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INSURANCE & FINANCIAL SERVICES OMBUDSMAN

Financial Markets Policy
Building, Resources and Markets
Ministry of Business, Innovation & Employment
PO Box 1473
WELLINGTON 6140

By email to: consumer@mbie.govt.nz

Insurance & Financial Services Ombudsman Scheme ("IFSO Scheme") Submission on Exposure draft of the Credit Contracts and Consumer Finance Amendment Regulations 2020 ("the exposure draft")

Thank you for the opportunity to make a submission on the exposure draft.

The IFSO Scheme supports the proposals in the exposure draft in principle. We have provided comments only where we have something specific to add to the discussion. Our specific comments are, as follows:

Paragraph 19:
We agree with the proposal to shift existing guidance in the Responsible Lending Code ("RLC") into regulations.

Paragraph 20:
The use of the word "*requires*" in this context is confusing. It is not clear if the lender must determine if the borrower "*needs*" the credit or whether it is an objective or subjective assessment.

Paragraph 21:
We agree borrowers should be specifically given the option of paying for additional features outside of the credit contract.

Paragraph 23
We agree there needs to be more rigour around "*additional features*" being added to credit contracts. In some complaints we have considered there appears to have been little consultation about insurance-type cover being added to the credit contract costs and some borrowers did not realise it was included in their credit contract.

We do not believe it is practical to require lenders to make enquiries about the borrower's circumstances and the other cover they have. That would require the lender to assess the entitlements a borrower had under their current insurance policies and

compare them with the cover the lender could provide and to determine how the cover the lender could provide might apply to each borrower. That is something financial advisers might be able to do but is not something lenders that are not also financial advisers would have the requisite skills to do.

There are often different "*levels*" of cover provided in insurance-type cover added to credit contracts. In complaints we have seen, borrowers have not known there were different levels, what level they had or why that level was chosen. We would like to see a requirement that the process for choosing and adding additional features to credit contracts be required to be documented, including a record of the discussion with the borrower about the options available, the choice they made and why they made that choice.

We understand lenders receive substantial commission for the addition of insurance-type cover to credit contracts. We believe they should be required to disclose that commission to borrowers.

Paragraph 26:
This guidance and further detail would be very useful.

Paragraph 30:
We agree that a degree of prescription is required. Some lenders we deal with have not understood or applied the RLC requirements with any degree of rigour.

Paragraph 34:
In our experience, it is in respect of enquiries made about a borrower's ability to "*afford*" credit that lenders are currently not meeting the RLC guidance. For that reason, we agree that these obligations need to be prescribed.

Paragraph 35:
While we agree applying this process to guarantors may seem disproportionate, the reason for having a guarantor for credit is to pay if the borrower defaults. We have seen situations where grand-parents or parents are guarantors where, clearly, they would not be able to afford the credit if they were applying for it themselves.

We believe requirements to satisfy section 9C(4)(a) should apply in the situation where the guarantor is a close family member or would be classed as a vulnerable person if they were applying for the credit themselves.

Paragraph 36:
The addition of insurance-type products can add thousands of dollars to a credit contract. For that reason, we believe it should be taken into account in the affordability assessment.

Paragraph 40:
It would be useful to have what constitutes a "*reasonable surplus*" to be specified, for example, by way of a percentage etc.

Paragraphs 43 – 63:
We agree with the process for assessing affordability proposed.

We agree with the proposal that lenders check the information provided by comparing the borrower's estimate of expenses against a reasonable level of expenses.

We agree with the test proposed in paragraph 59, although the threshold for what constitutes a high-cost loan is unrealistically high.

Annual returns:
In addition to the information listed, we suggest lenders also be required to report on loans in default relative to their total loans in existence. That will give an indication of whether the lender has systemic issues in respect of assessing borrowers' abilities to repay loans.

We also suggest lenders be required to report on a measure that indicates the length of time over which loans have been in default. That is because we are seeing loans that are being allowed to run with multiple defaults over relatively long periods of time (often years). In some cases, it appears lenders are not taking recovery action because the accumulation of default interest and additional fees results in the borrower repaying far more than the value of the loan.

We trust our comments are of assistance and encourage you to contact us if any clarification of the submission is required.

Yours sincerely

Karen Stevens
Insurance & Financial Services Ombudsman