

Targeted consultation - Policy and drafting proposal for rate cap on high-cost loans

To:

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Executive Summary

Tēnā koutou,

Thank you for the opportunity to provide feedback on the draft proposal for a rate cap on high-cost loans. Christians Against Poverty's (CAP) feedback approaches the stated questions from the perspective of providing the best possible protection for consumers, particularly those in vulnerability, poverty or material hardship. CAP adopts this position for two very important reasons.

Firstly, we recognise the intent of both the Credit Contract & Consumer Finance Act 2003 (the Act) and that of the Credit Contract and Consumer Finance Amendment Bill (the Bill) as being of this intention. The primary purpose of the Act is to:

“to protect the interests of consumers in connection with credit contracts...”

The Bill sets out to strengthen the Act's purpose having identified significant harm to vulnerable consumers from problem debt, identifying issues such as:

“...excessive cost of some consumer credit agreements; continued irresponsible lending and other non-compliance, including by mobile traders; unreasonable fees; and irresponsible debt collection practices.”

Secondly, CAP's feedback advocates for the best protection for consumers because of the desperation and struggle we witness daily in the lives of vulnerable people who are brave enough to reach out for help. Often experiencing isolation, anxiety, depression and severe stress due to problem debt, vulnerable people may not have the agency to speak up for themselves, to exercise rights or to make fully-informed decisions.

CAP's points of feedback below are considerations for the Select Committee as it drafts this bill to provide consumers in vulnerability and hardship the protection they deserve. The two most important elements of this feedback:

Question 7 - CAP is in favour of a definition of high-cost lending that includes the **total costs** payable under consumer credit loans by including all fees with interest charges. Fee terms are often confusing and difficult to compare. They quickly add to the cost of borrowing and often aren't advertised up front. Borrowers living in hardship can find making complex financial decisions difficult. People in hardship would be best protected by defining high-cost lending including **all** costs.

Question 8 - Vulnerable consumers and those in poverty and hardship often don't have the resources, the agency or the knowledge to be able to demonstrate that a fee is 'unreasonable'. This law reform presents an opportunity to protect their interests by shifting the burden of proving reasonableness away from debtors and towards creditors in a similar manner to that suggested in item 21 of the draft proposal.

I welcome any further questions you may have and thank you for the opportunity to provide input to your important decision-making.

Nāku noa, nā

Michael Ward
Christians Against Poverty

Introduction to Christians Against Poverty (CAP)

Free debt-counselling – CAP Debt Help

CAP has been operating in New Zealand for over 11 years. CAP's free **Debt Help** service has now helped thousands of New Zealanders to grow in financial capability. CAP **Debt Help** builds sustainable and liveable budgets; negotiates directly with creditors to ensure that debt repayments are affordable and fair; and supports clients long-term as they repay debt.

CAP works with its clients, on average, for two years (always free-of-charge) until they have repaid debts in full. CAP's **Debt Help** service is currently available in 47 locations across Aotearoa, from Kaitiaki to Dunedin. On average, clients come to CAP with **over \$28,000 of debt. Most of those clients present with debts specifically related to consumer credit** such as car loans, truck shops, personal loans, credit cards and payday loans. Over 70% of CAP clients rely on a benefit as the household's main source of income. Amongst CAP clients in paid employment, many still struggle to make ends meet and to provide for families because they receive the minimum wage.

CAP visits approximately 100 households each month. As a result, CAP constantly comes face-to-face with the crushing despair and misery created by debt. **Over half of CAP clients could not provide three meals a day for their children. Anxiety and depression caused by debt caused 65% of clients to isolate themselves.** Before coming to CAP, 1 in 4 clients had contemplated or attempted taking their lives.

"I was very stressed, depressed - I was afraid of being judged, embarrassed, agitated. My children [were] feeling and suffering with me, which caused separation with my husband of twenty plus years of marriage." - CAP Client

In the past ten years CAP has **helped thousands of clients to pay off over \$38 million of debts and bills.** In addition, we've **enabled the write-off of over \$30 million of debt** as result of negotiation with creditors and insolvency procedures.

The fruits of this work mean that over 1,540 people have become debt-free. Moreover, these numbers have positively transformed the homes of over 1,700 children.

Money Education – CAP Money

In response to the vast need that we saw in families struggling in debt, Christians Against Poverty developed the **CAP Money** course in March 2009. Since its launch, the course has helped thousands of families avoid unmanageable debt by organising their finances. Nearly 15,000 people have successfully completed a **CAP Money** course to learn how to take control of their finances by teaching them how to build and live on a budget, how to keep track of finances and how to rely more on cash as an effective method to manage spending.

Christians Against Poverty's experience at helping some of New Zealand's most vulnerable families gives us unique insight into the importance of cash to provide security to those on low incomes or those in financial hardship, and of the importance of cash to help manage and keep track of expenditure.

Feedback on proposal for rate cap on high-cost loans

Question 1: Do you have any comments on the high-level prohibitions for the rate cap? (Section 45D(1), (2) and (3).)

CAP would take this opportunity to reiterate the comment made by our CEO Aimee Mai when the rate cap was first announced.

“An interest rate limit is a step in the right direction. However, it's worth noting 0.8% per day is still effectively an annual interest rate of 292%. At this rate a \$500 loan costs over \$28 a week in interest alone. For many of our clients, that's the difference between being able to afford school uniforms or having to take out another loan.”

CAP believes that the proposed rate of 0.8% per day is still very high. High-cost loans are very often last-resort borrowing and are sought to pay for household necessities. We would like to see this rate lowered so that those in poverty and hardship can conserve the little they have to better support their households.

Question 2: Do you have any comments on the proposal to allow loans that would breach the rate cap only as a result of the borrower repaying it early? (Section 45D(6).)

CAP appreciates the desirability to ensure no creditors are breaching the rate cap just because a borrower chooses to repay their loan early.

We do note, however, that every effort should be made to ensure that lenders do not seek to take advantage of this. One could imagine, for example, lenders offering and perhaps even advertising some form of incentives or discounts for early full repayment in order to avoid being in breach but still being able to charge in excess of the rate cap.

Question 3: Do you have any comments on the proposal for simple interest? (Section 45E.)

CAP is supportive of the proposal to prohibit compound interest for high-cost loans.

Question 4: Do you have any comments on the consequences of breaching the rate cap provisions?

In a broader sense, any penalties need to be an effective deterrent of unwanted behaviour and appropriately compensatory to the affected party. As high-cost loans are often for smaller values, CAP believes that statutory damages equal to the lower limit of 5% of credit provided may not be appropriately high enough to sufficiently deter breaches. Additionally, the lower limit of 5% may not appropriately compensate a debtor when the value of high-cost loans is often relatively low.

Question 5: Do you have any feedback on the impact of confining the rate cap to high-cost consumer credit contracts?

CAP prefers this new definition of “high-cost consumer credit contract” which captures the total rate of all interest charges to that in the bill first drafted.

Question 6: Do you have any examples of contracts that would be below a 50% annual interest rate but break the 0.8% per day rate cap? How common is this?

The time permitted for this submission hasn't allowed for in-depth analysis, but we cannot find any examples to hand that would evidently meet the concern raised in point 14 of the draft proposal.

Question 7: Are there any other changes that you would make to the definition of "high-cost consumer credit contract"?

CAP is in favour of any changes that will comprehensively limit the **total costs** payable under consumer credit loans. Including all fees as well as interest ensures that people are getting better total protection. CAP anticipates that limiting interest rates will be met with lenders looking for new ways to maximise other charges. Already in the marketplace, there are a myriad of fees associated with loans – some lenders charge both an "Account Setup Fee" and an "Account Establishment Fee". These terms are often confusing and difficult to compare for borrowers. They quickly add to the cost of borrowing and often aren't advertised up front. Research has shown that borrowers living in complex circumstances, like hardship, find making complex financial decisions difficult. Whichever ways the Select Committee recommends limiting the costs of borrowing, the impact should be across **all** costs.

Question 8: What are your views on including a default fee in the Bill? Are there any other options that you think the Committee should consider?

CAP submits that a default fee limit should be included in the bill. CAP's preference is in line with that presented in point 21; i.e. that a declaration that a certain amount is reasonable, and that the onus lies on creditors to demonstrate why they believe that it would be reasonable to charge more.

This concept should be extended to all consumer credit fees. The Commerce Commission should be awarded the powers to setup and update annually a 'schedule of fees' that sets a reasonable limit to common charges.

This would be the most effective way to meet the requirements of the bill as stated, to address the issue of unreasonable fees becoming problem debt.

While the *Sportzone* case was necessary to establish that reasonable fees must only be limited to costs incurred, CAP believes that the onus should lie on a creditor to demonstrate why their high fee is *not* unreasonable, **rather than** on the borrower which may only be established by a costly, time consuming complaint and investigation process involving consumer advocates and regulatory body involvement.

Vulnerable consumers and those in poverty and hardship often don't have the resources, the agency or the knowledge to be able to demonstrate that a fee is 'unreasonable'. This law reform presents an opportunity to protect the interests of these people that often don't have a voice for themselves. In this context, the burden of proving reasonableness should shift to the creditors rather than on debtors. An appropriate regulatory body should also be resourced to effectively engage with lenders and consumer advocates to be able to establish reasonable fee limits.

Question 9: Do you have any suggestions for the proposed rate of charge calculation, or preferred alternatives to this methodology?

CAP has no comment on this question.

Conclusion

CAP strongly advocates for the protection of New Zealand's most vulnerable. We see the terrible impact of problem debt on families who are often stretched to breaking point. We strongly agree with the intention behind the Act and the Bill to protect vulnerable consumers.

We reiterate the importance of defining high-cost lending by including **all** costs associated with borrowing. We also reiterate the importance of shifting the responsibility of proving that a charge is unreasonably expensive away from the borrower and regulator and moving it towards lenders to demonstrate why it would be reasonable to charge more than an accepted standard.

Thank you for the opportunity to provide our feedback on this interest rate cap. We are happy to remain a point of further consultation in this process.