

BULLETIN NO 34 – JUNE 2002

Collection Issues: Sales of Debts, Credit Reporting and Mortgagee Sales

This Bulletin deals with a number of issues that have arisen in relation to collection of debts. The context is the increasing use of both outsourcing of collection activity and automated collection systems.

Sale of debts issues

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BULLETIN

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Sale of Debts

Effect on ABIO Jurisdiction

The fact that a debt has been sold will not prevent this office considering the dispute if the dispute concerns the actions of the financial services provider prior to the sale of the debt.

If the outcome of our consideration is that the financial services provider is liable for loss caused to the disputant, then compensation may take the form of a monetary award or an obligation to indemnify the complainant to the extent that the debt as collected by the assignee exceeds the disputant's liability to the financial services provider. It would appear to be appropriate, however, for financial services providers to seek to retrieve the debt from the assignee if a dispute is received by this office about the financial services provider's actions in relation to it.

If legal proceedings are issued by the assignee against the disputant before we receive the dispute or while the matter is being considered by this office then our view is that the whole matter may more appropriately be dealt with in the court, which may require the financial services provider being joined as a party. We would expect, however, that members would seek to ensure that assignees do not commence legal proceedings if a dispute about the debt is being considered by this office.

Debts should not be sold while a dispute is being considered by the ABIO

It has happened that a debt has been sold while a complaint is being considered by this office, resulting in collection activity by the assignee against the complainant. This may occur because of a system error but, nevertheless, debts should not be sold after this office has received a dispute. To do so unnecessarily complicates resolution of the dispute, results in undue pressure on the disputant and reflects unfavourably on the financial services provider as a scheme member.

Members should ensure that their internal systems prevent the sale of a debt or the passing of that debt to a collection agent while the matter is being dealt with by this office. If a debt is inadvertently sold while this office is considering a dispute, we expect the member to take immediate steps to retrieve the debt from the assignee.

Debtor's entitlement to information about a debt being collected

Where a debt is regulated by the Uniform Consumer Credit Code (UCCC) the debtor is entitled to information from the credit provider about the debt. These obligations apply even if, under the UCCC and the credit contract terms and conditions, the credit provider is entitled to cease sending statements. Financial services providers should ensure that staff and collection agents are aware of the financial services provider's obligations under:

- s 34 - obligation to provide information on request about how a debt has been calculated;
- s 76 - obligation to provide a written statement of the amount required to payout the debt including, if requested, details of the items which make up that amount; and
- s 163 - obligation to provide certain documents upon request.

If a debt is sold, financial services providers should ensure that the required information is retained or provided to the assignee so that it can be provided to the debtor on request.

This office will be conducting a survey on financial services provider record keeping practices shortly.

The purpose of the survey is to ascertain the record keeping practices of members of the scheme:

- to determine if there are standard record keeping practices;
- to assist in the development of a guideline for record keeping practices, if appropriate and necessary; and
- to assist in the early resolution of disputes by ensuring that requests for documents are directed and therefore more easily satisfied.

A section of the survey will relate to records kept by a financial services provider, and records passed on to the assignee when the debt is sold.

Statute-barred debts should not be collected or sold

Occasionally it appears from a dispute that the financial services provider is seeking to collect or has sold a statute-barred debt. Our view is that a financial services provider should not seek recovery of or sell such a debt. The fact that the debt is statute-barred does not, of itself, prevent it being sued for as it is for a defendant to raise the statute as a defence. However, once raised it is a complete defence. As collection activity will usually involve a representation that the debt is payable then in circumstances where there is a complete defence such a representation may well amount to misleading and deceptive conduct.

It should also be noted that a debt that is statute barred must not be listed (Credit Reporting Code of Conduct, cl 2.8).

Credit Reporting Issues

Listing of debts on overdrawn transaction accounts

This office has received a number of disputes from consumers who have discovered that an overdrawn amount, on a transaction account which otherwise does not have a credit facility, has been listed on their consumer credit file with Baycorp Advantage (formerly CRAA and Credit Advantage). The listing in each case has purportedly been of a payment default on a 'continuing credit contract'.

Of the disputes in a recent group, a number of the listings were in respect of overdrawings resulting from the honour of direct debits, although in some of these cases the disputant claimed that these had been cancelled. In other case the overdrawn amount was comprised of dishonour fees and other charges rather than arising because of transactions initiated by the account holder. Some disputants claimed to have been listed despite entering into a payment arrangement.

The practice apparent in these disputes raises a number of concerns.

A credit report must relate to credit provided

The fact that a debt is due does not of itself mean that credit has been provided. The provision of credit is generally understood to mean that an arrangement is in place under which the payment of a debt is *deferred* (see *Herbert v R* (1941) 64 CLR 461 at 467; [1941] ALR 100).

Under the Privacy Act 1988 (Cth) (the Act), a credit information file may only contain:

- credit related information
- court judgements
- bankruptcy orders
- serious credit infringement information
- the double dishonour of a cheque for more than \$100.

Credit is defined in the Act as a loan which meets certain requirements. A loan, in turn, is defined as a contract, arrangement or understanding by which an individual is permitted to either defer payment of a debt, or to incur a debt and then defer its payment (see s 6(1)). This is consistent with the definition of credit in s 4(1) of the UCCC:

'For the purposes of this Code, 'credit' is provided if under a contract-

- (a) *payment of a debt owed by one person (the debtor) to another (the credit provider) is deferred; or*
- (b) *one person (the debtor) incurs a deferred debt to another (the credit provider).'*

The Privacy Commissioner's Advice Summary number 1.8 (debit cards) states that for a customer's overdrawn transaction account to be viewed as the 'provision of credit', it must be *'the intention of both the credit provider and the individual that an application for credit is being made'*. For a listing to be permitted there must be *'a prior agreement or understanding between the parties that, where the account is overdrawn, the amount overdrawn is regarded as credit payable by the individual. This will usually involve a documented loan agreement of some kind, such as a credit facility attached to the savings account or other debit facility.'*

We note that Baycorp Advantage includes as a valid credit account code (for listing purposes) 'Deferred Payment Debit Card'. We are informed that this describes a debit account with a credit facility attached and is consistent with the type of facility described in the advice summary above.

In the absence of an agreed overdraft facility, or other agreement for the provision of credit, this office's view is that an overdrawn amount on a debit facility should not be listed and that any listing should be removed. If the terms and conditions of the account require that the account not be overdrawn and that if overdrawn be brought back into credit immediately it will be difficult for a member to argue that credit has been provided.

The listing may also be in breach of other requirements of the Act:

- s 18E(8)(c) requires a credit provider, at the time the account is opened, to disclose to the consumer that information might be disclosed to a credit reporting agency. This means that, even if the information can be said to be credit information, the listing would still be required to be removed if the terms and conditions of the account at the time it was opened failed to disclose the possibility of listing; and
- listing the payment default as being in respect of a 'continuing credit contract' is on its face misleading. Given the prohibition on misleading listings, this of itself may well mean that the listing has to be removed.

Listings without prior warning

Some disputes received by this office have related to a listing made without warning, that is, the overdue payment may have been demanded, and be more than 60 days overdue, but the consumer has not been notified that failure to pay will result in the debt being listed.

The Privacy Commissioner's Explanatory note 54 states:

'Where an individual becomes overdue in respect of credit given by a credit provider, the credit provider may not report the overdue payment to a credit reporting agency unless the credit provider has first notified that individual that the credit provider may lodge a report about the overdue payment against the individual with a credit reporting agency'.

The view of this office is that, as a matter of good practice, a financial services provider must warn the consumer at the time of demand that failure to pay may result in a credit listing.

Listing amounts less than 60 days overdue

This office has noted a number of disputes which involve the listing of all overdue payments and not just those which are 60 days overdue. For example, the minimum payment on a credit card account may be 60 days overdue but the listing includes all overdue payments and interest charges, including those which may only have become due within 30 or 14 days of the listing.

Following a review of the legislation and consultation with the Office of the Federal Privacy Commissioner, it is our view that a credit provider is only entitled to list the amount of a payment that is overdue if *the payment listed* is overdue for 60 days or more and the credit provider has sent a written notice to the customer's last known address which:

- Advises the customer of *the overdue payment* subsequently listed; and
- Requests payment of the amount outstanding.

In other words, our approach will be that members are only entitled to list payments which are overdue for 60 days or more and about which a customer has been informed in writing. Any other payments which have not been made, but which have been overdue for less than 60 days (and/or which the customer has not been notified in writing about), should not be included in the default listing.

In assessing disputes, this office will ask members to remove any payments from the listing with Baycorp Advantage where the above criteria are not satisfied.

This would also apply where a financial services provider relies on an acceleration clause to demand that the remaining loan balance be repaid by a customer. A listing of the remaining loan balance would also be subject to the above criteria.

Listing of commercial debts on consumer files

The Act regulates the reporting of defaults on loans provided wholly or principally for domestic, family or household purposes. It does not regulate the listing of defaults on business accounts. Separate files, called commercial files, are maintained by Baycorp Advantage for such listings. It is sometimes the case that one person will have both a consumer file and a commercial file. Members should ensure that listings are made on the correct file for the account. A listing of a commercial debt on a consumer file would be an error and the listing would be required to be removed.

Records of notices sent

In some automated collection systems, a copy of the notice actually sent to the customer is not retained. Instead, the financial services provider may seek to rely on a system generated collection note indicating that the relevant notice was sent together with a template notice kept on the system.

In particular cases, it will be crucial to establish that a notice was sent, its contents and the address to which it was sent. If members make a commercial decision not to retain such documentation, they should bear in mind that if there is a dispute about whether the required notice was sent, where it was sent or what it contained, inferences may be drawn against the financial services provider if it is unable to provide a copy of the actual notice sent.

Mortgagee Sales – some recent issues

The ABIO Policies and Procedures Manual sets out the questions this office will ask when considering a dispute about a member's exercise of the power of sale. The questions asked reflect the obligations on a financial services provider when selling a property as mortgagee in possession.

These obligations apply whether or not the sale process is outsourced to a property realisation company, a practice which appears to be becoming more common. In some cases there may be a chain of agents acting on the financial services provider's behalf in carrying out tasks such as engaging a real estate agent or engaging a valuer. Some recent disputes, involving outsourced sales, have suggested that there is a need for a reminder that the financial services provider must ensure that the conduct of its agents does not fall short of the standards required by the law.

Failure to advertise

In some recent cases, it is apparent that the property was sold after a valuation had been obtained but before advertising had commenced. The rationale for the sale was stated to be that the offers received had been within the range contained in a valuation and the early sale had saved marketing and advertising costs which would otherwise have been added to the loan account. While this may be convenient for those engaged to carry out the sale and there is no doubt that commissions would be earned in a shorter time and with less work, a mortgagee is not entitled to sell the property without advertising and to do so may result in liability for any loss caused.

While there are some parameters of a mortgagee's duty which are unclear, there is no doubt that adequate advertising is essential. Without adequate advertising, it is impossible to be satisfied that the market has been properly tested and therefore to be satisfied that the price obtained is a fair market value.

In *Pendlebury v Colonial Mutual Life Assurance Society Ltd* (1912) 13 CLR 676, the High Court was of the view that the failure of the mortgagee to place proper or sufficient advertising of a sale was so manifest as to amount to recklessness. In *Henry Roach (Petroleum) Pty Ltd v Credit House (Victoria) Pty Ltd* [1976] VR 309, Lush J stated that a mortgagee is not entitled to sell '*without advertising so as to bring the property to the notice of persons likely to be interested and so as to bring to the notice of possible buyers the potentiality of the property to be sold*'.

It may be, of course, that the property has been on the market, including being advertised, prior to the mortgagee taking possession. This will be taken into account in assessing whether the mortgagee's advertising is adequate provided that the property was listed for a similar price to that for which the mortgagee lists it and the mortgagee's listing price fits with that recommended in the valuation and any appraisals. Where, however, the property was previously listed at a higher price, the fact that there was earlier advertising will not absolve the mortgagee of its obligation to ensure that its sale follows on from proper advertising, including an adequate description of the property.

Records of steps taken - agent's files

When we investigate a dispute about a mortgage sale, we will ask for the financial services provider's files. Members have an obligation to provide all relevant information (see Guidelines to the Terms of Reference, p 45). Where any aspect of the sale has been outsourced, the files provided should include the files of all relevant agents, including those of any property realisation company engaged. In some cases, the task of instructing a valuer will itself be outsourced to a valuation firm. If that is this case, then the files of that valuation firm should be included.

Outsourcing costs

Costs passed on to the mortgagor's accounts must be properly incurred. If a multiplicity of agents has resulted in apparently excessive costs being passed on to the mortgagor, then this office will consider the extent to which those costs are recoverable by the mortgagee. The terms of the mortgage will also be relevant.

As always, we welcome feedback and comments on our approach to these issues.

Financial Services Consumer Helpline

On 21 June, the Treasurer for the Commonwealth of Australia, Peter Costello, launched a new consumer service which links the telephone contact facilities of the Australian Banking Industry Ombudsman Limited, Insurance Enquiries & Complaints Ltd and the Financial Industry Complaints Service Limited.

The telephone number is 1300 78 08 08. The existing contact numbers for the Australian Banking Industry Ombudsman Scheme ("the Scheme") will continue to operate in addition to the new telephone number. The new facility is managed by the Scheme.

The objective of establishing the new facility is to ensure that no consumer, having an issue to raise in respect of the operations of a bank, insurance company or other financial service provider (e.g. financial planner, stockbroker, life insurance company), is in any doubt about to where to go for assistance.

As far as the Scheme is concerned, entering into an arrangement whereby services are delivered with Insurance Enquiries & Complaints Ltd and the Financial Industry Complaints Service is an example of the co-operation which exists between the three largest deliverers of dispute resolution services in the financial services area.

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