

THE CREDIT CONTRACTS AND CONSUMER FINANCE ACT

CONSUMER RIGHTS UNDER A CONSUMER CREDIT CONTRACT – PREPAYMENT

Under the Credit Contracts and Consumer Finance Act (CCCF Act), a creditor must accept any extra payments a debtor makes under a consumer credit contract unless the contract specifically allows the creditor to decline them.

If the contract allows a creditor to decline an extra payment and one is received, the creditor can:

- accept it and credit it to the debtor's account as soon as practicable; or
- decline it and return it to the debtor as soon as practicable; or
- credit it according to the payment schedule specified in the contract.

PART PREPAYMENT

A creditor may charge a reasonable fee for part prepayment if the consumer credit contract allows it and the fee is properly disclosed.

A fee will be unreasonable only if it exceeds a reasonable estimate of a creditor's loss arising as a result of the prepayment. The fee may include the creditor's average reasonable administration costs arising from part prepayments under similar types of contract.

If any fee is payable upon part prepayment, the fee must be disclosed at the time the contract is entered and if the amount is not able to be ascertained then the method of calculating the fee must be set out.

FULL PREPAYMENT

A debtor is entitled to repay in full what they owe under a consumer credit contract at any time. A consumer credit contract must not prohibit full prepayment. A contract which does prohibit full prepayment will breach the CCCF Act and may also breach the Fair Trading Act.

A creditor cannot require a debtor who is prepaying in full to pay more than:

- the unpaid balance at the time of prepayment; this includes the interest and charges that would ordinarily accrue or be payable under the contract as at the date of prepayment; and
- if the contract expressly authorises it, an extra charge to cover administrative costs incurred as a result of the prepayment; and
- if the contract expressly authorises it, a creditor may be able to charge a fee that does not exceed a reasonable estimate of their loss.

Where consumer credit insurance is financed as part of the agreement this must be rebated and deducted from the amount to be paid. The CCCF Act sets out rules for calculating this rebate.

CALCULATING LOSS ON FULL PREPAYMENT

The CCCF Act's regulations set out a 'safe harbour' formula which if used correctly is presumed to give a reasonable estimate of a creditor's loss upon full prepayment. A creditor may use other methods to work out their loss, but will need to be able to show that their method also produces a reasonable estimate of loss. The contract must clearly set out the procedure the creditor intends to use in the initial disclosure statement.

The safe harbour formula is designed to produce the difference in two future payment streams. One is the cashflow anticipated under the contract being repaid. The other is the cashflow based on a replacement contract at the interest rate prevailing at the time of the prepayment for the remainder of the fixed term of the original contract. The two payment streams are adjusted to a present value before the difference is calculated. The concept of assessing loss using the safe harbour formula is that the creditor mitigates its loss by relending the repaid funds.

However, the CCCF Act recognises that this is not the only means of assessing loss and creditors may use other appropriate procedures.

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REBATE OF INSURANCE PREMIUMS

If a consumer credit insurance contract is financed under a consumer credit contract the debtor must be provided with a proportional rebate on the premium if and when they fully prepay the contract. The CCCF Act sets out a formula, based on the Rule of 78, that **must** be used to calculate the rebate. This formula gives the minimum rebate to be credited to the debtor.

EXAMPLE

A finance company failed to correctly rebate credit-related insurance to customers who had paid back their loans early because of a computer software programme that was calculating rebates inaccurately. In a settlement with the Commerce Commission, the company acknowledged a breach of the CCCF Act and agreed to refund affected customers.

The safe harbour formula and the formula for calculating a rebate are available at www.legislation.co.nz under Credit Contracts and Consumer Finance Act Regulations.

DEFINITIONS

PART PREPAYMENT An extra payment towards a loan that is not required under the credit contract.

FULL PREPAYMENT An extra payment towards a loan that pays it off in full before the due date specified in the credit contract.

LENDERS AND BORROWERS

The CCCF Act uses a number of different terms to describe lenders and borrowers, depending on the nature of the transaction.

- Consumer credit contracts – creditors and debtors.
- Consumer leases – lessors and lessees.
- Buy back transactions – transferees and occupiers.

For the purposes of these fact sheets the terms creditor and debtor are used when referring generally to credit transactions, but the specific terms are used where relevant.

To check for updates to this fact sheet visit:
www.comcom.govt.nz/consumer-credit

This fact sheet is part of a series looking at the Credit Contracts and Consumer Finance Act. Other fact sheets can be downloaded from
www.comcom.govt.nz/consumer-credit

CONTACT

Contact the Commerce Commission with information about possible breaches of the Credit Contracts and Consumer Finance Act.

TELEPHONE

Our Contact Centre during office hours on 0800 943 600

WRITE

To us at Contact Centre,
PO Box 2351, Wellington 6140

EMAIL

Us at contact@comcom.govt.nz

This fact sheet is a guideline only, and reflects the Commission's view. The publication is not intended to be definitive, and should not be used instead of legal advice. It is traders' responsibility to remain up to date with legislation.

Only the courts can make an authoritative ruling on breaches of the Credit Contracts and Consumer Finance Act.