

In Confidence

OFFICE OF THE MINISTER OF COMMERCE AND CONSUMER AFFAIRS

The Chair
Cabinet Economic Growth and Infrastructure Committee

Regulations to implement the Credit Contracts and Consumer Finance Amendment Act 2014

Proposal

- 1 This paper seeks agreement for policy decisions on regulations under the Credit Contracts and Consumer Finance Amendment Act 2014 (the **Amendment Act**) to:
 - a. prescribe the 'costs of borrowing' information that lenders must make publicly available;
 - b. prescribe the minimum repayment warning that must be included on credit card billing statements;
 - c. prescribe the formulae for calculating proportionate rebates of amounts paid for a repayment waiver or an extended warranty upon prepayment of a consumer credit contract; and
 - d. exempt local government Voluntary Targeted Rate schemes from the unforeseen hardship and unreasonable fee provisions.

Executive Summary

- 2 The Amendment Act was passed on 6 June 2014 and comes into force in full by 6 June 2015. It makes a number of significant changes to consumer credit laws, including improvements to information disclosure requirements.
- 3 I propose that regulations be made to give effect to certain disclosure and rebate provisions and to exempt providers of Voluntary Targeted Rate schemes from specific provisions. Specifically these regulations will deal with:
 - a. **Costs of borrowing.** The Amendment Act requires lenders to make information publicly available about their costs of borrowing (such as credit fees, default fees and interest charges). Regulations will prescribe the information to be disclosed and require that the information be easily accessible by consumers;
 - b. **Minimum repayment warning on credit card billing statements.** The Amendment Act requires lenders to publish minimum repayment warnings on all credit card billing statements. Regulations will prescribe the form of the minimum repayment warning, how it is to be disclosed and any circumstances where the warning may not be required;
 - c. **Proportionate rebates.** The Amendment Act provides that if a borrower purchases a repayment waiver or extended warranty from the lender in connection with a consumer credit contract and then pays off the contract early, the borrower will be entitled to a proportionate rebate of the amounts paid for the waiver or warranty. Regulations are required to set the formulae for calculating these rebates; and

- d. **Voluntary Targeted Rate (VTR) schemes.** VTR schemes are consumer credit contracts offered by local and regional councils which are administered through the rating system. Regulations are required to exempt councils providing VTR schemes from the unforeseen hardship and unreasonable default fees provisions, as these provisions overlap with similar requirements under local government legislation.

Background

- 4 The Amendment Act received Royal Assent on 6 June 2014 and comes into force in full by 6 June 2015. The Amendment Act makes a number of improvements to consumer credit legislation, particularly the Credit Contracts and Consumer Finance Act 2003 (the **CCCFA**). The Amendment Act improves disclosure requirements, introduces a responsible lending framework, incorporates repossession laws and strengthens the overall enforcement protections.
- 5 A number of regulations need to be made before the Amendment Act comes into force. These include regulations to:
- a. give effect to provisions of the Amendment Act relating to disclosing costs of borrowing information, providing a credit card minimum repayment warning and calculating proportionate rebates; and
 - b. exempt VTR schemes from provisions of the CCCFA that conflict with similar requirements under the Local Government (Rating) Act 2002 (the **LGRA**).

Comment

Disclosure provisions

- 6 To give effect to the new disclosure provisions in the Amendment Act, regulations must be developed to prescribe:
- a. the costs of borrowing information that lenders must make publicly available; and
 - b. a minimum repayment warning for credit card billing statements.
- 7 To give lenders certainty in how to comply with the new requirements, these regulations must be completed before the provisions of the Amendment Act come into force by 6 June 2015.

Costs of borrowing

- 8 The Amendment Act requires all lenders to make publicly available “information about all the costs of borrowing in relation to every class of credit contract offered”. To give effect to the Amendment Act, regulations must prescribe the information to be disclosed, and may prescribe the form of disclosure. Costs of borrowing include:
- a. **Credit fees:** Fees payable by the borrower under the credit contract, such as establishment fees and prepayment fees;
 - b. **Default fees:** fees or charges payable on a breach of the credit contract by a borrower or on the enforcement of a credit contract by a lender; and
 - c. **Interest charges:** a charge occurring over time determined by applying a rate to an amount owing (and includes default interest charges).

- 9 The Amendment Act requires a lender to display costs of borrowing information on its website (if it has one), and to provide a copy of the information immediately and free of charge to any person who requests it. If a lender operates from business premises that are accessible to the public, the lender must display prominently a notice that a copy of the information is available.
- 10 I propose that the regulations require that costs of borrowing information is made publicly available (in accordance with new section 9K of the CCCFA) as follows:
- a. **Fees:** allow for disclosure of fees in a variety of ways, including disclosure of a dollar figure or a maximum dollar figure;
 - b. **Interest charges:** disclose an annual interest rate (or range of rates) and additional detail (such as the factors the lender will consider in selecting a rate within the range) and clarifying that the applicable interest rate or range of rates can refer to a representative figure or range if appropriate;
 - c. **Publication date:** costs of borrowing information will be disclosed with a publication date, where appropriate; and
 - d. **Disclosure on a lender's website:** prescribe that the fees and interest rates are located on the website in a way that makes these easy to find and compare.
- 11 The above approach will promote consumer understanding, accessibility and comparability, while minimising unnecessary compliance costs and accommodating different types of lenders and lending products.

Minimum repayment warning for credit card statements

- 12 New section 19(1)(i) of the CCCFA requires credit card providers to include a minimum repayment warning on credit card billing statements. The purpose of this warning is to highlight to consumers the consequences only making the minimum repayment each month. The Amendment Act requires that regulations prescribe the content and form of the warning.
- 13 I propose that regulations will require lenders to provide a written warning statement that includes a link to an online repayment calculator. The warning will highlight the general consequences of only making the minimum repayments each month and will direct consumers to an online calculator provided by the Commission for Financial Capability on its *Sorted.org.nz* website. The online calculator provides an avenue for consumers to calculate the costs of repaying their card balance at different repayment levels. This warning could be worded as follows:
- "If you only make the minimum payment each month, it will take you longer and cost you more to pay off your balance. Visit sorted.org.nz/creditcards to calculate how you can pay off your credit card balance faster and pay less in interest"*
- 14 This minimum repayment warning will be displayed prominently on the billing statement. Credit card providers may not be required to include this warning in certain circumstances, including where the outstanding balance on the card is very small, or where a payment plan or interest free period is in effect.

- 15 Other options for prescribing the minimum repayment warning were considered, and are analysed in the attached Regulatory Impact Statement. These options included prescribing a warning which sets out how long it would take, and how much it would cost, to repay a balance by only making the minimum repayment each month. Similar warnings have been adopted in Australia and the United States. I am not proposing this option as it would impose significant up-front costs on credit card providers and the benefit of this type of warning in the New Zealand context is unclear.
- 16 Officials will monitor the impact of the minimum repayment warning in a number of ways, including by:
- a. working with the Commission for Financial Capability to examine the number of consumers accessing and using the online calculator;
 - b. engaging with major credit card providers to examine the impact of the prescribed warning on repayment behaviour, and whether the proportion of consumers only making the minimum repayment has decreased; and
 - c. engaging with consumer groups to analyse whether the calculator is having an impact on the repayment behaviour of low-income cardholders, and whether they are utilising the online calculator.

Proportionate rebates

- 17 The existing CCCFA provides that a borrower may pay off the full amount owing under a consumer credit contract at any time. Upon prepayment, a lender must refund to the borrower a proportionate rebate of any amount paid for consumer credit insurance.
- 18 Under the Amendment Act, the lender will also be required to refund to the borrower a proportionate rebate of any amounts paid for a repayment waiver or an extended warranty agreement between the lender and the borrower. Regulations are required to set the formulae for calculating these rebates.
- 19 I propose that regulations will prescribe:
- a. for repayment waivers, a rebate formula which is equivalent to the existing rebate formula for consumer credit insurance – an equivalent product to a repayment waiver from a borrower’s perspective. The formula is based on the “rule of 78”, which recognises the diminishing benefit of the repayment waiver over time; and
 - b. for extended warranties, a straight-line formula.

Voluntary Targeted Rate schemes

- 20 VTR schemes are consumer credit contracts offered by local and regional councils which allow ratepayers to retrofit their homes with insulation or a clean heating source at a reasonable cost. Councils administer the schemes and collect payments through the rating process. Because of this, there is a tension between how councils comply with the provisions of the CCCFA in addition to the relevant legislation governing the collection of rates, which includes the LGRA.

- 21 Councils have expressed concerns that if they have to comply with certain provisions of the CCCFA, in addition to the requirements of local government legislation, they will incur compliance costs that may impact on their willingness to offer the schemes. Any compliance costs would likely be passed on to borrowers. In 2012, Cabinet agreed to exempt VTR scheme providers from provisions of the CCCFA relating to continuing disclosure, early repayment of interest and charging of interest in advance [EGI Min (12) 20/12 refers].
- 22 Councils have since requested that they also be exempt from the unforeseen hardship and unreasonable fees provisions of the CCCFA as these overlap with similar requirements set out under the LGRA.

Unforeseen hardship provisions

- 23 The CCCFA contains unforeseen hardship provisions that allow a borrower, who is unable to meet the obligations of a credit contract due to factors including illness or loss of employment, to apply to the lender for certain changes to the credit contract. These changes include extending the term of the contract or postponing payments.
- 24 Councils currently provide relief to ratepayers experiencing financial hardship through rates remission and postponement policies. Under remission policies, councils may reduce or waive the amount of rates owing, while postponement policies allow for the collection of rates to be delayed. The LGRA sets out how rates remission and postponement policies are implemented.
- 25 As VTR contracts are consumer credit contracts that are administered and repaid through the rating system, it is currently unclear how a council might offer relief given the inconsistent requirements of the CCCFA and LGRA for addressing hardship. Councils argue that they can only offer relief under their existing remission and postponement policies and that complying with the additional requirements of the CCCFA would increase the cost and complexity of providing VTR schemes.
- 26 I propose to exempt VTR scheme providers from the unforeseen hardship provisions of the CCCFA. This will ensure that councils can continue to offer the schemes at a reasonable cost. Borrowers will still have access to hardship relief under rates remission and postponement policies.

Unreasonable default fees provisions

- 27 The CCCFA contains unreasonable default fees provisions which state that any default fee applied to a consumer credit contract must not be unreasonable. In determining whether a default fee is unreasonable, the court must give regard to (in relation to the matter giving rise to the fee) whether the fee reasonably compensates the lender for any costs or losses it incurs.
- 28 The LGRA states that late payment fees cannot exceed 10% of the outstanding balance. In practice, local and regional councils generally charge a flat 10% penalty fee for late payment of rates. Because VTR schemes are administered through the rating cycle, and repayments are made with general rates payments, this flat 10% default fee is applied to both the general rate and the amount due on the credit contract. A flat default fee may not meet the unreasonable default fees provisions of the CCCFA.

- 29 If councils are to comply with the unreasonable default fee provisions they will have to change their method of calculating default fees to allow for the default fee on the VTR credit contract to be calculated separately. This would result in increased administrative costs and complexity.
- 30 I propose to exempt VTR scheme providers from the unreasonable fees provisions of the CCCFA. Borrowers will still be protected from being charged high default fees by the provisions of the LGRA.

Consultation

- 31 The following Government departments and agencies have been consulted on this Cabinet paper: Commerce Commission, Ministry of Pacific Island Affairs, Te Puni Kōkiri, Ministry of Social Development, Ministry of Justice and the Treasury. The Department of the Prime Minister and Cabinet, Reserve Bank and Financial Markets Authority have been informed.

Disclosure-related regulations

- 32 *A Credit-related Disclosure and Rebate Regulations Discussion Document* was released for public consultation in November 2014. Seventeen submissions were received. These submissions were considered in developing the policy proposals set out above.

VTR exemption regulations

- 33 Officials consulted with councils, Local Government New Zealand, the Energy Efficiency and Conservation Authority and the Commerce Commission on regulations to exempt councils from provisions of the CCCFA relating to unforeseen hardship. Submissions broadly supported exemptions from these provisions due to the unnecessary compliance costs that would result from having to comply with the overlapping requirements of the LGRA and CCCFA.
- 34 Officials subsequently contacted councils to seek views on whether scheme providers may also require an exemption from the provisions of the CCCFA relating to unreasonable default fees. Councils supported these exemptions.

Financial Implications

- 35 There are no financial implications from the creation of these regulations.

Human Rights

- 36 There are no inconsistencies between the proposals in this paper and the New Zealand Bill of Rights Act 1990 or the Human Rights Act 1993. There are no gender or disability perspective implications from the proposals in this paper.

Legislative Implications

- 37 Regulations will be prepared in accordance with section 138 of the Credit Contracts and Consumer Finance Act 2003.

Regulatory Impact Analysis

- 38 The Regulatory Impact Analysis requirements apply to the proposals in this paper relating to disclosure and VTR exemption regulations. Regulatory Impact Statements have been prepared for these proposals and are attached.

Quality of the Impact Analysis

- 39 The General Manager, Strategic Policy Branch and the Ministry of Business, Innovation and Employment Regulatory Impact Analysis Review Panel have reviewed the attached Regulatory Impact Statements (RISs) prepared by the Ministry of Business, Innovation and Employment. They consider that the information and analysis summarised in these RISs meets the criteria necessary for Ministers to fairly compare the available policy options and take informed decisions on the proposals in this paper.

Publicity

- 40 I intend that a copy of this paper will be published on the Consumer Affairs website, which is administered by the Ministry of Business, Innovation and Employment.

Recommendations

- 41 The Minister for Commerce and Consumer Affairs recommends that the Committee:
- a. **Note** that regulations are required under the Credit Contracts and Consumer Finance Amendment Act 2014 to prescribe the costs of borrowing information (including interest charges and fees) to be publicly disclosed by lenders;
 - b. **Agree** that, for costs of borrowing, fees be permitted to be disclosed by lenders in a variety of ways, including disclosure of a dollar figure or a maximum dollar figure;
 - c. **Agree** that, for costs of borrowing, lenders will disclose an annual interest rate (or range of rates), which may be a representative figure if appropriate, and additional detail (such as the factors the lender will consider in selecting a rate within the range);
 - d. **Agree** that costs of borrowing information will be disclosed with a publication date, where appropriate;
 - e. **Agree** that costs of borrowing must be located on the lender's website in a way that makes these easy to find and compare;
 - f. **Agree** that credit card minimum repayment warnings will be in the form of a written warning statement that directs consumers to an online calculator, that this warning be displayed prominently on the billing statement and that disclosure of this warning may not be required in certain circumstances;
 - g. **Agree** that Voluntary Targeted Rate schemes be exempt from the unforeseen hardship provisions of the Credit Contracts and Consumer Finance Act 2003;
 - h. **Agree** that Voluntary Targeted Rate schemes be exempt from the unreasonable default fees provisions of the Credit Contracts and Consumer Finance Act 2003;
 - i. **Agree** that the rebate formula for repayment waivers should be equivalent to the existing rebate formula for consumer credit insurance;
 - j. **Agree** that the rebate formula for extended warranty agreements between lenders and borrowers should be a straight-line rebate formula;
 - k. **Invite** the Minister of Commerce and Consumer Affairs to issue drafting instructions to the Parliamentary Counsel Office to draft regulations to give effect to the decisions in this paper;
 - l. **Authorise** the Minister of Commerce and Consumer Affairs to make further minor or technical changes, consistent with the policy framework in this paper, on any issues that arise during the drafting process;

- m. **Agree** to release this Cabinet paper and related Cabinet decisions online, subject to any deletions that would be justified if the information had been requested under the Official Information Act 1982.

Hon Paul Goldsmith
Minister of Commerce and Consumer Affairs

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