Submission on discussion document: Consumer Credit Regulation Review

Your name and organisation

Name	Clementine Baker
Organisation	

Responses to discussion document questions

Regarding the excessive cost of some consumer credit agreements

1	Do you agree that the problems identified with high-cost lending (even where it is compliant with the CCCFA) are significant? Do you have any information or data that sheds light on their frequency and severity?
	Yes
2	Do you support any of the extensions of Cap Option A? What would be the impact of these extensions on borrowers, lenders and the credit markets? Do you have any information or data that would support an assessment of the impact of these extensions?
	[Insert response here]
3	Do you agree with our assessment of the costs and benefits of the options for capping interest and fees? Are any costs or benefits missing? Do you have any information or data that would help us to assess the degree or estimate the size of these costs and benefits?
	[Insert response here]
4	Do you have any suggestions for the design of options for capping interest and fees? If so, what would be the impact of your proposed design on borrowers, lenders and the credit markets?
	[Insert response here]
5	Which interest rate cap options, if any, would you prefer? Which interest rate options would you not support? Please explain how you made your assessment.
	[Insert response here]

Regarding continued irresponsible lending and other non-compliance

6	If directors have duties to take reasonable steps to ensure that the creditor complies with its' CCCFA obligations, should any duties apply to senior managers?
	[Insert response here]
7	If there are to be more prescriptive requirements for conducting affordability assessments, what types of lenders or loans should these apply to?
	[Insert response here]
8	Should there be any change to the requirement that lenders can rely on information provided by the borrower unless the lender has reasonable grounds to believe the information is not reliable? What would be the impact of such a change on borrowers, lenders and the credit markets?
	[Insert response here]
9	Do you consider there should be any changes to the current advertising requirements in the Responsible Lending Code? If so, what would be the impact of those changes on borrowers, lenders and the credit markets?
	[Insert response here]
10	Do you agree with our assessment of the costs and benefits of the options to reduce irresponsible lending and other non-compliance? Are any costs or benefits missing? Do you have any information or data that would help us to assess the degree or estimate the size of these costs and benefits?
	[Insert response here]
11	Do you have any suggestions for the design of options for reducing irresponsible lending and other non-compliance? If so, what would be the impact of your proposed options on borrowers, lenders and the credit markets?
	[Insert response here]
12	Which options for reducing irresponsible lending and other non-compliance would you support? Which would you not support? Please explain how you made your assessment.

	[Insert response here]

Regarding continued predatory behaviour by mobile traders

13	Do you agree with our assessment of the costs and benefits of the options for covering additional credit contracts under the CCCFA? Are any costs or benefits missing? Do you have any information or data that would help us to assess the degree or estimate the size of these costs and benefits?
	[Insert response here]
14	Do you have any suggestions for the design of options for covering additional credit contracts under the CCCFA? If so, what would be the impact of your proposed options on borrowers, lenders and the credit markets?
	[Insert response here]
15	Which options for changes to cover additional credit contracts would you support? Which would you not support? Please explain how you made your assessment.
	[Insert response here]

Regarding unreasonable fees

16	If prescribed fee caps were introduced, who should they apply to, and what process and criteria should be used to set them?
	[Insert response here]
17	Do you agree with our assessment of the costs and benefits of the options for capping interest and fees? Are any costs or benefits missing? Do you have any information or data that would help us to assess the degree or estimate the size of these costs and benefits?
	[Insert response here]
18	Do you have any suggestions for the design of options for reducing unreasonable fees? If so, what would be the impact of your proposed options on borrowers, lenders and the credit markets?

	[Insert response here]
19	Which options for changes to fees regulation would you support? Which would you not support? Please explain how you made your assessment.
	[Insert response here]
20	Have you seen issues with excessive broker fees, or other unavoidable fees charged by third parties, being added to the loan? If so, are there any specific changes that should be made to the regulation of third-party fees? What would be the impact of these changes on lenders, borrowers and third parties?
	[Insert response here]

Regarding irresponsible debt collection practices

21	Is this an accurate picture of the problems for consumers experiencing debt collection? Do you have information that confirms or refutes these issues, or sheds light on how widespread or severe they are?
	[Insert response here]
22	What information should be provided to borrowers by debt collectors? When and how should this information be provided?
	[Insert response here]
23	Do you agree with our assessment of the costs and benefits of the options for addressing irresponsible debt collection? Are any costs or benefits missing? Do you have any information or data that would help us to assess the degree or estimate the size of these costs and benefits?
	See StepChange research into the costs
24	Do you have any suggestions for the design of options for addressing irresponsible debt collection? In particular, what is an appropriate frequency of contact with debtors before (and then after) a payment arrangement is entered into? Please state the likely impact of your proposed options on borrowers, lenders and the credit market.
	See below for more detailed comments. One option is to support a charitable debt collection service.

25	Which options for changes to the regulation of debt collection would you support? Which would you not support? Please explain how you made your assessment.
	[Insert response here]

Regarding other issues

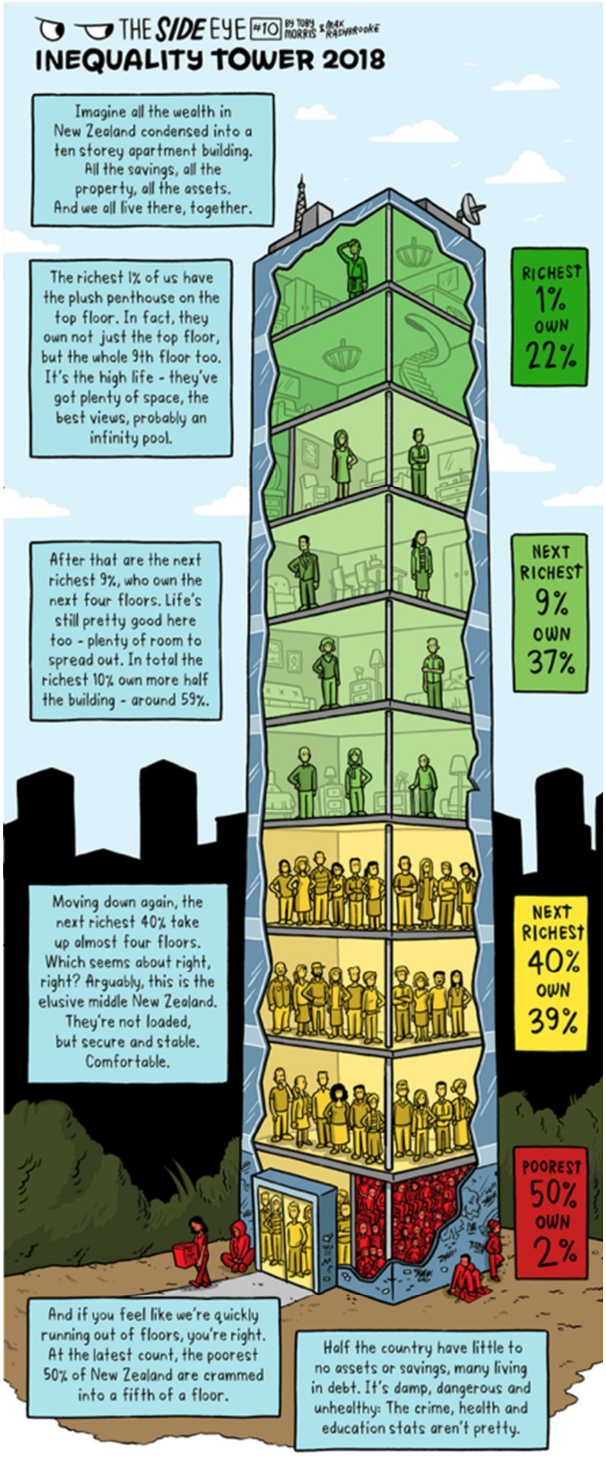
26	Are you seeing harm from loans to small businesses, retail investors or family trusts as a result of them not being regulated under the CCCFA?
	[Insert response here]
27	Do you think small businesses, retail investors or family trusts should have the same or similar protections to consumers under the CCCFA? Please explain why/why not.
	[Insert response here]
28	Are there any other issues with the CCCFA or its impact on vulnerable people that are not addressed in this discussion paper? If so, what options should MBIE consider to address these issues?
	[Insert response here]

Any other comments

	We welcome any other comments that you may have.
	See Below

Addressing problem debt In New Zealand

Addressing problem debt should be a top priority for policy-makers if we want to keep more people in work, paying taxes and contributing to the economy; keep families in their homes; and relieve the pressure on relationships and family life. To address problem debt and break the growing link between financial difficulties and long-term negative outcomes, we must prevent people from falling into problem debt and we must help people when they are in debt.



New Zealanders are struggling with problem debt

New Zealanders are spending $2 billion a year on interest payments on consumer loans[1] and then more again on establishment fees, pre-payment fees and default fees. One in 3 New Zealanders isn't paying off their credit card every month[2] and excessive use of credit facilities is the second biggest cause of insolvency[3]. Consumer advocates say debt collection practices are creating significant additional stress, mental health problems, relationship issues and family violence[4].

We know there is a problem, but we don't have comprehensive clear statistics on the scale of the problem in New Zealand. No single lender can communicate the extent of the issue because their borrowers are likely to have debt with multiple lenders. It is also difficult to collect data on a large scale about the social cost of problem debt.

The Side Eye's graphic representation of financial inequality in New Zealand[5] paints a bleak picture. It reveals why so many New Zealanders are forced to rely on credit to pay essential bills, to last until the next pay day and, increasingly, to keep up with existing credit commitments. And why budget advisors report that a growing number of New Zealanders have little or no financial resilience to cope with unexpected life events such as relationship breakdown, a change in employment or ill health.

[1] 2017 Reserve Bank statistics
[2] Illion, 2017
[3] 2016/17 MBIE
[4] MBIE Review of Consumer Credit Law discussion paper, 2018
[5] *https://thespinoff.co.nz/society/31-07-2018/the-side-eye-inequality-tower-2018/*

Why is problem debt a problem?

Problem debt causes significant economic and social costs for individuals, families, lenders and governments. Comprehensive international research reveals how problem debt affects people and estimates that it could be costing society around $5,400 for every person struggling with severe problem debt[6].

Problem debt costs the UK £8.3bn through the damage it causes to family life, mental and physical health, productivity and employment prospects as well as costs to the welfare state, the NHS, local government and other agencies[7]. This does not include the potential effects of creditors' losses as a result of problem debt. The negative effects of problem debt lead to costly negative outcomes for individuals and their families, particularly where people are experiencing underlying social, economic or health problems. These negative effects can include:

- Housing problems. People falling behind on their rent or mortgage risk losing their home or being forced to move.
- Employment costs. Stress, anxiety and other factors can undermine employment productivity, prolong unemployment and lead to people losing their job.
- Mental health problems. Debt pressures can exacerbate mental health conditions, such as stress, anxiety and insomnia.
- Older people's care. Deteriorating health can lead to older people needing extra and earlier care.
- Relationship problems. Debt stress can lead to pressure on relationships and breakups.
- Children's care. Mental health problems and relationship difficulties can lead to children in already precarious families being taken into care.
- Physical health problems. Debt stress can lead to physical health problems and greater pressure on health services.

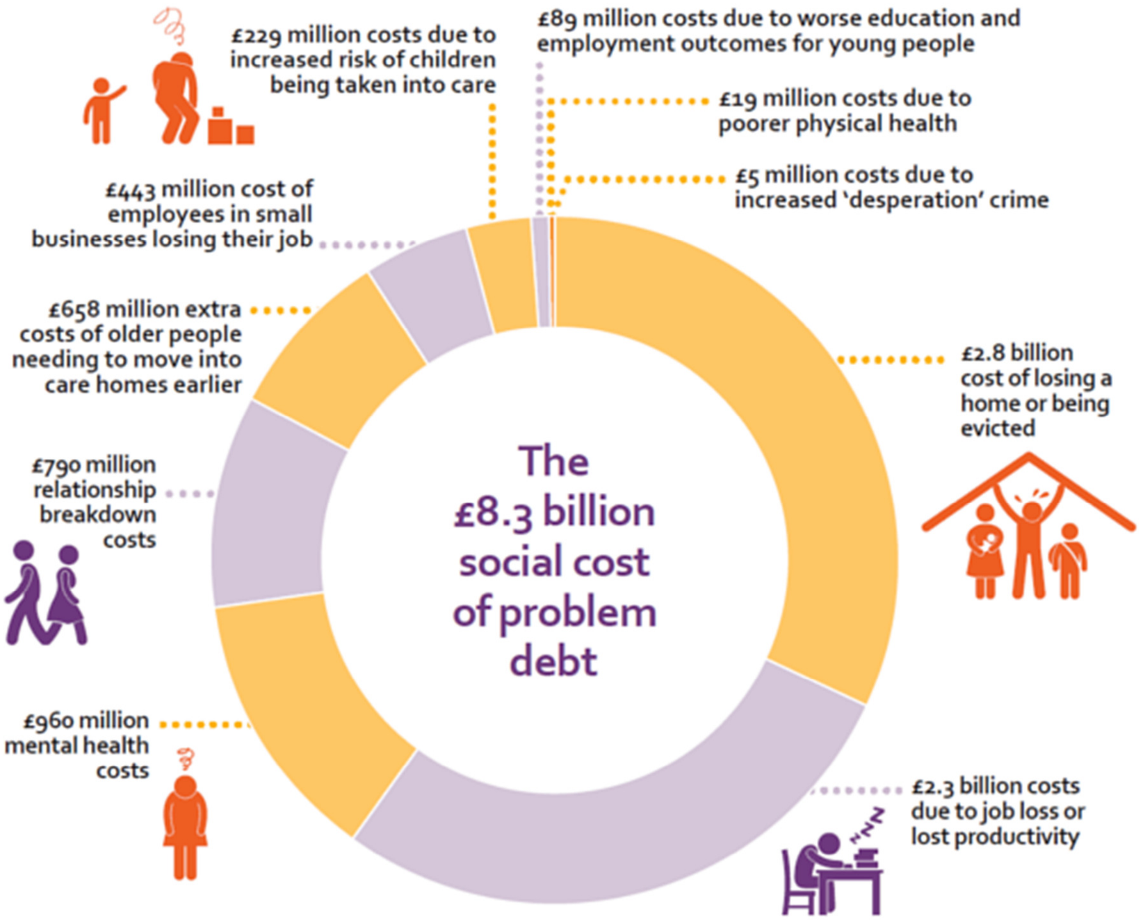
These are things that cost the government money and cause banks to lose customers.

A case study from the UK:

Jane was forced to move into rented accommodation with her son after fleeing a violent relationship. Despite working full-time in IT, Jane needed to use credit to keep up with high bills, eventually turning to payday loans. She became depressed as her debt spiralled quickly, with £3,658 worth of unsecured debt, a county court judgement for £1,355 as well as owing £3,500 to a family member, and the same amount to a friend. But exhausting support from family and friends led her to feel more isolated. Without support from StepChange Debt Charity, her depression could have risked her job, destitution could have prompted her to move back in with her abusive partner or become homeless, leading to other longer term costs for her and her son. (StepChange ***8 Billion Challenge***)

[6] StepChange Debt Charity has been operating in the UK for 25 years and has helped 5 million people to repay £4 billion of their debts. StepChange has undertaken a Social Return on Investment analysis of the cost of problem debt. StepChange estimates that the cost to society is £2,800 per person struggling with severe problem debt. https://www.stepchange.org/about-us/our-history.aspx

[7] Baker Tilly Report commissioned by StepChange: https://www.stepchange.org/policy-and-research/social-cost-of-debt.aspx



What can be done?

Problem debt can be caused by an unexpected life event like lost or reduced employment, illness or family breakups. Severe problem debt is more likely, more harmful and harder to deal with when there are bad lending decisions, poor product design and aggressive debt collection practices.

Change is needed to reduce the harm these practices cause for people with problem debt. Below are some proposed measures.

- Strengthen the affordability test

A strengthened and monitored affordability test is important for ensuring people are not borrowing when the cost of repaying the loan will cause them financial hardship. The focus of the affordability test should be on protecting people from being in a position where their inability to repay the loan would cause financial hardship. Some social lenders, like Good Shepherd Microfinance, are able to lend with no interest, meaning there is less risk of financial hardship in the event that they cannot repay within the agreed period. The affordability test could have a lower threshold where there is less risk for the borrower.

- Disincentivise bad practice

The affordability test is unlikely to be used properly if lenders are financially incentivised to do the opposite. Lenders are currently earning significant revenue from people experiencing hardship due to high default fees, high interest rates, minimal regulation around debt collection practice and few safeguards for people experiencing hardship. Some lenders are even targeting people with limited capacity to repay. This suggests that the current arrangement goes well beyond compensating lenders for the losses associated with lending to high-risk borrowers.

The social costs of problem debt to individuals, families and New Zealand are so great that the onus should be put on all creditors to ensure they are treating people experiencing hardship with care both at the time of giving a loan, and when collecting debts. The onus should not be on the person experiencing hardship to prove that they are, in fact, experiencing hardship. There should be appropriate oversight and penalties to disincentivise bad practice.

In Australia the banking industry is improving financial hardship assistance programs with new commitments to be included in the new Code of Banking Practice. For example, banks will proactively identify if someone is at risk of getting into financial difficulty so they can work with their customer to help prevent a situation worsening.[8]

- Cap the costs

To protect people at risk of financial hardship, the legislation could cap the costs associated with loans including:

- Putting a cap on interest rates. A small number of lenders are providing very high interest rates of up to 800%. A cap on interest is unlikely to affect most lenders and would benefit at-risk borrowers. Some lenders are concerned that a cap on interest rates would drive some lenders underground, but there is limited evidence of the extent to which that would happen and how much more social harm that would cause than the existing harm.
- no establishment fee or an establishment fee cap. I have spoken to accountants who have been asked by lenders to arrange their accounts in such a way as to inflate the cost of giving a loan so they can charge higher establishment fees.
- A limit on the number of different types of fees and charges that can be attached to a loan. It can be hard for consumers to understand the full cost and compare offerings from different lenders when there are so many different costs associated with a loan. These costs can include interest, credit fees, default fees, establishment fees, prepayment fees.

In the UK, the high cost short term credit market adapted to regulation imposing a maximum cost. The lenders introduced instalment loans, typically between 3-6 months, rather than the (intended) one month repayment period that was typical of payday loans. Meaning that although repayments may be lower and more manageable, there's more time for interest to build up making them more expensive overall. This suggests that regulating loan costs should be comprehensive, putting a cap on the total possible costs payable against a loan.

- Better debt collection – Fair Share approach

Debt collection practices should be based on supporting affordable and sustainable repayments and providing appropriate support to help customers in financial difficulties.

[8] ***https://www.betterbanking.net.au/wp-content/uploads/2017/05/ABA-Industry-Annual-Report-Banking-Reform-Program.pdf***

Fair, safe debt collection would be made easier if all lenders were required to subscribe to a fair share type model. The model requires that if a majority of lenders to a particular individual agree to a debt repayment agreement, then all lenders must agree. A fair share arrangement can ensure all creditors are equally supporting the individuals. It can give creditors comfort that they are not forgiving more of the debt than their competitors. It can also ensure creditors are not financially punished for being careful when dealing with people experiencing hardship. One of the reasons creditors and debt collectors chase so aggressively is that when there are signs a person may struggle to repay, they want to ensure it is their debt that's repaid over other creditors. The fair share arrangement could prevent this, and reduce the incentive on creditors to pursue aggressively. Individuals are then better able to be supported to repay as much of their debt as is safe for them to repay.

People should continue to be protected if their debt is either passed on to a third party agency or sold. In the event that debt is sold, both the original lender, and the third party should carry a responsibility to treat the lender with care.

Government should also commit to the highest standards in debt collection practice where it acts as a creditor, for example when collecting court fines. There should be a responsibility on anyone seeking to recover money from people to take care when that person is experiencing hardship. There is an opportunity for Government to take a leadership position in this. It is very common for people experiencing financial hardship to owe money to the Government. It would help people who are trying to repay their debt if the Government subscribed to the Fair Share approach also.

- Breathing space

The legislation could strengthen the changes that can be made in the event that a person is experiencing hardship. The legislation could require that if a person is experiencing financial hardship, that person is automatically granted breathing space rather than having to apply for it. Breathing space would stop interest, charges and enforcement action to enable people to seek debt advice and stabilise their finances.

UK research has highlighted how when a person is charged additional interest and charges it makes their recovery from financial problems more difficult, thereby reducing the likelihood they will be able to repay the original loan amount. StepChange research of people experiencing financial hardship found that:

- 68% said that default charges made their debt problems harder to deal with.
- 62% said that creditors and debt collectors continued to add fees and charges despite knowing the person was in financial difficulty.
- 52% said creditors and debt collectors continued to add fees and charges after they knew the person was seeking debt advice.

- Free debt advice

Effective free debt advice can support people who are experiencing problem debt.

I am working towards establishing a free debt advice charity service in New Zealand. It would operate as an intermediary between lenders and individuals and partner with existing budgeting and other community services to deliver effective debt advice to more New Zealanders.

StepChange Debt Charity in the UK has proven the value of a free debt advice service. StepChange has supported 5 million people over the past 25 years to repay £4 billion of their debts. In one year StepChange Debt Charity's advice saved £241 million in the social costs of problem debt.[9]

The Australian banks are also working towards the establishment of a debt repayment service to support customers experiencing financial difficulties. Banks are working with financial counsellors to establish a new debt repayment service for people struggling with multiple debts. This new service would be free for people to access and get assistance to put in place a repayment plan to pay off their debts with banks and other lenders and creditors. [10]

Cross-Government debt action plan

Problem debt is a significant problem that requires a broad, cross-Government debt action plan. It is important to consider changes to this legislation as part of a broad objective of addressing problem debt.

[9] https://www.stepchange.org/Portals/0/documents/media/reports/8_billion_challenge.pdf
[10] ***https://www.betterbanking.net.au/wp-content/uploads/2017/05/ABA-Industry-Annual-Report-Banking-Reform-Program.pdf***