CHiLD POVERTY ACTION GROUP

Credit and Debt for Low-Income and Vulnerable Consumers

M. Claire Dale

Child Poverty Action Group (Inc)

Backgrounder 01/08

January 2008

Child Poverty Action Group (Inc) is a non-profit group, formed in 1994 and made up of academics, activists, practitioners and supporters. CPAG advocates for more informed social policy to support children in Aotearoa New Zealand, specifically those children who currently live in relative poverty. CPAG believes our high rate of child poverty is not the result of economic necessity but is due to policy neglect. Through research and advocacy, CPAG highlights the position of tens of thousands of New Zealand children, and promotes public policies that address the underlying causes of the poverty they live in. If you are not already supporting CPAG and you would like to make a donation **to assist with ongoing work, please contact us at the address below or through our website:** www.cpag.org.nz

This is part of Child Poverty Action Group's series of background papers.

Child Poverty Action Group Inc.
P. O. Box 56 150
Dominion Road, Auckland.

www.cpag.org.nz

Child Poverty Action Group monographs and technical papers

Child Poverty Action Group also publishes an on-going series of monographs and technical papers about government policies and their impact on children:

Our Children: The Priority for Policy	**(2001, 2003)**
Room for Improvement: Current New Zealand housing policies and their implications for our children	**(2003)**
Cut Price Kids: Does the 2004 "Working for Families" budget work for children?	**(2004)**
Workfare: Not Fair for Kids?	**(2005)**
Hard to Swallow: Foodbank use in New Zealand	**(2005)**

These are available from www.cpag.org.nz/resources/publications/.

Table of Contents

Table of Tables

Introduction

The Backgrounder focuses on the issues of credit and debt for low-income and vulnerable consumers and their children, and concludes with recommendations. It draws on the CPAG Submission on the Review of Financial Products and Providers, and the presentations by CPAG and other contributors at the Ministry of Consumer Affairs Financial Summit, 23rd November, 2007. At the Summit, representatives of the financial sector (banks, credit unions, finance companies, Retirement Commission, Banking Ombudsman etc, and community and voluntary agencies working with people with problem debt and difficulties accessing affordable credit) discussed affordable credit options and ways of getting information and advice to consumers.

Most low-income, vulnerable consumers are parents with children

The suffering of families in severe hardship has been graphically described by representatives from Budget Services, Citizens' Advice Bureau, and the Auckland City Mission. It has been well documented in the Ministry of Consumer Affairs (Ministry of Consumer Affairs, 2007) and in the Ministry of Social Development's annual *Social Reports*.

When families suffer hardship, children suffer most, as shown in Child Poverty Action Group publications (Child Poverty Action Group, 2003), and in a report published in 2007 by the new Zealand Paediatric Society (Craig, Jackson, Y., & NZCYES Steering Committee, 2007). Ministry of Social Development research shows that 43 per cent of children in sole-parent families and 15 per cent of children in two-parent families live below the poverty line (Ministry of Social Development, 2006b). The proportion of children in severe or significant hardship rose from 18 per cent to 26 per cent between 2000 and 2004 (Ministry of Social Development, 2006a). Before Rogernomics and Ruthanasia, the core benefit for a sole parent with two children was 92 per cent of the average wage. By 1999, it was 62 per cent. In 2007, it is 58 per cent. The government’s much-hyped attempt to deal with family poverty, the Working for Families package, doesn't apply in full to beneficiaries and their children, many of whom have gained very little from the package and been left further behind.

Today approximately one child in every four is experiencing the effects of inadequate income. CPAG attributes this deterioration, and its consequent and ongoing social costs, to three main factors. The primary cause of the deterioration in the economic position of children is a tax regime that, over time, has shifted the tax burden to the poor while the real value of child benefits and tax credits was allowed to erode. The second set of factors include changes in demography and the labour market, and a philosophical shift that embraces privatisation of the costs of public goods such as education. A third cause is the lack of adequate consumer protection in the financial sector.

"Affordable" credit

Essential consumer services: housing, water, power, telecommunications, insurance and banking, need to be affordable. Some families *don't* have insurance, and *do* borrow money for everyday expenses, because they do not have sufficient household income. Adding to the risky environment of the daily lives of low-income and vulnerable families, the established banks and insurance companies are notably absent. For example, a UMR "public awareness" survey in 2007 found nearly a third (29%) of all respondents was not insured. Other research shows that so few Pasifika people are insured that the insurance industry does not separate out their statistics. The current "credit" environment, particularly for Pasifika people, is reminiscent of our fairly recent history when women weren't "preferred customers" for the banks, and couldn't get a mortgage unless a man guaranteed it. It is a sorry state of affairs when the "preferred customers" of the high street banks pay around 10% interest, and many low-income, vulnerable people, turned away by the banks, have their 30% interest finance company loans guaranteed by WINZ.

Table 1: Annual Family Income From All Sources by Family Type

Family income(1)	Couple without children (%)	Couple with child(ren) (%)	One parent with child(ren) (%)
$20,000 or less	7.1	3.3	31.0
$20,001–$30,000	16.0	4.6	24.2
$30,001–$50,000	20.1	16.4	24.4
$50,001–$70,000	18.8	21.3	11.0
$70,001–$100,000	18.4	23.5	5.8
$100,001 or more	19.5	30.9	3.5
Total	100.0	100.0	100.0

(1) The income bands in this table are not all the same size.
Note: Family types 'couple with child(ren)' and 'one parent with child(ren)' could include adult child(ren) contributing to the total family income.
Source: NZ Government Department of Statistics, 2006 Census, http://www.stats.govt.nz/census/census-outputs/default.htm

Ability to pay for high-cost credit is determined by income, and incomes, compared with the OECD average, are low. As Table 1 shows, in 2006, median annual family income from all sources was $75,600 for a couple with child(ren); $57,200 for a couple without children, and $27,400 for one parent with child(ren). The Minimum Family Tax Credit provides a guaranteed minimum family income to around 2,400 families who are in work.

Recipients are currently guaranteed a net income of $18,044 a year, rising to $18,460 from 1 April 2008 (Twist & Matthews, 2007). Conservative estimated annual costs for a family for rent of $16,640 pa (3 bedroom house in Manurewa), and services at approximately another $3,400 (water @ $400; power @ $2,160; telecommunications @ $800) takes $20,000 out of after-tax income before any spending on food, clothing or medical treatment for themselves and their children. The increasing prevalence of user charges for essential services, from water to education, adds to the financial burden of low-income families.

Access to "unaffordable" credit is always within easy reach. Instead of the main banks' interest charge of about 10%, stores such as The Warehouse offer their own credit lines at 15 to 20% per annum, and the major credit cards charge around 20 to 27% per annum. Taking their effective interest charges above 30% per annum, the large and small finance companies use add-ons such as large administration fees covering establishment, security inspection, documentation, and loan shortfall insurance policy, etc (Ministry of Consumer Affairs, 2007). For shorter-term loans, rates can be 20 to 25 per cent per *month*. One case is documented where charges of 10 per cent every seven days applied - 520 per cent on an annual basis (Collins, cited in St John & Wynd, 2008, forthcoming).

With the worst finance companies, vital information such as the full repayment cost is left off the contracts. Some unscrupulous companies insist that the borrower sign multiple Direct Debits. Then if the borrower cancels the payment for any reason, including full repayment, the lender can simply deposit another form with the bank. Clothing vans circulate in low-income neighbourhoods, and loan companies have also become mobile: door-to-door loan-sharking. Finance companies advertise relentlessly in the media, and locate themselves densely in the poorest neighbourhoods. There is a direct relationship between low incomes and the proliferation of high-cost lenders and pawn shops. Economic recovery in a community can be measured by a reduction in the number of loan sharks; they leave when the community has better options. In South Auckland, the loan sharks still outnumber the main banks.

The miracle is that the vast majority of these cruel loans are repaid. This indicates that the high risk that is assigned to low-income people by high street banks is not, in fact, justified. However affordability is defined, Aotearoa New Zealand prides itself on its high ranking in international tables as a good, safe place to do business. The same level of protections and benefits needs to be extended to our most vulnerable consumers and their children.

Recommendations

- Fast-track the legislation to register, regulate and monitor the financial products and providers sector. Make membership of and jurisdiction by industry disputes resolution schemes compulsory in the sector. This will assist in assuring consumer rights. Legitimate providers of financial products will also benefit from regulation of the sector.
- Extend the current legal definition of consumer to cover financial products. Include the full cost of credit in any credit contract.
- Extend the "financial literacy" public education campaign to inform consumers of the legal and regulatory changes in the financial sector, and of their existing rights and access to dispute resolution and redress.
- Spread this information using all available outlets, including Retirement Commission's financial literacy campaign, all relevant government websites, MCA's own publications, those of the banks and insurance companies, and the media, as well as budget advisory services and community organisations, community radio and even school newsletters.
- The successful contribution of microfinance schemes to relief of hardship is well known, for example, the Grameen Bank just won the 2007 Nobel Peace Prize. Less well known is the Maori Womens' Welfare League micro-financing scheme, run successfully for 17 years. CPAG recommends KiwiBank adopt such a model for vulnerable consumers with children: a microfinance instrument that makes small short term loans available at close to the rate paid by banks' preferred customers. The amount a particular consumer is able to borrow could increase as their successful repayment history builds.
- WINZ could guarantee these KiwiBank loans, while refusing to guarantee loans provided under contracts from loan sharks with exorbitant interest rates.

References

Child Poverty Action Group. (2003). *Our Childen: The priority for policy* (2nd ed.). Auckland: Child Poverty Action Group.

Craig, E., Jackson, C., Y., H. D., & NZCYES Steering Committee. (2007). *Monitoring the health of New Zealand children and young people: Indicator handbook*. Auckland: Paediatric Society of New Zealand, New Zealand Child and Youth Epidemiology Service.

Ministry of Consumer Affairs. (2007). *Pacific consumers' behaviour and experience in credit markets, with particular reference to the 'fringe lending' market: Research findings report and government's response strategy*. Wellington: Ministry of Consumer Affairs.

Ministry of Social Development. (2006a). *New Zealand living standards 2004*. Wellington: Ministry of Social Development.

Ministry of Social Development. (2006b). *The Social Report*. Wellington: Ministry of Social Development.

St John, S., & Wynd, D. (2008, forthcoming). *Left behind: How social and income inequalities damage New Zealand children*. Auckland: Child Poverty Action Group.

Twist, P., & Matthews, C. (2007). Rural Bulletin. December 2007, Rural Women New Zealand, www.ruralwomen.org.

Child Poverty Action Group Backgrounder Series

These backgrounders can be downloaded free of charge from:

http://www.cpag.org.nz/resources/backgrounders/

Backgrounder 01/2006: Committed to Fairness and Opportunity? The impact of the In Work Payment on Maori and Pasifika families. April 2006.

Rather than reversing existing disadvantage, the burden of discrimination built in to the new In Work Payment (IWP) will fall particularly hard on Maori and Pasifika families.

Backgrounder 25: CPAG alleges Child Tax Credit discriminatory. 28 November 2005.
A summary of CPAG's case to date, to the Human Rights Review Tribunal.

Backgrounder 24: Tax cuts don't make sense. 30 October 2003.
A critique of National's proposed tax cuts.

Backgrounder 23: Aussies win, hands down. 30 September 2003.
Asks why New Zealanders cannot see the importance of adequate tax-based and universal child benefits.

Backgrounder 22: Where is the commitment to eradicating child poverty? 30 April 2003.
A comment on the Child Tax Credit.

Backgrounder 21: Accommodation supplement. 30 June 2002.
Providing children with decent affordable accommodation is the most important step that can be taken to imporve the well-being and prospects of these children.

Backgrounder 20: Poverty primary care and child and youth health. 30 April 2002.
Child Poverty Action Group has become increasingly concerned by the evidence of deteriorating child health in Auckland and other parts of the country. This backgrounder has been put together by members Assoc. Professor Innes Asher, Head of Starship Children's Hospital Respiratory Service, Dee Parks, health manager and researcher, and Dr Carolyn Dakin, Paediatric Respiratory Specialist.

Backgrounder 19: Social hazards. 30 November 2001.
Reduce the prevalence of these social hazards requires appropriate legislation and education, combined with government policies which reduce poverty and its effects.

Backgrounder 18: Family financial assistance 1986 - 2001. 30 July 2001.
This discussion document analyses the effect on families of the failure to adequately adjust income support for inflation, and the effect of increased targeting of the payment.

Backgrounder 17: Who pays if you don't? 30 March 2000.
This backgrounder is a follow up to the complaints made by CPAG in 1998, regarding the factual

accuracy of advertisements depicting a boy who apparently missed out on soccer because of the non-payment by his father of child support, which were never resolved satisfactorily.

Backgrounder: Briefing paper to the incoming government – 1999. 30 December 1999.
A briefing paper to the Labour Government on issues relating to child poverty.

Backgrounder 16: Poverty and child health. 30 September 1999.
A backgrounder on the deteriorating health of our children.

Backgrounder 15: The student loans scheme. 30 August 1999.
A criticism of the current policies for the support of students.

Backgrounder: Schools, Telecom and distributional equity. 30 June 1999.
A study to determine any association between the socio-economic status of schools and the amount of donations they received from the Telecom New Zealand Ltd School Connection programme.

Backgrounder 14: Work and Income 1999. 30 June 1999.
This paper documents the experiences of some beneficiaries with WINZ and Income Support.

Backgrounder 13: The IRD Child Support infomercial 1998. 30 November 1998.
A backgrounder outlining the concerns of children's advocacy groups about the IRD's controversial TV campaign on child support.

Backgrounder 12: Housing update 1998. 30 August 1998.
This backgrounder shows why housing costs are the greatest single cause of poverty in Aotearoa/New Zealand. Lack of access to adequate, affordable and stable housing diminishes opportunities, health and well-being of families and children.

Backgrounder 11: Submission of the Social Security Bill Amendment No 6. 30 July 1998.
CPAG's representation to the select committee expressing objections and concerns relating to Social Security Amendment Bill 6.

Backgrounder 10: The code of social and family responsibility. 30 May 1998.
This backgrounder asks why are only parents and families selected by the government to be the focus of the questionnaire without reference to the other groups which also contribute to the lives and well-being of children?

Backgrounder 9: New Zealand and financial support for children. 30 March 1998.
CPAG's response to a dramatic change in the direction of family policy in the UK.

Backgrounder 8: The white paper and New Zealand. 30 July 1997.
CPAG's concerns about the impact of the proposed compulsory savings scheme on low income families.

Backgrounder 7: The state of our children's health. 30 June 1997.
A review of negative child health outcomes which result from poverty in New Zealand today.

Backgrounder 6: Policies for housing low-income families. 30 April 1997.
Many families with children face serious housing problems. These problems relate to the 1993 decision to deliver all housing assistance through a single cash-based Accommodation Supplement.

Backgrounder 5: The coalition agreement and New Zealand children. 30 April 1997.
On 11th December 1997 the New Zealand First Political Party and the New Zealand National Party agreed to the formation of a coalition government. Among the matters which were negotiated as part of the agreement were several that impinge on the well-being of children. However many of the policy initiatives are vaguely expressed and all funding proposals are subject to `being considered' within the agreed spending limits.

Backgrounder 4: Election 1996 – An analysis of party policies as they affect children. 30 October 1996.
Dr. Dorothy Howie's analysis of the policies of the political parties drawing on the principles spelled out within the U.N. Convention on the Rights of the Child, to which New Zealand is a signatory.

Backgrounder 3: Targeting and housing for low-income families. 30 September 1996.
Housing is fundamental to the well being of children. Unless children have stable, warm dry shelter, improving other aspects of income support for families will simply tinker around the edges.This backgrounder outlines the nature of the housing crisis.

Backgrounder 2: Targeting and the Community Services Card. 30 July 1996.
Child Poverty Action is very concerned about the current operation of the Community Services Card (CSC) and the impact on child health.

Backgrounder 1: Targeting and the Independent Family Tax Credit. 30 May 1996.
This backgrounder questions why child poverty is so endemic during an economic recovery, and suggests it is more than time to question the direction of social policy.