

In Confidence

Office of the Minister of Commerce and Consumer Affairs
Chair, Cabinet Economic Development Committee

Review of Consumer Credit Regulation

Proposal

- 1 This paper seeks agreement to proposals to better protect vulnerable consumers from irresponsible lending.

Executive summary

- 2 The Credit Contracts and Consumer Finance Act 2003 (CCCFA) aims to protect borrowers by mandating responsible lending, requiring disclosure of key information to borrowers and prohibiting unreasonable fees. In 2015, reforms to the CCCFA came into force to address concerns about irresponsible lending.
- 3 In December 2017, I commenced a review to assess whether the amendments had been effective at protecting vulnerable consumers, and to identify any further changes that might be needed. Officials consulted a wide range of stakeholders on the effectiveness of the reforms, and a discussion paper was released in June 2018 [DEV-18-MIN-0121].
- 4 The review found that despite the reforms, there is a continued problem of consumers being provided with loans that are unaffordable or unsuitable, and ending up in unmanageable debt. This seriously impacts their lives and those of their families. It particularly affects vulnerable people¹ and those already in hardship². Problem debt exacerbates financial hardship, and can contribute to persistent, intergenerational poverty.
- 5 To address these issues, I am proposing a range of further reforms. The main proposals are to:
 - 5.1 Limit the total accumulation of interest and fees on high-cost loans to 100 per cent of the original loan principal, over the life of the loan. This option would only apply to high-cost lenders, and would aim to prevent unmanageable debt and financial hardship from accumulating large debts from a small loan.
 - 5.2 Require all directors and top executives of lenders offering consumer credit contracts to meet a 'fit and proper person' test, as a requirement of registration on the Financial Service Providers Register. This will help prevent 'phoenix lenders'. I also propose new duties on directors and top executives of lenders to ensure CCCFA compliance by lenders.

¹ Vulnerable consumers, in this context, include those who have low literacy and numeracy, are not confident speakers of English, or are under financial and/or time pressure.

² Among adults in hardship, the following groups are overrepresented: Māori and Pacific peoples, sole parents (who are mostly women), people living in rental housing, and people with disabilities.

- 5.3 Strengthen the enforcement provisions in the CCCFA, including providing civil pecuniary penalties and statutory damages for breaches of responsible lender principles.
- 5.4 Provide greater prescription about how assessments of affordability and suitability must be conducted, and remove the presumption that lenders can rely on information provided by borrowers and guarantors without verification.
- 6 As a package, the changes are intended to reduce problem debt and resulting consumer harms (such as financial hardship and mental and physical health issues). They seek to achieve this by increasing compliance with existing lender responsibility requirements, enabling more efficient enforcement where requirements are not complied with, and lowering the cost of credit for people who default on high-cost loans (whether they are granted responsibly or not).
- 7 One consequence may be a tightening of access to credit, particularly where this was previously being granted in breach of affordability or suitability requirements. Alternative avenues will not necessarily be available or accessible to all families, so there may continue to be service gaps for some consumers. In recognition of this concern I have initiated cross-agency work with the financial services and community sectors on expanding access to microfinance and inclusive banking products. Further, the Ministry of Social Development (MSD) is currently developing a strategy on increasing access to safe credit, with a view to being ready to trial interventions in Quarter 4 of 2019.
- 8 While these credit reforms cannot directly reduce rates of poverty in New Zealand, they do aim to stop private sector lending practices which cause or deepen hardship. These improvements to consumer protection will complement the longer-term work underway at the Commission for Financial Capability and MSD, to lift financial capability.
- 9 *Financial implications.*

Background

- 10 In 2015, reforms to the CCCFA came into force to address concerns about irresponsible lending. These changes included the introduction of lender responsibilities, such as assessing whether loans were affordable and suitable for the borrower.

RESPONSIBLE LENDING OBLIGATIONS UNDER THE 2015 CCCFA REFORMS

Lenders must exercise the care, diligence, and skill of a responsible lender.

ASSISTANCE TO REACH INFORMED DECISIONS	SUITABILITY	AFFORDABILITY	ETHICAL AND REASONABLE TREATMENT	SAFEGUARDS FOR CONSUMERS SUBJECT TO REPOSSESSION
Lenders must assist borrowers and guarantors to reach an informed decision to enter into the agreement, and its implications.	Lenders must make reasonable inquiries to be satisfied that the credit product likely meets the borrower's requirements and objectives.	Lenders must be satisfied that the borrower or guarantor will make the payments under the agreement without suffering substantial hardship (e.g. being able to meet essential day-to-day expenses, and other pre-existing financial commitments.)	Lenders must treat borrowers and guarantors reasonably and ethically throughout the life of the loan.	A number of new requirements were introduced for repossessions, including licensing of repossession agents.

Review of 2015 amendments to the CCCFA

- 11 In December 2017, I commenced a review to assess whether the amendments had been effective at protecting vulnerable consumers, and to identify any further changes that might be needed. Officials undertook desk-based research³ and interviewed a wide range of stakeholders on the effectiveness of the reforms. A discussion paper was released in June 2018 [DEV-18-MIN-0121].
- 12 Submissions to the review indicated that despite the reforms there is a continued, widespread problem of consumers being provided with loans that are unaffordable or unsuitable, and ending up in unmanageable debt.⁴ This seriously impacts their lives and those of their families. Problem debt exacerbates financial hardship and stress, contributes to lasting health problems,⁵ and can contribute to persistent, intergenerational poverty. It presents a significant challenge to our ability to build a productive, sustainable and inclusive economy.
- 13 The specific issues are discussed further below, but included:
 - 13.1 The high cost of some consumer credit: there is evidence of some very high interest rates and fees for some credit products. These products were seen to contribute to unmanageable debt and 'debt spirals', where they were not repaid on time or are used frequently. A conservative estimate is that more than 200,000 borrowers⁶ use high-cost credit each year. Customer numbers for these credit products are growing rapidly.
 - 13.2 Significant levels of non-compliance: there is continued irresponsible lending, particularly when carrying out affordability assessments and in advertising practices. Stakeholders noted that the harm of irresponsible lending falls

³ This was a detailed review and analysis of lender websites. The report has been published on the MBIE website (<https://www.mbie.govt.nz/info-services/consumer-protection/review-of-consumer-credit-law>).

⁴ Two Whānau Ora sub-providers (one working with Pacific people and the other with Māori) advised that most of their client families are struggling with unmanageable debt. A survey of 74 Māori Housing New Zealand tenants by one of these providers found that 42 per cent had debt to lenders and 43 per cent had debt being pursued by debt collectors. Most of these tenants face hardship: 89 per cent of tenants said that they run out of food due to lack of money at least sometimes, with many running out of food every week.

⁵ As highlighted by the Auckland Regional Public Health Service in its submission on the Discussion Paper.

⁶ This has been extrapolated by MBIE from data provided by a small number of large high-cost lenders. As this is a very limited sample of the market, and we were unable to account for borrowers who are customers of more than one lender, the figure is conservatively low.

disproportionately on vulnerable consumers and in particular, people in hardship. These consumers are unlikely to complain or report their concerns.⁷

- 13.3 Continued predatory behaviour by mobile traders: mobile shopping trucks and traders making sales of goods on credit, at inflated prices, continue to target vulnerable consumers and generate unaffordable debts.
- 13.4 Unreasonable fees: as part of the broader problem of non-compliance, there are a range of concerns about the nature of fees charged, and their seemingly disproportionate amounts.
- 14 The discussion paper sought feedback on a wide range of options to amend and better enforce the CCCFA and to address issues that were harming vulnerable consumers. Based on submissions and further consideration of the options, I recommend a package of proposals to further reform the CCCFA.
- 15 Problems around irresponsible lending are not simple, and many relate to underlying poverty, hardship and financial capability. But consumer protection regulations can and should play a part in reducing consumer credit-related harm.

Comment

Interest and fee cap

- 16 Some lenders offer small loans over short timeframes. These credit products are referred to as 'high cost'⁸ on the basis of their high annual interest rates, or when compared against products offered by 'mainstream' lenders such as banks, credit unions and most finance companies. Historically, high-cost lenders have provided credit to people who, due to their credit histories, may not qualify for credit elsewhere.
- 17 While thousands of consumers use high-cost loans to address short-term financial needs, these loans sometimes worsen financial difficulties. Consumers who default or seek loan extensions can end up with unmanageable debt and in financial hardship, even if the original loan was affordable. This is because, if not repaid quickly, high interest rates and fees can result in the rapid accumulation of the loan amount. High-cost lenders are also a significant source of irresponsible lending. Consumer and industry stakeholders have noted that some lenders earn a substantial proportion of their revenues from ongoing default fees and default interest, rather than the original loan repayments. These lenders provide a small proportion of loans overall, but the impact on consumers' finances and wellbeing is serious.
- 18 Caps on interest and fees have the potential to help address these issues. As part of the Review of Consumer Credit Regulation, officials have consulted on a range of options for interest and fee caps, and obtained a significant amount of feedback on their respective costs and benefits.

⁷ It was not possible to quantify the extent of these problems. However, submissions to the review from community organisations, budgeting services and health and human rights agencies show that the problems are occurring around the country, causing widespread concern, and resulting in serious harm.

⁸ For the purposes of the Responsible Lending Code, 'a high cost' credit agreement is one where the annualised interest rate is 50 per cent or more. The definition will likely need some further development during drafting, for use in the context of statutory interest rate caps.

- 19 I propose that, for high-cost loans, interest and fees over the life of the loan be limited to 100 per cent of the original amount of the loan⁹. This means that even if the borrower defaults, they would repay no more than twice the original loan principal, including interest, default interest, and all fees. For example, if a consumer borrows \$500, they can never be required to pay the lender back more than \$1,000 in total. Lenders would be required to disclose the existence of the cap to consumers.
- 20 The limit would apply to interest and fees on both the original loan, and any subsequent loans provided by the same lender that are used to repay or replace the original loan. This would include new loans which are issued soon after the original loan is repaid. This prevents lenders from simply replacing the original loan with a new loan and continuing to charge interest and fees.
- 21 This proposal would limit the extent to which borrowers accumulate large debts from a single loan. Fewer borrowers, particularly more vulnerable borrowers, would accumulate unmanageable debt and get into financial hardship. Borrowers would pay less in interest and fees overall. It will not address issues caused by borrowers obtaining high cost loans from multiple lenders.
- 22 This proposal will mainly impact lenders who generate substantial or indefinite revenue from borrowers in default.¹⁰ These lenders are unlikely to be meeting their CCCFA lender responsibilities, and have business models causing the greatest concern. Some major high-cost lenders already apply a similar cap voluntarily, so this option should have limited distortionary impact on their business model. Most high-cost loans are repaid without problems.
- 23 I considered other options for interest and fee caps, which are discussed in further detail in the attached impact statement, but I do not favour them. These options involved limiting the interest rate charged, rather than focussing on the total cost to the consumer, including fees. These alternatives would significantly restrict access to credit without regard to individual affordability, and would create distortionary impacts on the credit market. Limiting interest rates would likely result in the closure of many high-cost lenders, and a significant tightening of lending criteria by those who remain. Lenders would likely offer customers longer-term credit in larger amounts, or seek to charge higher fees, in order to recoup the costs of lending. Borrowers with poor credit histories would have fewer options to deal with genuine short-term financial difficulties, and some would end up paying more in interest and fees overall.

Addressing irresponsible lending and non-compliance with the CCCFA

- 24 Across credit markets, there are significant levels of non-compliance with the lender responsibilities, such as assessing loan affordability, and other CCCFA obligations. Contributors include a lack of penalties for non-compliance, very low barriers to entry for lenders, and a lack of enforcement (both public enforcement and individual enforcement via consumer complaints).
- 25 It is currently very easy for individuals with a history of unscrupulous conduct to enter the consumer lending market. A lender must simply be registered on the Financial Service

⁹ As far as MBIE is aware, this is the lowest of the caps currently applied on a voluntary basis by New Zealand lenders.

¹⁰ These lenders provide a small proportion of all high-cost loans, but their consumers are among the most vulnerable. A proportion of people who are declined credit because they cannot afford it, go on to deliberately seek out lenders with less rigorous checks.

Providers Register to lend, and the disqualifications for directors are limited (e.g. they must not have been convicted of a dishonesty offence in the past five years). A history of misconduct by the person or the lenders they have been involved with does not disqualify them. The Commerce Commission has reported several cases of lenders who after being investigated or prosecuted, choose to go into liquidation, sell their loan book to a newly formed company, and simply go on collecting loan accounts.

- 26 There are also no penalties for breaches of the lender responsibilities. The courts can order the lender to pay compensation and exemplary damages for any loss to borrowers, and issue injunctions, but there are no offences or civil pecuniary penalties (unlike disclosure requirements, which have offences for breach).
- 27 The lender responsibilities are high-level 'principle-based' requirements, and there is no obligation on creditors to keep records of how these responsibilities have been met. Proving breaches is difficult, and the Commerce Commission has only filed one set of proceedings in three years.
- 28 I propose a package of changes, discussed below, to increase compliance with the lender responsibilities in the CCCFA. These include introducing a 'fit and proper person' test for directors and top executives of consumer lenders, new civil pecuniary penalties and other remedies for breaches of the CCCFA, and requiring lenders to substantiate their compliance with key lender responsibilities, on request.

'Fit and proper person' test for directors and top executives of consumer creditors¹¹

- 29 I propose that all directors and top executives¹² of consumer creditors be required to meet a 'fit and proper person' test as a requirement for registration on the Financial Service Providers Register. This would test for capability as well as good character. An exception would be made where a 'fit and proper person' test is already required (e.g. to obtain a licence under the Financial Markets Conduct Act). Creditors would need to inform the regulator if there was a change to directors and top executives. Regular confirmation of continuing eligibility for registration would be required. Almost all stakeholders and submitters (across lenders and borrower groups) believe that there should be greater restrictions and a higher bar on who can be involved in consumer lending. This change would reduce the risk that creditors will lend irresponsibly or otherwise breach the law.
- 30 I propose that this test will be undertaken by an independent assessments officer employed by the Commerce Commission (rather than being the function of a Commissioner). This role will be supported by Commission staff.
- 31 I also propose to make it easier to seek a banning order prohibiting or restricting people from being involved with consumer lending. The prior misconduct which makes a person eligible for a banning order would be expanded to include breaches of the Fair Trading Act, Financial Service Providers (Registration and Dispute Resolution) Act, Secondhand Dealers and Pawnbrokers Act or any equivalent overseas legislation. It would also be expanded to include situations where civil pecuniary penalties are incurred, or directors'

¹¹ 'Creditor' means the same as 'lender' but has been used in some places, to match the wording of legislation.

¹² It is proposed to align with the definition of 'senior manager' in the Financial Markets Conduct Act 2013, namely a person who is not a director but occupies a position that allows that person to exercise significant influence over the management or administration of a company (for example, a chief executive or a chief financial officer).

duties to ensure creditor compliance are breached. Lack of previous convictions would no longer prevent a banning order from being made. A court would still need to be satisfied the order is proportionate in the circumstances.

- 32 An alternative option to the proposals above could have been a comprehensive licensing regime for consumer credit providers. However, this would involve substantial upfront and ongoing costs to both lenders and the licensing agency. These compliance costs could well be passed down to consumers in the form of higher borrowing costs and may also have a negative impact on participation in the industry by lenders and reduce innovation.

Enhanced penalties and duties

- 33 I propose extending civil pecuniary penalties, statutory damages and expanded court powers for breaches of the CCCFA. Civil pecuniary penalties would provide stronger incentives for creditors to comply with lender responsibilities. The maximum civil pecuniary penalties would be \$200,000 for an individual or \$600,000 for a body corporate. This would ensure that civil penalties match the existing maximum penalties for offences in the CCCFA.
- 34 Statutory damages would be available for breaches of the responsible lending principles, and would make it easier for borrowers to claim compensation where lender responsibilities were breached. Where lending has been made in breach of responsible lending requirements, a standard level of statutory damages would be paid equal to the interest and fees that had already been charged. If the amount of statutory damages is less than \$200, the amount to be paid would be \$200. The existing ability for the Court to reduce statutory damages under the CCCFA would continue to apply. Together, this ensures that the Court can determine the appropriate consequences in accordance with the circumstances of each case. The court could also order that the credit contract be amended to provide for affordable repayment of the loan.
- 35 Currently the Commerce Commission is able to seek injunctions which prohibit conduct which has been found to constitute a breach of the CCCFA.. I propose that the power to make orders be expanded, to also enable orders that the creditor take positive steps to comply, or such other steps as the court considers necessary in the circumstances.
- 36 I propose a duty on directors and top executives of creditors to ensure that the creditor complies with its CCCFA obligations. Directors and top executives who breach duties would be personally liable for civil pecuniary penalties and for compensating borrowers. Introducing this personal duty and liability would create much stronger incentives for directors to ensure that there are systems in place to support the creditor to comply with its CCCFA obligations. Director and top executive diligence regarding responsible lending and broader compliance with the CCCFA is appropriate, and should already be a matter of course for responsible creditors. This is because irresponsible lending is (i) a financial risk to the business, (ii) causes serious harm to borrowers and to the reputation of the creditor caused by problem debt.
- 37 I propose that lenders be required to substantiate that they have made the required inquiries about affordability and suitability, and that their credit fees are reasonable. This would mean that all lenders would need to be able to provide evidence that they had made reasonable inquiries about affordability or suitability in a particular case, or evidence that their fees were reasonable, on request by the Commission, a dispute resolution scheme or the borrower. There would be penalties if the lender failed to

substantiate that their credit fees were reasonable or that they had made the required inquiries.

- 38 A substantiation requirement would serve as a deterrent to non-compliance and would make identifying and enforcing non-compliance easier if lenders do not comply. The vast majority of responsible lenders are already keeping sufficient records of their assessments to be able to satisfy this requirement. Those that are not currently should be doing so.
- 39 A further step that I propose is to remove the current presumption that lenders can take the information provided by borrowers and guarantors at face value without verification. Lenders would need to verify information (such as income and expenses and the suitability of the product for the borrower) where it was reasonable to do so.

Prescriptive requirements to support the Lender Responsibility Principles and Responsible Lending Code

- 40 I propose a new regulation-making power that would allow mandatory standards to be prescribed in relation to:
- 40.1 assessing loan affordability and suitability (particularly what must be considered in relation to income and expenses), and
 - 40.2 advertising responsibly (particularly disclosure of applicable interest rates).
- 41 Regulations would then outline the actions which must be taken to comply with the relevant lender responsibility principles. These prescriptive requirements would be kept to a minimum, and the finer details would be set in consultation with the sector.
- 42 These prescriptive requirements would complement the high-level lender responsibility principles and the guidance in the Responsible Lending Code. These changes would provide more certainty about lenders' legal obligations, which was requested by numerous lenders and consumer advocates. It would make it easier for borrowers, consumer advocates and advisers, financial dispute resolution schemes and the Commerce Commission to identify breaches and take enforcement action.
- 43 I also propose a mandatory requirement that when advertising is provided in a language other than English, disclosure for the credit contract must also be provided in that language. It would be an infringement offence to fail to do so. There is existing guidance under the Responsible Lending Code that where a lender reasonably suspects that the borrower does not have a good understanding of the English language, a lender should provide, or refer the borrower to, alternative methods or mechanisms for receiving the relevant information.

Requirements for debt collection relating to consumer credit

- 44 Debt collection for consumer credit contracts is currently regulated by the CCCFA. While quantitative data on the extent of issues is not available, consumer stakeholders have expressed concerns about the conduct of debt collectors, and complaints to the Commerce Commission about debt collection have increased steadily, from 23 in 2013 to 119 in 2017.

- 45 One issue that has been raised is the level of false and misleading claims. The majority (around 60 per cent) of debt collection complaints received by the Commerce Commission pertain to misrepresentation of the money owed, and misrepresentation of debtor rights. These include debt collectors seeking non-existent debts, debts owed to a different person, statute-barred debt, or inflated amounts of debt.
- 46 I propose a statutory obligation for key loan information to be shared with the debtor at the commencement of debt collection activity. The information to be disclosed would be specified in regulations, and would include the name of the original creditor, the date on which the debt was passed to the debt collection, any fees added in relation to the debt collection, information about the rights of the borrower, and contact information for relevant consumer support services.
- 47 This option would improve transparency and enable debtors to more readily understand the debt, work with debt collectors to establish a repayment plan, and challenge the debt if necessary. It would also benefit debt collectors, who can resolve the debt more readily if all parties understand the key facts of the loan. It has low costs, given that debt collectors indicated in their submissions that they already undertake a level of disclosure. To better understand and respond to concerns raised about hardship procedures, harassment and fees charged by debt collectors, officials will also be instructed to work with the sector to develop formal guidance on these points. No regulation or industry leadership currently exists on these matters.

Predatory behaviour by mobile traders and shopping trucks

- 48 Mobile shopping trucks and traders continue to target vulnerable consumers. Predatory and irresponsible behaviour, including in relation to the sale of goods on credit, has continued despite significant monitoring and enforcement activity. While some mobile traders are ceasing operation following enforcement action, new trading businesses are regularly being formed.
- 49 To address this, I propose introducing a fit and proper person requirement for all directors and top executives of mobile traders who offer goods or services door-to-door on deferred payment terms (even those who are not creditors under the CCCFA) and requiring these mobile traders to register on the Financial Service Providers Register. This would mean that all mobile traders are required to be registered in a publically accessible database, and required to be members of a dispute resolution scheme. This would have some new compliance costs for mobile traders, and administration and enforcement costs for government, but overall would raise the bar for entry, operation and monitoring of mobile traders and prevent individuals with a history of non-compliance from managing mobile trader businesses.
- 50 To complement this measure, I also propose to strengthen the ability of consumers to require mobile traders to leave or not enter their property. This would amend the Fair Trading Act 1986 provisions relating to uninvited direct sales to provide that any person engaging in an uninvited direct sale must leave the premises immediately if directed. Further, it would specify that a direction may be made in written form (such as through a sticker), and does not need to identify the individual being required to leave the premises.

Other regulatory changes

- 51 In addition to the main proposals to address high-cost credit and irresponsible lending, the review provides an opportunity to address a number of other issues.

Addressing rapid innovation and potential avoidance

- 52 A number of new products have been introduced into the credit markets in recent years that have the features of consumer credit contracts but fall outside the strict definition in the CCCFA. These include interest-free 'buy now pay later' products such as Afterpay, PartPay, Laybuy and Oxipay.
- 53 Consumer advocates and some lenders have raised concerns about these products being unregulated by the CCCFA. There is very limited evidence of harm from them to date, and the products are already subject to protections under the Fair Trading Act. I do not consider they should be brought within scope of the CCCFA at this time.
- 54 However, in light of the rate of innovation in the credit markets, I propose to create regulation-making powers to adjust the scope of the CCCFA to address harms that arise from new, unregulated products in the future. These powers could be used to address avoidance, and also to clarify the treatment of particular credit products (for example, to clarify that a new product is *not* a consumer credit contract). These powers would be similar to the designation power the FMA has under the Financial Markets Conduct Act. This enables FMA to declare that a product is a regulated financial product and also to declare that product is *not* a regulated financial product.

Technical amendments

- 55 I also propose the technical amendments set out in Annex 1. These will improve the operation of the CCCFA, reduce costs and support better outcomes for consumers.

Consultation

- 56 The following departments were consulted on this paper: the Department of Prime Minister and Cabinet (including the Child Poverty Unit), the Treasury, the Ministry of Social Development, the Ministry for Pacific Peoples, and Te Puni Kōkiri. The Commerce Commission, Financial Markets Authority and the Reserve Bank of New Zealand were also consulted.
- 57 The major proposals in this paper were subject to a public discussion paper, on which 86 submissions were received. Submitters included consumers, consumer advocates, lenders, debt collectors, industry associations and dispute resolution schemes. A summary of submissions is set out in the impact statement accompanying this paper.

Financial and operational implications

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Human rights

64 The Human Rights Commission's research has found that consumer protections around credit and debt are seen as a human rights issue in New Zealand communities.

65 The proposals in this paper are consistent with the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993.

¹³ 'Credit matters' includes a range of enforcement responses from low-level compliance activities to full investigations.

Legislative implications

- 66 The proposals in the discussion paper will be implemented through a Credit Contracts and Consumer Finance Amendment Bill, and supporting regulations. The Bill currently has Category 1 priority on the 2018 Legislative Programme.

Impact analysis

- 67 The impact analysis requirements apply to the proposals in this paper. An impact statement has been prepared and is attached as Annex 3. A cost recovery stage 1 impact statement has been prepared for the cost recovery proposal and is attached as Annex 4.

Quality of the impact analysis

- 68 MBIE's Regulatory Impact Analysis Review Panel has reviewed the attached Regulatory Impact Statement (RIS) prepared by MBIE. The Panel considers that the information and analysis summarised in the RIS meets the criteria necessary for Ministers to fairly compare the available policy options and take informed decisions on the proposals in this paper.
- 69 MBIE's Regulatory Impact Analysis Review Panel has reviewed the attached Cost Recovery Impact Statement (CRIS) regarding the proposed fees for fit and proper person assessments, prepared by MBIE. The Panel considers that the information and analysis summarised in the CRIS meets the criteria necessary for Ministers to fairly compare the available policy options and take informed decisions on the proposals in this paper.
- 70 The Treasury's Regulatory Impact Assessment Team has determined that the minor amendments proposed in Annex 1 are exempt from a regulatory impact statement as they have low or no regulatory impact.

Gender implications and disability implications

- 71 The consumer protections proposed in this paper were developed with a focus on vulnerable consumers generally. However, people in hardship are disproportionately women. Women are more likely than men to lead a sole-parent family, which is one of the high-risk factors associated with both poverty,¹⁴ and vulnerability as a consumer of credit. Similarly, people with disabilities are disproportionately in hardship, and may be particularly vulnerable if the disability relates to impaired decision-making. On this basis, a higher proportion of the people affected by these proposals are likely to be women, or people with disabilities.

Publicity

- 72 I intend to publicly announce decisions on this paper, in the week following Cabinet approval. This paper and a summary for non-technical audiences will also be published on MBIE's website.

¹⁴ Work and Income data on hardship grants 2015/2016; Statistics NZ General Social Survey 2014.

Recommendations

The Minister of Commerce and Consumer Affairs recommends that the Committee:

- 1 **note** that on 20 June 2018, the Cabinet Economic Development Committee agreed to the release of the discussion paper, *Review of Consumer Credit Regulation*;

[DEV-18-MIN-0121]

- 2 **note** that 86 written submissions were received on the discussion paper;
- 3 **note** that in addition to the regulatory reforms proposed in this paper, I have initiated cross-agency work with the financial services and community sectors on expanding access to microfinance and inclusive banking products;
- 4 **note** that the improvements to consumer protection resulting from the proposed reforms will complement the longer-term work underway at the Commission for Financial Capability and Ministry for Social Development, to lift financial capability;

Proposed improvements to consumer protections in the CCCFA

- 5 **agree** to cap accumulated interest and fees of a high-cost loan, and any loan that repays or replaces it, to 100 per cent of the original loan principal;
- 6 **note** that a 'high-cost loan' for the purpose of recommendation 5 above will be based on the relevant Responsible Lending Code definition: 'where the annualised interest rate is 50 per cent or more';
- 7 **agree** that creditors whose products are subject to the cap be required to disclose its application and effect;
- 8 **agree** that there be a system requiring all directors and top executives of creditors under consumer credit contracts to meet a 'fit and proper person' test, in order for the creditor to be registered on the Financial Service Providers Register, including:
 - 8.1 requirements for creditors to report changes to directors or top executives, or other changes of circumstances that impact on assessments as fit and proper persons;
 - 8.2 processes for deregistering a creditor if any of its directors or top executives are no longer fit and proper;
 - 8.3 an offence for providing false or misleading information in respect of the fit and proper person assessment, consistent with other offences in the CCCFA;
 - 8.4 creation of an independent assessment officer, to be employed by the Commission (rather than being the function of a Commissioner);
 - 8.5 an application and re-confirmation fee payable to the Commerce Commission by directors and top executives, or by the creditor, on a cost recovery basis, with the specific amounts to be provided for by Order in Council and supported by a regulatory impact assessment;

- 9 **agree** that the Commerce Commission will charge fees for administering fit and proper person assessments, and subsequent reconfirmations, on a cost recovery basis;
- 10 **note** that the proposed fees for assessments and confirmations will be consulted on with industry and other interested stakeholders, and that a further Cost Recovery Impact Statement will be prepared to inform Cabinet decision making;
- 11 **agree** to make it easier to seek prohibition or restriction orders for a creditor or a person involved in the management of a creditor, by broadening the range and reducing the number of proven contraventions that make a person eligible for an order;
- 12 **agree** to a new duty on directors and top executives of creditors to ensure that the creditor complies with its CCCFA obligations;
- 13 **agree** that lenders be required to substantiate that they had made the required assessments of affordability and suitability, and to substantiate that their fees were reasonable;
- 14 **agree** to remove the ability for lenders conducting affordability and suitability assessments for credit or credit-related insurance to rely on information provided by the borrower or guarantor;
- 15 **agree** to enable mandatory prescriptive standards in regulations for how creditors must:
- 15.1 assess loan affordability and suitability, including specifying matters that must be considered when determining income and expenses, and
- 15.2 advertise responsibly, including disclosure of interest rates;
- 16 **agree** that when advertising is provided in a language other than English, creditors be required to provide disclosure in that language in appropriate circumstances, with an infringement offence for failing to do so;
- 17 **agree** that when debt collection commences, the debtor must be informed of key loan information to be set out in regulations, including the name of the original creditor, the date on which the debt was passed to debt collection, any fees added in relation to debt collection and information about the borrower's rights;
- 18 **agree** to provide for civil pecuniary penalties and statutory damages for breaches of the CCCFA, and to expand the court's powers to order compliance. In particular:
- 18.1 civil pecuniary penalties to be available for breaches of the CCCFA, with maximum penalties of \$200,000 for an individual or \$600,000 for a body corporate;
- 18.2 statutory damages to be available for breach of responsible lending principles and the interest and fee cap on high-cost loans. Ability for the court to order a bar on further charging of interest and fees, and affordable repayment of the principal. The minimum amount of statutory damages would be \$200;
- 18.3 creating the ability for the court to make orders requiring creditors to take positive steps to comply with the Act, or to take such other steps as the court considers necessary in the circumstances;

- 19 **agree** to new regulation-making powers to prescribe the detail of the requirements set out in relation to the fit and proper person test, prescriptive standards, and disclosure regarding debt collection (recommendations 8, 15 and 17 above);

Mobile traders

- 20 **agree** to require all mobile traders who offer products or services door-to-door on deferred payment terms to be registered on the Financial Services Provider Register and be members of a dispute resolution scheme (even those who do not currently qualify as 'creditors'), and impose a fit and proper person test on directors and top executives as a prerequisite to registration;
- 21 **agree** to amend the Fair Trading Act 1986 to provide that a person engaging in an uninvited direct sale must leave the premises immediately if directed by a consumer, and that such a direction may be made in written form and does not need to specifically identify the person being required to leave the premises;

Technical changes

- 22 **note** that the changes proposed in this paper provide an opportunity to address a number of technical issues;
- 23 **agree** that a new regulation-making power be introduced to declare that a type of agreement is, or is not, a consumer credit contract, and to specify who is and is not a creditor under such an agreement;
- 24 **agree** to the minor policy changes set out in Annex 1;

Financial implications

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Legislative implications

- 30 **agree** to give effect to the above proposals through the Credit Contracts and Consumer Finance Amendment Bill, which has Category priority on the 2018 Legislation Programme
- 31 **invite** the Minister of Commerce and Consumer Affairs to issue drafting instructions to the Parliamentary Counsel Office to give effect to the above paragraphs;
- 32 **authorise** the Minister of Commerce and Consumer Affairs to make minor additional policy decisions (including timings for commencement) and technical changes, consistent with the policy intent of this paper, on issues that arise in drafting and passage;
- 33 **authorise** the Minister of Commerce and Consumer Affairs to release an exposure draft of regulations alongside the Parliamentary process for the Credit Contracts and Consumer Finance Amendment Bill;
- 34 **note** that Cabinet’s decision to amend s99(1A) of the CCCFA [DEV-18-MIN-0121 refers] will be implemented in the same Bill;

Communication

- 35 **note** that the Minister of Commerce and Consumer Affairs will publicly announce policy decisions, in the week following Cabinet approval;
- 36 **note** that this paper will be published on the Ministry of Business, Innovation and Employment’s website, and MBIE will also publish a short summary of the decisions for non-technical audiences.

Authorised for lodgement

Hon Kris Faafoi
Minister of Commerce and Consumer Affairs

Annex 1: Additional policy decisions

Topic	Status quo	Reason for change	Proposed change
Layby sales involving credit fees or interest charges	Layby agreements under the FTA are those where the consumer makes a number of payments (at least 2) and does not take possession of the goods until all or part of the price of the goods has been paid.	There are currently overlapping, and potentially conflicting, legal obligations for suppliers selling goods on deferred payment terms (where payments are made by instalments and not upfront at the time of purchase). Some types of deferred payment sales are subject to the FTA's layby sales provisions as well as the CCCFA's credit contract provisions, which have different disclosure requirements and cancellation rights.	Amend the FTA and CCCFA so that any agreement that is a layby sale under the FTA and also a consumer credit contract under the CCCFA will be subject to the provisions of the CCCFA (and will not have layby disclosure) but will have layby cancellation rights (and not CCCFA cancellation rights).
Disclosure of "full particulars" of a change to a credit contract	Under section 22 of the CCCFA, when the terms of a contract are varied, lenders must disclose the "full particulars of the change".	There is no definition of "full particulars" and it is not clear whether the consequential costs of changes must be disclosed. There is scope for significant disagreement with lenders, some of whom have interpreted the section more narrowly than may have been intended, because of the lack of legal clarity. For example, some lenders only disclose changes to terms, and not the effect of those changes, such as for example the effect the change has on the interest rate under the contract or the number of payments.	Clarify that the requirement on creditors to disclose "full particulars" when they make a variation disclosure includes the requirement to disclose the effect of the change (rather than just the change itself).
Guarantors of family trusts	Borrowing by those acting in their capacity as trustees of a family trust is expressly excluded from being a consumer credit contract in section 15(c). Trustees are excluded because they are expected to have a higher degree of expertise than a normal consumer, because of the duties they must legally meet as a trustee. They therefore do not need increased protection under the CCCFA. However, the same exclusion does not currently apply to guarantors who are acting in their capacity as trustees.	Trustees who are guarantors of a consumer credit contract are treated inconsistently with trustees who are debtors. Debtor trustees are not subject to protections of the CCCFA. This means that lenders may be unnecessarily applying the CCCFA lender responsibility principles (including requiring lenders to assist guarantors to make an informed decision and to make reasonable enquiries as to whether the guarantor will likely suffer substantial hardship in compliance with the guarantee), disclosure requirements, cancellation and provisions on interest charges and unreasonable fees.	Exclude a person acting in his or her capacity as a trustee of a family trust from the definition of guarantor under the Act.
Enforceable undertakings	When the Commerce Commission takes out-of-court enforcement action under the Act, it can enter into settlements. However, it does not have the ability to accept enforceable undertakings, which are significantly easier than settlements to enforce if they are breached. It can accept enforceable undertakings under the Fair Trading Act and under the Commerce Amendment Bill.	In addition to the settlements being difficult to enforce if they are breached, not having the ability to accept enforceable undertakings can create issues when an investigation crosses both the Credit Contracts and Consumer Finance Act and the Fair Trading Act, as different enforcement approaches must be taken for each Act. In addition, this would also clarify any uncertainty arising from the Supreme Court judgement in <i>Osborne</i> , relating to settlements.	Amend the CCCFA to allow for enforceable undertakings. Specify that an undertaking may include an undertaking to pay compensation, or to reimburse the Commission for its investigation costs.

Annex 2: Visual summary of proposed regulatory changes to CCCFA

