



COVERSHEET

Minister	Hon Dr David Clark	Portfolio	Commerce and Consumer Affairs
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List of documents that have been proactively released

Date	Title	Author
February 2022	Investigation into the impacts of recent Credit Contracts and Consumer Finance Act 2003 changes: Initial findings and proposals	Office of the Minister of Commerce and Consumer Affairs
21 February 2022	Investigation into the impacts of recent Credit Contracts and Consumer Finance Act 2003 changes: Initial findings and proposals CBC-22-MIN-0012	Cabinet Office

Information redacted

YES / NO [select one]

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Some information has been withheld for the reason of Confidential advice to Government.

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Office of the Minister of Commerce and Consumer Affairs

Cabinet Business Committee

Investigation into the impacts of recent Credit Contracts and Consumer Finance Act 2003 changes: Initial findings and proposals

Proposal

1 This paper provides the initial findings from the investigation into the impacts of recent changes under the Credit Contracts and Consumer Finance Act 2003 that came into force on 1 December 2021. It presents initial proposals to address some of the specific issues identified to date and sets out further work to be progressed as part of the investigation.

Relation to government priorities

2 The proposals in this paper seek to ensure that New Zealanders can access credit safely and responsibly and support the Government’s priority to improve access to the housing market for first home buyers.

Executive Summary

3 In January 2022, I initiated an investigation into the impacts of recent legislative and regulatory changes under the Credit Contracts and Consumer Finance Act 2003 (the CCCFA) that come into effect on 1 December 2021. The Terms of Reference (TOR) for this investigation were published on 31 January.

4 These recent changes were intended to address irresponsible lending practices and prevent problem debt in the form of unaffordable loan repayments by placing clearer affordability and suitability assessment requirements and a stronger penalties regime on all lenders. These changes were made following a review of the CCCFA conducted in 2018 [DEV-18-MIN-0204; CBC-20-MIN-0076]. I want to preserve this intent.

5 As part of the investigation, officials are meeting with key stakeholders and gathering relevant data. Officials also need to consider other factors, such as recent changes to interest rates and loan to value ratio (LVR) restrictions, to distinguish the impact the CCCFA may be having as compared to other factors in the lending environment.

6 Officials have advised me that the initial findings from the investigation suggest that, while there is an early indication that the new affordability and suitability assessment requirements and penalties are having some of the impacts intended, a number of potential unintended consequences are emerging. These include:

6.1 less targeted than expected reductions in access to credit

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- 6.2 slower processing times, and
 - 6.3 borrowers being subjected to inquiries that could be considered unduly intrusive.
- 7 A key concern raised by lenders relates to the fact that the same affordability assessment requirements apply to all lending types and all consumers, with limited lender discretion and narrow exceptions. Another key concern identified by some lenders is the new penalties regime, which some lenders claim is leading them to take a conservative approach to any uncertainty in the regime. These concerns require further consideration as part of the wider investigation.
- 8 A range of more specific issues have also been identified. While final advice from the investigation is not due until April, in this paper I recommend a set of initial proposals to make changes to the Credit Contracts and Consumer Finance Regulations 2004 (the **Regulations**) and the Responsible Lending Code (the **Code**) to address some of the specific issues relating to:
- 8.1 estimation of likely borrower expenses after the credit is provided
 - 8.2 surpluses, adjustments, and buffers used to address uncertainty about borrower income and expenses, and
 - 8.3 exceptions to the requirement to perform a full assessment of income and expenses.
- 9 I intend for these initial proposals to be in place by early June, following the public consultation on the Code as required by the CCCFA and proposed consultation on the Regulations.
- 10 The investigation is ongoing, and officials are still engaging with key stakeholders and gathering relevant data. However, I am proposing some immediate changes to the Regulations and the Code that represent a ‘no regrets’ approach and which have the potential to benefit consumers who have been unduly targeted by the CCCFA changes. These proposals do not depart from the original policy intent and are clearly in line with the purposes of the CCCFA.
- 11 There may be a risk that progressing with these initial proposals could be seen as inconsistent with the process set out in the TOR, and that not enough consideration has been given to any potential unintended consequences of these initial steps.
- 12 Financial mentors and some consumer advocates may view these tweaks unfavourably. Lenders and some consumers may indicate that these changes do not go far enough in addressing their concerns. Lenders may also be reluctant to implement these initial proposals ahead of the investigation being concluded.
- 13 I consider that these risks can be mitigated by:
- 13.1 clearly describing the recommendations made in this paper as the ‘initial proposals’ that align clearly with the original intent of CCCFA, and subject to targeted consultation with lenders, financial mentors and consumer advocates as part of the drafting of drafting instructions for the Regulations

and amendments to the Code , and further public consultation on the Code and an exposure draft of the Regulations;

- 13.2 making it clear that the impacts of the CCCFA changes and any further changes to the Regulations and the Code will be considered further as part of the remainder of the investigation to be concluded in April.
- 14 I believe making some ‘no regrets’ changes now, in line with the intent of the Act and in advance of the investigation’s conclusion, allows us to respond expeditiously to the concerns raised by consumers and lenders to ensure we are not unduly restricting access to credit for New Zealanders, including first home buyers, in the near term.

Background

On 1 December 2021, new affordability and suitability requirements and penalties for lenders under the CCCFA came into force

- 15 The Credit Contracts Legislation Amendment Act 2019 (the **Amendment Act**) was intended to address irresponsible lending practices and prevent problem debt in the form of unaffordable loan repayments, particularly in relation to people and whānau in vulnerable circumstances.
- 16 This followed a review of the CCCFA conducted by the Ministry of Business, Innovation and Employment (**MBIE**) in 2018. This review was based on feedback from a range of consumer advocates as well as MBIE’s discussions with lenders and other parties about lender processes.
- 17 While officials have relatively little information about the prevalence of problems across particular types of lenders, consumer stakeholders have identified irresponsible lending across all types of lenders. Consumer stakeholder examples and Commerce Commission complaints data suggested problems are particularly concentrated across finance companies and high-cost lenders. Credit card lending by banks has also been cited as a source of issues.
- 18 A 2020 survey (with a standard sample size of 1,000) found that in 2019, around 18% of consumer borrowers reported that repayment difficulties were having a moderate to severe impact on their lives.
- 19 A number of changes were made to the CCCFA and associated Regulations to address issues with non-compliance, unreasonable fees, high cost of borrowing and harm from debt collection and mobile traders. [DEV-18-MIN-0204; CBC-20-MIN-0076] (A visual summary of the CCCFA reforms is provided in **Annex One**).
- 20 Some of the changes related specifically to high-cost credit¹ (e.g. caps on interest rates and cost of credit and new restrictions on repeat lending). However, most were intended to cover all consumer lenders and all forms of consumer loans, including car finance, personal finance, and mortgages.

¹ Broadly, credit where the annual interest rate is 50 per cent or higher.

21 On 1 December 2021, the parts of the Amendment Act and Regulations that provide specifically for new more prescriptive affordability and suitability requirements and duties on directors and senior managers of lenders came into effect. This was an extension from the original implementation date of 1 October 2021.

In light of concerns raised by lenders and consumers, in January 2022 I brought forward an investigation into the impacts of these changes

22 Since these changes came into effect on 1 December 2021, there have been consumer anecdotes in the media and concerns raised by lender and financial adviser organisations about the impacts of these recent changes.

23 On 14 January 2022, I asked MBIE, in collaboration with the Council of Financial Regulators (CoFR), to bring forward an investigation into the impacts of these affordability and suitability changes. The TOR (enclosed at Annex Two) were published on 31 January and provides for initial findings in mid-February and final advice in April.

24 As part of the investigation, MBIE is conducting a series of stakeholder engagements expected to conclude in February (an overview is provided in **Annex Three**) and working in collaboration with CoFR agencies to gather relevant data.

25 I met with the five main banks on 3 February, with Financial Advice New Zealand on 9 February, and had a conversation with FinCap on 16 February.

26 I also provided an update to Cabinet as an oral item on 8 February.

Initial findings

27 The TOR requires MBIE, in collaboration with CoFR agencies, to investigate the intended or unintended impacts, beyond those expected by the initial implementation, of the parts of the changes relating to affordability and suitability assessments. The focus is primarily in relation to mortgage, but also other lending by banks and non-bank lenders in the current consumer credit market. This includes attempting to separate out the impacts of other factors like global economic conditions, LVRs, and the official cash rate (OCR).

28 My officials' initial findings based on engagements with stakeholders and data available to date are set out below. Officials will continue to engage with stakeholders and gather and analyse available data to inform the final advice due in April.

Official statistical data and independent credit reporting data available to date indicates that there has been a drop in all types of lending since 1 December 2021

29 Reserve Bank mortgage lending data for December 2021 published on 31 January 2022 showed a drop in new mortgage commitments from \$9.1 billion in November to \$7.9 billion in December. The Reserve Bank 'steady state' forecast range for December, taking an expected seasonal fall and market trends into account, was \$8.3 - \$8.6 billion, so the outcome was lower than expected. It should be noted that \$7.9 billion was still higher than lending in December 2017, 2018, and 2019.

- 30 Data from independent credit reporting agency Centrix (enclosed at **Annex Four**), which is used frequently as the basis of media commentary, presents similar trends. It shows that there has been a drop across all lending types, particularly in credit cards, but also car loans and other personal loans. It is important to note that Centrix data is not an official statistic, meaning it is subject to change and interpretation.
- 31 It should be noted that the full impacts of the affordability and suitability changes will take time to flow through to monthly lending data collected by the Reserve Bank, particularly for mortgage lending. This is because of the time lag between loan pre-approval, home purchase and settlement, as well as the time needed for banks to collate and provide the monthly data. The Reserve Bank estimates that it may be another two months before the full impacts of the affordability and suitability changes can be seen, noting that the February month mortgage commitment data will be published on 24 March 2022.

A range of factors may be impacting lending

- 32 Consumer credit markets (particularly the home loan market) are affected by a range of factors, such as house prices, seasonality, LVR limits and the OCR. Recent developments impacting some of these factors are likely to have exerted additional downward pressure on lending.
- 33 The restrictions on high LVR owner-occupier lending were tightened on 1 November. While the Reserve Bank advises that this will have affected a small proportion (less than 10%) of new owner-occupier mortgage lending by banks, the changes effectively halve the allowance for high LVR lending (only 10% of a bank's new owner-occupier mortgage lending can be at more than 80% LVR compared to the previous limit of 20%). The impact of these changes will have been limited to borrowers with lower deposits. However, these borrowers appear to be the subject of a significant proportion of recent media stories relating to the CCCFA changes.
- 34 The LVR limits do not apply to personal consumer lending or to non-bank mortgage lending. Changes to the limits do not generally require additional processing times, since banks already have well-established systems for operationalising these regulations.
- 35 Mortgage interest rates have materially increased since mid-2021, based on expectations that the OCR will increase over the next few years. This is likely to have put some downward pressure on lending and is probably the biggest factor affecting changes in the volume of lending.
- 36 The Reserve Bank notes that all banks test mortgage serviceability at higher interest rates (around 6 percent or above) but do not make frequent changes to the test rates. Test rates are generally more stable and do not normally change in line with OCR changes – banks did not reduce them much when the interest rate trend was downwards – but it is possible that recent increases in interest rate forecasts following a period of low interest rates may have prompted some banks to reconsider their test rates. Interest rate changes do not affect loan processing times.

However, a number of lenders consider that the drop in loan approvals is in part directly attributable to the recent CCCFA changes

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37 From the information available at the moment, it is not possible to separate out the impacts of the recent CCCFA changes from other factors. However, the banks (which cover approx. 98.5 percent of the total stock of home lending, and 95 percent of new home lending flows) have indicated that they consider that the recent CCCFA changes are resulting in reductions in home-loan approval volumes as a result of:

37.1 reduced numbers of loan applications, as front-line staff and brokers filter out borrowers, or brokers refer borrowers to other lenders

37.2 increased loan processing times, which delay loan approval

37.3 increased instances of withdrawal of applications due to increased loan processing times and requirement for additional documentation, and

37.4 increased loan declines, due to borrowers not meeting the new affordability and suitability requirements.

38 Increased loan declines are themselves attributable to:

38.1 an increase in estimated borrower expenses, as a result of the more in-depth inquiries into borrower expenses, in particular discretionary expenses, and more conservative approaches to estimation

38.2 an increase in surplus income requirements applied by lenders (i.e. by how much income needs to exceed expenses), and

38.3 the removal of internal bank processes that allowed lender discretion to approve loans where likely expenses exceed likely income.

39 Non-bank lenders, which cover a small proportion of the home lending market, have shared similar views.

40 Banks have indicated that the decline in credit card and other personal loans lending volumes and approvals is also attributable to recent CCCFA changes for similar reasons to those outlined above.

41 Similarly, non-bank lenders (which cover approx. 44 percent of total personal loan lending) attribute the decline in car loans and other smaller personal loans to the recent CCCFA changes.

While there is an early indication that the recent CCCFA changes may be resulting in the positive impacts intended ...

42 In general, it is too soon to state definitively the extent to which positive outcomes sought by the more prescriptive affordability and suitability assessments requirements are being achieved.

43 However, the following early insights gained through engagements with key stakeholders and data available to date appear to be consistent with the outcomes sought:

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- 43.1 all lenders my officials have spoken to have strengthened their affordability assessment processes – in particular some non-bank lenders – and are now identifying and taking account of important borrower outgoings that they may have been overlooked in the past, such as childcare, medical expenses and gambling
- 43.2 some financial mentors have reported being empowered by the new enforcement and penalties regime provided for by the Amendment Act (**Annex One** refers) to make more effective complaints about irresponsible lending
- 43.3 referrals to the financial helpline for budgeting and debt, MoneyTalks, have been increasing since August 2021, with January being the busiest month on record. The increase in calls would suggest that the new requirements on lenders to disclose information about financial mentoring and dispute resolution services are having the intended effect of enabling those in need to access financial advice, and
- 43.4 some of the areas where substantial lending declines have been observed (**Annex Three** refers), such as motor vehicle lending, have been identified in the past as areas that have generated particular consumer harm.

A range of potential unintended consequences are emerging

- 44 As noted above, officials are still engaging with key stakeholders and gathering relevant data.
- 45 Based on the engagements and data available so far, the following appear to be potential unintended consequences of the CCCFA changes:
 - 45.1 access to all types of consumer credit, including residential home loans, have been impacted in a less targeted way and to a greater extent than intended by the implementation of the affordability and suitability changes
 - 45.2 loan processing times and associated compliance costs have increased in a less targeted way than expected, and
 - 45.3 consumers facing unduly intrusive lines of inquiry, which give rise to privacy concerns.
- 46 There is also anecdotal evidence of concerns that need to be investigated further; namely:
 - 46.1 consumers facing barriers in refinancing or consolidation of loans from another lender, which may not meet strict affordability criteria, but are unambiguously more affordable than the original loan payment schedule
 - 46.2 consumers being diverted from lenders with more onerous processes and more conservative interpretations of the new requirements to those with less demanding processes and higher interest rates and fees. Lenders indicated

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that this is sometimes being driven by intermediaries such as brokers and motor vehicle dealers, and

46.3 more vulnerable consumers who are declined lending by bank and non-bank lenders may be pushed to non-compliant or black-market lending.

47 The concern identified in para 45.1 requires particular consideration. In relation to 45.2 and 45.3, I note the new penalties introduced as part of the CCCFA changes should provide a strong deterrent.

48 There are also concerns that small business lending, which is not covered by CCCFA lender responsibilities, may be indirectly impacted by the affordability and suitability CCCFA changes where borrowers are securing their borrowing against personal assets.

A number of issues with the recent CCCFA changes have been identified as a result of engagement with lenders so far

49 All lenders implemented changes to their processes based on legal advice and due diligence on the Amendment Act, the Regulations, the Code and Commerce Commission guidance. This has required investing in new technologies (e.g. many lenders have purchased systems for analysing bank transaction records) and substantial staff training. The total implementation costs have been high.

50 While lenders are supportive of the policy intent of the affordability and suitability changes, many considered that the changes, in particular the Regulations, were more extensive, onerous and invasive than warranted by the original policy intent. All lenders have commercial incentives to maximise profitable lending, while they also have a strong interest in ensuring that borrowers will make the required repayments. I want to ensure that lending is safe and responsible.

51 A key concern raised by lenders and some consumer groups relates to the fact that the same affordability assessment requirements apply to all lending types and consumers, with limited discretion and narrow exceptions. This reflects the difficulty in identifying situations in advance where a full income and expenses assessment is unnecessary and a lack of stakeholder consensus on these matters.

52 It is worth noting that in practice banks and other lenders have described slightly different processes to implement the new affordability and suitability requirements, which would suggest that there is some flexibility in how the new requirements can be implemented. Further work on understanding different drivers will need to be completed as part of the investigation.

53 Some lenders expressed concerns about the new penalties and statutory damages introduced by the Amendment Act (in particular personal liability for individual executives), which lenders are saying is leading them to take a conservative approach to any uncertainties in the regime. The new penalties and statutory damages are an important deterrent for lenders, in particular non-bank lenders. Whether there is a need to further clarify the application of the new penalties, in particular personal liabilities, will also need to be considered as part of the remainder of the investigation.

- 54 The Commerce Commission has provided significant information to lenders during its education reform programme which made it clear that it would take an educative approach to the new changes while they embed in and feedback is received on their implementation (including interpretation challenges). It did note to lenders, however, that serious and harmful behaviour would be addressed appropriately despite the embedding period, in line with its Enforcement Response Guidelines. It may be helpful to repeat the Commission’s messaging around this approach and discretion.
- 55 A number of more specific issues in relation to the Regulations and the Code have also been identified in conversation with lenders. These issues can be categorised in the following broad themes (a more detailed overview is provided in **Annex Five**):
- 55.1 scope and treatment of expenses (Reg. 4AE and 4AK, and Code Part 5), leading to excessive inquiries and lenders feeling unable to apply sufficient judgment in relation to ‘discretionary’ expenses
 - 55.2 uncertainty in relation to definition of ‘reasonable surplus’ (Reg. 4AF), leading to a more conservative approach to the application of adjustments and buffers, and
 - 55.3 very limited scope of the exception provisions (Reg. 4AG and 4AH and Code Part 5) meaning that a full assessment of income and expenses are being performed for many very low-risk applications.
- 56 It is important to note that this is an initial list of specific issues identified with the Regulations and the Code, and that additional issues may emerge as part of the investigation.

Financial mentors and consumer advocates are continuing to emphasise the importance of the new penalties provision and strong enforcement regime

- 57 For certain breaches, there are now pecuniary penalties of up to \$200,000 for individuals and up to \$600,000 for businesses, in addition to statutory damages. The Amendment Act also requires that lenders keep a record of inquiries made and provide a copy of this record to the borrower within 20 days of receiving a request.
- 58 Financial mentors and consumer advocates engaged with so far as part of the investigation have indicated that whether the recent affordability and suitability changes are working for consumers at risk of suffering hardship is only likely to become apparent over the next 6-12 months.
- 59 However, some suggested there may be some early positive impacts. Financial mentors and consumer advocates have expressed that they are now more empowered to bring forward breaches and complaints against lenders. Prior to the amendment, it was difficult to access records of inquiries made from lenders, as lenders could challenge their right to request. This meant they were less likely to submit breaches as they would not be able to meet the evidential burden required.
- 60 Financial mentors and consumer advocates emphasized the importance of the new penalties provision, strong enforcement regime, record keeping and request

provisions, information disclosure provisions, and stated that they found the training provided by the Commerce Commission to be useful.

Initial proposals to address specific issues identified in relation to the Regulations and the Code

61 While final advice is not due until April, this paper sets out a number of initial proposals to address some aspects of the specific issues identified during the engagement with lenders in relation to the Regulations and the Code. There are changes that represent a ‘no regrets’ approach and which have the potential to benefit consumers who have been unduly targeted by the recent CCCFA changes. They are outlined below (more detail is provided in **Annex Five**).

Initial proposals to address specific issues related to scope and treatment of expenses

62 As noted above, the scope and treatment of expenses in the Regulations (Reg. 4AE and 4AK) is leading to excessive inquires and inability for the lender to apply judgment in relation to ‘discretionary’ expenses.

63 Specifically, regulations include in the definition of ‘listed outgoing’s a paragraph **(d)** that the lender must assess ‘any regular or frequently recurring outgoing’s (for example, savings, investments, gym memberships, entertainment costs, or tithing) that are material to the estimate of relevant expenses and that the borrower is unable or unwilling to cease after the loan is granted or materially changes’. The definition is prescriptive and captures a wide range of discretionary expenses which could result in overestimating expenses, particularly in cases where costumers have had high discretionary expenses in the past. It also captures outgoing’s that are not expenses (savings and investments), penalising those consumers that have higher savings or investments.

64 My initial proposal is to **amend paragraph (d) of the definition of ‘listed outgoing’s** to remove the examples of ‘savings’ and ‘investments’.

65 The inclusion of savings and investments was a concern raised by lenders and some consumers. This option would remove these outgoing’s that are not expenses and provide for some immediate adjustments to address concerns. It would do so without reducing the clear prescription for lenders to establish which expenses the borrower will continue to incur. I consider this is an important protection for vulnerable borrowers.

66 It would, however, not address the other specific issues relating to the wide and prescriptive nature of the definition and the extent of lender inquiries that are of concern to other borrowers.

67 I considered an alternative of narrowing the paragraph to make it an objective test (e.g. ‘any regular or frequently recurring outgoing’s that are material to the estimate of relevant expenses, excluding outgoing’s that a reasonable lender would expect the borrower to cease to avoid substantial hardship’) supported by additional guidance in the Code. This option would be consistent with the affordability principle in the CCCFA and would go further to address issues relating to the wide and prescriptive nature of the definition and the extent of lender inquiries, allowing for more lender

judgment. It may also alleviate some of the concerns from consumers about the disproportionate and intrusive nature of inquiries.

68 However, according to financial mentors this alternative approach creates a risk that some lenders take a blunt approach to disregarding regular borrower expenses, without taking into account individual borrower circumstances. It is important that lenders continue to take into account outgoings such as tithing or overseas remittances that borrowers may be obligated to continue. While this risk could be mitigated through Code guidance, further work and consultation is needed as part of the investigation to understand whether there is any realistic prospect under such an approach of mitigating the potential unintended consequences.

69 Regulations (4AK) require lenders to estimate the borrower's likely living expenses based on asking the borrower, reviewing bank transactions and/or using information they already hold. Many lenders appear to be both asking the borrower and also attempting to reconcile living expenses from bank transactions records. This results in unnecessary (and unintended) effort, and invasive inquiries of borrowers who are asked to explain bank transactions.

70 My initial proposal is to **amend the Regulations and the Code** to clarify that:

70.1 when borrowers provide a detailed breakdown of their likely living expenses, and these are benchmarked against robust statistical data, there is no need to also inquire into their current living expenses from recent bank transactions, and

70.2 when lenders have estimated expenses from recent bank transaction records, 'asking the borrower about their relevant expenses' includes obtaining information about how relevant expenses are likely to change once the contract is entered into, and

70.3 the requirement to obtain information in sufficient detail only relates to information received from borrowers (e.g. ensuring that expense categories on application forms are sufficiently detailed) rather than relating to information from bank transaction records.

71 These clarifications are consistent with the original policy intent of the regulations and reflect processes that some lenders appear to have already adopted in accordance with the regulations. The clarification at 70.1 is consistent with typical bank practice prior to the affordability and suitability changes, which was intended to be continued by the Regulations. I acknowledge there will be some households who have additional costs based on their particular circumstances, for example a family member who might have a long-term illness where they will have to spend more on petrol than the average household. I intend for additional guidance to be provided in the Code to deal with such situations. The change at 70.2 reflects the fact that the Regulations were intended to require a forward-looking (rather than backwards looking) estimate of the borrowers' expenses, and the expectation that expenses will change once a credit contract is entered into. The change at 70.3 addresses an overly conservative interpretation of the Regulations, but lenders will still need to make use of detailed bank transaction records to verify expenses that cannot be benchmarked and, in many cases, to identify financial commitments that may have been omitted. These

clarifications mean that the Regulations continue to prescribe robust affordability assessments without undue compliance and inquiries.

Initial proposals to address specific issues in relation to surplus, adjustments, and buffers

- 72 Regulations (**4AF(2)(b(i) and 4AF(2)(b(ii))**) require that, as part of assessing potential financial hardship, lenders must conduct a full income and expense estimate for certain kinds of credit. This includes applying a reasonable surplus or buffers to address the risk of overestimation of income, underestimation of expenses, and/or other expenses. Reasonable surplus is not clearly defined. This means lenders have tended to be more conservative in calculation of a reasonable surplus value than they may otherwise need to be.
- 73 It is important to note that any surplus is in addition to buffers already applied by lenders to account for other factors, such as fluctuating interest rates.
- 74 My initial proposal is to **amend the Code** to further clarify when a ‘reasonable surplus’ or ‘reasonable buffer’ is required and how it should be set. This could be supported by the provision of examples of formulas of a reasonable surplus.

Initial proposals to address specific issues in relation to the exemptions

- 75 Regulations (**4AG**) provide that a full affordability assessment is not required if ‘it is obvious’ in the circumstances of the particular case that the borrower will make the payments under the agreement without suffering substantial hardship. The term ‘obvious’ in the exception to the general rule is ambiguous and difficult for lenders to apply. The example in the Code is of a high net worth individual obtaining a credit card with a relatively low limit, which is difficult for lenders to generalise to other situations and may suggest an excessively high test. This means that the exemption is not used in circumstances when it arguably should be.
- 76 My initial proposal is to **amend the Code** to remove the current example. However, I also propose that alternative Code guidance on this test be developed as part of the required consultation on Code changes. This could include guidance that, for example, it is obvious that a loan is affordable if, following an estimate of income, fixed financial commitments and living expenses, there is a large surplus available for other expenses.
- 77 It is important to note that these are only my initial proposals, and that other options to address the specific issues being identified on the nature of the exceptions, which could include changes to the Regulations (**Annex Five**), are being considered as part of the remainder of the investigation.

I intend to undertake targeted and public consultation on these initial proposals

- 78 To ensure that the initial proposals actually work in practice and do not result in any unintended consequences, I intend to instruct my officials to undertake a targeted consultation with key stakeholders as part of drafting the amendments to the Code and drafting instructions for the Regulations.

79 The CCCFA requires that any proposed changes to the Code are released for public consultation. Once finalised, the new Code comes into effect a minimum of 28 days later.

80 In parallel to the required consultation on the Code, I propose to undertake further public consultation with lenders, financial mentors and other key stakeholders on

	21 Feb - 25 Feb	28 Feb - 4 March	7 March - 11 March	14 March - 18 March	21 March - 25 March	28 March - 1 April	4 April - 8 April	11 April - 14 April	19 April - 22 April	26 April - 29 April	3 May - 6 May	9 May - 13 May	16 May - 20 May	23 May - 27 May	30 May - 3 June
Prepare drafting instructions on the Regulations, including targeted consultation	█														
PCO draft exposure draft of regulations		█	█	█											
MBIE develop new Code guidance, including targeted consultation		█	█	█											
Public consultation on Regulations and Code					█	█									
Make changes to Regulations and Code following feedback, finalise changes							█	█							
Publish the code (note 28-day delay to come into force)								█							
Legislative process for Regulations (<i>note this is subject to minimal ministerial and departmental consultation</i>)									█	█	█				
Regulations made by Order in Council											█				
Parts of the Code come into force												6/5/21			
Regulations come into force															3/6/21
Remaining parts of the Code come into force with the Regulations															3/6/21

any regulatory changes.

I intend for these initial proposals to be in place by early June

81 I intend to progress the work on the Regulations and the Code in parallel, which will enable for changes to be in place by early June.

82 An indicative timeline is above.

Further actions to be progressed as part of the investigation

Continue engagement with key stockholders and analysis to determine what additional changes to the Regulations and the CCCFA may be required

- 83 The investigation is still ongoing. Further work on whether additional changes are required to address concerns will be required. It will be important to ensure that any changes maintain protection to ensure that lending is affordable and suitable, while easing the compliance burden faced by those consumers who can afford lending.
- 84 I intend this to be covered as part of the final advice in April. As part of the remainder of the investigation, officials will also continue to engage with key stakeholders and analyse available data to understand and address the other issues and options identified in relation to the Regulations and the CCCFA so far (**Annex Five**), and to identify if there are other issues or options that need to be considered.

Conduct an international comparison to assist in determining how New Zealand's policy aligns with the global context

- 85 As it stands, New Zealand's consumer credit regime is, in general, more prescriptive in comparison to Australia and the UK.
- 86 During our consultation, many lenders and industry representatives expressed favourable views towards the Australian consumer credit regime. I understand that the current Australian government is in the process of deregulating certain kinds of financial products.
- 87 As part of the remainder of the investigation, officials will engage with their Australian counterpart to understand what can be learned from their recent experiences.

Undertake further work on understanding the impact of the CCCFA on local government led housing initiatives

- 88 While the investigation into the initial impacts of the CCCFA changes is focussed on commercial lending, I am also aware that concerns have been expressed by a number of local authorities about their ability to operate loan schemes for ratepayers. For a number of years, councils have provided loans for heating, insulation and energy efficiency improvements. These have been repaid by individual ratepayers through voluntary targeted rates. These schemes currently have a partial exemption from the CCCFA.
- 89 Some aspects of the CCCFA changes may be particularly difficult for councils to comply with, such as the requirement to obtain certification from the Commerce Commission that directors and senior managers are fit and proper persons.
- 90 Officials are engaging separately with councils on these matters, and are likely to provide advice in the coming months on whether a further exemption is warranted.

Separate work on small business lending

- 91 The primary purpose of the CCCFA is to protect the interests of consumers, so changes to the Act should not directly affect businesses lending. However, there may

be indirect effects. For example, small businesses owners often use their homes for security in business lending, and so practices relating to residential home loans could affect lending indirectly. This is a long-established practice and a long recognised challenge.

- 92 To date, MBIE officials have been exploring other ways to improve small- and medium-sized enterprises' access to finance [CBC-21-MIN-0067]. Part of this work will aim to address issues facing small firms, many of whom will only be able to secure lending on reasonable terms using their house as security for the loan.
- 93 Regulatory settings will be considered within the scope of the access to finance work, and as part of this work MBIE will investigate how the CCCFA changes are likely to affect business lending. MBIE's findings will be reported to the Minister for Small Business, and the Minister of Commerce and Consumer Affairs.

Risks and mitigations

- 94 The investigation is still ongoing. Officials are still in the process of completing the engagement with key stakeholders, such as Good Shepherd and Māori organisations. Officials also still need to collate and analyse data to carry out an in-depth analysis into the impacts of the CCCFA changes and conduct a full analysis of the options available to the Government and identify any unintended consequences that any further changes to the Regulations and the Code may introduce.
- 95 There may be a risk therefore that progressing with these initial proposals could be seen as inconsistent with the process set out in the TOR, and that not enough consideration has been given to any potential unintended consequences of these initial proposals. Financial mentors and some consumer advocates may view these tweaks unfavourably. Even though the initial proposals in this paper are straightforward and seek to clarify how the requirements relating to affordability assessments are to be implemented, financial mentors and some consumer advocates may consider that the proposed changes could result in worse outcomes for some consumers.
- 96 Lenders and some consumers may indicate that these changes do not go far enough in addressing their concerns.
- 97 Lenders may also be reluctant to implement these initial proposals ahead of the investigation being concluded. This is particularly the case because of the high profile and sensitive nature of this topic, and the cost involved with making changes to their systems and processes, and because operationally lenders will likely need to seek approval from their governing bodies to implement these changes. This may lead some lenders to defer implementing any changes until the conclusion of the investigation.
- 98 However, I consider that these risks can be mitigated by:
- 98.1 clearly describing the recommendations made in this paper as the 'initial proposals' that align clearly with the original intention of the CCCFA, and subject to targeted consultation with lenders, financial mentors and consumer advocates as part of the drafting of drafting instructions for the Regulations

and amendments to the Code , and further public consultation on the Code and an exposure draft of the Regulations;, and

98.2 making it clear that the impacts of the CCCFA changes and any further changes to the Regulations and the Code will be considered as part of the remainder of the investigation to be concluded in April.

99 I believe making some ‘no regrets’ changes now, in line with the intent of the Act and in advance of the investigation’s conclusion, allows us to respond expeditiously to the concerns raised by consumers and lenders to ensure we are not unduly restricting access to credit for New Zealanders, including first home buyers, in the near term.

Financial Implications

100 The proposals in this paper do not create any additional financial implications for the Crown.

101 The proposals may result in reducing compliance costs for both lenders and consumers.

Legislative Implications

102 Changes to the Regulations are needed to implement the proposals. PCO has been consulted.

103 The CCCFA requires that the proposed changes to the Code are released for public consultation. Once finalised, the new Code comes into effect a minimum of 28 days later.

Impact Analysis

Regulatory Impact Statement

104 Treasury's Regulatory Impact Analysis team has determined that the proposal to make changes to the Credit Contracts and Consumer Finance Regulations 2004 is exempt from the requirement to provide a Regulatory Impact Statement on the grounds that it has no or only minor impacts on business, individuals, and not-for-profit entities.

Climate Implications of Policy Assessment

105 A Climate Implications of Policy Assessment (CIPA) is not required for the proposals in this paper.

Population Implications

106 The recommendations in this paper seek minor changes to the Regulations and the Code, and Officials have not undertaken an analysis of whether there are any negative impacts on particular population groups.

107 However, I anticipate that an analysis of the impacts of any further actions identified in the April final advice will undertake then.

Human Rights

108 I have not identified any potential inconsistencies with the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993.

Consultation

109 The following CoFR agencies were consulted on the initial findings and recommendations in this paper: The Treasury, Reserve Bank of New Zealand, Commerce Commission and Financial Markets Authority. The Department of Prime Minister and Cabinet was informed.

110 The Reserve Bank does not recommend the proposed two-stage approach because of the impost on lenders, the risks of making decisions based on insufficient data and experience which may need to be unwound later and the other risks outlined above. The Reserve Bank suggests that decisions should be deferred until the final advice is available in April.

111 A number of key stakeholders were engaged so far, with further engagement to be conducted on the initial proposals in this paper and to inform the final advice in April (**Annex Three** refers).

Communications

112 I am intending to publicly announce that I have asked officials to progress work and consultation on these initial proposals.

Proactive Release

113 I intend to proactively release the Cabinet paper.

Recommendations

The Minister for Commerce and Consumer Affairs recommends that the Committee:

1 **note** that, in January 2022, I initiated investigation into the impacts of the parts of the Credit Contracts Legislation Amendment Act 2019 (the **Amendment Act**) and Credit Contracts and Consumer Finance (Lender Inquiries into Suitability and Affordability) Amendment Regulations 2020 (the **Regulations**) that came into force on 1 December 2021;

2 **note** that Terms of Reference were published on 31 January 2022 and state that final advice is expected in April 2022;

3 **note** the initial findings of the investigation presented in this paper suggest that:

3.1 the parts of the Amendment Act and Regulations that came into force on 1 December 2021 appear to be contributing to a drop in lending, including

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home lending and more significantly other personal lending (e.g. credit cards, car loans)

- 3.2 while some early impacts appear to be consistent with the outcomes sought by these recent affordability and sustainability changes, there also appear to be unintended consequences
 - 3.3 there are continued concerns that the new prescriptive affordability and suitability assessments provided for in the Regulations apply to all lending types and consumers, with limited discretion and narrow exceptions, and
 - 3.4 a range of more specific issues relating to particular parts of the Regulations and the Responsible Lending Code (the **Code**) are contributing to the unintended consequences;
- 4 **note** that while final advice is not due until April, this paper sets out a number of initial changes to address specific issues identified in relation to the Regulations and the Code;
- 5 **agree** that the Regulations and the Code be amended to address some of the specific issues identified, as follows:

Initial proposals to address specific issues related to scope and treatment of expenses

- 5.1 amend the Regulations to exclude savings and investments from the definition of the listed outgoings;
- 5.2 amend the Regulations and the Code to:
 - 5.2.1 clarify that when lenders ask borrowers about their likely living expenses, and these are benchmarked against statistical data about household expenses, there is no need to inquire into their current living expenses from recent bank transactions;
 - 5.2.2 clarify that when lenders estimate expenses from recent bank transaction records, lenders can ask the borrower about how expenses are likely to change once the contract is entered into; and
 - 5.2.3 clarify the requirement to obtain information in sufficient detail to minimise underestimation only relates to information received from borrowers (e.g. ensuring that expense categories on application forms are sufficiently detailed) rather than relating to information from bank transaction records etc;

Initial proposals to address specific issues related to surplus, adjustments, and buffers

- 5.3 amend the Code to further clarify when a 'reasonable surplus' is required and how it should be set;

Initial proposals to address specific issues related to exceptions

- 5.4 amend the Code to remove the current example for when affordability is 'obvious' and consider alternative guidance and examples in consultation with stakeholders;
- 6 **invite** the Minister of Commerce and Consumer Affairs to issue drafting instructions to the Parliamentary Counsel Office to give effect to the above paragraphs;
- 7 **authorise** the Minister of Commerce and Consumer Affairs to make decisions on minor or technical matters, consistent with the policy in this paper, on any issues that arise during drafting;
- 8 **note** that the Minister of Commerce and Consumer Affairs will instruct officials to undertake targeted consultation with lenders, financial mentors and consumer advocates as part of the drafting of drafting instructions for the Regulations and amendments to the Code;
- 9 **note** that under the Credit Contracts and Consumer Finance Act 2003, changes to the Code need to be publicly consulted;
- 10 **authorise** the Minister of Commerce and Consumer Affairs to consult publicly on an exposure draft of regulations in parallel to consultation on the Code;
- 11 **note** that further work will need to be conducted as part of the investigation to fully understand and address the issues and unintended consequences, and that the final advice is due in April 2022;
- 12 **invite** the Minister of Commerce and Consumer Affairs to report back on the final advice on the investigation in April 2022.

Authorised for lodgement

Hon Dr David Clark

Minister of Commerce and Consumer Affairs

Appendices

Annex One: Visual summary of CCCFA reforms

Annex Two: Terms of Reference

Annex Three: Stakeholder engagement

Annex Four: Centrix - Loan Conversion Report

Annex Five: Table of concerns options and impacts

Key

- problem
- contributing factors
- Act
- ▭ Regulation making powers

Set application fees etc.

Set prescriptive:
 - affordability & suitability requirements
 - advertising standards

Fit and proper person test for directors and top executives

Pecuniary penalties and statutory damages

Substantiation: affordability and suitability assessment more easily verified

Duty on directors and top executives
 Simpler banning order process, to prevent 'phoenix lenders'

Substantiation: reasonableness requirements more easily enforced

unreasonable fees

non-compliance

Interest and fees caps

cost of borrowing

debt spirals & unaffordable debt

harm from debt collection

Set additional disclosure requirements at the start of debt collection

Power to declare what is and is not a credit contract or creditor under the CCCFA

new products and services

harm from mobile traders

Extend responsible lending requirements to mobile traders
 New requirement to register on FSPR
 Fit and proper person test for directors and top executives

Investigation into the impacts of recent changes under the Credit Contracts and Consumer Finance Act 2003

Terms of Reference

Context

In response to recent concerns, the Minister of Commerce and Consumer Affairs has asked the Council of Financial Regulators (CoFR) - Kaunihera Kaiwhakarite Ahumoni (Ministry of Business, Innovation and Employment Hīkina Whakatutuki, Reserve Bank of New Zealand Te Pūtea Matua, Financial Markets Authority Te Mana Tātai Hokohoko, Commerce Commission Te Komihana Tauhokohoko and The Treasury Te Tai Ōhanga) to conduct an investigation into the initial implementation of recent changes to the Credit Contracts and Consumer Finance Act 2003 (CCCFA) that came into force on 1 December 2021. This investigation will be led by MBIE with critical input from other CoFR agencies.

Objective

The objective of the investigation is to identify any impacts of the recent CCCFA changes that came into force on 1 December 2021, considering the scale and nature of the impacts, to assess what, if any, further actions are needed.

Role of CoFR agencies

MBIE as the relevant policy agency will lead the investigation, including engagement with stakeholders, in collaboration with CoFR agencies. CoFR agencies will provide input to the investigation as well as review and feedback on the conclusions and recommendations of the draft and final reports in accordance with their relevant functions.

Scope

The scope of the investigation is to look at the intended or unintended impacts, beyond those expected by the initial implementation, of the parts of the Credit Contracts Legislation Amendment Act 2019 and Credit Contracts and Consumer Finance (Lender Inquiries into Suitability and Affordability) Amendment Regulations 2020 that came into force on 1 December 2021 primarily in relation to mortgage, but also other lending, by banks and non-bank lenders in the current consumer credit market.

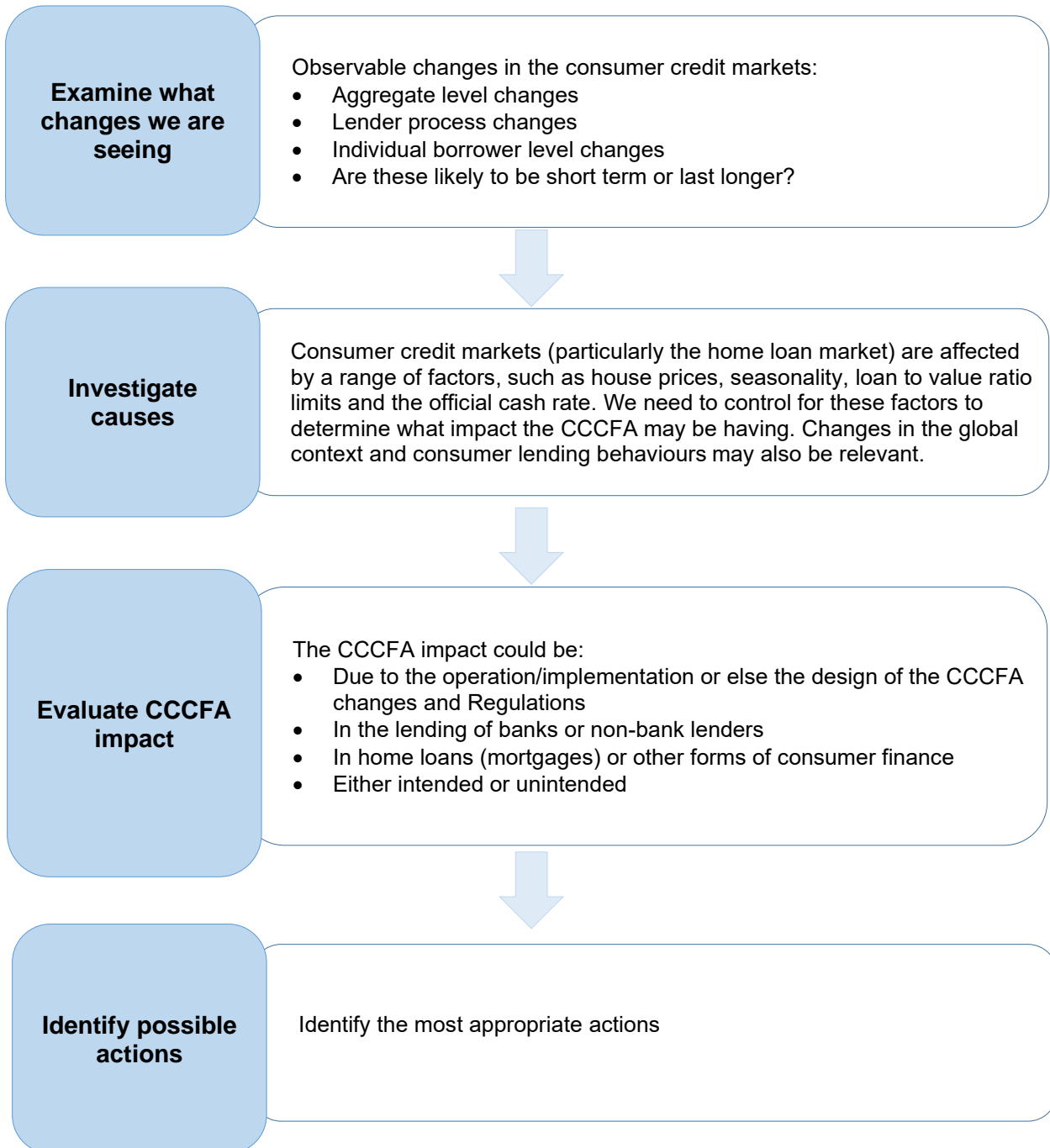
Lines of inquiry

The proposed lines of inquiry set out in Figure One overleaf seek to identify and gather available relevant information to discover potential impacts and identify if there are any potential problems that warrant further consideration. A potential outcome is that more work will likely need to be done to fully understand actual impacts.

Indicative timeframes

Initial advice is anticipated in early-mid February, followed by further advice in April.

Figure One: Lines of inquiry



Annex Three: Stakeholder engagement

Stakeholder:	Meeting date:
Kiwibank	26/01/2022
ANZ	27/01/2022
BNZ	27/01/2022
ASB	28/01/2022
Westpac	28/01/2022
NZ Banking Association	28/01/2022
NZ Financial Services Group	28/01/2022
Financial Services Federation	31/01/2022
Christians Against Poverty	2/02/2022
FANZ	2/02/2022
Banking Ombudsman	8/02/2022
Nelson Building Society	8/02/2022
Salvation Army	8/02/2022
Heartland	9/02/2022
TSB	10/02/2022
NZCU Baywide	10/02/2022
Centrix	11/02/2022
FinCap	11/02/2022
Full Balance	11/02/2022
Consumer NZ	14/02/2022
Office of the Privacy Commissioner	15/02/2022

Annex Three: Stakeholder engagement

Save My Bacon	16/02/2022
Ngā Tāngata Microfinance	16/02/2022
Australian Treasury	17/02/2022
Māori Bankers Ropu Tāwhia	18/02/2022
Good Shepherd	18/02/2022
FSCL	22/02/2022
Equifax	22/02/2022
Cooperative Bank	25/02/2022
Co-operative Bank	25/02/2022
Rabobank	TBD
SBS	TBD



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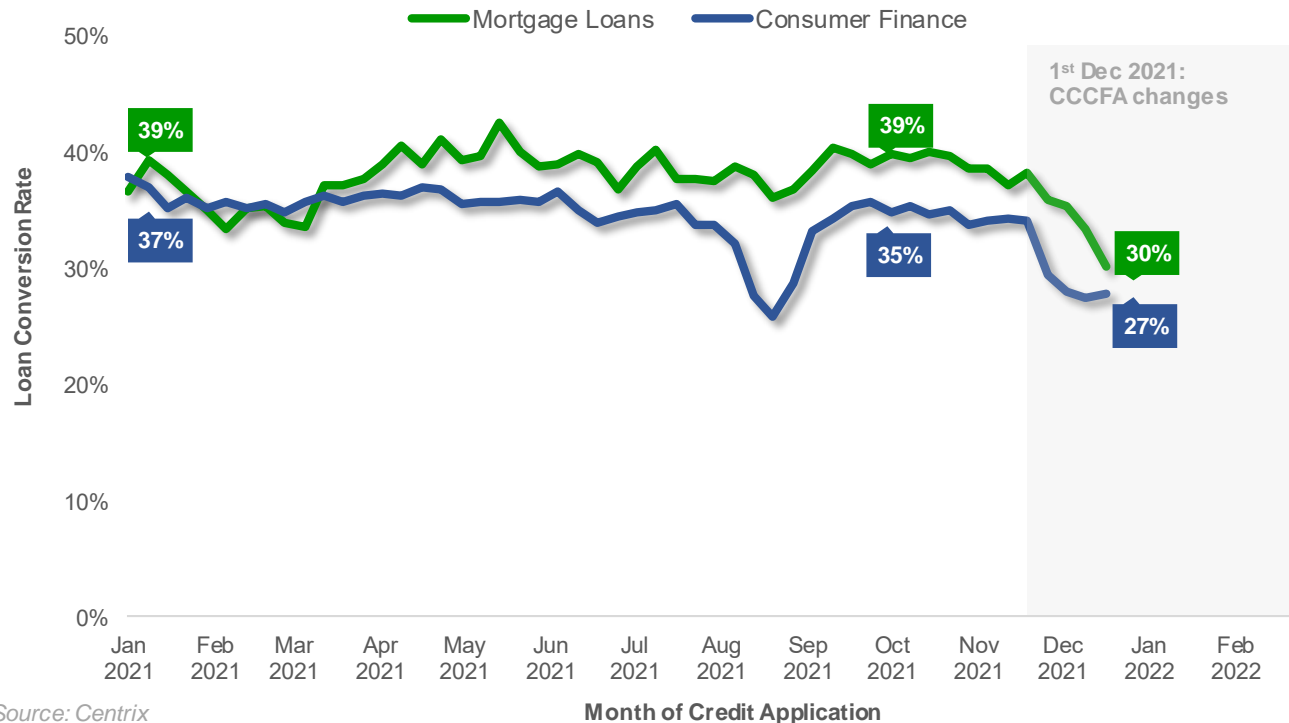
Loan Conversion Report

February 2022

Loan conversions drop amid tightened lending rules

Impact of new lending rules on loan conversion rates

Credit approvals as a proportion of application enquiries made



Source: Centrix

Updated: 10th February 2022

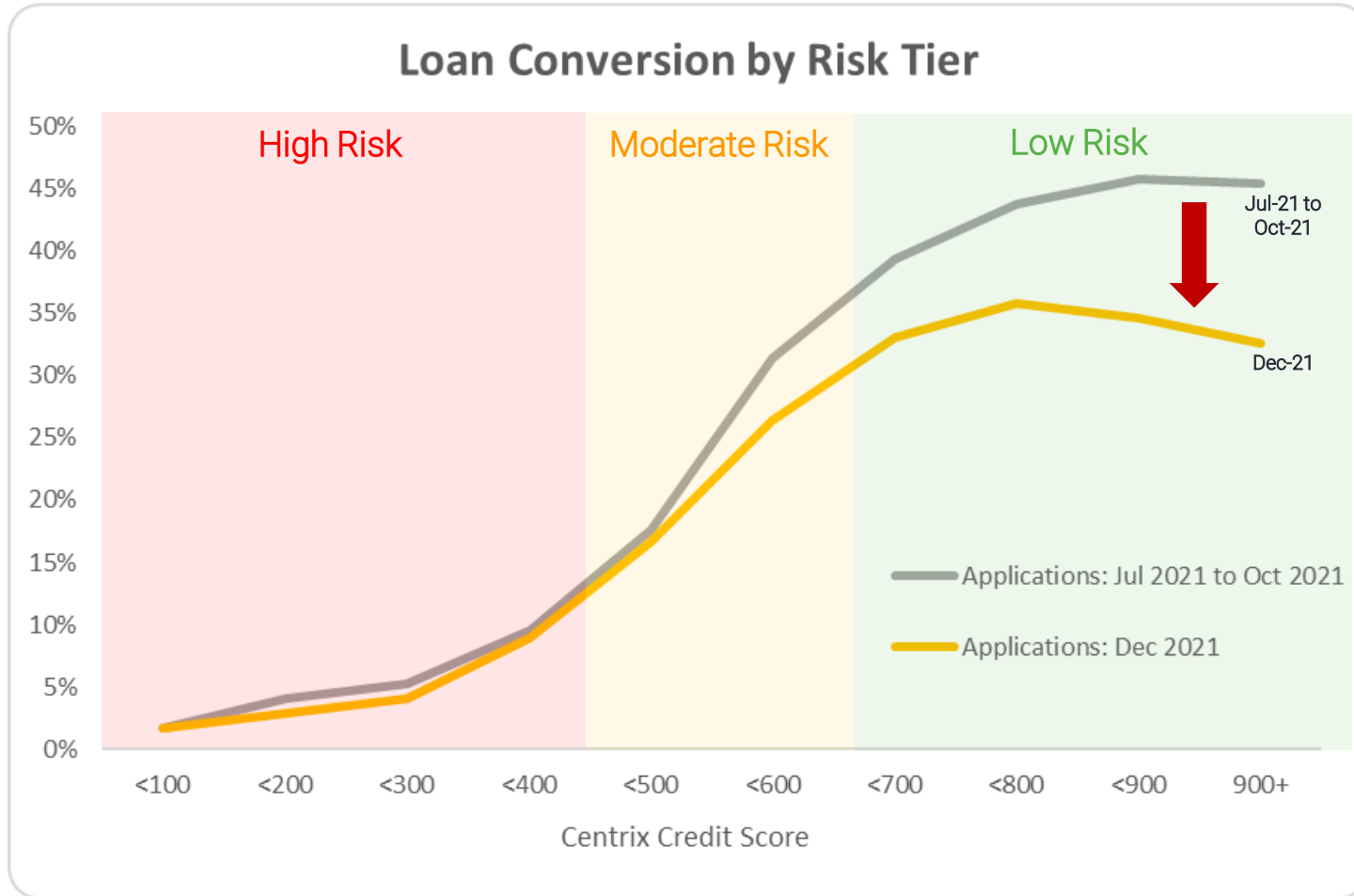
- Changes to lending rules kicked in at the start of November (LVR) and December (CCCFA).
- Proportion of **mortgage loan applications** that resulted in new home loans significantly dropped from **39%** (in October) to just **30%** (current level).
- Consumer finance** loan conversions (credit card, auto and personal loans) plunges from 35% to 27%.
- Hardest hit are **credit card applications** which has seen the sharpest drop in approvals.
- Government to bring forward their investigation** into whether banks and lenders are implementing the CCCFA as intended.

Conversion rates by loan type

Consumer Loan Type	Jul-2021	Aug-2021	Sep-2021	Oct-2021	Nov-2021	Dec-2021
Home Loans	38.5%	37.4%	39.3%	39.5%	37.7%	32.6%
Credit Cards	32.3%	29.6%	30.8%	32.1%	30.0%	19.5%
Personal Loans	31.4%	27.7%	30.8%	30.8%	29.9%	24.0%
Auto Loans	42.5%	36.4%	42.7%	43.2%	42.4%	36.3%

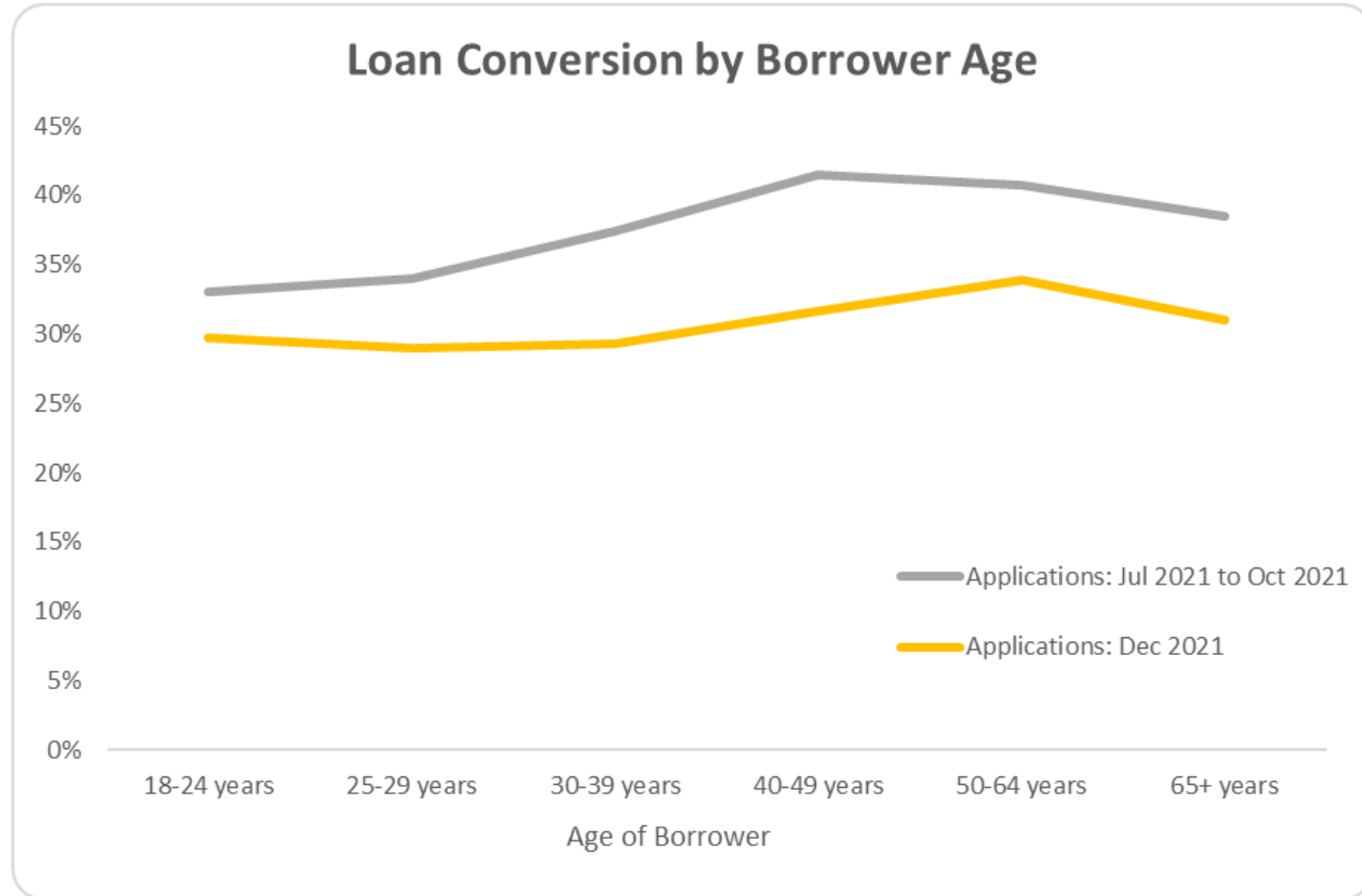
- ③ **Loan conversion** is defined as the number of new consumer loans as a proportion of credit applications made. Conversion rates have **dropped in December** for all main credit loan types.
- ③ Lenders appear to have **rejected 5 percent** of home loan applicants who would have qualified in November.
- ③ Proportion of **credit card applications** that resulted in new cards has fallen below 20% for the first time in December. Down from 32% just two months prior.
- ③ **Reporting lag of circa of 1 month** due to the monthly mechanism for lenders to report credit information to Centrix using Comprehensive Credit Reporting (CCR). See appendix for 2 year time series data.

Conversion rates by consumer risk tier



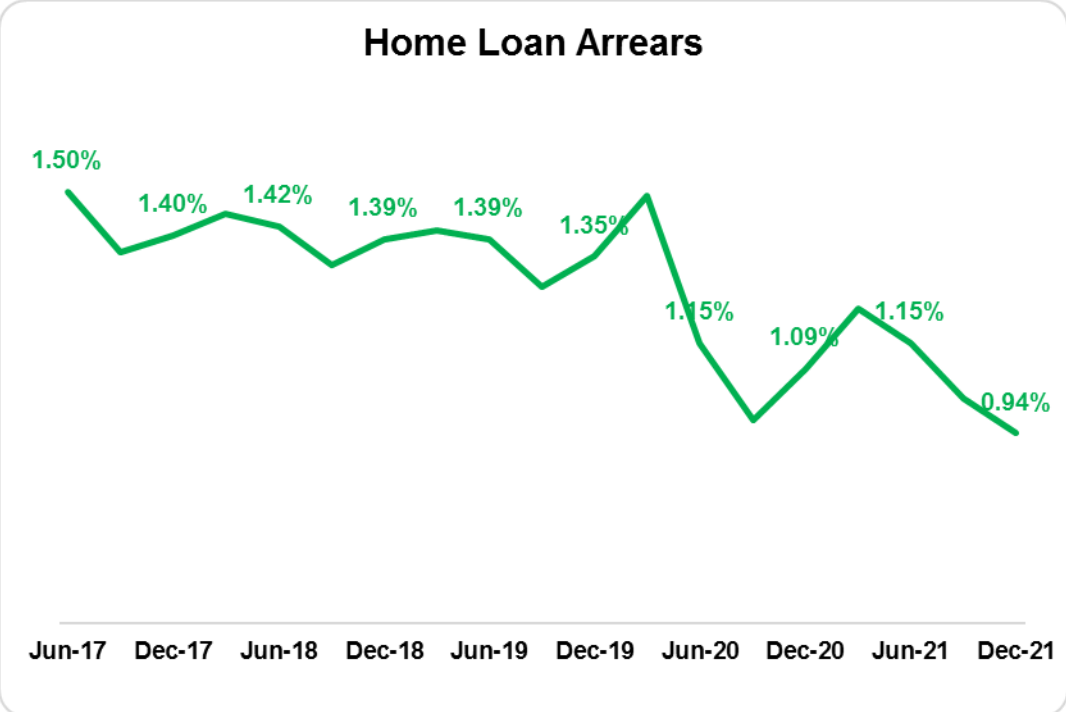
- Measuring loan conversion by **consumer risk tier** using the Centrix credit score.
- Credit score** ranges from 1 (highest risk) to 999 (lowest risk).
- Low risk consumers** are shown to have been impacted the most. Loan conversion rates have sharply dropped for those scoring 700 and above.
- High to moderate risk consumers** have had little or no change to their loan outcomes during this time period. Credit scoring and business rules being the key driver.
- See appendix for data split by **loan type**.

Conversion rates by age group

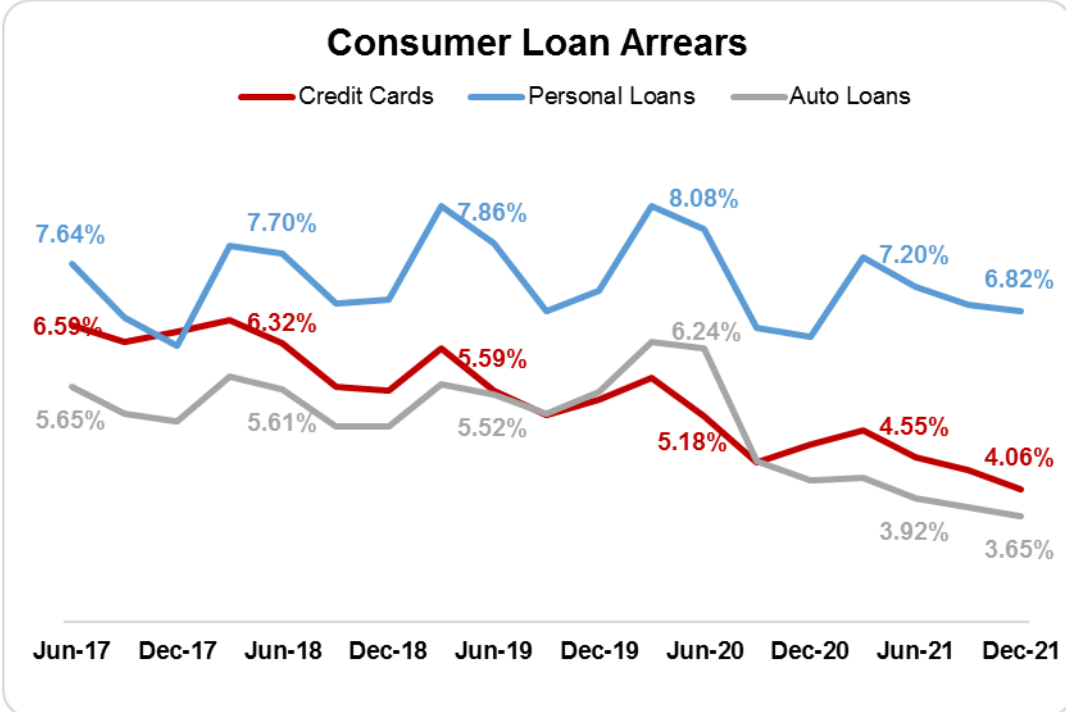


- Ⓢ Measuring loan conversion rates by the **borrower age group** as at the credit application.
- Ⓢ The change in the loan conversion rates is **fairly consistent** across the age groups of borrowers.
- Ⓢ **Younger consumers** less than 30 years old are shown to have been impacted the least.

Consumer arrears are at their lowest level

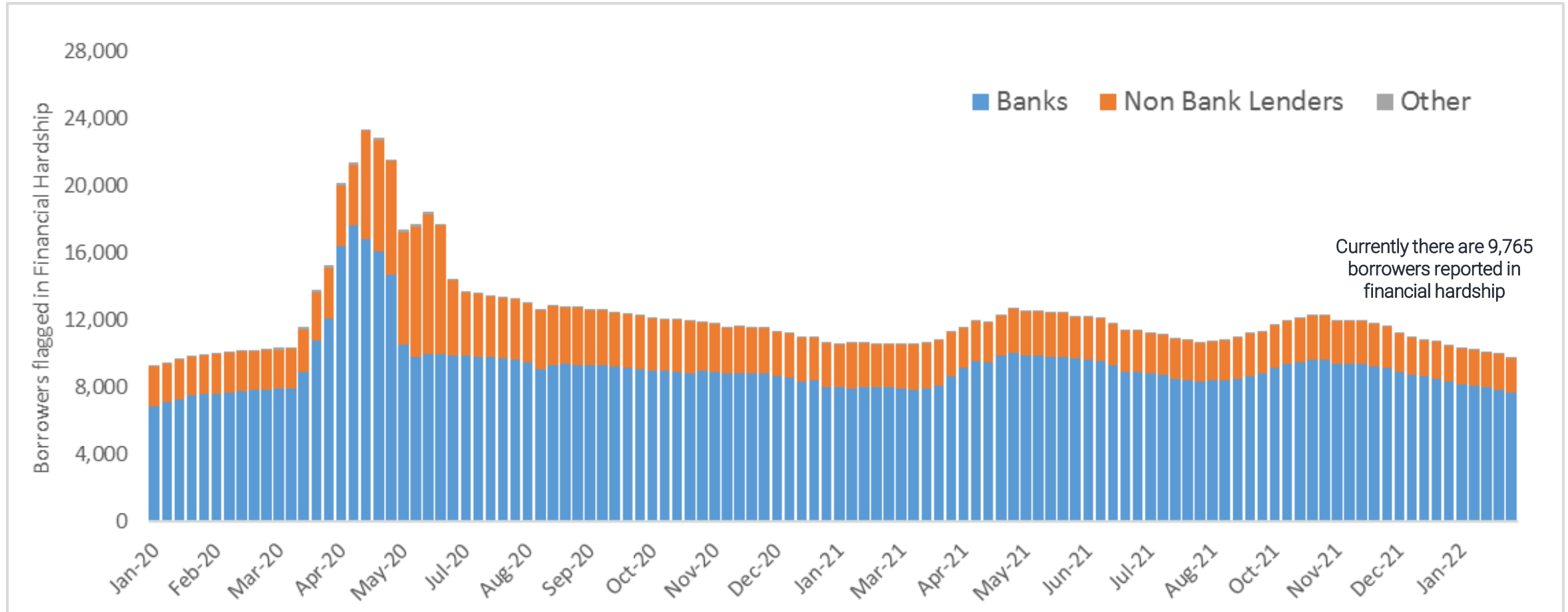


- Home loans in arrears have been **steadily improving** year on year.
- Proportion of home loans with missed payments now **below 1%** for the first time since CCR reporting commenced.



- Arrears on **credit cards** and **vehicle loans** are at their **lowest level** since CCR reporting has been in place.
- Personal loan arrears have been **holding steady** around 6-8% level for the last four years.

Financial hardship falls to a 2 year low



Appendix – loan conversion by product data

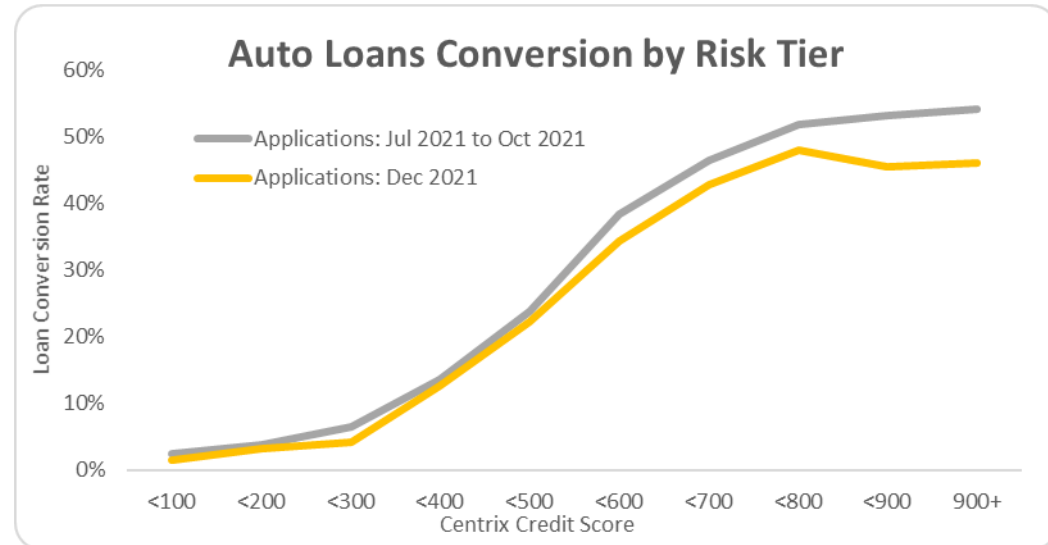
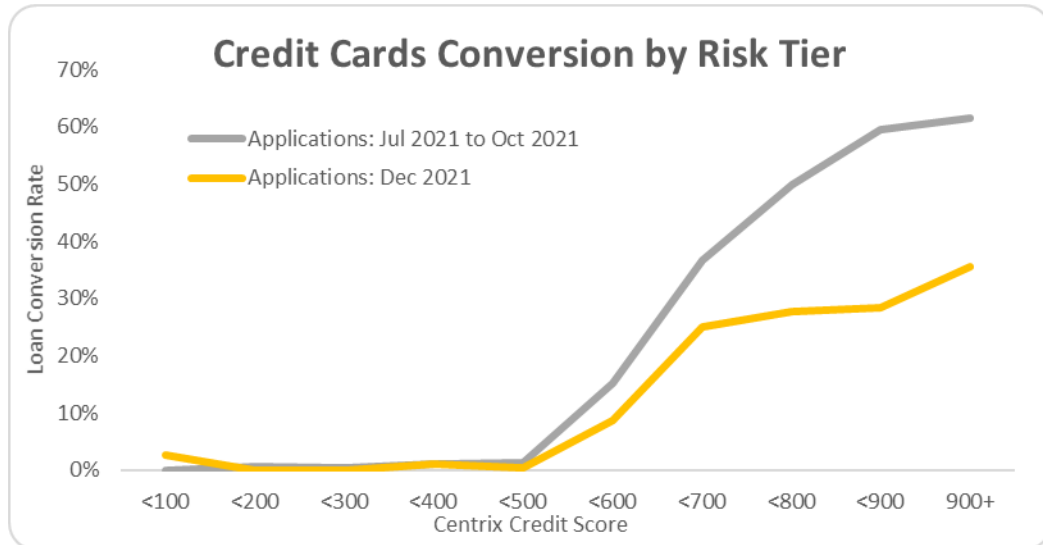
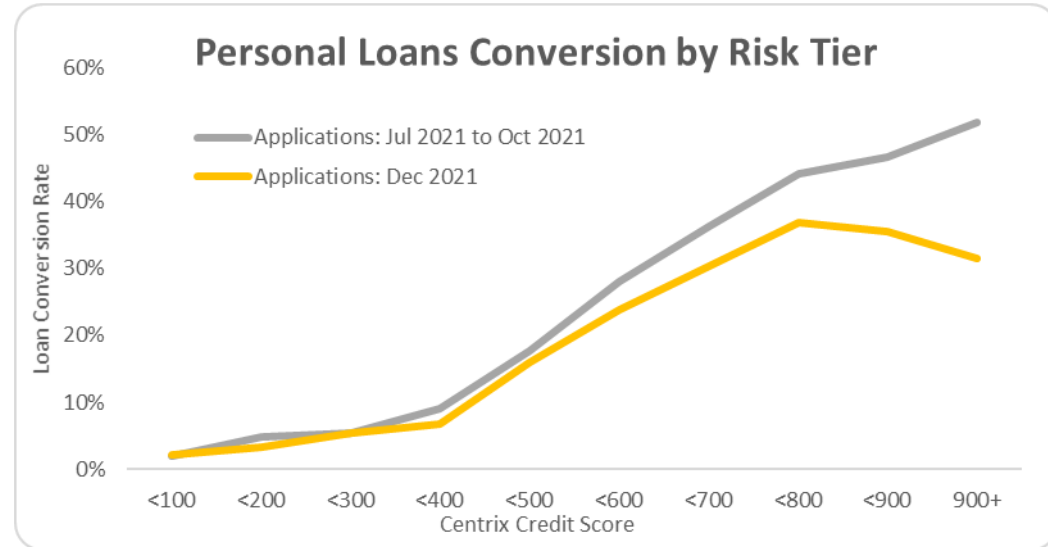
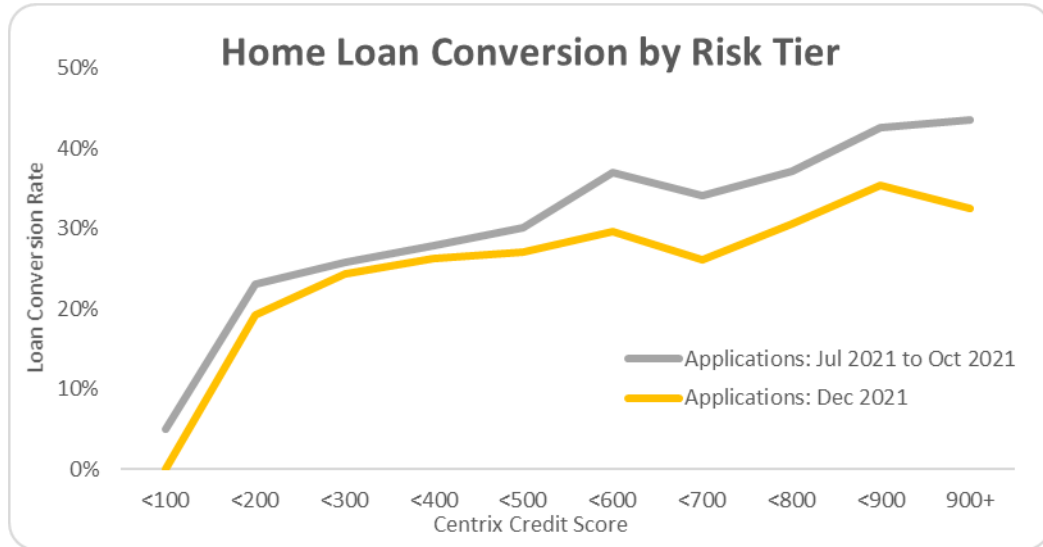
2020: Loan conversion rates

Conversion Rates	Home Loans	Credit Cards	Personal Loans	Auto Loans
Jan-20	33.1%	40.1%	30.9%	46.9%
Feb-20	29.1%	41.8%	30.1%	45.2%
Mar-20	24.6%	38.5%	21.0%	38.4%
Apr-20	28.3%	23.2%	11.4%	32.9%
May-20	34.4%	32.8%	27.6%	40.5%
Jun-20	35.9%	32.8%	29.3%	42.0%
Jul-20	36.0%	34.0%	30.4%	43.8%
Aug-20	35.7%	30.5%	29.3%	42.8%
Sep-20	35.2%	32.2%	29.9%	43.4%
Oct-20	36.3%	33.9%	30.9%	43.9%
Nov-20	36.2%	35.8%	30.6%	43.9%
Dec-20	36.2%	33.2%	33.7%	45.5%

2021: Loan conversion rates

Conversion Rates	Home Loans	Credit Cards	Personal Loans	Auto Loans
Jan-21	38.0%	36.0%	32.1%	45.0%
Feb-21	34.7%	32.7%	32.7%	43.1%
Mar-21	35.6%	33.2%	32.9%	42.8%
Apr-21	39.9%	35.1%	33.6%	43.5%
May-21	40.3%	34.3%	32.1%	43.3%
Jun-21	38.8%	33.2%	32.1%	41.5%
Jul-21	38.5%	32.3%	31.4%	42.5%
Aug-21	37.4%	29.6%	27.7%	36.4%
Sep-21	39.3%	30.8%	30.8%	42.7%
Oct-21	39.5%	32.1%	30.8%	43.2%
Nov-21	37.7%	30.0%	29.9%	42.4%
Dec-21	32.6%	19.5%	24.0%	36.3%

Appendix – loan conversion by risk tier by product



Our data

Centrix holds the richest dataset of consumer credit information available in New Zealand.

Our extensive and unique credit information database comprises of comprehensive credit information, utility data and supporting credit risk information aggregated from a wide range of sources.

Specifically our data comes from:

- ③ 71 registered banks and other contributors to Comprehensive Credit Reporting (CCR), providing payment behaviour data.
- ③ Contributors include finance companies, telco's and utilities.
- ③ Credit enquiries, when businesses or individuals apply for finance – indicative of real time credit demand.
- ③ Monthly snapshots of arrears trends and exposure (open accounts and credit limits).
- ③ Fintech providers such as Buy Now Pay Later (BNPL)
- ③ Payment history on more than 95% of individuals.

Questions?

Our team are here to help.

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CENTRIX
Credit Bureau of New Zealand



Table summarising concerns on CCCFA changes, potential options to address concerns, and impacts on those options

Concern				Option		Impact				
Name of concern	Context	Reference (Act, Regs, Code)	Issues raised (symptoms)	Option #	Description of option	Impact on customers protections	Impact on customers experience	Impact on lenders	Other commentary	
Specific issues related to expenses										
1	Excessive inquiries into 'other' outgoings	Lenders inquire into 'any regular or frequently recurring outgoings (for example, savings, investments, gym memberships, entertainment costs, or tithing) that are material to the estimate of relevant expenses and that the borrower is unable or unwilling to cease after the agreement is entered into or materially changed'.	Reg 4AE(d) Definition of 'listed outgoings'	This category captures outgoings that are not expenses (savings, investments), and results in intrusive inquiries into whether the borrower is willing to cease various regular expenses. It also could overestimate expenses where borrowers indicate that they will continue discretionary services that (if hardship arose) they would be prepared to forgo.	Option 1	Remove 'savings' and 'investments' from paragraph (d)	Minimal impact	+	+	Low impact overall
					Option 2	Narrow paragraph (d) and make it an objective test, e.g. 'any regular or frequently recurring outgoings that are material to the estimate of relevant expenses, excluding outgoings that it would be reasonable for lender to expect the borrower to cease to avoid substantial hardship'.	-	+	+	Closer to obligation in the Act
Confidential advice to Government										
2	Excessive inquiries into discretionary living expenses	Lenders must estimate the borrower's likely living expenses based on asking the borrower, reviewing bank transactions and/or using information they already hold.	Reg 4AK	Many lenders appear to be both asking the borrower and living expenses and also attempting to reconcile living expenses from bank transactions records. This results in unnecessary (and unintended) effort, and invasive inquiries of borrowers who are asked to explain bank transactions.	Option 1	Clarify that if borrowers are being asked about their likely living expenses, and these are benchmarked, there is no need to inquire into their current living expenses from recent bank transactions.	Minimal impact	+	+	Aligns with original policy intent.
3	Adjusting living expenses to remove discretionary components	Lenders must estimate the borrower's likely living expenses based on asking the borrower, reviewing bank transactions and/or using information they already hold.	Reg 4AK	Many lenders estimate living expenses based on bank transaction records (without asking the borrower to provide their own estimates). Bank transactions tend to overestimate likely living expenses, by including discretionary components, and these lenders feel unable to consider the willingness of borrowers to reduce discretionary expenses.	Option 1	Clarify that, if lenders have estimated living expenses from bank transaction records, 'asking the borrower about their relevant expenses' includes obtaining information about how relevant expenses are likely to change once the contract is entered into.	-	+	+	Aligns with original policy intent. Makes it more likely that lenders will get borrowers to agree to unrealistic cuts, though.
4	Ensuring that material experiences aren't missed	Lenders are required to ensure that information is "obtained in sufficient detail to minimise the risk of material expenses being missed or underestimated to an extent that is material to the estimate.	4AK(2)(b)	This obligation is driving a review of statement information to ascertain whether any expenses have been missed or underestimated to any material extent – adding time and difficult customer conversations to the lending application process. Results in multiple and manual reviews of transaction statements. Can be subject to seasonal variation and generates privacy concerns in order to comply with.	Option 1	Clarify that this requirement only relates to information received from borrowers (e.g. ensuring that expense categories on application forms are sufficiently detailed) rather than relating to information from bank transaction records etc.	Minimal impact	+	+	Aligns with original policy intent
Confidential advice to Government										
Require surplus, adjustments, and buffers uncertain or unnecessary										

5	Lack of clarity around 'reasonable surplus'	As part of assessing potential financial hardship lenders must conduct a full income and expense estimate for certain kinds of credit. This includes applying a reasonable surplus or buffer to address the risk of overestimation of income, underestimation of expenses, and/or other expenses.	Regs 4AF(2)(b)(i), Code	'Reasonable surplus' is not clearly defined. This means lenders have tended to be more conservative in calculation of a reasonable surplus value than they may otherwise need to be.	Option 1	Provide further clarification in the code on what a 'reasonable surplus' may entail. This could be supported by the provision of examples of formulas for calculating a reasonable surplus.	No impact	+	+	If lenders have greater clarity of a 'reasonable surplus', then they are likely to be less conservative.
					Option 2	Amend regulations and prescribe a reasonable surplus with a set formula, for example as a percentage of net income or a scaling of established expenditure.	No impact	+	+	The impact on consumer protection depends on the specific formula. The prescribed reasonable surplus could be informed through further consultation with lenders.
Confidential advice to Government										
Exemptions too narrow and uncertain										
6	Exception to general rule if obvious no hardship	A full affordability assessment is not required if 'it is obvious in the circumstances of the particular case that the borrower will make the payments under the agreement without suffering substantial hardship'	Reg 4AG	The 'obvious' threshold is ambiguous and difficult to apply, and the example in the Code suggests an excessively high test. This means that the exemption is not used in circumstances when it could be.	Option 1	Amend the Code to remove the example.	Minimal impact	?	?	Not clear whether this would change the use of the exemption on its own.
					Option 2	Amend the Code to adjust test for "obvious", e.g. the lender can demonstrate that it is obvious a responsible lender in the circumstances of the particular case would be satisfied it is more likely than not that the borrower will make repayments without substantial hardship, so as to make the inquiries required by regulation 4AF disproportionate	-	+	+	The proposed test was rejected during development of the regulations as being too low. If the lender makes minimal inquiries, it will statistically <i>always</i> be more likely than not that a borrower will make payments without substantial hardship.
Confidential advice to Government										
7	Debt Consolidation / Refinancing	A full affordability assessment is not required if the lender is replacing existing loans, they have with the borrower without granting new credit	Reg 4AH	This exception does not cover refinancing debt from other lenders, even if the refinance or debt consolidation would be in the customer's best interests.						
Penalties										
8	Liability	The Amendment Act included significant pecuniary penalties for breaching duties for directors as strong deterrent for non-compliance.	Act 59B and 103(1)	The pecuniary penalties for directors' duties [in combination with some ambiguity] has resulted in conservative interpretation of lending practices.						
Record keeping										
9			Act 9CA Code Part 5	Lenders have found the information requirements included in the Code as						

	Record keeping of inquiries	Lenders are required to ensure their records are fit for their intended purpose, including disclosure on demand to the Commission, dispute resolution service, the borrower, or guarantor		resulted in excessive information capture which consumes a large amount of time and is unnecessary.	Confidential advice to Government				
General concerns and cross cutting issues									
10	One size fits all	Regulations apply equally (with exceptions) to all lenders, loan types and loan sizes.		Many lenders consider that lesser requirements should apply to some lenders ('responsible' lenders) or smaller loans.	Option 1				
					Option 2				
					Option 3				
11	No lender discretion to give loans that fail affordability test	Likely income must exceed likely expenses, and in some cases a reasonable surplus	Reg 4AF	Lenders have previously given loans to borrowers whose likely expenses exceed their likely income, on the basis of case-specific judgement about what is affordable. This discretion is not permitted by the regulations, resulting in loan declines that lenders consider is not in the interests of borrowers.	Confidential advice to Government				

	Yellow options	Blue options	Purple options
Nature of option	Wording changes to regulations and code to allow for ease of implementation as the policy intended	Policy changes to regulations	Changes to policy intent
Time option will take to implement	Start of June 2022	6-8 months	12-18 months plus (depending on house time)
What option will take to implement	Code updated, No RIS	Regulation's amendment process	RIS etc, consultation, costs (FTEs), drafting time, House time,