office of Fair Trading (UK), *Vulnerable Consumers and Financial Services: the Report of the Director-General's Inquiry OFT255* (1999) 19.

Part III begins by considering the shortcomings of consumer protection theory that emphasises competitive markets and disclosure regulation. The resulting legislation is ineffective to discourage financial exclusion. There is no competition to provide services for the financially excluded, who may be regarded as too great a risk by mainstream service providers. Requiring the disclosure of fees and charges to borrowers with no alternative but to pay exorbitant charges and interest for a loan is likely to have little or no impact upon their decision to proceed with the loan. This is exemplified by the growth of the fringe credit market. We consider whether it would be possible to regulate fringe credit providers to provide loans on reasonable and fair terms, but suggest that the reliance on disclosure regulation in relation to fringe credit is an inadequate regulatory response and that 'command and control' models of regulation are likely to be necessary in regulating the fringe sector.

In Part IV we consider the ways in which the current regulatory structure for financial institutions in Australia hinders financial institutions from addressing financial exclusion. Firstly, we note that in Australia credit unions are regulated as if they were banks, ignoring their mutual natures and their potential to contribute to tackling financial exclusion by offering access to affordable loans to their members. This can be compared with the exemption from banking regulation granted to credit unions in the UK. Secondly, we argue that the work of community organisations which might potentially infringe current prudential regulation needs to be carefully considered, and afforded its own specific regulatory framework. Where organisations are concerned to provide loans for social purposes, and have demonstrated that by their conduct, a less interventionist regulatory response is called for, consistent with the regulatory strategy outlined as part of Ayres and Braithwaite's enforcement pyramid.² Finally, we argue that corporate mainstream financial institutions such as banks are limited in their ability to address financial exclusion, by the corporate law duties on directors to maximise the return of profits to shareholders. In this respect we question the effectiveness of voluntary corporate social responsibility as a regulatory measure.

II FINANCIAL EXCLUSION IN AUSTRALIA

A *Defining Financial Exclusion in Australia*

The term 'financial exclusion' has been in use since the early to mid-1990s, most widely in the government and community sectors in the UK, and has been closely linked to discussions on addressing poverty and social exclusion. For example, Chant Link and Associates note that '[f]inancial exclusion may be either a cause or a consequence of social exclusion, or both'.³

² See generally Ian Ayres and John Braithwaite, *Responsive Regulation: Transcending the Deregulation Debate* (1992).

³ Chant Link and Associates, *A Report on Financial Exclusion in Australia*, November (2004) 36, <http://www.anz.com/aus/aboutanz/community/programs/pdf/Financial_Exclusion-FinalReport.pdf> at 20 June 2005.

There is no commonly agreed definition of financial exclusion. Some commentators take a very broad approach - for example, seeing financial exclusion as 'processes that prevent poor and disadvantaged social groups from gaining access to the financial system'.⁴ Other definitions are more specific, and focus on access (or lack of access) to specific products or services.

To date, most definitions have originated from the UK, in a context where past studies have shown that a small, but significant, proportion of consumers have no engagement with the financial system.⁵ These consumers are the 'unbanked', and do not have even a basic savings/transactions account. In Australia, however, there is not the same level of complete disengagement from the financial system. Data from 2003 suggests that only 0.8% of the adult population owned no financial products, and 6% owned only a transaction product and no other financial products.⁶ Definitions developed in the UK are therefore less applicable in Australia.

Instead, financial exclusion in the Australian credit market can be best understood by focusing on a lack of access to the mainstream market (including products offered by banks), with its stronger regulatory framework, more established and reputation conscious players, and (in general) cheaper products and services. Those who cannot access the mainstream market are driven towards the credit products offered in the fringe market (for profit) and the community/informal 'market'⁷ (not for profit). Unfortunately, the reach of the community/informal market is very small, and most financially excluded consumers will find themselves resorting to the high cost and arguably exploitative products available in the fringe market. Applying this approach, Chant Link and Associates have suggested that financial exclusion in Australia is 'the lack of access by certain consumers to appropriate low cost, fair and safe financial products and services from mainstream providers'.⁸ In this definition, it is not simply exclusion from the mainstream market that is of concern; elements of appropriateness, low cost, fairness and safety of products are also incorporated. As we discuss later in this article, these elements are not ones that fit easily into the dominant theoretical approach to consumer protection regulation in Australia.

Financial exclusion is not necessarily absolute, and can be temporary or more permanent.⁹ In certain circumstances, and in the absence of interventions,

⁴ Ibid 29; see also Chris Connolly and Khaldoun Hajaj, *Financial Services and Social Exclusion* (2001) 8.

⁵ Financial Services Authority (UK), *In or Out? Financial Exclusion: a Literature and Research Review*, Consumer Research Report 3 (2000) 21.

⁶ Chant Link and Associates, above n 3, 120.

⁷ Of course, the community / informal sector is not a market in the commonly understood sense of the word, as the products are offered on a not for profit basis, and the schemes are based on cooperation, not competition and commercialisation.

⁸ Chant Link and Associates, above n 3, 58.

⁹ Chant Link and Associates, above n 3, 83; Connolly and Hajaj, above n 4, 9.

consumers with low levels of exclusion can be drawn into deeper levels of exclusion.¹⁰

B *Why is Financial Exclusion of Concern?*

Increasingly, there is recognition that some products and services are 'essential' to participation in social and economic life in developed economies, and that failure to ensure access to these services can have significant consequences for individuals and the broader community. This notion is most widely accepted in the case of utility services - including energy, water, and telecommunications. In these sectors, governments in Australia and elsewhere have imposed universal service obligations, retailer of last resort arrangements, pricing controls and/or other regulatory controls to ensure that all members of the community are able to access the minimum level of service necessary for full participation.¹¹

Given the centrality of financial services to developed economies like Australia, we argue that at least some financial services should also be seen as 'essential services'. There is commentary from the UK to the effect that these essential financial services include, amongst other things, access to cash transmission and banking services, as well as short-term consumer credit to cover emergencies and smooth out the cost of large purchases.¹²

As we explained above, financial exclusion results where consumers cannot access these essential services from the mainstream market. The consequences can be costly, and can create or prolong financial hardship.¹³ Connolly and Hajaj have noted that '[t]he options for operating a household budget without mainstream financial services are more expensive, often unregulated and very limiting'.¹⁴

For consumers on low incomes, the high cost of credit in the fringe market can in fact impede their ability to overcome financial difficulties, and can deplete their income and ability to save. The structure of some short-term loans (particularly payday loans) are such that in many cases the borrower will not be able to repay the loan at the end of the term, and will 'roll-over' the loan, thus incurring additional fees and costs.¹⁵ The use of high-cost loans can also send consumers further into

¹⁰ Chant Link and Associates, above n 3, 63.

¹¹ For example, in Queensland, the provision of electricity to residential customers is subject to an obligation to supply, standard customer contracts and price controls. *Electricity Act 1994* (Qld) ss 49, 50.

¹² Office of Fair Trading (UK), above n 1, 19.

¹³ Chant Link and Associates, above n 3, 93. See also Financial Services Authority (UK), above n 5, 56, for discussion of the consequences of exclusion.

¹⁴ Connolly and Hajaj, above n 4, 8.

¹⁵ For example, in a 2002 survey Wilson found that 65% of payday lending customers had taken out more than one loan and that the average number of repeat loans taken out by consumers was 6 loans over 12 months: Dean Wilson, *Payday Lending in Victoria – a Research Report*, for Consumer Law Centre Victoria Ltd (2002) 65, available from <<http://www.clc.v.net.au>> at 20 June 2005.

debt spirals from which it becomes difficult to escape: as more and more income is used to pay high interest, fees and charges, the likelihood of default increases, and the consumer will become further excluded from the mainstream market.¹⁶ Bankruptcy, and its attendant individual and social consequences, can become an end result.¹⁷

Credit from the fringe market can also have a broader social impact. Over-indebted consumers on low incomes can place strains on government, community and welfare services, as emergency relief is sought to meet the basic living expenses that cannot otherwise be met because income is tied up in debt repayment. Other costs are imposed on government and community services to provide income support, administer bankruptcy and court processes, and/or to respond to the adverse health impacts arising from financial exclusion. In addition,

The money a household spends servicing high-cost debt in the second-tier marketplace is not available for spending at the neighbourhood grocery stores, service stations, pharmacies, or other local businesses.¹⁸

Financial exclusion therefore merits a strong legal, policy and government response.

C *The Extent and Causes of Financial Exclusion*

Despite its importance, there are no accurate estimates of the extent of financial exclusion in Australia. Unless a product ownership analysis is used whereby the level of financial exclusion is measured in terms of 'the proportion of the population lacking ownership of any (or many) financial products',¹⁹ levels of financial exclusion are difficult to measure. However, even a product ownership approach to measuring financial exclusion is not sufficient where the definition of financial exclusion includes gradations and focuses on access to 'appropriate low-cost, fair and safe products'. In this definition, we need to make some value judgments about whether particular products are low-cost, fair and safe,²⁰ and a broad-brush product ownership analysis cannot do this.

The product analysis approach is even more limiting when considering financial exclusion in consumer credit. Firstly, there is little data available on ownership of fringe credit products.²¹ Secondly, the conclusions that can be drawn from high or

¹⁶ Lynn Drysdale and Kathleen E Keest, 'The Two-Tiered Consumer Financial Services Marketplace: the Fringe Banking System and its Challenge to Current Thinking about the Role of Usury Laws in Today's Society' (2000) 51 *South Carolina Law Review* 589, 663.

¹⁷ 'Excessive use of credit' was the second most common self-reported cause on non-business bankruptcies in 2003: Insolvency and Trustee Service Australia, *Profile of Debtors 2003* (2004) 10.

¹⁸ Drysdale and Keest, above n 16, 664.

¹⁹ This was the approach taken in the research by Chant Link and Associates, above n 3, 120.

²⁰ Chant Link and Associates, above n 3, 145.

²¹ Chant Link and Associates, above n 3, 135.

low levels of credit product ownership are not immediately obvious. As the UK Financial Services Authority has noted: '[m]easuring the number of people who are excluded from credit facilities is difficult, as not everyone without credit wants or needs it'.²² Thirdly, the demand for consumer credit is frequently unavoidable for many vulnerable, low-income consumers, but it can also raise concerns about the risk of over-indebtedness.²³ This relationship between overcoming financial exclusion and reducing over indebtedness can be difficult to resolve.

While we cannot definitively assess the extent of financial exclusion, many community and consumer advocates are concerned that levels of financial exclusion are rising,²⁴ and see consumer credit as the area most in need of attention.²⁵

Reflecting the complexities of this issue of financial exclusion, there is a range of commercial and personal factors that drive or cause financial exclusion in consumer credit.

From a commercial perspective, mainstream institutions have become increasingly reluctant to provide consumer credit services to low-income and vulnerable consumers, or to consumers with poor credit records. In part, this appears to be driven by a concern that these customers are high-risk, and more likely to default on loans. However, we might question these assumptions in the light of the repayment rates of this same customer group when using community-based no-interest loan schemes.²⁶

Some commentators have suggested that many low-income consumers are seeking loans for relatively small amounts, with fixed (affordable) rates and a relatively short time frame for repayment.²⁷ These are precisely the type of loans that are available in the community/informal sector. Minus the characteristic of affordability, they are also the type of loans available in the fringe market. However, mainstream providers have largely withdrawn small loans from the market, perhaps because they are not as profitable as other products,²⁸ and most

²² Financial Services Authority (UK) above n 5, 41.

²³ Peter Cartwright, *Banks, Consumers and Regulation* (2004) 228.

²⁴ Chant Link and Associates, above n 3, 82.

²⁵ The most needed services or financial exclusion issues were considered to be access to small personal loans, financial counselling (especially on credit/debt management) and access to fairer, safer major credit cards: Chant Link and Associates, above n 3, 107.

²⁶ Australia Street Company Review of No Interests Loan Schemes (1999) commissioned by the NSW Department of Fair Trading, 14, suggests 80-95% of loans are repaid in full. One consumer advocate has suggested that, with more recent access to Centrepay system, some schemes regularly show repayment rates of more than 90%: email from David Tennant to Nicola Howell, 8 July 2005.

²⁷ Wilson, above n 15, 80-1. See also Sue Lott and Michael Grant, *Fringe Lending and 'Alternative Banking: the Consumer Experience* (2002), available from <<http://www.piac.ca>>, which refers to a preference for 'highly structured forms of short term cash': 49.

²⁸ Financial Services Authority, above n 5, 17-18.

now have minimum loan amounts of between \$1,000 and \$5,000.²⁹ Those requesting small loans are directed to credit cards and other sources of open-ended credit.³⁰ These products entail their own risks,³¹ and some low-income consumers appear to be wary of using them.³²

Mainstream providers also fail to meet the service needs and preferences of low income and vulnerable consumers. For example, studies have suggested that fringe lending customers appreciate the friendlier, more welcoming and respectful service of these lenders compared to mainstream institutions,³³ and that mainstream providers have been unable (or unwilling) to meet preferences of fringe lending customers for greater speed and accessibility of services (ie longer opening hours, street access, face-to-face service) of services.³⁴ Interestingly, Ramsay has suggested that fringe lenders often cultivate 'fictive friendships' in order to reduce the likelihood of the customer shopping around for a cheaper product.³⁵

Also relevant is the increasing reliance by mainstream providers on automated credit scoring systems, which cannot take account of individual circumstances or explanations for defaults. In contrast, fringe lenders may be prepared to take a more flexible approach to credit histories, and some prominently advertise that poor credit reports or previous bankruptcies will not be a barrier to loan approval.³⁶

One of the most frequently mentioned individual drivers of financial exclusion is low income or poverty,³⁷ and there is clearly a circularity of cause and effect between financial exclusion and financial hardship or poverty. Having a low income facilitates the need for consumer credit, as 'households on very tight budgets are among those most likely to need to borrow, being less likely to have savings safety nets in a case of emergency or to be in a position to save towards

²⁹ See Cannex, *Selected Personal Loans – Unsecured* <<http://www.cannex.com.au/surveys/perunsec.htm>> at 20 June 2005.

³⁰ Iain Ramsay, *Access to Credit in the Alternative Consumer Credit Market* (paper prepared for: Office of Consumer Affairs, Industry Canada, and Ministry of the Attorney General, British Columbia, 2000) 2, <[http://cmcweb.ca/epic/internet/incmc-cmc.nsf/vwapj/ramsay_e.pdf/\\$FILE/ramsay_e.pdf](http://cmcweb.ca/epic/internet/incmc-cmc.nsf/vwapj/ramsay_e.pdf/$FILE/ramsay_e.pdf)> at 20 June 2005.

³¹ One study suggests that, because of their structure, mainstream products can be more costly than fringe products, which better reflect typical repayment patterns of low-income consumers: Department of Trade and Industry (UK), *The Effect of Interest Rate Controls in Other Countries* (2004) 28, <<http://www.dti.gov.uk>> at 20 June 2005.

³² Wilson, above n 15, 80.

³³ Ramsay, above n 30, 18; Lott and Grant, above n 27, 46; Wilson, above n 15, 76.

³⁴ Willis suggests, 'no money down and a quick decision were more frequently cited by subprime borrowers than by borrowers overall as reasons for choosing a particular lender or broker'- Lauren E Willis 'Decisionmaking and the Limits of Disclosure: the Problem of Predatory Lending' (Legal Studies Paper No 2005-14, Loyola Law School, June 2005) 23.

³⁵ Ramsay, above n 30, 18.

³⁶ One lender advertises: 'Loans for any purpose even if you ... have no financials, have a bad credit history or are ex-bankrupt, have arrears or defaults ...' and 'Decisions in ten minutes (in principle)': *Yellow Pages Brisbane 2005*, 1038. Similar advertisements abound in the local and regional newspapers across Australia.

³⁷ Chant Link and Associates, above n 3.

essential services'.³⁸ However, having a low income also means that mainstream lenders are reluctant to provide finance. Other related factors linked to financial exclusion are said to include employment status and housing tenure.³⁹

Evidence that most customers of fringe lenders and community organisations primarily use credit to meet daily living expenses, pay bills and cover emergency costs⁴⁰ suggests that credit plays a role in smoothing out expenses and/or compensating for inadequate incomes. Broader measures to reduce poverty are clearly critical in addressing financial exclusion; however, analysis of any reform that is needed is beyond the scope of this article.

III THE SHORTCOMINGS OF DOMINANT CONSUMER PROTECTION THEORY IN THE CONTEXT OF FINANCIAL EXCLUSION

A Consumer Protection Theory

There are a number of different rationales or theories for consumer protection regulation and, in this Part, we explore how the dominant consumer protection ideology behind consumer protection regulation in Australia has produced legislation that has little or no capacity to discourage financial exclusion. An exposition of the range of theories and models for intervention on consumer protection grounds is outside the scope of this paper. However, some of the key ideas are outlined. For example, Duggan refers to consumer protection measures being applicable to one or more of the following values: welfare considerations, equity considerations and 'paternalism'.⁴¹ In a later paper, he suggests that various consumer protection initiatives can be understood as reflecting economic efficiency considerations, loss distribution considerations and/or paternalistic concerns.⁴² Howells suggests that there are broadly three consumer protection rationales for intervention into 'the foundational ideology of contract law' - that is, freedom of contract⁴³ - and these are: promoting competition, achieving individual justice and realising social justice.⁴⁴ And, in their development of 'information-based principles' for consumer protection policy, Hadfield et al focus on an economic conception of the objectives of consumer protection.⁴⁵ In contrast, Ramsay talks of a 'third way' approach to consumer credit regulation, that both recognises the importance of the market, and of empowering consumers within that market, and

³⁸ Office of Fair Trading (UK), above n 1, 10.

³⁹ James F Devlin, 'A Detailed Study of Financial Exclusion in the UK' (2005) 28 *Journal of Consumer Policy* 75, 96-7.

⁴⁰ Wilson, above n 15, 66-7; Lott and Grant, above n 27, 41-2.

⁴¹ Anthony Duggan, 'Some Reflections on Consumer Protection and the Law Reform Process' (1991) 17 *Monash University Law Review* 252, 254.

⁴² Anthony Duggan, 'Saying Nothing with Words' (1997) 20 *Journal of Consumer Policy* 69, 73.

⁴³ Geraint G Howells, 'Contract Law: the Challenge for the Critical Consumer Lawyer' in Thomas Wilhelmsson (ed), *Perspectives of Critical Contract Law* (1993) 327, 331.

⁴⁴ *Ibid* 335.

⁴⁵ Gillian K Hadfield, Robert Howse and Michael J Trebilcock, 'Information-Based Principles for Rethinking Consumer Protection Policy' (1998) 21 *Journal of Consumer Policy* 131, 132.

also focuses on the relevance of social policy in achieving goals that cannot be met relying on the market alone.⁴⁶

In Australia also, there is a mix of ideologies and models behind consumer protection initiatives, and it has been argued that the policy objectives for interventions are often inconsistent.⁴⁷ However, in recent years, the dominant approach has been to provide consumer protection by promoting competition and eliminating market failures. As Bourgoignie explains:

The usual rhetoric in consumer law and policy has as its foremost aim to enable the consumer to fully play his [sic] role in the economic market, assigning to him [sic] adequate opportunities for choice and negotiation. *The predominant conception is therefore integrative; it continues to be based on the illusion of the effective sovereignty of the consumer in the market.*⁴⁸

In this approach, the understanding is that vigorous competition between traders will promote and protect the interests of consumers. Informed consumers will shun traders that overcharge, or provide poor quality or service, and transfer their purchasing power to those traders offering competitive pricing, quality and service. In this way, consumers will activate the competitive process.⁴⁹ Rivalry between traders ‘generally provides incentives for least cost production and for prices to mirror costs’,⁵⁰ to the ultimate benefit of consumers.

This competition and market-based approach to consumer protection is reflected in current government policies and pronouncements. For example, in a recent speech, the Parliamentary Secretary to the Treasurer, whose portfolio includes consumer protection, noted:

the way I see it, the future direction for Australian consumers must be based on two important principles. Number one – we have to ensure that real benefits flow to Australian consumers from a competitive market. And, two – we have to understand the vital role that confident consumers play in actually making the benefits of competition real and tangible.⁵¹

⁴⁶ Iain Ramsay, ‘Consumer Credit Regulation as “The Third Way”?’ (speech delivered at the Australian Credit at the Crossroads Conference, Melbourne, Australia, 8 November 2004) 5.

⁴⁷ See eg Duggan, above n 42, 77-79.

⁴⁸ Thierry Bourgoignie, ‘Characteristics of Consumer Law’ (1992) 14 *Journal of Consumer Policy* 293, 303 (emphasis in original).

⁴⁹ See eg Louise Sylvan, ‘A Global View of Consumer Issues: Then and Now’ (speech delivered at the American Council on Consumer Interests 50th Anniversary Conference, 1 April 2004, Washington, USA) 7; and Louise Sylvan, ‘Activating Competition: the Consumer – Competition Interface’ (2004) 12 *Competition and Consumer Law Journal* 191.

⁵⁰ Productivity Commission, *Review of National Competition Policy Reforms Inquiry Report No 33* (2005) 54.

⁵¹ Hon Chris Pearce, MP, ‘Opening Address to Consumer Representatives’ Forum’ (speech delivered at the Consumer Representatives’ Forum, Melbourne, Australia, 15 June 2005), <<http://parlsec.treasurer.gov.au/cjp/content/speeches/2005/010.asp>> at 22 July 2005. See also Department of Industry Science and Tourism, *Codes of Conduct Policy Framework* (1998) 9: ‘In deciding the most appropriate method of achieving a [consumer protection] objective, the

The focus on competition to provide consumer benefits and consumer protection has also resulted in a heavy reliance on disclosure initiatives to protect consumers.⁵² This is evident in the consumer credit sector, where the *Uniform Consumer Credit Code* (UCCC) sets out a detailed framework for disclosing information about prices, terms and conditions.⁵³ To a large extent, providers can structure and price their products as they like, as long as the disclosure requirements in the UCCC are met.

However, a focus on facilitating competition and information disclosure does not address issues of financial exclusion. As we discussed above, financially excluded consumers are not seen as attractive by mainstream lenders and, in this context, no amount of competition will induce lenders to meet their needs. Excluding the application of discrimination laws, there are no legal or other obligations imposed on mainstream lenders to provide services to any individual consumer, and governments have been reluctant to impose such an obligation. For example, efforts to seek government support for legislative requirements upon banks to provide a basic banking account for low income and vulnerable consumers were unsuccessful⁵⁴; although, interestingly, many institutions have now introduced such an account.

Relying on well-informed consumers choosing between various product offerings in the market to address the issues of financial exclusion is also problematic. Studies have suggested borrowers of fringe lenders do not fully appreciate the costs of the credit⁵⁵ and do little or no shopping around between different lenders.⁵⁶ There is little price advertising by fringe lenders in Australia and, as far as we are aware, no external sources providing comparison information for the majority of fringe lending products in Australia.⁵⁷ Customers of fringe lenders rarely discover the cost

general approach that the Government will take ... is that the market generally produces better results, including greater choice and lower prices for consumers.'

⁵² Hadfield et al, above n 45, 134. These authors criticise the simplistic application of an informed consumer approach – and refer to 'the paradox of attempting to use costly information procedures ... to solve the problems created by the cost of being informed': 141.

⁵³ *Consumer Credit Code* s 15 (matters that must be disclosed in contract document).

⁵⁴ For example, none of the recent enquiries into the banking or financial services system recommended that institutions be required to provide a basic banking account, or that banking be considered to be an essential service: Connolly and Hajaj, above n 4, 6-7. See also, for a summary of developments in this area, W S Weerasooria, *Banking Law and the Financial System in Australia* (5th ed 2000) 59-66.

⁵⁵ Lott and Grant, above n 27, 44; Wilson, above n 15, 77. Willis suggests that many consumers reduce the number of attributes that they consider to a very small number, perhaps only the monthly repayment: Willis, above n 34, 19-20.

⁵⁶ Willis, above n 34, 21, suggests that many customers of fringe lenders choose a price ceiling, and accept the first loan that they are offered under that ceiling.

⁵⁷ Cannex, the major collator of price information, does include information about some fringe home loans (see Cannex, *Selected Specialist Lending* at <<http://www.cannex.com.au/surveys.html>>, 28 July 2005) but does not include smaller loans from fringe lenders. In the Canadian context, Ramsay, above n 46, 19, also notes that there is less reliable third party information on alternatives to mainstream products.

of credit until they are at the point of sale and, by this time, they are likely to have psychologically committed to the transaction and are unlikely to take away this price information to compare with another lender. This tendency is compounded if the borrower is under pressure to obtain finance and/or feels that no other lender will assist, as is the case for many financially excluded consumers.⁵⁸

In addition, a competitive market potentially creates risks for vulnerable or disadvantaged consumers in particular. For example, a market that is fully competitive from a classical economic perspective is one that has 'low barriers to entry, low sunk costs, many rivals, and rapid rates of entry and exit'.⁵⁹ However, the ease of entry and exit can also facilitate the emergence of unscrupulous operators, as has happened in the credit market.

Finally, beyond the prohibition against unjust transactions⁶⁰ and some provisions dealing with the terms of credit contracts,⁶¹ competition models and the UCCC do not impose any obligations to provide credit products that are both fair and safe for potential borrowers. Without these characteristics, financial exclusion cannot be adequately addressed.

Despite a heavy focus on competition and competitive markets to provide outcomes for consumers, some Australian States and Territories have retained controls on the cost of credit through prescribing maximum interest rates for consumer loans.⁶² In theory, such mechanisms should force out the very high-cost products from the market, but they do not make excluded consumers any more attractive to mainstream lenders. Critics of interest rate caps also suggest that they in fact harm, rather than protect, low-income and vulnerable consumers.⁶³ In addition, interest rate caps can be easily avoided, by loading additional costs into the largely unregulated additional fees and charges.⁶⁴

⁵⁸ For an extensive analysis of the reality of consumer decision making in the context of home loans, see Willis, above n 34.

⁵⁹ Hadfield *et al*, above n 45, 153.

⁶⁰ *Consumer Credit Code* s 70.

⁶¹ *Consumer Credit Code* s 24 (accepting early payments), s 80 (requirements to be met before enforcing a credit contract), s 82 (requirements to be met before enforcing a guarantee), s 83 (requirements to be met before repossessing secured goods).

⁶² *Consumer Credit (New South Wales) Special Provisions Regulation 2002* (NSW) reg 7.

⁶³ Thomas A Durkin, 'An Economic Perspective on Interest Rate Limitations' (1993) 9 *Georgia State University Law Review* 821, 825; Kathleen C Engel and Patricia A McCoy, 'A Tale of Three Markets: the Law and Economics of Predatory Lending' (2002) 80 *Texas Law Review* 1255, 1313.

⁶⁴ In NSW, for short-term contracts only, fees and charges are included for the purposes of calculating the maximum annual percentage rate: *Consumer Credit (New South Wales) Act 1994* (NSW) s 11(1A); *Consumer Credit (New South Wales) Special Provisions Regulation 2002* (NSW), reg 8(1). The NSW Government has released exposure draft legislation that would apply this requirement to all consumer credit contracts: *Consumer Credit (New South Wales) Amendment (Maximum Annual Percentage Rate) Bill 2005*.

In Australia, there is no regulator or government agency with responsibility for ensuring access to financial services or for addressing financial exclusion, and governments do not seem to have acknowledged the essential nature of financial services. However, in its recently announced review of consumer credit, the Victorian government has committed to working with credit providers to 'improve access to affordable finance for disadvantaged groups', and the review issues paper suggests that the government will take seriously any potential solutions that might encourage mainstream lenders to provide affordable microfinance and thus reduce financial exclusion.⁶⁵

B *The Application of Consumer Protection Theory to Fringe Credit*

One clear example of the inadequacy of disclosure regulation as a form of consumer protection is the attempt to regulate fringe credit providers simply by bringing them within the jurisdiction of the UCCC. Before 2001, many fringe lenders had not been regulated under the UCCC, which did not apply to loans for periods of less than 62 days. Under the 2001 amendments⁶⁶ the 62 day threshold still applies, but only where fees and charges do not exceed 5% of the loan amount and the interest rate does not exceed 24% per annum.⁶⁷ This means that most fringe loans will be subject to the disclosure provisions of the UCCC. As we have argued, however, this form of 'disclosure regulation'⁶⁸ will be ineffective given the evidence that vulnerable consumers do not regard themselves as having any choice but to borrow at high interest rates.⁶⁹ The current regulatory focus on disclosure requirements in protecting consumers who access credit through fringe lenders seems misconceived, given that low-income earners without real choice are unlikely to be influenced by the fees and charges disclosed in accepting a loan offer.⁷⁰ It has been noted in relation to disclosure regulation generally that

the risks associated with some products or activities may be so great that policy-makers may feel that it is inappropriate merely to inform affected parties about those matters and command and control methods may be deemed necessary.⁷¹

These comments would seem particularly applicable to fringe credit.

⁶⁵ Consumer Affairs Victoria, *Consumer Credit Review: Issues Paper* (2005) 14, <www.consumer.vic.gov.au>, at 20 June 2005.

⁶⁶ *Consumer Credit (Queensland) Amendment Act* 2001 (Qld).

⁶⁷ UCCC s 7(1).

⁶⁸ A term used by Robert Baldwin and Martin Cave, *Understanding Regulation: Theory, Strategy and Practice* (1999) 50, to mean regulation which requires the disclosure of information to consumers so as to allow consumers to make informed decisions on products.

⁶⁹ Justin Malbon, *Taking Credit: a Survey of Consumer Behaviour in the Australian Consumer Credit Market* (1999) (a report undertaken for the Consumer Credit Code Post Implementation Review Committee on behalf of the Ministerial Council on Consumer Affairs).

⁷⁰ See discussion on this point in Therese Wilson, 'The Inadequacy of the Current Regulatory Response to Payday Lending' (2004) 32 *Australian Business Law Review* 193, 197-8.

⁷¹ Baldwin and Cave, above n 68, 49.

Further in relation to the inadequacy of the current regulatory response, the ability of borrowers to apply under the UCCC⁷² to reopen unjust transactions or review unconscionable or other interest charges is unlikely to assist low-income consumers who will tend not to have the resources nor inclination to bring applications before a court or tribunal.⁷³

In terms of an appropriate regulatory response, the ‘conduct’ of this industry must lead us to conclude that models of self-regulation or enforced self-regulation would not be adequate. As noted in a report to the Queensland Minister for Fair Trading in 2000, voluntary codes of conduct rely on there being a strong industry body, peer pressure from participants within the industry and a fear of ostracism from the industry body. In relation to payday lenders it was noted that

Each market participant seemed to be interested only in ensuring the growth and strength of its own organisation, as is normal in fledgling industries, with little consideration of its fellow market participants.⁷⁴

‘Command and control’ models of regulation through legislation imposing strict penalties for exploitative lending practices, whilst perhaps also providing incentives for providing financial products to low-income consumers at reasonable rates and on reasonable repayment terms, should be considered.

Further research will be required to answer the question as to whether fringe credit providers, such as payday lenders, should be allowed to continue to service low-income consumers, on the basis that regulation could be enacted which would facilitate and require the provision of loans by them on reasonable and fair terms. Their ability to provide such loans profitably seems a crucial question, as is the likelihood of their commitment to lending on fair and non-exploitative terms. Many argue vehemently that there is no place in the market for these lenders, who have been described as exploitative and predatory.⁷⁵ There is no doubt that many low-income consumers who use the services of these lenders find themselves in a ‘debt spiral’ from which it can be impossible to escape. Nevertheless, fringe credit providers seem to provide a service which is in demand and which has captured a market, in the absence of any current viable alternative. In considering the role of fringe credit providers in addressing financial exclusion, a determination needs to be made as to whether these credit providers are capable of assisting to address financial exclusion under an appropriate regulatory structure, or whether they can only exacerbate the problem. If the latter is the case, then a regulatory ban would seem to be the only feasible option.

⁷² *Consumer Credit Code* ss 70(1)-(2), 72.

⁷³ See discussion in Hazel Genn, *Paths to Justice: What People Do and Think About Going to Law* (1999) 101, 160.

⁷⁴ Queensland Office of Fair Trading, *Payday Lending – a Report to the Minister for Fair Trading* (2000) 21.

⁷⁵ See for example Charles Brusch, ‘Taking the Pay out of Payday Loans: Putting an End to the Usurious and Unconscionable Interest Rates Charges by Payday Lenders’ (2001) 69 *University of Cincinnati Law Review* 1257, 1280.

IV FINANCIAL REGULATION

A *Regulatory Limits on the Role of Credit Unions*

Historically, credit unions have been the perfect vehicle for solving the needs of a community for affordable finance. The union was formed, and members pooled their savings and were able to borrow from the pool at affordable rates. The credit unions were established as mutual organisations in the sense of being owned by those who saved with and borrowed from them. Many credit unions have now succumbed to what has been termed the ‘demutualisation feeding frenzy’⁷⁶ whereby the credit unions cease to be member-owned mutual organisations and members’ interests convert to shares in a proprietary limited company. Further, the current regulatory environment is said to hinder the establishment of new credit unions at grass roots levels, and to prevent existing credit unions from performing their traditional roles as providers of affordable credit within communities. Race Mathews argues that

What is needed is a recognition from government - preferably explicit - that credit unionism is about enabling ordinary people and communities to engage in self-help, and thereby is entitled to special consideration ... This means getting rid as much as possible of the statutory and regulatory requirements which are blocking the establishment of new credit unions, cramping the development of current credit unions or inhibiting them from striking out in new directions in response to new needs, and obliging communities which have been deserted by the major commercial banks to establish community banks as a second-best substitute for credit unions.⁷⁷

This has been well-articulated and accepted in the UK, where the Department of Trade and Industry has suggested that one way of minimising the problem of over-indebtedness is to ensure that low-income consumers have access to affordable credit and that credit unions have a role to play in this. The Department recognises that ‘the credit union ethos of thrift, financial planning and self-help, together with their ability to offer access to affordable loans, means they are well placed to make an important contribution to tackling financial exclusion’.⁷⁸

In the UK, therefore, credit unions have been granted an exemption from the Banking Directives and the UK Banking Acts, notwithstanding that they are able to accept deposits. This has been described as a ‘significant exception and entirely

⁷⁶ R Mathews, ‘A Future or No Future: Credit Unions in a Globalising Economy’ (2003) (speech delivered at the 41st Annual Conference of the New Zealand Association of Credit Unions, Hamilton, NZ, 12 September 2003) 1, <http://www.australia.ccop/race_mathews.htm> at 17 June 2005.

⁷⁷ R Mathews, ‘Mutualist Options for Regional Economic Development and Empowerment: the Mondragon and Desjardins Cases’ (2001) 10, <http://www.brisinst.org.au/papers/mathews_race_mutualism/print.html> at 15 June 2005.

⁷⁸ Department of Trade and Industry (UK), *Fair, Clear and Competitive: the Consumer Credit Market in the 21st Century* (2003) 87.

justified since credit unions offer competition to banks in savings and credit, particularly (but not exclusively) in savings and credit for social purposes'.⁷⁹

It is notable that in Australia, since the enactment of the *Australian Financial Institutions Commission Act 1992*, only three new credit unions have formed.⁸⁰ One of these is an example of the good that can be achieved within communities by the establishment of a credit union. The Traditional Credit Union, which was incorporated in December 1994, with branches in remote parts of Australia, serves a membership comprised predominantly of Indigenous people on low incomes. Its services include savings, budget and Christmas club accounts, clan accounts for joint saving, personal loans of up to \$10,000 and small business loans of up to \$15,000.⁸¹

The problem in Australia with respect to regulation of credit unions seems to be a failure to recognise the differences between credit unions and banks, treating credit unions for regulatory purposes as if they are banks.⁸² It is argued that, by imposing the same capital adequacy requirements on credit unions, the potential for them to form and grow is lost, and management is required to focus upon financial targets which are not necessarily consistent with the mutual goals of credit unions.⁸³ The mutual nature of credit unions has been largely ignored by regulators.

B *The Contribution of Community Organisations*

The work to facilitate reasonable access to short term credit by low-income consumers being undertaken by mutual societies such as Foresters ANA, and community organisations such as Good Shepherd Youth and Family Services and Brotherhood of St Laurence, could also be expanded upon by removal of certain regulatory hurdles. Foresters ANA, for example, has fostered the development of savings and loans circles in Queensland, whereby small groups of people meet regularly and contribute savings to a pool (often initiated with seed funding from a community organisation), which pool is available to members of the group after a certain period of time in the form of no-interest loans.⁸⁴ Difficulties might arise,

⁷⁹ Udo Reifner, *Micro-Lending - a Case for Regulation: General Report on the Regulation of Credit for Social Purposes by Non-Banks in the EU*, <<http://www.money-advice.net/media.php?id=225>> at 7 July 2005.

⁸⁰ Mathews, n 77, 15.

⁸¹ Bev McMillan, 'Traditional Credit Union Access to Financial Services', <http://www.indigenousforums.nt.gov.au/dcm/indigenous_policy/forums/pdf/Bev%20McMillan.pdf> at 17 June 2005.

⁸² This is reflective of the 'one size fits all' approach apparent in the Wallis report, more correctly referred to as the *Financial Systems Inquiry Final Report 1996*.

⁸³ Bananacoast Community Credit Union Ltd, *Submission to the Inquiry into the Regulation of Australian Financial Institutions*, <<http://fsi.treasury.gov.au/content/downloads/PubSubs/000059.doc>> at 9 July 2005.

⁸⁴ See Foresters ANA web site <<http://www.forestersana.com.au>> at 18 June 2005; and explanation of the savings and loans circles in Ingrid Burkett, *Microfinance in Australia: Current Realities and Future Possibilities* (report financed by the Westpac Foundation, 2003) 38.

however, if an organisation such as Foresters sought to expand on the savings and loans idea and itself administer the collection of savings and the making of loans. It might then be regarded as conducting a deposit-taking business which, pursuant to the *Banking Act 1959* (Cth),⁸⁵ would be regarded as 'banking business' that may only be undertaken by authorised deposit-taking institutions - that is, banks, building societies and credit unions authorised to conduct banking business by the Australian Prudential Regulatory Authority. The same hurdle would be encountered by Good Shepherd Youth and Family Services if it wished to extend its No Interest Loans Scheme⁸⁶ to enable low income consumers who had completed payments on their no-interest loans, to continue to make payments by way of savings to allow for future financial emergencies. The possibility for such initiatives should surely be encouraged not hindered by regulation.

Credit unions, other mutual societies and community organisations have a crucial role to play in addressing the problem of financial exclusion in Australia, and financial regulation needs to be responsive to that, with regulators taking into account 'the conduct of those they seek to regulate in deciding whether a more or less interventionist response is needed',⁸⁷ and then commencing with the least interventionist regulatory response, moving only to a more interventionist one when that fails.⁸⁸ In short, regulatory theory would suggest that the regulatory rope should be loosened from the necks of credit unions, mutual societies and community organisations on the basis that their 'conduct' in providing savings and credit facilities for social purposes should invoke a minimal regulatory response, enabling those organisations to contribute to overcoming financial exclusion to the greatest extent of their potential, while still leaving adequate consumer protection measures in place.

C *Corporate Law as a Limitation on the Contribution of Banks*

As we noted above, mainstream institutions such as banks have largely deserted the small loan market. However, in response to community concerns about high-cost credit in the fringe market, we are now seeing a number of the major banks dip their toes back in this market.

For example, in 2004 the National Australia Bank, in partnership with the Good Shepherd Youth and Family Service, piloted a low-interest loan product, the Step-Up Loan.

Step Up Loan is a National product facilitated by Good Shepherd Youth and Family Service. These personal, unsecured loans are between \$800 and \$3000 for individuals and families living on a low income and are offered at a reduced interest rate of

⁸⁵ *Banking Act 1959* (Cth) Pt II Div I, ss 7-11.

⁸⁶ See Valerie Ayres-Wearne and Janet Palafox IBVM, *NILS@: Small Loans – Big Changes* (2005).

⁸⁷ John Braithwaite, *Restorative Justice and Responsive Regulation* (1992) 29.

⁸⁸ *Ibid* 30.

6.9%. The loans provide affordable credit for the purchase of essential household goods and services (eg. refrigerators, washing machines, beds etc). In addition, repaying a Step Up Low Interest Loan establishes a credit rating and an entry into the mainstream credit system.⁸⁹

In addition to obtaining a low-interest loan, borrowers are mentored through the loan process and repayment period, and thus have access to support and further information. However, the Step Up Loan is being piloted in only five locations in Victoria and NSW, and it is not known if and when it will be made more widely available. Indeed, the fact that borrowers are mentored by a micro-credit worker throughout the loan period suggests that it might be difficult and expensive to roll out such a loan product on a more extensive basis.

Following the release of its discussion paper on community development finance⁹⁰ and its commissioned research on financial exclusion,⁹¹ ANZ Bank has also committed to develop and deliver, in partnership with relevant organisations:

- a small loan program for consumers who may otherwise use payday lenders; and
- microfinance programs to assist Indigenous communities develop viable businesses.⁹²

In addition to developing their own pilot projects, some of the major banks financially support the No Interest Loan schemes offered by community organisations.⁹³

These initiatives might be viewed as examples of voluntary ‘corporate social responsibility’ (CSR). There is no doubt that these initiatives, which largely involve partnerships between banks and community organisations, are valuable and could provide a framework for more extensive participation by banks in this area.⁹⁴ At this stage, however, these initiatives are on a small scale, have very limited geographic coverage and eligibility requirements,⁹⁵ and barely make a dent in overcoming financial exclusion. We will argue here that corporate law, and its mandate that

⁸⁹ National Australia Bank, *Step Up Low Interest Loans*, <<http://www.national.com.au/Community/0,49804,00.html>> at 22 July 2005.

⁹⁰ ANZ Bank, *Community Development Finance in Australia: a Discussion Paper* (2004).

⁹¹ Chant Link and Associates, above n 3.

⁹² ANZ Bank, *Community Development Finance in Australia: ANZ Response to Consultation* (2004) iii.

⁹³ Including the National Australia Bank (see National Australia Bank, *Supporting the No Interest Loans Scheme*®, <<http://www.national.com.au/Community/0,,49805,00.html>> at 23 May 2005) and Westpac (see Westpac Banking Corporation, *Pressing On: 2004 Social Impact Report* (2004) 28).

⁹⁴ Ramsay, above n 46, 6.

⁹⁵ For example, ANZ has a Saver Plus program which is not open to social security recipients (ANZ Bank, *Community Saver Plus*, <<http://www.anz.com.au/aus/aboutanz/Community/Programs/Saver.asp>> at 22 July 2005).

directors act in the best financial interests of shareholders, limits the extent of any initiatives undertaken by way of voluntary corporate social responsibility, and will prevent these initiatives from expanding to any desirable level without external regulation to both require and permit their expansion.

Company directors are under a duty to act in the best interests of the company under *Corporations Act 2001* (Cth) s 181 and under general fiduciary principles. The company has been defined in this regard to mean 'the shareholders as a whole'⁹⁶ or, where a company is insolvent, 'the creditors'.⁹⁷ In either case, it is the financial interests of those groups – as linked to the company's financial interests – that are regarded as relevant. This would seem to preclude an exercise of discretion by directors in favour of social welfare, unless some clear benefit to shareholders in terms of financial return can be demonstrated. Put another way, directors will potentially breach their duty to act in the best interests of shareholders if they exercise social responsibility in a manner that might impact on profits.

This understanding was reflected in the comments made by a spokesperson for the Australian Shareholder's Association in January 2005, criticising corporate donations to aid tsunami relief, stating that

firms should not generally give without expecting something in return ... in most circumstances, donations should only be made in situations that are likely to benefit the company through greater market exposure.⁹⁸

This is consistent with Milton Friedman's view that 'corporate expenditure on social causes is a violation of management's responsibility to shareholders to the extent that the expenditures do not lead to higher shareholder wealth'.⁹⁹ Australian case law confirms this position, but notes that, where an exercise of social responsibility or philanthropy can benefit the company - for example, by improving the company's reputation - then such acts can be justified.

A company may decide to be generous with those with whom it deals. But – we put the matter in general terms – it may be generous to do more than it need do only if, essentially, it be for the benefit of or for the purposes of the company that it do such. It may be felt inappropriate that the company acquire a reputation of being such.¹⁰⁰

⁹⁶ *Greenhalgh v Arderne Cinemas* [1945] 2 All ER 719.

⁹⁷ *Kinsela v Russell Kinsela Pty Ltd (In Liq)* (1986) 4 NSWLR 722.

⁹⁸ ABC News Online, 'Shareholder Group Opposes Tsunami Donations' (2005), <<http://www.abc.net.au/news/newsitems/200501/s1278005.htm>> at 18 January 2005.

⁹⁹ Milton Friedman quoted in Bernadette Ruf, Krishnamurthy Muralidar, Robert Brown, Jay Janney and Karen Paul, 'An Empirical Investigation of the Relationship between Change in Corporate Social Performance and Financial Performance: a Stakeholder Theory Perspective' (2001) 32(2) *Journal of Business Ethics* 14, 143.

¹⁰⁰ *Woolworths v Kelly* (1990) 4 ACSR 431, 446 (Mahoney JA).

The social expectation that companies will behave as good corporate citizens and exercise voluntary corporate social responsibility often seems to conflict with the legal requirements on boards of directors. This was very apparent in comments made by the chair of the board of the James Hardie group of companies, Meredith Hellicar, in response to criticisms of the group's restructure, which saw a separation of the group's ongoing asbestos liabilities from the balance sheet of group companies, leaving a shortfall in funds available to meet those liabilities. She commented:

In considering the sometimes competing - or even conflicting - requirements of the law, community expectations and our own moral precepts, we did not respond with offers of funding support for any shortfall of the foundation.¹⁰¹

There is little doubt that, in contributing to overcoming problems of financial exclusion, the boards of banks are mindful of their responsibilities to shareholders and will limit their contributions to what might be termed 'strategic' corporate social responsibility - that is, CSR, which enhances reputation and therefore contributes to shareholder wealth. Taking a more cynical view, Joel Bakan argues that CSR is no more than an attempt by corporations to improve their reputations and hide their true, self-interested natures.

Corporate social responsibility is their new creed, a self-conscious corrective to earlier greed-inspired visions of the corporation. Despite this shift, the corporation itself has not changed. It remains, as it was at the time of its origins as a modern business institution in the middle of the nineteenth century, a legally designated 'person' designed to valorise self-interest and invalidate moral concern.¹⁰²

It seems clear that, despite the best intentions of individuals working within the corporate structure of banks, banks will be unable to contribute to the financial inclusion of low-income consumers to any greater extent than is necessary for strategic purposes such as improving their corporate reputation, without clear and effective regulation to allow and require their more meaningful contribution. Relying on voluntary CSR initiatives will never be enough.

The nature of the regulatory response that should follow needs careful consideration. The enactment of legislation such as the US *Community Reinvestment Act*¹⁰³ has been recommended for the consideration of the Commonwealth Treasury by the Parliamentary Committee on Corporations and Financial Services.¹⁰⁴ Under that Act there is periodic evaluation of the performance of financial institutions in meeting the credit needs of the communities in which

¹⁰¹ Mathew Charles, 'Hardie Bid to Woo Investors', *Courier Mail* Brisbane 16 September 2004, 37.

¹⁰² Joel Bakan, *The Corporation: the Pathological Pursuit of Profit and Power* (2004) 28.

¹⁰³ *Community Reinvestment Act 1975* (USA).

¹⁰⁴ Parliamentary Joint Committee on Corporations and Financial Services, *Money Matters in the Bush* (Inquiry into the Level of Banking and Financial Services in Rural, Regional and Remote Areas of Australia, 2004) 304.

they maintain branches, including the needs of low- and moderate-income consumers. That record is taken into account in considering an institution's application for deposit facilities, including in the case of proposed mergers and acquisitions.¹⁰⁵ Notwithstanding the absence of such legislation in the UK, banks in England are reporting to the Bank of England on a voluntary basis along the lines required under the *Community Reinvestment Act*. The engagements of banks in addressing financial exclusion, and their related reporting, seem to have been spurred on by the threat of legislation.¹⁰⁶ It is likely that banks in Australia have been similarly spurred on to action in the interests of regulatory risk management, due to the threat of legislation such as the *Community Reinvestment Act*. Arguably, therefore, some risk of legislative intervention may be necessary to maintain and increase the participation of banks in this area. In terms of the responsiveness of regulation, however, regulatory theorists have suggested that the most suitable form of regulation will depend upon context, and upon the conduct of the industry in question:

regulation should respond to industry conduct, to how effectively industry is making private regulation work. The very behaviour of an industry or the firms therein should channel the regulatory strategy to greater or lesser degrees of government intervention.¹⁰⁷

We have given reasons as to why relying on voluntary corporate social responsibility, a form of self-regulation, will not be enough, and we have suggested that some form of public sanction such as under the *Community Reinvestment Act*, may be necessary to achieve the desired level of banks' participation in the effort to overcome financial exclusion in Australia. That said, in taking into account the recent conduct of most of the major banks in contributing in this area, a less interventionist model than that involved in enacting community reinvestment legislation might be more appropriate. An alternative to the *Community Reinvestment Act* model would be a model of 'enforced self-regulation', which can be described as the public enforcement of privately written rules.¹⁰⁸ One key difference between this and the enactment of community reinvestment legislation is that this model would be based upon industry members writing their own regulatory rules, perhaps by amending the *Code of Banking Practice 2003*, which would then be approved by a relevant regulator such as the Australian Prudential Regulatory Authority or the Australian Securities and Investments Commission¹⁰⁹ and be enforceable by that regulator if those rules were not voluntarily complied with. It is suggested that the enforcement mechanism would need to be more effective than that provided by the existing Code Compliance Monitoring Committee, which may

¹⁰⁵ Federal Financial Institutions Examination Council web site, <<http://www.ffiec.gov/hdma/history.htm>> at 8 June 2004.

¹⁰⁶ Reifner, above n 79, 46.

¹⁰⁷ Ayers and Braithwaite, above n 2, 4.

¹⁰⁸ Baldwin and Cave, above n 68, 133.

¹⁰⁹ ASIC currently has a 'codes approval power' for codes in the financial services sector. However, the model envisaged would involve a more extensive approval, monitoring and enforcement power.

prove to be a ‘toothless tiger’ given that its ultimate enforcement mechanism consists of ‘punishing’ banks by naming them in its annual report.¹¹⁰ The advantages of ‘enforced self-regulation’ include firstly, the opportunity for banks to internalise ethical standards and concepts of community service obligations, rather than obligations being externally imposed upon them. An external imposition of obligations might lead to banks seeking to avoid those obligations. Under this model it is more likely that banks will be committed to meeting those obligations. Secondly, the rules written by industry members might be well informed and therefore more effective and appropriate.¹¹¹ In relation to the regulation of mainstream financial institutions in this manner, however, it is acknowledged that further investigation is necessary to determine precisely upon which mainstream financial institutions any such obligations should be imposed.

V CONCLUSION

In this paper, we have explored the phenomenon of financial exclusion in Australia, with a particular focus on financial exclusion in the consumer credit market. Although definitions of financial exclusion vary, we have sought to explain the concept in light of concerns about access to fair, safe and affordable products from mainstream providers. We argue that short-term consumer credit should be treated as an essential service, particularly for low income and vulnerable consumers. Without access to products in the mainstream market, these consumers are largely restricted to either the fringe credit market, where products are often high-cost and fail to meet the criteria of affordable, fair and safe, or to the no-interest loan products offered by community and welfare organisations – these products are affordable, fair and safe, but are not widely available, nor widely publicised.

It is difficult to measure with any certainty the extent of financial exclusion in Australia, but there is evidence to suggest that it is a growing problem, and that the impacts of financial exclusion can be serious and long-lasting, for individuals, their families and the broader community. Similarly, it is difficult to isolate an individual factor that drives financial exclusion. Instead, there are a variety of personal and commercial/marketplace factors that can work together to drive financial exclusion, with the result that there is unlikely to be one simple solution to eliminating it.

We have sought to show how the regulatory framework also has a major impact on the extent or otherwise of financial exclusion in Australia. The regulatory framework relies heavily on competition and disclosure to protect consumers; however, in the absence of an obligation to supply, these approaches do not create incentives for mainstream suppliers to provide services to financially excluded consumers. Disclosure initiatives are also limited, given the personal and practical constraints facing financially excluded consumers in need of finance. As an

¹¹⁰ However, we note that, as from 1 April 2005, the role and effectiveness of the Code Compliance Monitoring Committee has been under review by the Foundation for Effective Markets and Governance, <<http://www.femag.anu.edu.au>> at 29 July 2005.

¹¹¹ Baldwin and Cave, above n 68, 40.

example, we have argued that the disclosure and other requirements in the UCCC do not ensure that fringe lenders are obliged to provide fair, safe and affordable loans to financially excluded consumers.

The regulatory framework also places significant barriers in front of industry or community organisations that are trying to develop effective ways of meeting the needs of financial excluded consumers. The treatment of all financial services providers as the same does not allow credit unions to develop a different, more effective approach. And there are also risks for community organisations seeking to meet client needs, if, for example, their products amount to deposit-taking products and require regulation. In terms of mainstream providers, obligations to shareholders imposed through the *Corporations Act* severely limit the extent to which micro-finance products can be offered if they are not profitable in isolation.

Although the regulatory framework is not the only mechanism for addressing financial exclusion in Australia, it can play a vital role. Reform to corporate, financial services and consumer credit regulation is needed to:

- create space for the development of voluntary initiatives by both community and for-profit organisations without the fear of inappropriate regulation;
- explore ways in which corporate social responsibility can be better accommodated within existing corporate structures;
- impose obligations on mainstream providers to meet the finance needs of financially excluded consumers; and
- ensure that exploitative products are simply not available in the marketplace.

Without such changes, many consumers will continue to be financially excluded, at considerable cost to themselves, their families and the broader community.