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20 June 2024

Consumer Policy
Building, Resources and Markets
Ministry of Business, Innovation and Employment

By email: consumer@mbie.govt.nz

Submission to the Ministry of Business, Innovation & Employment

Fit for Purpose Consumer Credit Legislation – Discussion Document May 2024

Credit Corp Financial Solutions Pty Limited, trading as Wallet Wizard ('**Wallet Wizard**'), is grateful to the Ministry for the opportunity to respond to its draft discussion document: *Fit for Purpose Consumer Credit Legislation* ('**the Paper**').

Wallet Wizard is an online lender offering New Zealand consumers responsibly lent, affordable loans between $500 and $8000. The Wallet Wizard product operates as an unsecured revolving credit contact, with affordable weekly or fortnightly repayment amounts. The product offers choice to consumers with limited borrowing alternatives. The only cost of borrowing is an annual interest rate of 47.8% per annum on the drawn balance and a low, one-off, establishment fee of $12. No default, late payment, or early repayment fees apply. The interest rate applicable to our product is 83.6% lower than the maximum interest rate cap applicable to high cost credit contracts.

Wallet Wizard offers choice to consumers who are excluded from mainstream borrowing. Absent such choice, these consumer would typically resort to payday loans from high cost credit providers which operate on interest rates as high as 292% per annum and typically require repayment over very short terms.

We are concerned that the proposal to reduce the high cost credit threshold to 30% would, due to the negative perception attached to the label 'high cost credit', cause institutional lenders (financiers of lenders in the sector) to retreat from the sector, limiting access to funding and reducing competition.

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Further, we are concerned that a reduction in the threshold for the high cost credit definition would mean that more lenders will become subject to the high cost credit provisions at s45G of the *Consumer Contracts and Consumer Finance Act 2003* ('**CCCFA**'), preventing lenders with rates between 30% and 50% from approving loans for consumers with current or recent high cost credit contracts. This will restrict consumers' access to more suitable lending alternatives, and lead to poor consumer outcomes.

High Cost Credit

Financial mentors and consumer advocates in New Zealand and internationally have long expressed concern with the payday lending model, due to the high interest rates and short repayment terms. The short repayment terms require unsustainably large repayments. This causes consumers to fall behind on other liabilities while they meet those repayments, leading to a cycle of repeat borrowing known as a 'debt spiral', the effect of which is that consumers carry a perpetual liability at extremely high interest rates.

The government has recognised the consumer harm caused by repeat borrowing under payday loans, and in 2022 it legislated to address the harm, enacting the high-cost credit provisions[1]. These provisions restrict high cost credit providers from entering into new high cost consumer credit contracts where the applicant has:

a) an unpaid balance on any other high-cost consumer credit contract, or has had an unpaid balance on any other high-cost consumer credit contract in the preceding 15 days; or
b) entered into two or more high-cost consumer credit contracts in the past 90 days.

While the government's enactment of the high cost credit provisions has been helpful in addressing the consumer harm caused by repeat borrowing under high cost credit, there are other important reasons why the high cost credit sector has been in decline. First, there has been strong competition from market disrupters such as Wallet Wizard, offering cheaper and more sustainable loans. As outlined in the Paper, nine former HCC lenders have redesigned their product, reducing interest rates below the current 50% threshold to avoid being labelled 'high cost credit'. This has offered greater choice of products at lower interest rates for consumers with limited borrowing alternatives.

Another key reason that payday lending by high cost credit providers has been in sharp decline is access to funding. Large institutional lenders, who place significant value in their reputation, do not want their brand associated with the negatively perceived 'high cost credit' label. Accordingly, institutional lenders have no appetite for exposure to this market sector. Labelling products between 30% and 50% as 'high cost credit' is likely to see an exodus from

[1] See section 45G – High-cost consumer credit contracts with certain repeat debtors prohibited.

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the sector by these institutional lenders, which will impact funding for those lenders who have brought market disruption and competition to the sector. If funding remains available, it is likely to be more expensive, resulting in products becoming unviable or increased costs of credit.

As outlined in the Paper, a reduction in the threshold to 30% will mean that the product offerings of at least 26 lenders will newly attract the label of 'high cost credit'. This number is likely to be understated, as loans with lower APR's which are subject to default interest rates may also fall in scope of the high cost credit definition. Each of these lenders are important market participants, bringing strong competition to the sector.

While lenders have been able to reduce rates to avoid the "high cost credit" label based on current thresholds, lenders are unlikely to be able to respond to further reductions in the threshold by reducing rates further, as the economics will not allow a further reduction in interest rates while making credit available for consumers in this market sector. Costs borne by lenders are largely fixed, regardless of the amount of credit advanced. Accordingly, lenders who serve borrowers' needs for smaller credit amounts over shorter durations incur similar operational and compliance costs to those incurred by lenders of larger sums over longer terms. Costs are therefore disproportionately higher for smaller amount lenders, necessitating a higher interest rate.

The inability to lower rates further while maintaining a viable product offering would likely decrease the availability of credit for consumers who already have limited borrowing options, further restricting their access to credit.

In the event that lenders' funding arrangements are impacted, many will elect, or be forced, to exit the sector. This is particularly true of larger international operators who may elect to depart New Zealand, a jurisdiction which is already less attractive due to the inability to achieve the same economies of scale that may be achieved in more populous jurisdictions. This would be more likely if laws in New Zealand were less favourable than other comparable jurisdictions. In Australia, the interest cap applicable to mainstream consumer lending under the *National Consumer Credit Protection Act 2009* is a 48% annual percentage rate. We understand that in the United Kingdom, high-cost short-term credit is defined as credit agreements with annual percentage rates of 100% or more which are due to be repaid within 12 months. In the UK, more responsible and conventionally funded providers have chosen to operate at an annual percentage rate just under 50%. In the event New Zealand becomes comparatively less favourable, more responsible lenders are likely to elect to deploy capital in more favourable jurisdictions, leaving reduced competition, and allowing high cost lenders to once again re-emerge in a less competitive market.

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While the key objectives of the proposed reforms are to improve outcomes for consumers and improve appropriate access to credit, setting the threshold for high cost credit to 30% per annum will have exactly the opposite effect.

We understand that one consideration for proposing to reduce the threshold of high cost credit is to ensure that lenders take greater steps in their responsible lending assessments in circumstances where the risks of consumer detriment from errors in the assessment are heightened. We note that the CCCFA already requires a lender to take "reasonable steps" to ensure the borrower will make payments under the contract without substantial hardship. This obligation is further echoed in the Responsible Lending Code. These obligations are scalable and the "reasonableness" of the steps a lender takes will have regard to the risk of consumer harm if there are errors in the assessment. A high interest rate may be one factor in determining what is "reasonable". However, it is not the sole factor. Other factors may include things such as the size of the repayment, the proportion of the payment relative to the consumer's available disposable income, the default fees that may apply, the duration of the loan, amongst other things. We consider that the existing scalable obligations under the CCCFA already adequately address the risk of consumer harm.

Recommendation:

We strongly encourage MBIE to give consideration to the undesirable outcomes that are likely to flow from a reduction to the high cost credit threshold, and maintain the status quo, with the threshold for high cost credit remaining at 50% per annum.

Best Regards

Privacy of natural persons

James Treloar
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Credit Corp Financial Solutions Pty Limited – Trading as Wallet Wizard

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