

Credit Law and Consumer Protection
Exposure Draft Credit Contracts and Consumer Finance
Amendment Bill

Consultation Documents

April 2012

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(These documents are also all accessible as individual parts)

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Part 1: Credit Law and Consumer Protection

Explanatory Information

The Credit Contracts and Consumer Finance Amendment Bill will amend the Credit Contracts and Consumer Finance Act 2003 (CCCFA).

The Bill will introduce responsible lending as a new principle in the CCCFA, and strengthen the legal rights and protections of consumers when they borrow money. The policy decisions underpinning the Bill were made by Cabinet in October 2011. The purpose of releasing the exposure draft of the Bill and this Explanatory Information is to invite submissions on how the policy decisions have been translated in the draft Bill.

The Explanatory Information provides brief discussion on the key amendments set out in the exposure draft of the Bill. After the discussion of each of the amendments, there are some questions to assist you in making a submission. There is no requirement to provide a response to all of the questions. Your views on just those topics of particular interest to you would be most welcome.

Responsible Lending

Responsible lending means lenders have a duty to look out for their customers. They cannot be indifferent to the circumstances of their customers or the effect of the debt they are providing. In some circumstances that debt can be harmful to the individual borrowers and to society generally.

This is a change from the primary principle in existing consumer credit law, which is that consumer credit contract disclosure will empower borrowers to make the best decisions and ensure they understand the terms of the credit they purchase, and disclosure will also promote competition that will drive down the cost of credit and protect borrowers. There are some provisions in the existing law which regulate aspects of lenders' businesses, and which provide some protections for borrowers, but the main emphasis of the CCCFA is on disclosure of consumer credit contract terms.

Adding a new responsible lending principle for consumer credit law is consistent with the regulation of other services provided to potentially vulnerable consumers, especially in the financial services markets. The overarching purpose of responsible lending is to protect consumers, but it will also enable lenders who are already lending responsibly to compete more effectively with other lenders. The objective of responsible lending is to lift the business practices of lenders towards an industry best practice standard.

The Bill provides for a new section 9A in the CCCFA that sets out a series of responsible lending principles. The responsible lending principles all refer to conduct by lenders that will provide protection for borrowers from potential harm. More detailed elaboration and guidance on the responsible lending principles will be provided through a Responsible Lending Code. The content of the Code, and the process for developing the Code (including consultation), are set out in new sections 9C and 9D of the CCCFA. The Code will have the status of delegated legislation.

One of the important issues for the Code is how it should be enforced. The Bill provides for a principles-based approach. In other words, rather than prescribing what action a lender must take, the principles set out the outcomes required. Responsible lending principles are set out in the Bill, and the Code will expand and provide guidance on the application of those principles. The Code will not be a prescriptive set of rules.

The responsible lending principles will empower the courts to make orders under section 108 of the CCCFA, banning creditors who fail to comply with the Act (including the responsible lending principles). A breach of the responsible lending principles will also be an indication of an oppressive credit contract which can be re-opened by the Court.

1. How well do you think the responsible lending principles in the Bill (new section 9B) reflect the principles which should apply?
2. Should any additional principles be included in (or removed from) the principles of responsible lending?
3. Should a responsible lending code be developed by the Minister of Consumer Affairs in consultation with affected people, or by a code committee as with the Code of Professional Conduct for financial advisors?
4. Is it appropriate for the code to elaborate and provide guidance on the responsible lending principles in the Bill, or should it be more prescriptive?

Other new consumer protections

The Bill also makes a range of other amendments designed to improve the protection for borrowers under the CCCFA.

Amended Purpose Section

The amended purpose section of the CCCFA set out in the Bill follows a form similar to the purpose section in the Financial Markets Conduct Bill. The content of the purpose section is recast to give primary emphasis to consumer protection, and also to include reference to the general purposes of consumer law being added by the Consumer Law Reform Bill to the Fair Trading Act, Consumer Guarantees Act and Weights and Measures Act. Those purposes include promoting the confident and informed participation in markets by consumers and lenders, and promoting and facilitating fair, efficient, and transparent markets for credit. The effect of the amended purpose section is to provide guidance and context for Courts and other users interpreting particular provisions of the CCCFA.

5. Do you agree with the new CCCFA purpose clause emphasising consumer protection and the market behaviours stated in new section 3(2)(a) and (b)?
6. Should any additional purposes to those in new sections 3(1) and 3(2) be included (or be removed) in order to ensure that the CCCFA is interpreted in a way that meets its objectives?

Disclosure

Credit contract disclosure remains an important feature of the CCCFA, and the Bill aims to make disclosure more useful for consumers. The Bill provides that credit contract disclosure must be made up front, addressing an issue with the current timing of disclosure. At present, various types of disclosure, including initial disclosure, can be made up to 5 working days (and in some cases 15 working days) after the credit contract, variation agreement or credit related insurance contract is made. The reason disclosure can be made after the credit contract is made is that there is a 3-day cooling off period in the CCCFA which allows borrowers to change their mind after disclosure is made.

Disclosure after the contract is made is too late to provide any assistance to a borrower deciding whether or not to enter into a credit transaction, and the cooling off period is of limited use when the consumer has probably spent the borrowed money and would need to find alternative finance to repay the disclosed loan.

There are two changes to the disclosure rules in the Bill. Each type of disclosure is required to take place on or before the relevant transaction is made, and the cooling off period is extended from 3 working days to 5 working days. The longer cooling off period is consistent with the cooling off periods for uninvited direct sales and extended warranties being provided in sections 36M and 36U of the Fair Trading Act through the Consumer Law Reform Bill.

7. Looking at amended sections 17, 22 and 23, is there any justification for consumer credit contract disclosure being made after the contract is made?
8. Looking at amended section 27, do you envisage any unintended consequences that from extending the cooling off period from 3 working days to 5 working days?

Standard Terms and Costs of Borrowing

Consumer credit contract disclosure on or before the transaction is made is still insufficient to allow borrowers to compare competing offers, or to inform the market generally. Interest rates and fees charged by first and second tier lenders are already relatively transparent, but this is not always the case with third tier lenders. Interest rates and fees which are already publicly available can be incomplete, and it may still be difficult for consumers to make meaningful comparisons between lenders.

The Bill provides for lenders to make their standard terms and costs of borrowing publicly available at their premises and on their websites if they have a website. This is intended to increase market transparency and competition. The details of how the standard terms and costs of borrowing will be required to be published will be provided in regulations. The objective of the regulations will be to make it easier for consumers to make direct comparisons between competing lenders.

9. Looking at new sections 9H and 9I:
 - a) Will making standard terms and costs of borrowing available at creditors' premises and on their websites be sufficient to improve transparency and improve competition?
 - b) To what extent will these provisions promote shopping around by borrowers and effective competition among lenders?

Fees

One of the consumer protections in the CCCFA is that unreasonable credit fees and default fees are prohibited. The principles underpinning these provisions are not as clear as they could be, which makes it difficult for the Commerce Commission and consumers to enforce the prohibition, and for businesses to know what their compliance requirements are. For most lending, the intention is that lenders should primarily compete on their interest rates, and fees should only be used by lenders to recover specific costs and losses. The Bill makes this clearer. The Bill also removes the one-year limitation period on challenging fees as being unreasonable under the CCCFA, so the three-year period which applies generally in the CCCFA will also apply to unreasonable credit fees.

10. Looking at the amendments to sections 40, 41, 43, 44, 45, 51, 52 and new sections 44A and 52A:

- a) To what extent do the amendments and additions adequately describe the process by which an unreasonable fee may be altered?
- b) Do these provisions meet the objective of making the law clearer about what an unreasonable fee might be?
- c) Do the provisions leave open any avenue to charge a fee which is unreasonable?

Hardship

Another consumer protection in the CCCFA is that borrowers can apply to the creditor to postpone payments or make other changes to assist the borrower if he or she is suffering unforeseen hardship because of the types of changed circumstances set out in section 55 of the CCCFA. The creditor does not have to agree to a request from a borrower, although the borrower can apply to the Court to make a change on the ground of hardship if the creditor rejects the application. The current provisions do not apply if the borrower is already in default, and that is often the case with hardship applications. There are also no process requirements or time limits on creditors processing hardship applications. The Bill remedies these deficiencies, including allowing borrowers to apply to postpone payments or for other changes to assist the borrower if the borrower has been in default for not more than 2 months, and imposing timeframes and a requirement to provide reasons on the creditor.

11. Looking at the amendments to sections 57 and 58:

- a) Will the new unforeseen hardship provisions improve access to hardship protections for those in genuine need?
- b) Are additional changes necessary to protect consumers?
- c) Are additional changes necessary to protect lenders from abuse of the provisions?

Unregistered Creditors

Creditors are required to be registered under the Financial Service Providers (Registration and Dispute Resolution) Act 2008 (FSP Act). The main effect of registration is that creditors are required to join a dispute resolution scheme which provides an avenue to investigate and make decisions on consumer complaints. Research by the Ministry of Consumer Affairs indicated that not all creditors were registered under the FSP Act, or were registered incorrectly. This disadvantages consumers who cannot easily access dispute resolution. The Bill discourages non-registration by providing that unregistered creditors are prevented from recovering the costs of borrowing for so long as they remain unregistered. The costs of borrowing include credit fees, default fees and interest.

12. Looking at the new section 99A, are additional provisions needed to ensure unregistered lenders are not operating in the marketplace or to protect consumers from unregistered lenders?

Oppression Provisions

Another protection for borrowers under the CCCFA is that Courts have the power to re-open credit contracts if they are found to be oppressive. This protection applies to borrowers under all credit contracts – it is not limited to consumer credit contracts. The problem with this protection from a consumer point of view is that the oppression test applied by the Courts sets the bar too high, and transactions and conduct which might reasonably seem to be harsh or unjustly burdensome are regarded as being properly enforceable by the Courts. The Bill includes extra guidelines for the Courts to regard, in an attempt to make it easier for borrowers to meet the oppression threshold when they challenge a credit contract. The extra guidelines generally reflect the tests applied by the Courts in any event, and there is a risk that the definition of “oppressive” will still be narrowly construed by the Courts.

13. Do you think the amended Guidelines for reopening credit contracts, consumer leases and buy-back transactions will improve the protection of consumers from oppressive credit contracts (amended section 124)?
14. As an alternative, should we follow the approach to the re-opening jurisdiction in the Australian National Consumer Credit Protection Act 2009, and refer to "unjust" credit contracts rather than "oppressive" credit contracts?

Disclosure of Statement of Rights

The key information for initial disclosure of consumer credit contracts is set out in Schedule 1 of the CCCFA. It is not proposed to change this requirement. However, Schedule 1 does not refer to the debtor's ability to apply for relief on the grounds of hardship, or the right to complain about a lender's decision to the dispute resolution scheme the lender is required to have joined under the FSP Act. The Bill amends Schedule 1 of the CCCFA to add these details.

The key information required to be disclosed under Schedule 1 includes very specific information about the debtor's right to cancel the credit contract during the cooling off period following initial disclosure. The specificity of the information about the right to cancel is not always helpful or appropriate, and it is not in keeping with the more general description of other key information required to be disclosed. The Bill simplifies paragraph (s) of Schedule 1.

The Bill also adds a regulation-making power to prescribe the form of disclosure statements and how the disclosed information must be presented. There will be separate consultation on the specific disclosure regulations.

15. Do you think the amendments to the CCCFA Schedule 1 - Key information concerning consumer credit contract - will sufficiently improve disclosure or should additional information be provided in disclosure documents?

Transitional Provisions

There will be existing credit contracts in place when the amendments to the CCCFA come into force. The general rule is that amendments to Acts should not have retrospective effect on existing agreements, and the Bill follows that approach. There are some situations where the new law will have an effect on existing agreements and these are set out in the Bill. They include future request disclosure, disclosure and responsible lending obligations for future contract variations, hardship applications and fees incurred after the amendments come into force.

16. Are all the situations where the new law should have an effect on existing contracts covered in the Bill?

After Acquired Goods and Powers of Attorney

The Law Commission is reporting separately on the Credit Repossession Act 1997. Creditors taking and enforcing security over personal property is a critical part of consumer credit law. One of the areas of concern which has been identified which is not directly an issue under the Credit Repossession Act is the use of “all present and after-acquired property” clauses in loan agreements which create “drag-net” securities over all the personal property of borrowers, including future property. Section 44 of the Personal Property Securities Act 1999 protects consumers by saying (implicitly) a security interest in after-acquired consumer goods must be “specifically appropriated” by the consumer. Specific appropriation is a concept from the Sale of Goods Act 1908, and it requires the consumer goods to be clearly identified and distinguished from any other goods.

Some secured creditors are using powers of attorney in their loan agreements to get around the protection in section 44 by “specifically appropriating” after-acquired consumer goods on behalf of the borrower, and then repossessing those goods if the loan goes into default. Clause 32 of the Bill amends section 44 to make it clear this behaviour will not be lawful.

<p>17. In your experience, will the amendment of section 44 of the Personal Property Securities Act 1999 prevent the practise of "drag-net" securities over all personal property?</p>
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Part 2:

Other Matters Relevant to the Credit Contracts and Consumer Finance Amendment Bill Exposure Draft

This note discusses three matters that are not covered in the Credit Contracts and Consumer Finance Amendment Bill Exposure Draft.

CCCFA Regulator

The regulator currently responsible for enforcing the Credit Contracts and Consumer Finance Act (CCCFA) is the Commerce Commission. The Commerce Commission is also responsible for enforcing the Fair Trading Act.

The Exposure Draft includes new responsibilities and obligations on creditors, and new enforcement powers exercisable by the regulator.

One of the issues that arose in reviewing the CCCFA was whether the Commerce Commission was the optimal regulator, or whether the new Financial Markets Authority could more appropriately be given responsibility for regulating credit alongside the markets for other financial products. Creditors are required to be registered under the Financial Service Providers (Registration and Dispute Resolution) Act 2008, and the Commerce Commission is not the regulator under that Act.

No changes to the regulator responsible for enforcing the CCCFA have been included in the Exposure Draft. At this time, it is not intended that any change be made.

Credit Repossession

The Law Commission has been undertaking a review of the Credit Repossession Act 1997 in parallel with the development of the Credit Contracts and Consumer Finance Amendment Bill.

The Law Commission's report will be tabled in Parliament shortly and will make a number of recommendations.

The Government has three months to respond to the Law Commission recommendations which are likely to affect both the Credit Repossession Act and the CCCFA. Accepting the recommendations may require a substantial addition to the Bill, which would best be made before the Bill is introduced.

The Law Commission's report will be released before the closing date for submissions. If you have any comments on the recommendations these would be welcomed as part of your submission on the Credit Contracts and Consumer Finance Amendment Bill Exposure Draft.

Cost of Finance Caps

Very high cost credit can lead to over-indebtedness and financial hardship. Cost of finance caps are a statutory tool used in various countries (including Australia) to limit the amount of interest and fees that can be charged for consumer credit. Cost of finance caps stop credit providers charging

very high interest rates and fees, and they also stop consumers accessing very high cost credit. Some consumers may not be able to access credit at all, or may be driven to borrow illegal credit.

The changes in the Bill are directed to the problems of over-indebtedness and financial hardship. Lenders will be required to make responsible lending decisions, and protections for consumers are being strengthened through greater disclosure requirements, the prohibition on unreasonable fees, and improved access to remedies in the event of unforeseen hardship and oppression.

If these initiatives are successful, cost of finance caps will be unnecessary in New Zealand. Your views are sought on whether you agree that the package of reforms in the Bill make cost of finance cap provisions unnecessary.

Part 3: Consultation Questions on Credit Contracts and Consumer Finance Amendment Bill Exposure Draft

The following questions are provided to assist you in making a submission on the Credit Contracts and Consumer Finance Amendment Bill Exposure Draft. There is no requirement to provide a response to all of the questions. Your views on just those topics of particular interest to you would be most welcome.

Responsible Lending

1. How well do you think the responsible lending principles in the Bill (new section 9B) reflect the principles which should apply?
2. Should any additional principles be included in (or removed from) the principles of responsible lending?
3. Should a responsible lending code be developed by the Minister of Consumer Affairs in consultation with affected people, or by a code committee as with the Code of Professional Conduct for financial advisors?
4. Is it appropriate for the code to elaborate and provide guidance on the responsible lending principles in the Bill, or should it be more prescriptive?

New Purpose Clause

5. Do you agree with the new CCCFA purpose clause emphasising consumer protection and the market behaviours stated in new section 3(2)(a) and (b)?
6. Should any additional purposes to those in new sections 3(1) and 3(2) be included (or be removed) in order to ensure that the CCCFA is interpreted in a way that meets its objectives?

Disclosure

7. Looking at amended sections 17, 22 and 23, is there any justification for consumer credit contract disclosure being made after the contract is made?
8. Looking at amended section 27, do you envisage any unintended consequences that from extending the cooling off period from 3 working days to 5 working days?

Publication of Standard Terms and Costs of Borrowing

9. Looking at new sections 9H and 9I:
 - a) Will making standard terms and costs of borrowing available at creditors' premises and on their websites be sufficient to improve transparency and improve competition?
 - b) To what extent will these provisions promote shopping around by borrowers and effective competition among lenders?

Fees

10. Looking at the amendments to sections 40, 41, 43, 44, 45, 51, 52 and new sections 44A and 52A:
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Unregistered Lenders

12. Looking at the new section 99A, are additional provisions needed to ensure unregistered lenders are not operating in the marketplace or to protect consumers from unregistered lenders?

Oppressive or Unjust Contracts

13. Do you think the amended Guidelines for reopening credit contracts, consumer leases and buy-back transactions will improve the protection of consumers from oppressive credit contracts (amended section 124)?
14. As an alternative, should we follow the approach to the re-opening jurisdiction in the Australian National Consumer Credit Protection Act 2009, and refer to "unjust" credit contracts rather than "oppressive" credit contracts?

Disclosure of Statement of Rights

15. Do you think the amendments to the CCCFA Schedule 1 - Key information concerning consumer credit contract - will sufficiently improve disclosure or should additional information be provided in disclosure documents?

Transitional Provisions

16. Are all the situations where the new law should have an effect on existing contracts covered in the Bill?

After Acquired Consumer Property

17. In your experience, will the amendment of section 44 of the Personal Property Securities Act 1999 prevent the practise of "drag-net" securities over all personal property?

Making a submission

The Ministry of Consumer Affairs invites submissions on the Credit Contracts and Consumer Finance Amendment Bill Exposure Draft and the consultation questions.

If you wish to make a submission please forward it to us by Friday 11 May 2012.

Submissions should be emailed in either Adobe PDF or Microsoft Word format to the Ministry of Consumer Affairs (CCCFA@mca.govt.nz), with "Submission on Credit Law Exposure Draft" as a subject heading.

Alternatively, submitters may send hard copies of their submission to:

Consumer Policy
Ministry of Consumer Affairs
PO Box 1473, Wellington

We will acknowledge receipt of all submissions. Please contact us if you do not receive an acknowledgement of your submission within a week.

Consideration of submissions

Taking into account the submissions received, the Ministry of Consumer Affairs will report to the Minister of Consumer Affairs on progressing amendments to the Credit Contracts and Consumer Finance Act.

Official Information Act 1982

Please note that any submissions you make may be published and subject to a request for release under the Official Information Act 1982.

In providing your submission, please advise us if you have any objections to the release of all or part of your submission and the basis of your objection. When preparing and releasing any summary of submissions and when considering any Official Information Act requests, the Ministry will carefully review any representations you make in this regard.

Privacy Act 1993

Any personal information that you supply to the Ministry in the course of making a submission will be used only by the Ministry when considering matters covered by the Credit Contracts and Consumer Finance Amendment Bill Exposure Draft.

When preparing any summary of submissions, it is the Ministry's normal practice to set out the names of parties making submissions. Your name will be included in any such summary unless you inform the Ministry that you do not wish your name to be included. To indicate your wishes, or to view personal information held about you in relation to matters covered by the Exposure Draft, or to request correction of that information, please contact the Ministry of Consumer Affairs (CCCFA@mca.govt.nz).