Effective Support in Financial Hardship

christians against poverty

CAP

Introduction

The covid-19 pandemic has exposed a widespread lack of financial resilience in New Zealand households. 34% (608,000 households) are already experiencing financial difficulties and 40% (715,000 households) do not have the financial resilience to manage any further drop in income[1]. "Families are living on the edge of disaster, with high commitments and no savings and are turning to borrowing to make ends meet. Families in hardship need access to advice and support however there is a risk that this is ineffective when we underestimate the widespread harm caused by financial hardship.

In this report, Christians Against Poverty (CAP) unpacks **three important dynamics of financial hardship**, drawing on our experiences providing debt counselling and financial capability training. This report then makes recommendations to help guide effective support to those in financial hardship.

Firstly, **the lending industry often underestimates the depth of financial hardship**. Families in financial hardship are often spending any savings and sacrificing essential living costs. A loan default is not the first sign of financial hardship, but the last. Help intended for those in financial hardship must seek to understand how deep financial hardship extends.

Secondly, **financial hardship is about so much more than money**. It affects the whole family: relationships, mental health, self-esteem, and parenting. Growing debt and the incapacity to fix the situation is stressful, frustrating and energy consuming. Providing help to those in genuine hardship must acknowledge the challenges that are present in other life domains.

Thirdly, **people are at risk of falling into further harm when they're struggling**. Many of CAP's clients have struggled for years in debt. Shame, embarrassment, fear of judgment and lack of bandwidth effectively paralyse them. There is a real risk that families will undertake steps that provide short-term relief (taking out further loans, accessing Kiwisaver) but that are disastrous for long-term health.

Identifying families that are in hardship and in need of advice and advocacy is crucial to improving their current situation, but acknowledging the complexity and full impact of financial hardship on a household will help in the development of targeted and appropriate support so that more families can receive the help they desperately need.

1. CFFC – Impact of the covid-19 crisis on financial wellbeing in New Zealand, May 2020

The Depth of Hardship

This section explores the depth of hardship and the difference between industry definitions and the experience of those in hardship. Strategies to help those in financial hardship must acknowledge that effective support will be proactive across all loan products and will address the financial wellbeing of the household.

From all directions

There is a common narrative that high-cost loans (>50% interest p.a.) are the products causing most harm, although only 28% of CAP clients have a high-cost loan. CAP sees families living in unaffordable situations and debt **across the spectrum of loan products**.

74%
owe money for a bank product – an overdraft, personal loan or credit card

78%
owe money to non-bank lenders – finance companies, non-bank credit cards, truck shops

69%
owe money to Work and Income

51%
owe money **specifically for a car loan**

It is common, in CAP's experience, for **a client's vehicle finance to be the most significant factor contributing to their financial hardship.** The family car is often essential to get to work and school, but high loan repayments leave too little to pay for essential living costs. Families go into arrears on rent, utilities, and take out more debt. They don't have savings for maintenance or repairs. When the car breaks down, they feel they have no option but to trade in their wreck and get another car on finance.

> *It was the van payments that made me realise, whoa, I'm struggling, struggling struggling...it was almost a third of my income. In the end, I had to give the van back but I still owed for it and the courts got involved and made me pay for it.*

When does hardship start?

It is common to hear lenders and policy makers treat loan defaults as synonymous with financial hardship. For example, lenders may only flag an account as potential hardship when a debtor has missed a series of payments or is in default. Similarly, the CFFC report in their May report on financial wellbeing[2] used "First signs of hardship" in reference to families being in arrears on at least one financial commitment. However, in CAP's experience, **a loan default is a poor indicator of financial hardship**. This is because families who are in financial hardship are often significantly cutting out spending on essentials before defaulting on loans. Before coming to CAP:

67%
skipped meals, often regularly, to make loan repayments

30%
owed money for medical or school expenses

65%
owe money for utilities and housing

CAP's experience is in line with the StatsNZ findings of lack within families experiencing material hardship[3]. Families in hardship are not saving, not eating enough or of good quality, are putting up with feeling cold, are postponing health visits, not replacing damaged appliances and not spending money on clothing and shoes for their family.

My kids missed out on everyday activities... playground, couldn't afford petrol, snacks to take them. Kids always ate spaghetti or sometimes a loaf of bread for the day...

This indicates that all too often a loan default is likely not the first sign of financial hardship; it can very often be the last sign. Measuring financial hardship from a point of loan default is often under-representing the actual level of financial hardship that people are experiencing.

Out of arrears, out of hardship?

The approach to financial hardship by many lenders is within the context of the Credit Contracts and Consumer Finance Act 2003. This means lenders typically use quite a narrow definition of financial hardship as occurring when one cannot meet existing financial obligations because of a change in circumstances. This fails to address the many instances of hardship that borrowers end up in where there has really just been an accumulation of debt obligations that are unserviceable rather than an obvious sudden change. This often leads to hardship applications that are rejected as there has been no clear reason. This excludes a large number of people from accessing an arrangement that could alleviate the very real hardship they face.

2. CFFC – Impact of the covid-19 crisis on financial wellbeing in New Zealand, May 2020
3. Stats NZ - https://www.stats.govt.nz/methods/measuring-child-poverty-material-hardship, May 2020

This definition also unfortunately encourages lenders to equate arrears with hardship. Lenders are thus incentivised to lower the number of their loans in 'hardship' by focussing on the elimination of arrears. Once an arrangement has been entered into with a debtor to deal with arrears, lenders often re-categorise accounts as no longer in 'hardship'. While a lender may be able to satisfy themselves that the account is no longer in arrears, **there may not necessarily have been any improvement to the long-term financial resilience of the household.**

Limited liability?

Most lenders only have a commercial interest in addressing their particular debt rather than restructuring the entire financial circumstances and debt obligations a debtor may have.

Conversations with clients often focus on how and when their one particular debt will be cleared, with little consideration for the essential living costs that haven't been saved for or other obligations that may be in arrears.

Informal payment arrangements and hardship applications can be really quite beneficial to lenders as they get to roll up any arrears and restructure a loan under a different arrangement with a borrower. Clients that enter into loan variations under a hardship arrangement are generally still paying more debt over longer and any relief that this arrangement provides is only artificially reducing the very real hardship within the household.

More than Money

In CAP's experience, it is clear that financial hardship is not just limited to defaulting on debt. This section explores the impact of financial hardship on the many other areas of a families' life. **Each of these areas acts as a barrier to people reaching out for help.** Strategies to help those in financial hardship must acknowledge the challenges that are present in other life domains and how difficult it can be for people to reach out for help.

Stress... shame... depression

Growing debt balances and lack of capacity to fix the situation is stressful, frustrating and energy consuming. **Before coming to CAP:**

96% said debt made them feel **stressed**

55% said debt made them **fearful**

68% said debt made them feel **ashamed**

I felt lost, unsure, stress, and mostly embarrassed that I had accumulated debt and it was out of control. I did not want to talk about it or address it. The phone call to CAP was one of the hardest things I have ever had to do. I was so relieved that the CAP staff did not judge me or make me feel any lower than I was already thinking.

92% of clients said that their **health was affected** as a result of debt. Of these, **71%** specifically mentioned that they felt **depressed or were on medication for depression**

30% of clients admitted that before CAP they had **thought about, or attempted,** suicide as a way out

Depressed suicidal thoughts everyday and feeing overwhelmed and wanting to give up and die almost everyday.

"I felt like a failure as a parent"

Financial hardship also affects the health and wellbeing of children. Of CAP clients that are parents or caregivers

62% said that they couldn't buy healthy food

62% couldn't buy adequate clothes or shoes

82% felt they couldn't be a good parent

She couldn't live with me anymore, she had to live with family who could pick her up on time so that I could focus on getting a better job and working to pay the debts off and learn how to budget. She is sad to be separated from me.

Broken relationships - disrupted families

Over 80% of clients in a relationship said that debt affected their relationship, reporting that it caused frequent arguments and, for 30% of respondents, it caused a full relationship breakdown.

> *The hardest thing was trying to keep our family together, our marriage together. It was just destroying both of us because we got to the stage we really didn't talk we just barked at each other.*

> *I did think of leaving my marriage. Packing up and taking the kids, but where was I going to go? I got no money, I got nothing, I had nothing.*

91% **of clients say being in debt made them stay away from people; of these:**

67%	66%	62%
stayed away from **social/sporting**	stayed away from **friends**	stayed away from **family**

> *When we have family get togethers you got to bring a plate. We had no plate to bring. It was like, make any excuse - 'oh two of the kids are sick'...or 'we can't go, we don't have any gas.'*

Multiple & complex needs

Many people in financial hardship present with multiple complex needs, and are disadvantaged in several life domains: income, housing, employment, safety and social connectedness. Each of these areas requires support from social services and can be incredibly exhausting for clients to have to manage alongside their financial hardship.

An estimated **80% of CAP clients are living with a very significant condition** that we recognise as requiring extreme care. These conditions include clinical depression, anxiety, panic attacks, and chronic addictions. Some CAP clients are living with a permanent disability, or recovering from traumatic injury, cancer, strokes or heart attacks.

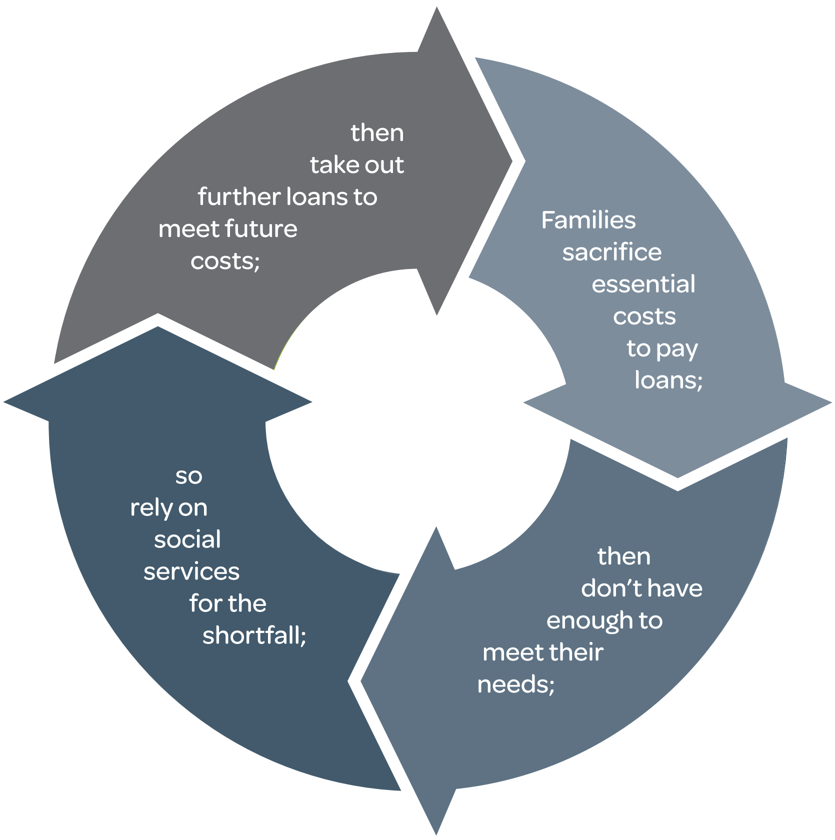
> *Depressed suicidal thoughts every day and feeling overwhelmed and wanting to give up and die almost every day. Feeling emotional and hyper tensive over small situations when caring for my boys. Being paranoid whenever I get a call, txt or knock on door.*

Preventing further harm

When someone is in financial hardship, shame, embarrassment, fear of judgment and lack of bandwidth can effectively paralyse them from reaching out for help. This section explores the systematic barriers that prevent people accessing help and, in many cases, exacerbate financial hardship. **It is imperative that people in financial hardship have protection from falling further into financial hardship.**

Loans delay access to help

The research is clear: financial hardship can cause risky behaviour[4]. It is in this context of stress and fear that it is easier to understand the vicious cycle that people can fall into of taking out further debt:



There is a very real risk that families will take out loans that provide short term relief but that are disastrous for long term financial wellbeing. Loans very rarely alleviate financial hardship, rather **loans delay the time until a family has no option but to seek help**. Loans only delay early access to help.

4. MSD – The voices of people in hard to reach communities, October 2017

Harm within first-tier financial products

Several financial products like bank overdrafts, credit cards, and lines of credit are often advertised and intended as providing temporary flexibility:

> *"The reassurance of having extra funds if you ever need them, giving you flexibility and peace of mind."*[5]

However, CAP sees many clients that are permanently stuck in a position of maximum overdraft or of minimum credit card repayment.

> *I was in considerable debt, [which was] the result from years of unwise decisions with money. Getting credit cards and overdrafts, then getting a debt consolidation, but still using the overdraft before it was closed.*

It is very common for people in financial hardship to present to CAP, having spent months in near permanent overdraft, paying a monthly fee and interest for a product that they are unable to use as it was originally intended. People that are frequently in overdraft do not have access to the line of credit as intended and are more at risk of turning to high cost lending.

Unaffordable from the start

Sadly, CAP sees many examples of lenders that do not make reasonable effort to ensure their loans won't cause unnecessary hardship. Affordability assessments are not conducted properly and don't consider the reasonable and fair costs of looking after a household.[6]

> *It was the van payments that made me realise, whoa, I'm struggling, struggling struggling...it was almost a third of my income...In the end, I had to give the van back but I still owed for it and the courts got involved and made me pay for it.*

Lenders often fail to provide for essential living costs or existing obligations:

- Food and clothing are often under-estimated, especially for large families.
- No future expenses. Lenders may allow for petrol but not for WoF/Rego or maintenance.
- No savings for unexpected future needs or for retirement.
- Defaulted debts, court fines, utility arrears and rent arrears are ignored or not asked about.

Loans that don't assess affordability appropriately effectively trap families in hardship because they cannot afford to meet future expenses. These assessments are also unfortunately not isolated but are, rather, examples of systematic practice across different loan products and lenders.

Mortgage lenders use external expense benchmarking guidelines (eg. Sense Partners) to help assess affordability to help provide consistency across the market; the same industry consistency should be expected for other loan products. A lender's own internal guidelines for assessing affordability become a point of competition within the market – a 'race to the bottom' where firms are incentivised to include only the bare minimum of expenses, moving away from protecting the well-being of the borrower as the law is intended.

5. Overdraft product as described by one major New Zealand bank, May 2020
6. CAP NZ – Inadequate Affordability Assessments: Three case studies, February 2020

Piling on the pressure

Debt collection practices add significant harm to families that are already struggling. In talking to CAP clients about their experiences of being in debt, we regularly hear examples of bullying and harassment when debts are overdue. Some members of the community receive automated phone calls from debt-collectors multiple times every day. We've also heard of examples where debt collectors arrive at properties wearing uniforms (similar to law or court officials) in an effort to misrepresent their authority. This causes untold stress and anxiety for these families.

Unregulated and predatory collection practices exacerbate financial hardship because families under stress make payment arrangements that are unsustainable, just to get a break from the stress. Debt collection can also add thousands of dollars to debt balances making it impossible for families to ever catch up. Harassment and high costs of collection are causing significant emotional and financial harm to vulnerable borrowers. It is sickening to observe the negative impact on borrowers' mental health caused by frequent and oppressive contact by debt collection companies.

> *Stress levels were really bad. Made me worry about the next phone call I was gonna get from people asking for money.*

Unable to complain

CAP understands that compliance and enforcement strategy is, in part, reliant on consumer complaints. It is, however, CAP's experience that **there are several complex barriers to clients making a complaint about lenders** that may have broken the law.

- Borrowers don't know they are victims of illegal behaviour;
- They don't know about their right to complain;
- They are afraid to complain;
  - "Will the lender repossess my stuff? Will I be able to get finance in the future?"
  - "Will I get in trouble from the government? Maybe I did something wrong"
- Cultural barriers, language issues, mental health, time consuming
- There is no clear outcome to making a complaint.

Debt counsellors and financial mentors have a very detailed, first-hand knowledge of which lenders in the market are causing significant hardship.

Effective support – recommendations

The effects of financial hardship are not currently well understood within the finance industry. CAP makes the following recommendations to ensure financial products and customer care are offered appropriately and responsibly in Aotearoa, and struggling families can receive the help they so desperately need.

Government and regulators

1. **Regulators must develop affordability benchmarking guidelines** so that affordability assessment by different lenders treats customers in a consistent manner, both at the time of first loan assessment and also during any hardship application processes. This practice currently exists for mortgage lending and would extend this consumer protection across a wider range of loan products. Guidelines should be developed in collaboration with consumer advocates to ensure they are fair.

2. **Government must act to regulate debt collection** to prevent predatory collection practises. The law should cover contact, privacy and harassment issues. In Australia, the United Kingdom and the United States, extensive rules govern the way in which debt collectors can carry out their operations. CAP is aware that many active debt collectors in New Zealand also operate in Australia under the Australian regime and would not be disadvantaged by facing similar law in New Zealand.

3. **Regulators should ensure first-tier lenders are proactively taking action to help people** who are in frequent overdraft or making minimum credit card repayments. These products are typically a safer form of credit for consumers when used correctly. This would be an extension of the current culture and conduct review to ensure customers are not unnecessarily stuck with unsuitable loan products.

4. **Enforcement strategy should be developed in collaboration with debt counsellors and financial mentors** who have significant knowledge of lenders that are causing most harm in their communities. Enforcement strategy should rely less on a system of complaints, acknowledging the significant barriers people face to make a complaint.

Lenders

5. **Lenders should proactively provide clients in arrears with information about free, independent and non-judgemental help** that can support clients to make the best choice for all their life circumstances. This should happen whenever clients fall into frequent arrears or make a hardship application, acknowledging that borrowers in arrears are likely in urgent need of support.

6. **Lenders should give people in hardship a quick route to a case manager** so that clients don't have to wait on hold for long periods or share embarrassing details many times over.

7. **Lenders should collaborate with debt counsellors** to ensure their collections and recoveries processes are suitable and considerate of the complex nature of financial hardship and to ensure that help pathways are straightforward and easy to navigate for people in complex circumstances.

Conclusion

There are thousands of New Zealand households that are experiencing financial hardship. However financial hardship is not easy to recognise and is more complex than just the inability to meet a financial obligation. It is imperative that the consumer lending industry is protecting consumers from further financial harm and that effective customer care is available to help those from falling into further hardship.

This report has discussed, firstly, that the lending industry often underestimates the depth of financial hardship. Families that are defaulting on loans are very likely already in significant hardship and sacrificing essential living costs to try and make ends meet. A loan default is not the first sign of financial hardship but the last.

Secondly, this report has explored how financial hardship is about so much more than money. Providing help to those in genuine hardship must acknowledge the stress, shame and depression that comes with debt, as well as the deep impact that debt has on relationships and mental health.

Thirdly, this report has also uncovered the very real risk that families under stress will undertake steps that are not appropriate for long-term financial wellbeing; that further loans very often do not alleviate financial hardship at all, rather loans only delay early access to help.

Understanding the complexity of financial hardship means that strategic efforts to provide support to these families can be well targeted and appropriate so that more families can receive the help they desperately need.

About CAP

CAP partners with 46 local churches across Aotearoa to release people from debt and poverty, into a life filled with hope and freedom. Through a network of CAP Debt Centres, CAP offers a free face-to-face debt management service, with advice and ongoing support provided from CAP Head Office. In addition, CAP provides face-to-face financial education through the CAP Money Course, and tackles the causes of debt and poverty through its group services: CAP Job Clubs, CAP Life Skills and CAP Release Groups. All CAP's services are available to individuals regardless of age, disability, gender, sexual orientation, religion or belief.

Data

The statistics and data contained within this report are analyses of CAP's past and current clients. Where appropriate, we indicate data that has not been sourced by CAP.

All client quotes within the report are genuine but anonymous.

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