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Section 22 p1, p2

SUMMARY OF MAIN CHANGES TO REFORMS IN RELATION TO SMALL AMOUNT CREDIT CONTRACTS

Small amount credit contracts are referred to as 'SACCs' below

	ISSUE	*COMMENTS*
1.	Setting cap for SACCs at 20/4 level	20/4 cap to apply – increase from 10/2 cap originally announced by the Government as it allows for a viable industry.
2.	Shortening term for SACCs from 24 months to 12 months	Shorten term for SACCs from 24 months to 12 months, as the 4% monthly fee allows for too high a return after 12 months. No change to definition in relation to amount (cap applies to loans of $2000 or less). Secured contracts to be included in definition of SACC

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6.	200% total cap on charges for all lending	This protection is to be retained as it is supported by both lenders and consumer groups.

Section 22

ENHANCEMENTS BILL –UPDATE AND RESPONSES TO STAKEHOLDER ISSUES

IN RELATION TO SMALL AMOUNT CREDIT CONTRACTS AND THE CAPS ON COSTS

	ISSUE	*PROPOSAL*	*COMMENTS*
1.	Setting cap for SACCs at 20/4 level	20/4 cap to apply – so no changes proposed.	Government is committed to retaining the cap at this level.
2.	Shortening term for SACCs from 24 months to 12 months	Redefine SACCs to loans up to 12 months No change to amount (up to $2000) Secured contracts to be included in definition of SACC	The maximum term for SACCs is reduced from 24 months to 12 months, as the 4% monthly fee allows for too high a return after 12 months. This also resolves issues related to the 200% maximum repayment cap as longer loans may exceed 200% but remain under the cap on costs.

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Effect of refinancing on the 200% cap

The following example illustrates the effect of the 200% cap

The consumer borrows $500 over 4 months, having to pay charges of $180. After 1 month the consumer refinances their debt ($620). The refinance could be over 4 months or 12 months.

The position, in the absence of any statutory changes, can be summarised as follows:

	Adjusted credit amount	200% cap	Establishment and monthly charges	Maximum default charges (no changes)	Maximum default charges (if refinanced amount not included in calculation of 200% cap)
First Loan	$500	$1000	$180	$320 ($1000 minus $680)	N/A
Refinance A: $620 over 12 months	$620	$1240	$431	$189 ($1240 minus $1051)	Negative $51 ($1000 minus $1051)
Refinance B: $620 over 4 months	$620	$1240	$243	$357 ($1240 minus $863)	$157 ($1000 minus $863)

Changing the effect of the 200% cap so that it includes the refinanced amount can lead to anomolous results, where the cap would be lower than the total of the amount of credit and the permitted fees and charges.

Concerns as to how the 20/4 cap operates in practice

Some lenders have raised concerns as to how the 20/4 cap operates in practice, as both the 20% upfront fee and the 4% monthly fee are calculated on the adjusted credit amount, which excludes the establishment fee. It is argued that this does not allow credit providers a return on their establishment costs.

The 20/4 model is based on fees rather than interest, so that the comparison with a credit contract, in which interest can be charged on establishment fees is not relevant. For example, the use of fees means that the consumer does not get any benefit from making repayments early. While the 4% fee is calculated on a sum that does not include the establishment costs, it still provides a return that is intended to cover those costs in dollar terms, and is higher than the 48% interest rate would allow.