PART 4:

SECTOR SPECIFIC REGULATION

Chapter 11

The Regulation of Consumer Credit Products: The Effects of Baseline Assumptions

Graeme Austin[*]

11.1 Introduction

How do baseline assumptions affect regulatory responses? This chapter examines this question in the context of the Credit Contracts and Consumer Finance Act 2003 ("CCCFA"), an enactment whose principal aim is said to be "protect[ing] the interests of consumers in connection with credit contracts".[1] Consumer credit products regulated under the CCCFA include credit cards, overdraft facilities, mortgages, motor vehicle finance, and payday loans.[2] The regulation of consumer credit is an enormously complex task − one that has preoccupied expert policy-makers over many generations, not only in New Zealand, but in most other jurisdictions in which functioning consumer credit markets exist. The purpose of this chapter is not to engage with the broader agenda of how to achieve better regulation of markets; rather, its more modest aim is to explore the ideas that inform the concept of "protection" in the regulation of consumer credit products. How does

* Professor of Law, Victoria University of Wellington and the Melbourne University Law School.
Thanks to Ruth Upperton and Sarah Wilson for their excellent research assistance, Paul Scott for his expert commentary on an earlier draft, the various participants in workshops at which this research was presented, and the anonymous referees for their invaluable suggestions.

1 *Commerce Commission v Bluestone Mortgages NZ Ltd* HC Auckland CIV-2009-409-617, 21 October 2010 at [7].

2 The term "consumer credit contract" is defined in the Credit Contracts and Consumer Finance Act 2003, s 11. The Act principally operates to regulate these contracts.

New Zealand's consumer credit regime approach the issue of protection?[3] Against what do New Zealand consumers of credit contracts require protection? What assumptions inform regulators' approaches to consumer protection in this context?

The dominant regulatory approach in this area might be described as an "information disclosure" paradigm. The aim is to try and correct information asymmetries, and address accompanying market failure problems, by enhancing the quality of information received by consumers prior to entering into consumer credit contracts. Accordingly, the CCCFA includes detailed stipulations as to what must be included in a valid consumer contract.

There are, however, other ways to think about consumer "protection". As other scholars have noted, a "safety paradigm"[4] would emphasise the *safety* of consumer credit products in their purchasers' hands. What might be envisaged by a consumer "safety" paradigm is discussed in more detail in at [11.4]. Both paradigms are reflected in the CCCFA. However, as is examined in more detail below, the information disclosure model has arguably been afforded greater weight in policy deliberations and in the regulatory responses to those deliberations.

Consistent with the Stage One aims of the New Zealand Law Foundation's Regulatory Reform Project, this chapter aims to achieve two goals. First, it seeks to substantiate the case that the baseline assumptions for regulation of consumer credit products in New Zealand are more consistent with an information disclosure paradigm. Second, it advances a preliminary examination of the implications of putting greater emphasis on consumer safety in the regulation of these products.

11.2 Regulation of consumer credit "products"

At the outset, it is useful to explain the use of the term "consumer credit products", instead of the more traditional term (the term used in the CCCFA)

3 A more detailed discussion of the paternalistic approach can be found in: Kate Tokeley "Consumer Law and Paternalism: a Framework for Policy Decision-Making" in this volume (ch 10).

4 See generally Oren Bar-Gill and Elizabeth Warren "Making Credit Safer" (2008) 157 U Penn L Rev 101; Jodi Kantor and Ben Werschkul "Elizabeth Warren's Mission" (2010) New York Times Video Library video.nytimes.com/video/2010/03/24/business/1247467419428/elizabeth-warren-s-mission.html (last accessed 8 August 2011). Professor Warren has elaborated on the distinction between the regulation of credit products and traditional consumer goods.

consumer credit "contracts". "Product" is the term that is increasingly used in regulatory contexts.[5] Moreover, it is consistent with marketplace realities.

The use of the term "contract" here is suggestive of a legislative purpose to regulate a particular species of transaction so as to enhance the quality of information available to consumers and the choices they make. The term is also suggestive of the idea of the sovereign consumer. In reality, however, marketplace characteristics significantly constrain consumer choices.[6] Consumer credit contracts are invariably "standard form".[7] Recourse to such contracts is not, of course, problematic in itself: it can be fundamental to controlling transaction costs, a benefit to both creditor and debtor. However, when consumers are unable to negotiate contractual terms, and instead can only choose between different purveyors of credit (as the statement of legislative aims in the CCCFA puts it, "to distinguish between competing credit arrangements"[8]), it seems more realistic to regulate credit contracts as "products" rather than "contracts".[9]

Predictably, there is nothing in the statement of legislative aims in the CCCFA concerning the ability of consumers in the market for credit products to *negotiate* a better deal with a supplier of credit ex ante. The only real negotiation anticipated by the Act is in the context of ex post adjustment in cases of unforeseen hardship (and here, perhaps, this opportunity is tenable only because the cost to the lender of adjusting the terms of the contract is likely to be less than that of enforcement following default).[10] For the most part, the best that consumers can be offered is *information* about the different products from which they can choose.

---

5 For example, the term was used by the Council of Australian Governments when agreeing to their regulation by the Australian Government. See "COAG Agreement" (2009) Australian Government www.treasury.gov.au/consumercredit/content/coag_agreement/default.asp (last accessed 8 August 2011).

6 See Paul Scott "Competition Law and Policy" in this volume (ch 3).

7 Ministry of Consumer Affairs *Consumer Credit Law Review: Part 2: Application: What Transactions Should Consumer Credit Legislation Apply To?* (2000) at 14. The Review says that "the consumer credit market is generally based on standard form contracts, which further lessen the scope for negotiation between borrower and lender".

8 Credit Contracts and Consumer Finance Act 2003, s 3(b)(i).

9 Ministry of Economic Development *Review of Financial Products and Providers – Stage One: Framework, Problem Identification and General Directions for Reform – Report to Minister of Commerce* (2005). See generally Douglas Baird "The Boilerplate Puzzle" (2006) 104 Mich L Rev 933.

10 Ministry of Consumer Affairs *Consumer Credit Law Review: Part 4: Overindebtedness, Insurance and E-credit* (2000) at 7.

11.3 The current regulatory framework

It is useful to put the issue of indebtedness in context. In New Zealand, levels of personal debt have soared within the last decade. The personal debt of New Zealanders added up to NZ$74,235 million in 2000, but by 2009 this figure had grown to NZ$180,695 million.[11] Within this time frame the portion of this figure comprising consumer loans increased from NZ$2,895 million to NZ$5,023 million.[12] To put this into perspective, at the end of 2009, debt stood at 157.2 per cent of nominal household disposable income per annum.[13] In addition, New Zealanders' perceptions of their own indebtedness are changing. Twenty-eight per cent of people expect to have difficulty meeting their credit commitments within the next three months and there is a widespread perception amongst New Zealanders that their personal debt is set to increase in the near future.[14] The impacts of the CCCFA on New Zealanders are significant.

The CCCFA, which took effect from 1 April 2005,[15] is principally concerned with prescribing disclosure of information.[16] In broad outline, the requirements for initial disclosure are as follows:[17]

1. the full name and address of the creditor;
2. the initial unpaid balance;
3. the credit limit;
4. the annual interest rate and the method of charging interest, the total interest charges, and interest-free periods (if any);

---

11 Organisation for Economic Co-operation and Development "Households' financial and non-financial assets and liabilities" (2011) OECD Stat Extracts stats.oecd.org/Index.aspx?DataSetCode=7HA (last accessed 8 August 2011).

12 Reserve Bank of New Zealand "Household financial assets and liabilities" (2003) at table 4: available at www.rbnz.govt.nz/statistics/monfin/HHAandL.xls (last accessed 8 August 2011).

13 Reserve Bank of New Zealand "Key graphs – Household debt" (2011) www.rbnz.govt.nz/keygraphs/fig5.html (last accessed 8 August 2011).

14 Dun and Bradstreet "Credit proving a challenge for consumers: one in three expect difficulties meeting their upcoming credit commitments" (2011) dnb.co.nz/Header/News/Credit_proving_a_challenge_for_consumers/indexdl_7291.aspx (8 August 2011).

15 Credit Contracts and Consumer Finance Act 2003, s 2.

16 In general, the Act applies to consumer credit contracts; these are defined as contracts where the debtor is a natural person, who enters into the contract primarily for personal domestic or household purposes, and interest, credit fees or a security interest are charged under the contract. For the Act to apply, the creditor needs to carry on the business of providing credit, or make a practice of providing credit in the course of business. Where the debtor is a company, an incorporated society or similar incorporated body, a credit contract will not be a consumer credit contract for the purposes of the Act, and accordingly will not be subject to most of its provisions. Credit Contracts and Consumer Finance Act 2003, s 11(1).

17 Credit Contracts and Consumer Finance Act 2003, sch 1.

5. information relating to advances; payments and full repayment; default interest charges and default fees; total interest charges and any interest-free periods; a creditor's consent to receive electronic communication; a statement of the debtor's right to cancel and the frequency of continuing disclosure statements; a description of credit fees and charges; and any security interest; and
6. other information or warnings as prescribed by regulations.

This disclosure must be either before the consumer credit contract is made or within the following five working days.[18]

For continuing disclosure, the requirements are as follows:[19]

1. the opening and closing dates of the period covered by the statement;
2. the opening and closing unpaid balances;
3. the date, amount, and a description of each advance during the statement period, each interest charge debited to the debtor's account during the statement period, each amount paid by the debtor to the creditor or credited to the debtor during the statement period, and each fee or charge debited to the debtor's account during the statement period; and
4. the amount of and the due date of the next payment that must be made by the debtor under the consumer credit contract; and the annual interest rate or rates during the statement period (expressed as a percentage or percentages).

In addition to these disclosure obligations, the CCCFA contains other mechanisms for protecting consumers. These include: control of interest;[20] charges and fees;[21] the right to cancel the contract;[22] provisions enabling changes to the contract because of unforeseen hardship;[23] and the power to reopen oppressive credit contracts.[24] Some of these measures go further than merely trying to enhance the information provided to consumers. As is explained below, however, the relevant statutory thresholds and assessment criteria will likely impose significant costs and/or procedural barriers to their application and enforcement. It may be helpful to consider these additional measures in further detail.

[18] Credit Contracts and Consumer Finance Act 2003, s 17.
[19] Credit Contracts and Consumer Finance Act 2003, s 19.
[20] Credit Contracts and Consumer Finance Act 2003, ss 36-40.
[21] Credit Contracts and Consumer Finance Act 2003, ss 41-44.
[22] Credit Contracts and Consumer Finance Act 2003, ss 27-31.
[23] Credit Contracts and Consumer Finance Act 2003, ss 55-59.
[24] Credit Contracts and Consumer Finance Act 2003, ss 117-131.

11.3.1 *Unreasonable credit or default fees*

Section 41 of the CCCFA prohibits a creditor from charging an "unreasonable credit or default fee", a provision that the Commerce Commission has described as "fundamental".[25] The reasonableness of fees (other than "establishment fees"[26]) charged by a credit provider (such as "credit fees" and "default fees") is to be assessed according to criteria that reference both the costs associated with, and reasonable compensation for, both the provision of the service *and* "reasonable standards of commercial practice".[27] The Commerce Commission has said that in order for recovery to be both reasonable, and in compensation for service provided, there must be a causal nexus, broadly in line with the common law standard of "remoteness", connecting the fee to the cost incurred.[28] But, quite understandably, the Commission is only able to provide very general guidance as to what "reasonable standards of commercial practice" means. It does, however, stipulate that the credit provider must be able to justify the fee.[29] The Commission says only that it "is not in a position to stipulate in advance what will be a reasonable standard of commercial practice, and in every case it will depend upon the evidence available".[30] This point seems especially applicable in the case of default fees.

The Commission's approach is understandable. Even if courts are the final arbiters,[31] the inclusion of "reasonable standards of commercial practice" ties scrutiny of the reasonableness of the fee to the provider's assessment of what the market will bear. The CCCFA seems to anticipate that the charging of fees is a legitimate part of a credit provider's business − which suggests that the reasonableness criteria are drafted by the market's invisible hand,[32] animated by providers' profit motives. Commercial imperatives might, quite legitimately, account for a significant portion of the fee charged, making it difficult to tether the actual fee to the more objective criteria in s 44 that are grounded in the causal nexus between the fee charged and compensating for the service

25 *Commerce Commission Credit Contracts and Consumer Finance Act: Draft Guidelines for Consumer Credit Fees* (2010) at 1.

26 "Establishment fees" are instead governed by the Credit Contracts and Consumer Finance Act 2003, s 42, which expressly links the reasonableness of the establishment fee to the costs associated with application processing and related matters.

27 Credit Contracts and Consumer Finance Act 2003, s 44.

28 See also *Commerce Commission v Avanti Finance* (2009) NZBLC 102,662 (HC), which concerned the reasonableness of a pre-payment fee. As Priestley J noted in *Commerce Commission v Bluestone Mortgages NZ Ltd* HC Auckland CIV-2009-409-617, 21 October 2010 at [48]; the defendant in *Avanti* had in place a pre-payment compensation formula.

29 *Commerce Commission Credit Contracts and Consumer Finance Act: Draft Guidelines for Consumer Credit Fees* (2010) at 6.

30 *Commerce Commission Credit Contracts and Consumer Finance Act: Draft Guidelines for Consumer Credit Fees* (2010) at 7.

31 *GE Custodians v Bartle* [2010] NZSC 146, [2011] 2 NZLR 31 at [37].

32 See also Paul Scott "Competition Law and Policy" in this volume (ch 3).

provided. Accordingly, the reference to commercial practice in the statutory criteria may provide creditors with an important buffer against rigorous judicial scrutiny.

11.3.2 *Unforeseen circumstances*

Subpart 8 of the CCCFA allows changes to be made to credit contracts where debtors face unforeseen hardship. Debtors who are unable to meet their obligations under a credit contract because of illness, loss of employment, the end of a relationship or other reasonable cause may apply to the credit provider to extend the term of the contract and reduce the amount of each payment; postpone payments for a specified period; or both.[33] A reasonableness criterion applies to the inability to meet the obligations under the contract.[34] There is no provision enabling the debtor to apply to have any part of the unpaid balance written off, and the Act provides that the types of changes debtors can request do not include changes to the annual interest rate.

The applicable standards in this area are quite vague. For instance, any change must not be more extensive than is necessary to enable debtors to reasonably expect that they will be able to discharge their obligations.[35] Moreover, the change “must be fair and reasonable to both the debtor and the creditor in all the circumstances”.[36] Conversely, there are quite clear stipulations as to when the facility does not apply: the debtor must not have defaulted in a payment or allowed the credit limit to be exceeded.[37] Accordingly, it would appear that only well-organised and far-sighted debtors – those who act before getting into difficulties under the contract – will be advantaged by the new facility. In addition, it must not have been reasonably foreseeable to the debtor at the time the contract was made that the debtor would be unlikely to be able to discharge his or her obligations under the consumer credit contract because of the illness, the injury, the loss of employment, the end of the relationship, or the other reasonable cause.[38] This perhaps suggests that the more vulnerable the debtor’s position – consider the situation of debtors with histories of indifferent health – the less likely they will be able to take advantage of the new provisions. Finally, where the debtor will not agree to the requested change, application is in the first instance, to the District Court, not the Disputes Tribunal. This may impose an additional barrier to meaningful use of this procedure based on the potential cost and delay of such an application.

---

33 Credit Contracts and Consumer Finance Act 2003, ss 56–57.

34 Credit Contracts and Consumer Finance Act 2003, s 56(2).

35 Credit Contracts and Consumer Finance Act 2003, s 56(2).

36 Credit Contracts and Consumer Finance Act 2003.

37 Credit Contracts and Consumer Finance Act 2003, s 57(1)(a)–(b).

38 Credit Contracts and Consumer Finance Act 2003, s 57(1)(c).

11.3.3 *Power to reopen "oppressive contracts"*

Like its 1981 predecessor,[39] the CCCFA provides a judicial power to reopen "oppressive" contracts.[40] A court is able to consider whether non-credit terms (warranty disclaimers, other clauses excluding liability) as well as credit terms (terms relating to interest, fees, defaults) are oppressive. The court can also reopen a contract if it considers the contract itself to be oppressive or if a party to the transaction has exercised or intends to exercise a contractual power in an oppressive manner or if a party has induced another party to enter into the arrangement by oppressive means.[41]

The Act defines "oppressive" as: "harsh, unjustly burdensome, unconscionable, or in breach of reasonable standards of commercial practice".[42] A court will consider the following factors in determining whether or not to re-open a contract on the grounds of oppression:[43]

1. all the surrounding circumstances;
2. whether the amounts payable by the debtor are oppressive;
3. whether the time allowed to remedy any default is oppressive, given the likelihood of loss to the creditor;
4. whether a refusal to release a security is oppressive in terms of obligations secured and the extent of any security remaining after the release;
5. whether an amount charged on full prepayment is oppressive, bearing in mind the creditor's expenses and the likelihood the amount repaid could be re-invested on similar terms; and
6. any other matters the court thinks fit.

Ostensibly, it is a broad power – but there is a high threshold for judicial intervention. Tipping J has said that it is necessary to compare the actions of a defendant with "reasonable standards of commercial practice".[44] Accordingly, "[s]omething which is in accordance with … such standards could hardly be held to be oppressive".[45]

---

39 Credit Contracts Act 1981.

40 Credit Contracts and Consumer Finance Act 2003, s 120(a).

41 Credit Contracts and Consumer Finance Act 2003, s 120(b)-(c). In this context, a power includes: refusing to agree to end a contract early; refusing to vary or waive any contractual term; or imposing a condition on an agreement to terminate the contract early. See Credit Contracts and Consumer Finance Act 2003, s 121.

42 Credit Contracts and Consumer Finance Act 2003, s 118.

43 Credit Contracts and Consumer Finance Act 2003, s 124.

44 *Raptorial Holdings Ltd (in receivership) v Elders Pastoral Holdings* Ltd [2001] 1 NZLR 178 at [49], quoting Tipping J in *Greenback New Zealand Ltd v Haas* [2000] 3 NZLR 341 (CA) at [24].

45 *Greenback New Zealand Ltd v Haas* [2000] 3 NZLR 341 (CA) at [24]. This is underscored by the evidence that a court can consider under s 126 of the Credit Contracts and Consumer Finance Act 2003. Section 126 enables the court to hear evidence of commercial practice so that it may place the conduct complained of in context. More specifically, it may consider

More recently, however, the concept of "oppression" has been approached by some New Zealand judges in a way that evinces some concern with consumer safety issues. The power to reopen oppressive contracts was considered by the Supreme Court in *Bartle v GE Custodians Ltd (Bartle).*[46] The Court of Appeal had held in favour of the debtors, a retired couple who had purchased a product known as the "Blue Chip scheme". Under this scheme, people in the Bartles' situation who were "income poor" could use the equity in an unencumbered asset, such as a family home, to assist with the purchase of a residential apartment and thereby secure both an income stream (rent from the apartment) and a capital gain once the apartment was sold. Finance for the purchase was provided by the defendant, GE Custodians, under an arrangement with New Zealand-based lending brokers, including Tasman Mortgages Limited (TML). While the viability of the scheme anticipated a reasonably quick sale of the apartment (after four or five years) in order to realise the capital gain, the loan terms were actually for 25 years. Importantly, the interest was fixed for five years, but then was to revert to a variable rate. The product purchased by the Bartles might best be described as a form of "asset lending".[47] Hammond J characterised the scheme in these terms:[48]

> It is important not to let the fundamentals of this transaction be obscured by the "smoke and mirrors" which routinely attend a case of this kind. Those features included an investment scheme which was overly elaborate, poorly drafted and explained, and had no apparent business plan. It was hopelessly over-dependent on a distinctly rising real estate market. Even assuming the scheme went according to plan, and there were plenty of opportunities for it not to, the principal beneficiary would be Blue Chip. All there was in this scheme for the Bartles were fortnightly payments of $451, which they had borrowed to pay themselves, and the prospect of 10 per cent of any capital gain after four years on unit 701. For this they were placing their freehold home on the line.

The inevitable happened. The income stream was not as high as anticipated; the Bartles stopped receiving rents; Blue Chip went into receivership; the apartment was sold at significantly less than the original purchase price; GE called in the security for the loan and the Bartles were faced with the prospect of losing their home.

The Court of Appeal held that this was an oppressive contract. It also accepted that TML was an agent of GE for the purposes of the CCCFA. Disagreeing with the Court of Appeal's analysis of the agency issue, however, the Supreme Court overturned the decision. As a result, the Bartles' claim

evidence as to the terms on which credit, for example, was available from other persons at the relevant time; the rights and powers of other creditors; and inducements offered by other creditors.

46 *GE Custodians v Bartle* [2010] NZSC 146, [2011] 2 NZLR 31.

47 *Bartle v GE Custodians* [2010] NZCA 174, [2010] 3 NZLR 601 at [207].

48 *Bartle v GE Custodians* [2010] NZCA 174, [2010] 3 NZLR 601 at [25].

under the Act collapsed. Because the agency issue was the primary focus of the Supreme Court's analysis, much of the Court of Appeal's analysis on the substantive point − whether the contract was "oppressive" − arguably stays intact. That said, some of the statements in the Supreme Court's judgment, in particular comments about problems of too much "hindsight" in the analysis of the Blue Chip scheme,[49] perhaps call into question some aspects of the Court of Appeal's approach.

For present purposes, the uncertainty as to the scope of the court's power in the context of oppressive contracts underscores the basic point that as a practical matter the regulation of consumer contracts principally concerns the amount and quality of the information that purveyors of these products are required to provide to consumers. The power to reopen oppressive contracts is important, but it may not be particularly easy to apply in practice, as with other controls, such as the controls on credit and default fees.

11.4 Safety and credit products

What would a policy discussion look like if there were greater engagement with the issue of the "safety" of consumer credit products? A useful starting point is a thought experiment developed by Professors Elizabeth Warren and Oren Bar-Gill. Suppose that the safety of ordinary consumer products were regulated in the same way as consumer credit. Warren and Bar-Gill note that, in the United States, it is almost impossible to buy an unsafe consumer product − such as a toaster.[50] The safety of these kinds of products is regulated more directly.[51] But credit products that are unsafe in some consumers' hands are quite readily available. In the New Zealand context, Warren and Bar-Gill's point can be illustrated by the regulation of children's nightgowns: in New Zealand, we regulate the *safety* of children's nightgowns, not just the information that accompanies their sale. While the information provided to consumers is relevant in most consumer contexts, the sale of (some) unsafe children's nightwear is not *conditioned* on the adequacy of nightwear specifications to which consumers might have access prior to

49 *GE Custodians v Bartle* [2010] NZSC 146, [2011] 2 NZLR 31 at [59]. "... even if the apartment were to drop in value, someone looking at the situation without the benefit of our present hindsight might well have considered that the borrowing did not necessarily put the Bartles at risk of losing their home." See further at [64]: "... [o]n what they knew at the time, without hindsight, this was not a case where the transaction would have appeared so disadvantageous that no solicitor could advise the Bartles to proceed."

50 Oren Bar-Gill and Elizabeth Warren "Making Credit Safer" (2008) 157 U Penn L Rev 101 at 106.

51 As to the difference between hard and soft paternalism see Kate Tokeley's "Consumer Law and Paternalism: a Framework for Policy Decision-Making" in this volume (ch 10).

purchase.[52] With certain types of nightwear, parents are simply not permitted to make an informed trade-off between safety and price. To be sure, for some products, consumers regularly make such trade-offs − choices between different models of motor vehicle are a familiar example. Here, however, consumer choice is exercised only after manufacturers pass a baseline safety threshold. In contrast, consumer credit products might be quite unsafe in the hands of certain consumers for a variety of reasons: taking on more debt than one can bear can lead to deleterious effects on physical and mental health, for example. But for most practical purposes, the sale of such products is conditioned primarily on the provision of the prescribed information.[53]

"Information disclosure" and "consumer safety" paradigms reflect different baseline assumptions, and envisage different kinds of market intervention and different approaches to interference with contractual freedom in this context. These paradigms emphasise different kinds of reasons for regulatory intervention in consumer markets.[54] The "information disclosure" paradigm responds to information asymmetry problems by stipulations as to the quality and quantity of information available to consumers.[55] The "consumer safety paradigm" largely concerns the products themselves; it can lead to proscriptions against bringing certain products to the market even when it is possible to provide consumers with sufficient information about a product's risks. Measures that address informational asymmetries aim to make the process of contracting work better; many consumer safety measures, in contrast, aim to prevent some contracts from being entered into at all.

In the wider New Zealand policy context, increased attention has been given to personal safety issues associated with consumer credit products. Some government agencies have noted the deleterious effects associated with

---

52 The regulation of children's nightwear is contained within the Product Safety Standards (Children's Nightwear and Limited Daywear Having Reduced Fire Hazard) Regulations 2008, which are issued under the Fair Trading Act 1986, s 29. The Regulations are enforceable by the Commerce Commission. They require those who supply the relevant products to meet certain standards for product testing and labelling as required by the Australia and New Zealand Safety Standard AS/NZS 1249:2003: Product Safety Standards (Children's Nightwear and Limited Daywear Having Reduced Fire Hazard) Regulations 2008, sch 2. One of the product testing requirements, as outlined in [4.2] of the Standard, is that no children's nightwear may be sold if it has a surface burning time of less than 10 seconds. Fabrics which have a faster surface burning time can easily cause far more serious injuries than those with a slower surface burning time. The test for surface burning time of fabric is set out in: International Organization for Standardization "Textiles – Determination of surface burning time of fabrics: ISO 10047:1993" (1993) www.iso.org/iso/iso_catalogue/catalogue_tc/catalogue_detail.htm?csnumber=18012 (last accessed 8 August 2011).

53 See the discussion at [11.3].

54 As to the question when an intervention is paternalistic see Kate Tokeley "Consumer Law and Paternalism: a Framework for Policy Decision-Making" in this volume (ch 10).

55 See generally Ministry of Consumer Affairs *Consumer Credit Law Review: Part 1: Setting the Scene* (1999) at 21 (noting information asymmetry problems in this context).

the debt cycle – including physical and mental health problems,[56] stress on relationships,[57] disruption to family life, and so on. In 2009, the Ministry of Consumer Affairs noted that "many consumers are facing greater challenges in accessing, using and repaying credit".[58] A 2004 Ministry of Social Development paper suggested that "up to 15 per cent of New Zealand households may be over-indebted (in the sense of struggling to meet their financial commitments to pay monies owed) at some point during any 12-month period, one-third of whom may have longer-term problems requiring external intervention."[59] The same paper observed that "[b]eing over-indebted obviously had financial implications in terms of the ability to make ends meet, but it also appears to have negative impacts on (especially mental) health, and may be linked to suicide".[60]

A 2009 paper by the New Zealand Families Commission drew links between over-indebtedness and the marketing of consumer credit products.[61] The paper reported on a series of interviews with families that were experiencing problems with debt. Respondents reported family pressure or encouragement to shoulder more debt;[62] problems with understanding the implications of purchasing a credit product and understanding the "fine print";[63] and the feeling of being pressured to accept higher credit limits.[64]

---

56 Jaimie Legge and Anne Heynes *Beyond Reasonable Debt: A background report on the indebtedness of New Zealand families* (RR 8/08 Family and Retirement Commission, 2008) at 43.

57 Jaimie Legge and Anne Heynes *Beyond Reasonable Debt: A background report on the indebtedness of New Zealand families* (RR 8/08 Family and Retirement Commission, 2008) at 22.

58 Ministry of Consumer Affairs *Review of the Operation of the Credit Contracts and Consumer Finance Act 2003* (2009) at 1.

59 Oliver Valins *When debt becomes a problem: A literature study* (Ministry of Social Development, 2004) at viii.

60 Oliver Valins *When debt becomes a problem: A literature study* (Ministry of Social Development, 2004) at ix.

61 Nicolette Edgar and Janine McCardle (eds) *Escaping the Debt Trap: Experiences of New Zealand Families Accessing Budgeting Services* (RR6/09 Families Commission, 2009).

62 Nicolette Edgar and Janine McCardle (eds) *Escaping the Debt Trap: Experiences of New Zealand Families Accessing Budgeting Services* (RR6/09 Families Commission 2009) at 41. One participant said, at 46, "I was working and one of my friends she was working there, so that's why I went there ... My husband encouraged the loan".

63 Nicolette Edgar and Janine McCardle (eds) *Escaping the Debt Trap: Experiences of New Zealand Families Accessing Budgeting Services* (RR6/09 Families Commission 2009) at 46. Another participant in the Families Commission survey reported: "Yeah at the time I was probably in a rush, we weren't really thinking straight, I did it and I knew it was quite high... 30 per cent ... I know it's our fault too, we should really look at trying to read every fine print but you find that with the sales people they don't try and ... they don't make it clear, they don't say up front the final amount you will end up paying is ... they don't say that ... I was hesitant but I still went ahead."

64 Nicolette Edgar and Janine McCardle (eds) *Escaping the Debt Trap: Experiences of New Zealand Families Accessing Budgeting Services* (RR6/09 Families Commission 2009) at

What might an emphasis on consumer safety bring to policy deliberations in this context? The regulation of consumer safety is not necessarily an impediment to marketplace efficiency. Indeed, it sometimes operates in a similar way to measures that address information asymmetries through disclosure requirements. For example, key product variables relevant to safety of children's nightgowns, including product characteristics (the type of fabric for instance) are not easily detected by purchasers. Proscribing the use of certain types of fabric enables consumers to focus on product features that they *can* detect, such as the quality of stitching or design innovations, in order to make their choices. When consumers can rely on a regulatory framework, including inspections and prosecutions, the costs of looking behind any claims made by vendors are reduced. Furthermore, if there are economic incentives to manufacture and sell *unsafe* products, such as cheaper fabric, or the ability to source products from countries that do not collect data about components), regulating safety issues can protect manufacturers that avoid the use of unsafe fabrics from competition with those who do not. Accordingly, this type of regulation can facilitate better internalisation by some manufacturers of their investments in safety.[65]

The same could be true for consumer credit contracts. As was noted above, the legislative aims include helping consumers choose between different consumer credit products. Accordingly, if the regulatory aims included helping to ensure that consumers were protected from credit products that would have deleterious effects, consumers might have an enhanced ability to focus on other aspects of the product relevant to getting the best deal. This might also reduce free-riding on the efforts of scrupulous purveyors of credit products who *do* put resources into ensuring that consumer credit products are safer. Accordingly, focusing on consumer safety might be useful on its own terms. It might also contribute to policy analysis in the specific context of consumer credit products.

The kinds of issues that will be explored in more detail in later stages of the Regulatory Reform Project include the following:

1. First, the questions explored in this chapter might provide a basis for challenging some of the key baseline assumptions that exist in this area. Concerns about the deleterious effects of debt are sometimes deflected in the specific policy context of the regulation of consumer credit products. For example, in the 2000 discussion papers[66] that formed part of the policy background to the CCCFA in 2003, the Ministry of Consumer Affairs adverted to negative "externalities" associated with over-

51. Another participant reported: "[t]hey keep on talking you into putting your limit up, spending more money, so they get more money."

65 Oren Bar-Gill and Elizabeth Warren "Making Credit Safer" (2008) 157 U Penn L Rev 101 at 110.

66 See generally Ministry of Consumer Affairs *Consumer Credit Law Review: Part 1: Setting the Scene* (1999) at 22.

indebtedness, but did not develop the point much further. The Ministry concluded that "consumer credit legislation has only a limited role in preventing over-indebtedness",[67] and the statement was immediately followed by a discussion of other vehicles for protecting consumers against the deleterious effects of debt, such as financial literacy education.[68] Among the issues to be explored in later stages of the Law Foundation Regulatory Reform Project will be whether an emphasis on consumer safety might add usefully to the ideas and issues that inform the policy background. For example, if the consumer safety paradigm were given greater emphasis, it might be more difficult to deflect engagement with these kinds of externalities. To be sure, the same conclusion might be reached – that the CCCFA is not the best or the appropriate regulatory vehicle for addressing these concerns. Even so, an emphasis on consumer safety might require policy-makers to engage with more deliberative analysis of these issues before reaching this conclusion.

2. Secondly, an emphasis on consumer safety might invite greater concern with the risks associated with credit products in the hands of real-life consumers. Even if it is assumed that increasing consumer choice is a sensible regulatory aim, for a significant proportion of the New Zealand population choice is unlikely to be enhanced by merely providing more information. The information that is disclosed simply may be too complicated for many people to understand, and then to apply it when making decisions.[69]

3. Thirdly, a consumer safety approach might encourage greater attention to the reality that when consumers make decisions about purchasing credit products, deliberative risk analysis can be displaced by a range of different factors: stress, shame, brand loyalty, deference to experts or

---

67 Ministry of *Consumer Affairs Consumer Credit Law Review: Part 4: Over Indebtedness, Insurance and E-credit* (2000) at 6.

68 Ministry of *Consumer Affairs Consumer Credit Law Review: Part 4: Over Indebtedness, Insurance and E-credit* (2000) at 6–7. "[E]xtending and improving 'disclosure' requirements should help more consumers to understand their obligations when signing up for a consumer credit transaction. … Further options include: allowing contracts to be varied in cases of hardship, allowing transactions to be reopened in cases where lenders do not appropriately ascertain the ability of consumers to repay [and] requiring lenders to do a budgeting exercise with borrowers before extending credit."

69 The Ministry of Consumer Affairs has noted (as a conservative estimate) that 45 per cent of adult New Zealanders are functionally illiterate. Ministry of Consumer Affairs *Consumer Credit Law Review: Part 3: Transparency in Consumer Credit: Interest, Fees and Disclosure* (2000) at 13, citing Ministry of Education *Adult Literacy in New Zealand: Results from the International Adult Literacy Survey* (1997). Literacy issues are likely to be an extreme instance of a more general problem with understanding complex financial documents. The research noted that 500,000 New Zealand adults have nil or minimal reading capability, while an additional 750,000 cannot comprehend an everyday document. The Ministry of Consumer Affairs, in its report, commented that "the documents on which the survey was based are likely to be less complex than a typical credit contract", so these numbers would be even higher when evaluating understanding of credit contracts.

authority figures and so on. This is an issue to which the Families Commission has adverted in its work on family indebtedness,[70] but it has not been greatly focused upon in the context of the information disclosure approach.

4. Fourthly, it may be important to consider how the codification of soft law self-regulation fits within the regulatory scheme. Currently, this self-regulation is contained within the Code of Banking Practice.[71] The members of the New Zealand Bankers' Association have committed themselves to considering whether they believe that anyone seeking credit "will be able to meet the terms of the Credit Facility,"[72] and only providing credit when that consideration is answered in the affirmative. In the absence of such regulation, creditors may simply assess their own risk of not being repaid, rather than the risks undertaken by the purchasers of credit products.

Australia requires creditors to take these kinds of steps by incorporating them within the governing legislation, the National Consumer Credit Protection Act 2009.[73] Under that Act, creditors will assess a contract as unsuitable if it is likely that the purchasers of credit products can only satisfy their obligations by undergoing substantial hardship, or that the contract will not meet their requirements or objectives.[74] This goes beyond circumstances where the purchaser *cannot* meet the terms, to those where they *can* meet the terms whilst undergoing substantial hardship. This lowers the threshold for creditors to refuse credit. In the light of this, further consideration might be given to adopting in New Zealand law, protections similar to those in Australia. In turn, adoption of the Australian approach might also further related aims of the Regulatory Reform project: enhancing efficiency through adoption of consistent trans-Tasman regulatory approaches.

---

70 Jaimie Legge and Anne Heynes *Beyond Reasonable Debt: A background report on the indebtedness of New Zealand families* (RR 8/08 Family and Retirement Commission 2008) at 31-41.

71 New Zealand Bankers' Association "Code of Banking Practice" (2007) www.nzba.org.nz/banking-standards/code-of-banking-practice (last accessed 8 August 2011).

72 New Zealand Bankers' Association "Code of Banking Practice" (2007) www.nzba.org.nz/banking-standards/code-of-banking-practice (last accessed 8 August 2011) at [5.1.3]. There are other relevant obligations contained within the Code of Banking Practice. For example, the obligation to provide information to guarantors or providers of security about their obligations at [5.2].

73 National Consumer Credit Protection Act 2009 (Cth).

74 National Consumer Credit Protection Act 2009 (Cth), s 118(2). The Act is discussed in *Bartle v GE Custodians* [2010] NZCA 174, [2010] 3 NZLR 601 at [212].

11.5 Conclusion

In sum, if policy-makers were to take safety concerns seriously, there is a possibility that some of the baseline assumptions in this area of regulation would shift. Presently, the key assumption behind the CCCFA seems to be that consumers are rational welfare maximisers whose marketplace choices should be facilitated by improving the information they receive before purchasing consumer credit products. Introducing a consumer safety paradigm to this debate might challenge this assumption in a number of different ways. As is noted above, New Zealand policy makers might well reach the same conclusions as to the optimal regulatory regime for the New Zealand consumer credit product market. It is to be hoped, however, that the quality of policy analysis might be enhanced by greater awareness of the kinds of baseline assumptions that dominate in this area.