Consumer Policy Team, Ministry of Business, Innovation and Employment
Hon. Andrew Bayly, Minister of Commerce and Consumer Affairs

Monday 10 June 2024

Regarding Guidance for lenders on assessing affordability — Draft changes to the Responsible Lending Code Discussion Document

Introduction

Thank you for the opportunity for public comment on the Ministry of Business, Innovation & Employment's (MBIE's) *Guidance for lenders on assessing affordability: draft changes to the Responsible Lending Code Discussion Document* (Discussion Document).

We acknowledge the Minister's desire to enable quicker and easier access to suitable lending, particularly in the area of home loans.

This is a complex and important area. The potential consequences for the economy, lenders and individuals are large. Desire to reduce barriers to suitable lending must be considered alongside the desire to keep people from harm. The Responsible Lending Code (the Code) is an important document in keeping people safe from harm, particularly those who find themselves in situations of vulnerability at the time of and/or after taking a loan.

As we have noted previously, vulnerability isn't just a result of sustained hardship or long term poverty and/or low income. It also comes when borrowers are too tightly budgeted, and don't have the financial resilience to weather life events — changes in the economy, job loss, medical events, bereavement, etc. We need to consider not just protecting consumers experiencing vulnerability, but also note the way in which Government policies and lender products can increase the risk of creating vulnerability within consumers.

Overarching notes

We stand by our comments of 26 January (Notes following the roundtable discussion on CCCFA affordability regulations) and 6 May (Targeted consultation on the Credit Contracts and Consumer Finance Amendment regulations (No 2) 2024). We ask that you refer to those notes. There, we outline some of our concerns about the set of changes related to CCCFA and suggestions for mitigating harm.

One of the things we noted in those earlier papers was the speed with which early decisions about changes regarding the CCCFA were made, and the need to ensure promises are kept regarding later phases of change helping to mitigate harm. Consideration of the ways the RLC can help mitigate harm was and is important. We are concerned the proposed RLC does not protect against the new risks created for people who are experiencing or at risk of vulnerability. We are also concerned and disappointed that the pace of decision-making does not risks and mitigations to be properly considered and worked through.

Overall, we support the comments and recommendations in FinCap's submission, including their general comments and answers to specific consultation questions. We use that as the base for our submission, and add further notes as follows.

Responses to Consultation Questions

Q1. Do you have any concerns with changes proposed to paragraph 5.1, or other changes we should consider?

We support the comments and recommendations in FinCap's submission.

Q2. Do you have any concerns with any of the changes proposed to guidance on responsibly estimating the payments that will be required/made under the agreement?

We support the comments and recommendations in FinCap's submission.

Q3. Do you see any other guidance on this topic as desirable? If so, please explain

We support the comments and recommendations in FinCap's submission.

Q4. Do you have any concerns with the guidance proposed in paragraph 5.5? Is so, what changes should we consider?

We support the comments and recommendations in FinCap's submission. That said, we are reasonably comfortable with the wording that has been drafted.

Q5. Do you believe the Code should provide general guidance on use of surpluses, buffers and adjustments to account for uncertainty that the loan will be affordable? If so, what would you suggest it say, noting the potential for excessively conservative approaches by lenders.

We support the comments and recommendations in FinCap's submission. Good Shepherd works with clients who are on a low income, typically with very tight budgets. We (Good Shepherd) add in general buffer of $5-$10 per person per week.

Q6. Do you have any concerns with the changes proposed to guidance on inquiries into income, or believe we should consider any other changes?

We support the following comment in FinCap's submission:

"A lender should not be lending to a potential borrower in cashflow deficit or who will face this because of repayments. Borrowers should not be coerced into having assets secured in an agreement as the only means of making it affordable. Instead, they should be left to volunteer that they intend to pay by selling an asset, if the sale of that asset will not cause substantial hardship (for example a tradesperson's tools needed for income). The proposed guidance at 5.7.c. talks about means other than income which the borrower could use to meet payment under the agreement. MBIE should ensure it does not draft guidance that unintentionally encourages lenders to justify lending as affordable based on a borrower having to sell property or assets, when they intended to pay using regular income."

Like FinCap, we strongly support the proposed drafting at 5.8 in general. However, where FinCap recommends "it should be clearer through the deletion of the word '*consider*' and instead state that lenders *'should adjust any volatile, irregular or variable income'*", we believe 'consider' is appropriate. There are situations where variable income may be appropriate to use but lenders should be cautious.

We support the following comment in FinCap's submission:

"Often a borrower will have upcoming changes in their life that could significantly reduce their income. The person might be aware that they are coming to the end of fixed term employment, about to retire, be made redundant, or go on parental leave. These are part of a non-exhaustive list of known factors that could reduce a borrowers income and mean a loan repayment would cause substantial hardship. Guidance should also be included that reflects the current regulation 4AJ(2)(b) to ask the borrower about any likely changes in income. This is a reasonable action a responsible lender should undertake when inquiring about affordability."

Q7. What wording do you think would work best (in paragraph 5.9.c) to capture other, less essential expenses that may be important for the lender to account for?

We support the comments and recommendations in FinCap's submission.

Q8. Do you have any concerns with other changes proposed to guidance on inquiries into expenses, or believe we should consider any other changes?

We support the comments and recommendations in FinCap's submission. Good Shepherd already considers the suggested scope of 'utilities' in our lending decisions. This extra clarification of scope could help other lenders. Good Shepherd, or at the very least not excuse lenders from ignoring essential costs beyond power and water.

Q9. Do you believe guidance on joint expenses would be worthwhile. If so, would you have any issues with paragraphs 5.28 – 5.32 of the current Code being used?

We support the comments and recommendations in FinCap's submission.

Q10. Do you believe guidance on inquiring into spending through use of Buy Now Pay Later facilities is necessary? If we were to do this, would paragraph 5.33 of the current Code be a good approach?

We very strongly support the comments and recommendations in FinCap's submission: "Yes. Financial mentors report many whānau they support in substantial hardship having been regular users of Buy Now Pay Later loans. FinCap continues to recommend that these lenders be required to assess affordability under the relevant requirements of 9C(3) of the CCCFA."

Many low-income households rely on BNPL for everyday household costs, such as groceries. Further, BNPL debt is part of the unmanageable debt equation for many of our clients. It is important to take into account this form of spending and debt when assessing affordability.

It might be worth noting that our current credit policy, used to determine whether we can approve a loan, requires us to consider BNPL spending and does not allow us to consolidate BNPL debt. The main reason for not allowing this consolidation is the ease with which people can re-access BNPL finance. This highlights the prominence of BNPL in people's spending patterns and the significance of this easy-access finance on debt burden.

Q11. Would you have any concerns, based on the proposed guidance, about lenders making unreasonable assumptions that the borrower will reduce certain expenditure? If so, please explain why and what the Code might do to address this.

We support the comments and recommendations in FinCap's submission.

Q12. Do you have any concerns with the 2017 guidance on methods of inquiry? Please explain.

We support the comments and recommendations in FinCap's submission.

Q13. Do you believe further guidance on use of statistical information is necessary? If so, why?

We support the comments and recommendations in FinCap's submission.

Q14. Do you agree paragraph 5.14 is desirable to make lenders aware of their obligation under the Privacy Act 2020?

We support the comments and recommendations in FinCap's submission.

Q15. What might be the implications of using the 2017 guidance on verification? What changes, if any, would you suggest?

We support the comments and recommendations in FinCap's submission.

Q16. Do you have any other feedback on guidance relating to verification or use of information provided by intermediaries?

We support the comments and recommendations in FinCap's submission.

Q17. Do you believe the proposed guidance on extent of inquiries would encourage lenders to make their inquiries more proportionate to affordability risk, as intended? What changes might help to achieve this?

We support the comments and recommendations in FinCap's submission.

Q18.Do you have any other feedback on guidance to support lenders in assessing affordability risk and what that means for how they should approach inquiries?

We support the comments and recommendations in FinCap's submission.

Q19.Do you have any views on the need for guidance on record keeping and changes we should consider?

We support the comments and recommendations in FinCap's submission.

Q20. Do you have any views on the need for guidance on assessing affordability of high-cost credit and whether changes are desirable?

We support the comments and recommendations in FinCap's submission.

Q21. Do you have any views on guidance for assessing affordability in the case of pawnbroking?

We support the comments and recommendations in FinCap's submission.

Q22. Do you have any other feedback on how the draft content for Chapter 5 can better meet its objectives, including anything that might be missing?

We support the comments and recommendations in FinCap's submission.

Q23. Do you have any suggestions for how this content could be presented more clearly or usefully to users?

We support the comments and recommendations in FinCap's submission.

Example of client situation and lending assessment

Concerning affordability assessment leading to unsuitable unaffordable lending

Last year, we supported a client with a very challenging financial situation. This included the implications of a loan that, in our view, did not meet the expectations regarding responsible lending by that lender. Some of our concerns about that lending assessment included:

- Border income used in the affordability calculation is not evident on the bank statements.
- Clear evidence in statements of high cash spend - budget shows gross underestimation and unsatisfactory explanation.
- Omission of rent/mortgage payments although payments are evident in the bank statements.
- Food costs allowed for in budget significant underestimation based on actual spend in bank statements.
- Petrol costs allowed for in budget gross underestimation based on actual spend in bank statements.
- No allowance for vehicle expenses in the affordability calculation.

- Some other debts client was liable for have not been included in the affordability calculation.

The client had used a vehicle as security for the loan.

We requested the finance company to write off this debt and provide our mutual client with a full refund of all repayments made thus far. Our request was declined. We then escalated our concerns to the Insurance and Financial Services Ombudsman. Some remedies were required, but the Ombudsman was “regrettably” unable to go further. The client’s harm was not fully alleviated.

This is one example of where even the current Code does not sufficiently protect people in vulnerable circumstances from harm or further vulnerability. We are concerned the proposed changes in the Code will make it easier for lenders to provide unsuitable, unaffordable lending.

Further discussion

Please contact Emma Saunders, Chief Executive at Good Shepherd on or at emma.saunders@goodshepherd.org.nz to discuss any aspect of this submission. We will welcome the discussion.