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To the Finance and Expenditure Committee

Select Committee Office

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Secretariat: fe@parliament.govt.nz

Submission to the Finance and Expenditure Select Committee on the Credit Contracts Legislation Amendment Bill

Date: 14 June 2019

Name:

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Position:

Chief Executive

Organisation:

FinCap

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Foreword

2018 was the first time I ever took a payday loan. I'm a solo mum, my kids have their birthdays really close together and the budget was tight. I'd tried to save for it but there'd been some unexpected costs. I didn't want to let them down, so I borrowed $400. It was easy. I went online and had approval in a matter of minutes. I'd have to pay back nearly twice that but that was going to be OK once things picked up. I made the first couple of payments, they were big - nearly a quarter of my weekly income but then I missed one.

The penalties were bad but the rate they wanted repayment made at was worse - it was huge because the interest rate was huge. There were weeks where I was choosing between paying for electricity and paying for food. Meeting the loan repayments was the most important thing because having a bad debt against my record would have cost so much more in the long run.

In the end it got to the point where I was begging the lender to send the debt to a debt collector. The extra 20 or 30 percent added was worth it just to be able to pay it off over a longer period of time. They refused.

It only turned around when I finally got the local budgeting service involved and they made the lender send the debt to a collector. I'm almost debt free now, but it's come at a real cost to me and my kids.

This year, on my birthday the loan shark I borrowed from sent me an email that said something like "Happy Birthday Sarah - how about you treat yourself with a loan"? I felt ill.

I've looked at the changes this law will make, and I've put them up against my experience. They would have helped a bit, but they wouldn't have made the total cost of the loan less than it was to start with. The payments I had to make wouldn't have been any smaller. Maybe some of the penalties would have been smaller but I only just missed that third payment. If things had been a little different I could have paid it all back on time. Maybe at the cost of my kids' breakfasts and a couple of disconnection threats. Lots of people do.

If I had, I don't know if I would have said no when they offered me a new loan, or another after that. There's always a bill that needs to be paid, especially when you've been tightening the belt to pay the last loan. What I do know is my family would be a lot worse off for it.

I also know that a lot of other people are hurt by this kind of lending too. That's why I'm speaking out. It's not easy to tell my story so publicly. Being "bad with money" is seen as a shameful thing in New Zealand, but it's not as shameful as the way people like me are being preyed on by this industry. Please, make sure that this law change stops that.

Sarah Newham, Gisborne

Mother and (ex)Borrower

Executive summary

- Before 1999 high cost short term loans did not exist in New Zealand.
- The interest and fees from short term high cost loans take $120m a year out of the household incomes of mostly low-income New Zealanders.
- The current proposed Credit Contracts Legislation Amendment Bill (the Bill) contains many positive measures.
- However, the absence of an interest rate cap means those measures will not adequately protect borrowers.
- In particular, the proposed total amount repayable limit needs to be accompanied by an interest rate cap, as these are complementary measures.
- FinCap is aware of the concerns that an interest rate cap may leave a shortage of available credit and/or create a black market. Research has shown this has not been the result of the implementing of a cap in the UK or Australia. There is no evidence this would be the case in New Zealand.
- A great deal of the harm from predatory lending is caused by the size of repayments rather than the total cost of the loan itself. The total amount repayable limit will not address this unless it is accompanied by an interest rate cap.
- In addition to an interest rate cap FinCap believes changes to the Bill should include:
    - A percentage of borrowers' income protected from predatory loans,
    - A series of changes made to support enforcement,
    - The Bill's definition of retail trucks used to prohibit them,
    - The regulation of debt collection.
- A comprehensive summary of recommended changes is provided on pages 13 to 16 of this submission.

Who we are

FinCap (the National Building Financial Capability Charitable Trust) is a registered charity and the umbrella organisation supporting the work of local free financial capability and budgeting services in New Zealand. We do that by training Financial Mentors, hosting and analysing data from client interaction, supporting networking, and communicating and advocating around issues affecting those services. We receive around 75% of our income from Government.

Local financial capability and budgeting services

For over half a century New Zealand has had a network of local agencies committed to providing budgeting support to people in hardship. Now they comprise 200 distinct services delivering from over 316 locations spread nationwide. They are tasked with increasing New Zealanders' financial capability through providing one-to-one financial mentoring, peer-to-peer learning and community education.

Working at scale with New Zealanders in hardship

In 2018, 70,800 people received the service described above – a minimum one-hour kanohi ki te kanohi/face to face with a Financial Mentor, with follow-up advocacy and support. Often those sessions are repeated, and often referrals are made to mental health, addiction and related services. Budgeting services are gateway by nature – to other specialist support to address the driving cause or causes of financial hardship, and to a more hopeful financial future.

The financial scale of the issue we see is numbing. Those 70,800 people (often there on behalf of a whānau/family) represent around one in three New Zealanders living in poverty. 41% of service users are Māori, as are 32% of our 1200 Financial Mentors.

The law matters

Most of these local services are reporting that significant resource is being diverted from the task of building financial capability to deal with the growing personal crises caused by predatory, irresponsible and high cost lending. Getting the law right in this area is crucial to our network.

How we have worked in preparing this submission

There have been three rounds of engagement with the 200 services in our network, the first two in 2018 as MBIE developed proposals for law reform. A total of 110 services contributed to our submissions through that process. We held 11 hui nationwide in early 2019 to inform services of the content of the Bill, and to seek views on priority issues. This submission is based on what came out of that. Please not that all our activity in relation to the law reform is funded by non-government sources, in this case the Borrin Foundation and JR McKenzie Trust.

Our strong feelings on these issues are certainly not held by us alone. There are currently fourteen national organisations who have joined the coalition calling for an interest rate cap. These are: Iwi Chairs Forum, Age Concern1, Child Poverty Action Group, Christian Budgeting New Zealand, Christians Against Poverty, Citizens Advice Bureau NZ, Community Law Aotearoa, Family Works, FinCap, Good Shepherd NZ, Ngā Tangata Microfinance, NZ Council of Christian Social Services, The NZ Council of Trade Unions (including the CTU Komiti Pasefika) and The Salvation Army. In addition, we have cooperated with Victoria University of Wellington,2 the University of Canterbury,3 and Community Law Canterbury, in generating research and insights around this significant law reform.

We are grateful for the opportunity to submit on the Credit Contracts Legislation Amendment Bill. We wish to be heard by the Committee on this submission and request that we immediately precede or follow the Iwi Chairs Forum' appearance.

[1] See comments from Age Concern on this Bill in **Appendix 1**

[2] We would like to thank Victoria Stace from Victoria University of Wellington, whose tireless efforts have informed the drafting of this submission and the proposals we have made.

[3] We would like to thank Professor Jeremy Finn from The University of Canterbury, who has also submitted on the Bill and whose suggestions we endorse and have included in our submission. In summary, Professor Finn has submitted on issues around the commencement dates of various aspects of the Bill, verification of information provided by borrowers particularly in an online environment, charging for provision of records, some aspects of disclosure, the onus of proof in relation to reasonableness of fees, and has noted some serious issues with the proposed total amount repayable limit.

The problem of high cost and predatory lending

In her first Speech from the Throne, in October 2017, new Prime Minister Jacinda Ardern used the word "child" or "children" 22 times, mostly when talking about countering child poverty. We were incredibly hopeful. The 200 budgeting services we work with are up face-to-face with poverty and hardship and see a steady stream of debt-driven child poverty. Together with the campaign commitments from Coalition Government partners to crack down on loan sharks, we felt that that stream of misery might finally dry up, with the huge repayments to loan sharks that have been taking food and warmth from our children in struggling households finally being curtailed.

As drafted, the legislation this submission is addressing will not achieve this.

This is not because of what the legislation contains. In fact, we welcome all the changes being made. Most of this submission consists of modest amendments and recommendations relating to the law that Parliament passed at First Reading, now being considered by your Committee. Rather, this law will fail in its intent essentially because of one pivotal omission. It lacks an interest rate cap on high cost loans.

Interest and fees on high cost short term loans cost New Zealanders $120 million a year. That money is coming out of some of our poorest households. It is $120 million being diverted from children's meals, from rent payments, from prescriptions, from the absolute basics. Research from Australia shows that single parents are over-represented in high cost borrowing statistics.[4] The experience of our budgeting services indicates this is the case in New Zealand as well.

Unlike pawning or even general non-bank lending, high cost short term loans also known as payday lending[5] are a new phenomenon, born of the growing inequities in society. In Australia the first pay day loans appeared in 1998, and they had emerged in New Zealand by 2000. Life went on before then, and our argument is that life was a lot better without them. And it could be again.

Loan sharks' profits are like a hole in a bucket. The more that is put back into the home budgets of low-income New Zealanders - whether it be from minimum wage increases, Working for Families boosts, equal pay settlements, or increased welfare payments - the more that flows straight out to predatory lenders. Indeed, many local budgeting services report that lenders are using such

[4] See Banks, Marston, Karger and Russell "Caught Short, Exploring the role of small short-term loans in the lives of Australians" August 2012, at 19.

[5] High cost loans with interest rates over 50% per annum taken over short periods of time.

Government-initiated increases in income as a marketing opportunity to sell more toxic debt, or as a reason to pursue higher repayments.

Such approaches are all in a day's work for an industry that has shown itself to be nimble and rapacious. It practises data-matching and profiled targeting in the search for maximum profit and makes heavy use of online marketing tools backed up by TV and radio advertising. Many lenders' contracts contain fine-print permission for wage deductions - something that borrowers often do not discover until they find their pay-check short. Predatory lending is no longer the preserve of small dubious outfits from "the wrong side of the tracks". It is a large and sophisticated business that is predicated on taking money from those who need it most. Online lender Moola, for example, has repeatedly figured in Deloitte "Fast 50" list of growth companies and was celebrated as showing "incredible business growth". That's a fact given their 557% revenue growth last year. It is worth noting that Moola is one of the companies practising wage deductions (See **Appendix 2** for a sample wage deduction authority).[6]

In the UK, lender websites advertise interest rates of no more than 0.8% a day, since that is the interest rate cap operating there. That's a clear example of what the UK Government have done to protect their citizens – they have introduced an interest rate cap. In New Zealand, the Moola website states "***Loan Amount $100 - $1000, Loan Term 2 - 44 days*** *Interest is charged at 1.70% per day on the unpaid balance at the end of the day.*"[7] The difference in interest rates is because such a cap does not apply in New Zealand. Your Committee can change that.

The **total amount repayable limit** already included in the Bill (see new section 45A) is insufficient because if people pay back the loans on time, the repayment limit is unlikely to be reached. While they may pay back less than twice what they borrow, the interest rates are so high that the weekly repayments are difficult to keep up with. Often, repayment of that loan creates such financial pressures that further borrowing is required.

"The first loan free" is a common tactic designed to weed out the non-payers from the deep rich veins of follow-up business. This comes at the cost of higher interest rate loans for those who do pay, and harmful credit ratings for those who should never have been offered a loan in the first place. Many of

[6] Save My Bacon is also another high cost short term lender who uses wage deduction authorities. Save My Bacon requires the borrower to sign a wage deduction authority before the money under the loan is released.
[7] https://www.moola.nz/Static/Fees

those people end up being pursued by a debt collector,[8] who are able to add debt collection fees to the amount payable.

Given the way in which the Bill is currently drafted, it will not curtail the impact of loans that currently fall outside of the total amount repayable limit. Avoidance of the proposed law intended to stop one loan being used to refinance another would be easily achieved via cooperation between "unrelated" lenders. Further, there will only need to be a day-long gap between one loan and another for them to be considered separate under the law.[9] Enforcement would be heavily reliant on self-reporting by borrowers who are already (almost by definition) lacking agency, information, and power. In reality, the reporting to the Commerce Commission and dispute resolution services of potential breaches of the limit is primarily undertaken by Financial Mentors who are uniquely engaged with many of the borrowers.

The addition of **an interest rate cap** would change all of this. Lenders would not be able to receive double the amount of a loan in a matter of weeks. Enforcement would be as simple as identifying loan offerings over the cap - there wouldn't even need to be a borrower, and since most loans are now obtained online it would be easily discoverable. The limiting of revenue and profit would mean offerings of " a free first loan" would come at the expense of the lender, not the borrower. There is plentiful precedent. 76 nations including the UK, Canada, and Australia implement an interest rate cap on high cost loans and we have been unable to find a country that imposes a total amount repayable limit, as proposed by the Government, without also implementing an interest rate cap.[10]

We would also like to see **the protection of a portion of borrowers' income from interest payments on high cost loans** to ensure that loan repayments are contained so there is always money available to meet basic needs.

Indeed, the three measures (interest rate cap, protection of a portion of the borrower's income and total amount repayable limit), along with properly enforced protections for borrowers, form the foundation of sensible, best practice, regulation of the high cost loan market. Omission of any one of these three measures effectively creates a way to circumvent the effect of the other two.

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[8] On average, across a sample of 76 agencies, it appears that around half of clients with high-cost loans have been referred to a debt collector. See Dr Liz Gordon Research Report: Survey of financial mentoring and budgeting services in Aotearoa on high cost loans, debt collection and other consumer credit issues (Community Law Canterbury and FinCap, February 2019) at 24 (Attached as **Appendix 9**)

[9] The Bill refers to there being an unpaid balance "at all times" so the gap between one loan and the next could be even less than one day.

[10] A list of countries that have interest rate caps, taken from research done by the World Bank in 2014, is attached as **Appendix 3.**

While the inclusion of an integrated approach including an interest rate cap is critical, there are other aspects of the Bill that FinCap would like to see changed. These include **the prohibition of mobile traders** - something that is now achievable with the Bill's definition of a "mobile trader". This is a fundamentally abusive phenomenon not seen in other countries, because of our loosely worded legislation. However, we note that traders which are operated by a non-governmental organisation should be exempt from this ban because they sell at retail prices and interest free, which does not create the same harm as for-profit mobile traders.[11]

We also want to see **clarity around the way lenders are required to present the cost of their products to borrowers**. As it stands some lenders are legally able to present their interest rates as simple rates when they are in fact compounding. By way of example, 1% per day at a simple rate is 365% per annum. Compounding daily, it is in the order of 3780% per annum. That difference needs to be made clear to borrowers and such clarity is a fundamental consumer right.

We also seek a **prohibition on high cost lenders being allowed to take deductions via a wage deduction authority over the debtor's wages.** It is not appropriate that the high cost lender gets to take its repayments before the borrower can decide the priorities for bill payments, especially given that many borrowers are struggling to meet basic living expenses.

None of these are unreasonable asks from a Government that has said it wants to "take a tough stance on loan sharks".[12] These asks are in line with international practice, they are strongly supported by frontline services, and their effectiveness is demonstrated by a considerable body of research, referenced and or appended to this submission.

We acknowledge that there is more work to be done to meet the needs of those who are unable to meet the basic living expenses and might be currently tempted to turn to a high cost loan. Provision of a high cost loan is, however, not the answer and mostly leads to a worse financial situation, when the borrower finds they are not able to keep up with the repayments on top of all their other expenses.

This submission tells the stories of ordinary New Zealanders who have been supported by those 200 local services, and each story highlights the strength of the arguments for change. The human impact of all this is fundamental. Seldom does the opportunity arise to do good so clearly and so easily. Please, take this opportunity.

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[11] For example, The Salvation Army operates a mobile trader named "The Good Shop" which provides groceries, household and personal items at store prices on interest-free terms. https://www.salvationarmy.org.nz/get-help/welfare/good-shop

[12] "Government crackdown on loan sharks" (press release, October 10, 2018). http://www.scoop.co.nz/stories/PA1810/S00087/government-crackdown-on-loan-sharks.htm

Summary of recommendations requiring amendments to the Bill

We have three key and interrelated "asks" in relation to the Bill. They are:

- For an interest rate cap (more properly referred to as a "total cost of credit" cap, as it would include both interest and fees on the loan);
- For a protected earnings cap (meaning that a lender would be prohibited from lending in circumstances where a borrower would be committing more than a certain percentage of their income to high cost loans); and
- For strengthening of the total amount repayable limit that is already included in the Bill, so that it is harder to avoid.

One woeful failing related to the current legislation has been poor monitoring and enforcement of the intention of the law. These three measures would, in combination, transform that by providing three firm, enforceable prevention interventions which would have a massive impact in reducing harm to those in hardship.

These "asks" are summarised in the following paragraphs and elaborated on in the body of this submission. We have several other "asks". Some of these complement an interest rate cap. Some are measures that will assist with enforcement. Others relate to debt collection.

- The Bill should be amended to allow for **a limit to be set (via regulation) on the total cost of credit in relation to a high cost loan (an interest rate cap)**. The Bill should also prohibit a lender from offering or providing a high cost loan which exceeds that limit. A power to impose a total cost of credit limit by regulation should be added to s 138 of the Credit Contracts and Consumer Finance Act 2003 (the regulation making power). This submission will refer to this total cost of credit limit as an "interest rate cap", but the cap we are asking for is broader than just applying to interest, as it would cap interest and fees payable during the agreed loan duration. We elaborate on our reasons for asking for an interest rate cap in the next section of this submission.
- The Bill should also include **a protected earnings cap** under which a lender could only lend in circumstances where a borrower was not committing more than 10% of net income to repayments under high cost loans. This can also be done by regulation. This measure would draw a firm line aligned closely with the lender responsibility principles. We note that MBIE

found in its review that there were high levels of non-compliance with those principles by high cost lenders.[13] This single measure would address that.

- **The total amount repayable** limit that is already included in the Bill (see clause 22 and new section 45A). We submit that it should be strengthened to reduce the opportunities for lenders to avoid its application. At present the total amount repayable limit could quite easily be avoided and would merely add to the complexity and ineffectiveness of legislation in this area.
- On behalf of our services **we also ask that serious consideration is given to extending the total amount repayable limit (under which a borrower can never be required to pay back more than twice what they borrowed, including all interest, fees and default fees), to loans below the high cost threshold.** Services see harm being caused by loans below the high cost threshold on a regular basis, in particular finance company loans, consumer finance loans and bank loans. Introduction of a total amount repayable limit on all these types of loans would greatly assist with protection of consumers.

The following additional measures would **support an interest rate cap** and would help address the high rates of non-compliance with the lender responsibility principles:

1. Anti-avoidance provisions;
2. A general prohibition on irresponsible lending; *and*
3. A requirement that lenders advertise the annual percentage rate (APR) of loans offered, based on either a compounding interest rate (if the lender charges compounding interest) or simple interest (if the lender charges simple interest).

Certain specific reforms should be included in the Bill to assist with enforcement. These are:

- **All lenders should have to have a designated compliance officer** who is responsible for ensuring that all Credit Contracts and Consumer Finance Act (CCCFA) obligations are complied with;
- Where **a borrower is in default on a high cost loan within 1 month of taking out a high-cost loan**, the lender should be obliged to self-report the matter to the dispute resolution scheme with which they are registered;
- All high cost lenders should be subject to a rule that **before the lender agrees to make a high cost loan to a vulnerable borrower it must have been provided with a budget** for the borrower prepared by an independent person such as a Financial Mentor; and

[13] See MBIE's "Review of consumer credit regulation: Additional information to support the discussion paper" at 25.

- **A rebuttable presumption should be included in the prescriptive requirements around affordability assessments** (which are to be in regulations) that a high cost loan is presumed to be unaffordable if the borrower is in default under another high cost loan or has held two or more other high cost loans in the past 90 days (similar to the rebuttable presumption that exists in Australian small amount credit contract law).

In relation to **debt collection**, this submission supports the disclosure requirements being introduced in the Bill and has two specific and additional requests.

- The first is that all debt collectors that collect debt under consumer credit contracts be brought within the scope of the CCCFA. This can be done by using the call-in power in the regulations (see clause 43 of the Bill, new section 138 (1) (abc)). Specifically, we ask that the regulations currently being drafted include a regulation declaring debt collectors that act as agents of the creditor to be themselves "creditors under a consumer credit contract."
- The second is that your Committee should recommend that primary legislation be developed and introduced to apply to and regulate the activity of all debt collectors of consumer debt. This legislation would either directly enact law or would empower the promulgation of a code/guidance that would, in either case, set out good practice for all debt collection in relation to consumer debt, as exists in Australia, the UK and the USA.

Finally, there are **a range of measures that we would like to see included in the Bill to address issues that local budgeting services are frequently seeing commonly in association with high cost lending, or to strengthen the reforms included in the Bill**. These are:

- Mobile traders should be banned;
- If mobile traders are not banned then they should be made subject to the CCCFA;
- If mobile traders are not banned then "do not knock stickers" should be legally enforceable;
- 'Buy now pay later' products should be treated as consumer credit contracts;
- The 'reasonable fees' provisions should be made more easily enforceable;
- There should be more prescription around affordability assessments;
- Certain types of payments to borrowers should be excluded from income for the purposes of doing affordability assessments;
- Wage deduction authorities should be banned;
- Direct debit authorities should not be permitted in relation to loans to beneficiaries;
- Lenders should have to make disclosure in a prescribed format;

- Clauses in the Bill allowing the court to reduce the effect of disclosure failure should be deleted;
- Lenders should have a responsibility to make borrowers aware of avenues for making complaints or seeking help;
- An obligation should be placed on lenders to cooperate with people advocating for borrowers;
- Use of funds from infringement fees and unclaimed money from settlements to go MBIE;
- Advertising of high cost loans should be banned;
- Public notification should be introduced for people applying for fit and proper person certification;
- The new due diligence requirements on directors and senior managers should be strengthened; and
- High cost lenders should be required by law to provide information on their business to the regulator on an annual basis.

Reasons why we are asking for an interest rate cap

The issue of an interest rate cap has come before Parliament before, most recently in 2014 when the Credit Contracts Consumer Finance Act (CCCFA) was last amended. At the Select Committee stage of the Bill going through, the minority report from Labour and the Greens supported an interest rate cap for the same reasons outlined in this submission.[14] In 2017 the incoming Minister of Commerce asked MBIE to review the changes to the law that had been made in 2014. That review looked at whether those law changes had been effective in reducing the harm from irresponsible lending. There was a specific request from the Minister of Commerce to consider interest rate caps. It is important to note that the conversation about interest rate caps was initiated in this term of Parliament by the Minister of Commerce.

The primary purpose of the Credit Contracts and Consumer Finance Act 2003 is "to protect the interests of consumers in connection with credit contracts, consumer leases, and buy-back transactions of land".

The changes in the Bill increase the protections for consumers from predatory lending in a range of ways. We warmly support these changes. However, this Bill as it is currently drafted does not adequately address the harm caused to consumers by predatory lending, high cost loans and irresponsible loans. We are particularly concerned about the absence of an interest rate cap in this Bill to protect people from making expensive repayments which frequently drive them into a debt spiral.

It is a misconception that the limit on the total amount repayable (we call this the total amount repayable limit in this submission), which is included in the Bill, is a substitute for an interest rate cap. They serve different and complementary purposes. Without a total amount repayable limit, an interest rate cap would likely result in longer running, more expensive loans, as well as borrowers getting into debt spirals caused by default fees and penalty interest.

However, without an interest rate cap, a total amount repayable limit will cause or at least allow the interest rate to be excessive and will encourage short very high cost loans. There is also nothing to stop the lender repeat-lending at an excessively high rate of interest to a person that has repaid one

[14] Credit Contracts and Financial Services Law Reform Bill Commentary - http://www.legislation.govt.nz/bill/government/2013/0104/23.0/DLM5998204.html

high cost loan, meaning that in effect a series of short-term high cost loans can be made without ever encountering the restrictions imposed by the total amount repayable limit.

We consider that the most important change required to the Bill is the addition of an interest rate cap. It is important to note that when we refer to an "interest rate cap", we mean a cap on the cost of credit under the loan which includes both interest and fees charged during the agreed loan duration. This is sometimes referred to as a total cost of credit cap.

It is not enough simply to impose a cap on interest as that creates an incentive for the lender to impose high fees, while staying within the interest rate cap. The cap must cover both interest and fees (for example, establishment and administration fees) payable on the loan. This is how the UK interest rate cap works – in the UK there is a cap of 0.8% per day on high cost loans and that includes the interest and all fees payable during the agreed duration of the loan.[15] We note the requirement for fees to be reasonable under the current legislation and the strengthening of this requirement under the Bill. Problems were identified with the current provisions by MBIE and we do not consider the law requiring fees to be not unreasonable is strong enough to justify excluding fees from a cap –so we are asking for a total cost of credit cap that includes interest and fees.

What are the benefits of an interest rate cap?

The cost of borrowing reduces

High cost loans are a toxic product. Even if repayments are, in total, limited to twice the amount borrowed, the loan will result in harmful repayment levels if that limit is squeezed into too short a period. To use an example that is quite ordinary by payday loan standards, a $500 loan resulting in a $1000 debt that is to be paid in eight weeks results in repayments of $125 per week at simple annual interest rate of 650%. The removal of $125 from a low-income household's weekly budget can have a very significant effect, especially when it comes week after week. Often the result of managing to meet these loan repayments is that borrowers feel the need to take a new loan to "catch up".

The proposed total amount repayable limit will do nothing to limit this level of interest charges where the loan is for a short term. An admittedly extreme example is provided by the practice recorded by

[15] Default charges are subject to their own separate cap under the UK regime. Under the Australian regime, the only limit on the default fees that can be charged is that the total amount payable on default cannot exceed twice the amount borrowed.

the District Court in *Commerce Commission v Twenty Fifty Club Ltd* [2016] NZDC 7242,[16] where loans were for only seven days, at a "fee" of 50% of the amount borrowed. That gives an annualised simple interest rate of over 2600%. The total amount repayable limit may well not lower interest rates but instead encourage creditors to shorten the terms of loans made to maximise the effective interest rate.

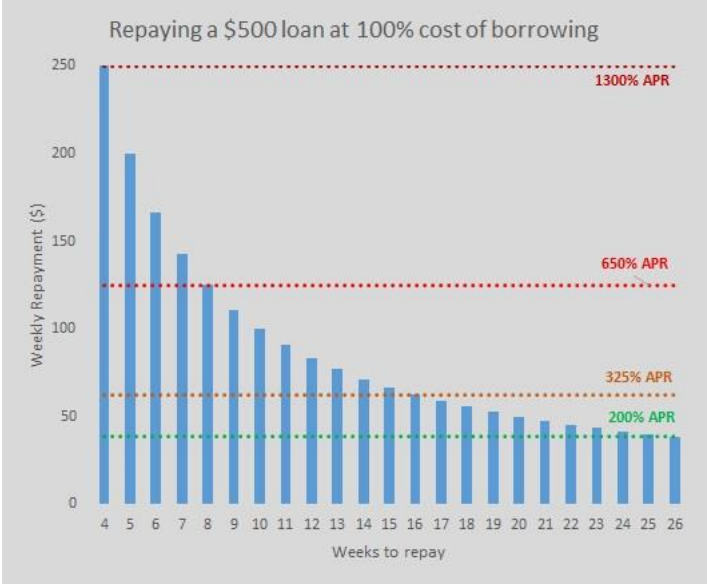
Other examples of high interest rates by payday lenders (based on a review of lenders' websites done in June 2019) are CashTillPayDay, who charge 693.5% pa or 1.9% per day. Cash Burst also charges 693.5% pa or 1.9% per day. Moola charges 1.7% per day or 620.50% pa. Save my Bacon charges 1.5% a day, or 547.5% pa. Cash Converters charges 480% pa. In all cases the annual rate given is based on simple interest being charged. Some of these lenders charge compounding interest, meaning that the true annual interest rate is a lot higher.

In some respects, the borrowers who default can be considered the lucky ones. Many borrowers have told our budget services that getting a loan referred to a debt collector can be a relief despite the additional collection fees and potential extra interest it attracts, as it gives them time to pay and some breathing space. Often default comes after several loan payments have been made at significant cost to the borrower and their whānau/family. However, we do not wish to downplay the serious issues that currently exist around debt collection practices. These are discussed later in the debt collection section of this submission. The fact that many borrowers prefer the debt to go to debt collection despite the serious issues around harassment and high fees (in particular) associated with debt collection just emphasises the level of pain being caused by high cost loans.

The simplest way to fix the excessively high rates of interest being charged is with an interest rate cap. In the example above, if the total cost of interest is halved to 325% the time to repay doubles and the amount taken from the borrower's weekly budget halves. The lower the interest rate cap the longer time the borrower has to pay and the less the loan repayments take from the borrower's weekly budget.

[16] *Commerce Commission v Twenty Fifty Club Ltd* [2016] NZDC 7242 at [31]-[36].

Fig 1. Graph of interest rate vs repayment period with total amount repayable limit in place



Note: APR is based on simple interest rate

Fig 2. Example of a Payday Loan Calculator – Save My Bacon

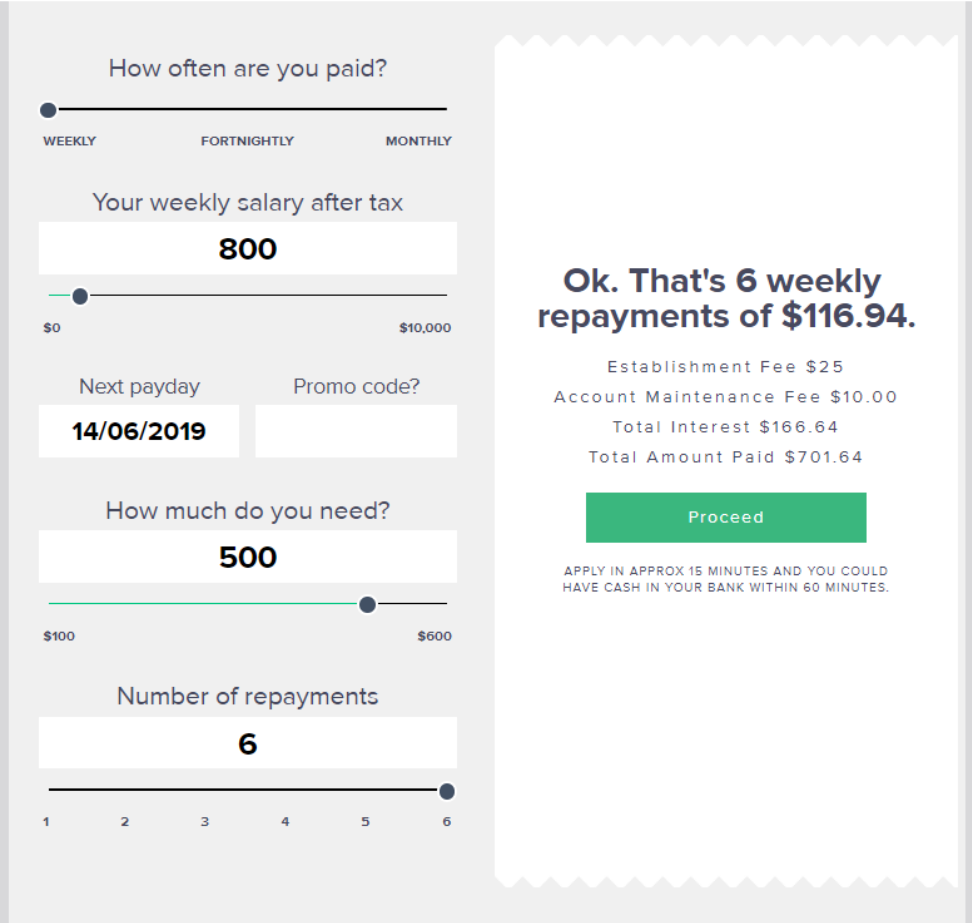
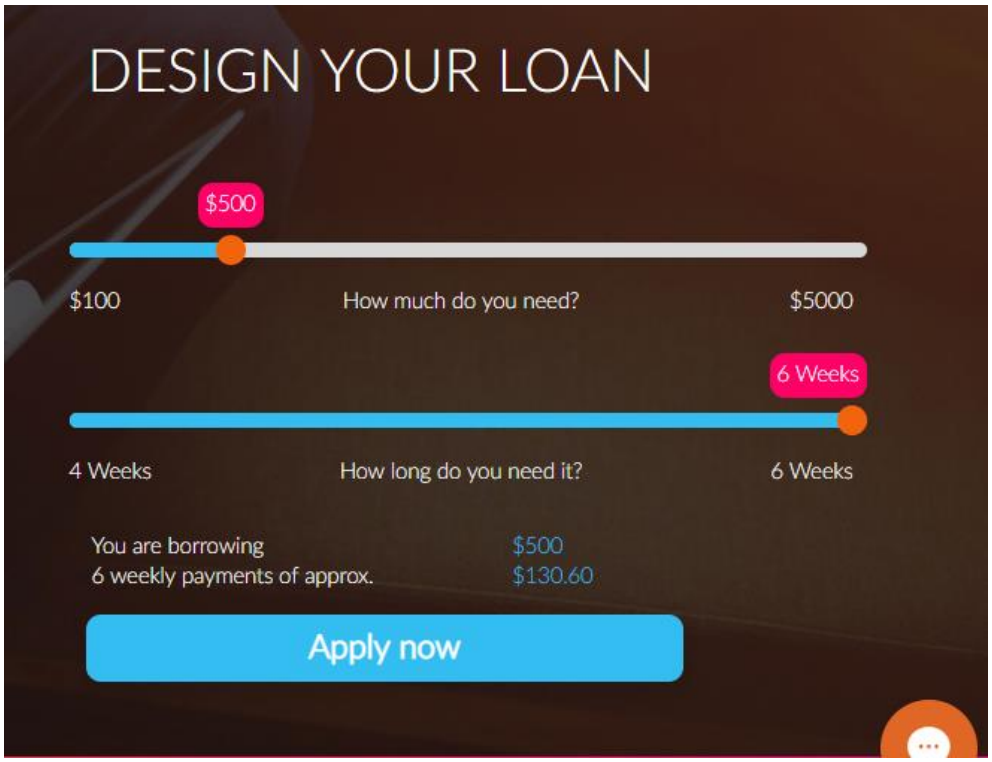


Fig 3. Example of a Payday Loan Calculator – Moola



Loan Amount $100 - $1000
Loan Term 2 - 44 days

Interest is charged at 1.70% per day on the unpaid balance at the end of the day

620.50% Annualised Interest Rate (AIR)

Establishment Fee: $21.23

Cancelling a direct debit: $20.00

Defaulted Fee: $20.08

Direct Debit Fee: $1.92

Debit Card Payment Fee: $5.42

Extension Fee: $11.12

Manual Payment Fee: $0.62

Veda Lodgement: $20.00

Wage Deduction Fee: $29.78

Proactive enforcement is enabled

An interest rate cap is more easily enforced than most protections currently available to borrowers.

Unlike enforcement of the responsible lending obligations, or the proposed total amount repayable limit, the regulator does not have to insert themselves into a pre-existing relationship between a borrower and a lender to enforce an interest rate cap. The test for enforcement is simple: "Does the rate offered (inclusive of fees) breach the cap?"

In the case of the responsible lending obligations, enforcement depends on borrowers making a complaint or the Commerce Commission being proactive in taking investigations to uncover irresponsible lending. Borrowers are unlikely to make a complaint, due to either lack of knowledge of their rights, stigma around the situation they are in or reluctance to damage a relationship with a lender. In addition, it is only after a borrower is approved for finance that the law can be applied.

The responsible lending obligations and the proposed total amount repayable limit are very important measures. However, they are both largely reactive and to be applied, rely on significant auditing of contracts or on self-reporting by borrowers who may not feel they are able to engage in a dispute with the lender or to approach the regulator. In the case of the total amount repayable limit, breach will often only be determinable after the loan contract is struck and the repayments have been billed.

By contrast, enforcement of the interest rate cap can be done proactively. If lenders were required to disclose an APR (annual percentage rate) for the loan (which would include interest and fees) then it will be clear if the rate offered by that lender falls below a cap (that is based on an annualised rate). Alternatively, if the cap is based on a daily maximum rate, then lenders would be required to disclose the daily rate of the loan - again clearly showing if the cap is breached or not.

Irresponsible lending would reduce

For many lenders (in particular high cost lenders) there is little incentive to lend responsibly. Indeed, rather than implement time-consuming and costly assessment of borrowers' ability to repay, high cost lenders can take a prospecting approach of using the first loan as a test. Because individual loans are quite small by revenue standards and there is no cap on the interest rate that can be charged, the losses made by writing off loans can be bundled into the cost of loans that are repaid. Borrowers who default have their credit rating damaged. Borrowers who do not default pay for borrowers who do - usually through a higher interest rate.

An interest rate cap removes the headroom available for companies to pass this loss on. By passing the cost of defaulting to the lender it provides a financial incentive to the lender to lend responsibly.

Analysis done by the Association of Chartered Certified Accountants in 2014 (the ACCA Study) on the online payday lending market in the UK prior to the introduction of the UK interest rate cap regime in 2015 found that lenders' incentives to, on the one hand, lend responsibly and, on the other, make profits, are not aligned.[17] This research looked into the business model of payday lenders, with a focus in particular on online lenders. Relevant key findings were as follows:

- The key costs of an online high cost lending business were customer acquisition costs and loss rates.
- High customer acquisition costs (including, for example, advertising and processing costs, and potentially lead generator[18] costs) mean that repeat lending is more profitable than new customers.[19]
- A high interest rate makes it harder for the borrower to repay in full, but, coupled with low financial capability, makes the borrower more likely either to roll over or return for another loan within a relatively short time frame.[20]

The research stated that "profitability is dependent on repeat lending".[21]

The ACCA Study asked why a business which takes on only new borrowers with a high probability of repayment is not automatically more profitable than one which takes on new borrowers with a low probability of repayment. It concluded: "*The answer seems to lie in the trade-off between incurring the costs associated with performing meaningful Affordability Assessments and incurring the costs of higher defaults on small first loans.*"[22] In other words, "*it makes perfect business sense to lend to people who will not pay back as long as lenders do not keep on lending to them. If a subset of repeat borrowers are generating the lion's share of the loans (and paying an extremely high total cost of credit as a result), this would make it possible to operate profitably while taking on new borrowers with very*

[17] Payday Lending - Fixing a Broken Market, Association of Chartered Certified Accountants, May 2014 (Fixing a Broken Market), at 38.
[18] Lead generators are third parties who source borrowers' details and sell them to the highest bidder.

[19] Fixing a Broken Market, n17, at 12 and 27. An Australian study undertaken in 2015 entitled Trends in the Small Loans Markets also found that high cost lenders make their money from repeat lending, stating that "A common characteristic of all small loan business models is that, because start-up costs are high and margins low, SACC revenue lines only tend to become profitable after the second or third loan." "Profits are overwhelmingly derived from chronic borrowers and the international industry is built around maximising repeat business" See pages 6 and 36 of Trends in the Australian Small Loans Market, Australian Centre for Financial Studies Commissioned Paper Series, Oct 2015.
[20] Fixing a Broken Market, n17, at 39.
[21] Fixing a Broken Market, n17, at 21.
[22] Fixing a Broken Market, n17, at 37.

high default probabilities."[23] "*The cost of defaults is borne ultimately not by lenders who operate profitably, but by borrowers in the form of high charges and fees*."[24]

The report of the ACCA Study stated:[25] "*When lenders do not suffer losses as a result of poor lending decisions they are incentivized to extend credit regardless of affordability, potentially a bad outcome for borrowers. This effect is magnified where loans are originated via 'lead generators' (third parties, essentially credit brokers, who source borrowers' details and sell them to the highest bidder), who are paid per loan written. Lead generators have no 'skin in the game' — they get paid regardless of whether or not the loan is eventually repaid."* There is evidence that lead generators operate in the high cost lending market in New Zealand, but they have not yet been the target of regulatory scrutiny.[26]

The report suggested that an interest rate cap would help because: "*Imposing a cap on the total cost of credit, assuming it is at least high enough to cover the operating costs of making loans, implies imposing a cap on losses due to default. A cap on the total cost of credit places an upper band on the amount of underwriting risk a lender can take in a much clearer and more straightforward way than a vague requirement to 'assess affordability'. A cap at the right level will also make loans affordable, enabling more borrowers to successfully repay in full and on time*."[27]

A 2017 review of the operation of the UK reforms (including an interest rate cap) found that there were no longer incentives for lenders to adopt business models that involve customers extending loans or otherwise failing to pay back in full and on time. In other words, following the cap regime in the UK, lenders are more likely to successfully collect the contractual interest payments, rather than relying on revenues from rollovers and late fees. This change in incentives has led to a greater focus on creditworthiness checks and affordability assessments.[28]

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[23] Fixing a Broken Market, n17, at 37.
[24] Fixing a Broken Market, n17, at 25.
[25] Fixing a Broken Market, n17, at 54.
[26] See the submissions to the June 2018 Discussion Paper of Save my Bacon and Moola – both these lenders wanted lead generators regulated.

[27] Fixing a Broken Market, n17, at 39.

[28] See "Impact of Regulation on High Cost Short Term Credit: How the Functioning of the HCSTC Market has evolved", Consumer Finance Association, March 2017, (Impact of Regulation on High Cost Short Term Credit), at 12.

Evidence of the positive impact of an interest rate cap

There have been concerns raised from some quarters that capping the interest rate may leave some high-risk borrowers unable to access the finance they require or encourage them to borrow from black market sources (i.e. lenders operating outside of the law). **Our research has revealed that introduction of an interest rate cap in the UK and Australia did cause a contraction in the lending market and made it harder for some people to borrow.** Those that were previously just eligible for a loan (in other words, those at highest risk of defaulting) were being denied a loan after the cap was introduced**. However, overall those borrowers considered this a positive result. There was no evidence that borrowers turned to illegal lenders.**

A 2017 Financial Conduct Authority (FCA) review of the UK regime, conducted after an interest rate cap regime was introduced, found that the outcomes for consumers were positive. Since the introduction of the cap, consumers pay less, repay on time more often and are less likely to need help from debt charities. Most consumers turned down for loans believed they were better off. There was no evidence of an increase in the use of illegal money lenders.

Specifically, the FCA 2017 review stated that:[29]

"We have found improved outcomes for consumers since setting the cap. Consumers pay less, repay on time more often and are less likely to need help with HCSTC[30] products from debt charities. Debt charities have also indicated that consumers are presenting themselves earlier and with lower debts, suggesting that underlying problems are being addressed sooner."

"We found no evidence that consumers who have not been able to get HCSTC products since the cap have generally had negative consequences as a result. The majority (63%) of consumers turned down for HCSTC products since the cap was introduced believe that they are better off as a result. We have not seen a significant 'waterbed effect' with consumers increasing their use of other high cost credit products after failing to get a HCSTC loan. We also found no evidence that consumers who have been turned down for HCSTC are more likely to have subsequently used illegal money lenders."

"While the market has got much smaller since 2014, many firms have been able to continue operating under the cap. There has been a slight increase in the number and value of HCSTC loans issued since its low point in 2015 and we see some evidence of stronger competition within the market."

[29] High-cost credit, including review of the high-cost short-term credit price cap, FS17/2 FCA, July 2017, (High Cost Credit Review), at [1.15-1.17].

[30] 'HCSTC' stands for high cost short term credit.

A 2017 paper prepared by the Consumer Finance Association, the UK industry body for short term lenders, reported on research undertaken to assess how the high cost short term market in the UK had evolved since the introduction of the cap.[31] This paper reported that the cost of credit had come down by around a third, default rates had roughly halved, and that lenders had been incentivised to offer affordable loans and were offering longer term loans (with the opportunity to repay early). Whereas previously lenders had been generating significant revenue from late fees, extending loans and relending, the report estimated that lenders were now receiving more than 80% of revenue from the contracted interest payments. However, access to high cost credit had significantly reduced, to a larger degree than the FCA expected. The FCA had estimated that the cap would result in 11% of borrowers no longer having access to a high cost loan.[32] The actual decline in consumers that have access to this credit was twice what was expected.[33] The UK's StepChange Debt Charity reported in 2017 that it had seen significantly fewer clients coming to it with high cost short term debts.[34] 16% of StepChange's clients had high cost short term debts in the first half of 2016 compared to nearly a quarter (23%) in 2013. The report stated: "*This suggests fewer people are getting these loans and less of those who take out HCSTC are struggling to repay*."[35] However, the charity continued to see issues with repeat borrowing and around affordability assessments.

There has been no research undertaken in New Zealand that provides specific information on the likely impact on borrowers of a contraction in the high cost lending market. However, a 2018-2019 report on a survey of financial capability services on high cost lending and other issues found that 90% of participant agencies believed that clients were worse off overall (not just financially) by having taken out a high cost loan.[36] This survey is attached as **Appendix 9**. Similarly, in a survey of Australian Financial Counsellors done in 2011, 79% of respondents thought that payday lending "never" helped to improve their clients' financial situation.[37]

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[31] Impact of Regulation on High Cost Short Term Credit, n28.

[32] Proposals for a price cap on high-cost short-term credit, CP14/10, July 2014, FCA, July 2014, 33-34 (CP14/10), at [1.27].

[33] Impact of Regulation on High Cost Short Term Credit, n28, at 16.

[34] Payday loans: The next generation", StepChange Debt Charity, 2017, (Payday loans: The next generation) accessible at: https://www.stepchange.org/Portals/0/documents/Reports/Payday-loans-next-generation.pdf

[35] Payday loans: The next generation, n33, at 2.

[36] Survey of financial mentoring and budgeting services in Aotearoa on high cost loans, debt collection and other consumer credit issues, Dr. Liz Gordon, Justice Innovation Centre, Community Law Canterbury 2019, 19 (Survey of Services in Aotearoa) accessible from: https://www.fincap.org.nz/big-changes-needed-to-protect-consumers-from-high-cost-loans-and-debt-collection-practises/

[37] What Financial Counsellors say about Payday Lending", Financial Counselling Australia, October 2011, at 8-9.

A recent (2018) study done in the UK sought to find out what happened to consumers who had previously taken out high cost loans but were now denied such loans due to the tightening up of criteria.[38] The study found that while the FCA originally predicted that 60% of borrowers with no access to high cost credit would no longer borrow at all, a significant proportion of the people denied loans were still looking for borrowing options. Participants were more likely to seek credit from another source (either an alternative formal lending route or friends and family) than "go without." The most common step that an individual took after being declined was to access credit from friends and family.

The study's results supported the FCA's view that the cap on the cost of a payday loan did not increase levels of borrowing among informal creditors undertaking criminal activity.[39]

A Consumer Finance Association paper produced in 2017 references another survey of consumers (also done in the UK) which asked high cost borrowers what they would have done if the loan had not been available.[40] The majority (over 35%) stated they would have borrowed from family or friends, with the second most popular answer being that they would have gone without the daily essentials.

The UK charity StepChange also undertook a survey to find out what had happened to consumers who were denied a payday loan.[41] This research looked at clients who applied for a high cost loan, had previously been accepted but, since introduction of the cap, had been rejected. It looked at where these people turned after they could not get a high cost loan. Some borrowed from other lenders, including other high cost providers, credit cards, overdraft or home credit loans. Many missed an essential bill or another loan payment or borrowed from friends and family. One of the key recommendations of the StepChange report was that the government should look at new ways to provide greater access to more affordable credit safety nets for the most financially vulnerable, including looking at international examples of no and low interest loan schemes.

A 2012 study done by US based Pew Charitable Trusts found that if faced with a cash shortfall, and a payday loan was unavailable, 81% of borrowers said they would cut back on expenses. Many said they

[38] Appleyard, Packman, Lazell, "PayDay Denied: Exploring the lived experience of declined payday loan applicants", Carnegie UK Trust 2018 (Payday Denied),
[39] Payday Denied, n38, at 32.

[40] Impact of Regulation on High Cost Short Term Credit, n28.

[41] Payday loans: The next generation, n34.

would delay paying the bills, rely on friends and family or sell personal possessions. Borrowing from friends and family was the third most popular option chosen.[42]

Finally, a study done in 2016 looked at the experiences of former payday loan borrowers in Arkansas, seven years after the United States Supreme Court banned usurious payday lending rates.[43] The study entitled 'Into the Light', conducted by Southern Bancorp Community Partners, surveyed 100 former payday loan borrowers on their experiences since the State began enforcing the constitutional interest rate cap. The State constitution effectively banned payday lending by prohibiting interest rates higher than 17%pa and limiting fees. However, a typical interest rate for a payday loan was 391%pa or more. In 2009 payday loan stores closed for business after the United States Supreme Court declared payday lending unconstitutional.

Findings of this survey were:

- Most borrowers said they were better off in the wake of the industry departure (nearly 90% in total said they were better off (59%) or the same (29%) after the payday lenders left);
- Borrowers desired fairer small loan products to address financial crunches;
- Borrowers acknowledged they were industry targets and wanted strong consumer protections; *and*
- Borrowers used a few safe, non-credit options to address financial shortfalls. The most popular alternative was turn to family or friends for money.

Some submitters to MBIE's June 2018 Discussion Paper directly addressed the concern about illegal lending. For example, Dunedin Budget Advisory Service was not so concerned about lenders going underground, saying Financial Mentors will be told about these lenders and can report on them (*at page 3 of their submission*). The Family Finances Services Trust commented that illegal lenders are already out there, and the police have the power to act against them (*at page 2 of their submission*).

The bottom line on the issue of potential harm from introduction of an interest rate cap is that for a person that is not able to access a loan once a cap is imposed, it is not the answer to allow lending at an even higher rate. These are the people that it becomes "unaffordable" for the lender to lend to, because they are highest risk borrowers. The UK 2017 review of the operation of the price cap explored the profile of people denied a high cost loan after the cap was introduced. It found that

[42] See Payday lending in America: Who borrows, where they borrow and why, Pew Charitable Trusts, produced as part of the Pew Safe Small-Dollar Loans Research Project, available from https://www.pewtrusts.org/~/media/legacy/uploadedfiles/pcs_assets/2012/pewpaydaylendingreportpdf.pdf

[43] See Into the Light, A survey of Arkansas borrowers seven years after state Supreme Court bans usurious payday lending rates, accessible at: https://banksouthern.com/sbcp/into-the-light/

declined applicants had an average annual income lower than those accepted for a loan, were more likely to be in households receiving income from benefits and were less likely to be in full time employment. Declined applicants were on a trajectory of increasing debt.[44]

It is not the solution to the financial need of a person in this category to make a high cost loan available. While it might relieve an immediate need for funds, for example to pay the rent or a bill, the repayments will cause more hardship and make it harder to meet that rent payment or bill the next time around. Allowing a person under serious financial stress access to a high cost loan is like throwing a brick to a drowning person.

The Panel that reviewed the Australian reforms that had introduced an interest rate cap also found that allowing consumers access to high cost credit did not necessarily result in "financial inclusion". The Panel's report said:[45]

> *The Panel does not consider that access to finance, irrespective of the cost, means that a consumer is financially included. Financial inclusion is a broader and more complex concept that takes into account the relationship between high charges and broader social consequences, such as financial hardship, insecurity in housing tenure and adverse impacts on the consumer's health, and is concerned with improvement in the consumer's situation, rather than it deteriorating or remaining unchanged.*

The Panel recommended that a range of measures be introduced to support the interest rate cap regime that is in force in Australia, including a protected earnings amount for all borrowers (which is one of the proposals supported by this submission). These proposals were designed to increase financial inclusion, by for example reducing the risk that consumers may be unable to pay for basic needs or default on other necessary commitments.

The other concern that is often raised when the topic of interest rate caps is discussed is that lenders will raise their rates up to the level of the cap thereby reducing competition. The Consumer Finance Association review done in 2017 of the impact of the UK reforms found that (at page 20): "*As one would expect in a competitive market, a number of lenders are pricing loans below what is required by the price cap, as they compete for a diverse customer base including customers who may otherwise choose non-HCSTC products, such as instalment loans over 12 months or credit cards. Pricing below the cap can be observed by various lenders at all different loan durations*."

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[44] High Cost Credit Review FCA, n29, at [2.39] – [2.42].

[45] Review of the Small Amount Credit Contract Laws, Final Report, March 2016, Australian Government, The Treasury, (SACC Final Report) at 3.

However, the Australian review of its reforms[46] found that "*the vast majority of SACC providers charge the maximum permitted fees. This might suggest an absence of market competition between SACC providers and it would be unfortunate if the existence of the present cap, which as previously stated is a concession from the 48 per cent APR cap which applies to other credit contracts, has discouraged competition or led to inefficiencies. While not recommending a change to the cap, the Panel reminds SACC providers that the cap is a maximum and encourages them to seek to look to ways which might allow them to reduce their fees below the cap and make their products more affordable for their consumers most of whom are vulnerable because they have no other credit options*."

What happened in Australia suggests that there is a risk that high cost lenders will price products to the level of the cap. This should not be considered a reason to not impose a cap. It should be a relevant consideration in the design of the cap. At the end of the day, interest rates of 50% per annum are much less damaging that 500%.

What would an interest rate cap in New Zealand look like?

FinCap is very clear that a rate should be created by regulation rather than legislation. This would allow the rate to be adjusted to respond to economic conditions.

The design of the cap should be the result of a careful and thorough review of the options and the likely impact on the market. This is the process that UK and Australia went through before deciding on the design of their respective caps.

In both those countries, the reforms were prompted by research that revealed the harm being caused by high cost lending, in particular to vulnerable consumers. There is a striking similarity between the situation that existed in both the UK and Australia before their reforms, and the situation in New Zealand now, as revealed by recent survey of Financial Mentors undertaken by Community Law, Canterbury (this research is set out in **Appendix 9** and is summarised later in this submission).

[46] SACC Final Report, n45, at 21.

UK research and design of their interest rate cap

The UK then implemented a 0.8% per day cap which is combined with: limits on default fees, a total repayment limit, a limit on the number of roll-overs and restrictions on the use of continuous payment authorities. The 0.8% per day cap includes both fees and interest payable on the loan.

The 2013 Office of Fair Trading (UK) report found that (prior to law reform including an interest rate cap):[47]

- there was poor compliance with the law (and guidance) across the market and throughout the lifecycle of payday loans, from advertising of loans to debt collection;
- lenders competed by emphasising speed and easy access to loans, but borrowers were not getting a balanced picture of the costs and risks of taking out a payday loan;
- most lenders were not conducting adequate affordability assessments and their revenue streams relied heavily on rolling over or refinancing loans; and
- around one in three loans was repaid late or not repaid at all.

Australian research and design of their interest rate cap

Under the 2013 Australian reforms, one-off loan contracts for 15 days or less for amounts of up to $2,000 are banned. For loans for amounts of up to $2,000 for longer than 15 days but less than one year, no interest can be charged but the lender can charge an establishment fee of up to 20% of the loan amount, a monthly fee of up to 4%, a default fee, enforcement costs and any government fee payable. The maximum the borrower will have to pay back in the event of default is twice the loan amount.

Loan contracts for amounts of between $2,000 and $5,000 for terms of up to 2 years attract different rules, an interest rate cap of 48%pa plus a $400 maximum fee.

Two key Australian studies of payday lending informed the Australian reforms: *Payday Loans: Helping Hand or Quicksand?*[48] and *Caught Short: Exploring the Role of Small, Short-Term Loans in the Lives of Australians.*[49] These and other studies found that consumers of payday loans usually received low

[47] Payday Lending, Compliance Review Final Report, Office of Fair Trading, March 2013, OFT 1481.

[48] "Payday Loans: Helping Hand or Quicksand?" Community Action Law Centre, September 2010, (Payday Loans: Helping Hand or Quicksand?) accessible from https://consumeraction.org.au/wp-content/uploads/2012/05/PayDayLendingReport-FINAL.pdf

[49] Banks, Marston, Karger and Russell, "Caught Short, Exploring the role of small short-term loans in the lives of Australians", August 2012, (Caught Short) accessible at: https://researchbank.rmit.edu.au/view/rmit:49930

incomes and had minimal, if any, savings. "*Compared with the general population, payday loan borrowers are more likely to have been raised in poverty, and many are disadvantaged by physical or mental illness and disability…Borrowers are more likely to be unemployed, and single parents with dependent children are over-represented*"."[50] Both key studies found that more women than men used payday loans. Borrowers often had relatively low levels of English proficiency, general education and financial literacy and often had significant physical, psychological or emotional health problems. They tended to lack the knowledge (or confidence) to pursue legal rights or remedies which may have been available. Consumers overwhelmingly used high cost short term loans to meet basic needs.[51] Repeat and frequent use of payday loans was common and the number of borrowers using payday loans as one-off transactions was relatively low.[52]

The comments by many borrowers around how they felt caught in a vicious cycle of being 'trapped' or 'stuck' reflects the lending patterns of most respondents, who were continuously indebted to one or more payday lending companies. Financial Counsellors reported what they saw as the irresponsible lending practices of some payday lenders. This included structuring loans to facilitate an endless 'borrowing cycle' and lending to low-income borrowers or those with vulnerability factors, such as mental illness or lack of education. Financial Counsellors reported how these factors could impact on a borrower's ability to properly assess the viability of the loan.

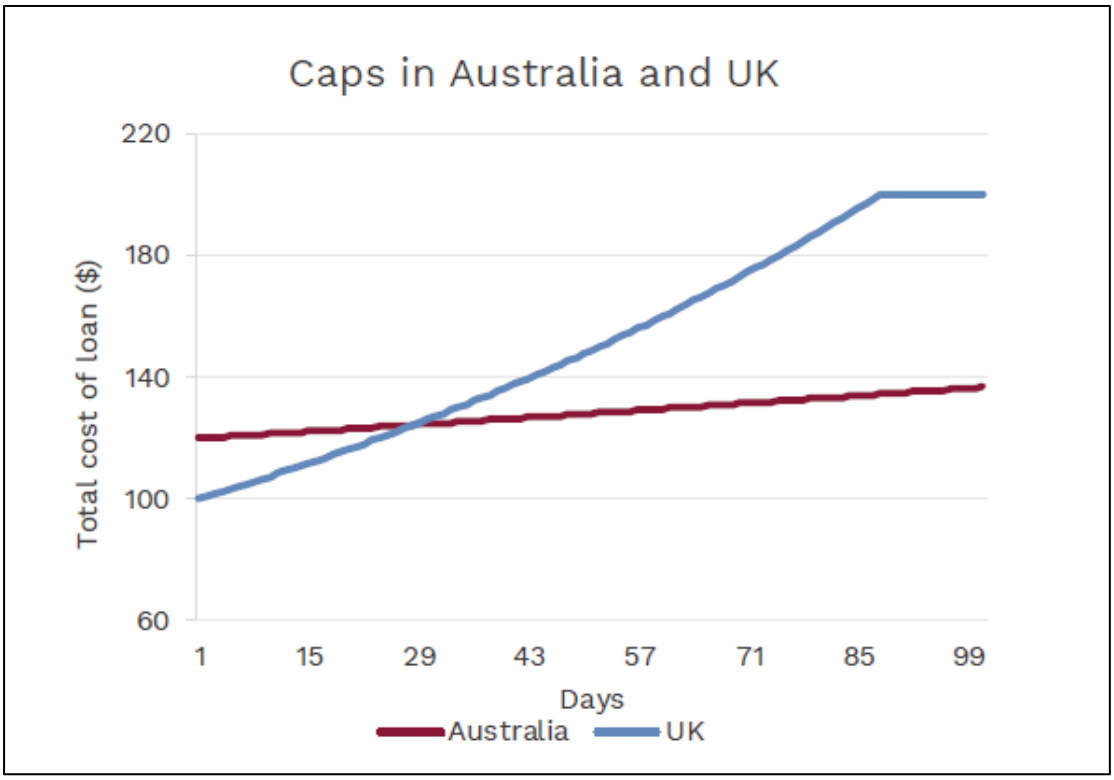
https://www.researchgate.net/profile/Marcus_Banks2/publication/273461528_Caught_Short/links/589ea923aca272046aa94101/Caught-Short.pdf

[50] Ali, McRae and Ramsay, "The Politics of Payday Lending Regulation in Australia", Monash University Law Review, Vol 39(2), 2013, 411 (Politics of Payday Lending in Australia), at 420-421.

[51] Payday Loans: Helping Hand or Quicksand? n48, at 5.

[52] Politics of Payday Lending in Australia, n50, at 425.

Fig. 4 Comparison of interest rate caps in Australia and the UK[53]



New Zealand research

Recent research conducted by Community Law Canterbury gives insight into the current situation in New Zealand.[54] This research was carried out in December 2018 and reported in February 2019. It reports on information obtained from 76 budgeting agencies from all regions of New Zealand ("participant agencies"). Key relevant findings of the Community Law Canterbury report were as follows.

Around 15,000 clients were seen by participant agencies in 2018. Women made up more than half of those clients, with around half of all clients being Māori and 20% Pasifika.

The clients often came to agencies as a "last resort", and in "dire straits". Most had high levels of consumer debt, and payments were often in arrears. Most debts were triggered by factors such as unemployment, change in circumstances, mental illness, or family demands.

[53] Green, Sam, Robertson, Nick, and Nana, Dr Ganesh, *The harm from high cost lending – The case for improved regulation*, BERL, 2019, attached as **Appendix 7.**
[54] Survey of Services in Aotearoa, n36, attached as **Appendix 9**.

The main types of debt were to Work and Income, store or consumer debt, direct sales, overdraft/ credit card or loans. Most had more than one type of debt, an increasing debt burden, the inability to make minimum payments and/ or the need to borrow for basic items. Multiple loans were the norm.

A major section of the research was around high cost loans. These were defined as those with interest rates more than 50%, often taken out on a short-term basis. Many such loans have real interest rates in hundreds of percent. One example given, using fees and costs of an agency, showed a person borrowing $100 for two weeks being required to pay back over $250 on time, with default fees if the deadline was missed.

Such loans can often be applied for online and are easy to obtain, even with a poor credit rating.

Most high cost loans were taken out to cover household expenses, car repairs, car registration or rent. As they are usually short term, they appear to fill a gap between the cost of basic needs and the ability to pay for these. This means, in effect, that many whānau end up struggling to pay their basic costs plus the very high burden of servicing/repaying a high cost loan.

Most people who took out high cost loans did so because they were unable to obtain credit in other ways, and/ or because these loans were accessible and convenient and could be processed quickly, alongside other factors. Most agencies reported that, on average, clients were unable to repay such loans on time, causing higher fees and further debt.

Agencies reported that most clients with high cost loans had a low or very low understanding of the fees or costs they were incurring. Also, most appeared to have more than one high cost loan, with either the same or more often different lenders. Reasons for multiple borrowing included a worsening of their general financial situation, repayment of prior debt, needing a loan for new and different reasons or because they were encouraged by lenders to borrow more. More than one in four appeared to have three or more high cost loans. Most such loans were of low value (up to $1,000) although many were also larger.

The “very few” alternatives to high cost debt included: good budgeting to alleviate household debt, Work and Income loans, a new low- or no- interest scheme and non-financial support (e.g. food banks).

The main influences on client borrowing overall were the ability to borrow funds when needed and widespread advertising promising ‘easy’ money. Nearly all agencies agreed or strongly agreed that “the more vulnerable the client, the less likely they are to be influenced by interest rates”.

The similarities between the situation in New Zealand and the situation in both Australia and the UK just prior to the introduction of an interest rate cap regime in those jurisdictions are obvious. It is also

a that an interest rate cap would alleviate a lot of the harm that New Zealanders are experiencing due to use of high cost loans.

FinCap's view on the rate of the cap

Simply put: the lower the better. High cost short term loans are harmful debt products that have no place in a financially healthy society.

Our preference is for the lowest possible rate, and the frontline experience indicates that the rate should be 50% or lower to remove the highly damaging payday loan market. That is a principled position with a predictable outcome. We recognise that a higher rate than 50% may be the cost of getting a cap implemented, but believe that will be inadequate. We are however, confident that even if a cap is introduced that is higher than 50%, the empirical evidence will quickly indicate the benefits of an incremental reduction towards that rate. Which is why there is intense pressure in Australia and the UK for a reduction of the cap towards 50%.

We note that the Loan Shark Prevention Bill was recently introduced to Congress in the United States by Bernie Sanders and Alexandria Ocasio-Cortez with a 15% interest rate cap on all consumer loans.[55]

BERL has indicated that the UK rate of 0.8% per day would be appropriate. We refer to the BERL report that is attached as **Appendix 7.** Researchers from Victoria University of Wellington and Canterbury University who prepared a research paper on interest rate caps have noted that adopting the Australian system would be in line with what several of the lenders to the June 2018 Discussion Paper suggested. This research paper is attached as **Appendix 8.**

One submitter to the June 2018 Discussion Paper was Sunshine Loans, which is an Australian high cost lender considering setting up business in New Zealand. This lender said in its submission: "*The Australian reforms that commenced in 2013, involving a detailed and graduated capping system, provide a continuation of commercial lending - while consumers pay less. Sunshine Loans has found that, while profits were reduced following the replacement of the Australian interest rate and (some) fees for small loans by a 20% flat permitted establishment fee and a 4% flat permitted monthly fee, it has been possible to survive as a creditor lending these small loans*."

Sunshine Loans was not the only lender that suggested New Zealand adopt the Australian cap regime. Acorn Finance and Rapid Loans both suggested in their submissions to the June 2018 Discussion Paper that New Zealand consider adopting a similar cap to that in Australia. Adopting a regime like that

[55] See https://theintercept.com/2019/05/09/alexandria-ocasio-cortez-bernie-sanders-bank-legislation/

which applies in Australia would also be in line with the Australian and New Zealand governments' commitment to trans-Tasman co-ordination of business laws.[56]

We reiterate that a level of around 50% per annum would be the clearest, most principled, consumer orientated and appropriate way forward.

In terms of how to facilitate the inclusion of an interest rate cap into the Bill, we suggest that the best way to do it would be to:

- Include a power in the regulation-making power section (section 138 of the CCCFA) to cap the total cost of credit for high cost consumer credit contracts, *and*
- Insert a prohibition on offering or entering into a consumer credit contract where the credit cost exceeds the prescribed cap. The prohibition should be backed up with criminal and civil penalties, as well as relief for any borrower affected.

We attach as **Appendix 4** a draft amendment to the Bill that we suggest would enable the cap to be put in place by regulations.

[56] See the Memorandum of Understanding between the Government of New Zealand and the Government of Australia on Coordination of Business Law, 22 February 2006, which states: "This Memorandum of Understanding reflects our desire to deepen the trans-Tasman relationship within a global market, through increased coordination of business law, thereby creating a mutually beneficial trans-Tasman commercial environment."

Alternatives to high cost short term lending

One of the key considerations arising in the context of a discussion about interest rate caps is what other options are there for borrowers in need of credit. We have researched this and found that there are some other options in New Zealand, but more can still be done.

In New Zealand, Work and Income (part of the Ministry of Social Development) offers a range of one-off payments for persons (beneficiaries and non-beneficiaries) who need emergency funding for food, accommodation, bills and certain other types of expenses and have no other credit options. The type of payment available depends on whether the borrower is a beneficiary or not and some of the payments (especially for non-beneficiaries) do have to be repaid. Grants (which do not have to be repaid) are available for food and some dental care. Interest free loans are available for other types of expenses, with flexible repayment terms.

The charity Good Shepherd offers a 'Step-up' loan of up to $5000 at a concessionary (6.99%) interest rate. Good Shepherd also offers a no-interest loan scheme for individuals and families on low incomes. No-interest loan amounts are up to $1,000 for essential goods and services. Repayments are set up at an affordable amount over a set period. There are criteria for borrowers such as being entitled to a community services card and having resided at the same address for more than three months. Good Shepherd services are delivered through 16 providers around New Zealand (for example, The Salvation Army). The Step-up loan is a more popular product than the no-interest loans. Work and Income is seen as the preferable source of no-interest loans due to the strict criteria imposed by Good Shepherd around affordability.

Micro finance provider Ngā Tangata Microfinance Trust was set up in 2009 with a strong sense of financial and social justice for those on low incomes, and needing to borrow. Kiwibank came on board in 2010 and Ngā Tangata began to offer no interest and no fee loans in early 2011. Approximately 45 budget services throughout the North Island and Dunedin currently work in partnership with Ngā Tangata. No-interest loans are available through the recommendation and support of Financial Mentors for up to $2,000, being purposed for family assets or well-being. To be eligible to apply, the borrower must be 18 years or over, have lived in the same place for two months or more, be on a low income and have enough in the budget to comfortably make the repayments within two years. Ngā Tangata also offers a no-interest debt relief loan of up to $3,000 for repaying loans with high interest charges. The debt relief product is the most popular product offered by Nga Tangata. The borrower must be able to establish ability to repay and will have to have been working with a financial mentor to be eligible.

There are also several independent no-interest locally focused lenders for example the Newtown Ethical Lending Trust.

No New Zealand research is available to assess whether these options are likely to be adequate to cope with the increase in demand on these services that may result from an interest rate cap, or on whether there could be other barriers to consumers using these services, such as inaccessibility, inability to service repayments, ineligibility, lack of awareness or a reluctance to admit extreme need. Several of the submitters to the June 2018 Discussion Paper suggested that more in the way of micro finance options were needed.

One of the current issues with expecting micro finance providers to fill the gap if high cost lenders become more constrained in who they lend to, is that microfinance providers take their responsible lending obligations seriously (while at the same time endeavouring to be as flexible as possible to meet the economic-and social need). A loan will not be offered unless the microfinance organisation is confident that the applicant will be able to safely repay. This is at least in part because Kiwibank (which funds Nga Tangata) and BNZ (which funds Good Shepherd) expect a low default rate (e.g. well under ten percent).

A significant Access to Safe Credit initiative has been established by the Government (through the Ministry of Social Development working with MBIE and TPK) to look at ways to improve access to safe credit for low income and vulnerable New Zealanders. Stakeholders have been invited to discuss the issues that arise at a series of workshops. A strategy is emerging.

We accept that more work needs to be done to find ways to accommodate the need for credit for those who would be unable to borrow if an interest rate cap was imposed. However, we feel strongly that the answer is not to allow high cost credit as an option. The cap in the UK resulted in many borrowers being unable to access high cost credit. But this was a positive outcome not a negative one. These were borrowers that could least afford the repayments and for whom a high cost credit loan was most likely to lead to further financial and social hardship, as the repayments would take away money needed for essential living expenses.

Other measures that are needed to support an interest rate cap

In addition to an interest rate cap, it is essential that the Bill include both **a protected earnings cap on borrowers' income** and an **effective total amount repayable limit.** The Bill includes a total amount repayable limit, but we think, as detailed below, that as drafted it is capable of avoidance.

We also ask that the Bill include a range of other measures that would provide significant protections for borrowers from unscrupulous lenders. These are: **introducing anti-avoidance provisions into the Bill, introducing a statutory prohibition on irresponsible lending**, and **requiring lenders to advertise the APR (annual percentage rate) of the loan**, based on a compounding interest rate (f that is what the lender charges) or a simple interest rate (if that is what the lender charges). These measures are all detailed below.

Protected earnings cap

Under Australian law, for borrowers whose predominant source of income is Centrelink payments (in New Zealand terminology, beneficiaries), the total payable towards all high cost loans due and not repaid cannot exceed 20% of the borrower's gross income. The report that reviewed the operation of the 2013 Australian reforms recommended that the 20% limit be replaced with a 10% limit of the borrower's net income and apply to all borrowers of high cost short term loans, not just those in receipt of a benefit.[57] This recommendation was accepted by the Australian Government in its response to the report[58] and endorsed by the recent Senate Inquiry.[59] The government response noted that "*it is unusual to have such prescriptive requirements regarding the amount that a consumer can devote to a particular form of finance; however, the panel's report highlighted the vulnerable customer base of SACCs"*.[60] The Panel noted that the principles-based responsible lending obligations appear

[57] SACC Final Report, n45, Recommendation 1, at vii.

[58] See Australian government media release 28 November 2016 "Government response to the final report of the review of the small amount credit contract laws" (Government response to SACC report), available at http://kmo.ministers.treasury.gov.au/media-release/105-2016/

[59] Credit and Hardship; Report of the Senate Inquiry into credit and financial products targeted at Australians at risk of financial hardship, The Senate, Economics Reference Committee, February 2019 (Senate Inquiry), at [1.21] and [3.99].

[60] 'SACC' stands for small amount credit contract.

insufficient alone to prevent observed harm; a more strict affordability test is warranted. The Australian Government accepted this proposal."[61]

This measure would draw a firm line enabling certainty of compliance with the lender responsibility principles, both protecting borrowers and assisting in enforcement.

Its effectiveness would be increased if there was some way of verifying all high cost loans the borrower was currently indebted under. A lender will only have first-hand knowledge of the loan history of any borrower with that lender and will only have the borrower's information on what other loans the borrower has. A national database of high cost loans, as operates in Oklahoma and certain other states in the US,[62] or mandatory comprehensive credit reporting, as is being currently introduced in Australia,[63] could be considered as measures to assist in the effectiveness of a protected earnings cap.

We submit that the Bill should include a protected earnings cap set at a level of 10% of the borrower's net income. It should apply to all borrowers who take out a high cost loan. Alternatively, it could apply to borrowers who are identified as more vulnerable. The easiest way to do that would be, as in Australia, to look at whether the borrower is in receipt of a Work and Income benefit. At the very least then, we submit that any person whose income consists of 50% or more from a benefit from Work and Income should be subject to a protected earnings cap under which the maximum that could be committed to high cost loans to all lenders would be 10% of their net income. The prohibition would be on the lender lending in circumstances that breached the limit.

This request is supported by a recent report prepared by BERL: *The harm from High Cost Lending* (attached as **Appendix 7**). We include suggested drafting that would empower such a cap by regulations, in **Appendix 4.**

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[61] Government response to SACC report, n58.

[62] See A Serpell, "Protecting the Desperate – Regulation of Payday Lending", [2015] Federal Law Review 147, at 170, for discussion of the issues around establishing a database of loans.

[63] See the National Consumer Credit Protection Amendment (Mandatory Comprehensive Credit Reporting) Bill 2018 available from https://treasury.gov.au/sites/default/files/2019-03/Exposure-Draft-EM_0.pdf. As of 1 July 2018, the major banks are required to share 50% of customers' credit data with credit bureaus. This will be increased to 100% by 1 July 2019.

The proposed total amount repayable limit

We are concerned that the total amount repayable limit, included in new subpart 6A of the CCCFA (see clause 22 of the Bill and new section 45A), will be easy to avoid. The prohibition attempts to capture loans made after the first loan, and to include subsequent loan amounts into the calculation of the total cap amount. It does this through the definition of 'related consumer credit contract'. However, the definition requires that the lender under both loans be the same person or an associated person. 'Associated' is defined in s 8A. It also requires that the first and second loan are continuous, meaning there must always be an unpaid balance on the loan to the first lender (or any associated lender).

It would be very easy for a lender to ensure that a second loan was not a 'related consumer credit contract' by having an arrangement with another lender (not associated) whereby the first loan could be paid off by a loan from the other lender, then (even one day) later the first lender could make a second advance that paid off the friendly lender and was not captured in the amount repayable limit.

We suggest this may be addressed by adding the words "*or a person acting jointly or in concert with*" into para (b) of the definition of "related consumer credit contract". There is a precedent for the use of those words in the Takeovers Code. Two persons are associated for Takeovers Code purposes if they are acting jointly or in concert. Case law has established what is meant by acting jointly or in concert (such as where there is an understanding between those parties).

A second issue is that the total amount repayable limit can be avoided by the second loan being made by the original lender, not to the original borrower but to a partner or some family member of the original borrower. We suggest this might be addressed by adding the words "or related to the debtor under contract A" into para (a) of the definition of "related consumer credit contract."

We understand the intent behind the drafting. The scope for avoidance is one reason why the legislation should not rely on the total amount repayable limit alone to address the harm from high cost lending**. We have not been able to find any other country in the world that just utilises a total amount repayable limit as a way of regulating high cost lending.**

It is necessary that the total amount repayable limit be supported by other mechanisms, most importantly by an interest rate cap. But there are other measures that should also be introduced. One of these is a protected earnings cap, discussed above. Another is a general anti-avoidance provision that would capture a lender that engages in conduct that has the intent or effect of avoiding the total amount repayable limit. A third is a general prohibition on irresponsible lending. These measures are discussed below.

Difficulties with enforcing the total amount repayable limit

The status of loans providing for interest and fees totalling more than 100% of the amount borrowed is unclear. Under the general law, a contract entered into in breach of a statute would be an illegal contract, and therefore of no effect. However, under s 136 of the Credit Contracts and Consumer Finance Act 2003, entry into a credit contract, a consumer lease, or a buy-back transaction in breach of this Act does not make the contract illegal. Section 136 appears to have been intended to avoid any possibility of the courts or the Disputes Tribunal using statutory powers of this kind to vary and validate loan contracts which breached the law, particularly by significantly changing the interest rate payable under the contract or awarding compensation to a borrower who had already paid a significant sum by way of interest on a relatively small sum borrowed.

Unless the principal Act is amended, where the loan contract stipulates fees and interest totalling more than 100% of the loan amount, the contract remains in force until and unless re-opened by a court or tribunal having jurisdiction under the Act. The borrower must pay the sums stipulated – even though they exceed the statutory maximum - and then seek to have the contract reopened either by legal action launched by the borrower or by the Commerce Commission. Action by a borrower to have a high-interest consumer loan set aside under the current law is very unlikely because the borrower will have neither inclination nor resources to bring a legal action where the borrower must show that fees are unreasonable, or a contract is oppressive.

There are two potential solutions to this issue:

1. Firstly, contracts in breach of the total amount repayable limit should be illegal contracts;
    - This opens the way for a creditor to seek relief under the illegality provisions of the Contract and Commercial Law Act 2017.
2. Such contracts be void at the time of making so that the creditor has no right to collect accruing interest and fees.
    - It is desirable to also provide that the principal amount is not recoverable. This would result in significant financial consequences for the creditor's attempts to circumvent the total amount repayable limit, which is a more effective deterrent than pecuniary penalties or infringement procedures.

Under cl 36 inserting s 107E, which states that an insurance contract that indemnifies a person for the person's liability to pay pecuniary penalties is void, it is desirable to state clearly whether a contract made void by the section is an illegal contract for the purposes of the Contract and Commercial Law Act 2017. The context suggests the contract will not apply, which is the most appropriate solution. This matter should be clarified.

Consideration may also need to be given to the primacy of the statutory damages remedy for cases where the contract beaches the principal Act. It would seem inappropriate that where a contract has been re-opened because the total amount repayable limit is breached, the borrower may receive less than his or her actual losses just because the creditor has in other cases complied with the law - as is possible under s 92.

The proposed s 45A mechanism renders unclear the power of the courts to re-open loans as oppressive, or to refuse to allow recovery of all interest and fees claimed. Under the current law, judges in the District Court have effectively created a rule that lenders cannot recover interest at the default rate under a high-interest loan contract for more than a year. The initiation of that practice is described in *Aotea Finance (West Auckland) Ltd v Hiku Aotea Finance (West Auckland) Ltd v Hiku* [2015] NZDC 22553, and is premised on courts being able, of their own motion, to re-open credit contracts which were on the face of it oppressive. The rule has been applied in cases where an application for summary judgment has not been opposed but the Judge considers the level of fees or default interest charges to be, in the circumstances, oppressive. One consequence of this rule of judicial practice appears to be that some lenders now voluntarily limit the quantum of default interest claimed. Such a limit, whether voluntary or compulsory, may be effective to limit the "debt spiral" in which borrowers may otherwise be trapped. The Bill should make the position clear, and we submit that a contract could still potentially be oppressive even if within the total amount repayable limit.

The total amount repayable limit should be extended to loans below the high cost loan threshold

We ask that the Government give serious consideration to extending the total amount repayable limit (*see clause 22 of the Bill and new section 45A*) to loans below the high cost loan threshold (excluding mortgages). We believe that serious harm is being caused by both secured and unsecured loans that requires addressing. The total repayment cap proposed in the Bill will not affect these loans. We do not, however, think the repayment limit should include mortgage lending.

Story from a budgeting service:

A low income earner with fluctuating hours' contract, supporting a family of seven. Presented with a debt schedule totalling $60,000 showing 4 Finance company debts, 1 store credit card and 1 Bank Credit Card, Student loan and debts to School and utilities in arrears. After investigation by Financial Mentor it was found debts to finance companies were being paid down by consolidation loans and KiwiSaver hardship withdrawals. Once the balances were cleared, lending was being approved again within a very short time frame. An

investigation by the Commerce Commission did not lead to prosecution; however, the company changed its policy but provided no redress for the person concerned. The finance company did not realise that someone paying out a loan with a Kiwisaver hardship withdrawal meant the person had to be in hardship and that signing them up to a loan a month later then another loan 3 months later was irresponsible lending! Reduction of debt level to $30,000 12 months later included another KiwiSaver withdrawal applied for under the guidance of the Financial Mentor, working 3 jobs and sometimes 4, applying for emergency grants from NGOs, regular food parcels and writing off some debt and 26 sessions with the Financial Mentor! The majority of loans were at 30% interest p.a. and attracting default interest and all sorts of fees for letters etc. Two loans secured against family vehicles. The family income needed to be $1,400 per week to meet debt repayments and cover basic living expenses.

Other measures we seek that would support both the total amount repayable limit and an interest rate cap

Anti-avoidance provisions

The recent Australian Senate inquiry *Credit and Hardship; Report of the Senate Inquiry into credit and financial products targeted at Australians at risk of financial hardship*, *The Senate, Economics Reference Committee, February 2019* (Senate Inquiry), found that providers of payday loans (and consumer leases) in Australia are structuring their businesses to avoid regulatory obligations. It considered that "*the entire consumer credit architecture would benefit from more robust anti-avoidance mechanisms*."

In October–November 2017 the Australian Treasury conducted consultations on an exposure draft of the National Consumer Credit Protection Amendment (Small Amount Credit Contract and Consumer Lease Reforms) Bill 2017 (the SACC Bill), which was the Australian Government's response to the review of the effectiveness of the small amount credit contract laws (the SACC Review). The exposure draft introduced broad anti-avoidance provisions and strengthened penalties for failure to comply.

These Australian reforms seem to have stalled. That exposure draft is currently not progressing. Labor introduced its own bill that replicated the Treasury bill to progress these reforms, but the Labor bill is also not progressing. We understand this is due to lobbying by the finance industry and not due to any underlying concerns with the draft legislation itself. The recent (2019) Senate Inquiry recommended that these reforms be progressed and in particular that the anti-avoidance clauses be introduced. They are attached as **Appendix 5** to this submission.

There is a real possibility that lenders in New Zealand will also try to structure their products and lending practices in a way that avoids the letter of the new law. We strongly submit that anti-avoidance provisions be included in the Bill. These Australian provisions provide a model.

A general prohibition on irresponsible lending

We submit that **a general statutory prohibition on irresponsible lending**, coupled with increased mechanisms to assist claims to get to court, should be included in the Bill to assist in reducing irresponsible lending. Such a prohibition could be similar to the general prohibition on misleading conduct in section 9 of the Fair Trading Act 1986. Under section 9 of that Act there is a general prohibition on misleading or deceptive conduct in trade. Breach attracts civil consequences only. Any person who has suffered loss by reason of the conduct can bring an action for breach (as do the Commerce Commission and rival traders). If breach is established, and that involves looking at case law to determine the tests for when conduct is misleading or deceptive, then a claimant seeking compensation must establish that the defendant's conduct was the, or an, effective cause of their loss. That then gives the court access to a range of orders. Injunctive relief is also available, so for example a rival trader could bring a claim for breach of section9 without having to establish any loss.

A prohibition in the CCCFA could work in a similar way. It could be a broadly-worded prohibition on irresponsible lending, for example "*no person shall, in connection with a consumer credit contract, engage in irresponsible lending*." The phrase 'irresponsible lending' would not be defined, but it would be left to the courts to establish tests for determining if that threshold had been met, guided by the Responsible Lending Code. Any person, including the Commerce Commission or a borrower, could bring an action for breach, and breach could lead to the award of a pecuniary penalty or order for compensation.

There are issues with expecting a borrower to bring an action to enforce any such new prohibition. Research shows that borrowers of high cost short term loans are generally unlikely to take action to enforce the existing responsible lending obligations.[64] Possible reasons for this include the borrower not being aware of their rights, being ashamed to admit that they have taken out a high cost loan, or not wishing to damage a relationship with a lender that they may need to turn to in desperate circumstances. It is often the consumer advocate (commonly a Financial Mentor) that will enter discussions with a lender on behalf of a borrower. We believe that reforms could address these issues through more effective enforcement.

One party that could get involved to assist with enforcement is a dispute resolution scheme. All high cost lenders are required to be a member of a dispute resolution scheme under the Financial Service

[64] See Senate Inquiry, n59, at 4, Caught Short, n49, at 78, and Payday Loans: Helping Hand or Quicksand, n48, at 212- 213.

Providers (Registration and Dispute Resolution) Act 2008. A suggestion that came from submissions (which FinCap supports) was that **a lender should be required by law to refer the matter to their dispute resolution scheme if a borrower was in default on a loan within a certain period after the loan was made** (for example, defaulting within the first month after the loan was made).[65] The scheme would then have the opportunity to review the situation, to let the borrower know their rights, and if the matter seemed to be a systemic one with that lender to alert the Commerce Commission to a possible breach of the prohibition on irresponsible lending. This could also assist with enforcement of a prohibition on irresponsible lending.

Another suggestion supported by FinCap for inclusion in the Bill that came through the submissions to the June 2018 Discussion Paper was that **a borrower should have to see a consumer advocate before taking out a high cost loan**, if the borrower met certain criteria designed to identify more vulnerable consumers (for example, a beneficiary, someone already in default under a high cost loan or someone that had taken out a certain number of high cost loans in the last 12 months).[66] A requirement such as this would get the consumer advocate involved at an earlier stage, could assist the borrower to consider other options, and could provide the advocate with the opportunity to alert the Commerce Commission to potential breaches of the Principles. We support this submission as well.

We propose that both reforms should be considered for inclusion in the law, in addition to the general statutory prohibition on irresponsible lending. Both these reforms are also included in our discussion (see below) of measures that could be taken to improve enforcement of the current regime more generally.

Clarity in advertising of the cost of the loan

High cost lenders commonly advertise that their loans are X% interest a year or Y% interest per day. If the interest compounds, which it often does, these rates are usually misleading. It is often very difficult even for a financially literate person to work out if the interest payable to any particular high cost lender compounds or not. For example, on Cash Converters' website is a sample agreement for a "cash advance" that states: *Interest charges are calculated daily by multiplying the balance outstanding at the end of each day by a daily interest rate. Interest does*

[65] See the submission of Financial Services Complaints Ltd.

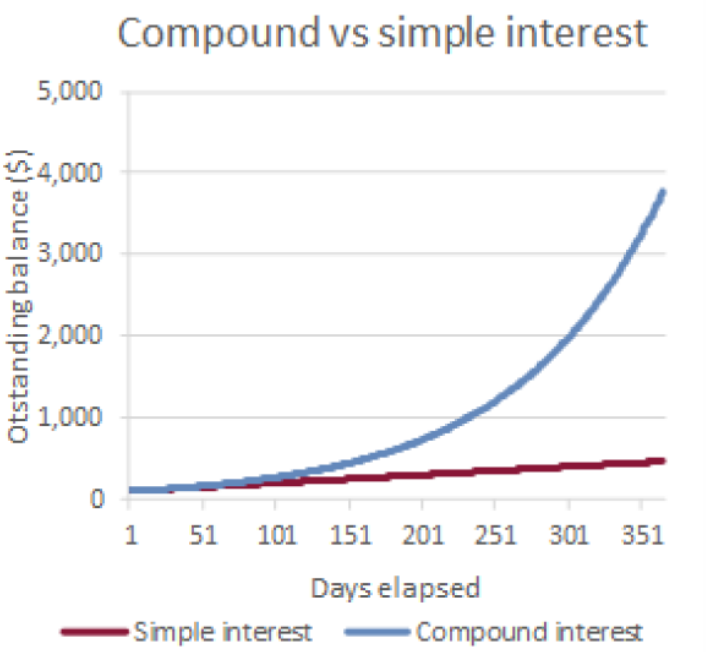
[66] See for example the submission of Waahi Whaanui Trust (Huntly).

not compound. However, on the sample agreement for a Cash Converters' "personal loan" the interest clause states: *Interest charges are calculated daily by multiplying the balance outstanding at the end of each day by a daily interest rate and applied to your account monthly. The daily interest rate is calculated by dividing the annual interest rate of 144% by 365.* This clause indicates that interest compounds. But this would not be easy for the average borrower to work out. Moola and Save my Bacon also seem to charge compounding interest.

We submit that the law **requires all high cost lenders to state very clearly the APR for the loan which is the annual rate of interest.** If the lender charges compounding interest on the loan, then the APR must be provided based on a compounding rate (and include all fees). If the lender does not charge compounding interest, then the APR must be based on simple interest (and include all fees). This would give borrowers more accurate information of the actual cost of the loan and allow for better comparisons between loan options. This will also allow borrowers to make better-informed decisions over which loans are the best for them.

We refer to the BERL report attached as **Appendix 7** which recommends that the law requires an APR provided based on compounding interest.

Fig. 5 Simple and compound interest at 1 percent per day on $100 loan



Other aspects of the Bill on which we want to make specific submissions

Enforcement should be strengthened

Financial Mentors have reported that noncompliance with the responsible lending principles is widespread, particularly in the area of affordability assessments. FinCap supports the enforcement measures that are being introduced in the Bill, including pecuniary penalties, statutory damages and compliance orders. Currently there are no penalties for irresponsible lending. Introducing these penalties will be a deterrent for breaking the law. These measures have been proven to be effective in Australia, especially with the comprehensive scheme of "penalty units" for each provision which provides the maximum amount of pecuniary penalties that can be imposed on a lender in their equivalent consumer credit Act.

New enforcement measures that can be adopted easily into the Bill

Measures that can be adopted in a straightforward manner into the Bill without the need for further policy analysis, and which we submit in favour of, are: require all lenders to have a designated compliance officer, put an obligation on lenders to report borrowers in default to the dispute resolution scheme, require an independently prepared budget before making a high cost loan to certain borrowers, and introducing a rebuttable presumption that loan is unaffordable in certain circumstances.

The requirement that all lenders to have a designated compliance officer

All lenders should be required to have a designated compliance officer who is responsible for ensuring that all CCCFA obligations are complied with and that there are internal policies, procedures, staff training and reviews necessary to ensure the lender is complying.

This is an established practice in the context of the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (AML/CFT Act). Section 56 of that Act requires reporting entities[67] to designate an employee to be an AML/CFT compliance officer. The compliance officer is responsible for detecting money laundering and the financing of terrorism and managing and mitigating the risk of this. The compliance officer must also be vetted under the reporting entity's AML/CFT programme.[68] FinCap submits that as compliance officers are an established practice in New Zealand for the AML/CFT Act, this should be included in the current reforms to ensure high cost lenders are designating an employee to ensure compliance with CCCFA obligations.

Compliance officers are also an established practice under the Health and Safety at Work Act 2015 (HSWA). The Act requires a person conducting a business or undertaking (PCBU)[69] to have an officer to exercise due diligence in ensuring that the PCBU meets their obligations under the HSWA under s 44 of the Act.[70] As the practice of a compliance officer is also established under the HSWA, FinCap submits that it is also important for lenders to be obliged to have a compliance officer who exercises due diligence in determining whether there is compliance with their CCCFA obligations.

[67] Under s 5 of the Anti-Money Laundering and Countering Financing of Terrorism Act, a "reporting entity" is defined as a casino, a designated non-financial business or profession, a financial institution, a high-value dealer, the New Zealand Racing Board, and includes people who are declared to be a reporting entity for the purposes of this Act and any other persons who are required by enactment to comply with this Act.

[68] Anti-Money Laundering and Countering Financing of Terrorism Act, s 57.

[69] Under s 17 of the Health and Safety at Work Act 2015, a person conducting a business or undertaking (PCBU) is a person who conducts, with or without others, a business whether or not the business is conducted for profit or gain. A PCBU does not include a person who is employed or engaged solely as a worker in, or officer in, the business or undertaking; a volunteer association; an occupier of a home to the extent that the occupier employs or engages another person solely to do residential work; a statutory officer to the extent that they are a worker, or officer of, the business or undertaking; or a person/class of persons declared by regulations to not be a PCBU for the purposes of the Act.

[70] Under s 44(4) of the Health and Safety at Work Act 2015, "due diligence" means that the officer takes reasonable steps to acquire, and keep up to date, knowledge of work and health and safety matters; gain an understanding of the operations of the PCBU and generally of the hazards and risk associated with those operations; ensure that the PCBU has the available resources, and uses those resources, to minimise risks to health and safety from work carried out as part of the conduct of the business or undertaking; ensure that the PCBU has appropriate processes for receiving and considering information regarding incidents, hazards, risks and for responding in a timely way to that information; and ensure that the PCBU has, and implements, processes for complying with any duty or obligation of the PCBU under the Act.

An obligation on lenders to report to dispute resolution schemes when borrowers are in default

The Bill should put an obligation on a lender to report the matter to the lender's dispute resolution scheme (DRS) if a borrower is in default on a high cost loan within 1 month of taking out the loan.

If default occurs into this early period of the loan, this suggests the loan initially may not have been affordable for the borrower. The DRS can investigate and if it appears there has been irresponsible lending, the scheme can assist in a negotiation with the lender and potentially report the matter to the Commerce Commission. Further, if there are repeated instances of the lender approving loans in these circumstances, the DRS can assist in the enforcement process by notifying the Commerce Commission of that fact.

This suggestion is simple to implement and would benefit consumers by having an independent third party reviewing the practices of high cost lenders. This requirement is also likely to reduce irresponsible lending because the dispute resolution scheme will be aware if the high cost lender repeatedly lends to borrowers who default early into their loan, therefore the DRS has the necessary evidence of irresponsible lending to bring a claim to the Commerce Commission. The DRS Financial Services Complaints Ltd in its submission to MBIE in June 2018 suggested a law reform along these lines (see page 7 of the Financial Services Complaints submission).

An obligation on lenders to obtain an independent budget before agreeing to make a high cost loan

The Bill should put an obligation on the lender that before it agrees to make a high cost loan it must have been provided with a budget for the borrower prepared by an independent person such as a Financial Mentor, if the borrower is in a category identified as vulnerable and is taking out a high cost loan. This could be, for example, if the borrower was in receipt of a Work and Income benefit which comprised 50% or more of the borrower's income, or has already taken out and defaulted on a high cost loan from that lender, or has taken out more than three high cost loans from that lender in the last 12 months. This reform is supported by the BERL report attached as Appendix 7.

Introduce a rebuttable presumption (as in Australia) where a loan is presumed to be unaffordable if the borrower is in default

The Bill should introduce a rebuttable presumption (as in Australia) where a loan is presumed to be unaffordable if the borrower is in default under another high cost loan or has held and additional two or more high cost loans in the past 90 days. In other words, the loan would be presumed to be in breach of the responsible lending principle that the lender must be satisfied that the borrower will make the payments under the agreement without suffering substantial hardship. A rebuttable presumption is likely to put the lender on notice that the borrower is either unlikely to be able to make repayments, or that they are suffering hardship in taking out multiple high cost loans in a short period of time. The lender should have an obligation to record (and make available to the Commerce Commission on demand) the evidence that it relied on to rebut the presumption.

Enforcement related aspects of the Bill that relate to enforcement that require amendment

Aspects of the Bill that relate to enforcement that require amendment and that we ask for are: strengthening of enforcement of the total amount repayable limit, compensation for reasonable mistake defence rather than an offer to compensate, the imposition of pecuniary penalties if there is no criminal liability and a natural person should not be able to indemnify liability for pecuniary penalties.

Enforcement of the total amount repayable limit should be strengthened

Clause 33 of the Bill imposes fines on an individual or body corporate who knowingly makes a false or misleading statement in documents required for fit and proper person certification. These fines, let alone any sanctions, are not in place for breaches of the total amount repayable limit. Severe penalties for breaching this provision lenders must be imposed, which the Act should introduce. It is apposite here to quote Justice Hayne's comment on the need for members of the banking industry to be accountable for their misconduct (Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (2019), p 3):

> *…Too often, financial services entities that broke the law were not properly held to account. Misconduct will be deterred only if entities believe that misconduct will be detected, denounced and justly punished. Misconduct, especially misconduct that yields profit, is not deterred by requiring those who are found to have done wrong to do no more than pay compensation. And wrongdoing is not denounced by issuing a media release.*

It would be appropriate for there to be a specific offence of breaching the total amount repayable limit. Such an offence could well be one of strict liability (i.e. allowing the defendant to prove lack of fault on the balance of probabilities). Setting the appropriate penalty is more difficult, but various options could be explored, such as providing for a fine and/or a banning order to be made for a first offence, and a prison sentence to be imposed for a second or subsequent offence

The inclusion of such an offence is likely to have a significant deterrent effect on creditor companies, directors and managers. Secondly criminal prosecutions have a denunciatory effect which actions for penalties or infringement proceedings will not achieve. Thirdly, prosecutions – which are likely to be widely reported – serve to communicate to the pool of potential borrowers more information about their rights and about the obligations of creditors than would be achieve by other means of enforcement.

Reasonable mistake defence should require compensation, not merely an offer to compensate

A further change to cl 34 amending s 106 of the principal Act should be made. Section 106 of the CCCFA provides a person with defences to a claim for statutory damages or fines in relation to a breach of the Act. Section 106(1)(c) provides that a person has a defence to a claim for statutory damages if they have compensated or offered to compensate any person who has suffered loss or damage by a breach of the CCCFA. Since proceedings against a creditor or related person will only occur after a substantial period has elapsed since the breach, the section should require that compensation has been made. An offer to compensate the person who has suffered loss should not be sufficient.

Pecuniary penalties should be imposed if there is no criminal liability and a natural person should not be able to indemnify liability for pecuniary penalties

The express provision for pecuniary penalties under cl 36 of the Bill is desirable. However, it is submitted that there are theoretical and practical problems with the proposed new s 107C, the relationship between pecuniary penalties and criminal liability, and the wording of the proposed new s 107D, which is the restriction on indemnities.

The new s 107A is generally apt for the task. The provisions of s 106 will allow a person against whom an action for a pecuniary penalty is brought subs (2) to raise as a defence, as further matters to which the court should have regard, any attempts made by the person to remedy the breach once discovered and the provision of any compensation or other steps to lessen the impact of the breach on any borrower.

The proposed s 107C should be deleted. This is because the general law does not usually allow a person to escape civil liability based on having been criminally prosecuted, nor to avoid prosecution on the basis that civil proceedings have taken place. There does not seem to be any substantive justification for departing from this general principle.

If, contrary to the above, the proposed section is retained, it should be amended to make it clear that any proceedings for a pecuniary penalty which have been stayed can be reinstated if the person proceeded against has been acquitted or discharged in the criminal proceedings. It is quite possible that a case alleging a breach of the Act will fail because of the high standard of proof required in criminal proceedings but there would be more than enough evidence on the civil standard (as per the proposed s 107B) to establish the basis for a pecuniary penalty order. It would be unfortunate – and unduly favourable to creditors and their agents – for any stay to be permanent.

While the proposed new s 107D is highly desirable in principle, it does not prevent a natural person from indemnifying a person's liability to pay pecuniary penalties. As the provision stands, it forbids indemnity by the body corporate or any related body corporate in respect to a director, employee, or agent, or former director, employee or agent's liability to pay pecuniary penalties. It does not forbid the provision of an indemnity by a natural person – for example a shareholder, director or manager of the body corporate in question. It is submitted that the proposed section be amended to forbid, and make void, any indemnity offered by a natural person as well as by a body corporate.

Other suggestions to improve enforcement

Many other suggestions were made by submitters (both lenders and consumer groups) to MBIE's June 2018 Discussion Document aimed at improving enforcement of the CCCFA. These suggestions are in addition to (or extend) the reforms that FinCap has asked for and which are set out immediately above These other suggestions, which FinCap endorses, are not included in the Bill. They include the following:

- There should be more resourcing for advocates such as Financial Mentors and the Commerce Commission.
- The Commerce Commission should have a legal obligation to regularly audit all high cost lenders;
- A national database of high cost loans should be established, which can be used to assist lenders to assess affordability and suitability; and
- There should be a legal requirement for mandatory positive credit reporting by lenders.

Story from a budgeting service:

A beneficiary asked for $300 from [lender] over the counter. A $1,000 personal loan was approved. She borrowed $400 again a month later without making any payments on the first loan - interest rate on both loans 485% p.a. During the verbal affordability check, $50 was accepted for food costs when a family tax credit weekly payment of $283 was included income, indicating there were at least four children in the family. When the Financial Mentor challenged their affordability assessment the lender's manager asked what outcome was wanted. A write-off of both loans was raised as the best outcome for the beneficiary. The write-off was actioned that day. The family debt schedule showed the two high interest loans, two debt collection demands, a Work and Income debt and advances plus overdue utilities - a total of $20,000.

Debt collection should be regulated

Background

Financial Mentors report that often debt that has gone to debt collection causes considerable harm to their clients. Debt collection includes debt that originated as consumer loans or that originated as bills that were not paid, such as utilities bills.

The pressure placed on debtors by debt collectors can exacerbate existing anxiety or other mental health problems. Contact between the debt collector and the debtor is often at a frequency that causes stress to the debtor. It is not uncommon for a debt collector to harass the debtor (sometimes until the debtor applies for bankruptcy) by calling many times per day, sometimes using automated dialler technology (robocalls). In one case that we know of, a debtor received 33 calls in one day. Evening visits are also sometimes made (between 6pm and 10pm). Contact is generally by cell phone or landline, email and in person. However, social media, work phone and other forms of contact are also used. When debt collectors talk to a debtor's family or workplace, they are breaching the debtor's privacy and causing further stress to the debtor.

Our budgeting services have many stories of the impact that debt collection practices can have on mental health. **New legislation to regulate communication between debt collectors and debtors with the aim of reducing harassment should be enacted.** The nature and frequency of the contact made with the borrower can be a source of great stress for debtors. Accordingly, a key focus of new legislation to regulate debt collector practices should be preventing harassment.

Debt collectors sometimes use misrepresentations about consequences of non-payment to encourage payment, for example by telling the debtor that they will face litigation if they do not pay (when they will not). The Wellington City Mission has reported that some collectors hold themselves out as lawyers and threaten legal action if the debt is not paid. The Whangarei Budgeting Service has reported that some debt collectors display "extremely aggressive" behaviour. This aggression can lead to debtors paying more than they can afford to minimise further contact with debt collectors.

The following story from a budgeting service demonstrates the invasive and uncooperative practices exhibited by some debt collectors:

> *We have recently had a case in point, where a client had already told the trading company that she could not afford the agreed repayments and was going to be seeing a Financial Mentor. The Financial Mentor also contacted the company and asked them for a week to*

come back with a proposal. They agreed, but a debt collector from the company still turned up at the client's home after 7pm, unannounced, and harassed the client, refusing to leave until she had signed an agreement to pay (more than she could afford). The Financial Mentor phoned the company the next day to cancel this agreement and get some clarification and was stonewalled. The person she spoke to didn't know which Financial Services Disputes Organisation they were registered with (actually didn't know what the Financial Mentor was talking about), and finally suggested that the Financial Mentor was at fault and their collectors would never act in that way.

MBIE recorded in its June 2018 Discussion Paper that there were various problems in relation to debt collection practices.71 Problems include collectors setting unaffordable repayment schedules, charging excessive fees, and harassing debtors. MBIE's findings were reinforced by the submissions made in response to the Discussion Paper, which recorded harassment by debt collectors and demands for unreasonable repayments. Further evidence of poor debt collection practices emerged from research among local budget services undertaken in 2018/9 by Community Law Canterbury. 72The final report resulting from that research stated that harassment and the addition of unreasonable fees were not uncommon.

New Zealand does not have the comprehensive regime regarding debt collection in New Zealand which exists in comparable jurisdictions. Accordingly, debt collection practices vary significantly. The few laws which regulate the practices of debt collectors are split across several pieces of consumer legislation which makes it difficult for debtors to know or enforce their limited rights and gives leeway to companies.

Based on responses to the June 2018 Discussion Paper it seems that several lenders, debt collection businesses and industry bodies are in favour of New Zealand adopting regulation like that which applies in Australia, including: Sunshine Loans, Rapid Loans, the Financial Services Federation, Baycorp, Intercoll and Illion. Many debt collectors currently active in New Zealand operate under the Australian regime and would not be commercially disadvantaged by similar law in New Zealand.

The changes proposed in the Bill do not address the most concerning aspects of debt collection, which are issues with harassment and the high costs of debt collection (which are passed on to the debtor).

[71] See Discussion Paper: Review of consumer credit regulation Ministry of Business, Innovation and Employment (June 2018) at 35-36..

[72] See 2018-2019 the Survey of Financial Mentoring and Budget Services in Aotearoa on high cost loans, debt collection and other consumer credit issues attached as **Appendix 9,** at 24-26.

We recognise that the comprehensive changes to debt collection may be out of the scope of Credit Contracts Legislation Amendment Bill, but the Committee can act in two areas. Disclosure requirements for debt collection are already being addressed by this bill. We support this change. We ask that all debt collection businesses be bought under the Credit Contracts and Consumer Finance Act so that all debt collectors are required to act responsibly.

We also ask that the Committee request that further work is done on regulating debt collection in New Zealand as a matter of urgency. Regulation is needed to specifically address the practices of debt collectors, with a focus on ending harassment and placing a duty on collectors to negotiate a reasonable repayment plan with the debtor (or their Financial Mentor).

Disclosure before debt collection

We support the disclosure requirement in the Bill at cl 42.73

We recommend that the debt collector be required to send a letter or email to the debtor to set out the rights and obligations of the debtor at the start of the debt collection process, as well as all fees and charges to be imposed by the debt collector. The disclosure document should be limited to one page and only include key information to make the notice easy for the borrower to understand.

All debt collectors collecting debt under consumer credit contracts should be subject to the CCCFA

All debt collectors, including collectors who purchase debt and collectors who act as agents,74 should be subject to the CCCFA as if the collector was a lender under a consumer credit contract (where the original loan agreement was a consumer credit contract). This would bring all debt collectors under the lender responsibility principles, meaning that all debt collectors would be required to treat borrowers reasonably and in an ethical manner. Collectors who are assigned debt are subject to the

[73] This requires debt collectors to "ensure that disclosure of as much of the key information set out in the regulations as is applicable to the contract is made to every debtor under the contract before debt collection starts under the contract".

[74] There are different ways in which debt collection is undertaken: the lender may conduct the collection itself via its in-house debt collection process, it may engage a third-party debt collector to act as an agent on its behalf, or it may sell the debt to a third party which then takes over all the rights of the lender. In the latter situation the third party purchases the debt from the lender, generally at a discounted price, and then recovers the debt from the borrower.

CCCFA because they are included in the definition of “creditor” in s 5 of the CCCFA. Some debt collectors are third parties which act as agents of the creditor. These agents are not directly subject to the CCCFA.

Making all collectors subject to the CCCFA would also mean that all collectors may only charge "reasonable fees". Fees and charges are added to a debt when it goes to debt collection to cover the cost of collection. Generally, these fees are provided for in the original lending contract in broad terms, for example: “all costs associated with debt collection will be borne by the debtor.” All debt collectors would also have to be a member of a dispute resolution scheme (which at present debt collection agents do not have to be).

Some debt collectors charge the debtor high fees for the debt collection process and some charge interest as well. Examples of individual fees include a $30 letter fee incurred when the debt is initially passed on to the debt collector and a fee of $15 per phone call. In some cases, total collection costs are bigger than the initial loan.

All debt collectors could be brought within the scope of the CCCFA by the use of the s 138(1) (abc) power to declare all debt collectors to be creditors under a consumer credit contract. This would ensure that all collectors are subject to the lender responsibility principles and the CCCFA’s provisions on reasonable fees.

Broader reforms to debt collection law are required

Broader reforms to debt collection law are required but given that such reforms are outside the scope of this Bill, we encourage the Select Committee to recommend that Government prioritises the development of new legislation to regulate debt collectors. Again, this legislation should apply to all debt collectors that collect consumer debt (whether it be a high cost loan, a consumer lease, a credit card or any other debt taken on by a consumer), and whether the collectors are operating within the original lender’s in-house debt collection team or as an agent of the original lender or as a third party which has purchased the debt.

This new legislation should contain detailed debt collection standards. The new law should prohibit a debt collector from harassing a debtor, for example by contacting a debtor’s employer or by contacting the debtor multiple times per day. It should also place obligations on the debt collector to negotiate a reasonable repayment plan with the debtor.

This would align New Zealand's law more closely with that of the UK, the USA and Australia. The USA has had Federal legislation providing for such protections for over 40 years.75 The Australian Debt Collection Guidelines, which set out what behaviour is acceptable in very specific detail, should be used as a model. New Zealand fails significantly against international standards. We attach as Appendix 6 to this submission a comparison table that shows the different approaches to debt collection regulation taken in Australia, the UK, the USA and New Zealand.

[75] In the United States, debt collection is regulated by Fair Debt Collection Practices Act 15 USC § 169 (US) (passed in 1978). For more information see https://www.ftc.gov/enforcement/rules/rulemaking-regulatory-reform-proceedings/fair-debt-collection-practices-act-text

Mobile traders should be banned

These operations will be well known to Members of Parliament. The mobile trader model is reportedly unique to New Zealand and has proven to both be resistant to enforcement, and notably damaging at a community level. The model has multiple points of negative impact on vulnerable people:

- It is focused geographically on lower income communities, especially those with poor public transport services; and there is rich evidence that mobile trucks target especially vulnerable consumers (e.g. those in temporary or sheltered accommodation) and consumers in vulnerable locations (e.g. kindergartens);
- It offers a unique level of convenience (at the doorstep or in the street outside) and appeals to universal human yearning for "something a little special";
- It only operates through what are in effect credit contracts, so purchases which would not normally be caught up in those arrangements (including food from some companies) are subject to all the risks of credit contracts including default and eventual involvement of debt collectors;
- It starts off with prices generally well above those in local shops, plus the extra financial impact of credit arrangements;
- It aims to generate long term customers who, as they pay down debts, are induced to roll over; and
- It is comparatively easy to set up an operation fast, in anonymous vans, in a way which significantly evades the deliberative and lengthy enforcement processes that apply to other types of credit contracts.

The Commerce Commission has been targeting this sector and has seen both immediate success (because nearly all companies were breaking the law) with company closures, only to see new operations spring up again in classic "Whack a Mole" style. This threatens to continue unabated, and nothing in the legislation as drafted will impact significantly on it.

Clause 6 of the Bill defines the term "*mobile trader*" as a "person who carries on a business of offering or agreeing to supply, in person and outside of fixed premises, consumer goods to a natural person -

(a) under a credit sale (regardless of whether the contract is a consumer credit contract); or
(b) where all or part of the supply of the consumer goods is to be financed by a consumer credit contract under which a creditor is an associated person of that person -

(whether or not the business is the provider's only business or the provider's principal business).

They may provide a unique service to people that are unable to buy goods in cash or have limited access to transport, but this is at a massive financial cost to some of the poorest people in our society. **We support a total ban on mobile traders, which the definition contained in the Bill makes possible.** We propose that this ban exclude mobile traders operated by non-governmental organisations, such as The Salvation Army's "The Good Shop", which provides items at retail prices on interest-free terms as they do not create the same harm as for-profit mobile traders.[76]

If the Committee is does not agree to a ban, then we submit that mobile traders should be subject to the CCCFA as if they are creditors under a consumer credit contract.

Some mobile traders will already be lenders for the purposes of the CCCFA, where they sell goods or services through consumer credit contracts. However, other mobile traders do not fall within the CCCFA, where payment for the good is made in instalments, but does not involve interest charges, credit fees, or security interest (but may involve default fees). All mobile traders must be made subject to the CCCFA whether or not the arrangement falls outside of the definition of "consumer credit contract".

We note that MBIE recommended that a regulation making power be introduced that would allow contracts entered into by mobile traders to be declared to be consumer credit contracts (see the Impact Statement released by MBIE in October 2018, at pages 42-43). There is a call in power in the Bill, in clause 43 (which inserts a new section 138(1)(abb)). We ask that the regulations that are currently being drafted utilise this power to declare that all contracts entered into by mobile traders be consumer credit contracts.

These arrangements in substance involve an element of credit, as the purchase price is in effect lent to the purchaser, who takes the goods on day one and then repays the loan over time. This would ensure that mobile traders will have to comply with the same laws as other lenders offering consumer credit contracts.

Mobile traders themselves should also be declared to be creditors under consumer credit contracts (using the call in power in new s 138(1)(abc). This would mean (in particular) that that mobile traders would have to undertake affordability assessments when mobile trader accounts are established.

[76] For more information on The Salvation Army's "The Good Shop", see https://www.salvationarmy.org.nz/get-help/welfare/good-shop

If the Committee does not agree to a ban, then we submit that "Do not knock stickers" should be legally enforceable

If a person has a Do not knock sticker it means that they have taken proactive steps to not purchase from mobile traders. Do not knock stickers are often ignored by mobile traders at the moment. Breaching this request should have legal consequence.

We understand that this proposal is being considered in the review of the Fair Trading Act. Because it was announced as part of the proposals to reform consumer credit law we ask the committee to follow up on this proposal with officials.

Story from a budgeting service:

One of our Total Money Management clients went to pick up his son from daycare and saw a Home Direct Truck parked outside. He went in for a look and ended up purchasing a (very overpriced) cellphone for several hundred dollars, payable weekly by Direct Debit from his personal bank account. He was not asked any questions about his ability to pay for this. When he realised his mistake he sent the phone back (within 7 days) to Home Direct, but they returned it saying there was a scratch on the screen and it had not been reset to factory settings. When we became aware of this we examined the phone and could not find any scratch. We reset it to factory settings and returned it again to Home Direct with an accompanying letter asking what procedures were followed to ascertain if the client could afford to buy the phone.
Following this, Home Direct agreed to refund the client.

Another story from a budgeting service:

Three door to door companies selling to couple in late 50s on benefits totalling $5,000 owing. There were clear signs the couple would be unable to repay. They only had $8.74/week for food so didn't need the chest freezer they were sold. Letters were sent to each of the lenders [by the financial mentor] and the contracts were cancelled.

Buy Now Pay Later/After Pay products should be called in to the Bill and treated as consumer credit contracts

e submit that buy now pay later schemes be included in the scope of the CCCFA. This would allow products of this type to be regulated in the same way as other credit-related loans.

The inclusion of buy now pay later products into the CCCFA is important because they are credit products. While the payments do not incur interest, fees are charged. There is no requirement to undertake an affordability assessment as there is for other forms of credit when giving a person a credit limit for a buy now pay day scheme.

We note the new call-in power in section 138 (see clause 43 of the Bill) that will authorise regulations to enable the government to bring these products into the scope of the CCCFA. Regulations to bring post pay products into the Bill should be included in the regulations currently being prepared by MBIE.

The reasonable fees provisions should be more easily enforceable

We support the strengthening of the current rules around reasonable fees, in particular, the substantiation obligations. However, the prohibition against "unreasonable" fees as drafted is an inadequate measure. This is because "unreasonable" is subject to a wide definition and we have heard instances of this measure being breached. Also, the party challenging the unreasonableness of the fees must prove that they are not reasonable.[77] This is an obstacle to the effect of the provision because vulnerable borrowers are unlikely to have the knowledge, or the money, to challenge the unreasonableness of the fees. Vulnerable borrowers are also those most likely to be oppressed by unreasonable fees and charges.

A solution that we support is to move the onus of proof of reasonableness to the creditor. If the fees and charges have been properly assessed prior to imposition, the creditor should be readily able to establish reasonableness. If they were arbitrary figures, they will incur the costs of proving reasonableness. Again, a pecuniary cost is likely to deter non-compliant behaviour.

We support the requirements that creditors keep records about how fees are calculated and to make these records available to the Commerce Commission or the relevant dispute resolution scheme.

[77] See *Commerce Commission v Sportzone Motorcycles Ltd (in liquidation)* [2013] NZHC 2531; [2014] 3 NZLR 355; final appeal dismissed *Sportzone Motorcycles Ltd (in liquidation) v Commerce Commission* [2016] NZSC 53; [2016] 1 NZLR 1024.

Another addition to cl 21 to improve the disclosure of the reasonableness of fees is to require the creditor to disclose their records of fees to the borrower and the guarantor upon request. The differences in disclosure approaches between this section and cl 11 about the lender's inquiries, is not justified. It should be explicitly stated that these records must be provided free of charge when they are requested.

Stories from budgeting service on fees:

Evidence of unreasonable fees by a budgeting service: A client was charged an establishment fee of $600 for each addition to an original loan, even when the addition was only $1,000. Each time there was an increase, instead of merely adding these successive amounts, a new loan was created, and each time the new loan was created an Establishment fee of $600 was charged. On a total of $11,400 borrowed over 3 years, these Establishment fees amounted to $4,800. Interest was, by default, applied to the extra charges. The establishment fee ranged between about 16% and 60% of the individual loan amounts. This practice is not ethical and cannot be justified, the lender is using this tactic to justify charging an establishment fee each time the loan is increased.

A different client was being charged $7.50/wk. for defaulting on paying arrears, until she was recommended to tackle the lender. The client's ability to pay this alone is extremely low as she lives on a benefit. As at 12.7.18 that lender has stopped the late payment fee and reversed one month's late payment fees. The reason for this change is still under investigation but this shows that the borrower had to initiate the change. Many borrowers do not have the ability to investigate and negotiate such changes to their benefit. Management fees (admin, default, late payment, property search, etc.) and collection fees should reflect the true cost of managing the loan or collection. In many cases these charges accumulate automatically with little to no attention being paid to the loan. Computer programmes are designed to allow such loans to operate with little to no attention or intervention by the lender.

There should be more prescription around affordability assessments

We support the strengthening of the regulations to support the current principle that lenders must make reasonable inquiries of a borrower to ensure that payments will not cause them substantial hardship. We support the change that lenders will need to verify information provided by borrowers. However, cl 10 should state explicitly that the requirement to make reasonable inquiries obliges the lender to verify as far as reasonable possible the information provided by borrowers, for example, by asking for confirmatory documents.

An increasing number of borrowers are taking out loans through electronic communications which are processed by a computer algorithm with little or no human oversight. A specific provision requiring verification may slow the borrowing process down (not necessarily a bad thing) and certainly encourage greater compliance with the responsible lender provisions that now appears to be the case.

We support the existing change in the Bill that requires records to be kept about inquiries and those records to be made available to the Commerce Commission, the borrower, the guarantor, or the relevant dispute resolution scheme on request. Financial Mentors would be able to access these records using a standard privacy waiver. Borrowers often find it difficult to obtain information about their loan and the assessments made which makes it more challenging to identify whether there has been a case of irresponsible lending. The wording of cl 11 of the Bill inserting this provision should be amended to clarify that the creditor may not charge for the provision of any of the records covered by the new section 9CA.

Cooperation with Financial Mentors is also essential for improved affordability assessments. As reported by a budgeting service, Aotea Finance charge $20 to provide the affordability assessment to Financial Mentors. For more information, see the paragraph entitled "*An obligation should be placed on high cost lenders to cooperate with people advocating for borrowers*".

There is also scope for a rebuttable presumption (as described in the Enforcement section of this submission) to be included in the regulations.

We look forward to the opportunity to comment on a consultation draft of the proposed regulations that will implement this reform.

Certain types of payments to borrowers should be excluded from income for the purposes of doing affordability assessments

Lenders should not be able to include certain streams of payment for the purposes of assessing income in an affordability assessment. The streams of payment that should not be included as income for the purposes of assessing affordability should be items that are not treated as income by the IRD. These include board payments received, Family Tax Credits, Child Support and Disability Allowances.

This is to ensure that lenders are not assessing loans as being affordable by requiring the borrower to make repayments using the money they receive from these sources. The money that is granted under these payments and benefits is for a purpose, not for a lender to take advantage of by taking these benefits in loan repayments. This can be achieved by defining what is "income" for the purposes of affordability assessments. Currently, the lender is given guidance on how to assess income in the Responsible Lending Code but we understand that parts of the Code are going to become 'hard law' in the regulations currently being drafted. We ask that those regulations include a definition of income that excludes these payments.

Wage deduction authorities should be banned

Many lenders use wage deduction orders to get repayments. An example is included in **Appendix 2.** Borrowers often sign these not knowing what it means or because the clause is hidden away in a long, dense and complex contract. The implications can be really harmful for borrowers. Once the deduction order is in place the lender can get access to the borrower's wages as soon as they are paid, before the borrower has any chance to decide what the most important expense is.

People should have a choice over what debt obligations they prioritise, particularly when they are servicing multiple debts. This is an important part of building a person's financial capability. It is inappropriate that the high cost lender should have the first claim on the borrower's income when these borrowers are often struggling to meet daily living expenses, such as food, rent and utilities. Sometimes the borrower is a beneficiary and the deduction order is put in place, meaning that Work and Income pays the lender before the beneficiary gets their benefit. The practice of high cost lenders using wage deduction orders must be prohibited.

Direct debit authorities should be banned in relation to loans to beneficiaries

There are similar issues involving the use of direct debit authorities. At present many lenders require a direct debit to be set up by the borrower (in other words, an instruction to the bank to pay the lender at regular intervals).

The use of direct debit payment authorities in the case of borrowers who are beneficiaries should be banned. These borrowers have very little income to cover daily expenses and the lenders use their powerful bargaining position to insist on taking repayments out of the bank account as soon as the benefit is paid in. When direct debits fail there are also additional bank charges that cause more hardship for the borrower.

Lenders should be required to disclose information in a specific format

The Bill does not propose any changes to the disclosure requirements under s 17 of the Credit Contracts and Consumer Finance Act 2003, which is a substantial weakness.

Under the current law there is no requirement for lenders to consistently present their information. This makes it virtually impossible for a would-be borrower to make any effective comparison of different lenders and different products. An example is that data about fees and charges is often very hard to locate.

The Act, or the regulations, should impose a requirement that all creditors present information to potential borrowers in a standard format. This format could be approved by the Commerce Commission. Any such regulations should make express provision for minimum font size and line spacing to deal with the occasional practice of some lenders (particularly mobile traders) of using so-called 'mouse-print" with tiny fonts and compacted lines of print.

A further matter that could and should be addressed in Regulations or in the statute is the use of interest calculators. Many, but not all, websites do provide interest calculators so that a would-be borrower can establish the total obligations they are entering into. This is undoubtedly a very useful and user-friendly way of providing the information.

It is submitted that all creditors advertising their products electronically (e.g. on the internet, by social media etc) should be required to provide an interest rate calculator in a stipulated format. That

stipulated format should also include provision for automatic display of the fees and charges associated with the loan and their effect on the total indebtedness that will accrue.

Clauses allowing the court to reduce effect of failure to make initial or variation disclosure should be deleted

Clause 29 of the Bill proposes to insert two new provisions into the principal Act, sections 95A and 95B. These sections are unnecessary and should be deleted from the Bill as they allow creditors to potentially escape liability from their failure to disclose.

The proposed section 95A would allow a creditor to apply to the court for an order which would effectively either remove or limit the liability of the creditor for failure to comply with the law. There is no justification for such a provision. Creditors should always be required to comply with the law. To allow creditors to seek indemnity from, or limitation of, liability would be to place credit contracts on a very different footing from other types of contracts. There is no parallel provision under the Fair Trading or Consumer Guarantees legislation, or under the contractual remedies provisions of the Contract and Commercial Law Act 2017.

Further, it is highly likely that if the proposed new sections are enacted, creditors will effectively be unopposed in their applications as borrowers will rarely, if ever, be in a position to contest the application. This is exacerbated by the lack of a provision in the Bill requiring notice of this application to borrowers or other affected parties. Although the proposed section 95B leaves the court with a residual discretion, there may be a tendency for judges presented with only one side of the argument to decide the matter more favourably to the creditor than would be the case if the application were proposed.

A responsibility should be placed on lenders to make borrowers aware of avenues for making complaints or seeking help

All lenders are required to advertise on their website and in all communications that there is a dispute resolution scheme that they belong to and that the borrower can complain to for free if there is a dispute over any aspect of the loan. This is part of being on the Financial Services Register.

We propose that all lenders should be required by law to advertise a national helpline for financial hardship and debt, such as the MoneyTalks service operated by FinCap.78 on their communications, particularly their websites.

Legislation could ensure that it is prominently positioned on websites and all electronic and other correspondence and profiled in public-facing offices. It should also be promoted by the lenders when somebody gets in arrears. This will open greater opportunities to the borrower, and at the very least it should encourage more borrowers to discuss their money issues with qualified Financial Mentors.

There are examples from the UK where similar legislative intervention has worked to reduce consumer detriment. In the gambling industry all companies must promote a campaign entitled 'when the fun stops, stop' on their websites, in advertising and in written communications. It is important to note that it is gambling companies fund the cost of the 'when the fun stops, stop' service.79

[78] MoneyTalks is a service provided by FinCap which offers free and confidential phone, live chat, email and SMS budgeting advice by a financial mentor. It operates as the national debt helpline. https://www.moneytalks.co.nz/

[79] "When the fun stops, stop" is a campaign set up by The Senet Group, who is an independent body promoting responsible gambling standards. https://senetgroup.org.uk/; and The Senet Group Operator guidance regarding affiliate marketing arrangements (May 2018) at 3. https://senetgroup.org.uk/wp-content/uploads/2018/12/Senet_Group_Affiliates_16_May_2018.pdf

An obligation should be placed on lenders to cooperate with people advocating for borrowers

e submit that an obligation to be placed on high cost lenders to cooperate with Financial Mentors and budgeting services in defined ways.

These includes by having a positive duty in law to negotiate with borrowers' advocates and interact with advocates in good faith and being proactive about referrals to a national helpline for financial hardship and debt, such as the MoneyTalks service operated by FinCap, when borrowers are in default on loans.[80]

Use of funds from infringement fees and unclaimed money from settlements to go MBIE

The Bill introduces infringement fees in relation to the CCCFA, Under S105E of the Bill, "What the Commission does with infringement fees", any funds generated will go into the Crown bank account. This is even though it is extremely likely that those fees may be generated in large part from the dedicated and expert advocacy work of Financial Mentors. In addition to this settlement funds (unclaimed money from settlements) are subject to negotiation between lenders and the Commerce Commission. The recipient of unclaimed monies can at times become a contentious issue.

We submit that a dedicated fund is created, managed by MBIE to achieve a more equitable outcome. This will ensure the benefit of these funds has the intended impact for the borrowers who have been affected by lender's conduct and similar conduct elsewhere. We understand that a comparable arrangement has been established by the Australian Securities and Investment Commission (ASIC) and funds are applied to appropriate activities in the Financial Counsellor arena.

[80] MoneyTalks is a service provided by FinCap which offers free and confidential phone, live chat, email and SMS budgeting advice by a financial mentor. It operates as the national debt helpline. https://www.moneytalks.co.nz/

Advertising high cost short term loans should be banned

Advertising for high cost short term loans should be banned. These products are extremely harmful and are advertised as desirable products, or as commonplace commodities in society.[81] Advertising is often targeted at vulnerable communities through radio, local newspapers and the internet. This means that these advertisements are readily accessible.[82] A total ban on advertising for high cost short term loans recognises that these products cause social harm, like the ban on advertising of other harmful products, such as tobacco.

We support the amendment that disclosure must be in the language that a loan was advertised in. However, under cl 2 of the Bill, the new disclosure requirements are not coming into force until September 2020. Clause 14 can be introduced in a shorter period of time than the proposed commencement of the amendment. FinCap proposes that cl 14 comes into force on 1 March 2020. Protection of borrowers for whom English is not their first language is an urgent matter and should not be delayed any longer than necessary. There does not seem to be any justification for delaying the introduction of s 17A into the law as a business would not require this long period of time to comply with these disclosure requirements. The same arguments can be made for bringing into force the amendments in cl 2(4)(c) and (d) earlier than September 2020.

Clause 14 is an important provision requiring the creditor to disclose in the language that the loan was advertised in, but FinCap suggests that this section could be simplified. The better approach is that any creditor who advertises in a language other than English must prepare all required disclosure materials in both English and the language used in the advertisement *and* must expressly give the borrower the option of disclosure in English only or in both English and the language used in the advertising. Consideration should also be given to requiring the use of appropriate diagrams or charts to assist consumers to comprehend the meaning of the documents.

There is substantial evidence that many borrowers who take out high interest loans is do not have English as their first language and/or have significantly limited capacity to correctly comprehend the

[81] See MBIE "2018 Desk-based study of Lenders: An overview of the New Zealand lender landscape and lender advertising and disclosure practices" at 19, 20 and 21. The themes that MBIE examined in lender advertising were aspiration (where advertising targets desires of consumers), flexibility (where range of amounts and wide variety of reasons for borrowing are advertised), incentives (rewards or discounts are offered for taking out a loan or referring others to take out a loan), normality (advertisements portray that loans are common and lots of people use these services), and speed and ease (communicated that it is easy to borrow and credit can be obtained quickly).

[82] See MBIE "2018 Desk-based study of Lenders: An overview of the New Zealand lender landscape and lender advertising and disclosure practices" at 18. Out of 116 newspapers examined in the study, finance companies and other lenders were responsible for 119 advertisements.

meaning of documents in other than very plain English. While the current Act and the Fair Trading Act 1986 do prohibit the use of material that is likely to mislead, it is not clear whether this is to be judged from the perspective of a "ordinary" person or of the customers actually dealt with who may be likely to be confused or misled by statements which are technically correct but phrased in a style with which the consumer is not familiar.

We support the strengthening of the advertising standards for all other loans.

Story from the Commerce Commission

"We spoke to a borrower in the course of one of our investigations who had just paid off a high cost loan and had received a text from the lender offering more credit. T He borrower texted "stop" but more texts followed. He told us he tried to opt out a second time but eventually applied for a new loan following further texts offering more credit."[83]

Public notification should be introduced for people applying for fit and proper person certification

The introduction of Fit and Proper person's certification requirements is a welcome provision. Some form of certification is long overdue, and the proposed new sections should have some effect in preventing unscrupulous creditors from continuing to operate or similar persons entering the market. The registration regime should provide for public notification of the intention to apply for certification, and for members of the public to file objections to the application, which can then be resolved by the certifying body. A suitable model exists in the Private Security Personnel and Private Investigators Act 2010, Part 2, Subpart 1.

[83] See Commerce Commission submission on Discussion Document: Consumer Credit Regulation 1 August 2018, https://comcom.govt.nz/__data/assets/pdf_file/0025/98260/Submission-to-the-Ministry-of-Business-Innovation-and-Employment-on-the-Review-of-Consumer-Credit-Regulation-1-August-2018.pdf

The new due diligence requirements on directors and senior managers should be strengthened

The extension of liability to directors and senior managers is welcome. An additional improvement that could be made is under cl 23 of the Bill, inserting s 59B, where the wording of subsection (3) should be amended by the insertion of the word “all” between “taking” and “steps”. This would bring the test for due diligence into line with the general use of that phrase in other areas of law, by requiring directors and senior managers to take all reasonable steps before it can be said that they are exercising due diligence. It should not be enough that a manager or director has taken only some of the reasonable steps available to them to ensure compliance. The director or manager should have taken all the reasonable steps open to them.

High cost lenders should be required by law to provide information on their business to the regulator on an annual basis

We recommend that all high cost lenders should have to report certain information about their business in the last 12 months to the Commerce Commission annually so that information can be gathered on the amount of loans being made, numbers of defaults, profile of borrowers, and compliance with the lender responsibility principles.

Appendix 1

Age Concern New Zealand - comments on Credit Contract Legislation Amendment Bill

Age Concern New Zealand agrees that an interest rate cap must be included in the Credit Contracts Amendment Bill. We would like to see an interest cap that ensures high cost lenders cease to operate in the market. Fringe lenders and high cost lenders prey on vulnerable people, including older kiwis, who have limited incomes and no-where else to turn.

National Superannuation used to be sufficient for retirees to live on. The assumption was they owned their own home and had no debt. These were protective factors that enabled older kiwis to have a reasonable standard of living and not require high cost credit.

However, in 2018, 13.8% of older people had not paid off their mortgage by age 65[84], the current age of eligibility for national superannuation. There's also a clear trend of decreasing home ownership in New Zealand. For example, sixty-eight percent of older people owned their own home in 2013 compared to 74% in 2001[85].

It is predicted that within ten years one quarter of the total population will be people aged 65 years and above [86] and more than half of those turning 65 will be renters[87].

Māori are more disadvantaged. Since 1986 the proportion of Māori living in private rentals increased by 88.3% while it went up by 42.7% for the general population[88].

There are further disparities in home ownership for Māori and Pacific peoples.[89] Between 1986 and 2013 the proportion of people living in owner occupied homes fell 15.3% overall. However, the decline rate was 34.8% for Pacific and 20% for Māori.

New Zealand's increasing gap between rich and poor is contributing to an underclass of disenfranchised people on limited incomes. This disenfranchised group includes many older people. This makes their situation precarious and can entrap them in poverty. It also increases the likelihood of them sourcing loans from fringe lenders and high cost lenders.

This situation is compounded for Māori who are more likely than non-Māori to live in areas of high deprivation and struggle with poverty. It is well documented that women are more likely to earn less

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[84]See http://www.superseniors.msd.govt.nz/about-superseniors/ageing-population/better-later-life-report/index.html

[85]See http://www.superseniors.msd.govt.nz/about-superseniors/ageing-population/better-later-life-report/index.html

[86]See https://www.radionz.co.nz/news/national/361746/desparate-need-to-house-lonely-seniors-it-is-a-hidden-problem

[87]See https://www.nzherald.co.nz/nz/news/article.cfm?c_id=1&objectid=12134518

[88] Statistics New Zealand. 2016. *Changes in home-ownership patterns 1986-2013: Focus on Māori and Pacific people.* New Zealand Government.*18*

[89] Statistics New Zealand. 2016. *Changes in home-ownership patterns 1986-2013: Focus on Māori and Pacific people.* New Zealand Government.*18*

over their working life and have lower levels of savings[90]. In 2015 a study indicated that middle aged, middle class women were more likely to be in debt than any other group[91]. These situations makes both Māori and women more vulnerable to high interest creditors.

It is important for New Zealand to have strong regulation of credit contracts and a cap on interest rates to improve wellbeing and people's ability to save for later life.

Age Concern New Zealand is supportive of 'Do not knock' stickers becoming legally enforceable and truck shops being banned, other than ethical shopping trucks such as the ones set up by the Salvation Army[92].

We offer a couple of scenarios based on composite personal situations Age Concern has encountered in our work.

Scenario A

Molly continues to live in the state house that she and her husband were pleased to be allocated when they had young children. Molly was always the keen gardener and kept the family in vegies in the growing season. Even though the neighbourhood had changed a lot, children in the street pop round as Molly still keeps a biscuit tin of baking for visitors. There used to be a group of shops on the corner, but they are all boarded up now. Instead businesses in trucks came around with a kitchen and clothes items for sale on credit. Even though Molly knew she had never bought from them, they arrived at her door saying she owed them money. There were repeated "discussions" at the door step, in which she explained that someone else must have been using her name and address. Molly felt so anxious she stopped answering the door. But instead the letters addressed to her showed an ever mounting debt in her name.

Scenario B

Two years ago Ted and June had been asked to sign as guarantor for a car loan on behalf of their granddaughter. Their granddaughter also had her first baby. Six months later their granddaughter's partner left for Australia and she needed a car to get the baby to day-care so she could return to work. A year later, their granddaughter went to Australia to visit the partner with the baby for a holiday - or so Ted and June had understood. When they received summons for loan failure, they discovered that car loans repayments had not been made and they were responsible for the principle and the interest.

Age Concern New Zealand

Serving the needs of older people

[90] See http://www.superseniors.msd.govt.nz/about-superseniors/ageing-population/better-later-life-report/index.html
[91] See https://www.nzherald.co.nz/lifestyle/news/article.cfm?c_id=6&objectid=11517717
[92] See https://www.salvationarmy.org.nz/news/salvation-army-wheels-out-first-ethical-shopping-truck

Appendix 2

Sample wage deduction authority from high cost short term loan contract

Employer's Deduction Authority

To:

I, Example Customer

299 Durham Street North
Christchurch Central
Christchurch

hereby:

1 Give written consent pursuant to section 5 of the Wages Protection Act 1983 for you to deduct from any salary, wages or other moneys owing to me, any amount which may be owing by me to MOOLA.CO.NZ LIMITED; and

2 authorise you to pay to MOOLA.CO.NZ LIMITED, upon its written request to , such sum as is owing by me to MOOLA.CO.NZ LIMITED. This authorisation may be withdrawn by me at any time by me giving written notice to my employer; and

3 authorise you to release to MOOLA.CO.NZ LIMITED personal information concerning my employment.

Dated this 10 day of April 2019

Signed by: Example Customer

Appendix 3

List of countries with interest rate caps (World Bank research)

List of countries with interest rate caps as at 2014[93][94]

Sub-Saharan Africa	East Asia and Pacific	Europe and Central Asia	Latin America and the Caribbean	Middle East and North Africa	South Asia	Western Europe	Others
Eritrea	China	Armenia	Argentina	Algeria	Bangladesh	Belgium	Australia
Ethiopia	Japan	Estonia	Bolivia	Egypt, Arab Rep.	India	France	Bahamas
Ghana	Lao PDR	Kyrgyz Republic	Brazil	Libya	Pakistan	Germany	Canada
Guinea	Myanmar	Poland	Chile	Malta		Greece	United States
Mauritania	Philippines	Slovak Republic	Colombia	Syrian Arab Republic		Ireland	
Namibia	Thailand	Slovenia	Ecuador	Tunisia		Italy	
Nigeria	Vietnam	Turkey	Guatemala			Netherlands	
South Africa			Honduras			Portugal	
Sudan			Nicaragua			Spain	
Zambia			Paraguay			Switzerland	
Western African Economic and Monetary Union[95]			Republic Dominican			United Kingdom	
Central African Economic and Monetary Community[96]			Uruguay				
			Venezuela,				

[93] This list was taken from *Interest Rate Caps around the World, Still Popular but a Blunt Instrument*, Policy Research Working Paper 7070, World Bank Group October 2014:

[94] *Sources*: Helms and Reille 2004; Mbengue 2013; Castellanos 2012; Porteous, Collins, and Abrams 2010; iff/ZEW 2010; EIU 2012, 2013; CGAP-MIX 2011; Steiner and Agudelo 2012.

[95] West African Economic and Monetary Union (also known by its French acronym, **UEMOA**) are Benin, Burkina Faso, Côte D'Ivoire, Guinea-Bissau, Mali, Niger, Senegal, and Togo

[96] The Central African Economic and Monetary Community (**CEMAC**) is made up of six States: Gabon, Cameroon, the Central African Republic (CAR), Chad, the Republic of the Congo and Equatorial Guinea.

OECD countries with interest rate caps (as at May 2019)

25 out of 36 OECD countries have interest rate caps on high cost lending. The countries that do not have interest rate caps are:

Austria, Denmark, Luxembourg, Norway, Sweden, Finland, Latvia, South Korea, Israel, Mexico and New Zealand.

Notes on some other countries missing from the list (information accurate as at 2014):

Romania established interest rate ceilings by law in 1938 but does not currently apply caps on bank loans or credit lenders. Peru allows interest rates to be determined by the market, but in exceptional circumstances the central bank has the power to set caps. In Mexico, the central bank by law can regulate interest rates but has not done so. Panama, which used to have caps based on its usury law, eliminated the law in 2008. Morocco has the option to impose ceilings according to its Law on Microcredit Associations but has not exercised it. Neither Austria nor Denmark has maximum interest rates. Denmark debated the issue in early 2009 and 2010 but did not follow up. Finally, Cyprus, which used to have interest rate ceilings, ended the practice in 1999 to enhance its competitiveness in the banking sector.

A recent development:

Finland's Finance Committee said (in February 2019) it wants lawmakers to consider whether consumer access to so-called payday loans is actually necessary or appropriate. The committee proposed several measures to help address problems linked to the quick loans that carry high interest rates and fees, in another attempt to deal with the major risks and problems that payday loans can pose.

One of the measures proposed by the committee is to place a 20 percent cap on payday loan interest rates.

The finance committee is responsible for dealing with government budgets, long-term budgetary planning, legislation regarding taxes and other financial matters.

Earlier in February 2019 the finance ministry put forward a bill to legislate a 30 percent cap on interest rates on such loans.[97]

[97] See https://yle.fi/uutiset/osasto/news/finance_committee_proposes_20_interest_rate_cap_on_payday_loans/10665655

Appendix 4

Proposed drafting for implementing an interest rate cap and protected earnings cap

Drafting that will enable an interest rate cap to be introduced by regulations

New section 45B:

45B – Cost of credit must not exceed prescribed amount

The cost of credit (including interest and all fees) in relation to a high-cost consumer credit contract or any class of high-cost consumer credit contract must not exceed the amount or amounts prescribed by regulation.

In section 138(1)(f) insert a new section (fc) that reads:

(fc) prescribing a maximum cost of credit (including interest and all fees) in relation to a high-cost consumer credit contract or any class of high-cost consumer credit contract.

(Note – new regulation making power (fa) in the Bill will have to be consequently amended)

Drafting that will enable a protected earnings cap to be introduced by regulations

New section 45C:

45C – Total of all amounts outstanding under high-cost consumer credit contracts must not exceed prescribed proportion of borrower's income

The total amount outstanding (including interest and all fees) in relation to all high-cost consumer credit contracts under which a borrower has an outstanding liability (whether due to be repaid or not at that point) at any point in time must not exceed the proportion of the borrower's net income prescribed by regulation.

In section 138 (1)(f) insert a new section (fd) that reads:

(fd) prescribing the maximum amount that may be outstanding at any time under all high-cost consumer credit contracts for any borrower or all borrowers or any class of borrowers, by reference to the borrower's net or gross income.

Appendix 5

Anti-avoidance clauses in the Australian Treasury Draft Legislation for the National Consumer Credit Protection Amendment (Small Amount Credit Contract and Consumer Lease Reforms) Bill 2017

323A Prohibition on avoidance in relation to small amount credit contracts and consumer leases

Prohibition on avoidance

(1) A person must not (either alone or with others) enter into, or carry out (to any extent), a scheme if it is reasonable to conclude that a purpose of the person doing so is to prevent a contract (the ***contrived contract***) covered by the following paragraphs from being a small amount credit contract or a consumer lease:

(a) the contract is between a consumer and either the person or someone else who is or was connected with the person;

(b) the contract is connected with the scheme.
Civil penalty: 2,000 penalty units.

*Meaning of **scheme***

(2) A ***scheme*** is:

(a) any agreement, arrangement, understanding, promise or undertaking, whether express or implied; or

(b) any scheme, plan, proposal, action, course of action or course of conduct, whether unilateral or otherwise.

Whether it is reasonable to draw conclusion as to purpose

(3) For the purpose of determining whether it is reasonable to draw a conclusion described in subsection (1):

(a) regard must be had to the extent to which the circumstances described in subsection (4) exist; and

(b) the more any of those circumstances exist, the more it is reasonable to draw that conclusion.

This does not limit the matters to which regard may be had in making the determination.

(4) The circumstances are as follows:

(a) the contrived contract or the scheme has a similar effect, operation or structure to a small amount credit contract or consumer lease, but the contrived contract is not a small amount credit contract or consumer lease because of the artificiality or complexity of the contrived contract or scheme or because of one or more of the following:

(i) there are more parties to the contrived contract or scheme than is necessary for the provision of credit, or hire of goods, to the consumer;

(ii) there are more elements of the scheme than are necessary for the provision of credit to the consumer under a small amount credit contract or for the

hire of goods to the consumer under a consumer lease;

(iii) the contrived contract deals with fewer transactions than are reasonable, but the scheme deals with at least as many transactions as are reasonable, for the provision of credit to the consumer under a small amount credit contract or for the hire of goods to the consumer under a consumer lease;

(b) the consumer has been or is to be charged in connection with the contrived contract an amount (however described) that, if the contrived contract were a small amount credit contract or consumer lease:

(i) would be a fee, charge or liability whose imposition is prohibited by section 23A or 31A of the National Credit Code; or

(ii) the consumer would not be liable to pay because of the operation of section 175AB or 175AC of the National Credit Code;

(c) the consumer is required to pay under the contrived contract:

(i) repayments that, if the contrived contract was a small amount credit contract and another party to that contract had been a licensee, the consumer could not have been required to pay under the contract because of the operation of section 133CC, 133CD or 133CE; or

(ii) amounts that, if the contrived contract was a consumer lease and another party to that contract was a licensee, the consumer could not have lawfully been required to pay because of the operation of section 156A or 156B of the Act;

(d) if:

(i) the contrived contract was a small amount credit contract or a consumer lease; or

(ii) the scheme had resulted in the entry into a small amount credit contract or consumer lease with a consumer or the making of an offer to a consumer to enter into a small amount credit contract or a consumer lease;

the person or someone else connected to the person would, if they had been a licensee, have contravened any of the provisions in Parts 3-2C, 3-3, or 3-4;

(e) both of the following apply in relation to the consumer's financial obligations under the contrived contract or under any aspect of the scheme:

(i) the person or someone else connected with the person has secured or will secure the performance of those obligations by taking an interest in the consumer's principal place of residence, a motor vehicle of the consumer or goods of the consumer that are essential household property for the purposes of section 50 of the National Credit Code (the ***mortgaged property***);

(ii) it is reasonable to assume that the person took the security because:

(A) the consumer would likely only be able to comply with their financial obligations under the contract by selling the mortgaged property; or

(B) the person did not make reasonable inquiries into whether the consumer would only be able to comply with their financial obligations under the contract (or under another aspect of the scheme) by selling the mortgaged property;

(f) the person, or someone who is or was connected with the person:

(i) represents to any consumer that the person or someone who is or was connected with the person could provide credit or finance (however described) or hire goods to a consumer where, if the consumer entered into a small amount credit contract or consumer lease whose terms comply with

this Act, that contract would likely be unsuitable for that consumer for the reason described in paragraphs 123(2)(a), 133(2)(a), 146(2)(a) or 156(2)(a); or

(ii) represents that the person or someone who is connected with the person would provide credit or finance (however described) or hire goods where a reasonable person would conclude that the representation is directed to a class of consumers whose members are more likely than people who are not members of the class to, if they entered into a small amount credit contract or a consumer lease whose terms comply with this Act, have entered into a small amount credit contract or consumer lease that would likely be unsuitable for the reason described in paragraphs 123(2)(a), 133(2)(a), 146(2)(a) or 156(2)(a);

(g) one or more suggestions are or were made to the consumer that the consumer give, in connection with the scheme or the contrived contract, information that:

(i) is not true, or does not accurately reflect the consumer's intention, when the information is, or is to be, given; and

(ii) relates to a matter relevant to determining whether the contrived contract is a small amount credit contract or consumer lease;

(h) all of the following apply:

(i) before the scheme is carried out, the person, or someone who is or was connected with the person, carried on a business of providing credit or hiring goods to consumers in a different way (the ***old way***);

(ii) there has been a change in the law relating to the providing of credit, or hiring of goods, to consumers since the business was carried on in the old way;

(iii) had whoever carried on the business continued to do so in the old way, he or she would, because of the change in the law, have been subject to obligations to which he or she was not subject when carrying on the business in the old way;

(i) the scheme is or has been advertised or promoted to consumers in a manner:

(i) that a reasonable person would conclude was likely to give consumers the impression that the scheme would likely result in an offer to enter into, or entry into, a small amount credit contract or consumer lease; or

(ii) that indicates that consumers will be provided with access to a small amount credit contract or consumer lease; and

that is inconsistent with the legal operation or effect of the scheme;

(j) the person, or someone who is connected with the person, has advertised or promoted the scheme in circumstances where they do not offer small amount credit contracts or consumer leases in the ordinary course of business;

(k) the person, or one or more others who are or were connected with the person, are or were inappropriate persons as defined in regulation 3 of the *National Consumer Credit Protection Regulations 2010.*

Offence

(5) A person commits an offence if:

(a) the person is subject to a requirement under subsection (1); and

(b) the person engages in conduct; and

(c) the conduct contravenes the requirements.

Criminal penalty: 120 penalty units, or two years imprisonment, or both.

Presumption of avoidance for certain schemes

(6) For the purposes of subsection (1) (but not for the purposes of subsection (5)), if:

(a) the person engages in conduct of the kind referred to in paragraph (1)(a) or (b) in relation to a scheme; and

(b) the scheme is of a kind prescribed by the regulations or determined by ASIC under subsection (8);

then it is presumed that it would be reasonable to conclude that the purpose, or one of the purposes, of the person engaging in that conduct was to prevent a contract from being a small amount credit contract or a consumer lease.

(7) Subsection (6) does not apply if the person proves that, having regard to the matters referred to in subsection (4), it would not be reasonable to conclude that the purpose, or one of the purposes, of the person engaging in that conduct was to prevent the contract being a small amount consumer contract or consumer lease.

(8) ASIC may, by legislative instrument, determine a scheme for the purposes of subsection (6).

Exceptions

(9) This section is subject to section 323B (Schemes and conduct that are not prohibited).

Note: Section 179 provides for remedies for persons who suffer loss or damage as a result of a contravention of this section.

323B Schemes and conduct that are not prohibited

(1) Subsection 323A(1) does not apply to a scheme which is connected with a contract that:

(a) is a contract for the provision of credit to which the National Credit Code would apply apart from section 6, 203A or 203B of the National Credit Code; or

(b) would be a consumer lease apart from section 171, 203A or 203B of the National Credit Code.

(2) Subsection 323A(1) does not apply to conduct by a person if:

(a) the person is exempt from subsection 29(1) under section 109 or regulations made for the purposes of section 110; or

(b) both the following apply:

(i) the conduct would be a credit activity if a contract connected with the scheme were a small amount credit contract or a consumer lease;

(ii) credit activity of that kind is exempt from subsection 29(1) under section 109 or regulations made for the purposes of section 110.

323C Further prohibition on avoidance in relation to small amount consumer contracts and consumer leases

Prohibition on avoidance

(1) A person must not (either alone or with others) enter into, or carry out (to any extent), a scheme if it is reasonable to conclude that a purpose of the person doing so is to avoid the application of a provision of this Act that would apply in respect of:

(a) a consumer lease but not a credit contract; or

(b) a small amount credit contract but not:

(i) a consumer lease; or

(ii) a credit contract that is not a small amount credit contract;

in relation to:

(c) the person; or

(d) any other person (a ***connected person***) who has, or has had, any connection (whether of a business, family or other nature) with the person.

Civil penalty: 2,000 penalty units.

*Meaning of **scheme***

(2) A ***scheme*** is:

(a) any agreement, arrangement, understanding, promise or undertaking, whether express or implied; or

(b) any scheme, plan, proposal, action, course of action or course of conduct, whether unilateral or otherwise.

Whether it is reasonable to draw conclusion as to purpose

(3) For the purpose of determining whether it is reasonable to draw a conclusion described in subsection (1):

(a) regard must be had to the extent to which the circumstances described in subsection (4) exist; and

(b) the more any of those circumstances exist, the more it is reasonable to draw that conclusion.

This does not limit the matters to which regard may be had in making the determination.

(4) The circumstances are as follows:

(a) each of the following apply:

(i) the person, or a connected person, has a practice of changing or otherwise altering the operation or effect of a credit contract or consumer lease after, or at the time, it has been entered into; and

(ii) the effect of the change or alteration is disadvantageous to the consumer who is a debtor under the credit contract or the lessee under a consumer lease because it results in the avoidance of provisions of the Act that would otherwise have applied for the benefit of the consumer had they entered into a small amount credit contract or consumer lease; and

(iii) the person, or a connected person, has made the change or alteration:

(A) unilaterally; or

(B) without reference to, or consideration of, the consumer's financial situation;

(b) the circumstances prescribed by the regulations.

(5) A person commits an offence if:

(a) the person is subject to a requirement under subsection (1); and

(b) the person engages in conduct; and

(c) the conduct contravenes the requirements.

Criminal penalty: 120 penalty units, or two years imprisonment, or both.

Presumption of avoidance for certain schemes

(6) For the purposes of subsection (1) (but not for the purposes of subsection (5)), if:

(a) the person engages in conduct of the kind referred to in paragraph (1)(a) or (b) in relation to a scheme; and

(b) the scheme is of a kind prescribed by the regulations or determined by ASIC under subsection (8);

then it is presumed that it would be reasonable to conclude that the purpose, or one of the purposes, of the person engaging in that conduct was to avoid the application of a provision of this Act.

(7) Subsection (6) does not apply if the person proves that, having regard to the matters referred to in subsection (4), it would not be reasonable to conclude that the purpose, or one of the purposes, of the person engaging in that conduct was to avoid the application of a provision of this Act.

(8) ASIC may, by legislative instrument, determine a scheme for the purposes of subsection (6).

323D Exemption by ASIC

(1) ASIC may, by legislative instrument, exempt a scheme, or class of schemes, from all or specified provisions of sections 323A and 323C.

(2) An exemption may apply subject to any specific conditions imposed by ASIC.

Appendix 6

International comparisons of debt collection regulation

	Australia	United Kingdom	United States	New Zealand current	New Zealand proposed
Debt collectors required to provide information to debtors	Yes	Yes	Yes	No	Yes
Debt collectors prohibited from pressuring debtors to agree to unreasonable repayment plans	Yes	Yes	No (but general duty of fairness)	No	No
Debt collectors' contact with debtors regulated	Yes	Yes	Yes	No	No

Australia

In Australia, debt collection is regulated under the Competition and Consumer Act 2010. Specific guidelines (produced by the Australian Competition and Consumer Commission and the Australian Securities and Investments Commission) provide guidance to debt collectors on how to ensure compliance with the law.

The guidelines state that when the debt collector makes initial contact with the debtor, the collector should provide the debtor with basic information about the debt. Additionally, any request for information by the debtor must be addressed without delay.

Repayment negotiations with debtors should be "realistic" and "flexible". Such an approach requires debt collectors to take account of living expenses, whether a debtor is on a fixed low income (for example a disability pension or other welfare payments), and to ensure that repayment plans are meaningful and sustainable.

The guidelines feature extensive detail regarding contact between debt collectors and debtors. The guidelines stipulate appropriate hours of contact and advise that debt collectors should only contact

the debtor when necessary, and not more than three times per week or 10 times per month at most. The guidelines also state that face-to-face contact should be avoided, and in particular debt collectors should not turn up uninvited at the debtor's workplace.

In some cases, the debt collector should stop contacting the debtor, for example if there is a dispute about the debt or if a payment plan has been set up and is being followed (unless the debt collector has reasonable grounds to assume that the financial position of the debtor has changed). Once a debt collector knows that a debtor is represented, they must not continue to contact the debtor directly.

United Kingdom

Debt collection law is regulated by multiple statutes in the United Kingdom. The United Kingdom's Financial Conduct Authority (the body which regulates debt collectors) published detailed obligations for debt collectors in the Consumer Credit sourcebook.

If the original lender assigns debt to a debt collector, the lender must notify the debtor of this. Additionally, a debt collector must provide the debtor with information on the amount of any arrears and the balance owing.

Debt collectors must treat borrowers in default or in arrears difficulties with forbearance and due consideration. Collectors must not refuse to negotiate with a debtor who is developing a repayment plan and must allow for alternative, affordable payment amounts to repay the debt in full. Debtors must be given reasonable time to prepare for a visit from a debt collector and should not be coerced or pressurised into immediate discussions or decisions.

The Consumer Credit sourcebook also sets out clear requirements regarding contact between the debt collector and debtor. For example, debt collectors must not contact debtors at unreasonable times and must not act in a way likely to be publicly embarrassing to the debtor. The Sourcebook sets out what type of behaviour is not appropriate if a debt collector visits the debtor's house, for example, the collector must not act in a threatening manner.

United States

In the United States, debt collection is regulated by the Fair Debt Collection Practices Act 15 U.S.C. 1692.

The Act requires debt collectors to provide debtors with information about the debt within five days of first contact.

There is no specific law regarding the negotiation of repayment plans. However, there is a general prohibition on debt collectors from collecting any debt using unfair or unconscionable means.

The Act contains an overriding prohibition on debt collectors from harassing, oppressing or abusing debtors. Additionally, the debt collector must not make contact at inconvenient times and places and should not make contact before 8am or after 9pm (unless a contrary arrangement is made with the debtor). Debtors are also entitled to request that debt collectors cease contact and if the debtor does this, the debt collector may only contact the debtor to inform them that further efforts to collect will be terminated and that they (the debt collector) may invoke other remedies.

Attached reports

The following reports have been attached to this document for further information. These reports were produced with support of the Michael and Suzanne Borrin Foundation.

Appendix 7

High Cost Lending - Report by BERL

Appendix 8

Working Towards a Fairer Consumer Credit Market - Report by Victoria Stace and Professor Jeremy Finn

Appendix 9

Survey of financial mentoring and budgeting services in Aotearoa on high cost loans, debt collection and other consumer credit issues by Dr Liz Gordon