Level 6, 330 Lambton Quay
PO Box 25332 (Featherston Street)
Wellington
Email: info@fincap.org.nz
Phone: 04 471 1420

www.fincap.org.nz www.facebook.com/fincapnz

20 April 2022

Submitted via: consumer@mbie.govt.nz

Competition and Consumer Policy
Building, Resources and Markets
Minister of Business, Innovation & Employment
Wellington

RE: Updated Credit Contracts and Consumer Finance Regulations 2004 and Responsible Lending Code Exposure Draft

Whānau should not face a position where lending that was always going to be unaffordable causes or compounds hardship. The onus must be on lenders to not disregard that collection on due repayments is likely to cause harm.

FinCap welcomes the opportunity to comment on the Ministry of Business Innovation and Employment (**MBIE**) Updated Credit Contracts and Consumer Finance Regulations 2004 and Responsible Lending Code Exposure Draft (**Exposure Draft**). Over many years financial mentors have seen endless examples of collection on loans that were always going to be unaffordable. This causes very avoidable but very significant harm in our communities.

The introduction of regulations relating to affordability assessment requirements under the Credit Contracts and Consumer Finance Act in December 2021 level the playing field. Any further clarification in regulatory or guidance changes must be extremely careful not to give the 'green light' for unfair lending practices. Even if such practices turn out to be misinterpretations and clear breaches, the harm caused would have been avoidable. It often takes unreasonable efforts from a whānau and their financial mentor to get anything close to timely and fair redress for the mess caused by irresponsible lending.

We expand on these comments in our responses to the consultation questions below.

About FinCap

FinCap (the National Building Financial Capability Charitable Trust) is a registered charity and the umbrella organisation supporting the 200+ local, free financial mentoring services across Aotearoa. These services support more than 70,000 people in financial hardship annually. We lead the sector in the training and development of financial mentors, the collection and analysis of client data and encourage collaboration between services. We advocate on issues affecting whānau to influence system-level change to reduce the causes of financial hardship.

Responses to consultation questions

1. Do you agree with the way that the draft Regulations are phrased? If not, what changes would you make?

The removal of two examples from 4AE(d) is straightforward for what officials have been instructed to do. We do not support any further rephrasing or removal of examples in this section of the regulation, if this is proposed by other stakeholders.

Gym memberships are often sold with break fees or other conditions that make them unreasonably hard for a person to cease for the purpose of freeing up cash flow. Financial mentors report frustration with these contracts and we consider it a systemic issue that needs further action for effective consumer protection. However, finding such solutions takes time and lenders should not be able to turn a blind eye to such issues.

We would also specifically make the point that tithing practices in relation to general wellbeing are not well understood and continue to need specific reference. This means a lender cannot claim ignorance is acceptable when collecting on a loan they have approved based on an assumption that tithing will cease without ever having discussed this with the borrower.

We also strongly recommend that lenders are reminded that every whānau has unique circumstances and that intentions around the purpose of certain savings or investments. These unique circumstances as to whether these would be forgone if the borrower was facing substantial hardship otherwise should be a matter for clarification in conversation with a borrower. Although removed as examples in regulations we recommend this reminder is placed in guidance.

We support the proposed amendment of regulation 4AK(2)(b) on the basis that our interpretation is correct. Our interpretation is that this clarification still means that a safeguard in verification of information supplied by an intermediary such as a car salesperson will prevent deliberate distortions of living expenses to meet requirements being put forward by those incentivised by commission-based selling. Although this is clearly unethical and illegal, it occurs too frequently and financial mentors mop up the mess, a safeguard is required.

2. Do you agree with the way that the guidance relating to expenses is communicated in the Draft Code? If not, how do you suggest it is improved?
We strongly support the inclusion of the drafted second and third lines of 5.4. It is essential that lenders are not guided to ignore clear inconsistencies in information that might indicate lending will likely cause substantial hardship.

Benchmarks can only do so much. Each whānau has a unique relationship with their money. Where such inconsistencies arise, there should be a conversation about why. It may simply be that a borrower was purchasing takeout food for leisure and plans to cut back to a reasonable benchmark for kai. However, we have seen examples where someone was working much more than full time hours between multiple jobs to make ends meet. For this person takeaway meals were a necessity to save time and be able to maintain income. Lenders should not be left to make assumptions about information that indicates there is a risk of hardship.

Financial mentors also report instances where lenders accept an estimate for food costs. When the mentor looks at the bank transaction information the lender had acquired it clearly shows no or very little spending on food. In these cases, this is because the whānau they assist were already receiving food support due to substantial hardship. This points to the need to remind lenders they cannot turn a blind eye to inconsistencies in information that could mean hardship is likely.

Some lenders have criticised the regulations and guidance, saying that discussions around expenditure with potential customers can be a point of tension. From the observations of FinCap and financial mentor's, there seems to be an issue with judgemental communication from lender's staff that is inappropriate. We regularly hear anecdotes of (and at times extremely) disrespectful comments from all types of lenders' staff about spending when financial mentors are negotiating hardship arrangements. It is therefore unsurprising that this might be occurring at the start of a loan too. An example might be callous comments about spending relating to addiction issues that stem from long term disadvantage or comments about a mistake made in spending while under significant pressure from overlapping social issues.

The proposed '5.6' drafting introduces guidance around discussions about future changes to discretionary spending. We recommend additional drafting that makes it clear that lenders must have systems in place to safeguard against salespeople 'coaching' answers ahead of an affordability assessment conversation. An example of such coaching could be a salesperson telling someone they should say they would 'cut back' on an expense when they have no way to do so. Consumer protections struggle to keep up with high pressure sales tactics and skilled salesperson will often take advantage of gratuitous compliance. We are unsurprised such high-pressure sales issues arise given flex commissions are almost uniform in some environments according to recent work by the Commerce Commission.[1]

In such a scenario an example might be questions on reduction of the payment of a mobile phone services where the potential borrower is in a contract that has a significant break fee if exited before the end of a three-year term. A salesperson might know this often 'trips up' a sale for them and pressure a vulnerable buyer to say their food costs are going to cut back by half which is unrealistic while giving no context about why they are being asked. They may also pressure the borrower to say they plan to change phone services when this isn't actually possible. The way lenders structure discussions on future expenses could undermine this becoming a systemic issue.

Financial mentors have strengths based, non-judgemental conversations with people about money every day and regularly recommend from their observations that creditors should have guidance on strengths-based communications. We put this forward as something that could be added to the Responsible Lending Code.

We would speculate that some reports in the media about potential borrower dissatisfaction with communication about their spending seem to have stemmed from intermediaries like mortgage brokers. This may be through misrepresenting the purpose of checks when trying to reduce the friction for earning a commission. Otherwise, conversations with lenders themselves could have been improved where the purpose of the communication is clear and any responses to whānau financial spending decisions are non-judgemental and professional about the relationship to affordability and suitability of a loan.

To be clear, overall we generally recommend that lenders are guided wherever there is doubt to have a discussion with borrowers about whether the loan they are seeking will likely lead to the life they want to live afterwards while being affordable as well as suitable. Such conversations can lead to clear understanding between both lenders and borrowers to avoid financial disaster or dissatisfaction due to unsuitable or unaffordable lending.

3. Should the guidance be limited to certain types of expenses e.g. food?

The phone plan issue discussed above could be another example for contrast. While some are on prepay arrangements and can easily adjust, a lender likely only sees a direct debit to a telecommunications company and could ask more questions. A reasonable question might be 'are you locked into regular repayments to a phone and internet company, or could you change to a plan with a lower cost while still getting the services you need if money became tight?'

---

[1] https://comcom.govt.nz/__data/assets/pdf_file/0037/269947/Motor-vehicle-financing-and-add-ons-review-10-November-2021.pdf

4. Are there other practices for estimating expenses that the Code should endorse?
We are generally comfortable with the general approach in the proposed drafting with adjustments for our above recommendations.

5. Is the new wording in the Draft Code on how lenders may apply a reasonable surplus to comply with regulation 4AF(2)(b)(i) relating to changes to expenses clear? If not, how do you suggest it is improved?
We find the proposed drafting of '5.19' clear and consistent with the intention of the clarification committed to. It is important that the link to 4AM(2)(b) remains so a lender does not miss that they cannot systematically reduce an initial estimate down to a benchmark. Doing so systematically would risk substantial hardship for borrowers when affordability assessments ignore unique circumstances.

6. Do you have any other proposals for additional guidance on surpluses?
No.

7. Is the updated guidance and examples on 'obvious' affordability helpful? Do the examples represent situations where affordability is obvious? If not, how could they be improved?
We consider the updated guidance in '5.26 a.' to be practical. It makes it clear that affordability assessments can be halted at a point where a lender is willing to accept the risk of assessing that affordability is obvious.

The onus should be on lenders to justify why affordability was 'obvious.' It is also the responsibility of regulators to take action where assessments are flawed, and lending is unreasonably risking or causing substantial hardship for borrowers.

We strongly support the draft guidance proposed in '5.27.' A credit check is not an appropriate substitute for an affordability assessment.

We recommend the following additions to the proposed example of 'Lender L, Borrower K and Borrower C' to avoid lenders not seeking some crucial information:

- The beginning of the case study should mention that Borrower K has made clear they do not anticipate any changes to their financial obligations or circumstances in the term of the loan.
- The $5000 personal loan discussed at the end of the example should also clarify that Borrower K has confirmed their circumstances have not changed at the time of the loan as well as that the lender has carried out relevant checks as to suitability.

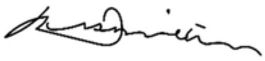
The above recommended additions remind lenders that checks should occur so that no anticipated changes in circumstances, like a new dependent or the end of a fixed term contract, mean that affordability isn't obvious. We are also concerned that the $5000 personal loan aspect of the example might mean a cohort of lenders now charging just below the threshold of now defined high-cost lending see an opportunity to ignore the unsuitability of their offerings to whānau.

8. Do you have any other proposals for additional guidance and examples for 'obvious' affordability?
No.

9. Would any of these initial changes require changes to lender systems before they could come into force? If so, what are the likely timeframes for making these changes?
Please also consider training time for community support workers like financial mentors if any changes mean the Commerce Commission must amend previous training.

Please contact either Jake Lilley on Privacy of natural persons or Janeka Rutherford-Busck on Privacy of natural persons to discuss any aspect of this submission further.

Ngā mihi,



Ruth Smithers
Chief Executive
FinCap