



17 November 2009

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Dear James

### **Review of the Operation of the Credit Contracts and Consumer Finance Act 2003**

The Contract and Consumer Law Reform Committee (the Committee) appreciates the opportunity to comment on the Ministry of Consumer Affairs' (Ministry) Review of the Operation of the Credit Contracts and Consumer Finance Act 2003 (CCCFA) (Review).

#### **Information Disclosure**

##### *Motor vehicle finance*

The Committee agrees with the Ministry that there are problems with the CCCFA's disclosure provisions when it comes to motor vehicle finance. Neither the five working day disclosure window nor the three working day "cooling off" period work effectively in the case of motor vehicle finance. As the Ministry notes, if the borrower decides to cancel the credit contract once disclosure of the terms is received, the dual-contract nature of the transaction means that the vehicle cannot be returned in order to recoup the money required to repay the lender. Requiring on-the-spot disclosure of credit terms when accessing credit through a motor vehicle trader is a reasonable and practical solution to this problem.

The Committee also recognises the difficulties associated with such a requirement, including the fact that the lender may not be present at the time of purchase to make the necessary disclosure. The purchase will either have to be delayed until the borrower can meet the lender and organise finance (which may encourage the borrower to shop around for a better deal) or the disclosure obligations will need to be delegated to the motor vehicle trader, acting as the lender's agent. This is frequently the case in practice, with financiers operating an online contract setup. While this might skew the choice of financier in favour of the trader's choice of financier, the borrower will still have the "cooling off" period to seek alternative finance. The Committee considers that the interests of the borrower outweigh the difficulties associated with on-the-spot disclosure.

##### *Credit related insurance*

It is reasonable to require that credit related insurance disclosure (under section 70(1) of the CCCFA) meets the disclosure requirements of sections 32, 33 and 35 of the CCCFA. Although the Committee agrees that the requirements of section 32 should be sufficient for this type of disclosure, the Ministry will need to ensure that regulating credit related insurance disclosure

through section 32 does not reduce the amount of information borrowers receive as compared with what insurers are currently providing borrowers under section 70(1).

### *Prepayment fees*

Some form of disclosure relating to the method of calculation of prepayment fees is desirable from a consumer protection perspective. Such disclosure should avoid excessive detail and focus on conveying the key elements of prepayment fees that are of concern to a borrower. An effective way of providing this information would be through examples aimed at the specific loan being applied for. For example, a five year term loan contract could include a table setting out what the prepayment fees would be if the loan was repaid at various stages (i.e. two years in or four years in), taking into account the effect of one or more nominated floating or fixed interest rates.

### *Credit card statements and minimum payment amounts*

The practice of stating a minimum payment amount on a credit card statement, with no explanation of the implications of paying only that amount, is not in the best interests of borrowers. Adopting a similar approach to that recently introduced in the United States would be a sensible option for New Zealand. Specifically, the United States legislation requires that credit card statements include a written statement that "Making only the minimum payment will increase the amount of interest you pay and the time it takes to repay your balance". The Committee also considers that the total balance outstanding should be expressed clearly on the credit card statement.

### *Pawnbroking*

The Committee agrees that the current inconsistencies between the disclosure requirements of the CCCFA and the Secondhand Dealers and Pawnbrokers Act (SDPA) are undesirable and supports the Ministry's proposal to allow compliance with section 59 of the SDPA to be deemed compliance with section 17 and schedule 1 of the CCCFA. However, the Ministry's proposal may not go far enough in addressing all the inconsistencies between the two pieces of legislation. Pawnbrokers and their activities should be exempted from all sections of the CCCFA, with the possible exception of Part 5 (oppression provisions). The Committee would also consider supporting an exemption from the Part 5 oppression provisions should the Ministry introduce provisions relating to "unfair contract terms" into either the CCCFA or the Fair Trading Act 1986, as suggested in the Review.

## **Credit Fees and Charges**

### *Guidelines for Credit Fees*

The Committee considers that the draft Guidelines for Credit Fees released by the Commerce Commission earlier this year provide sufficient advice for the industry to develop "reasonable" fee structures. Any greater regulation or more prescriptive guidelines may require lenders to amend existing fee structures which already satisfy the "reasonable fee" test.

The principle-based approach of the draft Guidelines provides enough freedom for lenders to develop their own fee structures, while still providing borrowers with sufficient information about how and why credit fees are charged.

The Committee suggests the addition to section 24 of the CCCFA of a provision allowing borrowers to enquire as to what the credit fees cover and how they are calculated. Alternatively,

and possibly more realistically, the credit contract disclosure provided at the commencement of the contract could refer the customer to the Commerce Commission's Fee Guidelines for more information.

#### *Frontloading fees*

The Committee agrees with the Ministry that consideration should be given to amending the CCCFA to prevent fees for services to be carried out in the distant future (as against fees relating to the initial administration of the contract) being debited at the commencement of a credit contract, until those services are performed. The objective should be to minimise the risk of interest being charged on fees for services yet to be performed, and which may never be performed if early repayment is sought.

#### *Timing of "reasonableness" applications*

The Committee agrees that the current time limit for bringing an application for a reasonableness order under section 41 of the CCCFA is causing difficulty for the Commerce Commission in responding to complaints from borrowers. There are two possible options to address this. The first would be to define a longer period for bringing a complaint. The second would be to allow the time limit to run from the time the Commerce Commission receives the complaint, as opposed to running from the time the infringement occurred. Either of these options would allow the Commerce Commission to bring effectively all relevant complaints before the Court and, as the Commission would still have to work within a time frame, would also ensure that borrowers did not suffer undue delays and that lenders were not disadvantaged through being "encouraged" to continue charging fees which the Court might consider to be unreasonable.

Removing the time frames altogether would not be in the best interests of borrowers, because it could lead to the Commerce Commission's investigations being unnecessarily long and drawn out. Whether or not the time limit for bringing an application is changed, it would be sensible for the time limit to be brought to the borrower's attention as part of the initial credit contract disclosure.

#### *Third party fees*

The Committee agrees that lenders passing on third party fees that are not from a genuine, independent third party is a practice that the CCCFA should aim to prevent. The Committee suggests adding a provision to the CCCFA (possibly by way of an amendment to section 45) requiring fees or charges passed on from a third party not at an arm's length from the lender to satisfy the "reasonableness" test as required of other credit fees and charges. This would sufficiently protect borrowers from being on-charged fees that are not genuine, while still allowing lenders to pass on legitimate third party fees, at cost, as was the intention of the CCCFA.

### **Hardship Provisions**

#### *Availability of hardship relief for borrowers in default*

It is appropriate hardship relief be available to borrowers who are in default by less than 2 months. Initial disclosure in the credit contract should make this time frame clear and should emphasise that making an application early will reduce the amount of default interest charged. It should also be emphasised that while default interest will not be charged during the hardship application process, it will be charged for the entire period should the hardship application be

refused. Lenders should ensure they provide borrowers with this information both at the commencement of the credit contract, at the time the borrower is first in default, and again at the time an application for hardship relief is made.

#### *Timeframes for acknowledging hardship applications*

The Committee agrees that lenders should be required to acknowledge receipt of a hardship application, in writing, and that the proposed five working day time frame for this is appropriate. The acknowledgement should include information relating to:

- the time within which the borrower can expect to hear about the outcome of application;
- the suspension of default interest during the application process (and the fact that it may be charged for the whole period if the application is declined); and
- the borrower's right to take the matter to the Disputes Tribunal (and the process for doing so) should the application not be decided within the appropriate timeframe.

Lenders should be required to provide reasons for declining a hardship application and to advise borrowers of their right to have the decision reviewed by the Disputes Tribunal.

Lender should also advise the borrowers of their right to have the decision reviewed by the Disputes Tribunal and be required to provide reasons for declining a borrower's hardship application to the Disputes Tribunal when required to do so.

#### *Fees for hardship applications*

Charging fees for hardship applications is contrary to the purpose of the hardship provisions. The Committee agrees with the Ministry's proposal to prohibit the charging of such fees.

#### *Disclosure about hardship options*

Many of the issues with the hardship provisions highlighted in the Review would be lessened by requiring lenders to provide greater disclosure about options for borrowers facing unforeseen hardship. The contract documentation is likely to be the first place a borrower looks for information when faced with financial hardship. If this disclosure is sufficiently clear, the borrower is more likely to contact the lender within the specified time frames.

### **Unsolicited Credit**

The Committee supports the Ministry's proposal that credit and finance card increases should only occur on an "opt-in" basis. This would require borrowers to make a conscious decision about their financial obligations and will not allow them to increase their debt through lack of action.

The Ministry should consider placing a restriction on the method by which such extra credit can be offered. For example, requiring that extra credit be offered, and accepted, in writing so that the borrower is not forced to make an on-the-spot decision, as may happen if such an offer is made over the phone.

### **Oppressive Conduct**

Further consideration should be given to including provisions relating to "unfair contract terms", similar to those recently introduced in Australia, to either the CCCFA or the Fair

Trading Act 1986 (FTA). The Committee would appreciate the opportunity to consider this point further under the review of the FTA. At this stage the Committee reserves its position in respect of this issue, noting that New Zealand consumer law (particularly the non-contractual Consumer Guarantees Act 1993) has a more consumer friendly approach to fairness.

### **Credit (Repossession) Act 1997**

It is in the best interests of borrowers for the CCCFA to require any property over which a lender has a security interest to be identified clearly and specifically in the document creating that interest. The Committee supports the addition of a requirement into the Credit (Repossession) Act 1997 (CRA) that any property seized must have been identified specifically in the credit contract (in accordance with the CCCFA) and must also be sufficiently identified in the pre-possession notice. This proposal will benefit both lenders and borrowers because it will allow a lender to ensure it has adequate security while also ensuring borrowers are made aware of the implications of granting a lender security over their property.

The remaining issues raised by the Ministry in relation to the CRA are important and require further and more detailed consideration. Repossession of a borrower's personal property is a distressing enforcement measure and, as such, should be regulated strictly. Accordingly, there needs to be enforcement of compliance with the Act by an authority such as the Commerce Commission.

The balance between borrower and lender rights under the CRA would be enhanced by the introduction of penalties for non-compliance (including penalties against repossession agents as well as against non-complying lenders), broader relief provisions for borrowers, and possibly a requirement for a lender to obtain a "repossession order" similar to the Tenancy Tribunal order required by a landlord, although analysis of the financial impact of this would be necessary.

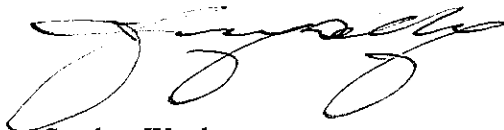
The Committee encourages the Ministry to conduct a more detailed assessment of the operation of the CRA in light of the issues raised in the Review and would appreciate any opportunity to comment further on such an assessment.

### **Fringe Lending Practices**

The Ministry raises relevant and important concerns in relation to fringe lending in New Zealand. The Committee would support further initiatives regarding unfair credit contract terms and responsible lending requirements, similar to those initiatives currently being introduced in Australia.

The Committee trusts that these comments are of assistance. If you have any further queries please contact the Committee Secretary, Fionnuala Kelly, phone (04) 463 2960, or email, [fionnuala.kelly@lawsociety.org.nz](mailto:fionnuala.kelly@lawsociety.org.nz).

Yours sincerely



Stephen Ward

**Convener, Contract and Consumer Law Reform Committee**