New Zealand Banking Association
Te Rangapū Pēke

10 June 2024

Hon Andrew Bayly
Minister of Commerce and Consumer Affairs
Parliament Buildings
Wellington

By Email

CC: Paul Stocks
MBIE

Stan Christian
RBNZ

Dear Minister Bayly,

Phase 2 Financial Services Reform

The NZBA member banks thank the Minister for initiating a review of New Zealand's financial services legislation, including the Credit Contracts and Consumer Finance Act 2003 (**CCCFA**). We fully support the consumer protection elements of the CCCFA, and we welcome the opportunity to respond to MBIE's consultation on phase 2 of the financial services reforms.

However, we wanted to write directly to you regarding two issues that currently present the greatest barrier to banks providing access to consumer credit in a timely, efficient and safe manner. We consider that addressing these issues offers the greatest opportunity to improve the current regime for the benefit of all New Zealanders and want to bring them to your attention directly. We will also raise these points with MBIE in our response to their consultation.

We propose two primary changes to the CCCFA:

1. The retrospective repeal of section 99(1A) of the CCCFA which provides that a debtor is not liable for the costs of borrowing (interest and fees) in relation to any period during which the creditor has failed to comply with its initial or agreed variation disclosure obligations.
2. The repeal of section 59B, which requires directors and senior managers to exercise due diligence to ensure that the creditor complies with its duties and obligations under the CCCFA.

While there are other potential reform options (e.g., confirming the courts have discretion when granting relief by the retrospective application of s 95A), we consider that together, these two sections have driven unduly conservative lending practices due to the significant risks they create for lenders and the financial system, and therefore operate against consumer interests overall.

We summarise why these changes are necessary and appropriate below, and we have attached a detailed explanation prepared with the assistance of James Every-Palmer KC.

Section 99(1A)

We agree it is important that consumers receive accurate disclosure in relation to their credit contracts. A lender should be held responsible for errors in disclosure and required to compensate consumers for any harm caused. The CCCFA has appropriate protections to do just that. The issue with section 99(1A) is that, if the interpretation advanced by some parties is correct, it has added to the regime a disproportionate liability in respect of disclosure failures.

In a worst-case (but not fanciful) scenario, an error in a disclosure document, which has not caused any harm to consumers, could create a liability that threatens the solvency of the lender with adverse outcomes for depositors, shareholders, and the New Zealand financial system as a whole.

For example, suppose a lender makes a technical or drafting error or omission in its standard form disclosure statements for each contract in a $2 billion loan book. If that error persisted undetected for three years, at current interest rates the costs of borrowing could be around $500m.

On the “forfeiture” interpretation of s 99(1A) a potential half billion dollar liability is created that could easily threaten the solvency of the lender. As explained in the attachment, s 99(1A) was introduced in 2015 with little analysis and in circumstances where the CCCFA already provided for borrowers to be fully compensated for any harm and included penalties against lenders for disclosure errors. There was never a “gap” that required filling, and so the resulting financial stability risk is a regulatory mis-step.

In 2019, changes were made to the CCCFA in an attempt to mitigate the potential impacts of s 99(1A), but these are inadequate and do not fully address the solvency and stability issues. A retrospective repeal of this section is the only way to neutralise the potential financial stability risks caused by the introduction of s 99(1A).

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Section 59B

This section requires directors and senior managers to exercise due diligence to ensure that the creditor complies with its duties and obligations under the CCCFA. A failure to comply exposes the director/manager to financial penalties and liability (shared with the lender) for statutory damages and compensation to customers. A director/manager cannot be insured or indemnified for the penalties, or the legal costs of defending a penalty.

The MBIE discussion document recognises concerns that s 59B has led to unduly conservative lending practices. It raises particular complications for large lenders where the board's attention will appropriately be on governance matters rather than day-to-day operational matters. In addition, the risk of a personal action against a director or senior manager is a real disincentive to taking up such an appointment or supporting a lender to embrace innovation and flexibility in its approach to providing credit to consumers.

As explained in the attachment, there is a risk that directors become more risk averse and lenders decide not to offer innovative products (such as disclosure in alternative languages) due to potential CCCFA liabilities.

We consider the correct approach is for liability to sit at the entity level. This will still ensure lenders are motivated to comply with the Act, while directors and senior managers will still be liable to satisfy their duties to exercise reasonable care, diligence and skill, but reduce the motivation to adopt unduly conservative practices that are not in the best interests of New Zealand as a whole.

We trust that this letter will be of assistance to you in considering how phase 2 should be implemented We look forward to engaging further with you and MBIE to help deliver a fair, efficient, and effective regime to regulate financial services for the benefit of all New Zealanders.

Yours sincerely,

S9(2)(a)

[redacted]

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ATTACHMENT 1

Prohibited enforcement

Introduction

1. Section 99(1A) of the CCCFA provides that a debtor is not liable for the costs of borrowing (fees and interest charges) in relation to any period during which the creditor has failed to comply with its initial or agreed variation disclosure obligations.

2. It has been argued that, as well as preventing a creditor from enforcing fees and interest during a period of non-compliant disclosure, s 99(1A) creates a duty to refund any costs of borrowing received during this period. The MBIE discussion document refers to this as "forfeiture". While MBIE treats this as the black-and-white effect of s 99(1A), NZBA does not agree and notes that there are various issues in relation to the application of s 99(1A) that are yet to be tested in court.

3. NZBA considers that s 99(1A) should be repealed as it has created significant and unwarranted risks for lenders, and for the financial system as a whole. It considers that this should be with retrospective effect to June 2015.

The problem with s 99(1A)

4. Section 99(1A) has a troubled legislative history that is not explained in the MBIE discussion document.

5. It was introduced into the 2014 amendment Bill despite not being included in the preceding extensive consultation. The driver appears to have been a concern that recent Court decisions (the *Norfolk Nominees* litigation) meant that enforcement could occur in relation to a period of non-disclosure once corrective disclosure had been made, and that this was "unintended and could in some circumstances be unjust".

6. The first problem with this analysis is that *Norfolk Nominees* in fact reflected an orthodox reading of the CCCFA where a disclosure failure created only a *temporary* freeze on enforcement. This represented a careful balancing of the factors at play. The temporary freeze incentivised the creditor to ensure appropriate disclosure, and to correct any problems that arose. Separately, the creditor could be prosecuted for failures to make proper and timely disclosure. However, the temporary freeze was not intended to be punitive or leave the lender out-of-pocket. On the consumer side, the borrower was protected as they could still pursue statutory damages and compensatory orders and had a right of cancellation if initial disclosure had not been made.

7. Given this careful balance of incentives in the CCCFA, the desire to reverse the *Norfolk Nominees* decision is best seen as a hasty reaction to a problem that, on a more careful analysis, did not exist. That is, the ability to enforce after corrective disclosure (and to retain interest and fees already paid in relation to this period) was neither unintended nor unjust. Instead of patching a gap, s 99(1A) (as interpreted by MBIE) cuts across the detailed and carefully calibrated regime in the CCCFA.

8. The second problem is that, if the interpretation advanced by some parties is correct, s 99(1A) has created a draconian regime with disproportionate liability in respect of disclosure failures. In a worst-case (but not fanciful) scenario, s 99(1A) could create a liability that would put the lender in financial jeopardy for a widespread error, even if the error was inadvertent and had not caused any harm to consumers.

9. We agree it is important that consumers receive disclosure in relation to their credit contracts. However, it cannot be said that requiring the creditor to write off interest and fees over the relevant period is a proportionate response in each case where there is a disclosure failure. For example, the failure may be inconsequential to the consumer.

10. Given the remedies available to a consumer who has been prejudiced by a breach of the CCCFA (statutory damages, compensation orders and, in relation to initial disclosure, a right of cancellation), a refund of interest and fees is unnecessary from a consumer protection perspective.

11. In these circumstances, we consider that making the loan interest free is a windfall gain for the consumer, and disproportionate and punitive for the lender.

12. It cannot be overstated how disproportionate the impact on the lender could be. Suppose that a moderate sized lender makes a technical or drafting error or omission in its standard form disclosure statements for each contract in a $2 billion loan book. In practice, disclosure problems can persist for an extended period without being detected, particularly when the impact on the consumer is minor. Assuming a three-year period for a minor disclosure issue, at current interests rates the associated costs of borrowing could be around $500m. It is also important to note that the costs of borrowing include any interest on the loan, even though the lender has likely paid away a portion of that interest to depositors. This means the lender may well be paying back more than its net interest margin, e.g. more than it has earnt on the loan, leaving it out of pocket.

13. In such a scenario, the lender would be faced with a potential liability that could put it in breach of its capital ratios or other prudential requirements, or even threaten its solvency. Indeed, the costs of borrowing amounts have the ability to undermine an otherwise sound lender's balance sheet and threaten its solvency with adverse outcomes for depositors, shareholders and the financial system as a whole.

14. Section 99(1A) therefore creates a genuine financial stability risk to New Zealand for no meaningful benefit to consumers.

15. MBIE's discussion document suggests that the rationale for s 99(1A) was to "ensure lenders do not profit from borrowing decisions that were based on incomplete information". This rationale appears to be a recent construct not advanced in previous reviews. However, in relation to initial disclosure, the goal of preventing unwarranted benefit to creditors is already met by statutory damages, compensatory orders and the right of cancellation. Enjoying the benefits of a loan without paying any interest or fees goes much further than ensuring lenders do not profit as they are by definition left out of pocket. This explanation is also inconsistent with s 30(2) of the CCCFA which provides for a borrower to pay interest and reasonable expenses where it exercises a right of cancellation including due to a failure to provide initial disclosure. And, in relation to agreed variation disclosure, the rationale does not apply at all since the disclosure records what was agreed and no borrowing decision is based on the subsequent disclosure of the particulars of the change.

The "just and equitable" discretion in s 95A does not resolve these problems

16. An attempt to ameliorate the potential impacts of s 99(1A) was made in 2019. Section 95A was introduced to allow a creditor to apply to the courts to make a "just and equitable" reduction to this potential liability.

17. This was, however, an inadequate response to the problem created by s 99(1A). First, s 95A does not fully address the potential solvency and stability issues. Taking the example above of the lender with a $500m costs of borrowing issue, the immediate issue is how to treat this in terms of reserve ratios and prudential requirements. Here, disagreement over the effect of s 99(1A) may be compounded by different views as to what must be included in agreed variation disclosure (the Regulation 4F issue) and what constitutes corrective disclosure to bring a period of non-compliance to a close. The existence of the broad discretion in s 95A as to whether and how to reduce this liability if it eventuates does not significantly ease these issues. Indeed, the very act of applying for relief proactively could itself exacerbate a situation requiring very careful management.

18. Secondly, relief is only available in respect of fees and charges incurred after 20 December 2019. Accordingly, it provides no solution to the period from June 2015 to December 2019.

19. Despite it being recognised by MBIE since at least 2016/17 that forfeiture could be unjust, disproportionate and have highly damaging consequences, the risk remains today. We strongly urge the present Government to finally resolve this issue.

NZBA's proposal

20. In light of this history and the perverse solvency and financial stability risks created by s 99(1A), NZBA proposes that s 99(1A) is removed with retrospective effect from June 2015. As an alternative, it could be removed with prospective effect only, but s 95A extended back to June 2015. However, given the problems with s 95A in practice this is a very much less preferred option.

A retrospective fix is appropriate and required in the circumstances

21. It is uncommon for legislative amendments to apply retrospectively. However, here it is the only way to neutralise the financial stability risks caused by the introduction of s 99(1A).

22. As already noted, the courts have not yet considered whether the forfeiture interpretation of s 99(1A) is correct. NZBA considers that it is not correct, so it is possible that the stability risk does not arise on the correct interpretation of the CCCFA. However, tens of millions of dollars would be spent on legal proceedings to determine this. There is also a real risk that any judgment resulting from a particular set of facts would be limited to those facts and would not provide the certainty needed for other lenders or the sector as a whole. The present situation of ambiguity is caused by legislation and is best resolved by legislation. Accordingly, it should be dealt with once and for all through the retrospective removal of s 99(1A).

23. In a 2017 discussion paper, MBIE raised concerns with fixes applying retrospectively. First, MBIE was concerned that debtors would be prejudiced by making the change fully retrospective. Secondly, MBIE suggested full retrospectivity may allow creditors who have already settled with the Commission to attempt to "undo" the settlements.

24. In our view, debtors would not be prejudiced by making the change retrospective. The amendment would not affect a debtor's entitlement to statutory damages or the Court's power to award additional compensatory damages. Accordingly, debtors would not suffer loss or damage as a result of the amendment being made retrospective. All that debtors would lose is the chance of receiving a windfall. In terms of past settlements, NZBA does not consider that the change would provide a basis for reopening these settlements. A party entering a "full and final" settlement assumes the risk that its true legal position might turn out to be different based on facts that later become known, subsequent judicial decisions or the actions of Parliament including retrospective legislation.

25. MBIE has put forward two other options. In terms of the possibility of limiting s 99(1A) to material breaches (option E1), the difficulty with this is that it leaves an open-ended issue (materiality) to be determined by litigation and even if the disclosure issue is material, the liability may still be disproportionate. In terms of putting a limit on a lender's total liability under s 99(1A) for a single disclosure error (option E2), it is difficult to see

how this could be allocated between borrowers and would result in contention about whether there was one or several disclosure errors in a particular situation, with each giving rise to its own cap.

Removal of s 99(1A) does not leave a gap in the CCCFA

26. NZBA supports consumers being compensated for any harm caused by errors in disclosure. It considers that the CCCFA already provides for such compensation outside of s 99(1A). In particular, consumers:

    a. have a presumptive entitlement to statutory damages of 5% of the loan amount capped at $6,000 (with the court having a discretion to make a just and equitable adjustment);

    b. can claim compensation for any loss or damage (to the extent that any statutory damages that are to be paid do not adequately compensate the person for the loss or damage);

    c. in relation to a failure to make initial disclosure, can cancel the contract; and

    d. can claim damages and compensation for any harm caused by a breach of the lender responsibility principles which are also likely to be relevant to any significant disclosure failure.

27. These provisions allow the consumer to be compensated for any loss that they suffer.

28. The MBIE discussion document contains the Commission's view that some lenders only began paying due attention to their disclosure obligations because of s 99(1A). It is not clear what evidence supports that view and in any event we do not agree. Moreover, even if it was correct, we do not consider that an entire industry should be regulated according to the actions of outliers. We consider that the CCCFA contains ample incentives for compliant disclosure without s 99(1A).

29. First, the corollary of the consumers' rights to damages and compensation is that the creditor has a strong incentive to provide compliant disclosure.

30. Secondly, a creditor who fails to make compliant disclosure is subject to other potential penalties under the CCCFA. In particular:

    a. it commits an offence and is liable for a fine of up to $600,000 under s 103; and

    b. civil pecuniary penalties were introduced in December 2019 and, while failures of initial or variation disclosure do not directly come within this jurisdiction, contraventions of the lender responsibility principles do and, as noted above, any significant disclosure failure may also be a contravention of the lender responsibility principles.

31. Thirdly, a range of other orders are available to deal with a recalcitrant lender include banning orders under s 108.

32. To the extent that there is a concern that these measures provide insufficient deterrence, the answer would lie in adjusting the parameters (for example, increasing the maximum fine) or introducing a civil pecuniary penalty directly for disclosure failures. The answer does not lie in s 99(1A) or any modified application of s 99(1A), which was simply a false step.

Liability regime for directors and senior managers

The problem

33. Section 59B of the CCCFA requires directors and senior managers to exercise due diligence to ensure that the creditor complies with its duties and obligations under the CCCFA. A failure to comply exposes the director/manager to a civil pecuniary penalty and/or shared liability with the lender for statutory damages and compensatory payments. Indemnities and insurance for civil pecuniary penalties imposed on directors/managers are prohibited by the CCCFA (including the legal costs of defending a penalty) by ss 107D and 107E. The relevant sections came into effect on 1 December 2021.

34. The MBIE discussion document recognises concerns that s 59B has led to unduly conservative lending practices and that it raises particular complications for large lenders where the board's attention will appropriately be on governance matters rather than day-to-day operational matters.

35. The common experience is that the CCCFA gives rise to a number of complex questions relating to affordability assessments, disclosure obligations and remediation processes if problems are found. This means that there is a great deal of judgement and balancing required. Directors and senior managers are also conscious that their actions will be judged with hindsight, and in circumstances where they may not have had direct involvement or detailed knowledge of these day-to-day operations. Given all these uncertainties (and uncertainty as to how the regulator will treat a particular issue), the argument that due diligence is not an onerous standard does not carry much weight and the threat of personal (and uninsurable) liability can result in unduly conservative settings.

36. As a result, there is a tendency for lender boards to approve recommendations of defensive behaviour from management (for example, in relation to affordability assessments) even though this may not be in the interests of consumers. In addition, the risk of a personal action against a director or senior manager is also a disincentive to taking up such an appointment as a director or senior manager.

37. We have seen many instances of this playing out in practice:

a. As evident from the Institute of Directors surveys, directors are becoming increasingly concerned about potential personal liabilities and becoming more risk averse in business decision-making.

b. Some NZBA members have decided not to offer innovative products (for example, disclosure in alternative languages) due to potential CCCFA liabilities.

c. The need for the Credit Contracts and Consumer Finance (Exemption for Emergency Relief) Amendment Regulations 2023 in light of the 2023 weather events illustrates that affordability assessments have become unduly conservative and inflexible.

NZBA's proposals

38. The two reform options considered by MBIE are to: remove the prohibition on indemnification and insurance (A1); and/or remove the due diligence obligation for licensed lenders (A2).

39. NZBA considers that removing the prohibition on indemnification and insurance represents a bare minimum level of reform If it is simply removed, then only the general restriction in s 162 of the Companies Act would apply and indemnification and insurance will generally be permissible (including for past events). The issue was recently considered at Select Committee in relation to the Deposit Takers Bill and the recommendation, which became part of the Act, was to remove any special restrictions on insurance and indemnities.

40. NZBA considers that removing the prohibition on insurance and indemnities does not remove the incentive to comply with the disclosure requirements. Allowing insurance and indemnities would reduce unduly conservative behaviour, but at the same time directors and senior managers would have professional and reputational reasons to continue to discharge the due diligence duty. In addition, the cost of indemnities and insurance (including excess/deductibles) would incentivise lenders to put controls in place to ensure that the due diligence obligations are met and those protections are not drawn upon.

41. While removing the prohibition on insurance and indemnities would improve the current position, NZBA questions whether s 59B should remain at all.

42. The potential extent of personal liability of directors has increased significantly over the last decade. NZBA considers that the correct approach is to impose liability at the entity level. Imposing personal liability risks putting a thumb-on-the-scales in favour of unduly conservative practices and away from competitive and innovative behaviour.

43. Accordingly, NZBA's preferred approach is to simply repeal s 59B.

Hon Andrew Bayly

Minister of Commerce and Consumer Affairs
Minister for Small Business and Manufacturing
Minister of Statistics

3 July 2024

S9(2)(a) [redacted]

CCAB 2425-005

S9(2)(a) [redacted]

NZBA letter on Credit Contracts and Consumer Finance Act 2003 (CCCFA) disclosure penalties and director due diligence provisions

Thank you for sending the letter on 10 June 2024, from S9(2)(a) [redacted] S9(2)(a) [redacted] regarding the New Zealand Banking Association's concerns on the CCCFA disclosure penalties and director due diligence provisions.

As you know, these matters are in the scope of phase two of the financial services reforms.

I am currently considering options to address the unintended consequences section 99(1A) of the CCCFA, and due diligence provisions have on lenders and consumers (liability and penalty risks are leading to overly conservative lending practices that could potentially increase costs, reduce appropriate access to credit, and hinder innovation).

I understand that you raised your concerns and preferred approach to address these respective matters in your response to MBIE's consultation on phase two of the financial services reforms.

I appreciate your active participation in this reform process, and your feedback is being duly considered as part of the policy options analysis. I encourage you to continue engaging with my officials.

Thank you for sharing your concerns.

Yours sincerely

Hon Andrew Bayly
Minister of Commerce and Consumer Affairs

MBE/NZBA 12, 7, 24

s 99(1A).

9(2)(b)(ii)

- Ants'
- James E-P.

- Risk is not theoretical 'grey swan'.

- class funder seeking s 9(2)(b)(ii) in ASB + ~~A~~NZ class action.

Prudential risk: Big bank, small bank, build~~es~~ing societies.

Note of clarification - example given was a loan book of 100, 000 loan of $300k each with an interest rate of 7 per cent.

lender book of ~~$~~100k loans

$321k p/loan. breach

→ return $2.1b

over 5 yrs

→ $10.5b.

s 9(2)(b)(ii)

Class action: still at proce~~e~~dural stage: ANZ 2yr

ASB 5yr

variation disclure

Note of clarification - ANZ 1 yr, ASB 5yr.

Note of clarification - ANZ's breaches were not for the entire 2015-2019 period.

- name of DR scheme wrong
- 3.5days late.
- 50c discrepency in payment amounts.

ASB + ANZ class action covers 2015 – 2019

Contingent liabilities

Pay ~~a~~ interest back to borrower interest margin 2-3%.

s 9(2)(b)(ii) [redacted]

s.95A – court: buying into full cost of borrowing argument, as opposed to debating this s 9(2)(b)(ii) [redacted]

s 9(2)(b)(ii) [redacted] FMCA stat damage.

Proportionality of other offences eg cartels - largest penalty $7.5M.

Fortitude as consequence argu → not right?

Argument that RLC covers these types of offences

S108 banning order directo

Issues still coming out w/ big 4. And mid-tier firms & just coming out.

Disclosure regime: Painful + expensive but s 99IA key.

C. Options for penalties for incomplete disclosures by lenders

Lenders argue section 99(1A) should be repealed, with some advocating for its retrospective repeal, while others believe the status quo is necessary to protect borrowers so should be retained.

Problem/opportunity

Section 99(1A) creates potential for disproportionate consequences (i.e. forfeiture of all the costs of borrowing) where a lender fails to make initial or agreed variation disclosure as required. Relief available under section 95A was developed to remove this risk, but has yet to be applied by a court, meaning lenders are still not certain they can avoid over-compensating borrowers.

Our assessment is that this is continuing to cause lenders excessive concern, which may translate to inefficiencies, and private litigation may create unnecessary costs where the disclosure failure was of no consequence to the borrower. We do not believe there is a historical problem that could justify retrospective repeal of section 99(1A), but you may wish to consider making relief under section 95A available retrospectively.

Options	*Advantages*	*Disadvantages*	*Recommendation*
Status quo (Option C1) Maintain the 2019 solution to this problem (relief provided by section 95A).	• Ensures borrowers are adequately compensated, with minimal costs/procedure. • Strong incentives on lenders to make proper disclosures and identify and notify any failures immediately.	• Although relief available under s95A is designed to make liability proportionate to harm, uncertain liability likely continues to produce some inefficiencies. • Possible costs of dealing with harmless failures.	**We do not recommend this option.** We believe the problem has not been fully addressed by the 2019 amendments. *Agree/Disagree/Discuss*
Option C2 Cap the percentage that can be forfeited, depending on the kind of failure, with discretion to remove/reduce liability further still available under section 95A.	Depending on how caps are set: • May slightly improve lender confidence forfeiture won't be disproportionate, which may reduce inefficiencies. • Lenders better assess their liability.	• Depending on how caps are set, there is risk they prevent adequate compensation of borrowers in some cases. • Adds some complexity, even though caps would be clear. • Doesn't address costs of dealing with harmless failures.	**We do not recommend this option.** We do not think it improves overall on the status quo. *Agree/Disagree/Discuss*
Option C3 C3(a): No section 99(1A) liability for disclosure failures that caused no prejudice to borrowers. Lenders would need to show no prejudice under s95A process.	• Likely to improve lender confidence no forfeiture required in harmless cases, which would reduce litigation costs and could address inefficiencies. • Fairness increased/more apparent. • Some potential for reduction in costs passed onto consumers.	• Borrowers and FMA may incur costs from greater likelihood of dispute over impact of the failure on borrowers, but onus still ultimately on lenders to make case for relief. • Some limited risk of reduced transparency by lenders where prejudice is debateable.	**We do not recommend this option.** We would expect this improve to improve very marginally on the status quo (lessen the problem with minimal downsides). *Agree/Disagree/Discuss*
C(3)(b): Affected borrowers (or the FMA on their behalf) face burden of convincing a court the failure caused prejudice.	• Further improves lender confidence no forfeiture required in harmless cases. • Reduced litigation costs for lenders with burden reversed, with some potential for reduction to be passed on to consumers. • Fairness of outcomes increased/more apparent.	• Burden of demonstrating prejudice means: ○ Higher litigation costs for borrowers would tend to be prohibitive which would be costly. ○ Reduced incentives for lenders to ensure complete disclosure and remedy failures where prejudice is debateable. Both could be mitigated to some extent by FMA intervention, particularly if option A2 is chosen.	**We recommend this option.** We think this option best addresses the problem without obviously undermining protections for consumers.
Option C4 Repeal section 99(1A), 95A and 95B, and consider increasing statutory damages instead.	• Fully addresses the problem. • Significantly reduces likely costs for lenders for each failure.	• Significantly reduces compensation that is likely for borrowers affected by failures (because statutory damages are not an automatic entitlement and must be actively pursued in each case). • Limited incentives to avoid disclosure failures and remedy them when they happen, meaning more borrowers likely to be affected. • This undermines transparency and fairness. • Additional litigation costs for affected borrowers – though more likely for the FMA intervening on their behalf.	**We do not recommend this option.** We would expect it to make outcomes worse than the status quo. *Agree/Disagree/Discuss*
Option C5 Retrospectively apply section 95A so that disproportionate liability from June 2015 is limited by availability of relief under that section. This would affect active proceedings (i.e. the class action)	• More likely than the status quo to provide judicial decision that reduces uncertainty about how section 95A operates to avoid disproportionate consequences. If this works out, it would: ○ enable lenders to more realistically (and, we would expect, less conservatively) assess their liability	• Only be effective in addressing uncertainty about relief available under s95A if the class action proceeds to judgment either while the Bill is before the House or after enactment. The main risk to this outcome is the class settling out of court or abandoning proceedings. • Legislation with retrospective effect is generally against the principles of good lawmaking and only justifiable when it is entirely to the benefit of parties affected. This option would reach back in	**Discuss.** This option could be considered in addition to others. It would better ensure proportionate outcomes for historical liability, but present weighty concerns and challenges. *Discuss*

as a way to test judicial application of section 95A. **Note: this option could be combined with any others (which only apply prospectively)**	○ put the Government in a better position to assess the possible need for improvements to these provisions. • Arguably more likely than the status quo to promote 'fair' markets for credit.	time to alter legal rights or duties to the disadvantage of affected borrowers who entered into these agreements based on the law that existed at the time. • Would raise constitutional issues, as it involves Parliament either changing the law that is actively being applied by the judiciary or overturning a judicial decision. LDAC guidelines suggest this would need to be "justified as being in the public interest and impairing the rights of litigants no more than is reasonably necessary to serve that interest." The strength of the public interest in this case is doubtful. • Procedural challenges (e.g. scrutiny by the Crown Law Office, LDAC, and the human rights vetting team at MoJ) and risks to navigate.	

D. High cost credit review

During consultation, stakeholders expressed opposing views. Lenders and industry bodies favoured maintaining the status quo, while consumer advocates preferred reducing the interest rate threshold to 30% (or even 20%).

Problem/opportunity

Section 45L of the CCCFA requires you to review the operation and effectiveness of the high-cost credit provisions. The review must consider whether the interest rate that defines a high-cost consumer credit contract should be reduced to a rate between 30% to 50%.

We are not confident that applying the high-cost credit provisions to loans with an interest rate between 30% to 50% would address the harm the provisions are intended to address.

Options	*Advantages*	*Disadvantages*	*Recommendation*
Status quo (Option D1) Maintain the interest rate that defines a high-cost consumer credit contract at 50%.	• Our review has found that the high-cost credit provisions have effectively addressed debt spirals and problem debts caused by this type of credit. • Financial mentors stated that borrowers are now turning to lower-cost credit alternatives (like interest-free loans – buy now pay later). • Our analysis did not find widespread harm that would warrant extending the provisions to interest rates between 30%-50%.	• An estimated 150,000 would-be borrowers are no longer able to access this type of credit (but can access other credit) because 12 former high-cost lenders exited the market, and nine restructured their products.	**We recommend this option.** *Agree/Disagree/Discuss*
Option D2 Expanding the definition of high-cost consumer credit contracts with interests above 30%.	• It would extend protections against excessive cost of credit, excessive debts and repeat borrowing to an additional estimated 171,000 would-be borrowers (however not all of them would have experienced financial harm caused by these loans).	• Little evidence of financial harm caused by these loans that high-cost credit provisions could address (only 11% of cases closed by FinCap's financial mentors since January 2024 involved debt to a lender in this interest rate range). • Would affect an estimated 24 lenders that would either comply (very unlikely), restructure their loan products (by increasing loans' minimum value or terms) or exit the market. • Likely to increase costs for lenders (if they comply or restructure their offers) and the regulator (as different rules would apply to more lenders). • We heard that high-cost lenders would have difficulty accessing transactional banking facilities. • Likely to reduce access to short-term credit, tighten lending criteria, and harm competition in the consumer lending market.	**We do not recommend this option.** As part of this option, we have considered amendments to other high-cost credit provisions to mitigate identified risks. However, our recommendation remains unchanged. The risks outweigh the benefits given the evidence we have. Issues we heard about vehicle finance could not be addressed under this option as interest rates of vehicle loans are typically under 30%. *Agree/Disagree/Discuss*

In Confidence

Office of the Minister of Commerce and Consumer Affairs

Cabinet Economic Policy Committee

Financial Services Reforms: policy decisions

Proposal

1 This paper seeks policy decisions on a package of proposals to streamline and ensure the effectiveness of financial services regulation.

Relation to government priorities

2 The proposals in this paper respond to:

2.1 the Coalition Agreement between the National Party and the ACT Party to 'Rewrite the Credit Contracts and Consumer Finance Act 2003 (CCCFA) to protect vulnerable consumers without unnecessarily limiting access to credit',

2.2 the commitments to reform financial services regulation in the National Party's 100-point plan for rebuilding the economy, and

2.3 the Government's commitment to cut red tape and provide regulatory clarity to make it easier to invest and grow New Zealand's capital markets.

Executive Summary

3 In May 2024, Cabinet approved the release of a package of discussion documents [CBC-24-MIN-0031 refers]. These documents set out options for reforming the financial services regulatory landscape, with the objective of reducing red tape and compliance burden. Cabinet also invited me to report back by August 2024 with the outcomes of the consultation and proposed policy changes.

4 Following consultation, I am now seeking agreement to several policy proposals, some of which will require amendments to legislation.

5 In relation to *Fit for purpose consumer credit legislation,* Cabinet's decision to transfer responsibility for consumer credit from the Commerce Commission (the Commission) to the Financial Markets Authority (FMA) raises questions of whether the current consumer credit regulatory model is still appropriate and if the requirements are proportionate for lenders. This paper sets out my proposals. My proposals are to:

5.1 Regulate consumer creditors via a single market services licence, to simplify and streamline current regulatory arrangements.

5.2 Remove the due diligence duty and attendant personal liability for senior managers and directors.

5.3 Retain the consequences for failure to make initial disclosure or disclosure of agreed changes, but only where the borrower or the FMA can show the failure caused harm.

6 I also have a statutory obligation to review rules in the CCCFA that apply to high-cost credit. Following public consultation, I am not proposing any changes.

7 I also seek agreement to exempt Buy Now, Pay Later (BNPL) providers from the fee requirements in sections 41 and 44A of the CCCFA, with conditions that permit reasonable cross-subsidisation for defaults by other borrowers. This exemption reflects that the current fee provisions in the CCCFA are likely to constrain how BNPL providers calculate and charge default fees and could put their businesses in jeopardy.[1] The conditions I am proposing are aimed at providing bespoke protections against excessive default fees and future-proofing against potential unreasonable fee increases by BNPL providers. An alternative (which the Minister for Regulation prefers) is to exempt BNPL lenders from these fee requirements without any conditions. This approach would provide BNPL lenders with more flexibility in setting their default fees, but would not provide adequate protection for consumers. Furthermore, the regulator would be unable to take action if concerns about excessive fees arose without returning to Cabinet to seek necessary changes to the fee provisions (and any changes would not apply retrospectively).

8 In relation to *Fit for purpose financial services conduct regulation,* several legislative reforms have been made to financial markets conduct regulation over the past decade. While this has improved conduct and outcomes, it has also led to a complex regulatory landscape and some unnecessary compliance costs. I therefore propose to:

8.1 Simplify and clarify minimum requirements for fair conduct programmes.

8.2 Retain the current open-ended definition of the fair conduct principle.

8.3 Require the FMA to issue a single licence covering different classes of market services, including for consumer credit where applicable.

8.4 Allow the FMA to rely on an assessment made by the Reserve Bank of New Zealand (RBNZ) in some circumstances.

8.5 Introduce change in control approval requirements.

8.6 Introduce on-site inspection powers for the FMA.

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[1] BNPL providers do not charge interest or other fees to consumers – except default fees. One BNPL provider considers that the default fee provisions in the CCCFA will limit it from charging late fees of more than $2, which it says is not suitable for its model and would require it to increase merchant fees (which is not possible while merchant contracts are running) or introduce interest charges.

9 I am also seeking agreement to progress some minor and technical amendments to the Financial Markets Conduct Act 2013 (FMC Act) and its associated regulations. Although these minor and technical amendments have not come out of the consultation process itself, they are related to the package in that they will also help to reduce red tape and regulatory burden.

10 In relation to *Effective dispute resolution,* financial dispute resolution schemes are not as effective as they could be. I therefore propose to:

10.1 Enhance the process for reviewing the schemes.

10.2 Commission work to create a shared front door for all schemes.

11 I intend to return to Cabinet later this year to seek additional policy decisions, including on consumer credit, ahead of introducing a Bill in December 2024.

Background

12 On 25 January 2024, Cabinet noted my intention to reform the regulatory landscape for financial markets in two phases [CBC-24-MIN-0013 refers]. This package of reform will remove undue compliance costs currently imposed on financial services and improve outcomes for consumers. Reform of financial services regulation is needed because the succession of new rules and requirements over the past decade has led to a duplication of the roles of the RBNZ and the FMA, unnecessary compliance burden for businesses, and overly prescriptive lending rules resulting in unintended impacts on consumers.

13 On 25 March 2024, Cabinet agreed to my proposals for the first phase of reforms, which have now all been delivered, namely:

13.1 exempting local authorities from the CCCFA, and removing duplicative reporting requirements from certain non-financial services – effective 25 April 2024,

13.2 revoking redundant exemptions from these regulations, relating to COVID-19 – effective 7 June 2024,

13.3 better aligning jurisdictional rules between the financial dispute resolution schemes – effective 18 July 2024, and

13.4 removing prescriptive affordability requirements from regulations made under the CCCFA, and updating guidance on assessing affordability in the Responsible Lending Code – effective 31 July 2024.

14 At that meeting, Cabinet also agreed to transfer all regulatory functions under the CCCFA from the Commission to the FMA [*EXP-24-MIN-0010* refers].

15 On 20 May 2024, Cabinet approved the release of the following three discussion documents and asked me to report back by August 2024 with policy proposals [CBC-24-MIN-0031 refers]:

15.1 ‘*Fit for purpose consumer credit legislation*’,

15.2 ‘*Fit for purpose financial services conduct regulation*’, and

15.3 ‘*Effective financial dispute resolution*’.

Proposals to ensure fit for purpose consumer credit legislation

16 MBIE received 37 submissions on the '*Fit for purpose consumer credit legislation* discussion document. My policy proposals are intended to promote an efficient and transparent credit market, ensure compliance costs are proportionate, and effectively protect the interests of consumers.

17 Access to credit can help consumers manage their living costs or support them in increasing their means but can also result in financial hardship. The following proposals will reduce the regulatory burden on lenders, while providing the FMA with effective tools to intervene where necessary to protect the interests of consumers.

18 I intend to come back to Cabinet later in the year to seek additional policy decisions.

I propose to transition consumer credit to a single market licence regime to simplify and streamline current settings

19 The FMA will be taking on new regulatory functions under the CCCFA. I propose that consumer credit providers no longer have to be certified. Instead, they will have to be licensed by the FMA. The FMA will have powers to monitor and take action against licensed consumer creditors that are the same as the powers it has for people who need a licence to provide licensed market services. These powers include the ability to set conditions on licences, censure, request action plans, give directions, require reports, and suspend and cancel licences.

20 I propose that the fair dealing and restricted communication provisions in Part 2 of the FMC Act apply to consumer credit rather than the Fair Trading Act 1986 provisions. The FMA can issue direction orders to address breaches of Part 2. The FMA can also order people to stop making restricted communications.

21 Applying this approach to consumer credit is consistent with my single licence proposal discussed below. It will enable the FMA to intervene early to better protect the interests of consumers and makes the regulatory landscape for credit more consistent with other financial services.

22 Creditors exempt from certification on the basis they are licensed by the FMA or RBNZ (i.e. all registered banks and non-bank deposit takers) will not be exempt from the requirement to hold a licence.

23 However, creditors currently exempt from certification under the Credit Contracts and Consumer Finance Regulations (e.g. vehicle dealers who have arrangements with a finance company) will be exempt from the requirement to hold a licence.

24 To make it easy for consumer creditors to transition to the new licencing framework, I propose to deem all existing consumer credit lenders who are either certified or exempt from certification (on the basis that they are licensed by the FMA or RBNZ) to be licensed, at no cost.

25 There are other possible changes I intend to consider to ensure the FMA has the flexibility to regulate the credit market effectively. This may result in me bringing further pragmatic and more technical proposals to Cabinet before introduction of this legislation.

Other proposals to enable an effective transfer from the Commerce Commission to the Financial Markets Authority

26 There will be some other changes necessary to facilitate the transfer, including incorporating provisions from the Financial Markets Authority Act 2011 (FMA Act) rather than the Commerce Act 1986 provisions. I propose to make additional consequential amendments where needed to avoid duplication or inconsistency.

27 As part of a smooth transfer process, I propose that the commencement, continuation, or enforcement of proceedings relating to the Commission's functions under the CCCFA may instead be carried out by or against the FMA without amendment.

28 Confidential advice to Government

I propose to remove directors and senior managers' due diligence duty and personal liability

29 I propose to remove the duty on directors and senior managers to undertake due diligence (section 59B) to ensure the lender's compliance with the CCCFA and the attendant personal liability. These settings contribute to overly conservative decision-making by lenders, which can negatively impact access to credit and increase compliance costs that are passed on to consumers.

30 The added scrutiny the FMA will be able to provide, through the proposed licensing model and other regulatory tools, makes the role of this duty and liability questionable. Directors and senior managers would still be personally liable where they were knowingly or deliberately involved in a contravention.

I also propose to retain the consequences for lenders failing to meet disclosure requirements but only where the borrower or the FMA can show the failure caused harm

31 The CCCFA requires lenders to disclose specified information to consumers to ensure they have what they need to make informed decisions before and during the loan. If the lender fails to do this, one of the consequences is that the lender is not entitled to the costs of borrowing until that failure is corrected (section 99(1A)). This applies only to initial and agreed variation disclosure.

32 Where the disclosure failure affected a large number of borrowers and was not discovered quickly, the scale of liability created by section 99(1A) could be significant (i.e. in the billions of dollars).

33 To address this, relief was made available from December 2019 to ensure any forfeiture is proportionate in view of the nature and effect of the failure and actions of the lender (sections 95A and 95B).

34 This relief is not available for disclosure failures that preceded the change in 2019. This means some lenders may have historical liability (from June 2015) that was not addressed. I understand there is a class lawsuit relating to this period that is currently before the court. It is being monitored by the RBNZ (as the prudential regulator of affected lenders), as the financial consequences could prove significant.

35 I propose to retain this form of liability for failure to meet disclosure requirements but ensure it only arises where the borrower or the FMA can show that the failure caused harm to affected borrowers. In practice, this would mean that section 99(1A) would only apply where harm was established; and sections 95A and 95B would then apply to determine forfeiture in a way that is proportionate.

36 This would continue to incentivise lenders to make sure they are properly disclosing information and remedying any failure to do so, while addressing the risk of excessive forfeiture for harmless failures. It would also transfer some litigation costs to affected borrowers or the FMA, should it intervene on the borrower(s) behalf. Although this could be seen as weakening protections for borrowers, the additional licensing and supervisory tools I have proposed above should enable the FMA to monitor disclosure practices and intervene effectively.

37 I have also considered whether lenders' concerns about historical liability for disclosure failures prior to December 2019 justifies retrospective intervention. Although backdating the relief could help to ensure a court is able to award proportionate compensation to affected borrowers, this change would raise constitutional and natural justice issues. As further analysis is required, I am not proposing any retrospective changes at this time.

I do not propose any immediate changes to the CCCFA disclosure requirements about the information that must be disclosed

38 I will continue to consider potential issues with requirements relating to variation disclosure and disclosure before debt collection. These disclosure requirements are subject to amendments proposed for Regulatory Systems Bills (one of which is currently before a Select Committee, [redacted] Confidential advice to Government [redacted]), which are expected to alleviate issues.

I propose to keep the annual interest rate that defines a high-cost consumer credit contracts to 50 per cent

39 High-cost consumer credit contracts are broadly defined as a contract with an interest rate of 50 per cent or greater. Additional requirements for high-cost credit contracts took effect in 2020 to protect consumers from the harm caused by accumulating excessive debts and repeat borrowing under these contracts. These include limits on the total costs of borrowing, a daily rate limit, restrictions to lend to some repeat borrowers, a prohibition on compound interest and a rebuttable presumption that default fees over $30 are unlawful.

40 I am required under the CCCFA to review the effectiveness of these provisions and consider whether the interest rate that defines a high-cost consumer credit contract should be reduced to a rate between 30 per cent and 50 per cent. The provisions have been very effective at reducing harm caused by the excessive cost of these loans, repeat borrowing and debt spirals as intended.

41 After public consultation, I propose to keep the interest rate at 50 per cent.

42 During consultation, I also heard about concerning debt collection practices. I am interested in exploring this issue further and will consider it in a review of the Fair Trading Act 1986, which I expect to commence next year.

43 I am also concerned that some lenders may be charging excessive default fees that do not comply with the CCCFA. My expectation of the regulator is that it works hard to identify breaches of the CCCFA and takes appropriate enforcement action where required. For default fees, this will mean that where borrowers do fall behind on their repayments, lenders should comply with the law.

I also propose to exempt Buy Now, Pay Later (BNPL) lenders from the fee requirements under the CCCFA

44 In October 2022, the then Cabinet Government Administration and Expenditure Review Committee agreed [GOV-22-MIN-0038] that BNPL contracts be declared to be consumer credit contracts under the CCCFA. The Regulations were made to protect BNPL consumers with more proportionate obligations on BNPL providers having regard to the nature of this type of credit and the lack of interest charged. The Regulations will come into effect on 2 September 2024.

45 I have heard concerns from BNPL providers that complying with the CCCFA's default fee provisions (sections 41 and 44A) would constrain how they calculate and charge default fees to an extent that could put their businesses in jeopardy. The CCCFA's default fee provisions limit default fees to reasonable amounts directly related to the costs incurred by the provider due to the default. These provisions were designed for traditional credit products that can recover other costs through interest charges.

Commercial Information

46 There are two options to mitigate this risk:

46.1 Option one: My preferred option is to exempt BNPL providers from sections 41 and 44A of the CCCFA, with conditions that permit reasonable cross-subsidisation for defaults by other borrowers. These conditions are aimed at providing bespoke protections against excessive default fees and future-proofing against potential unreasonable fee increases by BNPL providers. BNPL providers will also have to comply with section 41A that requires lenders to keep and review records about how default fees are calculated. This would enable the regulator to hold BNPL providers accountable for how they charge their default fees and to take action if it considers the default fees charged are excessive. This option is presented as option four (MBIE recommended option) in the *Regulatory Impact Statement Addendum: Buy Now, Pay Later Regulations.* Without these conditions, the regulator would be unable to take action if concerns about excessive fees arose without returning to Cabinet to make necessary changes to the fee provisions (and any changes would not apply retrospectively).

46.2 Option two: The Minister for Regulation's preferred option is to exempt BNPL providers from sections 41 and 44A of the CCCFA without any conditions. This would provide more flexibility and legal certainty to BNPL providers by not limiting what costs and losses can be recovered. However, this option would not provide any consumer protections against excessive default fees. If Cabinet chose this option, I would monitor the risk of excessive default fees, and if needed, come back to Cabinet in future to make necessary changes to the fee provisions. This option is presented as option five in the *Regulatory Impact Statement Addendum: Buy Now, Pay Later Regulations*.

47 Whatever the option chosen by Cabinet, the changes would be achieved by regulations made under section 138 of the CCCFA. Under both options, the Act and the Regulations will still apply to BNPL, requiring responsible lending practices, hardship policies, credit reports, and disclosure, ensuring protections to consumers and transparency of BNPL providers' policies.

48 Neither of the two options will come into force before 2 September 2024, when the current Regulations will take effect. I understand the Commerce Commission intends to take a pragmatic approach to enforcement in view of any position Cabinet takes on BNPL late fees.

Proposals to provide fit for purpose financial services conduct regulation

49 Officials received 37 submissions on the *Fit for purpose financial services* consultation document. Most submitters agreed that the overall approach and intent of New Zealand's conduct regulation was sound but that changes could be made to improve it.

50 I am now proposing changes to the Financial Markets (Conduct of Institutions) Amendment Act 2022 (CoFI Act), which will require banks, insurers and non-bank deposit takers (financial institutions) to comply with conduct obligations for the provision of core retail banking and insurance products and services to consumers. The CoFI Act is due to come fully into force on 31 March 2025; before this date, financial institutions will need to have applied for and obtained a licence from the FMA to continue providing these products and services to consumers. The changes I propose will streamline regulation and remove unnecessary compliance burden without impacting on the fair treatment of consumers.

51 I also propose making changes to improve the broader regulatory framework, including ensuring the FMA has effective monitoring powers.

I propose to retain the current open-ended definition of the fair conduct principle

52 The CoFI Act sets an overarching fair conduct principle (section 446C) that financial institutions must treat consumers fairly. The definition of what fair treatment includes is left open-ended. I consider that the current open-ended definition strikes the right balance between flexibility and certainty, and aligns best with the principles-based approach of the CoFI regime. It also aligns with the approach taken by other overseas jurisdictions, e.g. Australia. The fair conduct programme requirements in the CoFI Act will provide financial institutions with a high degree of certainty about what they need to do to comply with the CoFI Act.

I propose to simplify and clarify minimum requirements for fair conduct programmes

53 The CoFI Act requires financial institutions to establish, implement and maintain a fair conduct programme before applying for their conduct licence. The programme can include anything the financial institution considers relevant, but must include the minimum requirements listed in the Act (section 446J).

54 I believe it is essential all financial institutions have in place fair conduct programmes that cover the following aspects of their businesses:

- 54.1 How financial institutions engage appropriately with their clients and customers.
- 54.2 How financial institutions develop new policies and products to be fit for purpose and meet regulatory requirements.
- 54.3 Establishing transparent fee structures and charging arrangements particularly with intermediaries.

54.4 Development of an adequate complaints processes.

55 The CoFI Act largely covers the first two aspects, however I want to clarify that I consider it is necessary that fair conduct programmes should also include the following minimum requirements:

55.1 how financial institutions will apply, disclose and review fees and charges, and

55.2 how financial institutions record and resolve consumer complaints.

56 At the same time, I also want to reduce unnecessary prescription and compliance costs. Specifically, I propose to:

56.1 Remove the requirement that fair conduct programmes include policies, processes, systems and controls for enabling the financial institution to meet all of its legal obligations to consumers. This requirement is duplicative and has been perceived as requiring the 're-documenting' of existing procedures.

56.2 Adjust the requirements relating to training, supervising and monitoring employees. This will reduce prescription and clarify the purpose of these requirements (which is to ensure that fair conduct programmes consider how employees can be supported to ensure the financial institution fulfils its conduct obligations).

56.3 Remove the requirement to include methods for regularly reviewing and systematically identifying deficiencies in the effectiveness of the programme. The Act already requires that financial institutions "establish, implement and <u>maintain</u> effective fair conduct programmes".

56.4 Update the Financial Markets Conduct Regulations 2014 (FMC Regulations) to make equivalent changes to the minimum requirements for fair conduct programmes of Lloyd's managing agents, who have slightly different CoFI obligations due to the unique structure of the Lloyd's insurance market. They will differ to those applying to other financial institutions only to the extent necessary to ensure they are workable for the structure of the Lloyd's insurance market.

57 Importantly, I consider that while these changes will allow for more flexibility, they will not negatively impact on the fair treatment of consumers.

I propose to require the FMA to issue a single conduct licence covering multiple market services

58 Firms providing market services currently may need to hold multiple FMA licences (e.g. financial advice provider, manager of a registered scheme, derivatives issuer). CoFI will add an additional type of licence. Under the FMC Act, the FMA may issue different licences for each type of market service or alternatively may issue a single licence covering multiple types of market services. I have already set an expectation for the FMA to streamline its conduct licensing processes to reduce unnecessary compliance costs for firms, and the

FMA has indicated that it intends to move to the approach of issuing a single conduct licence.

59 The FMA can achieve this without legislative change, however there would be additional costs and difficulties that would arise (e.g. the FMA would potentially need the consent of each individual firm to consolidate existing licences). I consider legislative change to *require* the FMA to issue a single conduct licence covering multiple market services is necessary to enable a clean and efficient transfer to a single licence for all firms. The legislative change will provide a framework that supports the FMA to make operational changes to its licensing approach (e.g. to align standard conditions and regulatory returns) and will facilitate an efficient consolidation process for existing licences, avoiding costs and complexity for firms.

60 The majority of submitters supported making legislative amendments that would require the FMA to issue a single conduct licence covering multiple market services. The FMA also prefers this option as it avoids additional costs as stated above. Under this proposal, holders of existing licences under Part 6 would be deemed by legislation to hold a single licence.

I propose to enable the FMA to rely on an assessment by the RBNZ where appropriate

61 Both the FMA and RBNZ have regulatory oversight of financial institutions from their independent prudential and conduct perspectives. At times requirements may overlap; e.g. both regulators have an interest in the operational resilience of financial institutions.

62 I propose amending the FMC Act to provide the FMA with a broad power that, where appropriate, enables it to rely on work done or assessments carried out by RBNZ when assessing matters related to financial institutions. A reliance provision may be helpful if the proposed new FMA power for change in control approval requirements (discussed in paragraph 68) is agreed.

63 The consultation document also sought feedback on amending prudential legislation to introduce an equivalent provision allowing the RBNZ to rely on an assessment by the FMA. Submitters were generally supportive of this option, but amending prudential legislation is outside the scope of these reforms.

I propose to provide the FMA under the FMA Act with the power to conduct on-site inspections

64 I propose to provide FMA under the FMA Act with the power to conduct on-site inspections without prior notice. I intend for this power to be similar to the RBNZ on-site inspection power within the Deposit Takers Act 2022. This power would be used in limited circumstances (e.g. where giving notice would defeat the purpose of the visit or where urgency is required to prevent potential consumer harm), for the purpose of carrying out market conduct monitoring of financial market participants.

65 On-site inspections in these circumstances are a key part of the regulatory toolkit of conduct regulators internationally. The FMA's predecessor (the

Securities Commission) conducted on-site inspections and it was intended the FMA would be empowered to undertake them. However, a court decision in 2012[2] clarified that that this was not within scope of the information gathering powers that were translated across into the FMA Act.

66 I expect that the vast majority of on-site inspections would continue to be carried out with prior notice and the financial market participant's consent. The 'without notice' aspect of the power would only be used rarely, e.g. in circumstances where giving notice would defeat the purpose of the visit.

67 This power will be subject to the following safeguards to ensure the power complies with the New Zealand Bill of Rights Act 1990 and legislative guidelines relating to entering premises without a search warrant:

67.1 the FMA only being able to exercise the power at a reasonable time and in a reasonable manner consistent with the purpose of the power,

67.2 exclusions for inspections of private dwellings and marae, and

67.3 the FMA's authorisation of employees, or suitably qualified or trained persons, to carry out inspections.

I propose to introduce change in control approval requirements

68 Officials consulted on a proposal to introduce a change in control approval requirement for FMC Act licensed firms. This would mean that the prospective purchaser/owner of a firm would need to seek approval from the FMA in advance of the change in control taking place.

69 Currently, prudentially licensed firms require approval from the RBNZ in advance of a change in control. These firms do not need to seek approval from the FMA in advance. The FMA has advised that there have been instances where conduct issues regarding consumer treatment have developed as a result of changes made by new owners, and the FMA's ability to assess the change in advance and respond proactively has been limited.

70 Industry stakeholders generally opposed the introduction of these requirements due to concerns about regulatory burden and disagreeing that this power was relevant to the FMA's conduct remit, while consumer groups generally agreed that the FMA needs effective monitoring tools such as change in control approval requirements to prevent consumer harm.

71 I propose to introduce change in control approval requirements for firms licensed under Part 6 of the FMC Act. New Zealand's twin peaks model of regulation places equal importance on prudential and conduct considerations, and omitting the conduct assessment before a change in control takes place creates a regulatory gap. For example, a proposed transaction may comfortably satisfy prudential criteria (e.g. solvency) while still raising serious concerns about the post-sale treatment of consumers.

[2] *Perpetual Trust Ltd v Financial Markets Authority* (No 3) [2012] NZHC 2307.

I also propose a series of technical amendments to the FMC Act, FMA Act, and FMC

72 I also propose technical amendments to the FMC Act, the FMA Act and the FMC Regulations as set out in **Appendix 1**. These will cut red tape, improve the operation of the legislation and regulations, and reduce costs on business as well as costs to government. Changes to the FMC Regulations will be progressed through an Order in Council.

73 The minor amendments are in three areas:

73.1 Adjusting disclosure rules. I propose technical changes to the FMC Regulations to alter disclosure requirements in certain circumstances. For example, in response to industry concerns, I propose to extend the time within which managed funds must provide six-monthly statements to investors from 10 working days to 20 working days which will reduce compliance costs.

73.2 Regulatory change to embed certain FMA exemptions. I propose to make seven of the FMA's exemptions permanent by changing the FMC Act and FMC Regulations. Most of these exemptions have already been made for two five-year periods by the FMA and it is clear they are needed long-term, which is most efficiently done through regulatory changes. The exemptions relate to things like adjusting quarterly reporting requirements for schemes that are closed to new members and removing financial reporting requirements for notional schemes where the reports would have no meaningful information. The FMA has estimated this could avoid over $50 million in compliance costs per year for industry, as well as ensure resource savings for government.

73.3 Minor and technical changes that were to be progressed through the next appropriate legislative vehicle. These are minor and technical changes to keep the FMA Act and the FMC Act up-to-date. They include technical changes to terms or definitions and inconsistencies with the operation of the legislation.

Proposals to drive effective financial dispute resolution

74 Dispute resolution provides an important avenue for consumers to seek redress when issues arise with their financial service provider. Anyone providing financial services to retail clients must belong to an approved financial dispute resolution scheme. There are currently four approved schemes (the Schemes).[3]

75 The Schemes are not effective as they could be. Consumer advocates have pointed to inconsistencies in performance across the Schemes and consumer surveys have indicated there are inconsistencies in how effectively their services are reaching consumers (for example, while 49 per cent of consumers

[3] The Schemes are the Insurance and Financial Services Ombudsman Scheme, Financial Services Complaints Limited, the Banking Ombudsman, and the Financial Disputes Resolutions Service.

are aware of the Banking Ombudsman scheme, awareness of the other three schemes is much lower at 28 to 16 per cent).

76 Therefore, I consulted on:

76.1 options for improving scheme effectiveness, through measures which enhance accountability and consistency across schemes, and

76.2 options for improving consumer access and awareness of the schemes.

77 MBIE received 30 submissions on these issues, from the financial services industry, the Schemes, and consumer advocates and support organisations. I propose to progress with some actions now, and, as set out below, report back in later this year on issues relating to the governance of the Schemes, and key performance indicators (KPIs).

I propose to enhance the process for reviewing the schemes

78 The Schemes are required to undertake an independent review at least once every five years. The Schemes appoint different people to carry out these reviews, which happen at different times and under different processes.

79 Almost all submitters that commented on this issue noted that there should be greater consistency in how these reviews are carried out.

80 To achieve this, I propose providing the responsible Minister with a power to set terms of reference for these reviews (which can be used to ensure assessment against agreed KPIs), the form and manner of the resulting report, direct when they must take place, and determine the person who undertakes them. I expect the Schemes to continue to pay for the reviews.

81 This would allow government to approve a single reviewer, who could review all of the Schemes at the same time under a single process. I consider that this will result in more robust reviews, that better identify common issues and highlight where some schemes may be underperforming in relation to their peers. It may also better identify if there are issues requiring a scheme's approval to be revoked under the Financial Service Providers (Registration and Dispute Resolution) Act 2008 (FSP Act).

I propose to report back about governance arrangements of the Schemes

82 Each of the Schemes are private entities. They are governed by boards (and in one instance, overseen by an advisory council) which contain a mix of consumer and industry representation, headed by an independent chair. Government does not have the power to direct or appoint scheme board members.

83 Many consumer advocacy groups submitted that government should have a greater role in who sits on the scheme boards to ensure greater independence of the Schemes from industry. Most other stakeholders did not agree.

84 I have discussed this issue with the majority of the Schemes to better understand their views, and canvass options for changes in this area. In general, they have agreed that changes to their governance arrangements could be beneficial to help ensure greater scheme independence. I have also asked officials to undertake further work on options in this area. I plan to report back to Cabinet on this issue later this year. This report-back will note any changes the Schemes may voluntarily make, or if any legislative changes which may be required to address independence of governance arrangements.

I propose to report back on options for enhancing reporting measures

85 The Schemes report on a mix of performance measures through their annual report, including on average times for resolving cases, the outcome of closed complaints and common complaint themes.

86 I consider this reporting could be improved to be more consistent across the Schemes and to provide better insight into scheme performance. I have discussed this issue with the majority of the Schemes. They agree that KPIs could be improved and have indicated they are open to making changes in this area. I will report back to Cabinet on this issue later this year, including on any legislative or non-legislative action which may be required to enhance scheme KPIs.

I plan to request the Schemes improve consumer access and awareness of financial dispute resolution

87 Many submitters, including the Schemes, consumer advocates and some industry representatives noted there are barriers to consumers accessing dispute resolution schemes, including:

87.1 consumers lacking knowledge of their rights, and the availability of dispute resolution,

87.2 a perception that complaining would not make a difference, and

87.3 difficulties navigating complaints and disputes processes (particularly when the consumer may be suffering stress due to financial hardship).

88 The Schemes must comply with a principle of accessibility under the FSP Act. In accordance with the principle, the Schemes should promote knowledge of their services and make their scheme easy to use. I plan to remind the schemes of this obligation and request they improve efforts in this area.

I have also instructed officials to look into options to help facilitate access to the Schemes

89 One of the access issues highlighted by stakeholders is that the multiple scheme model is confusing, and makes it hard for consumers to know which scheme to use. I have engaged with most of the Schemes on this including options for an online portal to act as a “front door” to direct consumers to the correct dispute resolution scheme. They are supportive of the proposal. I am

mindful of the tight fiscal environment, and will be investigating options for industry to fund the service.

I do not propose to initiate work on consolidation of the dispute resolution schemes

90 Consumer advocacy and support agencies strongly recommended that the Schemes should be consolidated into a single entity. This was not something that was consulted on in the discussion paper.

91 Scheme consolidation would be a fairly major step, requiring greater consultation and analysis to fully assess benefits and costs. I am not proposing that government carry out this work now and would instead prefer to make the more immediate amendments proposed in this Cabinet paper. I am confident that these proposals will make meaningful improvements to financial dispute resolution.

92 I am also aware that two of the schemes have been discussing a proposed merger, which would be a step towards consolidation of the schemes. If this merger goes ahead, it will go some way to simplifying the current dispute resolution landscape.

93 I note that the issue of consolidation could be revisited in future, if evidence from future reviews of the schemes points to any major issues that would require assessment of the current scheme model.

Cost-of-living Implications

94 Access to credit can help consumers manage their living costs or support them in increasing their means but can also result in financial hardship when unaffordable. The proposals are intended to reduce the regulatory burden on lenders while ensuring the interests of consumers are effectively protected.

Financial Implications

95 In March 2024, Cabinet noted that I would recommend fiscally neutral transfers within Vote Business, Science and Innovation for 2025/2026 and outyears to give effect to the transfer of regulatory functions under the CCCFA from the Commission to the FMA [CAB-24-MIN-0101 refers].

96 Confidential advice to Government

97 This amount is based on the historic costs to the appropriation of running this function, deducing the contribution from third-party fees to these costs. In 2024/2025 the Commission has budgeted for $0.302 million in CCCFA costs to be met from third-party fees. As the FMA will not collect certification fees, it will have less funding for CCCFA costs. While the FMA will collect licencing fees, these will be used for the licencing system itself and it is unlikely this revenue will be able to be used for other CCCFA costs.

98 I intend to review the FMA's funding requirements and levy after the transfer to ensure it is appropriately funded for its expanded remit. The Commission has a deficit estimated to be no more than $0.564 million on 30 June 2025 due to the expenses of the CCCFA's Fit and Proper Person certification system. Originally meant to be funded by certification fees, the system's transition to a licensing model under the FMA means those fees will not be collected. The Commission can offset this deficit with its $1.609 million in cash reserves.

99 I consider that the proposed amount to be transferred to the FMA and the proposal for the deficit be retained by the Commission balance the fiscal implications on both agencies. The total amounts I recommend transfer from appropriations funding the Commission to appropriations funding the FMA are:

($m)	2024/2025	2025/2026	2026/2027	2027/2028	2028/2029 & outyears
Commerce and Consumer Affairs: Enforcement of General Market Regulation (MCA) *NDOE* Enforcement of Consumer Regulation category	-	(5.629)	(5.779)	(5.779)	(5.779)
Commerce and Consumer Affairs: Litigation Funds (MCA) *NDOE* Commerce Commission Internally-Sourced Litigation category	-	(0.885)	(0.885)	(0.885)	(0.885)
Commerce and Consumer Affairs: Litigation Funds (MCA) Non-Departmental Other Expenses: Commerce Commission Externally-Sourced Litigation	-	(0.476)	(0.476)	(0.476)	(0.476)

Services and Advice to Support Well-functioning Financial Markets (MCA) *NDOE* Performance of Investigation and Enforcement Functions category	-	6.514	6.664	6.664	6.664
Commerce and Consumer Affairs: Financial Markets Authority Litigation Funds *NDOE*	-	0.476	0.476	0.476	0.476

Legislative Implications

100 Legislation is required to implement these proposals:

100.1 Confidential advice to Government

100.2 There will be some consequential changes required to the Credit Contracts and Consumer Finance Regulations and changes to implement my proposals relating to Buy Now Pay Later.

100.3 The proposals for financial services conduct regulation require amendments to the FMC Act and FMA Act. Confidential advice to Government

100.4 The proposals for financial dispute resolution schemes require amendments to the FSP Act. Confidential advice to Government I expect changes to this Act will be relatively minor.

100.5 Technical amendments to the FMC Regulations will require changes to secondary legislation that may be progressed independently of the primary legislative changes.

101 Confidential advice to Government

102 Confidential advice to Government [redacted] These Bills are necessary to give effect to coalition agreement commitments to reform financial services.

103 Confidential advice to Government

Impact Analysis

Regulatory Impact Statement

104 Impact analysis requirements apply to and have been prepared for the following proposals:

104.1 Consumer credit legislation,

104.2 Financial services conduct regulation.

105 The Ministry of Business, Innovation and Employment's Quality Assurance Panel has reviewed the Regulatory Impact Statements.

105.1 Regarding the *Fit for purpose consumer credit legislation: Regulatory Impact Statement*, the Panel considers that it fully meets the quality assurance criteria. The Panel was satisfied with the problem definition, options identified, analysis undertaken and the consultation process.

105.2 A Regulatory Impact Statement addendum has been prepared for the change to the Buy Now Pay Later Regulations. The Panel considers that it fully meets the quality assurance criteria for Ministers to make informed decisions on the proposals in the paper.

105.3 Regarding the *Fit for purpose financial services conduct regulation: Regulatory Impact Statement*, the Panel considers that it fully meets the quality assurance criteria. The Panel was satisfied with the problem definition, options identified, analysis undertaken and the consultation process.

106 Regulatory Impact Statement exemptions have been provided for proposals to enhance the review of financial dispute resolution schemes, and for the technical amendments to the FMC Act 2013, FMA Act 2011, and FMC Regulations. The Ministry for Regulation and the Treasury's Regulatory

Impact Analysis team determined that the proposals are exempt from the requirement to provide a Regulatory Impact Statement on the grounds that they have no or only minor impacts on businesses, individuals, and not-for-profit entities.

Climate Implications of Policy Assessment

107 The policy proposals in this paper do not have any climate implications.

Population Implications

108 The consumer credit proposals in this paper are likely to affect different groups of consumers differently. The benefits of improved access to credit and greater efficiency are more likely to accrue to consumers who access credit from relatively sophisticated lenders (such as banks), are better informed of their financial situation and the implications of the credit, and better able to assert their contractual rights where necessary.

109 The potential for harm is likely to be greater for consumers who are made more vulnerable to poor financial decision-making, for example, as a result of financial stress (including poverty) and low levels of financial literacy. Māori, Pasifika, beneficiaries and disabled consumers are likely overrepresented in this population. At the same time, some of these consumers would benefit from improved access to credit as a result of proposals, if that credit is provided responsibly to meet genuine need.

110 Risks to these groups are intended to be mitigated in part by equipping the FMA with regulatory tools that enable it to intervene effectively to protect consumers.

Human Rights

111 The proposal for the FMA to have a power, at any reasonable time, to, without notice or consent, enter and remain on the premises of a regulated entity for the purpose of conducting an on-site inspection could be seen to limit the right to freedom from unreasonable search and seizure.

112 I consider this proposal to be consistent with the FMA's purpose to facilitate the development of fair, efficient, and transparent financial markets, and reasonable in the circumstances. The power will be subject to appropriate safeguards such as requiring that it be exercised at a reasonable time. Officials will be working with the Ministry of Justice to ensure that any concerns relating to the New Zealand Bill of Rights Act 1990 are addressed.

Use of external resources

113 No external resources such as contractors or consultants have been engaged and remunerated in relation to the proposals contained in this paper or the policy development process.

Consultation

114 The Treasury, the RBNZ, the Commission, the FMA, the Ministry of Justice and the Ministry of Social Development have been consulted on this paper.

115 In relation to the proposals for BNPL default fee provisions, my officials recommend option one (or option four as described in the RIS), which is to exempt BNPL providers with conditions that provide bespoke protections against excessive default fees. However, the Ministry for Regulation has a different view on this issue and makes the following comment:

116 The Ministry for Regulation noted that the *Regulatory Impact Statement Addendum: Buy Now, Pay Later Regulations* demonstrates that financial mentors are concerned about the risk of increasing BNPL default fees. However, there is limited evidence that providers will increase these default fees in this way if the matter is left to market forces. Competitive pressure in the market is managing this risk by setting the default fees at current levels, and the BNPL providers are already subject to unfair contract provisions under the Fair Trading Act. Option one (or option four as described in the Regulatory Impact Statement Addendum: Buy Now, Pay Later Regulations, a partial exemption conditional on compliance with a reasonable cross-subsidisation requirement) will therefore impose additional costs to the providers (including increased litigation risk relating to the uncertainty about the legal definitions of "reasonableness"), with no benefit other than maintaining current behaviour by BNPL providers. While the BNPL providers have indicated that they can live with option one, a better response would be an exemption (option two), with monitoring to enable future intervention if evidence of a problem arises (e.g. following a 3-year review). Both options are preferable to the other options set out in the RIS.

117 The Reserve Bank was consulted in the preparation of this Cabinet paper. It notes that, as the prudential supervisor, it continues to monitor any emerging financial stability risks associated with historic liabilities (referred to in paragraph 37). Reserve Bank will work with MBIE and the Treasury to ensure Ministers receive advice on financial stability implications of any liabilities (noting these could be large, as it understands, but more analysis is required).

Communications

118 I intend to announce these Cabinet decisions at the Financial Services Council conference on 4 September. It is important that I announce these decisions soon to provide certainty to industry, and to the staff affected by the transfer of the CCCFA function from the Commission to the FMA about matters relating to their future employment.

Proactive Release

119 I intend to proactively release this paper when I announce these decisions.

Recommendations

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

1 **note** that in May 2024, Cabinet agreed to the release of three discussion documents on financial services reforms to consult on the costs and benefits of any changes to legislation to achieve fit-for-purpose regulation [CBC-24-MIN-0031];

2 **note** that Cabinet invited the Minister of Commerce and Consumer and Affairs to report back to Cabinet by August 2024 with the outcomes of consultation and proposed policy changes;

Consumer credit legislation

3 **agree** to align consumer credit regulation with the financial markets conduct regime by:

3.1 removing the certification regime under the Credit Contracts and Consumer Finance Act 2003 (CCCFA) and, in its place, applying the market services licence regime to providers of consumer credit contracts by adding it as a licensed market service under Part 6 of the Financial Markets Conduct Act 2013 (FMC Act);

3.2 exempting entities currently exempted from certification under the Credit Contracts and Consumer Finance Regulations 2004 from needing to hold a market services licence; and

3.3 having the fair dealing and restricted communication provisions in Part 2 of the FMC Act apply to consumer credit (rather than the Fair Trading Act 1986), and CCCFA disclosure breaches being grounds for a stop order.

4 **agree** to provide for effective transfer of the regulator function to the FMA, including the ability for FMA to continue proceedings,

Confidential advice to Government

5 **agree** to deem all creditors who are currently required to be certified, or are exempt from certification on the basis they are licensed by the FMA or RBNZ, to have a market service licence as would otherwise be required by the decision in recommendation 3.1;

6 **agree** to other changes to the CCCFA, FMC Act, the Financial Markets Authority Act 2011 (FMA Act) and the Financial Service Providers (Registration and Dispute Resolution) Act 2008 (FSP Act) that are necessary or desirable to reflect Cabinet's decision to transfer all regulatory functions under the CCCFA to the FMA;

7 **agree** to remove the due diligence duty and attendant personal liability for all consumer credit providers (section 59B) on the basis the duty duplicates

equivalent obligations under the FMC Act, they will remain subject to personal liability where the individual is involved in the contravention, and these providers will be monitored by the FMA under the licensing regime;

8 **agree** to limit the effect of section 99(1A) of the CCCFA (that a borrower is not liable for the costs of borrowing in relation to a period of non-compliant disclosure) to cases where a person, including the FMA, can show the borrower was harmed by the failure to make initial or agreed variation disclosure;

9 **agree** to make regulations under section 138(1)(ab) of the CCCFA exempting Buy Now Pay Later lenders from having to comply with provisions in the CCCFA relating to unreasonable fees (such as sections 41 and 44A), **either**:

9.1 with conditions that provide bespoke protections against excessive fees, while allowing some cross-subsidisation for defaults by other borrowers;

OR

9.2 with no conditions attached.

10 **agree** to keep the current definition of a high-cost credit contract in section 45C of the CCCFA at an interest rate of 50 per cent or more;

11 **note** that I intend to come back to Cabinet later in the year to seek additional policy decisions on consumer credit;

12 Confidential advice to Government

Financial services conduct regulation

13 **agree** to amend the fair conduct programme minimum requirements in the FMC Act (as amended by the Financial Markets (Conduct of Institutions) Amendment Act 2022) to:

13.1 remove the requirement that fair conduct programmes include policies, processes, systems and controls for enabling the financial institution to meet all of its legal obligations to consumers;

13.2 adjust the requirements relating to training, supervising and monitoring employees to reduce the level of prescription;

13.3 remove the requirement to include methods for regularly reviewing and systematically identifying deficiencies in the effectiveness of the programme; and

13.4 insert requirements for fair conduct programmes to include policies, processes, systems and controls relating to applying, disclosing, and reviewing fees and charges, and recording and resolving consumer complaints;

14 **agree** to amend the Financial Markets Conduct Regulations 2014 (FMC Regulations) to make equivalent changes to the minimum requirements for the fair conduct programmes of Lloyd's managing agents;

15 **agree** to amend the FMC Act to:

15.1 require the FMA to issue a single licence covering the market services that a firm has been approved to provide under Part 6 rather than having the ability to issue separate licences; and

15.2 provide that existing holders of licences for the provision of market services under Part 6 are deemed to hold a single licence;

16 **agree** to amend the FMC Act to enable the FMA to rely on work done or assessments carried out by RBNZ when performing its functions on matters relating to financial institutions where appropriate;

17 **agree** to amend the FMA Act to provide that the FMA will have a power, at any reasonable time, to, without prior notice, enter and remain on the premises of a financial markets participant for the purpose of conducting an on-site inspection to carry out market conduct monitoring of the financial market participant's compliance with conduct obligations;

18 **agree** to amend the FMC Act to require the proposed controller of a firm licensed under Part 6 of that Act to obtain regulatory approval from the FMA prior to the proposed change in ownership or control of the licensed firm taking effect;

19 Confidential advice to Government

Technical amendments to the FMC Act, FMA Act, and FMC Regulations

20 **note** that this paper provides an opportunity to reduce the regulatory burden and compliance cost on businesses by addressing a number of technical issues in the FMC Act, the FMA Act, and the FMC Regulations;

21 **agree** to the minor policy changes set out in Appendix 1;

22 **note** that the policy changes to FMC Regulations will be progressed separately through an Order in Council;

Financial dispute resolution schemes

23 **agree** to amend the FSP Act to:

23.1 require that independent reviews carried out by approved financial disputes resolution schemes be undertaken by a reviewer determined by the Minister responsible for the FSP Act;

23.2 provide the Minister responsible for the FSP Act with a power to set terms of reference for such reviews, and the form and manner of the resulting report; and

23.3 provide the Minister responsible for the FSP Act with a power to direct the schemes to undertake the review at a particular time;

24 **note** I will report back to Cabinet on issues relating to governance arrangements of and enhancing the reporting metrics used by the financial dispute resolution schemes later this year;

25 **note** that I am investigating non-regulatory options for improving access and awareness of financial dispute resolution, including:

25.1 options for an online portal that directs consumers to the correct scheme; and

25.2 advising the schemes of my expectation they make improvements in this area, in line with Schemes having to comply with a principle of accessibility under legislation;

26 **note** many stakeholders proposed consolidating or reducing the number of schemes, this is a significant step, and I would prefer it be looked at in future, should any major issues appear with the current scheme model;

27 Confidential advice to Government

28

Financial implications

29 **note** that in March 2024, Cabinet [CAB-24-MIN-0010 refers]:

29.1 agreed to transfer all regulatory functions under the CCCFA from the Commerce Commission to the FMA; and

29.2 noted the Minister of Commerce and Consumer Affairs will recommend fiscally neutral transfer within Vote Business, Science and Innovation for 2025/2026 and outyears to give effect to the transfer of those functions;

30 **approve** the following fiscally neutral adjustments totalling $28.410 million over the forecast period to provide for the transfer of all regulatory functions under the CCCFA from the Commerce Commission to the FMA, with no impact on the operating balance and net core Crown debt:

	$m – increase / (decrease)				
Vote Business, Science and Innovation Minister for Commerce and Consumer Affairs	**2024/25**	**2025/26**	**2026/27**	**2027/28**	**2028/29 & Outyears**
Multi-Category Expenses and Capital Expenditure:					
Commerce and Consumer Affairs: Enforcement of General Market Regulation (MCA)					
Non-Departmental Output Expenses:					
Enforcement of Consumer Regulation	-	(5.629)	(5.779)	(5.779)	(5.779)
Multi-Category Expenses and Capital Expenditure:					
Services and Advice to Support Well-functioning Financial Markets (MCA)					
Non-Departmental Output Expenses:					
Performance of Investigation and Enforcement Functions	-	6.514	6.664	6.664	6.664
Multi-Category Expenses and Capital Expenditure:					
Commerce and Consumer Affairs: Litigation Funds (MCA)					
Non-Departmental Other Expenses:					
Commerce Commission Internally-Sourced Litigation	-	(0.885)	(0.885)	(0.885)	(0.885)

Multi-Category Expenses and Capital Expenditure: Commerce and Consumer Affairs: Litigation Funds (MCA) Non-Departmental Other Expenses: Commerce Commission Externally-Sourced Litigation	-	(0.476)	(0.476)	(0.476)	(0.476)
Non-Departmental Other Expenses: Commerce and Consumer Affairs: Financial Markets Authority Litigation Funds	-	0.476	0.476	0.476	0.476

31 **note** that the Commerce Commission incurred a CCCFA-specific deficit for the Fit and Proper Person certification system which was to be paid for by third-party fees which is estimated to be $0.564 million on 30 June 2025;

32 **note** that the Commerce Commission will not be able to continue to collect Fit and Proper Person certification fees with which to pay down the $0.564 million deficit once the CCCFA function transfers to the FMA and changes to a licencing scheme;

33 **note** that the deficit can be paid from the Commerce Commission's uncommitted cash reserves, which is estimated to currently be $1.609 million;

Further policy decisions

34 **invite** the Minister of Commerce and Consumer Affairs to report back to Cabinet later this year to seek any further policy decisions as needed;

Legislative implications

35 **authorise** the Minister of Commerce and Consumer Affairs to issue drafting instructions to the Parliamentary Counsel Office to give effect to the above recommendations;

36 **authorise** the Minister of Commerce and Consumer Affairs to make additional policy decisions and minor or technical changes, consistent with the policy intent of this paper, on issues that arise during the drafting of the Bills and regulations.

Authorised for lodgement

Hon Andrew Bayly

Minister of Commerce and Consumer Affairs

Cabinet Economic Policy Committee

Minute of Decision

Financial Services Reforms: Policy Approvals

Portfolio **Commerce and Consumer Affairs**

On 28 August 2024, the Cabinet Economic Policy Committee:

Background

1 **noted** that in March 2024, the Cabinet Expenditure and Regulatory Review Committee agreed to a number of regulatory amendments to the financial services regime, comprising phase one of the proposed reforms [EXP-24-MIN-0010];

2 **noted** that in May 2024, the Cabinet Business Committee approved the release of discussion documents on phase two of the proposed reforms, and invited the Minister of Commerce and Consumer Affairs to report back in August 2024 on the outcome of the consultation and proposed policy changes [CBC-24-MIN-0031];

Consumer credit legislation

3 **agreed** to align consumer credit regulation with the financial markets conduct regime by:

3.1 removing the certification regime under the Credit Contracts and Consumer Finance Act 2003 (CCCFA) and, in its place, applying the market services licence regime to providers of consumer credit contracts by adding it as a licensed market service under Part 6 of the Financial Markets Conduct Act 2013 (FMC Act);

3.2 exempting entities currently exempted from certification under the Credit Contracts and Consumer Finance Regulations 2004 from needing to hold a market services licence;

3.3 having the fair dealing and restricted communication provisions in Part 2 of the FMC Act apply to consumer credit (rather than the Fair Trading Act 1986), and CCCFA disclosure breaches being grounds for a stop order;

4 **agreed** to provide for the effective transfer of the regulator function to the Financial Markets Authority (FMA), including the ability for the FMA to continue proceedings, Confidential advice to Government [redacted]

5 **agreed** to deem all creditors who are currently required to be certified, or are exempt from certification on the basis they are licensed by the FMA or Reserve Bank of New Zealand (Reserve Bank), to have a market service licence as would otherwise be required by the decision in paragraph 3.1 above;

6 **authorised** the Minister of Commerce and Consumer Affairs to approve other changes to the CCCFA, FMC Act, the Financial Markets Authority Act 2011 (FMA Act) and the Financial Service Providers (Registration and Dispute Resolution) Act 2008 (FSP Act) that are necessary or desirable to reflect Cabinet's decision to transfer all regulatory functions under the CCCFA to the FMA;

7 **agreed** to remove the due diligence duty and attendant personal liability for all consumer credit providers (section 59B) on the basis that the duty duplicates equivalent obligations under the FMC Act, they will remain subject to personal liability where the individual is involved in the contravention, and these providers will be monitored by the FMA under the licensing regime;

8 **agreed** to limit the effect of section 99(1A) of the CCCFA (that a borrower is not liable for the costs of borrowing in relation to a period of non-compliant disclosure) to cases where a person, including the FMA, can show the borrower was harmed by the failure to make initial or agreed variation disclosure;

9 **agreed** to make regulations under section 138(1)(ab) of the CCCFA exempting Buy Now Pay Later lenders from having to comply with provisions in the CCCFA relating to unreasonable fees (such as sections 41 and 44A), with no conditions attached;

10 **agreed** to keep the current definition of a high-cost credit contract in section 45C of the CCCFA at an interest rate of 50 percent or more;

11 **noted** that the Minister of Commerce and Consumer Affairs intends to come back to Cabinet later in 2024 to seek additional policy decisions on consumer credit;

12 Confidential advice to Government

Financial services conduct regulation

13 **agreed** to amend the fair conduct programme minimum requirements in the FMC Act (as amended by the Financial Markets (Conduct of Institutions) Amendment Act 2022) to:

13.1 remove the requirement that fair conduct programmes include policies, processes, systems and controls for enabling the financial institution to meet all of its legal obligations to consumers;

13.2 adjust the requirements relating to training, supervising and monitoring employees to reduce the level of prescription;

13.3 remove the requirement to include methods for regularly reviewing and systematically identifying deficiencies in the effectiveness of the programme;

13.4 insert requirements for fair conduct programmes to include policies, processes, systems and controls relating to applying, disclosing, and reviewing fees and charges, and recording and resolving consumer complaints;

14 **agreed** to amend the Financial Markets Conduct Regulations 2014 (FMC Regulations) to make equivalent changes to the minimum requirements for the fair conduct programmes of Lloyd's managing agents;

15 **agreed** to amend the FMC Act to:

15.1 require the FMA to issue a single licence covering the market services that a firm has been approved to provide under Part 6 rather than having the ability to issue separate licences;

15.2 provide that existing holders of licences for the provision of market services under Part 6 are deemed to hold a single licence;

16 **agreed** to amend the FMC Act to enable the FMA to rely on work done or assessments carried out by the Reserve Bank when performing its functions on matters relating to financial institutions where appropriate;

17 **agreed** to amend the FMA Act to provide that the FMA will have a power, at any reasonable time, to, without prior notice, enter and remain on the premises of a financial markets participant for the purpose of conducting an on-site inspection to carry out market conduct monitoring of the financial market participant's compliance with conduct obligations;

18 **agreed** to amend the FMC Act to require the proposed controller of a firm licensed under Part 6 of that Act to obtain regulatory approval from the FMA prior to the proposed change in ownership or control of the licensed firm taking effect;

19 Confidential advice to Government

Technical amendments to the FMC Act, FMA Act, and FMC Regulations

20 **noted** that the paper under ECO-24-SUB-0178 provides an opportunity to reduce the regulatory burden and compliance cost on businesses by addressing a number of technical issues in the FMC Act, the FMA Act, and the FMC Regulations;

21 **agreed** to the minor policy changes set out in Appendix 1 to the paper under ECO-24-SUB-0178;

22 **noted** that the policy changes to FMC Regulations will be progressed separately through an Order in Council;

Financial dispute resolution schemes

23 **agreed** to amend the FSP Act to:

23.1 require that independent reviews carried out by approved financial disputes resolution schemes be undertaken by a reviewer determined by the Minister responsible for the FSP Act;

23.2 provide the Minister responsible for the FSP Act with a power to set terms of reference for such reviews, and the form and manner of the resulting report;

23.3 provide the Minister responsible for the FSP Act with a power to direct the schemes to undertake the review at a particular time;

24 **noted** that the Minister of Commerce and Consumer Affairs will report back to Cabinet on issues relating to the governance arrangements of, and enhancing the reporting metrics used by, the financial dispute resolution schemes later in 2024;

25 **noted** that the Minister of Commerce and Consumer Affairs is investigating non-regulatory options for improving access and awareness of financial dispute resolution, including:

25.1 options for an online portal that directs consumers to the correct scheme;

25.2 advising the schemes of the Minister's expectation they make improvements in this area, in line with schemes having to comply with a principle of accessibility under legislation;

26 **noted** that:

26.1 many stakeholders proposed consolidating or reducing the number of schemes;

26.2 this is a significant step, and the Minister of Commerce and Consumer Affairs would prefer that it be looked at in future, should any major issues appear with the current scheme model;

27 Confidential advice to Government [redacted]

28 Confidential advice to Government [redacted]

Financial implications

29 **noted** that in March 2024, the Cabinet Expenditure and Regulatory Review Committee:

29.1 agreed to transfer all regulatory functions under the CCCFA from the Commerce Commission to the FMA;

29.2 noted the Minister of Commerce and Consumer Affairs will recommend fiscally neutral transfer within Vote Business, Science and Innovation for 2025/2026 and outyears to give effect to the transfer of those functions;

[EXP-24-MIN-0010]

30 **approved** the following fiscally neutral adjustments totalling $28.410 million over the forecast period to provide for the transfer of all regulatory functions under the CCCFA from the Commerce Commission to the FMA, with no impact on the operating balance and net core Crown debt:

	$m – increase / (decrease)				
Vote Business, Science and Innovation **Minister for Commerce and Consumer Affairs**	**2024/25**	**2025/26**	**2026/27**	**2027/28**	**2028/29 & Outyears**
Multi-Category Expenses and Capital Expenditure: Commerce and Consumer Affairs: Enforcement of General Market Regulation (MCA) Non-Departmental Output Expenses: Enforcement of Consumer Regulation	-	(5.629)	(5.779)	(5.779)	(5.779)
Multi-Category Expenses and Capital Expenditure: Services and Advice to Support Well-functioning Financial Markets (MCA) Non-Departmental Output Expenses: Performance of Investigation and Enforcement Functions	-	6.514	6.664	6.664	6.664
Multi-Category Expenses and Capital Expenditure: Commerce and Consumer Affairs: Litigation Funds (MCA) Non-Departmental Other Expenses: Commerce Commission Internally-Sourced Litigation	-	(0.885)	(0.885)	(0.885)	(0.885)
Multi-Category Expenses and Capital Expenditure: Commerce and Consumer Affairs: Litigation Funds (MCA) Non-Departmental Other Expenses: Commerce Commission Externally-Sourced Litigation	-	(0.476)	(0.476)	(0.476)	(0.476)

Non-Departmental Other Expenses: Commerce and Consumer Affairs: Financial Markets Authority Litigation Funds	-	0.476	0.476	0.476	0.476

31 **noted** that the Commerce Commission incurred a CCCFA-specific deficit for the Fit and Proper Person certification system which was to be paid for by third- party fees, and that this is estimated to be $0.564 million on 30 June 2025;

32 **noted** that the Commerce Commission will not be able to continue to collect Fit and Proper Person certification fees with which to pay down the $0.564 million deficit once the CCCFA function transfers to the FMA and changes to a licensing scheme;

33 **noted** that the deficit can be paid from the Commerce Commission's uncommitted cash reserves, which is currently estimated to be $1.609 million;

Further policy decisions

34 **invited** the Minister of Commerce and Consumer Affairs to report back to Cabinet later in 2024 to seek any further policy decisions as needed;

Legislative implications

35 **authorised** the Minister of Commerce and Consumer Affairs to issue drafting instructions to the Parliamentary Counsel Office to give effect to the above paragraphs;

36 **authorised** the Minister of Commerce and Consumer Affairs to make additional policy decisions and minor or technical changes, consistent with the policy intent of the paper under ECO-24-SUB-0178, on issues that arise during the drafting of the Bills and regulations.

Rachel Clarke
Committee Secretary

Present:
Hon David Seymour
Hon Nicola Willis (Chair)
Hon Brooke van Velden
Hon Louise Upston
Hon Matt Doocey
Hon Simon Watts
Hon Melissa Lee
Hon Penny Simmonds
Hon Nicola Grigg
Hon Andrew Bayly
Hon Andrew Hoggard
Hon Mark Patterson
Simon Court MP
Jenny Marcroft MP

Officials present from:
Office of the Prime Minister
Officials' Committee for ECO

Regulatory Impact Statement: fit for purpose consumer credit law

Coversheet

Purpose of Document	
Decision sought:	**Proposed reforms to consumer credit law**
Advising agencies:	**Ministry of Business, Innovation and Employment (MBIE)**
Proposing Ministers:	**Minister of Commerce and Consumer Affairs**
Date finalised:	**21 August 2024**

Problem Definition

On 19 March 2024, Cabinet decided to transfer regulatory responsibility for the *Credit Contracts and Consumer Finance Act* (CCCFA) from the Commerce Commission to the Financial Markets Authority (FMA) [*EXP-24-MIN-0010* refers]. This change is to simplify the regulatory landscape for financial service providers. It refines New Zealand's 'twin peaks' approach to regulation so the FMA becomes the single regulator for financial markets conduct, including credit.

As part of reforms that are necessary to facilitate this transfer, the Government has also committed to addressing other known issues with the CCCFA that undermine its efficiency and effectiveness. The following is a summary of the four issues forming the basis of this regulatory impact statement. These issues are analysed fully from paragraph 40 of this paper.

A. Consumer credit and other financial services have different regulatory models, including entry and ongoing requirements and different tools the regulator can use to promote compliance with legal obligations. Transferring responsibility for consumer credit to the FMA without better alignment of these models would:

- **create significant inefficiencies for the regulator by requiring the FMA to operate two different and inconsistent models within financial markets conduct regulation**
- **perpetuate those inefficiencies for lenders who provide products and services already regulated by the FMA, and require the regulator to treat the same firm differently for equivalent consumer financial services**
- **limit the FMA's ability to intervene and regulate lenders effectively (through licensing tools and other less formal interventions), which reduces consumer protection.**

B. In 2022, an MBIE-led investigation found that the due diligence duty (set out in section 59B of the CCCFA) and personal liability for directors and senior managers were, at least in part, driving overly conservative lending practices. This has been reinforced by recent consultation on these settings. Overly conservative decision-making by lenders can result in inefficiencies (such as excessive compliance costs) and poor outcomes for consumers (such as substantially longer processing times). Furthermore, alignment of the CCCFA's regulatory model with that currently used by the FMA (as proposed) would remove the need for the duty and associated personal liability.

C. If a lender fails to disclose certain information, the affected borrower is not liable for the costs of borrowing in relation to the period before that disclosure is made (section 99(1A) of the CCCFA). The potential for this consequence to be substantially disproportionate to the breach was reduced in 2019 by making relief available to lenders on application to a court (under section 95A). However, lenders report that these consequences continue to produce overly conservative approaches to ensuring compliance with disclosure requirements. We believe these settings:

- are unduly burdensome for lenders given the potential sums involved across a class of affected loans
- can result in over-compensation or unnecessary litigation costs where the borrower was not harmed by the disclosure failure.

D. Provisions applying to high-cost credit contracts have led to the elimination of high-cost lending (at interest rates of 50% or more). Under section 45L of the CCCFA, the Minister is required to consider whether the interest rate that defines a high-cost consumer credit contract should be reduced to a rate between 30% and 50%. This provides an opportunity to place pressure on lending below 50% to reduce interest rates.

Executive Summary

The primary purpose[1] of the CCCFA is to protect the interests of consumers in connection with credit products. It does this by creating obligations on lenders, including to disclose certain information that may affect consumer decision-making, lend responsibly, and charge appropriate fees. Reforms to the CCCFA over time have:

- increased the overall burden of these obligations and liability for breaching them
- been developed independently of other financial markets legislation.

This has resulted in differences in how financial services are regulated and the complexity of that regulation for financial service providers.

The Government is committed to reforming the CCCFA and simplifying the regulation of financial services. Cabinet has agreed to transfer responsibility for credit contracts and consumer credit regulation from the Commerce Commission to the Financial Markets Authority (FMA). This would simplify the financial services landscape by making financial service providers (including lenders) accountable to two regulators (the Reserve Bank of New Zealand and the FMA) instead of three (when the Commerce Commission was also overseeing the credit market).

This regulatory impact statement examines four areas of reform to the CCCFA (noted in the 'problem definition' above).

We have consulted on possible reforms in each of these areas and analysed them against criteria reflecting the Government's objectives, as well as the purposes of the CCCFA. Our preferred options would form a package of reforms which involve a shift from managing the conduct of lenders through accountability of directors and senior managers and formal interventions to managing conduct through a licensing model that expects lenders to be capable of effectively

[1] The CCCFA's secondary goals include promoting confident and informed participation by consumers, as well as promoting/facilitating fair, efficient, and transparent credit markets.

delivering the service and less formal interventions by the regulator. The reforms forming this package (with some interdependencies between them) are as follows:

A. *Align the model the FMA would use to regulate credit contracts and consumer credit with other financial services.* Consumer credit lenders would transition to FMA monitoring under a market services licence, and the FMA would have core regulatory tools (such as the power to make stop orders). Transitioning to licensing would involve replacing the current certification regime with market services licensing by deeming all consumer credit lenders to hold a market services licence. This means only new entrants need to obtain a licence. This would give the FMA tools to regulate existing and future lenders effectively in the interests of consumers. It is expected to achieve efficiencies from alignment with other financial services regulation without necessarily increasing the regulatory burden on lenders.

B. *Remove the due diligence duty and personal liability for directors and senior managers.* This form of accountability and incentives for individuals would largely duplicate licence obligations associated with the regulatory model proposed above. That model would enable the FMA to take a more proportionate approach to incentivising compliance, thereby addressing the overly conservative lending practices we have observed as a result of personal liability.

C. *Limit the application of a provision (section 99(1A)) that creates potentially significant consequences for lenders when they fail to make initial or variation disclosures, by requiring harm to the borrower to be shown.* Our view is that these consequences should be retained because they play an important role in incentivising lenders to make proper disclosures and remedy any failure to do so. This option would address uncertainty about these consequences, including litigation costs in the case of harmless failures. Although this option would transfer the burden of proof to borrowers, the FMA can intervene to secure redress where it believes borrowers have been harmed by the disclosure failure. Licensing (as proposed above) would support the FMA to do this.

D. *No change to the high-cost credit provisions.* Our assessment is that these provisions have been effective at achieving their stated purpose. Based on the evidence available to us, we do not consider that the risks of harm are such as to require lowering the interest rate threshold that defines high-cost credit.

This package of reforms is expected to increase the effective regulation and efficient operation of markets for credit. It presents some risks to the interests of consumers. These can be mitigated in large part by providing the FMA with a range of regulatory tools and powers to intervene effectively.

The proposed changes to the regulatory model would coincide with the transfer of functions to FMA, transferring the Commission's existing appropriation for its regulatory responsibilities under the CCCFA, and may require transitional arrangements for matters, such as ongoing litigation.

We propose to monitor these reforms and compare their actual impacts with those presented in this regulatory impact statement between three and five years after their commencement.

Limitations and Constraints on Analysis

Officials consulted with the FMA, RBNZ, the Treasury, and the Commerce Commission in developing options for consultation. A discussion document was prepared in a short timeframe and consulted on over a period of four weeks. We received 37 submissions from a range of stakeholders including industry organisations, financial markets participants, consumer representatives and law firms. The options we consulted on polarised stakeholders, which limited information they provided about the impact of more moderate options.

There are some minor differences between the options we consulted on and those analysed in this regulatory impact statement. More time for our policy development prior to consultation and a longer consultation period could have enabled us to include higher quality options and analysis in the discussion document, as well as a higher quality of responses. However, we are satisfied that responses received, when combined with other information we have, is reasonably sufficient for analysis of the policies considered in this paper.

Quantitative information

For options that relate to section 99(1A), high-cost credit, and to an extent the due diligence duty and personal liability, we have access to quantitative data that helps us to understand national trends in the consumer credit lending market and the scale of activities likely to be affected by some options. The data does not definitively show the impact of past and future changes to consumer credit law because trends (e.g. the default rate for loans) are influenced by a range of external factors (e.g. economic factors).

For the high-cost credit analysis, as national lending data does not capture interest rates, we looked at financial mentor client datasets, in which loans could be differentiated by interest rate. These data only relate to loans that have caused consumers to seek assistance from those mentors, so is not representative of all loans. This limitation has contributed to our assessment that there is a lack of evidence of systemic harm from lending at certain interest rates (or attributable to those interest rates).

Qualitative information

For all options, we have largely relied on qualitative evidence from submissions and through discussions with lenders, consumer advocates, the Commerce Commission and the FMA. Because views were different and often conflicting between lenders and consumer advocates, we have used judgement (e.g. directors of lenders are best placed to comment on impacts from personal liability settings) and noted assumptions in the analysis.

In general, it is difficult to attribute specific impacts to specific settings in the CCCFA. The changes most relevant to this regulatory impact statement were part of wider reforms intended to have a similar impact. For example, the high-cost credit provisions came into force in May 2020 and, shortly after in December 2021, both the due diligence duty and personal liability settings and the new, prescriptive affordability requirements came into force.

Our reliance on qualitative information (and the impact of these constraints) is much lower in judging the impacts of the regulatory model that would be in place once the FMA takes over regulatory responsibility for consumer credit.

Key assumptions made in our analysis

We have assumed that unnecessary compliance costs to lenders (resulting from inefficiencies or excessive regulatory burden) are passed on to consumers. We expect lenders do this either by pricing additional costs into their offerings or directly through the fees they charge (which are required by the CCCFA to be calculated on the basis of direct cost-recovery). We have also assumed that competitive pressure between lenders results in them passing on savings to consumers. We note the Commerce Commission’s market study has raised questions about competition for the provision of home loans, describing the intensity of that competition as 'sporadic'[2]. This detracts slightly from our assumption that savings would tend to be passed on to consumers, but, in our view, does not negate it.

The comparative costs and benefits of options for three of the four issues (all except high-cost credit) would vary depending on how they are implemented by the FMA. We have made certain assumptions about this based on discussions with FMA staff. For example, we assume the FMA would administer a licensing model and use the proposed regulatory tools in a way that:

- does not meaningfully increase the current standard for entry into the market
- promotes compliance with obligations under the CCCFA comparably to the due diligence duty and personal liability settings.

Responsible Manager
Sally Whineray Groom Acting Manager Consumer Policy Ministry of Business, Innovation and Employment 21 August 2024

Quality Assurance	
Reviewing Agency:	MBIE
Panel Assessment & Comment:	MBIE's Regulatory Impact Assessment Review Panel has evaluated the Regulatory Impact Statement "fit for purpose consumer credit law" and considers that it **meets** the quality assurance criteria. The panel is satisfied with the problem definition, options identified, analysis undertaken, and the consultation process.

Section 1: Diagnosing the policy problem

What is the context behind the policy problem?

Markets for consumer credit meet diverse needs

1. Using credit is a normal part of everyday life for many New Zealanders. Credit products include home loans, personal loans, credit cards, consumer leases, vehicle finance, pawnbroking agreements, mobile trader credit sales and buy now pay later. These are all contractual agreements by which consumers can defer payment of debt.

2. In April 2024, the Centrix Credit Indicator Report revealed that consumer credit demand has increased by 3.5% from the previous year. Around a quarter of consumers have entered into a credit contract in the past two years.[3]

[2] The Commission's draft report can be found on this page: Commerce Commission - Market study into personal banking services (comcom.govt.nz). The final report will be published on 20 August 2024.

[3] New Zealand Consumer Survey 2024, commissioned by MBIE and the Commerce Commission to Ipsos.

3. Consumers generally choose consumer credit products depending on their preferences and needs.[4] Long-term loans are commonly used for housing or vehicles, while credit cards are frequently obtained without a specific purpose in mind. Overdrafts and short-term loans serve various purposes such as renovations, bills, vehicles, and debt servicing. Buy now pay later credit products are often used for purchasing clothing, electronics, and appliances.

4. Different types of entities provide consumer credit. There are currently 544 consumer credit lenders in New Zealand registered on the Financial Services Providers Register. There are an additional 496 lenders who are exempt from certification because they are vehicle dealers who have arrangements with a finance company whereby they only provide credit on an interim basis before transferring it to the finance company.

5. Although there are only 16 banks offering personal banking services in New Zealand, as of January 2024, 96% of housing and personal consumer lending was provided by registered banks.

6. In addition to registered banks, non-bank businesses also provide personal banking services. This includes:

    a. 15 licensed non-bank deposit takers, such as credit unions and building societies; and

    b. other finance companies, including peer-to-peer lenders.

Consumer credit is regulated by the Credit Contracts and Consumer Finance Act 2003 (CCCFA)

7. The CCCFA came into force in 2005, repealing and amalgamating the Credit Contracts Act 1981 and the Hire Purchase Act 1971. Its primary purpose is to protect the interests of consumers in relation to various forms of consumer credit. This reflects that:

    a. Markets for consumer credit are characterised by information asymmetries between lenders and borrowers. Even when consumers have a good level of financial literacy, they are rarely in the same position as the lender to evaluate how their interests might be impacted by the contract terms being offered, and to compare these with other available products.

    b. Consumers often exhibit cognitive biases that can affect their ability to make rational financial choices in their own long-term interests[5], or can be made vulnerable to poor decision-making by their circumstances (such as strong pressure to make a purchase) or shortcomings (such as poor literacy).[6]

8. The CCCFA's secondary purposes include promoting confident and informed participation by consumers as well as promoting and facilitating fair, efficient, and transparent credit markets.

9. The Commerce Commission is currently the agency responsible for enforcing the CCCFA.

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[4] MBIE Consumer credit Research Report 2024, conducted by Verian, accessible here: https://www.mbie.govt.nz/dmsdocument/28546-consumer-credit-research-report-march-2024.

[5] See for example: *Household Finance* in *The Journal of Finance* (2006), Campbell, J. Y. 61(4), 1553–1604 and *Judgment under uncertainty: Heuristics and biases* in *Science* (1974), Tversky, A., & Kahneman, D. 185(4157), 1124–1131.

[6] The New Zealand Retirement Commission has published a financial capability survey 2021 that found, among other things, that New Zealanders, among other countries that did this survey, score at the bottom or near the bottom for spending restraint, not borrowing for day-to-day expenses, and informed product choice. The report can be found here: TAAO-RC-NZ-FinCap-Survey-Report.pdf (retirement.govt.nz).

The CCCFA has been amended several times, resulting in unintended impacts for both consumers and lenders

10. Reforms to the CCCFA over the last decade have been motivated by concerns about its effectiveness in protecting the interests of consumers, particularly against irresponsible lending. Those reforms increasingly placed greater responsibility and regulatory burden on lenders to act in the best interests of borrowers.

11. These reforms are summarised in **Annex 1**. There were two main periods of reform:

    a. In 2015, changes were intended to address unscrupulous lending by creating lender responsibility principles, new disclosure requirements and increased liability for lenders who breach the CCCFA.

    b. Between 2019 and 2021, changes were made in response to concerns about problem debt and continued non-compliance (including in the high-cost credit market). They included prescriptive affordability assessment requirements, greater scrutiny and accountability for a lender's directors and senior managers, increased liability for breaches and additional rules targeted at high-cost loans.

12. Some of these reforms have been perceived to create a regulatory burden that is disproportionate to risks to consumers and, in many cases, may undermine their interests. We observed some of these effects in 2022 as part of our investigation CCCFA changes that took effect in December 2021, which identified the following unintended impacts:[7]

    a. more borrowers across all lending types who should pass the affordability test are subject to declines or reductions in credit amount;

    b. borrowers are subject to unnecessary or disproportionate inquiries that are perceived by them as intrusive.

The CCCFA also has evolved independently of other financial services legislation, complicating the wider regulatory landscape

13. Lenders subject to the CCCFA are also subject to other financial markets legislation. In summary:

    a. All lenders need to be registered under the Financial Service Providers (Registration and Dispute Resolution) Act 2008 and be part of a dispute resolution scheme.

    b. Some lenders, such as registered banks and non-bank deposit takers, are also subject to:

        i. Prudential regulation (including registration or licensing by the NZ Reserve Bank) to ensure stability of the financial system, and

        ii. Conduct regulation for other financial products or services (including licensing) by the FMA.

    c. Banks and non-bank deposit takers will also, from 31 March 2025, be subject to the *Financial Markets Conduct (Conduct of Financial Institutions) Amendment Act 2022* (CoFI Act). This requires them to have effective systems and policies for designing,

[7] The 2022 investigation report is accessible here: [Early implementation and impacts of 1 December 2021 credit law changes (mbie.govt.nz).](mbie.govt.nz)

distributing and supporting the ongoing provision of products and services to customers, including consumer credit.

d. Lenders that are not already licensed by or registered with the New Zealand Reserve Bank or licensed by the Financial Markets Authority (e.g. finance companies, mobile traders) must meet the the CCCFA 'fit and proper person' certification requirement. This is administered by the Commerce Commission.

14. These various forms of legislation applying to financial service providers have evolved independently over time. They are administered by different regulators (the Commerce Commission, FMA and RBNZ) using different regulatory models. This has led to excessive layering of regulation and loss of coherence across the financial services regulatory environment.

The Government wants to streamline and simplify how financial services, including consumer credit, is regulated

15. The Government's commitment to reform the CCCFA is expressed in:

a. the *National* Party's 100-point plan for Rebuilding the Economy (which includes a commitment to 'cut financial red tape that is stifling investment, including significantly reducing the scope of the CCCFA which has restricted access to credit'), and

b. the National and ACT Coalition Agreement (which includes a commitment to 'Rewrite the CCCFA to protect vulnerable consumers without unnecessarily limiting access to credit').

16. Cabinet has already agreed to transfer all regulatory functions under the CCCFA from the Commerce Commission to the FMA [EXP-24-MIN-0010 refers]. This decision is intended to deliver a clearer 'twin peaks' model for the sector, whereby the FMA is responsible for all conduct regulation and the RBNZ for all prudential regulation.

The Government is pursuing reforms to financial services regulation through two phases.

17. Phase one has resulted in the following changes to regulations:

a. a full exemption from the CCCFA for voluntary targeted rates schemes administered by local authorities and removal of duplicative reporting requirements – effective 25 April 2024

b. removal of redundant exemptions relating to COVID-19 from regulations under the CCCFA – effective 7 June 2024

c. alignment of certain rules for different financial dispute resolution schemes – effective 18 July 2024

d. removal of prescriptive affordability requirements from regulations made under the CCCFA (and development of new guidance on affordability in the Responsible Lending Code) – effective 31 July 2024.

18. Phase two reforms include the proposals in this regulatory impact statement and:

a. a targeted review of the CoFI Act and other conduct requirements under the *Financial Markets Conduct Act 2013* (FMC Act) and *Financial Markets Authority Act 2011* (FMA Act)

b. improving consumer access to and the effectiveness of the financial dispute resolution system.

19. Following Cabinet approval, we undertook public consultation on phase two reforms over four weeks ending 19 June 2024 and recieved 37 submissions from a range of interested parties.

How is the status quo expected to develop?

20. We answer this question in the context of Cabinet's decision to transfer all credit finance and consumer credit regulatory functions to the FMA, and as it pertains to four areas of the CCCFA that we consulted on as part of the financial services reforms package in the discussion document *Fit for purpose consumer credit regulation*.

Issue A: Regulatory model

21. The regulatory model and regulatory tools under the CCCFA are in contrast to those the FMA uses to regulate other financial services. This means lenders are subject to different requirements depending the type of entity they are (see paragraph 13).

22. The Commission's approach to regulating consumer credit is influenced and limited by the regulatory tools the CCCFA provides. The current approach emphasises deterring non-compliance through investigations, formal interventions and strong penalties over prevention (which requires more administrative regulatory tools).

23. The CCCFA's certification requirement, which took effect in 2021, gives the regulator some scrutiny over lenders entering the market. Certification ensures, every five years, that a lender's directors and senior managers are 'fit and proper persons' to hold their respective positions. It was introduced to improve compliance, and reduce irresponsible lending and phoenixing (i.e. individuals escaping accountability by winding up the business and starting a new one). There is limited discretion to impose conditions on certification and change those conditions.

24. Certification provides the regulator with some oversight of individuals, but no direct oversight of conduct. The regulator is still confined to regulating conduct through formal interventions, used in response to potential non-compliance. This is in constrast to the FMA's licensing model, which provides direct oversight of conduct and the ability to intervene informally. A licence requirement carries the expectation that the lender is capable of effectively carrying out the service and meeting their legal obligations.

25. If the regulatory model does not change when functions under the CCCFA are transferred to the FMA, the FMA would not have the regulatory tools it normally uses and which are necessary to provide direct oversight of conduct in the market for consumer credit:

    a. Market services licensing gives the FMA broad powers to monitor and oversee licencees' conduct. Formal licensing powers include being able to set conditions[8] (e.g. about the service or regulatory returns), require action plans, give directions, issue censures, and suspend or cancel the licence.[9] The FMA can tailor regulatory requirements through licence terms and conditions.

    b. Licensing is complimented by the FMA's ability to make direction orders (directing compliance or stipulating steps to remedy non-compliance), stop orders (preventing offering, advertising, or entering transactions for financial products or services), exemptions and designations (i.e. a call-in power), which do not require a court order.

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[8] Section 403, FMC Act 2013.

[9] Under sections 402 - 428, FMC Act 2013.

Issue B: Personal liability settings

26. Under the status quo, directors and senior managers have a duty under section 59B of the CCCFA to "exercise due diligence to ensure that the creditor complies with its duties and obligations under this Act." They are personally liable for certain damages and pecuniary penalties that can be awarded by a court if they do not meet this duty. Their liability for pecuniary penalties cannot be indemnified or insured against.

27. Like certification, these settings were intended to increase accountability for directors and senior managers, and reflect a deterrence approach to regulating lenders (rather than a more proactive relationship with the regulator, enabled by tools such as licensing). We have seen signs that these settings cause lenders to take overly conservative interpretations to requirements relating to affordability and a reluctance to exercise discretion as intended.[10]

28. If the status quo continues (and even if a licencing model was applied), we would expect the settings to continue resulting in lenders taking overly conservative approaches to meeting their legal obligations.

Issue C: Consequences for incomplete disclosures

29. Sections 17 and 22 of the CCCFA require lenders to disclose certain information to ensure that consumers are able to make informed decisions before and after entering into a loan agreement.

30. If lenders fail to make disclosure to a consumer as required by section 17 (initial disclosure) or section 22 (agreed variation disclosure), section 99(1A) provides that the borrower is not liable for the costs of borrowing during that period of non-compliance. In other words, the lender forfeits the right to any interest or fees it charged during this period. This applies when a lender fails to make disclosure at all or only partially meets disclosure requirements.

31. Section 99(1A) has operated since June 2015. A 2017 review found that forfeiture of all interest and fees would be disproportionate to the seriousness of the failure in many cases (i.e. would over-compensate borrowers).[11] The risk of disproportionate consequences has also resulted in over-compliance by lenders.

32. The solution developed to address this is found in sections 95A and 95B, which took effect in December 2019. Section 95A makes relief available by enabling a court to extinguish or reduce the effect of section 99(1A) if that is considered 'just and equitable' and applying factors in section 95B.

33. Despite calls at the time, these provisions were not applied retrospectively. They apply to disclosures failures from December 2019 onwards, but not to disclosure failures that occured prior. This means that, under the status quo, the consequences for the lender of a disclosure failure depend on when the failure happened:

    a. Between June 2015 and December 2019, relief under section 95A is not available (although the Commission negotiates settlements on a similar basis to section 95A). Where private litigation is brought, lenders may face consequences that are

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[10] See MBIE's report: *Early implementation and impacts of 1 December 2021 credit law changes*, accessible here: https://www.mbie.govt.nz/dmsdocument/23262-early-implementation-and-impacts-of-1-december-2021-credit-law-changes.

[11] You can read about the 2017 review on this webpage: [Review of Section 99(1A) of the Credit Contracts and Consumer Finance Act 2003 | Ministry of Business, Innovation & Employment (mbie.govt.nz)]

disproportionate to the seriousness of the disclosure failure. There are 18 lenders with relevant disclosure failures over this period that the Commission has resolved in some manner (excluding high-cost lenders and mobile traders).

b. After 1 December 2019, relief via section 95A is available. However, no court has made an order under this provision. It is therefore not certain how a court might apply it in practice to reduce or extinguish the effect of a failure to disclose. We would expect this to continue in the absence of either regulatory change or judicial guidance on section 95A that confirms lenders will be protected from disproportionate consequences. Maintenance of the status quo may increase lenders' desire to test section 95A, but we are not confident this would occur.

Issue D: High-cost credit provisions

34. In 2020, the Credit Contracts Legislation Amendment Act 2019 introduced new requirements that apply to high-cost consumer credit contracts. These formed new subpart 6A. Their purpose was to reduce problem debt by addressing the excessive cost of credit for these loans and repeat borrowing by vulnerable consumers.

35. Under the status quo, the CCCFA defines a high-cost consumer credit contract as a contract with an annual interest rate of 50% or more (or where the rate is likely, when combined with default interest, to be 50% or more). Provisions that apply to these contracts are:

    a. The costs of borrowing must not exceed the loan advance (i.e. a borrower can never be required to repay more than twice what they borrowed).

    b. Lenders are prohibited from entering into a high-cost consumer credit contract with a consumer who:

        i. has an unpaid balance or has had an unpaid balance on any other high-cost consumer credit contract in the preceding 15 days

        ii. has entered into two or more high-cost credit consumer contracts in the past 90 days.

    c. The rate of charge (including interest and fees but excluding default fees) for high-cost consumer credit contracts is capped at a maximum of 0.8% per day.

    d. Compound interest is prohibited.

    e. There is a rebuttable presumption that default fees are unreasonable if exceeding $30 (or other prescribed amount, if any).

36. Section 45L requires the Minister of Commerce and Consumer Affairs, as soon as practicable after three years, to review the effectiveness of the high-cost credit provisions. It also requires the Minister to consider whether the interest rate that defines a high-cost consumer credit contract should be reduced to a rate between 30% and 50%.

37. This review found that the high-cost credit provisions have led to the elimination of high-cost credit. Twelve high-cost credit providers left the market. Although nine remain, they have restructured their products to fall below the 50% interest rate threshold.

38. The elimination of high-cost loans has meant an estimated 150,000 potential borrowers no longer have access to this source of credit.[12]

39. A former high-cost lender stated that the combined effects of the high-cost credit provisions have rendered this type of credit economically unviable. Under the status quo, high-cost credit products are likely to remain unavailable. Moreover, banks are now reluctant to offer their services to lenders categorised as “high-cost” because of the potential harm to their reputation.

[12] Ministry of Business, Innovation and Employment (28 August 2019). *Review of consumer credit regulation – further policy recommendations.* ***https://www.mbie.govt.nz/assets/review-of-consumer-credit-regulation-further-policy-proposals.pdf***

What are the policy problems or opportunities?

Issue A: Regulatory model

40. Transferring regulatory responsibility to the FMA without better alignment of the regulatory model and tools available under the CCCFA would make it more difficult for the FMA to effectively regulate consumer credit. We would expect:

    a. significant inefficiencies for the FMA by requiring it to operate two fundamentally different models within financial markets conduct regulation

    b. inconsistencies by requiring the FMA to treat the same firm differently for equivalent consumer financial services

    c. similar inefficiencies for lenders who provide products and services already regulated by the FMA and have to navigate fundamentally different regulatory models

    d. inadequate regulatory tools for the FMA to intervene and regulate lenders effectively, which reduces consumer protection.

Issue B: Liability settings

41. The due diligence duty and personal liability for directors and senior managers have a tendency to produce more conservative lending practices than intended. We have observed this directly in our interactions with some lenders and from the approach many of them took to implementing affordability requirements that have now been revoked from regulations.[13] This can be characterised as a tendency to adopt overly cautious (and sometimes surprising) interpretations of their legal obligations, a reluctance to exercise discretion that is available, and excessive risk-aversion.

42. For example, in relation to these affordability requirements:

    a. some lenders were interpreting the definition of 'listed outgoings' as including discretionary expenditure

    b. lenders were making very little use of exceptions that were intended to reduce the burden of these requirements in lower risk cases.

43. It is difficult to disentangle the role these settings play in producing this outcome from other possible causes. They came into force as part of the 2019-2021 suite of reforms that increased the regulatory burden on lenders and, in particular, the perscriptive affordability assessment requirements. However, from what lenders have shared with us, we consider the personal liability settings are a plausible explanation for overly conservative lending behaviour.

44. Overly conservative lending practices is a regulatory failure, in that it can reduce consumers' access to appropriate credit and increases costs which can be passed onto consumers. A lack of confidence that consequences are proportionate is also likely to inhibit innovation that serves the interests of consumers.

45. These personal liability settings reflect the CCCFA's current approach of promoting compliance through the threat of significant consequences, rather than a relationship with the regulator whereby compliance is more actively managed (enabled by appropriate regulatory tools).

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[13] MBIE. (2022). Early implementation and impacts of 1 December 2021 credit law changes – Investigation report. Page 59. Supported by stakeholder submissions from 2024 FSR consultation.

Alignment with the licensing model used by the FMA would likely remove the need for these settings.

Issue C: Consequences for incomplete disclosures

46. The relief provided in 2019 (sections 95A and 95B) does not appear to have fully addressed the problem of over-compliance that is caused by the prospect of full forfeiture of interest and fees under section 99(1A).

47. Although relief under section 95A has in theory lessened, if not removed, the risk of disproportionate consequences for any disclosure failures after December 2019, the extent of relief it provides is uncertain. This has failed to fully restore lenders' confidence they can avoid disproportionate consequences. Given the potential scale of liability across a class of affected loans, we can see how this lack of confidence would continue to result in excessive compliance costs.

48. Moreover, where the disclosure failure was of no consequence to the borrower:

    a. there is potential for borrowers to be compensated despite not being affected at all

    b. lenders may incur unnecessary litigation costs in seeking to avoid this outcome.

49. We also continue to hear concerns about the risk of disproportionate consequences being applied to failures to disclose information that happened between 2015 and 2019. Notably, there is a class action against two of the largest banks that is being pursued through the courts, despite a settlement with the Commission that resulted in less than the full costs of borrowing being refunded to affected borrowers.

Commercial Information

50. Commercial Information

51.

52. The Commission has negotiated outcomes with 18 lenders for relevant disclosure failures over the period before December 2019, issued compliance advice letters to another four and has

unresolved investigations into the actions of another four lenders. It is unclear to what extent lenders may have other undisclosed liability from this period.

53. The opportunity to bring any civil or criminal proceedings is time-limited by the CCCFA (to three years after the failure was discovered or ought reasonably to have been discovered).

Issue D: review of the high-cost credit provisions

54. The CCCFA requires the Minister to review the operation and effectiveness of the high-cost credit provisions. This review should also consider whether the interest rate defining a high-cost consumer credit contract should be lowered to a rate between 30% and 50%.

55. Our analysis suggests that the high-cost credit provisions have effectively addressed the intended issues, and we have no evidence that the same kind of issues are caused by loans with a lower interest rate.

56. However, we have identified 13 lenders offering loans with interest rates of between 47.5% and 49.95%. The high-cost credit provisions provide an opportunity to place downward pressure on those interest rates. While this may benefit borrowers in this part of the market, a factor to consider is the availability of short-term loans and credit for those borrowers who cannot access more traditional forms of credit, for example, due to poor credit scores.

What objectives are sought in relation to the policy problems?

57. The Government's reform objectives for the financial services regulatory landscape are as follows:

    a. simplify and streamline regulation of financial services (including reducing duplication)

    b. remove undue compliance costs for financial market participants

    c. improve outcomes for consumers.

58. Within this, more specific policy objectives have been developed for this review of consumer credit. These sub-objectives are:

    a. removing disproportionate compliance costs for consumers and lenders

    b. supporting consumers to access credit that meets their needs

    c. ensuring regulatory obligations and the institutional arrangements supporting them are clear and simple.

59. These objectives reflect the often competing interests of consumers in having access to credit from lenders who can innovate and operate efficiently, and being protected from harm created by irresponsible lending.

Section 2: Deciding upon options to address the policy problems

60. Our analysis has been informed by feedback from a range of stakeholders, including 37 submissions from different types of lenders (e.g banks and finance companies), law firms, organisations representing consumers, financial mentors and individuals. We have also continued to work closely with staff at the Commerce Commission and FMA to consider the implications of options.

Summary

61. The following table provides a summary of the options considered for each of the four problems/opportunities and our analysis of those options. Our preferred options form a package of reforms that have some interdependencies. In particular, our preference for option A2 (market services licensing) justifies some of our other preferences.

Area	Options	Expected Impact
A) Approach to regulating consumer credit following transfer of functions to FMA	A1: Retain 'Fit and proper' certification (the counterfactual) and add some FMA tools	**Advantages:** Greater certainty for lenders and some potential improvements in effective regulation from addition tools. **Disadvantages:** Misalignment of regulatory tools/approach creates inefficiencies for both the FMA and some regulated parties.
	A2: Transition to a market services licence and apply all FMA licensing and core tools– **preferred**	**Advantages:** Provides FMA with the regulatory tools to provide a proactive, responsive, proportionate, and effective oversight of lenders. More consistency and transparency for market participants. **Disadvantages:** Potential for higher standard for entry and competition impacts from approach to transitioning market. However, we understand from the FMA this is unlikely in practice.
B) Personal liability settings	B1 (the status quo): Retain due diligence duty for directors and senior managers, personal liability and restrictions on indemnities and insurance	**Advantages:** Incentivises care in ensuring compliance with the CCCFA, transparency and personal accountability for breaches. **Disadvantages:** Incentives appear to be excessive, in that these settings produce overly conservative lending practices and unnecessary compliance costs. These incentives are likely to be made redundant by licensing model if adopted (under Option A2).
	B2: Retain due diligence duty but remove restrictions on indemnities and insurance	**Advantages:** Same level of liability, but able to be redistributed, meaning incentives largely retained to protect consumers. **Disadvantages:** Unlikely to meaningfully shift conservative lending practices (including because it depends on availability and cost of insurance).
	B3(a): Remove due diligence duty and attendant personal liability	**Advantages:** Addresses overly conservative practices for licenced lenders who account for a significant proportion of lending and claim to be the worst affected.

	for deposit takers licensed under CoFI	**Disadvantages:** Creates different standards of conduct and liability for different types of lenders, with potential for competitive disadvantage.
	B3(b): Remove due diligence duty and attendant personal liability for all lenders on the basis of licensing (see option A2) - **preferred**	**Advantages:** Addresses overly conservative decision-making and supplants liability settings with more proportionate scrutiny and accountability from licensing, assuming this is the approach taken by the FMA. **Disadvantages:** Potential for lenders to take more liberal lending approaches, which may harm consumers. This can be mitigated by the FMA's approach to monitoring.
C) Consequences for incomplete disclosures by lenders	C1: The status quo: retain the 2019 solution without change to addressing risk of disproportionate consequences under section 99(1A)	**Advantages:** Borrowers adequately compensated with no/minimal litigation costs. Strong incentives on lenders to make disclosures and remedy failures. **Disadvantages:** Uncertain liability continues to produce inefficiencies/costs, particularly where no harm caused.
	C2: Cap percentages able to be forfeited based on type of failure	**Advantages:** Slightly improves lender confidence consequences will be reasonable (with associated efficiencies). **Disadvantages:** Does not address costs associated with harmless failures. Low risk of inadequate compensation for affected borrowers (depending on how caps are set).
	C3(a): Remove liability for harmless failures – burden on lenders	**Advantages:** Slightly improves lender confidence consequences will be reasonable (with associated efficiencies). **Disadvantages:** Potential for small increase in litigation costs for lenders. May reduce incentives on lenders where able to argue the failure was harmless.
	C3(b): Remove liability for harmless failures – burden on borrowers – **preferred** (but relies on option A2)	**Advantages:** Further improves lender confidence consequences will be reasonable (with associated efficiencies). **Disadvantages:** Power imbalance and litigation costs mean compensation less likely for borrowers and this reduces incentives on lenders to make disclosure and remedy failures. Expected to be mitigated by FMA intervention, particularly given option A2.
	C4: Repeal provisions and adjust statutory damages	**Advantages:** Significantly reduces likely costs for lenders for each disclosure failure and associated inefficiencies. **Disadvantages:** Significantly reduces likely compensation for affected borrowers, even if statutory damages increased, with reduced incentives on lenders to make proper disclosure and remedy failures.

D) Review of high-cost credit provisions	D1: The status quo – maintain the interest rate threshold that defines a high-cost consumer credit contract at 50% - **preferred**	**Advantages:** Effectively targets contracts that have caused systemic harm (by regulating them out of existence). **Disadvantages:** However, some questions about whether consumers who used to rely on these loans are better or worse off and whether it has limited access to short term loans.
	D2: Reduce the interest rate threshold that defines a high-cost consumer credit contract to 30%	**Advantages:** Possibility of cheaper, more responsible credit in the case of loans closer to 30% (which could be achieved by lenders to avoid additional regulation without significant restructure of their loans). **Disadvantages:** Disruption to the market (20 lenders and 143,000 borrowers). Expected to reduce access to credit.
	D3: Reduce the interest rate threshold that defines a high-cost consumer credit contract to 40%	**Advantages:** Unclear. Lenders affected unlikely to reduce interest rates without significant changes to minimum loan amounts and/or durations. Possibility of more responsible credit of loans in this interest rate range if lenders decide to comply with the high-cost credit provisions. **Disadvantages:** Same as for option D2 but on a reduced scale (13 lenders and 93,000 borrowers).

What criteria will be used to compare options to the status quo?

62. To assess all the options in this RIS against the status quo, we have used three criteria that reflect the policy objectives:

    a. effectively protects the interests of consumers

    b. minimises regulatory burden/compliance costs

    c. promotes fair and transparent markets for credit.

63. We are weighting each criterion equally. They are intended to isolate key trade-offs, such as between protecting consumers for irresponsible lending and removing barriers to efficient loan processing. An explanation of how we are applying each criterion follows.

64. These criteria do not in all cases account for all costs and benefits of the options we analyse in this statement. Where any other factors are relevant in assessing options, we have indicated these separately.

Effectively protects the interests of consumers

65. This reflects the primary purpose of the CCCFA. The main interests that are included in this criterion are the interests of consumers in being able to make informed decisions and being protected from the harm that can be caused by irresponsible lending. However, these interests vary for different consumer groups (e.g. are greater for consumers with poor financial literacy or other vulnerabilities). Other interests may also be relevant here, such as access to affordable credit.

66. To avoid overlap with other criteria, we are excluding from this criterion:

a. the interests of consumers in lenders operating efficiently and with minimal compliance costs, which are likely to be passed on to them (covered by criterion 2)

b. the benefits of competitive neutrality in how lenders are regulated (covered by the concept of 'fair markets' under criterion 3).

Minimises regulatory burden and costs

67. This criterion reflects the primary motivation for the Government considering these reforms and the reference in the CCCFA's other purposes to promoting and facilitating 'efficient' markets for credit.

68. The concepts of regulatory burden and costs both fall within that of efficiency, but are not necessarily identical. For example:

    a. regulatory burden can directly preclude lenders from innovating in a particular way (such as in how they structure the interest and fees chargeable to consumers)

    b. compliance costs can reduce efficiency by diverting resources to compliance that might otherwise be used to improve services or credit products (in ways permitted by the CCCFA).

69. Compliance costs affect consumers more directly than regulatory burden because they are likely to be passed onto consumers via interest charges or fees. Both are considered equally relevant under this criterion.

70. One of the Government's objectives is to streamline provision of financial services, including by avoiding duplication. Under this criterion we also consider any additional regulatory burden or compliance costs that arise from:

    a. differences in how credit is regulated by the FMA compared with other financial services

    b. duplication of requirements for lenders who operate in more than one market regulated by the FMA.

71. Costs include inefficiencies or costs incurred by the regulator (such as those that arise from the regulator needing to operate different regulatory approaches for different markets) .

Promotes fair and transparent markets for credit

72. The concepts of 'fair' and 'transparent' markets for credit are also recognised in the purposes of the CCCFA.

73. Fairness is a subjective term, but there are three main senses in which we apply it:

    a. the CCCFA providing a fair or level playing field for lenders (i.e. competitive neutrality)

    b. just/proportionate outcomes where breaches of the CCCFA occur

    c. natural/procedural justice.

74. Transparency is assessed as transparency for consumers and enforcement under this criterion. It is a matter of how easy it is for consumers to understand credit products, how transparent about their processes and decisions lenders are with consumers, the regulator and dispute resolution schemes, and how openly parties are able to or expected to communicate, other than through specific disclosure requirements.

75. By considering fairness and transparency together within this criterion, we are effectively half-weighting them. It is possible they would counteract each other, making an option neutral against this criterion.

What scope will options be considered within?

76. The scope, issues and options reflect the Government's objectives for the reform. The pace at which the Minister wishes to pursue these reforms has meant we have prioritised the issues that are seen as the most pressing. We have been working towards the Minister's aim of having legislation for all financial services reforms introduced by the end of this year. This has precluded us from:

    a. exploring ways to more fully resolve differences between consumer credit law and other financial services regulation, such as by integrating the CCCFA into the FMC Act

    b. more fully reviewing certain settings, such as disclosure requirements

77. This means other reforms may be desirable in the near future.

78. The statutory review of high-cost credit specifically requires the Minister to consider expanding the definition of high-cost credit to an interest rate between 30% and 50%.

Issue A: Regulatory model

What options are being considered?

Option A1 (the counterfactual) – Retain 'fit and proper' certification and add some FMA tools

Description

79. Under this option, the transfer of regulatory responsibility from the Commission to the FMA would be achieved by adding some FMA core regulatory tools (i.e. direction and stop order powers) but retaining the current certification model.

80. Lenders would continue to apply to the regulator (FMA) for certification that their directors and senior managers are fit and proper persons to hold their positions, every five years, unless exempt (e.g. because they are already licensed by the FMA or RBNZ). Certification by the Commerce Commission costs $1,055 (excluding GST) for each director and senior manager every five years – though this fee would instead be based on cost-recovery for the FMA.

Advantages/benefits

81. Adding the FMA core regulatory tools would allow for the FMA to be a reasonably responsive regulator with a wider range of tools than under the status quo. This improves the FMA's ability to protect the interests of consumers, although less than option A2. Furthermore, this option would cause relatively little disruption to the industry.

Disadvantages/costs

82. This option limits the FMA's toolkit and ability to monitor and regulate conduct effectively and efficiently in the interests of consumers. Retaining a certification model is inconsistent with the approach to regulating other consumer financial services. This would lead to inefficiencies for lenders (e.g. banks) who also operate in those other markets, and for the FMA in having to navigate two different systems and procedures. The lenders affected by this difference in approach account for a significant proportion of lending.

83. Lenders who are not exempt would need to renew their certification every five years. As well as the cost and time to prepare for recertification, application fees are currently $1,055 (excluding GST) for each director and senior manager.

84. Regulating consumer credit differently to other market services continues fragmentation and duplication, and risks that markets are less fair and transparent.

Stakeholder views

85. Lenders and an industry bodies suggest the certification model provides lower entry criteria than a market services licence. They suggest this benefits smaller lenders and helps to increase diversity and innovation within the industry. They view competition and innovation within the consumer credit market as advantageous for consumers. A consumer advocate points to the Commerce Commission's market study into personal banking draft report to indicate New Zealanders are not well-served with regards to competition in this area.

86. A law firm views the existing model as sufficient for current purposes, and believes retaining the 'fit and proper' certification will cause the least disruption to the industry.

Option A2 – Transition to a market services licence and apply all FMA licensing and core tools (preferred)

Description

87. Under this option, transfer of regulatory responsibility to the FMA would be achieved by requiring all consumer lenders to have a market services licence for consumer credit. It also provides the FMA with all its regulatory toolkit for licensing and direction and stop orders.

88. Licensing establishes a monitoring relationship between the FMA and regulated entities. The FMA must be satisfied that the entity is capable of effectively performing the service and there is no reason to believe the entity is likely to breach its obligations. The FMA is able to impose and vary licence conditions, as well as suspend or cancel the licence where the lender's conduct justifies this. Once licensed, a lender does not need to have it renewed.

89. Under this option, lenders would be 'deemed' to hold a market services licence from the FMA if they:

    a. are already certified by the Commission (there are currently 457)

    b. are currently exempt from certification on the basis they are licensed by the FMA or licensed by or registered with RBNZ (there are currently 32).

90. The lenders who are currently exempt from certification for other reasons (e.g. certain securitisation arrangements or interim credit provided by non-financial service businesses[14]) would be exempt from this licensing requirement. This includes 496 non-financial service businesses who are currently exempt from certification under regulation 28.

91. Only new entrants to the consumer credit market would be required to obtain a licence. There is a one-off cost to obtain a licence, which we expect would be in the order of $700 - $1,000 (excluding GST) based on the current cost of a licence for providing a financial advice service (for which there are three categorises, with different costs).

92. The approach to 'deem' most of the existing consumer lenders to hold a licence differs to the transitional approach we consulted on. We consulted on automatically providing existing lenders with transitional licence which they would need to upgrade to a full licence at the end of the transitional period.

93. Based in part on advice from the FMA, we have since concluded that a 'deemed' licence approach would work better under this option than a transitional licence approach. The lenders receiving deemed licences would be a known population, because they are registered on the Financial Services Providers Register or exempt because they are regulated by the FMA or RBNZ already.

Advantages/benefits

94. Where the FMA has its core regulatory tools and licensing powers, this would enable the FMA to deliver cost-effective and proportionate regulation and respond to harm without subjecting firms or the wider sector to unnecessary regulatory burden or costs.

[14] See e.g. regulations 27 – 28, Credit Contracts and Consumer Finance Regulations 2004.

95. The availability of tools like action plans likely improves the FMA's ability to act quickly and protect the interests of consumers. It also delivers efficiencies from consistency and alignment of consumer credit with other financial services.

96. A deemed licence removes the uncertainty and regulatory burden of needing to prepare for a licensing application process and would have no licensing costs or process for lenders (certified or exempt at date of commencement of relevant provisions). It would in fact reduce costs for existing lenders, who would otherwise be required to renew their certification every five years.

97. A deemed licence would also enable the FMA to effectively supervise these lenders on an ongoing basis.

98. The FMA has advised that deemed licensing will not create an additional regulatory burden on existing lenders.

Disadvantages/costs

99. The extent of regulatory and compliance burden under this option depends on how the licensing regime is designed and implemented by the FMA.

100. The approach of 'deemed' licensing treats existing lenders and new entrants differently. In the discussion document, we noted that this option risks negatively impacting competition by advantaging incumbents and inhibiting entry into the market and associated diversity and innovation.

101. Having discussed this further with the FMA and the Commission, we have downgraded our assessment of these impacts. Even though the conditions required to be met by existing and new entrant lenders will be different, we anticipate little to no change in terms of compliance costs and entry rate in practice. However, it is theoretically possible for the FMA's licensing approach to impose a higher standard. A higher standard for entry would also have potential to lessen competition and innovation by new lenders.

102. There is a potential increase to regulatory burden or compliance costs associated with *ongoing* monitoring by the FMA under a licensing model. One example is that the FMA may at some stage require lenders to provide with more information than required under the status quo to support its monitoring of lenders.

Stakeholder views

103. Stakeholders have stated that there will be better enforcement with this model. A law firm stated that adopting a licensing model would create consistency accross entities licensed by the FMA, and aligns with the single licence proposal in CoFI.

104. However, it is a common view amongst various stakeholders that there will be higher costs for those that are not already licensed through understanding the new obligations and implementation of new processes. This can mean that some lenders will leave the market, and compliance costs may increase which may be passed onto consumers.

105. Some lenders further pointed to the 2024 Commerce Commission personal banking services draft report to show the importance of competition and innovation.

106. A financial mentor saw a higher entry criteria as a benefit as it means lenders overall would be more aware of their obligations, which protects the interests of consumers.

How do the options compare to the status quo/counterfactual?

	Option One (A1) – Retain 'fit and proper' certification (counterfactual) and apply some FMA tools	Option Two (A2) – Transition to a market services licence and apply licensing and all core FMA tools
Effectively protects interests of consumers	+ Provides the FMA with some additional tools.	++ The FMA will have additional tools that enable it to more closely and proactive oversee lenders, which is more conducive to protecting the interests of consumers.
Minimises regulatory burden/costs	**-/0** Re-certification is required every 5 years. Continues misalignment with regulation of other market services.	+ The deemed licensing approach would be cheaper for lenders already certified or exempt in terms of up-front costs. Ongoing costs/burden from FMA monitoring depend on its approach. One licensing regime is likely to be less costly for the FMA to administer and less costly for lenders that operate in other markets.
Fair and transparent markets for credit	**0** Lenders continue to know what to expect to demonstrate compliance. However, FMA having to develop a different regulatory approach for other markets creates uncertainty for lenders.	+ Potential unfairness for lenders wanting to enter the market (unlevel playing field), but considered unlikely in practice. Better FMA powers and opportunities to supervise conduct in the credit market expected to improve transparency.
Overall assessment	**0/+**	++++

Key for qualitative judgements:

++	much better than doing nothing/the status quo/counterfactual
+	better than doing nothing/the status quo/counterfactual
0	about the same as doing nothing/the status quo/counterfactual
-	worse than doing nothing/the status quo/counterfactual
- -	much worse than doing nothing/the status quo/counterfactual

What option is likely to best address the problem and deliver the highest net benefits?

107. We assess option A2 as most likely to address the problem and produce net benefits against the critieria. It would enable the FMA to more effectively regulate consumer credit in the interests of consumers. This option may support lenders to operate more efficiently, depending on the FMA's approach to assessing new licences and overseeing lenders.

Issue B: Personal liability settings

What options are being considered?

Option B1 (the status quo) – Retain due diligence duty, personal liability for directors and senior managers and restrictions on indemnities and insurance

Description

108. This option retains the current settings for due diligence and personal liability for directors and senior managers. The due diligence duty was introduced in December 2021, alongside other changes, to help drive compliance with and accountability under the CCCFA.

109. Under a different provision in the CCCFA, directors and senior managers are also held liable where they were knowingly or deliberately involved in contravention.

110. Under the certification model, the FMA would be limited to using formal interventions and have limited direct regulatory oversight of consumer credit.

Advantages/benefits

111. This option provides strong incentives on directors and senior managers to ensure the lender is complying with its obligations under the CCCFA.

112. It is unclear the extent to which compliance and protection for consumers have improved in the short time since the duty and liability has existed. We understand breaches of the due diligence duty are typically only discovered when the Commission investigates other potential breaches of the CCCFA, rather than proactively.

Disadvantages/costs

113. We would expect these settings to continue producing overly conservative lending practices, which can be inefficient and costly.

114. Retaining the settings for personal liability, insurance and indemnity continue a different and harsher regulatory setting for consumer credit compared to other consumer financial services.

115. If licensing is progressed, retaining the due diligence duty would duplicate the equivalent obligations under the FMC Act licensing provisions.

Stakeholder views

116. Some lenders reiterated that 2021 reforms to consumer credit law resulted in more conservative lending decisions than intended, and reported their experiences of these reforms. This included that personal liability for breaching the due diligence duty and interpretational difficulties have led to them taking a more conservative lending approach.

117. One lender stated that their approval rates fell from an average of 33% in the 12 months prior to the reforms to 11% immediately after the 2021 CCCFA reforms. A finance company considers that the CCCFA is not fit for purpose as it is making people too cautious, prevents innovation and startups. A law firm has submitted that, in their experience, the due diligence duty and personal liability has led to overly conservative lending approaches.

118. However, some stakeholders, including a consumer advocate, viewed the CCCFA as operating as intended, and that the status quo should be kept to incentivise lenders to comply with their obligations to protect consumers. A consumer advocate thought that lenders with more revenue would be able to take risks smaller lenders could not, and shield directors and senior managers from penalties.

Option B2 – Retain due diligence duty but remove restrictions on indemnities and insurance

Description

119. This option would preserve the current due diligence duty and personal liability for directors and senior managers, but remove the restriction on indemnities and insurance.

120. Directors and senior managers may also be held liable where they were knowingly or deliberately involved in contravention.

Advantages/benefits

121. This option continues to provide incentives for directors and senior managers to take their lending responsibilities seriously but allows the consequences to be transferred (if an indemnity or insurance or both can be obtained) from the individuals to the business (in the case of indemnity) and/or an insurer (for insurance).

Disadvantages/costs

122. There may be additional costs to lenders in securing indemnity or insurance. We expect little change to lenders' compliance costs, as the risk would merely be transferred from the individuals rather than removed.

123. Retaining the settings for personal liability continue a different and more expensive regulatory setting for consumer credit compared to other financial services.

124. We do not anticipate any change in how this option promotes fair and transparent markets, nor do we consider that this option will improve lender behaviour.

Stakeholder views

125. Two lenders stated that, although the availability of insurance and indemnities would make lenders "more comfortable", it would not make a change in their conservative lending, citing reputational reasons. A financial mentor and a law firm shared similar views. A law firm stated that indemnification may not make material changes where compliance is embedded in lender processes, but it may help senior managers and directors feel more confident in taking more balanced risk-based decisions on challenging compliance decisions.

126. A lender indicated that retaining personal liability would continue to strongly incentivise lenders to adopt an inflexible, conservative approach to lending. Other stakeholders expressed similar views. Some lenders suggested that there may be difficulty for lenders in finding adequate insurance within the NZ market, or it will be at great expense if available.

127. Some lenders have indicated that removing a restriction on insurance and indemnities may benefit smaller lenders in attracting directors and senior managers.

Option B3 – Remove due diligence duty and attendant liability for licenced lenders (preferred)

128. This option would remove the due diligence duty for directors and senior managers of licensed lenders, that is, either:

    a. Option B3(a) for consumer credit lenders who have a market services licence for acting as a financial institution (CoFI licence), or

    b. Option B3(b) for licensed consumer credit lenders (preferred if chosen with option A2).

129. If a licensing model was adopted (Option A2), this would reduce, if not remove, the need to retain the due diligence duty and personal liability for licensed lenders' directors and senior

managers. The need to meet licensing obligations on an ongoing basis would become the conduct incentive in place of due diligence.

130. The role of the due diligence duty and associated personal liability plays in incentivising directors and senior managers to develop good systems for complying with CCCFA is similar to that played by the FMA's oversight of market services licence holders. The CCCFA approach incentivises conduct via a statutory duty, while market services regulation under the FMC Act combines general duties with direct monitoring and intervention to shape conduct. Licence holders are required to be capable of effectively carrying out the service.

131. In any case, directors and senior managers can still be held liable where they were knowingly or deliberately involved in contravention.[15]

Advantages/benefits

132. To a limited extent, this option would realign credit law with financial markets and general corporate law.

<u>B3(a) - financial institutions only</u>

133. Although due diligence duty and personal liability would be removed for CoFI lenders under this option, these lenders would still be subject to greater scrutiny over the products and services they provide.

134. Lenders that hold a CoFI licence are already subject to obligations under the FMC Act. This option removes duplicated duties and may make lenders licensed under the CoFI Act less inclined to take conservative lending approaches. However, this may not make a significant difference for those lenders where compliance is built into their processes.

<u>B3(b) - licensed consumer credit lenders (if Option A2 is adopted).</u>

135. The removal of the due diligence duty and personal liability will likely result in fewer conservative lending practices from consumer credit lenders. It may also help to attract or retain senior managers and directors to firms.[16]

136. The FMA states that there will be no further regulatory burden if the licensing model was proceeded with.

Disadvantages/costs

<u>B3(a) - financial institutions only</u>

137. This option will likely mean non-licensed consumer lenders whose directors and senior managers are subject to the due diligence duty and personal liability will continue to take a conservative lending approach.[17]

138. It may provide licensed under CoFI a competitive advantage over other lenders if the due diligence duty will no longer be tied to personal liability, meaning they may be less inclined to take a conservative approach to lending and have more resources to invest in innovation.

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[15] Sections 93(d) and s107A(1)(c) – (f) of the CCCFA.

[16] Supported by multiple non-bank deposit takers, law firm and a lender.

[17] Sections 93(d) and s107A(1)(c) – (f) of the CCCFA.

Lenders and the FMA would have to navigate the two-tiered approach, which involves different obligations and regulatory models.

<u>B3(b) - licensed consumer credit lenders</u>

139. Whether this would continue to protect the interests of consumers and whether compliance costs increase will depend on the enforcement approach that the FMA takes.

Stakeholder views

140. Some stakeholders, including lenders, indicated that the due diligence duty has led to overly conservative approaches to their lending, slowed down credit processes, increased costs, and reduced their ability to provide access to credit by increasing the compliance burden. One lender indicated that their home loan approval rates dropped by a third post-2021 CCCFA reforms from 33% to 11% due to its conservative approach.

141. Some lenders indicated that larger lenders have an advantage over smaller lenders to comply with their due diligence obligations due to resourcing. They indicated this puts a higher onus on directors and senior managers of these smaller lenders which creates additional barriers to competition.

142. Various stakeholders suggest that because CoFI and CCCFA regimes are different, the obligations and penalties should be different.

143. Several stakeholders including lenders and a consumer advocate question whether ongoing oversight through licensing would be able to encourage responsible lending compared the due diligence duty itself. Many of the same stakeholders state that the due diligence duty provides a deterrence for bad behaviour and irresponsible lending by lenders.

144. A lender thought that if due diligence was removed only for those licensed under the CoFI Act it would create an unfair advantage those lenders. A law firm stated that the difference between CoFI licensing and the certification is not large enough to justify different treatment for licensed lenders.

145. The Commerce Commission is of the view that obligations under CoFI licensed lenders are not a precise substitute for the CCCFA due diligence duty.

146. A law firm, although they support the removal of the due diligence duty, states that success may depend on the extent of ongoing supervision and licensing processes.

How do the options compare to the status quo/counterfactual?

	Option One (B1) – *Status Quo / Counterfactual*	**Option Three (B2)** – Retain the due diligence duty but remove restriction on indemnities and insurance	**Option Two (B3)** – Remove due diligence duty for licenced lenders
Effectively protects interests of consumers	**0** Provides strong incentives to ensure compliance with CCCFA obligations	**0** Retains personal liability for directors and senior managers, providing some relief to lenders.	**-/0** **B3(a)** Although due diligence duty is removed for CoFI lenders, these lenders will still be subject to scrutiny over the products and services they provide. Directors and senior managers will still be liable where they were knowingly or deliberately involved in contravention. **0** **B3(b)** May be effective when paired with the licensing model under option A2. However, this will depend on the supervisory approach the FMA takes. Directors and senior managers will still be liable where they were knowingly or deliberately involved in contravention.
Minimises regulatory burden/ costs	**0** High compliance costs and regulatory burden, resulting in overly conservative lending practices	**0/+** Lenders' compliance costs and regulatory burden will be redistributed without reducing the lender's overall liability. Potential for this to reduce the burden in practice, with liability at arm's length from directors/senior managers and availability of insurance	**+** **B3(a)** Likely to reduce compliance costs for licensed CoFI lenders who account for a significant proportion of lending. No change expected for other lenders. **++** **B3(b)** The FMA suggests they are likely to expect roughly the same efforts from lenders as the due diligence duty. Some efficiencies possible for CoFI lenders from consistency of approach.

Fair and transparent markets for credit	**0** Fairness and transparency promoted by due diligence duty and personal accountability of directors and senior managers	**0** No material change expected	**-** **B3(a)** The two-tiered approach would reduce fairness and transparency for non-licensed consumer credit lenders. Assuming those lenders continue to take conservative lending approach, this may lead to CoFI lenders having a competitive. **0** **B3(b)** This would maintain fairness as all senior managers and directors of lenders will no longer be personally liable for due diligence duty unless they are knowingly or deliberately involved in a contravention of the CCCFA.
Overall assessment	**0**	**0/+**	**Option B3(a): -/0** **Option B3(b): ++**

Key for qualitative judgements:

++	much better than doing nothing/the status quo/counterfactual
+	better than doing nothing/the status quo/counterfactual
0	about the same as doing nothing/the status quo/counterfactual
-	worse than doing nothing/the status quo/counterfactual
- -	much worse than doing nothing/the status quo/counterfactual

What option is likely to best address the problem and deliver the highest net benefits?

Although option B3(b) relies on option A2 (which we prefer independently), assessing option B3(b) on its own merits, we believe it is most likely to address the problem and produce net benefits against the critieria. This reflects our understanding the FMA would use its regulatory tools in a manner has all the benefits of the status quo, while avoiding the problems identified.

Issue C: Consequences for incomplete disclosures by lenders

What options are being considered?

Option C1 (the status quo) – Forfeiture of costs of borrowing with relief available under section 95A (from December 2019)

Description

147. This option would maintain the current consequences under section 99(1A) and the current method of avoiding disproportionate consequences via relief under section 95A from December 2019 onwards. Section 99(1A) gives affected borrowers an entitlement to not pay or to recover the costs of borrowing for the period before the failure is corrected. Lenders can ask the court to have this entitlement removed or reduced as appropriate in the circumstances under section 95A.

Advantages/benefits

148. Lenders are effectively incentivised by the nature of this liability to ensure they are providing borrowers with the information required, and to immediately address any failure to do so. This is consistent with the Commerce Commission's observation that, when section 99(1A) took effect in 2015, it significantly improved the quality of information disclosed to consumers. This helps to protect the interests of consumers by giving them an effective remedy in the event they are harmed by a disclosure failure, and one that is easier in practice to access than other remedies, such as statutory damages.

Disadvantages/costs

149. The Commerce Commission states that it takes a proportionate approach in responding to any disclosure failures subject to this provision, even where those failures precede section 95A. It tends to apply a materiality test as well as sections 95A and 95B to reduce the compensation it expects from lenders when section 99(1A) is triggered. For instance, the Commission does not tend to invoke section 99(1A) if a lender fails to disclose information that is unlikely to be material to the borrower.

150. Nonethless, uncertainty on how the relief will be applied, means that the problem of overly conservative approaches to ensuring compliance with disclosure requirements, and unnecessary litigation costs, has not been fully addressed by the relief available under section 95A. Inefficiencies and disproportionate costs would therefore continue to impact lenders and borrowers.

Stakeholder views

151. Lenders express strong concerns with section 99(1A), and argue that it poses threats to their solvency, stability or existence. This appears to relate largely to the fact relief under section 95A was not applied retrospectively. However, the industry also believes section 95A has not adequately addressed the problem. They do not believe it is reasonable to expect them to apply to a court for this relief (which no lender has yet done because these matters tend to get settled out of court) and suggest the potential consequences for disclosure breaches remain excessive.

152. On the other hand, consumer advocates and financial mentors believe that the status quo should be retained as it provides incentives for lenders that are necessary to ensure their compliance with the disclosure requirements.

Option C2 – Cap the percentages that can be forfeited to each borrower, depending on the type of disclosure failure

Description

153. This option involves setting limits to ensure the lender never forfeits more than a certain percentage of the costs of borrowing to a particular borrower, depending on the type of disclosure failure. There would still be discretion for a court to determine the amount of relief that is appropriate under sections 95A and 95B, but only within these limits.

154. Though noting that harm to the borrower is generally fact-dependent, maximum percentages could be set is to distinguish the relative seriousness of:

   a. failure to make disclosure at all (e.g. ensuring a lender is never required to forfeit more than 75 percent of the costs of borrowing)

   b. failure to disclose all the particulars required by the CCCFA (e.g. ensuring a lender is never required to forfeit more than 40% of the costs of borrowing)

   c. complete disclosure that is made just after the statutory deadline (e.g. ensuring a lender is never required to forfeit more than 20% of the costs of borrowing).

Advantages/benefits

155. Depending on how the caps are set, this option could improve lender confidence that forfeiture will not be disproportionate. It also makes it much easier for lenders to assess the potential extent of their liability for a given failure, while preserving their ability to seek relief.

156. This may create some efficiencies in how lenders meet disclosure requirements, with a reduction in compliance costs passed onto consumers.

Disadvantages/costs

157. If caps are set too low, this option could involve a risk of under-compensating borrowers for the harm caused by disclosure failures. This could also reduce incentives for lenders to take appropriate care to disclose the information required and quickly address any failure to do so. We consider this risk to be low.

158. This option would not address inefficiencies and costs associated with lenders responding to harmless disclosure failures.

Stakeholder views

159. The original option we consulted on involved a cap on total liability for a given disclosure failure affecting multiple borrowers. Lenders argued the original option would be difficult to design and implement. This option has been modified to address these concerns.

160. Consumer advocates generally did not support the original option either.

Option C3 – Exclude disclosure failures that cause no harm to borrowers

161. This option would confirm that no forfeiture of interest and fees is required for a disclosure failure that has not harmed the borrower. We have identified two ways this could work (as sub-options) in terms of which party has the burden of proving harm (or its absence):

   a. Option C3(a): section 99(1A) would not apply if the lender can satisfy a court there was no harm. The idea is that lenders would have more confidence they can avoid forfeiture in these circumstances (e.g. be insulated from unreasonable demands for forfeiture).

Where the lender accepts there was harm, or fails to persuade a court there was no harm, a court could still award relief under section 95A.

b. Option C3(b): section 99(1A) would only apply if affected borrowers, or the FMA on their behalf, satisfy a court that the lender's failure did cause harm. The court could then make a declaration that section 99(1A) applies and award any relief to the lender it considers appropriate under section 95A. The idea is that this would further reassure lenders they are not liable where the failure was not prejudicial because the burden of proving otherwise would be on borrowers or the FMA. Where the FMA has concerns about the impact on borrowers, it would have tools it could use to address the potential misconduct. The FMA may also negotiate/secure compensation for borrowers (particularly if Option A2 is pursued).

Advantages/benefits

162. Retaining the potential for lenders to forfeit some or all of the costs of borrowing under section 99(1A) continues effective incentives (that are not provided by other forms of liability) for lenders to comply, and promptly remedy defective disclosure. This benefits borrowers.

163. We would expect both sub-options to address the problem associated with harmless failures. They would improve the confidence of lenders that they can avoid any forfeiture of interest and fees in these cases, and we would expect this to improve negotiated outcomes for lenders (outside of court). Although we understand the Commission already applies a 'materiality' threshold, lenders would also be protected from action by private parties in these cases. This is likely to produce some modest efficiencies as a result of lenders making more proportionate efforts to disclose the particulars required by the CCCFA, and through avoided litigation costs where harmless failures do occur.

Benefits specific to sub-option C3(b): section 99(1A) only applies if affected borrowers or the FMA satisfy a court that the lender's failure did harm borrowers)

164. The FMA favours this sub-option on the basis that it could intervene on behalf of borrowers, particularly if the licensing powers under option A2 are available.

165. Sub-option C3(b) would have further advantages in terms of efficiencies and avoided costs for lenders, as it transfers the burden of proof (of the harm suffered) from the lender to affected borrowers or the FMA on their behalf. It also transfers some of the associated litigation costs where harm is disputed.

Disadvantages/costs

166. Both sub-options have the potential to reduce transparency by lenders and compensation for borrowers affected by a failure wherever there is an argument that they were not harmed.

167. The Commission's experience is that lenders commonly take the view that incomplete disclosures have caused no harm to borrowers, even where more than one item of what the CCCFA treats as 'key information' was missing from initial disclosure.

Disadvantages specific to sub-option C3(b): section 99(1A) would only apply if affected borrowers or the FMA satisfy a court that the lender's failure did harm borrowers

168. The risk of harm to the interests of consumers is greater under sub-option (b) because it is only where affected borrowers or the FMA can prove to a court there was harm that lenders have any liability under section 99(1A).

169. Affected borrowers are generally not well placed and resourced to discharge this burden. This may mean that lenders are less incentivised to ensure they comply with the disclosure requirements and work with affected borrowers or the FMA to remedy failures.

170. The worst case scenario under this sub-option is that the incentives provided by section 99(1A) are completely removed and the effect is comparable to option C4 (below). This could be the outcome if the prospect of a court declaring borrowers were harmed by a failure is too low for section 99(1A) to faciliate compensation in practice (e.g. because it is easier to obtain statutory damages, which do not require proof of harm),

171. Our view is that Option A2 would be necessary to ensure the benefits of this sub-option outweigh the potential harm to the interests of consumers. The oversight approach enabled by Option A2 would give the FMA effective mechanisms to detect failures and work with lenders to secure an appropriate remedy for affected borrowers without recourse to court.

Both sub-options

172. There are likely to be litigation costs associated with an increase in disputes over whether the lender is liable to forfeit any of the costs of borrowing. The two sub-options distribute these costs differently:

    a. Sub-option (a) assigns those costs to lenders, which may not differ from the costs they already incur in dealing with relatively harmless disclosure failures under section 95A

    b. Sub-option (b) assigns these costs to affected borrowers, or the FMA. This may present a significant barrier to affected borrowers obtaining compensation or otherwise create additional costs for the FMA in needing to intervene for borrowers. With effective regulatory tools (i.e. those available under Option A2), the FMA may be able to find more cost-effective ways to address the potential misconduct and to negotiate to secure compensation for borrowers.

Stakeholder views

173. Lenders argued a threshold along the lines of 'harm' or 'materiality' of the failure would contribute to uncertainty about their liability.

174. Some other stakeholders also had concerns about added complexity, depending on how the test is formulated, particularly if borrowers have the burden of proof.

175. It is difficult to know to what extent opposition to this option is the result of strong preferences for either repeal or the status quo.

176. Lenders and consumer advocates differed predictably on whether lenders or borrowers should have the burden of showing the failure was material/harmful. Consumer advocates point to a power imbalance and higher barriers to justice in support of their view.

Option C4 – Repeal sections 99(1A), 95A and 95B and adjust statutory damages

Description

177. This option is to repeal section 99(1A), so that lenders are never required to forfeit the costs of borrowing in the event of a disclosure failure. Lenders would still be unable to enforce the contract until they correct the failure, but would be entitled at that point to recover any unpaid interest and fees.

178. Under this option, we would consider whether the amount of statutory damages prescribed by section 89 remains sufficient to continue:

a. incentivising lenders to take appropriate care in making proper disclosures

b. ensuring adequate compensation for borrowers.

179. This recognises important differences between the consequences of section 99(1A) and statutory damages, which may explain the Commission's obversation of signficantly improved disclosures since 2015:

a. Whereas section 99(1A) creates an entitlement on part of all affected borrowers (which must be implemented by the lender), statutory damages must be sought by individual borrowers (for example, through dispute resolution schemes) or the Commerce Commission on their behalf.[18] In practice, this likely means that borrowers who are aware of the failure are less likely to be compensated than where section 99(1A) applies.

b. The maximum amount of statutory damages is specified by the CCCFA, and not based on a calculation of the costs of borrowing that have accumulated since the breach.

Advantages/benefits

180. This option would most effectively address the problem by significantly reducing the possible consequences of failure to disclose information properly to borrowers. This is likely to create efficiencies and reduce compliance costs.

Disadvantages/costs

181. We would expect this option, more than any other, to reduce incentives on lenders to take appropriate care in making proper disclosures and to identify and to rectify any failures to do so. Other remedies available to borrowers, even with statutory damages increased, provide less meaningful incentives and makes enforcement more costly for affected borrowers.

182. It would also increase costs associated with pursuing other remedies, particularly statutory damages. These costs are likely to be incurred by the FMA, rather than dispute resolution processes, given disclosure failures generally affect multiple borrowers.

Stakeholder views

183. Several lenders consider this option would most effectively address the disproportionate impacts of section 99(1A). They consider that the CCCFA already allows consumers to be compensated for any loss they suffer. They also consider that other potential penalties under the CCCFA would provide adequate incentives to ensure proper disclosures.

184. Confidentiality

[18] There are a few examples of statutory damages also being sought by the Commission, but this tends to be reserved for more egregious breaches affecting a class of borrowers.

185. Consumer advocates strongly oppose this option and reiterate the value of section 99(1A) in protecting consumers.

Application of relief under section 95A retrospectively to limit pre-2019 liability

186. In 2019, we considered retrospectively applying the ability for lenders to seek relief (under what it is now section 95A) from the problems with section 99(1A). It was dismissed on the basis that legislation with retrospective effect can generally only be justified where it is intended to be entirely for the benefit of those affected, with no adverse impacts for others.

187. We have not consulted on or analysed in this RIS any options with retrospective effect. However, we note the ongoing concerns expressed by lenders.

188. One way of retrospectively changing the effect of section 99(1A) that remains is to back-date the relief from disproportionate liability provided by section 95A to June 2015 (when section 99(1A) took effect). This would limit any liability arising from failures during that period which have not already been settled. This would give lenders the opportunity to ask the court to extinguish or reduce the amount of compensation under section 95A. If it does result in judicial application of section 95A, this option may reduce uncertainty about how section 95A operates and its effectiveness.

189. Retrospective intervention in this case would raise some natural justice questions (e.g. by altering the rights of borrowers that were provided by the law at the time they entered into their loan agreements) and constitutional questions (e.g. by changing the law that is actively being applied by the judiciary or, potentially, overturning a judicial decision), and a key consideration would be whether it would be in the public interest to do so.

How do the options compare to the status quo/counterfactual?

	Option C1: Status quo	Option C2: Capped percentages	Option C3(a): Consequences do not apply if the lender can establish no harm	Option C3(b): Consequences only apply if borrower can establish harm	Option C4: Repeal sections and adjust statutory damages
Effectively protects interests of consumers	**0** Borrowers are well compensated for breaches with minimal costs/procedure. Strong incentives to ensure complete disclosure and remedy errors.	**0/-** Risk of negative impact on interests of consumers, would depend on how caps are set.	**0/-** Lenders may be slightly less incentivised to remedy failures where harm is debateable.	**-** Lenders less incentivised to ensure complete disclosure and remedy failures (particularly where harm is debateable). Harder for consumers to seek compensation. Mitigated by effective FMA intervention (dependent on option A2).	**- -** Would reduce incentives on lenders to comply or notify.
Minimises regulatory burden/costs	**0** Relief available under s95A is designed to make liability proportionate, but uncertain liability continues to produce some inefficiencies/costs.	**+** Slightly improves lender confidence forfeiture won't be disproportionate, but little impact on costs relating to harmless cases.	**0/+** Marginally improves lender confidence no forfeiture required in harmless cases (at least where private action is threatened). May reduce inefficiencies/costs, but likely offset by small increase in private litigation costs.	**+/++** Further improves lender confidence no forfeiture required in harmless cases, which may reduce inefficiencies/costs. Some additional costs incurred by FMA where it accepts burden of proving harm.	**++** Reduces likely costs for lenders for each failure. May increase costs to FMA in pursuing other remedies to harm.
Fair and transparent markets for credit	**0** Liability promotes transparency where failures occur, and s95A designed for fairness	**0** Transparency and fairness neutral.	**+** Fairness increased/more apparent in harmless cases	**+** Fairness increased/more apparent, assuming credible threat of FMA intervention to	**-** Fairness and transparency materially reduced.

				prevent lenders failing to recognise genuine harm.	
Overall assessment	**0**	0/+	+	+/++	-

Key for qualitative judgements:

++	much better than doing nothing/the status quo/counterfactual
+	better than doing nothing/the status quo/counterfactual
0	about the same as doing nothing/the status quo/counterfactual
-	worse than doing nothing/the status quo/counterfactual
- -	much worse than doing nothing/the status quo/counterfactual

What option is likely to best address the problem and deliver the highest net benefits?

190. We assess option C3(b) as most likely to address the problem and produce net benefits against the critieria. This conclusion relies on the assumption that liability under section 99(1A) and the regulatory tools proposed under option A2 would together enable the FMA to intervene effectively to secure compensation for borrowers who have been harmed by a disclosure failure. Option C3(a) is a close second. It is the only other option that we would expect to improve on the status quo.

Section 3: Delivering an option

How will the new arrangements be implemented?

230. Each of the preferred options would require changes to the CCCFA (and other legislation). They would predominantly be implemented by the FMA, who will have responsibility for the operation and enforcement of consumer credit.

231. The success of the preferred options largely depends on effective implementation by the FMA in terms of the systems, procedures and policies it develops to license, guide, monitor and intervene in markets for consumer credit. The commencement of the relevant legislative changes would be delayed to ensure the FMA is in a position to implement them.

232. Changes to the regulatory model and personal liability settings would coincide with the transfer of functions to the FMA and the transfer of the Commission's credit-related appropriation. Changes proposed to align aspects of the CCCFA with the financial markets conduct regulatory model (such as licensing, direction and stop orders) will require updates and adaptation of existing systems, processes, and procedures and regulatory approach to include credit. The FMA has recently been given responsibility for new regulatory areas such as conduct of financial institutions regime, insurance contract law, climate-related disclosures, and has experience adapting to change.

233. The transfer will also include standard transitional provisions relating to ongoing matters, such as decisions on certification and allowing the new regulator to take over certain proceedings.

234. It is important that the transition and changes are well communicated to key stakeholders. The FMA, as it has done for financial advice providers and conduct of financial institution (CoFI) changes, will proactively engage with stakeholders ahead of the changes coming into force. This includes supporting lenders who are not currently regulated by the FMA to make the transition to licensing (through a deemed licence), to provide certainty to all lenders about FMA's regulatory approach, and to support other stakeholders to migrate existing relationships and channels of communication to the FMA.

235. The monitoring and oversight relationship created by licensing (including deemed licensing) would support the FMA to establish working relationships with lenders and greater familiarity with their practices. This would help the FMA to work out how to best prioritise its resources.

236. If the Government decides to extend the high-cost credit provisions to lending at lower interest rates, we would provide advice on what notice period is reasonable to enable affected lenders to either comply with those provisions or restructure their loans to ensure they are not affected.

How will the new arrangements be monitored, evaluated, and reviewed?

Monitoring

237. The system-level impacts of the proposals will be monitored primarily by the FMA as part of its role in monitoring and responding to market conduct issues and in enforcing the credit obligations following the transfer of regulatory responsibility for CCCFA to FMA.

238. We will monitor the actions of the FMA as the new regulator for credit, including its licencing programme to assess whether the expected impacts on the lending market do in fact occur.

239. MBIE is the monitor for the FMA and we use financial and non-financial performance metrics as part of the annual Crown Entity monitoring programme. Our monitoring work will also include stakeholder engagement, complaints data and environmental scanning.

240. As the enforcement agency for the CCCFA, the FMA will have access to annual return information from lenders collected under the existing regime. This provides some limited statistical information in relation to the lender's business. Lenders must also keep records of about the Responsible Lending inquiries they make, and the results of those inquiries. The FMA can use this information, as well as other information and data they have access to and information from other government and community agencies, to identify current issues and emerging risks that have the potential to affect consumers or markets. This will enable the FMA to present a picture of the consumer credit environment, including the number of complaints, enforcement responses and prosecutions for breaches.

241. We would also rely on FMA reviews, investigations, cases etc. on an ongoing basis. This information, as well as data on the costs of implementing and enforcing the changes from the FMA, would be exchanged with MBIE.

242. We have ongoing engagement with lender, industry group, consumer and government stakeholders through regular catch-ups, and formal engagement through forums such as MBIE's Consumer Protection Partnership Forum (comprised of consumer advocates and government agencies) and the Responsible Lending Code Advisory Group (comprised of lenders, dispute resolution schemes, and consumer advocates). These forums provide the opportunity for us to monitor the impacts on lenders and consumers and identify any issues with the new arrangements.

Evaluation and Review

243. We intend to review the changes 3-5 years following commencement (subject to resource constraints). This will give enough time for the changes to bed in, whilst also enabling us to quickly understand what has worked, and any unintended consequenses.

244. This review will also be an opportunity to undertake a more fulsome review of consumer credit law to understand if there are further opportunities to align consumer credit regulation with financial markets conduct regulation.

245. Earlier this year, we conducted a baseline consumer survey already to help us understand the current state of the market.[22] Having a stocktake of the consumer credit markets before the changes come into force will enable effective monitoring and evaluation of the law changes when they are reviewed. We will conduct another survey when we come to evaluate the proposals so we can see what has changed over this period.

246. The monitoring identified above is likely to capture any unexpected results or impacts which may arise as a result of the changes. Any issues or concerns that stakeholders have in relation to implementation of the changes can be directed to the relevant enforcement body, the FMA.

247. The FMA has a statutory function to keep under review the law and practices relating to financial markets, financial markets participants. The FMA conducts regular market surveys and thematic reviews on various issues as and when it considers relevant. These mechanisms may be used in respect of the CCCFA if appropriate.

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[22] The report on these survey results is available on the following webpage: Consumer credit research | Ministry of Business, Innovation & Employment (mbie.govt.nz)

Annex 1: Short history of reforms to the CCCFA

When the CCCFA first came into force in 2005 (repealing and amalgamating the Credit Contracts Act 1981 and the Hire Purchase Act 1971), it mostly sought to protect consumers by:

- addressing information asymmetries through disclosure requirements (to promote informed borrowing decisions by consumers)
- providing consistent rules about how interest and fees are calculated and charged (to ensure they are not unreasonable)
- enabling borrowers to seek relief in contract terms in the event of unforeseen hardship
- allowing consumers to seek relief from the Court to prevent oppressive conduct
- making other forms of redress available, including reparation from the Disputes Tribunal
- giving the Commerce Commission responsibility for promoting compliance with the Act.

The first major reforms to the CCCFA were made in 2015, following a review process that began in 2009 and was primarily concerned with unscrupulous 'fringe' lenders (an estimated 35% of whom were unregistered). The main changes were:

- introduction of responsible lending principles (and development of a responsible lending Code), including an obligation to be satisfied by reasonable inquiries that the loan is likely to be both suitable and affordable for the borrower (section 9C(3)(a) of the CCCFA)
- increased disclosure requirements
- new procedural requirements when the borrower makes an application on the grounds of unforeseen hardship
- making lenders liable for the costs of borrowing for any period during which they are unregistered (s99B) or have failed to make the initial disclosures required by section 17 or disclosure of agreed changes required by section 22 (s99(1A))
- incorporation of repossession laws into the CCCFA, with some improvements (based on recommendations from a Law Commission report).

The *Credit Contracts Legislation Amendment Act 2019* and amendment regulations made a series of reforms intended to address risk of harm to vulnerable consumers. This was in response to observations of continued irresponsible lending, unacceptable rates of non-compliance, uncertainty about how to fulfil certain obligations, and poor visibility of lending practices. With the exception of rules for high-cost credit, these reforms were applied to all lending in the interests of consistent standards and competitive neutrality.

The main changes and when they commenced were as follows:

- December 2019 – penalties created for breaching lender responsibility principles, statutory damages increased, new regulation-making powers, ability for court to reduce consequences of failure to make correct disclosures.
- May 2020 – additional restrictions (including a cost of credit cap) for high-cost credit.
- June 2020 – CCCFA obligations applied to mobile trader credit sales.
- June 2021 – introduction of 'fit and proper person' test for directors and senior managers.
- December 2021 – due diligence duty for directors and senior managers, requirement to maintain records showing how certain fees are calculated, requirement to maintain (and share on request) records of inquiries made into affordability, regulations prescribing minimum standards for assessing suitability and affordability of loans as well as advertising standards.

Matthew Weaver

From: Glen Hildreth
Sent: Monday, 2 September 2024 11:24 am
To: s 9(2)(a) @asb.co.nz>
Cc: Andrew Hume; Marcus Smith; Michelle Schulz; Katrina Melville
Subject: CCCFA discussion this afternoon [IN-CONFIDENCE: RELEASE-EXTERNAL]

Hi s 9(2)(a)

I hope that all is well. Ahead of our meeting this afternoon I wanted to send you some information about what we'd like to discuss.

As you're aware, as part of the Government's financial services reforms we have sought feedback on options to amend disclosure requirements, and the associated consequence for failures to disclose (i.e. section 99A), in the CCCFA. We discussed with the NZBA a few months ago the issue of potential consequences for failures that may have occurred during the period for which there is no relief available under section 95(A). I understand you also raised this issue with Andrew Hume.

We are keen to better understand the possible prudential risk. I thought we could use the meeting this afternoon to discuss the questions that we had below in a little more detail, with a view to getting responses from ASB after the meeting (ideally in the next week or so). Please note that we would like to share your responses with RBNZ.

- Has ASB done modelling of their exposure now that the CofA has said borrowers don't have to opt in – are there stability risks / solvency risks / reputational risks to banking sector at play because of that decision? Or is the concern wider than the class action in terms of other potential undiscovered breaches and the flow on implications for those.
- What is the timeline of this litigation? Does ASB have an estimate of how long it is going to go on for?
- What are the chances that this case is going to settle?
- It would be good to have an explanation of the defences ASB is running and an assessment of how strong ASB thinks the defences are. Conversely, where does ASB see weaknesses in its arguments?
- How far would retrospective application of sections 95A and 95B (NZBA's second best retrospective option) go toward reducing solvency/stability/reputational concerns?
- Is ASB seeing any adverse implications right now as a result of the class action – e.g. any significant reputational damage so far or other consequences?
- Have the banks been involved in other court proceedings where the amount claimed is similar or more than what the class action is claiming (or at a similar level as the exposure that their modelling suggests)?

Thanks

Glen Hildreth
MANAGER

Consumer Policy | Building, Resources and Markets
Ministry of Business, Innovation & Employment

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NZBN 9429000106078

From: Glen Hildreth
Sent: Monday, 2 September 2024 3:51 pm
To: 9(2)(a) [redacted]
Cc: Andrew Hume; Michelle Schulz; Marcus Smith; Katrina Melville
Subject: CCCFA discussion tomorrow [IN-CONFIDENCE: RELEASE-EXTERNAL]

Kia ora 9(2)(a) [redacted]

I hope that all is well. Ahead of our meeting tomorrow I wanted to send you some information about what we'd like to discuss.

As you're aware, as part of the Government's financial services reforms we have sought feedback on options to amend disclosure requirements, and the associated consequence for failures to disclose (i.e. section 99A), in the CCCFA. We discussed with the NZBA a few months ago the issue of potential consequences for failures that may have occurred during the period for which there is no relief available under section 95(A).

We are keen to better understand the possible prudential risk. I thought we could use the meeting this afternoon to discuss the questions that we had below in a little more detail, with a view to getting responses from ANZ after the meeting (ideally in the next week or so). Please note that we would like to share your responses with RBNZ.

- Has ANZ done modelling of its exposure now that the CofA has said borrowers don't have to opt in – are there stability risks / solvency risks / reputational risks to banking sector at play because of that decision? Or is the concern wider than the class action in terms of other potential undiscovered breaches and the flow on implications for those.
- What is the timeline of this litigation? Does ANZ have an estimate of how long it is going to go on for?
- What are the chances that this case is going to settle?
- It would be good to have an explanation of the defences ANZ is running and an assessment of how strong ANZ thinks the defences are. Conversely, where does ANZ see weaknesses in its arguments?
- How far would retrospective application of sections 95A and 95B (NZBA's second best retrospective option) go toward reducing solvency/stability/reputational concerns?
- Is ANZ seeing any adverse implications right now as a result of the class action – e.g. any significant reputational damage so far or other consequences?
- Have the banks been involved in other court proceedings where the amount claimed is similar or more than what the class action is claiming (or at a similar level as the exposure that their modelling suggests)?

Thanks

Glen Hildreth
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NZBN 9429000106078

Reserve Bank of New Zealand Te Pūtea Matua

Memorandum for the Ministry of Business, Innovation and Employment

Copied to	Jess Rowe, Director (Prudential Policy), Ken Nicholls, Manager and Avi Yankanna, Adviser (Financial Stability Assessment & Strategy)
From	Mark Holden, Adviser (Prudential Policy)
Date	1 October 2024
Subject	Request for advice: potential financial stability implications of the class actions relating to disclosure failures under the Credit Contracts and Consumer Finance Act 2003.
For your	Information

Purpose

1. You have requested the Reserve Bank's advice on the potential financial stability implications of class action lawsuit's relating to disclosure failures under the Credit Contracts and Consumer Finance Act 2003 (the CCCFA). This memo outlines our advice in response to this request.

Summary

2. Assessing the potential financial stability impacts accurately is difficult as there is uncertainty on how the existing litigation, and any potential future litigation, could play out. We understand that there are different legal arguments being made which could impact the quantum of a result. A decision is also likely a number of years away providing time to consider mitigating actions. It is also unclear whether other banks, non-bank deposit takers and wholesale funded lenders may face claims.

3. We have undertaken high-level modelling based on the known facts (i.e. customers impacted, length of breach, and potential claim size etc) of both class actions and applied this across banks operating in the New Zealand financial system. The modelling does not take into account the probability of success or the likely quantum of damages, as this is legally complex and uncertain.

4. Emphasising this uncertainty, the modelling results indicate possible low to medium impacts on the capital ratios for individual banks and the wider financial system. In the scenarios modelled, most banks were able to maintain their minimum capital requirements (although the prudential capital buffer would be reduced). The impact on profit to recover the cost of litigation for individual banks could range from low to high depending on the scenario - potential impacts were greatest on the domestic banks for which residential lending makes up

a larger proportion of their lending book. Action would be required to return to full capital buffers.

5. We note as well that the modelling is a static assessment., it does not take into account other potential factors which may affect impacted institutions such as future profitability, impacts on the cost of borrowing or the ability to raise further capital to return to full compliance with capital requirements.

6. We do not consider there is an imminent financial stability threat given that we understand that the two class actions will likely take at least two years before a High Court decision is received. We understand that deposit takers should not be required to quantify/provision until a High Court judgement is delivered. Accordingly, at this time, we plan to monitor the situation, gathering more information and formulating a supervisory plan to manage entity exposure.

Analysis

7. We have undertaken modelling based on the two current class actions being undertaken against ANZ and ASB. This analysis tests the potential impacts based on the ANZ and ASB facts, applied to other banks in the New Zealand financial system to estimate the impact of a shorter (1 year – ANZ based) and longer (4 years – ASB based) disclosure failure. The analysis should be treated as indicative of the potential scenarios outlined, it does not take into account the uncertainties discussed later in this memo. The table below provides a summary of the sensitivity analysis undertaken.

Scenario	Description	Estimated impact[1]
Sensitivity 1 – ANZ CCCFA actual settlement of $35m in Mar-2020	This scenario models the compensation of other banks by allocating the estimated payout per loan based on each bank's residential lending. The relative payout will depend on the share of mortgage lending for each bank.	**Insignificant impact** on capital ratios, most banks were able to cover cost of compensation with a month's profit. These are shown below in Figures 1 and 2. **Estimated financial system impact[2]**: $0.1 billion.
Sensitivity 2 - ANZ Plaintiff Case (1 year disclosure failure)	For ANZ this scenario applies a payout of all interest for 1 year to the customers in the plaintiff case. The compensation of other banks has been modelled by allocating the estimated payout per loan based on each bank's residential lending. The relative payout will depend on the share of mortgage lending for each bank.	**Low impact** on capital ratios (refer Figure 1), all banks able to meet the minimum capital requirements. **Banks with a high residential lending concentration** s 9(2)(b)(ii) require **more than a year's profit to recover the cost of litigation** (refer Figure 2). **Estimated financial system impact:** $4.5 billion.
Sensitivity 3 - ASB Plaintiff Case (4 year disclosure failure)	For ASB this scenario applies a payout of all interest for 4 years to the customers in the plaintiff case.	**Low to medium impact** on capital ratios (refer Figure 1), few banks were unable to meet the minimum capital requirements.

[1] Impact severity is assesed based on the year's of profit it takes a bank to recover the cost of litigation.
[2] All figures for estimated financial system compensation are based on the aggregate impacts for the 13 largest banks.

Scenario	Description	Estimated impact[1]
	The compensation of other banks has been modelled by applying the share of the value at risk to the mortgage book of individual banks to find the compensation cost and impact to all the other banks over the 4 years. s 9(2)(b)(ii)	s 9(2)(b)(ii) and Banks having a high residential lending concentration s 9(2)(b)(ii) require more than two year's profit to recover the cost of litigation (refer Figure 2). Estimated financial system impact: $12.9 billion.

8. Figures 1 and 2 below outline the results for individual banks and the overall financial system. The s 9(2)(b)(ii) have the most significant impacts on their years of profit to recover the cost of litigation. This reflects the heavily weight of residential lending in their business compared to other banks.

s 9(2)(b)(ii)

s 9(2)(b)(ii)

s 9(2)(b)(ii)

[redacted]

Uncertainties

9. The results of the modelling outline the potential individual and system impacts of similar disclosure failures to the ANZ and ASB class actions being successfully pursued against other banks. Each scenario outlines a potential upper bound of the given scenario. However, the likelihood of each scenario playing out to the full extent is highly uncertain. The scenarios do not take into account the:

    9.1. **Timeframes over which the litigation will progress, financial disclosure and the ability of banks to prepare for an adverse outcome:** it is uncertain when a decision will be reached, but we understand even in an optimistic scenario a High Court decision is likely two years away. This makes it difficult to assess when any potential financial impact could occur for impacted banks. We understand that the banks should not be required to disclose or provision until there is a substantive High Court judgment.

    This suggests that there could still be a number of years before there is a direct financial impact. The potential lead time before any adverse findings means that there is time for impacted entities to plan how they would respond.

    9.2. **Probability of success of the banks in defending the class actions occurring and the possibility of a settlement:** the existing class actions are still in early procedural phases of the litigation. We understand that there are a number of legal questions of interpretation to be resolved which means that it is uncertain what the likelihood of a worst case adverse judgment is. This makes it difficult to assess what a 'likely' financial impact could be. The estimates in the sensitivity analysis do not take into account decisions in the litigation which could reduce the quantum of an adverse judgment. Even a successful decision for the plaintiffs could result in an outcome less than the full amount estimated in the sensitivity analysis.

9.3. Likelihood of other banks facing similar litigation: the possibility of other banks facing similar litigation is uncertain. While the Commerce Commission has undertaken a number of settlements with other banks for disclosure failures, we understand that there are no other private claims that have been made. For a number of settlements that have been made we understand that the period of time since they were made suggests that the likelihood of further private litigation relating to those disclosure failures that have already been settled could be reducing.

We understand that the Commerce Commission has open investigations on disclosure failures over the 2015-2019 period. This, combined with the unknown potential for further disclosure failures to arise from this period, means that further private litigation cannot be ruled out.

10. In addition to the sensitivities we have outlined, we considered the impact of more extreme variations on these sensitivities. In these scenarios, the potential impact on the financial system would be much more severe. However, we have not included these results as, while instructive on potential impact, the scenarios are speculative compared to the scenarios we have outlined which are anchored in two real world scenarios.

Conclusion

11. The impacts of the sensitivity analysis range from insignificant on all the bank's capital ratios to a low to medium impact of some banks. The impact on profit to recover the cost of litigation for individual banks could range from low to high depending on the scenario - potential impacts were greatest on the domestic banks for which residential lending makes up a larger proportion of their lending book.

12. These results do not immediately suggest a systemic effect. However, the outcomes of the current litigation, and the potential for further litigation are highly uncertain. This uncertainty makes it difficult to assess what the likely impact is on the individual banks current impacted or the potential for impact more widely within the financial system.

13. We suggest that further monitoring and engagement with impacted banks is required as the litigation progresses. We plan to proactively engage with our regulated entities to monitor and assess potential risks for individual institutions and the financial system as the uncertainties reduce.

Annex: Model variables and general assumptions

The model design was developed with limited information regarding the two cases, along with several unknowns & limitations to estimate the compensation required from the individual banks and the implications on their profit and capital levels. The table below provides a list of variables and limitations taken into consideration in developing the model:

Variables	Known	Unknowns/limitations	Assumptions
Banks	ANZ and ASB are Plaintif cases only	Other banks which may be implicated	Applied sensitivity to all banks
Customers affected	ANZ – 101535 ASB – 73120	Customers of other banks which may be affected	Estimated the number of affected customers of other banks based on the estimated value at risk.
Coverage period	ANZ - 6 June 2015-May 2016 ASB - 6 June 2015 - 18 June 2019	Can the period of coverage for ANZ/ASB extend till 2024? Can coverage period for ANZ extend to 2019 or 2024? Coverage period for other banks?	Sensitivities assumed coverage period to be 1 year, 4 years and also extended till 2024 for all banks.
Exposure at risk	Loan variation exposures at risk. Consumer credit exposures only	Actual exposure at risk New loans/customers at risk.	Assumed residential mortgage exposure[4] at risk. Also, factored in new residential mortgage lending in one of the sensitivities.
Compensation amount	Maximum liability to banks will be the interest and fees chared plus any legal costs.	Actual compensation cost. Legal component of compensation. Actual interest & fees	Compensation value is assumed to be the estimated interest and fees chared during the relavant periods to the affected customers.
Compensation period		Obligation to compensate within a certain timeframe.	Loss is compensated based on the assumption that latest fye profit is earned by banks in the following years to compensate loss.

s 9(2)(b)(ii)

MINISTRY OF BUSINESS, INNOVATION & EMPLOYMENT
HĪKINA WHAKATUTUKI

BRIEFING

Financial Services Reforms: Proposal to make 2019 reforms to section 99(1A) of the CCCFA retrospective

Date:	10 October 2024	**Priority:**	High
Security classification:	Sensitive	**Tracking number:**	BRIEFING-REQ-0004273

Action sought		
	Action sought	**Deadline**
Hon Andrew Bayly **Minister of Commerce and Consumer Affairs**	**Agree** to seek Cabinet approval to amend the CCCFA with retrospective effect to ensure the courts have discretion to consider the nature and circumstances of each disclosure failure, regardless of when it occurred. **Refer** a copy of this briefing to the Minister of Finance.	14 October 2024

Contact for telephone discussion (if required)			
Name	**Position**	**Telephone**	**1st contact**
Glen Hildreth	Manager, Consumer Policy	04 901 0687	✓
Marcus Smith	Senior Policy Advisor, Consumer Policy	09 928 2747	

The following departments/agencies have been consulted
The Reserve Bank of New Zealand, Treasury, Commerce Commission, Financial Markets Authority and Ministry for Regulation.

Minister's office to complete:

- ☐ Approved
- ☐ Noted
- ☐ Seen
- ☐ See Minister's Notes
- ☐ Declined
- ☐ Needs change
- ☐ Overtaken by Events
- ☐ Withdrawn

BRIEFING

Financial Services Reforms: Proposal to make 2019 reforms to section 99(1A) of the CCCFA retrospective

Date:	10 October 2024	**Priority:**	High
Security classification:	Sensitive	**Tracking number:**	BRIEFING-REQ-0004273

Purpose

To seek your agreement to amend the Credit Contracts and Consumer Finance Act (CCCFA) with retrospective effect to ensure the courts have discretion to consider the appropriate effect of section 99(1A), regardless of when the failure occurred.

Executive summary

- In September, you indicated to Cabinet you would be receiving further advice on risks posed by how section 99(1A) operates in relation to certain disclosure failures by lenders that pre-dated reforms in December 2019.

- Section 99(1A) provides that the borrower is not liable to pay interest or fees over any period of non-compliant disclosure made before loans are entered into or varied. In 2019, the CCCFA was amended to give the courts explicit discretion to extinguish or reduce the effect of this provision in order to reach a just and equitable outcome.

- The 2019 reforms were not applied retrospectively, meaning the courts may still be bound to require lenders to forfeit the full costs of borrowing to all affected borrowers. This question is being considered in class litigation against ANZ and ASB.

- If the plaintiffs in that litigation are successful, the financial consequences could spill over to an unknown number of other lenders who had compliance issues over this period.

- RBNZ has undertaken modelling of scenarios that did not find any imminent stability risks, but indicates possible impacts that leave us concerned about the health of the market for supply of consumer credit, including potential competition impacts (disproportionately affecting locally-owned lenders who rely more heavily on income from consumer lending) and a reduction in access to credit.

- To address this, we recommend you seek Cabinet approval for amendments to the CCCFA with retrospective effect. Our view is that the courts should have the explicit discretion that was provided by the 2019 reforms to arrive at a just and equitable outcome, regardless of when the disclosure failure took place. The further reforms Cabinet agreed on 2 September would continue to apply only prospectively.

- Although it is uncertain how exactly this proposal would change the way the courts apply section 99(1A) to disclosure failures predating December 2019, increasing their discretion is more conducive to avoiding the concerns we have.

- If you agree with the proposal, we recommend you seek Cabinet approval for it as soon as possible so that it can be reflected in the introduction version of the CCCF Amendment Bill, which is currently being drafted.

Recommended action

The Ministry of Business, Innovation and Employment recommends that you:

a **Note** the CCCFA did not give the courts explicit discretion to consider whether the effect of section 99(1A) is just and equitable (on an application by the lender) until December 2019.

Noted

b **Agree** to seek Cabinet approval to amend the CCCFA with retrospective effect so that this discretion is available to the courts regardless of when the disclosure failure giving rise to liability under section 99(1A) occurred.

Agree/ Disagree

c **Agree** to forward a copy of this briefing to the Minister of Finance.

Agree/ Disagree

Glen Hildreth	Hon Andrew Bayly
Manager, Consumer Policy	**Minister of Commerce and Consumer Affairs**
10 October 2024	..... / ...... / ......

Background

1. On 2 September 2024, you indicated to Cabinet that you would be taking further advice on concerns about how section 99(1A) may be applied by the courts to disclosure failures pre-dating reforms in December 2019. In the meantime, you obtained Cabinet approval for a further change limiting the effect of section 99(1A) prospectively [*CAB-MIN-0334* refers].

2. We have further investigated the potential implications of section 99(1A) in view of a class action against ANZ and ASB, including by seeking advice from the Reserve Bank of New Zealand (**RBNZ**).

3. This briefing sets out MBIE's advice and recommends legislative change with retrospective effect to ensure the courts have discretion to arrive at a just and equitable outcome, having regard to the nature and circumstances of each disclosure failure, regardless of when the failure occurred. This decision would require Cabinet approval.

The issue with section 99(1A) of the CCCFA

Section 99(1A), introduced in 2015, provides that borrower is not liable for the costs of borrowing over a period of non-compliant disclosure

4. Section 99 prohibits lenders from enforcing consumer credit contracts before they have made 'initial' disclosure[1] or 'agreed variation' disclosure.[2]

5. Section 99(1A) was added in June 2015. It provides that the borrower is not liable for the costs of borrowing (i.e. interest and any fees) over any period in which the lender has failed to make initial or agreed variation disclosure (until they make corrective disclosure). Equivalent provisions were added for disclosure failures in relation to consumer leases and buy-back transactions.

6. The Act did not expressly provide the courts with any discretion to avoid the lender having to forfeit the full costs of borrowing where that amount would be disproportionate to the nature and circumstances of their failure [3] It did not clearly account for the fact that some disclosure failures affect the borrower's ability to make informed decisions less than others.

7. Where a relatively immaterial failure affected a large number of borrowers, and was not noticed (and therefore able to be corrected) until many years later, the full costs of borrowing could amount to a significant sum that is disproportionate in the circumstances.

Reforms in 2019 provided the courts with an explicit discretion to consider the nature and circumstances of a disclosure failure

8. In 2019, reforms designed to address this took effect. Section 95A makes relief available to lenders by expressly enabling a court (on an application by the lender) to "extinguish or reduce the effect of section 99(1A)" if that is considered "just and equitable". In doing so, the court must consider factors in section 95B. These factors relate to the objective of incentivising compliance with the CCCFA, how the breach occurred, the harm it caused and what the lender did in response, as well as "any other matters the court thinks fit".

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[1] This is 'key information' about the lender and the agreement being entered into, such as the interest and fees payable, and the details of the lender's dispute resolution scheme.
[2] This is disclosure of the details of the change to the agreement the parties have agreed and its effect on other terms of the agreement (such as the total interest that will be charged, if that changes).
[3] The implications of this provision, at least as applied in particular situations, is subject to legal testing in litigation.

This explicit discretion does however not apply to disclosure failures that occurred between June 2015 and December 2019

9. The decision at the time was to make this relief available only to disclosure failures that occur after the commencement of the change (i.e. from December 2019 onwards), and not retrospectively to disclosure failure that occurred between June 2015 and December 2019. There was no clear policy reason that the discretion should not have been available for earlier disclosure failures.

10. This could mean the courts consider they are bound to require full forfeiture, with no discretion to reach a just and equitable outcome.

Litigation will determine how the courts apply section 99(1A) without explicit discretion over that period

11. Lenders have raised with you and with officials that they have ongoing concern about the potential consequences of how section 99(1A) may be applied by a court to disclosure failures over this period. These potential consequences are at issue in class litigation against ANZ and ASB. We have further considered this litigation and sought advice from RBNZ about the potential impacts.

12. Our understanding of the facts relevant to the class litigation is summarised in **Annex One**. The plaintiffs in the case are arguing the banks failed to make compliant agreed variation disclosure and must therefore refund the full costs of borrowing (which is a sum significantly greater than that they paid to affected borrowers in their settlements with the Commerce Commission).

13. We cannot comment on the probability of the court finding in favour of the plaintiffs. However, if that outcome eventuates, the impacts on lenders could be on such a significant scale that it ultimately undermines the interests of consumers, as explained below.

A range of other lenders could be affected if the plaintiffs are successful

14. A decision favourable to the plaintiffs could extend to other lenders who had issues complying with these disclosure requirements over the relevant period.

15. The Commission has provided a sense of the number of lenders this could include. As of 12 August 2024, the Commission had resolved compliance issues with disclosures from this period with 15 active lenders, s 9(2)(f)(iv) [redacted] However, it is possible other lenders have either not identified disclosure failures from this period or have chosen not to take any remedial steps that would draw attention to them.

16. The impact on other lenders is likely to be limited by statutory deadlines, including a limitation period in the CCCFA of “three years after the date on which the loss or damage was discovered or ought reasonably to have been discovered”. However, there is uncertainty both about how and whether this would apply to disclosure failures triggering section 99(1A) (as opposed to six years under the Limitation Act 2010).

They could be affected in ways that damage the market and consumers

17. The financial impact on lenders may result in costs being passed onto consumers or in a reduction of lending activity that affects access to credit. This may negatively impact competition. These impacts could be more significant for smaller lenders – some of whom are co-operative companies and would need to consider raising capital from its customers (who are its shareholders).

18. The RBNZ modelling (summarised in **Annex Two**) did not find any imminent financial stability risks. However, it indicates (subject to a range of constraints and uncertainties):

    a. possible low to medium impacts on the capital ratios for individual banks and the wider financial system

    b. that not all banks are able to maintain their minimum capital requirements in every scenario modelled (although prudential capital buffers would be reduced)

    c. the impact on profit to recover the cost of litigation for individual banks could range from low to high depending on the scenario, with the greatest potential impact on the domestic banks for which residential lending makes up a larger proportion of their lending book.

19. Banks are also concerned about the impact this could have on depositor confidence. Where banks are aware of relevant disclosure failures, they may be required to disclose in their financial statements that they have contingent liability to refund costs of borrowing. The relevant international auditing standard requires disclosures for contingent liability and disclosure in respect of "a present obligation that probably requires an outflow of resources" (assuming the liability can be measured reliably).[4]

Recommended amendment to the CCCFA

We recommend you seek Cabinet approval to amend the CCCFA with retrospective effect to provide courts with explicit discretion regardless of when the failure occurred

20. In light of the potential consequences above, our view is that the courts should have explicit discretion to arrive at a just and equitable outcome (by extinguishing or reducing the effect of section 99(1A)) regardless of when the disclosure failure took place. This would require legislative change with retrospective effect. The further change Cabinet agreed on 2 September would continue to apply prospectively.

21. The Financial Markets Authority supports this proposal. The Commerce Commission has not expressed a view on the policy, but raised concerns about potential implications for its past and active enforcement activities relating to disclosure failures from the relevant period. Our assessment at this stage is that these could be managed (as discussed below).

[4] IAS 37: Provisions, Contingent Liabilities and Contingent Assets: xrb.govt.nz/dmsdocument/2413/

22. There is no guarantee this intervention would change how the courts decide litigation concerning relevant disclosure failures pre-dating December 2019, with certain implementation risks discussed below. However, it would ensure the courts are explicitly empowered to exercise discretion about the effect of section 99(1A) as they see fit, having regard to the factors in section 95B.

s 9(2)(h)

[redacted]

[5] Legislation Design and Advisory Committee Guidelines: 2021 edition.

[6] Refer to *Mangawhai Ratepayers and Residents Association Inc v Kaipara District Council* [2015] NZCA 612 at [132] to [134]

s 9(2)(h)

[redacted]

Proposed timing

33. Should you agree with our recommendation, the CCCF Amendment Bill implementing financial services reforms provides a suitable legislative vehicle.

34. We recommend getting this policy agreed by Cabinet and drafted for inclusion in the Bill before introduction. Inclusion of this change in the Bill as introduced would maximise transparency to lenders and the public about the proposal, which we consider particularly important given we had not publicly consulted on this option. It would also immediately alleviate distress in the market caused by the prospect of a disproportionate outcome in the class litigation

35. We would need to act quickly to achieve this. There are limited remaining opportunities to obtain Cabinet agreement in time for further amendments to be drafted for introduction of a CCCF Amendment Bill (on the current timeline indicated by the Leader of the House).

36. We have provided you with a draft Cabinet paper on the wider financial services reforms [*Briefing REQ-0002999* refers]. That paper could be amended to make room for this proposal, but we may need to revisit the target Cabinet Economic Development Committee meeting date (currently 6 November). However, as the Bill will not be introduced until early 2025 a delay of two weeks or so to the Cabinet Committee date should be immaterial.

Next steps

37. We recommend you forward a copy of this briefing to the Minister of Finance, given the potential impact on deposit-takers and the financial system (as modelled by RBNZ). We are available to discuss if we can assist you and/or the Minister of Finance to reach a decision.

38. If you agree to pursue retrospective legislation in time for it to be included before introduction of a CCCF Amendment Bill, we would need to consider possible Cabinet Committee dates. Cabinet's regulatory impact analysis requirements would apply to our preferred option. In the interests of time, we are preparing a regulatory impact statement in anticipation of your agreement.

39. We would also work with your office to carefully consider the timing of an announcement, given this policy would have an immediate impact on certain decisions and activities.

Annexes:

Annex One: The class action against ANZ and ASB

Annex Two: Summary of RBNZ modelling and advice

Annex One: The class action against ANZ and ASB

What we know about the case

1. The case against ANZ and ASB is procedurally complex, as well as involving complexities in terms of how the law operated between June 2015 and December 2019. It is being funded by litigation funders.

ANZ's agreed variation disclosure issue

2. In May 2016, ANZ identified and fixed a coding error that had caused interest payments to be miscalculated when disclosing the details of loan variations to customers (as required by section 22). This had been affecting disclosures for variations of ANZ's home and personal loans since May 2015. Although it affected several details contained in disclosure statements, the miscalculation of payment amounts was very minor. About 102,000 customers were identified as affected.

3. In June 2017, ANZ notified the Commission of this issue. By April 2019, it had notified affected customers and paid remediation totalling approximately $8.3million.

4. In March 2020, ANZ settled with the Commission on terms including:

    a. an admission it had breached one of the lender responsibility principles in the CCCFA (section 9C(2)(a)(iii)) by failing to take sufficient steps to ensure the relevant disclosures were correct

    b. no admission of wider liability

    c. total remediation for affected customers of $35million (including that already paid).

5. s 9(2)(ba)(i)

6. The settlement with the Commission did not extinguish the right of affected customers to take further legal action.

7. The plaintiffs now argue:

    a. ANZ's error constitutes a breach of section 22

    b. section 99(1A) meant the borrowers were not liable for any costs of borrowing for the period of defective disclosure (approximately 12 months)

    c. section 48 required the costs of borrowing to be refunded to affected borrowers.

ASB's agreed variation disclosure issue

8. In June 2019, ASB addressed deficiencies that had been present in its procedures since June 2015 for providing variation disclosure. These deficiencies had meant that ASB had not consistently provided variation disclosure to its customers (until it addressed this around four years later).

9. This affected around 73,000 borrowers. However, the plaintiffs are arguing the class is much wider. On 19 July 2024, ASB announced on the NZX (and its parent company on the ASX) that "the class and the allegations made in the proceedings would potentially cover hundreds of thousands of loans."[7]

10. ASB reported this issue to the Commission in September 2019, accepting that some of its customers were not given variation disclosure. ASB settled with the Commission in 2021, agreeing to pay a total of just over $8million to affected customers. As with ANZ, ASB only admitted a breach of the lender responsibility principle, in that it failed to have systems and processes that were sufficient to ensure variation disclosure.

11. The arguments against ASB in the class action are essentially the same as those against ANZ.

Timeline for the litigation

12. There remain some procedural matters to be resolved relating to the fact that the litigation is being funded by litigation funders. The two banks have recently applied to the Supreme Court for leave to appeal the Court of Appeal's decision to make Class Funding Orders. It may be some time before the substantive issues in dispute are considered by the High Court. From our discussions with ANZ and ASB, we understand that this litigation could potentially take up to five years to be finally resolved.

s 9(2)(g)(i)

[redacted]

14. Whatever the High Court's judgment, there is the prospect that it is appealed all the way to the Supreme Court. This means, in all likelihood, that certainty about the consequences of the pre-2019 law is several years away.

What we do not know about the case

15. The outcome of the litigation depends on a range of arguments about how the CCCFA applies and how the court will ultimately interpret the relevant CCCFA provisions, including on:

   a. what is required to make variation disclosure

   b. whether section 99(1A) applies to incorrect (as well as incomplete) disclosures

   c. whether there is a de minimis exception to disclosure breaches

   d. whether section 99(1A) only applies in circumstances where a loan is in distress, meaning it only applies to prevent a lender going to court to seek to enforce the costs of borrowing during a period where disclosure breaches are occurring (i.e. it does not

[7] https://www.nzx.com/announcements/434795

give rise to an obligation to refund the costs of borrowing where they have been paid by a debtor);

e. when claims being made by the plaintiffs are out of time based on limitation periods in the CCCFA;

f. whether the court already had discretion (prior to section 95A) not to make an order requiring payment of the full costs of borrowing to affected borrowers.

16. We have not had enough exposure to the case to properly consider the merits of these arguments and what their success would mean for the outcome.

Annex Two: Summary of RBNZ modelling and advice

1. Assessing the potential financial stability impacts accurately is difficult as there is uncertainty on how the existing litigation, and any potential future litigation, could play out. We (RBNZ) understand that there are different legal arguments being made which could impact the quantum of a result. A decision is also likely a number of years away providing time to consider mitigating actions. It is also unclear whether other banks, non-bank deposit takers and wholesale funded lenders may face claims.

2. We have undertaken high-level modelling based on the known facts (i.e. customers impacted, length of breach, and potential claim size etc) of both class actions and applied this across banks operating in the New Zealand financial system. The modelling does not take into account the probability of success or the likely quantum of damages, as this is legally complex and uncertain.

3. Emphasising this uncertainty, the modelling results indicate possible low to medium impacts on the capital ratios for individual banks and the wider financial system. In the scenarios modelled, most banks were able to maintain their minimum capital requirements (although the prudential capital buffer would be reduced). The impact on profit to recover the cost of litigation for individual banks could range from low to high depending on the scenario - potential impacts were greatest on the domestic banks for which residential lending makes up a larger proportion of their lending book. Action would be required to return to full capital buffers.

4. We note as well that the modelling is a static assessment , it does not take into account other potential factors which may affect impacted institutions such as future profitability, impacts on the cost of borrowing or the ability to raise further capital to return to full compliance with capital requirements.

5. We do not consider there is an imminent financial stability threat given that we understand that the two class actions will likely take at least two years before a High Court decision is received. We understand that deposit takers should not be required to quantify/provision until a High Court judgement is delivered. Accordingly, at this time, we plan to monitor the situation, gathering more information and formulating a supervisory plan to manage entity exposure.

Analysis

6. The table below summarises the modelling undertaken. The analysis tests the potential impacts based on the s 9(2)(b)(ii) facts, applied to other banks in the New Zealand financial system to estimate the impact of a shorter s 9(2)(b)(ii) and longer s 9(2)(b)(ii) s 9(2)(b)(ii) disclosure failure. The analysis should be treated as indicative of the potential scenarios outlined, it does not take into account the uncertainties discussed later.

Scenario	Description	Estimated impact[8]
Sensitivity 1 – s 9 **CCCFA** s 9(2)(b)(ii)	This scenario models the compensation of other banks by allocating the estimated payout per loan based on each bank's residential lending. The relative payout will	**Insignificant impact** on capital ratios, most banks were able to cover cost of settlement with a month's profit.

[8] Impact severity is assesed based on the year's of profit it takes a bank to recover the cost of litigation.

Scenario	Description	Estimated impact[8]
	depend on the share of mortgage lending for each bank.	**Estimated financial system impact[9]:** $0.1 billion.
Sensitivity 2 - s 9(2)(b)(ii)	s 9(2)(this scenario applies a payout of all interest for s 9(2)(b)(ii) The compensation of other banks has been modelled by allocating the estimated payout per loan based on each bank's residential lending. The relative payout will depend on the share of mortgage lending for each bank.	**Low impact** on capital ratios, all banks able to meet the minimum capital requirements. **Banks with a high residential lending concentration** would require **more than a year's profit to recover the cost of litigation.** **Estimated financial system impact:** $4.5 billion.
Sensitivity 3 - s 9(2)(b)(ii)	s 9(2)(this scenario applies a payout of all interest for s 9(2)(b)(ii) The compensation of other banks has been modelled by applying the share of the value at risk to the mortgage book of individual banks to find the compensation cost and impact to all the other banks over s 9(2)(b)(ii) s 9(2)(b)(ii)	**Low to medium impact** on capital ratios, few banks were unable to meet the minimum capital requirements. s 9(2)(b) **banks having a high residential lending concentration** would **require more than two year's profit to recover the cost of litigation.** **Estimated financial system impact:** $12.9 billion.

Uncertainties

7. The results of the modelling outline the potential individual and system impacts of similar disclosure failures to the s 9(2)(b)(ii) class actions being successfully pursued against other banks. Each scenario outlines a potential upper bound of the given scenario. However, the likelihood of each scenario playing out to the full extent is highly uncertain. The scenarios do not take into account the:

    a. *Timeframes over which the litigation will progress, financial disclosure and the ability of banks to prepare for an adverse outcome:* it is uncertain when a decision will be reached, but we understand even in an optimistic scenario a High Court decision is likely two years away. This makes it difficult to assess when any potential financial impact could occur for impacted banks. We understand that the banks should not be required to disclose or provision until there is a substantive High Court judgment.

       This suggests that there could still be a number of years before there is a direct financial impact. The potential lead time before any adverse findings means that there is time for impacted entities to plan how they would respond.

    b. *Probability of success of the banks in defending the class actions occurring and the possibility of a settlement:* the existing class actions are still in early procedural phases of the litigation. We understand that there are a number of legal questions of interpretation to be resolved which means that it is uncertain what the likelihood of a worst case adverse judgment is. This makes it difficult to assess what a 'likely' financial impact could be. The estimates in the sensitivity analysis do not take into account decisions in the litigation which could reduce the quantum of an adverse judgment.

[9] All figures for estimated financial system compensation are based on the aggregate impacts for the 13 largest banks.

Even a successful decision for the plaintiffs could result in an outcome less than the full amount estimated in the sensitivity analysis.

c. *Likelihood of other banks facing similar litigation:* the possibility of other banks facing similar litigation is uncertain. While the Commerce Commission has undertaken a number of settlements with other banks for disclosure failures, we understand that there are no other private claims that have been made. For a number of settlements that have been made we understand that the period of time since they were made suggests that the likelihood of further private litigation relating to those disclosure failures that have already been settled could be reducing.

   We understand that the Commerce Commission has open investigations on disclosure failures over the 2015-2019 period. This, combined with the unknown potential for further disclosure failures to arise from this period, means that further private litigation cannot be ruled out.

8. In addition to the sensitivities we have outlined, we considered the impact of more extreme variations on these sensitivities. In these scenarios, the potential impact on the financial system would be much more severe. However, we have not included these results as, while instructive on potential impact, the scenarios are speculative compared to the scenarios we have outlined which are anchored in two real world scenarios.

Proposal for retrospective legislative change to give courts discretion over consequences for breaches of disclosure obligations under the Credit Contracts and Consumer Finance Act

- In September, Cabinet made policy decisions on financial services reforms, including changes to consumer credit legislation (the CCCFA).

I intend to propose an amendment to the CCCFA with retrospective effect

- Section 99(1A), introduced in 2015, provides that the borrower is not liable to pay interest or fees over any period of non-compliant disclosure made before loans are entered into or varied. This may mean courts are **bound** to require lenders to **forfeit the full costs of borrowing to all affected borrowers**, no matter how little the disclosure breach affected borrowers' ability to make informed decisions.
- In 2019, the CCCFA was amended to address this by giving the courts **explicit discretion to remove or reduce these consequences**, but this was **not applied retrospectively.**
- Liability for breaches over **the 2015-2019 period** is being **actively considered** in class litigation against ANZ and ASB. Both cases are funded by LPF Group (an Australian litigation funder) and are in the preliminary stages.
- This is a legacy issue I am seeking to address by **backdating the 2019 reforms**. This would ensure the courts are able to remove or reduce the effect of section 99(1A) if they consider it just and equitable to do so. I plan to seek Cabinet approval for an amendment with retrospective effect in the new year.
- I propose this **discretion be available** in any case involving section 99(1A), including **the current litigation** against ANZ and ASB.

There may be impacts on the market if we do nothing

- Though the prospect of successful litigation against ANZ and ASB doesn't appear to pose a stability threat, the **financial consequences could be significant**.
- These consequences **could affect other lenders** who had compliance issues between 2015 and 2019. It is unclear how many other lenders this might affect and how adversely, but some would be **poorly placed to manage losses** on this scale.
- MBIE is concerned about the potential implications on the market for supply of consumer credit, including **the role played by smaller, locally-owned lenders** who rely more on income from this lending.

Retrospective legislation is unusual, but is considered appropriate here

- I acknowledge the **general rule** that legislation should not apply retrospectively, and not interfere with the judicial process in cases before the courts.
- However, my proposal **would not directly change any legal rights or duties**. Affected borrowers would still be able to seek the remedy provided by section 99(1A) of full costs of borrowing.
- I am only proposing to provide the court with **greater flexibility** in how it decides these cases, by giving it **clear discretion** to consider whether a different outcome is 'just and equitable' in the circumstances.
- This means there is no guarantee the amendment would change how the courts apply section 99(1A), including in current litigation. They would simply be **better empowered to avoid disproportionate outcomes.**
- In practical terms, the proposal is more likely to **favour lenders** than affected borrowers by reducing the likelihood of full forfeiture of the costs of borrowing. However, this is **necessary to address concerns** about the potential impact on the market (and therefore consumers more generally) of a finding that full forfeiture is required.

Chris Cuthbertson

From: Marcus Smith
Sent: Thursday, 21 November 2024 2:46 pm
To: Kathleen Henning; Michelle Schulz; Sam McLoughlin
Cc: Glen Hildreth; Sally Whineray Groom; Will Cosgriff (Parliament); Katrina Melville
Subject: RE: When proposal for retrospective change to s99(1A) could go to Cabinet
Attachments: 2024-11-19 Revised 1 pager for Minister on retrospectivity.docx

Kia ora Kathleen,

To minimise delays in consultation, we thought it best to provide you with a one-pager (attached) that assumes the Minister is comfortable with applying the proposed retrospective change to the active litigation against ANZ and ASB. Below is a summary of our reasons for recommending that approach. If all goes to plan, we will provide more formal advice on this next year, when the Minister is seeking ECO agreement to the policy (at the same time as seeking approval to introduce the Bill).

We can also amend the one-pager if the Minister would prefer to let the active litigation run its course (and use the amendment only to limit liability of lenders who are yet to face litigation). We can also provide a briefing if he wants more formal advice before he decides, but there isn't much to add to what's outlined below.

We'll next get to work on the Minister's letter for the Attorney General, to be delivered after consultation. The Minister's meeting with Hon Collins on Monday would be a good chance to make her aware of this proposal and explain why he is seeking to have it drafted in advance of Cabinet approval. I'm adding some talking points to the SBM event briefing.

Let us know if there's anything more you need for now, or suggest a different approach – this is another case of me calling you while you're busy and then emailing instead/as well.

Ngā mihi
Marcus

Short note for the Minister on why MBIE suggests the retrospective change should apply to active litigation against ANZ and ASB, and next steps

<u>Background</u>

- You agreed on 19 November to an amendment with retrospective effect that would give the courts express discretion to modify the effect of section 99(1A), regardless of when the disclosure failure occurred. We understand the Minister of Finance supports this proposal.
- A second-order question is whether this amendment should apply to the active court proceedings against ANZ and ASB. Our briefing noted some trade-offs relevant to this choice (briefing REQ-0004273 refers).

<u>Why MBIE suggests including current litigation against ANZ and ASB</u> s 9(2)(h)

- When we discussed this advice with you, we indicated our preference was to include active litigation. Although this approach is not clearly necessary to address concerns about the financial position of either ANZ or ASB, we have two main reasons for preferring it:
  - It would avoid inconsistency between how the courts are able to decide the active class action and any other cases relating to disclosure failures prior to December 2019. This seems relevant to your reform objective of simplifying regulation of financial services – not only would it be irrelevant when the disclosure failure happened, but also when proceedings commenced.
  - It would give the court greater flexibility to avoid a potentially grossly disproportionate result. We consider intervention now is appropriate given the early stage of that litigation. However, we note providing greater discretion to the court does not necessarily mean it will reach a different outcome.

- However, we acknowledge that applying this amendment to the active class action has “upside” potential for the banks only. This may have a practical impact on the litigation (including increased likelihood of settling), and result in criticism of having changed the “rules of the game” to their detriment.
- However, any impact on the plaintiffs’ position is ultimately subject to the court’s discretion. That discretion can only be used to achieve ‘justice’ and ‘equity’. We ultimately consider it legitimate to empower the court to consider what outcome is appropriate in active proceedings against ANZ and ASB.

Proposed process from here

- Given the controversial nature of this amendment, and the fact it relates to a “live issue”, we consider it is important to include it in the CCCFA Amendment Bill when it is introduced in the New Year. This would ensure transparency about the Government position and that the select committee is able to consider a range of views on it.
- The proper process would be for you to obtain policy approval from Cabinet (through the Economic Policy Committee (**ECO**)) before the amendment is drafted and included in the Bill. However, this would likely delay introduction of the Bill by a month or more.
- Given your desire to introduce the Bill as soon as possible in 2025, we suggest the amendment is drafted in anticipation of Cabinet approval. You would instead seek policy approval at the same time as you seek approval for the Bill to be introduced to Parliament. This would mean having ECO acting for Cabinet Legislation Committee when the Bill is ready for introduction.
- This approach can be used in exceptional cases with the Attorney-General’s written consent (as a prerequisite for instructing the Parliamentary Counsel Office). We would prepare a letter from you for this purpose. We are also providing talking points on this for your meeting with Hon Judith Collins on Monday 24 November.
- Although it may take some time to obtain a formal reply, this is likely to cause less delay than going to ECO on this specific proposal before having it including in the Bill for introduction.
- The Attorney-General is unlikely to provide consent without your assurance that senior Ministers and coalition partners support the proposal. We therefore recommend you begin socialising the proposal as soon as possible.
- We wish to emphasise that this proposal is commercially and **market sensitive***, and you would therefore be consulting on it in strict confidence. Please note this in your correspondence with others.

* The relevant Cabinet Circular is here: Cabinet Office Circular CO (23) 5: Guidelines for Dealing in Financial Products on Markets (Inside Information and Market Manipulation) - 12 July 2023 - Cabinet Office

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From: Kathleen Henning <Kathleen.Henning@parliament.govt.nz>
Sent: Thursday, November 21, 2024 9:16 AM
To: Michelle Schulz <Michelle.Schulz@mbie.govt.nz>; Marcus Smith <Marcus.Smith2@mbie.govt.nz>; Sam McLoughlin <sam.mcloughlin@parliament.govt.nz>
Cc: Glen Hildreth <Glen.Hildreth@mbie.govt.nz>; Sally Whineray Groom <Sally.Whineray@mbie.govt.nz>; Will Cosgriff (Parliament) <Will.Cosgriff@parliament.govt.nz>; Katrina Melville <Katrina.Melville@mbie.govt.nz>
Subject: RE: When proposal for retrospective change to s99(1A) could go to Cabinet

Thanks Michelle, that sounds like a good plan to me. Sam, let’s discuss

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From: Michelle Schulz <Michelle.Schulz@mbie.govt.nz>
Sent: Wednesday, 20 November 2024 6:56 PM
To: Marcus Smith <Marcus.Smith2@mbie.govt.nz>; Kathleen Henning <Kathleen.Henning@parliament.govt.nz>; Sam McLoughlin <Sam.McLoughlin@parliament.govt.nz>
Cc: Glen Hildreth <Glen.Hildreth@mbie.govt.nz>; Sally Whineray Groom <Sally.Whineray@mbie.govt.nz>; Will Cosgriff <Will.Cosgriff@parliament.govt.nz>; Katrina Melville <Katrina.Melville@mbie.govt.nz>
Subject: Re: When proposal for retrospective change to s99(1A) could go to Cabinet

Hi Kathleen

To add - Sam is looking to set up a conversation with Minister Collins on a SBM matter - may be worth to see if this could be added onto the agenda.

Michelle

Get [Outlook for iOS]

From: Marcus Smith <Marcus.Smith2@mbie.govt.nz>
Sent: Wednesday, November 20, 2024 3:27:36 PM
To: Kathleen Henning <Kathleen.Henning@parliament.govt.nz>
Cc: Glen Hildreth <Glen.Hildreth@mbie.govt.nz>; Sally Whineray Groom <Sally.Whineray@mbie.govt.nz>; Michelle Schulz <Michelle.Schulz@mbie.govt.nz>; Will Cosgriff (Parliament) <Will.Cosgriff@parliament.govt.nz>; Katrina Melville <Katrina.Melville@mbie.govt.nz>
Subject: RE: When proposal for retrospective change to s99(1A) could go to Cabinet

Kia ora Kathleen,

I'm now proposing to get you a briefing that provides advice on whether the change should apply to active litigation or not (i.e. the sub-options) and then annexes both:

- The one-pager for consultation (reflecting the Minister's decision on this)
- Two versions of a draft letter to the AG (that account for either preference the Minister might reach between the sub-options) – to be delivered only after consultation.

If you're happy with this approach (explained further below), I'll prioritise this and aim to get the briefing to you Monday.

Explanation:
On reflection, we believe it's important the one-pager conveys to Ministers and coalition partners whether the Minister proposes to apply the change to the active litigation or not. Although we verbally gave our view that it should apply the active litigation, we don't have the Minister's agreement to this approach. This is a fairly material choice that we feel he should make on further advice from us s 9(2)(h) [redacted] This further advice was foreshadowed in the original briefing (see from para 26).

Happy to discuss if that's helpful. Otherwise, will wait to hear if you support this plan.

Ngā mihi
Marcus

From: Kathleen Henning <Kathleen.Henning@parliament.govt.nz>
Sent: Tuesday, November 19, 2024 4:56 PM
To: Marcus Smith <Marcus.Smith2@mbie.govt.nz>
Cc: Glen Hildreth <Glen.Hildreth@mbie.govt.nz>; Sally Whineray Groom <Sally.Whineray@mbie.govt.nz>; Michelle Schulz <Michelle.Schulz@mbie.govt.nz>; Will Cosgriff (Parliament) <Will.Cosgriff@parliament.govt.nz>; Katrina Melville <Katrina.Melville@mbie.govt.nz>
Subject: RE: When proposal for retrospective change to s99(1A) could go to Cabinet

Hi Marcus

Thank you for the update. There's probably still merit in the Minister socialising the proposal with his Ministerial colleagues and coalition partners as soon as possible. We will kick that off once we have the updated one-pager.

Thanks,
Kathleen

From: Marcus Smith <Marcus.Smith2@mbie.govt.nz>
Sent: Tuesday, 19 November 2024 2:16 PM
To: Kathleen Henning <Kathleen.Henning@parliament.govt.nz>
Cc: Glen Hildreth <Glen.Hildreth@mbie.govt.nz>; Sally Whineray Groom <Sally.Whineray@mbie.govt.nz>; Michelle Schulz <Michelle.Schulz@mbie.govt.nz>; Will Cosgriff <Will.Cosgriff@parliament.govt.nz>; Katrina Melville <Katrina.Melville@mbie.govt.nz>
Subject: RE: When proposal for retrospective change to s99(1A) could go to Cabinet

Thanks very much for getting the briefing back to us Kathleen!

I've started revising that one-pager and will aim to get another version to you tomorrow. The draft letter for the AG will come across in a briefing, which I'll get logged shortly.

One development at our end that may affect timing:
I've just heard that PCO are now sounding more cautious about the idea of these amendments being drafted in advance of policy approval. (Possibly this is about the amount of work they still need to do to get this Bill in order for introduction early next year, noting it is proving less straightforward than hoped, and there's potential to hold up the other two Bills.) PCO want the chance to discuss this internally and then with us. I'm not sure how long they'll need for this, but they will be advising the AG on this matter – so we'll want a bit more confidence they support it.

The more immediate question is whether there is still merit in the Minister socialising the proposal with coalition partners before we know we have PCO's support to draft in advance. I suspect there is, but it's for him/the Office to judge. Even if the Minister does ultimately need to take this separately to ECO before having a Bill ready for approval, I'm not sure there is a down-side to having tested it with coalition partners early. It may make consultation before ECO run smoother.

Let me know if you want to discuss any of this. Otherwise, I'll keep you across developments.

Ngā mihi
Marcus

From: Kathleen Henning <Kathleen.Henning@parliament.govt.nz>
Sent: Tuesday, November 19, 2024 11:07 AM
To: Marcus Smith <Marcus.Smith2@mbie.govt.nz>
Cc: Glen Hildreth <Glen.Hildreth@mbie.govt.nz>; Sally Whineray Groom <Sally.Whineray@mbie.govt.nz>; Michelle Schulz <Michelle.Schulz@mbie.govt.nz>; Will Cosgriff (Parliament) <Will.Cosgriff@parliament.govt.nz>
Subject: RE: When proposal for retrospective change to s99(1A) could go to Cabinet

Kia ora Marcus

Thank you for your email, that sounds like a good plan!

And thank you for your offer to provide a letter to the Attorney-General on behalf of the Minister – that would be very helpful. Regarding the one-pager, I note we already have the **attached**. However, it would be great if you could shorten and sharpen it, as well as add more bolding/ italics, and bullet points.

In the meantime, please find **attached** the signed retrospectivity briefing.

Many thanks,
Kathleen

From: Marcus Smith <Marcus.Smith2@mbie.govt.nz>
Sent: Tuesday, 19 November 2024 10:16 AM
To: Kathleen Henning <Kathleen.Henning@parliament.govt.nz>

Cc: Glen Hildreth <Glen.Hildreth@mbie.govt.nz>; Sally Whineray Groom <Sally.Whineray@mbie.govt.nz>
Subject: When proposal for retrospective change to s99(1A) could go to Cabinet

Kia ora Kathleen,

I remembered just after our call that our proposed plan is to get amendments drafted in anticipation of Cabinet approval (with the Attorney-General's blessing) and then have ECO act for LEG in approving the Bill for introduction. We're hopeful this wouldn't affect the timetable we had earlier suggested: we could still aim for the last week of February (but for ECO, rather than LEG), with introduction and first reading possible in the first week of March. It would just increase potential for snags along the way.

We continue to recommend this approach. The alternative of running two processes so that we can have the amendments drafted following ECO approval would either mean:

- taking significant shortcuts to try and get the proposal through ECO in the last meeting this year; or
- holding up introduction of the Bill next year (by a month or so).

The main thing our recommended approach depends on is the Attorney-General authorising PCO to draft the amendments in anticipation. This involves the Minister providing a letter to the AG, which we can prepare.

One of the assurances the Minister would need to provide the AG is that coalition partners are likely to be on board. We have already consulted the Ministry of Regulation on the briefing, and they had no concerns with the proposal. But it may be advisable for the Minister to do some further consultation. We can provide more material (e.g. a one-pager) to facilitate this if you need. We would suggest this happens soon, as it can take a while for the AG to respond to these requests and we need to allow PCO a bit of time to draft these amendments before consultation next year on a complete Bill.

Please let us know who you'd like to proceed and how we can help.

Ngā mihi
Marcus

Hon Judith Collins
Attorney-General
Parliament Buildings
Wellington

Dear Judith

As discussed with you on 25 November, I am writing to request your agreement for the Parliamentary Counsel Office to draft an amendment in advance of approval by Cabinet. I am making this request in accordance with paragraph 7.55 of the Cabinet Manual.

The Government has agreed to a range of financial services reforms [*ECO-24-MIN-0178 and ECO-24-Min-0262* refer]. To implement consumer credit reforms, drafting is underway for a *Credit Contracts and Consumer Finance Amendment Bill* (**the Bill**).

The amendment in question would address a legacy problem with section 99(1A) of the Credit Contracts and Consumer Finance Act 2003. Section 99(1A) provides that debtors are not liable for the costs of borrowing during a period where a lender has breached disclosure requirements.

The amendment related to this provision would ensure the courts are empowered to reduce or extinguish the effect of section 99(1A) where they consider it just and equitable to do so – in other words, if necessary to avoid consequences that would be grossly disproportionate in the circumstances. This discretion was provided to the courts (on application by the lender) in 2019, but was not applied retrospectively at that time.

One of the reforms Cabinet agreed earlier this year is a further improvement to how consequences under section 99(1A) are determined. This change would also apply only prospectively (to new disclosure failures).

There are unresolved concerns about compliance issues lenders may have had before the reforms in 2019. Concern about the potential consequences of the pre-2019 law on the consumer lending market have increased in recent years, as a result of active class litigation against ANZ and ASB. My officials are particularly concerned about the potential impact on the position of smaller, domestic lenders.

Backdating the 2019 reforms would ensure the courts have the flexibility they need to facilitate just and equitable outcomes for all parties, regardless of when the disclosure failure occurred. This would be an amendment with retrospective effect, and it would apply equally to class litigation currently afoot.

s 9(2)(h) [redacted] as well as the Reserve Bank of New Zealand, have been involved in advice on this issue. I have already obtained the Minister of Finance's support for retrospective legislation.

The [*insert names of coalition parties and other senior Ministers*] are likely to support this amendment.

The Bill is necessary to give effect to coalition agreement commitments to reform financial services. It is time-critical because it implements a transfer of regulatory functions from the Commerce Commission to the Financial Markets Authority. I first announced this transfer in January. Affected staff and industry are awaiting certainty about the details and timing of this transfer. As well as criticism if enactment is delayed, there are also potential cost implications for the Commission. The Bill was Category 5 on the 2024 Legislation Programme, but its progress was delayed on reassessment. s 9(2)(f)(iv) [redacted]

Drafting of the rest of the Bill is well advanced. When I obtained Cabinet agreement for financial services reforms in September this year, I indicated I was expecting further advice on this issue, due to its potential market implications and retrospective nature. Obtaining Cabinet agreement before including the amendment would likely delay the Bill's introduction by two months. This, or introducing the proposal during select committee, would delay when enactment is possible, which risks pushing the transfer of functions s 9(2)(f)(iv) [redacted] To have the Bill enacted at the earliest opportunity requires drafting in advance of confirmation that Cabinet supports the proposal when approving the Bill for introduction.

If you agree, officials will begin instructing Parliamentary Counsel immediately.

Yours sincerely

Hon Andrew Bayly
Minister of Commerce and Consumer Affairs

MINISTRY OF BUSINESS,
INNOVATION & EMPLOYMENT
HĪKINA WHAKATUTUKI

AIDE MEMOIRE

Financial Services Reforms overview

Date:	4 March 2025	**Priority:**	High
Security classification:	**In Confidence**	**Tracking number:**	BRIEFING-REQ-0010349

Information for Minister
Hon Scott Simpson Minister of Commerce and Consumer Affairs

Contact for telephone discussion (if required)

Name	Position	Contact for	Telephone	1st contact
Tom Simcock	Manager, Financial Markets	Conduct and Dispute Resolution	s 9(2)(a) [redacted]	✓
Glen Hildreth	Manager, Consumer Policy	Consumer credit	04 901 0687	✓

Minister's office to complete:

- ☐ Approved
- ☐ Noted
- ☐ Seen
- ☐ See Minister's Notes
- ☐ Declined
- ☐ Needs change
- ☐ Overtaken by Events
- ☐ Withdrawn

Comments:

MINISTRY OF BUSINESS, INNOVATION & EMPLOYMENT
HĪKINA WHAKATUTUKI

AIDE MEMOIRE

Financial Services Reforms overview

Date:	4 March 2025	**Priority:**	High
Security classification:	**In Confidence**	**Tracking number:**	BRIEFING-REQ-0010349

Purpose

To provide you with an overview of the Financial Services Reforms package, including the Bills for introduction and the annexed Cabinet papers ahead of seeking Cabinet Economic Policy Committee approval on 12 March 2025.

Tom Simcock
Manager, Financial Markets
Commerce, Consumer and Business, MBIE

4 March 2025

Glen Hildreth
Manager, Consumer Policy
Commerce, Consumer and Business, MBIE

4 March 2025

Background

1. In 2024, Cabinet made decisions resulting in a package of reforms to streamline and ensure the effectiveness of financial services regulation [EXP-24-MIN-0010, CBC-24-MIN-0031, ECO-24-MIN-0178 and CAB-24-MIN-0445 refer].

2. The reforms support the Competitive Business Settings pillar under the Going for Growth economic agenda.

If you agree to progress this work, the next step is for Cabinet to approve legislation for introduction

3. The financial services reforms package is being delivered through the following three bills:

   a. Credit Contracts and Consumer Finance Amendment Bill ("Credit Bill"), to simplify and streamline the regulation of consumer credit.

   b. Financial Markets Conduct Amendment Bill ("Conduct Bill"), to strengthen financial markets conduct by making it easier for participants to comply with the requirements of the financial markets regulatory system and for the FMA to administer

   c. Financial Service Providers (Registration and Dispute Resolution) Amendment Bill ("Dispute Resolution Bill"), to improve the performance and governance of financial dispute resolution schemes.

4. A summary of the policies given effect by these three Bills is provided in **Annex 1.**

5. If you agree to progress this work, the next step is to seek Cabinet approval to make some additional policy decisions and introduce the three Bills.

Draft Cabinet papers

6. Two Cabinet papers seeking further policy decisions and approval to introduce the above Bills are ready to be lodged, subject to any feedback you have. We recommend they be lodged this week for the Cabinet Economic Policy Committee (acting for the Cabinet Legislation Committee[1]) meeting on 12 March:

   a. Cabinet paper one seeks:

      i. approval to introduce the Credit Bill

      ii. agreement to proposals highlighted in **Annex 1** that have been included in the Bill in anticipation of Cabinet's approval

   b. Cabinet paper two seeks:

      i. approval to introduce the Conduct Bill and Dispute Resolution Bill

      ii. agreement to proposals highlighted in **Annex 1** that have been included in the Bill in anticipation of Cabinet's approval

[1] Although the Cabinet Legislation Committee normally approves bills for introduction, these papers are more suitable for a policy committee because they seek approval for substantive policy changes included in the Bills.

iii. approval for a commencement order to introduce definition changes for the Contracts of Insurance (Repeals and Amendments) Act to simplify regulatory settings related to the CoFI Act coming into force on 31 March

iv. technical changes to FMC Regulations for the Depositor Compensation Scheme to provide regulatory certainty about disclosure settings for non-bank deposit takers when the scheme commences on 1 July.

Risks

Financial services reforms generally

7. Stakeholders were generally supportive of the reforms. There is a risk that some of the reforms may be seen as overloading the sector with more changes in a period of change, for example the Deposit Taker's Act changes happening at the same time. Overall, we expect that most of the changes will remove regulatory burden and have communicated proposals and timing where possible to mitigate impacts.

New policy approvals

8. Each of the Bills includes policy changes agreed by your predecessor, but which Cabinet has not yet approved. However, most of the new proposals have been subject to some consultation and regulatory impact analysis. The proposals are within the intent of the existing policy decisions.

9. The retrospective change included in the Credit Bill to consequences for lenders who failed to make certain disclosures as required may attract criticism from lawyers, consumer advocates and ANZ and ASB customers who are represented in active class litigation against those banks, whose case the change expressly affects. However, the change would not necessarily alter the outcome in that case, as it only ensures the court has discretion to decide what is just and equitable to all parties, given the nature and circumstances of the case.

Timing

10. Your predecessor sought for all three Bills to be passed this year, and sought indicative agreement from the Leader of the House for a shorter select committee report back (five months). In particular, for the transfer of functions and associated changes under the Credit Bill to be operationalised this year, the Bill would need to be passed by October 2025. Delays would prolong uncertainty for Commerce Commission staff whose roles will be disestablished and are subject to offers of equivalent employment with the Financial Markets Authority, conditional on the legislative change. The Credit Bill also creates uncertainty for industry.

11. We now understand the Bills are unlikely to have their first reading until April. With the planned five-month select committee process, this would leave only a few sitting weeks for the Bills to proceed through their final stages in the House before the end of October 2025.

12. Your predecessor intended to seek Business Committee approval to associate the Bills through all reading stages in order to save House time. This would require unanimous

agreement from all members. If the Business Committee does not agree to associate the Bills, they might progress on different timeframes which would impact implementation.

Next steps

13. If you agree to progress the Bills, we recommend the following next steps:

Timing	Step
Before Cabinet	Consult on associating the Bills
Before Cabinet	Confirm Select Committee timing. Your predecessor had indicative agreement from the Leader of the House to a shorter report back from the Select Committee (five months).
6 March	Subject to your views, lodge the two Cabinet papers for ECO on 12 March
12 March	ECO
After Cabinet approval (likely 17 March)	Introduce the Bills to the House and announce the Bills once introduced. We will provide a draft press release and reactive Q&A to you in mid-March.
After introduction, before first reading (likely week of 17 March):	Seek Business Committee approval to associate the Bills following introduction. An updated letter will be provided to your office.
Before First Reading (likely April):	Subject to Business Committee agreement to associate the Bills, move the Bills be read for a first time at First Reading and seek the Bills be referred to the Finance and Expenditure Committee. We will provide speech notes to your office.

14. We are available at your convenience, should you wish to be briefed fully on any of the proposals in any of the Bills.

Annexes

Annex One: Policies implemented by the three Bills

Annex Two: Cabinet paper seeking approval to introduce the Credit Bill

Annex Three: Cabinet paper seeking approval to introduce the Conduct and Dispute Resolution Bills

Annex Four: Regulatory Impact Statement for retrospective proposal relating to relief from consequences for disclosure failures by lenders

Annexes two-four are publicly available and listed in the document schedule attached to the response letter.

Annex One: Policies implemented by the three Bills

Bill		Policy change	Status
Credit Bill	Streamlining consumer credit regulation by transferring regulatory responsibility to the Financial Markets Authority and better aligning the regulatory model for with the Financial Markets Conduct Act		
	1	Transfer all functions under the Consumer Credit and Credit Contracts Act to the FMA	Cabinet approved September 2024
	2	Transition lenders from a certification regime to the FMCA's licensing regime (including by deeming incumbents to hold a licence)	
	3	Remove the due diligence duty on a lender's directors and senior managers and their personal liability for breach of that duty	
	4	Equip the FMA with other regulatory tools available under the FMCA (notably, stop order and direction order powers)	Cabinet decision to be modified
	5	Empower the FMA to make adjustments and clarifications to the scope of CCCFA obligations via declarations and exemptions in particular circumstances	Cabinet approved November 2024
	Moderating consequences for lenders' failure to make certain disclosures as required		
	6	Limit the effect of section 99(1A) (that a borrower is not liable for the costs of borrowing in relation to a period of non-compliant disclosure) to cases where a person, including the FMA, can show the borrower was harmed by the failure to make initial or agreed variation disclosure	Cabinet approved September 2024
	7	Retrospectively apply reforms made in 2019 which enable lenders to seek relief from consequences for disclosure failures that may be grossly disproportionate and apply this to active class litigation against ANZ and ASB	Yet to be approved by Cabinet
	Addressing less significant issues (minor and technical changes)		
	8	Several other changes that are necessary to reduce unnecessary regulatory burden, clarify obligations or extend protections, such as: • More consistent treatment of trusts • Clearer protections for 'insurance shortfall repayment waivers' and cancellation rights • Better defined boundaries around an obligation to provide disclosure before debt collection.	Yet to be approved by Cabinet
	Strengthen financial markets conduct by making it easier for participants to comply with the requirements of the financial markets regulatory system and for the FMA to administer		

Bill		Policy change	Status
Conduct Bill	9	Simplify and clarify minimum requirements for fair conduct programmes,[2] contained in the incoming Financial Markets (Conduct of Financial Institutions) Amendment Act 2022 (**CoFI Act**)	Cabinet approved September 2024
	10	Consolidate conduct licensing by requiring the FMA to issue a single market services licence covering different classes of market services, including for consumer credit where applicable	Cabinet approved September 2024
	11	Introduce change in control (CIC) approval requirements requiring persons in firms holding a market services licence under the FMC Act to obtain regulatory approval from the FMA prior to a proposed change in ownership or control of the licensed firm taking effect. This ensures that a proposed restructure does not negatively affect consumers and aligns with the prudential approach to CIC.	Cabinet approved September 2024 Additional Cabinet decisions are needed to: 1. cover significant transactions (asset sales) and amalgamations (mergers) 2. require 'authorised bodies' to seek CIC approval 2. include a new regulation-making power to carve out some groups from some or all CIC approval requirements
	12	Introduce an on-site inspection power for the FMA to enter without notice and inspect a financial market participant's place of business for routine and proactive compliance monitoring purposes.	Cabinet approved September 2024
	13	A range of minor and technical amendments to reduce regulatory burden. For example, • changes to independence requirements for licensed independent trustees of certain restricted investment schemes	Cabinet approved September. Minister approved additional changes February.[3]
	Improve the performance and governance of financial dispute resolution schemes		

[2] Fair conduct programmes are policies, processes, systems and controls that are designed to ensure the financial institution's compliance with the fair conduct principle

[3] Annex Five, BRIEFING-REQ-0006622

Bill	Policy change		Status
Dispute Resolution Bill	14	Require the responsible Minister to decide when and how the schemes must undertake their independent reviews, which must take place at least once every five years	Cabinet approved September 2024
	15	Provide a new regulation-making power which can be used to set the skills, experience and independence requirements of board members	Cabinet approved November 2024
	16	Minor and technical changes relating to reviews and annual reports	Minister approved February[4]

[4] Annex Five, BRIEFING-REQ-0006622

Credit Bill: section 99(1A) reforms

The current law

1. Section 99(1A) of the CCCFA (created in 2015) provides that the borrower is **not liable for the costs of borrowing** (all interest and fees charged) over any period in which the lender failed to make either:

    a. 'initial disclosure' – a requirement to provide certain 'key information' specified by the CCCFA before they enter into a loan agreement

    b. 'agreed variation disclosure' – a requirement to provide borrowers with details of an agreed change, in most cases, before the change takes effect.

2. This appears to mean the lender must **forfeit the costs of borrowing** to all affected borrowers, without exception.

3. Costs of borrowing **could be a significant sum** where the disclosure breach affected a large number of customers and was not identified quickly.

4. **Reforms in 2019 address potential for a disproportionate outcome**. They enable the courts to disapply section 99(1A) or reduce the amount owed, if that would be 'just and equitable'.

5. However, **this discretion was only provided prospectively** (i.e. for the costs of borrowings after December 2019).

Further (prospective) reforms already agreed by Cabinet

6. Last year, **Cabinet agreed to some further changes** to these provisions, aimed at more clearly reducing the potential impact on lenders where the disclosure failure was harmless:

    a. The Bill reverses the starting point (ie borrowers remain liable for costs of borrowing), but enables borrowers or the FMA to **seek an order from a court that the lender must refund some or all of the costs of borrowing**. The court would have to be satisfied the disclosure breach caused 'loss or damage'.

    b. These changes would apply prospectively only (they don't address a historical problem).

Class litigation has increased concern about the 2015-2019 period

7. In 2021, class litigation was brought against ANZ and ASB for **alleged breaches** of agreed variation disclosure **that occurred between 2015 and the 2019 reforms**.

8. A possible outcome is that the court finds it is **bound to require full forfeiture** of the costs of borrowing in relation to any disclosure failure from this period.

ANZ's compliance issue

Over a one-year period beginning in 2016, due to a coding error, ANZ's loan variation disclosure forms misstated the details of interest payable under the loan as varied. The miscalculations were very minor (e.g. out by less than $2 per month).

In 2017, ANZ notified the Commission of this. By 2019, it had paid $8.3million in remediation to 102,000 affected customers.

In 2020, ANZ settled with the Commission on the basis it had breached one of the 'lender responsibility principles' in the Act and agreed to pay total remediation of $35million to affected customers. S9(2)(ba)(i) [redacted]

9. Although full-forfeiture would mean significant losses for ANZ and ASB, modelling of this scenario **does not suggest imminent stability risks**.

10. Of greater concern is the **threat to smaller lenders** who may also have had compliance issues over this period, including **domestic banks** and **non-bank deposit-takers**. A full-forfeiture finding would likely spill over to these lenders.

11. They would be **less well placed** to absorb losses as a similar proportion of their loan book.

12. There is a **public interest** in avoiding this possible outcome, given it **could impact the supply** of credit to consumers and degree of **competition in the market**.

Proposed solution: retrospective amendment

13. The Bill would address this problem by **making the 2019 reforms apply retrospectively**. This would **ensure the courts have discretion** to consider what redress is just and equitable in the circumstances, for any disclosure failures made after 2015.

14. A second-order choice is **whether this amendment should affect litigation that is already afoot**, notably the class litigation against ANZ and ASB comprising:

    a. around 17,000 ANZ customers

    b. around 47,000 ASB customers.

15. The Bill does this (and expressly names that case) to ensure that the court:

    a. is able to decide **this case on the same basis** it would decide any future cases of this kind

    b. has **flexibility to avoid** an outcome that it could consider **excessive or unjust**.

16. This amendment will be criticised because it **appears to interfere** with the expectation of represented borrowers to have their case determined on the basis of the law as it stood at the time.

17. However, the amendment **does not necessarily change the outcome** in that case. It only **improves the court's ability to determine what is just and equitable** to all parties in the circumstances.

18. The class litigation is also **at an early stage** (has not proceeded to a hearing of the substantive matters yet).

Speaking points and Q+A for CBC on 17 March 2025: Approval to introduce financial services reform bills

Speaking notes

Key messages:

- I am seeking approval for two Cabinet papers which progress a package of reforms to financial services regulation.

- The papers seek approval to introduce three bills and associated policy approvals:

    - The **Credit Contracts and Consumer Finance Amendment (CCCFA) Bill**, which creates one conduct regulator for financial markets by transferring responsibility for consumer credit to the FMA and better aligning the CCCFA's regulatory model with financial markets legislation.

    - The **Financial Markets Conduct Amendment Bill** simplifies core system obligations on financial institutions, consolidates financial service licensing into a single licence, and ensures the FMA's regulatory toolkit is risk-based and proportionate

    - The **Financial Service Providers (Registration and Dispute Resolution) Amendment Bill** enhances the independence and effectiveness of the financial dispute resolution schemes and clarifies their annual reporting requirements.

- The legislation will cut red tape and reduce compliance costs by introducing more proportionate financial market regulation and ensuring protection for consumers.

not relevant to your request.

Possible questions and answers

What are the new policy proposals you are seeking agreement to?

Key proposals across the bills include:

- Amendments to the CCCFA with retrospective effect to address a legacy problem relating to consequences for lenders who breached disclosure requirements. This would backdate reforms made in 2019 to ensure that courts have the flexibility to decide what redress is appropriate in the circumstances of the breach. This will apply to active class litigation against ANZ and ASB.

- Widening the availability previously agreed by Cabinet of stop orders and direction orders the FMA would be able to make in response to breaches of the CCCFA.

not relevant to your request.

Do these reforms go far enough in removing red tape?

- These reforms simplify the approach to regulation in important ways that will reduce the burden on regulated entities.

- For example, lenders will be answerable only to one conduct regulator, using a consistent approach to securing compliance, and they will no longer be inhibited by excessive personal liability settings.

- The obligations imposed by the new CoFI regime are also being tailored and simplified, which will particularly help smaller institutions.

- These reforms are informed by wide feedback from industry. They are meaningful changes to progress now and do not preclude consideration of further changes in future, if necessary.

- It is important to move the Bills move quickly through the House. The Credit Bill, in particular, creates significant uncertainty for affected staff at the Commerce Commission who will be transferred to FMA, as well as for stakeholders.

How have stakeholders reacted so far?

- Stakeholders have been generally supportive of the reforms. There is a risk that some of the reforms may be seen as overloading the sector with more changes in a period of change – for example the Deposit Takers Act changes happening at the same time.

- Overall, we expect that most of the changes will remove regulatory burden and have communicated proposals and timing where possible to mitigate impacts.

Questions specific to the Credit Bill

not relevant to your request.

Should we be concerned about these reforms being blamed later for harmful lending?

- There is a risk some reforms are perceived to weaken protection for consumers (such as removal of the due diligence duty for directors and senior managers, and the s99(1A) reforms).

- However, we're also significantly improving the tools available to the regulator to intervene earlier and more effectively where necessary to protect the interests of consumers.

- Things like stop order and direction order powers are significant powers, and quite rare. The licensing model also means the FMA will have more direct oversight and ability to respond early to issues.

Why do we care about how section 99(1A) applied over five years ago (i.e. what is the historical problem)?

- Prior to reforms in 2019, there appeared to be no exception to the rule in section 99(1A) that lenders must forfeit the full costs of borrowing (i.e. all interest and fees) that borrowers paid without the information the lender was required to disclose. This could end up being a significant sum where:
  - the disclosure breach affected a large number of customers (e.g. because statements are produced by automated systems)
  - it took a long time for the lender to identify the issue and make corrective disclosure.

- This could result in lenders having to pay redress that is disproportionate to the nature and circumstances of the breach. The 2019 reforms were designed to address this by enabling the court to modify or extinguish the effect of section 99(1A) on application by the lender, based on what it considers 'just and equitable'.

- A range of lenders may have had compliance issues that exposes them to liability under the pre-2019 law. Officials are particularly concerned about the ability of smaller, domestic banks and other deposit takers to absorb losses on this scale. Therefore, if the court in the case against ANZ and ASB finds that it is bound to require full forfeiture, this law could therefore have implications for the supply of consumer credit and competition in the market.

- Backdating the 2019 reforms to June 2015 (when section 99(1A) took effect) would address this risk by ensuring courts can consider the appropriate redress on a case by case basis.

What are some examples of disclosure breaches relevant to section 99(1A)?

- There are two disclosure requirements relevant to this provision:
    - 'initial disclosure' is the requirement to provide borrowers with certain 'key information' specified by the CCCFA – before they enter into a loan agreement
    - 'agreed variation disclosure' is the requirement to provide borrowers with 'the full particulars of the change' and any consequential changes to the borrower's obligations – in most cases, this is required before the change takes effect.

- One example of a breach of the initial disclosure requirement was a finance company ('Cash in a Flash') who failed to disclose information to customers that included the details of its dispute resolution scheme and the borrower's right to apply for changes in the case of unforeseen hardship. They corrected these statements and agreed to pay refunds to affected customers.

- ANZ and ASB are both alleged to have breached agreed variation disclosure:
  - Over a one-year period beginning in 2016, ANZ's loan variation disclosure forms suffered from a coding error that misstated the details of interest required to be paid under the loan as varied.
  - Over a four-year period beginning in 2015, ASB had an issue with its procedures which meant it had not consistently provided variation disclosure to its customers

Why are we making changes to section 99(1A) prospectively while we're also extending the current law back in time?

- These two changes address distinct issues. The retrospective change is necessary to address a historical problem that could negatively affect the market, whereas the prospective changes are focussed on providing sufficient but proportionate incentives on lenders to make proper disclosures and quickly fix any failures.

- Backdating the 2019 reforms is an effective way to address the historical problem – the problem relates to the possibility that a court never has discretion over liability for the costs of borrowing, and the 2019 reforms ensure that discretion is available.

- Requiring a court to order that the lender must refund costs of borrowing following a disclosure breach, only once satisfied there was loss or damage, would give lenders more confidence they don't need to worry about trivial breaches while maintaining the possibility of having to refund a significant sum in more serious cases.

Do we actually need to apply the retrospective change to active class litigation?

- Although the case against ANZ and ASB could produce significant losses, officials do not have immediate concerns about their position. Those banks have generous capital buffers and are supported by their parent companies overseas. The concern relates more to how the finding in that case could affect smaller entities, such as domestic banks and non-bank deposit takers.

- The reasons I am seeking to have the amendments apply to the active litigation are to ensure that the court:

    - is able to decide this case on the same basis it would decide any future cases of this kind

    - has flexibility to avoid an outcome that it could consider excessive or unjust.

Won't it look like we're interfering to protect the big banks?

- This amendment does not necessarily change the outcome in that case. All it would do is ensure the court is able to use its discretion to decide what is just and equitable to all parties, given the nature and circumstances of any disclosure breach.

- There will likely be a perception that the Government is changing the 'rules of the game' after proceedings commenced, and in a way that has up-side potential only for the banks. However, this ultimately depends on how the court uses its discretion. Full forfeiture of the costs of borrowing to affected borrowers is still possible.

- Another reason the actual degree of interference with this case is questionable is that, although proceedings commenced in 2021, the case is still at an early stage (in that it hasn't proceeded to a hearing of the substantive matters).

not relevant to your request.

Regulatory Impact Statement: Whether to apply legislation retrospectively to give courts discretion when considering consequences for disclosure failures by lenders

Coversheet

Purpose of Document	
Decision sought:	Cabinet approval to amend the Credit Contracts and Consumer Finance Act with retrospective effect
Advising agencies:	MBIE
Proposing Ministers:	Minister of Commerce and Consumer Affairs
Date finalised:	5 March 2025

Problem Definition

Lenders who, before December 2019, breached certain requirements to disclose information to borrowers (under loan agreements entered into after June 2015) are subject to a law that arguably makes them liable to forfeit all interest and fees paid on the loan, accumulated over the full period of non-compliance, to all affected borrowers. Active class litigation is expected to reveal whether the courts are bound to award this remedy to borrowers. That possible outcome could significantly impact the financial position of an unknown number of lenders with compliance issues during that period. Accordingly, it poses a potential threat to the long-term supply of consumer credit and degree of competition in the market.

Executive Summary

Section 99(1A) of the Credit Contracts and Consumer Finance Act 2003 took effect in June 2015, applying to loan agreements entered into after that date. It (and comparable provisions in relation to consumer leases and buy-back transactions of land) provides that the borrower is not liable for the costs of borrowing over any period in which the lender failed to make compliant initial or agreed variation disclosure.

Full forfeiture of the costs of borrowing to all affected borrowers could be grossly disproportionate to the nature and circumstances of a disclosure failure. Reforms in December 2019 recognised this by enabling the courts to extinguish or reduce the effect of section 99(1A), on application by the lender, if it would be 'just and equitable' to do so. However, this discretion was only provided prospectively (i.e. for the costs of borrowings after December 2019).

In September 2024, Cabinet agreed to some further changes to these provisions, aimed at more clearly protecting lenders from liability where the disclosure failure was harmless. These changes would also apply prospectively only.

In 2021, class litigation was brought against ANZ and ASB for alleged disclosure failures pre-dating the 2019 reforms. A possible outcome in this litigation is that the court finds it is bound to require full forfeiture of the costs of borrowing in relation to any disclosure failure from this period. This creates the potential for significant losses for ANZ and ASB in the first instance, but also for lenders in a more precarious position than ANZ and ASB. This could threaten effective and competitive supply of credit to consumers over the long-term.

A direct way to address this problem is to make the 2019 reforms apply retrospectively. This would ensure the courts have discretion to consider what remedy is just and equitable in the circumstances, no matter when the disclosure failure occurred.

A key choice is whether this amendment should affect litigation that is already afoot, notably the proceedings involving ANZ and ASB. Doing so (Option Three) best improves on the counterfactual (no intervention) when assessed against our criteria. Providing the court with explicit discretion to deliver a just and equitable outcome is not, in our view, an objectionable kind of interference with proceedings already before a court. Option Three would ensure liability of a lender for any disclosure failure under section 99(1A) is able to be determined on the same legal basis.

This proposal would be included in a Credit Contracts and Consumer Finance Amendment Bill and its impact monitored by both the Financial Markets Authority and MBIE.

Limitations and Constraints on Analysis

This is a commercially sensitive matter for a range of lenders who may have liability under the law that is proposed to be amended with retrospective effect. How this area of the law applies is being actively considered by the courts in class litigation against two of the largest banks in New Zealand.

Although we were able to undertake some consultation on this issue, these two factors have limited the nature and extent of consultation we could appropriately undertake.

Relatedly, uncertainty about the number of lenders with liability under the historical law in question, and the extent of that liability, is a notable constraint on our understanding of the problem. The problem arises from a possible outcome of active litigation which has unknown implications for an unknown number of lenders other than the defendants. We have not been able to ascertain whether those implications would be on a scale that undermines the supply of credit, but rather have assumed this is a credible possibility.

The only relevant data we have are investigations opened by the Commerce Commission that appear to concern the conduct (and period) in question. These data are subject to various constraints and the reporting of issues (including self-reports of issues that may create significant liability for the lender).

A constraint on our ability to compare outcomes under the counterfactual and the legislative options is that they materially depend on how a court would apply the law with or without amendment. Outcomes will turn on questions of statutory interpretation that have not been directly answered by any case law to date, as far as we are aware. These questions create uncertainty relevant to our analysis, including whether a court would apply the preferred option in a manner that avoids the concerns ultimately motivating legislative change.

We also need to exercise restraint in speculating as to how the current or proposed law would be interpreted, given proceedings are currently before the courts.

Responsible Manager	
Glen Hildreth Manager Consumer Policy Ministry of Business, Innovation and Employment 5 March 2025	

Quality Assurance (completed by QA panel)	
Reviewing Agency:	MBIE
Panel Assessment & Comment:	A quality assurance panel with representatives from MBIE has reviewed this Regulatory Impact Statement (RIS). The panel has determined that the RIS meets the quality assurance criteria.

Section 1: Diagnosing the policy problem

What is the context behind the policy problem?

Section 99(1A), introduced in 2015, provides that borrower is not liable for the costs of borrowing over a period of non-compliant disclosure

1. Section 99 of the *Credit Contracts and Consumer Act 2003* (**CCCFA**) prohibits lenders from enforcing consumer credit contracts before they have made 'initial' disclosure[1] or 'agreed variation' disclosure.[2]

2. Section 99(1A) was added in June 2015, and applies to loan agreements entered into after that date. It was developed in response to a High Court judgment from 2013,[3] where a finance company had failed to make a compliant initial disclosure and sought to 'enforce' the contract after making compliant disclosure two and half years into the contract. The High Court found that the finance company was then, having remedied its non-compliance, entitled to recover all the interest and fees (the costs of borrowing) that should have been paid during the period of non-compliance.

3. Section 99(1A) was an attempt to reverse this position. It provides that the borrower is not liable for the costs of borrowing (i.e. interest and any fees) over any period in which the lender has failed to make initial or agreed variation disclosure, until they make corrective disclosure. Equivalent provisions were added for consumer leases and buy-back transactions (if similar disclosures were not made). This is essentially the position that a consumer should not incur any costs from a contract they entered into or varied without full information they are legally entitled to.

[1] This is 'key information' about the lender and the agreement being entered into, such as the interest and fees payable, and the details of the lender's dispute resolution scheme.

[2] This is disclosure of the details of the change to the agreement the parties have agreed and its effect on other terms of the agreement (such as the total interest that will be charged, if that changes).

[3] *Norfolk Nominees Ltd v King* [2013] NZHC 398

4. The limitation periods on damages/redress under the CCCFA were also amended in June 2015.[4] Prior to that, they used to extinguish a lender's liability three years after a breach occurred. Since 2015, they instead extinguish liability three years after the breach was discovered or "ought reasonably to have been discovered". As with section 99(1A), this only applied to new agreements, meaning lenders today have no liability to pay damages/redress for breaches preceding June 2015.

Section 99(1A) did not clearly allow for differential treatment of different circumstances

5. The original 2015 reforms did not expressly provide the courts with any discretion over what amount (if any) lenders should forfeit to affected borrowers. They did not clearly account for the fact that some disclosure failures affect the borrower's ability to make informed decisions less than others, or that the the full costs of borrowing could be excessive in some circumstances. Where a relatively immaterial failure affected a large number of borrowers, and was not noticed (and therefore able to be corrected) until many years later, the full costs of borrowing could amount to a significant sum.

6. Section 48 of the CCCFA requires lenders to refund money wrongly paid to them as soon as practicable. There is uncertainty about how the courts would apply these provisions, as there has not been any court judgments that we are aware of directly on the matter. It is possible that the combined effect of section 99(1A) and section 48 is to immediately require the lender to forfeit all interest and fees paid by the borrower over the period of defective disclosure.

Reforms in 2019 gave the court explicit discretion to consider the nature and circumstances of a disclosure failure

7. In December 2019, the CCCFA was amended to address the risk of disproportionate consequences. The reforms gave the courts explicit discretion, on application, to extinguish or reduce the effect of section 99(1A) (and equivalent provisions for consumer leases and buy-back transactions) if they consider it just and equitable to do so (section 95A). The court must consider certain factors in reaching this decision. These factors relate to the objective of incentivising compliance with the CCCFA, how the breach occurred, the prejudice it caused and what the lender did in response, as well as "any other matters the court thinks fit" (section 95B).

8. The Government of the day, supported by MBIE's advice at the time[5], made this relief available only for liability arising on or after the commencement of the change (i.e. from December 2019 onwards), and not retrospectively to liability arising between June 2015 and December 2019. This was a choice actively made at the time, with the result that the law appears to operate differently depending on whether the disclosure breach occurred before or after December 2019.

9. MBIE's advice was based largely on general legal principles. Although the policy rationale for the reforms did not extend back in time, there was no clear and specific policy reason the same discretion should not have been available for earlier disclosure failures.

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[4] Sections 90(3) and 95(2) of the CCCFA

[5] MBIE's advice was based on regulatory impact analysis in 2017, that can be found here: [Regulatory impact statement]

Policies agreed by Cabinet in 2024 included prospective changes to consequences for incomplete disclosure

10. The Government is progressing a range of financial services reforms aimed at streamlining regulation of the sector. Cabinet made policy decisions on these reforms on 2 September 2024 [*CAB-24-MIN-0334* refers]. These decisions include legislative changes to the CCCFA.

11. One of these policy changes was to limit the effect of section 99(1A) to cases "where a person can show the borrower was harmed by the failure to make initial or agreed variation disclosure" [*ECO-24-MIN-0178*, paragraph 8, refers].[6] This means the starting point will no longer be as described by section 99(1A). The borrower's liability for the costs of borrowing can only be removed if a court is satisfied harm resulted from a lender's failure to make initial or agreed variation disclosure and accordingly makes an order requiring the lender to return some or all of the costs of borrowing.

12. The September policy change would apply prospectively. However, the Minister of Commerce and Consumer Affairs indicated to Cabinet he was expecting further advice on disclosure failures that occurred between 2015 and 2019.

13. A table showing how this part of the CCCFA applies differently to disclosure failures over time (as a result of reforms, including those agreed by Cabinet in 2024) is provided as **Appendix one**.

Litigation will determine how the courts apply section 99(1A) without explicit discretion over the 2015 – 2019 period

14. Since 2015, lenders and their representatives have raised with MBIE and successive Ministers their concerns over section 99(1A), and the potential for disproportionate consequences relative to the seriousness of the disclosure failure.[7] While the changes made in 2019 reduced these concerns, lenders continue to raise concerns regarding the 2015-2019 period.

15. Proceedings against ANZ and ASB began in 2021. The litigants allege breaches of disclosure requirements for agreed variations affecting a class of borrowers. This followed settlements between each bank and the Commerce Commission relating to breaches of lender responsibility principles, which included compensation to affected borrowers.[8] As the alleged disclosure failures pre-date the 2019 reforms, the litigants argue that section 99(1A) and section 48 required the lenders to forfeit the full costs of borrowing to all affected borrowers.

16. This would be a sum of potentially Free and frank opinions (or, in any case, an amount substantially greater than the compensation already paid). It is not obvious from the nature of the alleged disclosure failures that they caused real harm to borrowers' ability to make informed decisions about those loans. This case is proceeding through the courts. It will likely be a few years or more before a judgment is delivered.

17. This litigation has renewed concern from a range of lenders about potential liability in the consumer lending market for disclosure failures in the 2015-2019 period if the court finds in

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[6] The RIS supporting this decision, and providing further background on the financial services reforms as well as the CCCFA, can be found here: Regulatory Impact Statement: Fit for purpose consumer credit law (mbie.govt.nz)

[7] See for example: New Zealand Banking Association's submission on MBIE's 2018 discussion paper: Submission on discussion document: Consumer Credit Regulation Review

[8] Details of both settlements can be found on the Commerce Commission's case register: Commerce Commission - ANZ Bank New Zealand Limited and Commerce Commission - ASB Bank Limited

favour of these litigants. The Court of Appeal has recently decided the class of affected borrowers in this case is determined on an ‘opt out’ basis, which increases the potential quantum of any settlement.

How is the status quo expected to develop?

18. It is not clear how the pre-2019 law would be applied by the courts without retrospective legislative change. The range of possible outcomes from this litigation, and implications for other lenders, depend on questions that include:

    a. what is required to make agreed variation disclosure (disclosure required when a lender and borrower agree to vary the loan terms)

    b. whether section 99(1A) applies to incorrect (as well as incomplete) disclosures

    c. whether there is a de minimis exception to disclosure breaches

    d. whether section 99(1A) only applies in circumstances where a loan is in distress, meaning it only applies to prevent a lender going to court to seek to enforce the costs of borrowing during a period where disclosure breaches are occurring (i.e. does not give rise to an obligation to refund the costs of borrowing where they have been paid by a borrower)

    e. when claims being made by the plaintiffs are out of time, based on statutory limitation periods

    f. whether the court already had inherent discretion (prior to section 95A) not to make an order requiring payment of the full costs of borrowing to affected borrowers.

19. One possible outcome is a finding that the law required lenders to forfeit the full costs of borrowing, no matter how inconsequential the disclosure failure (the ‘**full-forfeiture scenario**’).

20. The full-forfeiture scenario has the potential to affect other lenders who had issues complying with the relevant disclosure requirements prior to December 2019. This would likely happen through subsequent litigation against those lenders (assuming the lender denies liability for a relevant disclosure failure).

21. Both the number of other lenders affected and the amounts they could be required to forfeit under this scenerio are very uncertain:

    a. As of 12 August 2024, the Commerce Commission had resolved compliance issues with disclosures from this period with 15 active lenders, and has open investigations into four lenders. Many of these cases involve banks. However, it is possible other lenders have either not identified disclosure failures from this period or have chosen not to take any remedial steps that would draw attention to them.

    b. A key factor that would determine which of these lenders are affected is the relevant statutory deadline for filing a claim. It is uncertain both how and whether the CCCFA’s limitation period of “three years after the date on which the loss or damage was discovered or ought reasonably to have been discovered” would apply to disclosure failures triggering section 99(1A):

i. Free and frank opinions

ii.

iii.

c. The losses suffered by other lenders affected by a full-forfeiture scenario would depend on:

   i. the number of loans affected by that lender's disclosure failure

   ii. the amount of interest and fees charged under the loans affected (which depends on the period of time between the disclosure failure and when the lender corrected it, as well as the size of the loan)

   iii. the amount the lender has already paid to compensate affected borrowers for the failure.

22. Uncertainty about their potential liability for disclosure failures and costs of borrowing predating 2019 is generally unsettling for lenders.

What is the policy problem?

23. The law that applies to relevant disclosure breaches between 2015 and 2019 appears to make lenders liable for forfeiture of the full costs of borrowing, with a court having no explicit discretion to adjust or extinguish this result based on what it considers just and equitable.

24. This creates the possibility of a full-forfeiture scenario arising from active litigation. A full-forfeiture scenario would involve a transfer of wealth from lenders to their customers. Although this transfer could be considered somewhat arbitrary, it does not involve a direct cost to the New Zealand economy. The key question is what impact the transfer could have on the market for supply of consumer credit and the interests of consumers.

25. Our assessment is that it involves potential to reduce access to credit and reduce competition in the market, which ultimately affects consumers. This assessment is explained below.

The potential impact on ANZ and ASB is significant but probably not existential

26. Constitutional conventions

27.

Impact on the wider market is of greater concern

28. If smaller, domestically-owned deposit-takers or other lenders are found to have made relevant disclosure failures, they could be affected by the full-forfeiture scenario either because they are required to forfeit large sums or where they need to hold cash against the risk of such forfeiture. Some are co-operative companies and would need to consider raising capital from their customers (who are its shareholders).

29. Smaller lenders are less likely than ANZ and ASB to be able to manage similar losses as a proportion of their balance sheet. A disclosure failure that took years to correct and which affected a large proportion of their loan book could more easily present a threat to their solvency. Lenders who rely more heavily on consumer lending as a revenue source (i.e. whose income is less diversified) would also be more greatly affected than others.

30. The potential impact on small deposit-takers is a particular concern given the important role they play in servicing a diversity of consumers' needs and placing competitive constraint on larger lenders, notably banks. The Commerce Commission recently found a lack of strong competition in the market for the supply of personal banking services[9], which overlaps with the consumer lending market.

31. To the extent a full-forfeiture scenario does affect smaller lenders, it could constrain the availability of credit in two main ways:

    a. affected lenders either exit the consumer lending market or, if they stay, are less able to compete (i.e. put price pressure on their rivals, invest in improving their services, etc.), which may (if the effect is widespread) cause prices to increase overall

    b. affected lenders who stay in the market have reduced lending capacity (i.e. cashflow) and may therefore have to be more selective about who they lend to (which may disproportionately affect borrowers with worse credit histories).

What objectives are sought in relation to the policy problem?

32. The Government's general reform objectives for financial services are as follows:

    a. simplify and streamline regulation of financial services (including reducing duplication)

    b. remove undue compliance costs for financial market participants

    c. improve outcomes for consumers.

33. This issue particularly relates to two of those three wider reform objectives:

    a. *Improving outcomes for consumers* – All consumers stand to be affected if the market for supply of consumer credit is constrained or competition reduced.

    b. *Simplifying regulation* – Although regulation is normally aimed at incentivising beneficial conduct in the present, the fact the law determines consequences for disclosure failures differently depending on how far in the past a disclosure failure occurred potentially runs against the objective of simplification.

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[9] The Commission's final competition report can be accessed here: [Final-report-Personal-banking-services-market-study-20-August-2024-Amended-27-August-2024.pdf]

Section 2: Deciding on an option to address the policy problem

What criteria will be used to compare options to the status quo?

34. We have analysed options against the following criteria:

    a. protects the interests of consumers in connection to credit contracts (including access to credit[10])

    b. facilitates just outcomes (including compliance with legal principles relating to natural justice / procedural rights / constitutional factors)

    c. provides a straightforward and streamlined approach to consequences for lenders.

35. We are weighting each criterion equally. The criteria are intended to elicit key trade-offs and judgments. An explanation of how we are applying each criterion follows. While criterion A) is the primary purpose of the CCCFA, we have weighted this evenly with the other criteria for consistency with our 2024 RIS. Where any policy would require legislation with retrospective effect, careful consideration of legal principles is relevant to the analysis.

A) Protects the interests of consumers

36. This criterion reflects the primary purpose of the CCCFA (see section 3(1)). The main interests we see as relevant to this issue are the interests of all consumers in:

    a. being able to make informed decisions

    b. having access to safe credit by virtue of a well-functioning and competitive market

    c. being protected from the harm that can be caused by irresponsible lending.

37. However, these interests vary for different consumer groups (e.g. are greater for consumers with poor financial literacy or other vulnerabilities). To avoid overlap with the second criterion below, we have not included under this criterion the special interests of borrowers affected by disclosure failures during the 2015-2019 period in receiving redress for those failures over and above any redress that would be just in the circumstances.

B) Just outcomes

38. This criterion concerns the likelihood of the CCCFA producing consequences for lenders that are just, in the sense of being proportionate to the nature and circumstances of the disclosure failure. It also involves analysis of legal principles and conventions relating to retrospectivity[11], including:

    a. the presumption that legislation is prospective

    b. the convention that parliamentary legislation should not generally interfere with the judicial process in particular cases before the courts, and the entitlement of litigants to

[10] Relevant here is the CCCFA's purpose of promoting and facilitating 'fair, efficient and transparent markets for credit'.

[11] See the Legislation Act 2019, section 12 in respect of civil legislation, and the Legislation Design Advisory Committee Guidelines (chapter 12).

have their case determined on the basis of the law as it stood at the time of the events at issue (including their *interest* in their case being so determined).

39. If legislation is being considered that would alter the law at issue in existing proceedings, such legislation should be justified as being in the public interest and impairing the rights of litigants no more than is reasonably necessary to serve that interest.[12]

C) Provides a straightforward and streamlined approach to consequences for lenders

40. This criterion reflects the Government's objective of simplifying regulation of financial services. We have treated it as relevant to our analysis of options given the complexity created by the potential for section 99(1A) to operate differently depending on when a relevant disclosure failure occurred, and the uncertainty this creates for lenders about their liability over time.

What scope will options be considered within?

41. We have identified options directly relevant to the problem of courts lacking explicit discretion to moderate the effect of section 99(1A). As this problem was addressed by reforms in December 2019 (for all disclosure failures not rectified before that time), the options are limited to legislative changes that reach back in time and extend this solution to earlier disclosure failures (i.e. legislation with retrospective effect).

42. We have not considered retrospective repeal of section 99(1A) as an option in this RIS. Cabinet has actively decided to retain this form of redress, but change how/when it is available prospectively as part of the Government's financial services reforms.[13] This followed public consultation and regulatory impact analysis on options that included prospective repeal.

43. We have also not considered retrospective application of the changes recently agreed by Cabinet. They are intended to address a distinct problem, which is concerned with incentives these consequences provide for lenders in the present (and therefore cannot be influenced through retrospective legislation).

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[12] Legislation Design Advisory Committee (chapter 12, part 2).

[13] See recommendation 8 of the Cabinet minute: https://www.mbie.govt.nz/dmsdocument/29098-cabinet-minute-financial-services-reforms-policy-approvals-minute-of-decision-proactiverelease-pdf and MBIE's preferred option in the Regulatory Impact Statement: Fit for purpose consumer credit law (mbie.govt.nz).

What options are being considered?

Option One – the counterfactual

44. As discussed above, on the face of the provision, the courts may be bound to require full forfeiture of the costs of borrowing for a breach of relevant disclosure obligations during the 2015-2019 period, no matter how insignificant the breach.

Options Two and Three – legislative options with retrospective effect

45. Both Options Two and Three involve providing the court with explicit discretion (on application by the lender) to consider whether relief from section 99(1A) (and equivalent provisions) should be provided to the lender based on the nature and circumstances of the disclosure failure, regardless of when the failure took place. In other words, they involve backdating the effect of the reforms that took effect in December 2019.

46. The options differ in terms of whether they affect active litigation or not:

    a. Option Two – Amendment only affects proceedings that have not been filed before the date this policy is announced. Active litigation would run its course, unaffected.

    b. Option Three – Amendment also affects proceedings that have not been finally resolved by the courts before the commencement date.

How do the options compare to the counterfactual against the criteria?

The counterfactual: assessment against the criteria

Interests of consumers

47. The counterfactual risks undermining the long-term interests of consumers in having access to safe credit by virtue of a well-functioning and competitive market. If the full-forfeiture scenario were to arise, and to the extent this outcome spills over to a range of smaller lenders, consumers could be affected by higher borrowing costs and reduced availability of credit (including through reduced competition in the market).

Just outcomes

48. The counterfactual's ability to produce just outcomes appears to be reduced by the absence of explicit discretion for the courts to extinguish or modify the effect of section 99(1A), particularly given that discretion was provided by the 2019 reforms and not applied retrospectively. This may mean the courts are bound to require lenders to forfeit the full costs of the costs of borrowing to all affected borrowers, even where that would be unjust in the circumstances.

49. On the other hand, the counterfactual does not alter any of the legal rights or duties that applied at the time the disclosure failures occurred. It does not offend the presumption against retrospective legislation nor the entitlement of affected borrowers to have disclosure failures dealt with based on the law that applied at the time.

Straightforward and streamlined approach to consequences for lenders

50. Lenders may still have liability for disclosure failures under the pre-2019 law. That liability is uncertain until the courts determine how to apply section 99(1A) under that law. Additionally, lenders face uncertainty about how a court would use its discretion to provide relief from section 99(1A) as a result of the 2019 reforms.

51. Assuming consequences under section 99(1A) are determined differently by the courts under the two time periods, the counterfactual is not particularly straightforward. How redress for a relevant disclosure failure is determined would depend on whether it occurred before or after the 2019 reforms (and, if it occurred before those reforms, whether it was corrected before them).

52. This difference in treatment is likely to be greater the longer it was before the lender identified the failure. Long delays in identifying a failure that occurred before December 2019 make this difference in treatment somewhat arbitrary. Lenders can only determine their liability after the fact, and this involves trying to account for the difference in the law that applied before and after December 2019.

Option Two: comparison with the counterfactual

Interests of consumers

53. We do not know how or whether Option Two would change the way the courts apply sections 99(1A) and 48. This option only increases or makes more explicit their discretion to extinguish or vary the effect of section 99(1A) if they consider it just and equitable to do so. This means it is not possible to compare the impact of this option on the interests of consumers with that of the counterfactual.

54. Nevertheless, we consider it reasonable to assume that Option Two makes it less likely that lenders would be required to forfeit the full costs of borrowing in respect of relatively minor disclosure failures. Therefore, we would expect this option to improve on the counterfactual overall because it reduces the likelihood of negative consequences for consumers that could arise from the full-forfeiture scenario (see discussion at paragraph 31).

55. Option Two does not entirely remove this risk, as it would be open to a court to consider what law applied at a relevant time in deciding what is 'just and equitable' in the circumstances. At the very least, the ability for lenders to seek relief under the 2019 provisions would entitle them to have the particular circumstances of their disclosure failure considered. This would seem to reduce the likelihood of the problem arising.

Just outcomes

56. Option Two improves on the counterfactual in one sense, and performs worse in another.

57. On one hand, providing the courts with explicit discretion to vary or extinguish the effect of section 99(1A) can only improve their ability to reach a 'just and equitable' outcome for all parties. This is the stated purpose of the discretion they may use under section 95A (Court may reduce effect of failure to make disclosure) after considering the factors in section 95B (Guidelines for reducing effect of failure).

58. On the other hand, providing that discretion retrospectively would appear to conflict with the presumption against retrospectivity and relevant legal principles. These principles are not absolute, and our assessment is that the degree of conflict in the case of Option Two is minimal. Option Two would not affect any legal right or duties being asserted in active proceedings. Where Option Two affects any person's legal rights or duties as asserted after its commencement, it only affects them to the extent they would be considered unjust by a court.

Straightforward and streamlined approach to consequences for lenders

59. Option Two would provide greater consistency over how consequences under section 99(1A) are determined over time. It would remove the distinction made under the counterfactual

between how section 99(1A) operates for disclosure failures that pre-dated the December 2019 reforms and how it operates for disclosure failures unresolved or occuring after those refoms. However, to the extent proceedings are brought in relation to disclosure failures prior to December 2019, it would instead create a distinction between how those failures are treated depending on whether proceedings commenced before or after a date specified by Option Two.

60. Option Two could also be seen as making the approach to determining consequences less straightforward, in that it involves greater uncertainty about how a court might use its discretion under section 95A. However, this discretion increases the likelihood of parties settling out of court, without the need for complex court proceedings.

Option Three (preferred by MBIE): comparison with the counterfactual

61. Option Three improves on the counterfactual in largely the same ways as Option Two, with some differences noted as follows:

   a. *Interests of consumers* – Despite also applying to active litigation against ANZ and ASB, Option Three does not materially improve on Option Two in avoiding the consequences of concern under the counterfactual, given that concern is predominantly associated with how a finding in that litigation could disproportionately affect any other lenders/deposit-takers who had compliance issues before December 2019.

   b. *Just outcomes* – By including active litigation, Option Three involves greater potential for a just and equitable outcome than Option Two, but would also appear to involve greater conflict with legal principles. Legal professional privilege [redacted]

      [redacted] [redacted]

      [redacted] [redacted]

      [redacted] [redacted]

Legal professional privilege [redacted]

iv. Legal professional privilege

c. *Straightforward and steamlined approach to consequences for lenders* – Option Three would go further than Option Two in providing a consistent basis for the application of section 99(1A) by including active litigation. Option Two could be considered less streamlined in the sense that it replaces the current pre or post-2019 distinction with a distinction relating to when litigation was brought.

62. In summary, Option Three involves a greater trade-off than Option Two between the interests of borrowers affected by historical disclosure failures (by including those borrowers represented in active litigation) and the wider public interest in having consequences determined in a just and equitable manner, consistently over time.

	Counterfactual: pre-2019 law continues	**Option 2: retrospective amendment excluding active litigation**	**Option 3: retrospective amendment including active litigation**
Interests of consumers	0	+ The potential for impact on consumers' long-term interests arising from a full-forfeiture scenario is made less likely where the court has explicit discretion.	+ Same as for Option 2, given the active litigation has very little potential to negatively affect the interests of consumers.
Just outcomes	0	0 Improves the courts' flexibility to arrive at just outcomes in any **future** litigation concerning pre-2019 failures. Minimal conflict with convention against retrospective legislation.	0 Improves the courts' flexibility to arrive at just outcomes in **current and** any future litigation. Greater, but still minor, conflict with convention against retrospective legislation and other legal principles.
Straightforward approach to consequences	0	0/+ Slightly more straightforward approach than under the counterfactual. However, does not prevent the law differentiating treatment of different disclosure failures.	+ Provides a consistent legal basis for determining consequences irrespective of when the disclosure failure occurred and when proceedings were brought.
Overall assessment	0	+/++	++

What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

63. Our view is that the courts should have explicit discretion to arrive at a just and equitable outcome by extinguishing or reducing the effect of section 99(1A) regardless of whether or not the disclosure failure preceded reforms in 2019.

64. We find it inoffensive to extend this position to active litigation. The fact Option Three would affect proceedings that are before the courts does not put it beyond what might be considered an appropriate use of retrospective legislation. Given Option Three is necessary to put all disclosure failures on the same legal footing, we consider it is justified and impairs the rights of litigants no more than is reasonably necessary.

Key for qualitative judgements:

++	much better than doing nothing/the status quo/counterfactual
+	better than doing nothing/the status quo/counterfactual
0	about the same as doing nothing/the status quo/counterfactual
-	worse than doing nothing/the status quo/counterfactual
- -	much worse than doing nothing/the status quo/counterfactual

What are the marginal costs and benefits of the option?

Affected groups	Comment	Impact	Evidence Certainty
Additional costs of the preferred option compared to taking no action			
Lenders who failed to make disclosures as required	None identified	N/A	N/A
Borrowers affected by these failures	Less likelihood of borrowers being awarded the full costs of borrowing in relation to the period in question where the circumstances and nature of the disclosure failure do not justify this outcome.	Unknown. However, to illustrate the maximum potential costs of borrowing (before deducting compensation already paid), someone with a $500,000 mortgage may have paid in the order of $120,000 in interest over four years.	Low. The potential for a difference in outcome is assumed, but depends how the current law and proposed change would be applied by the courts.
Consumers generally	None identified	N/A	N/A
The regulator	Potential for some disruption to enforcement activities relating to the relevant period.	Low.	Low. This is a possibility the Commerce Commission has raised.
Total monetised costs	N/A	N/A	N/A
Non-monetised costs	As above	Unknown	Low
Additional benefits of the preferred option compared to taking no action			
Lenders who failed to make disclosures as required	Potential for reduced/avoided losses arising from these failures	Unknown. However, could be significant if there is a material difference between what amount a court would award under the counterfactual and what it would award under the preferred option.	Low. The potential for a difference in outcome is assumed, but depends how the current law and proposed change would be applied by the courts.
Borrowers affected by these failures	As below	As below	As below
Consumers generally	Less potential for future supply of consumer credit to be negatively affected	Unknown.	Low. The likelihood and scale of the threat to the market is highly uncertain and requires speculation.
The regulator	None identified	N/A	N/A
Total monetised benefits	N/A	N/A	N/A
Non-monetised benefits	As above	Unknown	Low

Section 3: Delivering an option

How will the new arrangements be implemented?

65. The preferred option would require changes to the CCCFA. The legislative vehicle for the amendment will be a CCCF Amendment Bill that is likely to be introduced to Parliament in early 2025.

66. There will be an opportunity to reconsider aspects of this proposal in view of submissions made during the select committee process for the Bill. This Bill will also contain the prospective amendments to section 99(1A) agreed by Cabinet in September 2024.

67. We consider it unlikely that the active proceedings could be finally disposed of before this Bill is passed. The Minister is committed to having this Bill passed as quickly as possible given the uncertainty it creates for staff affected by the transfer of regulatory functions from the Commerce Commission to the Financial Markets Authority, and for industry.

68. We see no reason to delay commencement of this change once the Bill is passed.

69. The Commerce Commission entered into full and final settlements with several lenders for disclosure breaches during the 2015-2019 period. It also has some open investigations following complaints and self-reports of potential issues with relevant disclosure requirements over this period. We will work with the Commission to manage any impacts of the policy change.

How will the new arrangements be monitored, evaluated, and reviewed?

70. Our approach to monitoring, evaluating and reviewing the preferred option would be consistent with that being used for other consumer credit law reforms being implemented through the same legislation. This was outlined in the original RIS[15] and includes the Financial Markets Authority's role in monitoring and responding to market conduct issues and enforcing the CCCFA. It also includes an intention to review these reforms in 3-5 years following commencement (subject to resource constraints).

71. No new data collection activity specfic to this amendment is proposed at this stage but will be considered if issues arise.

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[15] This RIS can be found here: https://www.mbie.govt.nz/dmsdocument/29099-regulatory-impact-statement-fit-for-purpose-consumer-credit-law

Appendix one: Laws determining consequences of the relevant disclosure failures over time

Time period	Law that operates	Relevant sections	Which disclosure failures this law applies to
Before 6 June 2015	The law provided only that the loan agreement would be unenforceable until disclosure is correctly made. In the *Norfolk Nominees Ltd v King 2013* case, the High Court found this meant the lender had no enforceable right to interest and fees during the period of the lender's non-compliance, but that they could recover interest and fees from that period once non-compliance is corrected.	99(1), 48	Any disclosure failure that arose from an agreement entered into before 6 June 2015.
6 June 2015 – 20 December 2019	The borrower is not liable for the costs of borrowing during any period of non-compliance with initial and agreed variation disclosure requirements (and likewise for consumer leases and buy-back transactions for land). The courts have no clear discretion to deviate from this outcome.	99(1), 48 99(1A), 101(2) and 102(2)	Any disclosure failure that arose from an agreement entered into on or after 6 June 2015, to the extent it was not corrected before 20 December 2019.
20 December 2019 – commencement of reforms agreed by Cabinet in 2024	The lender (lessor or transferee) can seek relief from the effect of section 99(1A) and the court then considers a range of factors in deciding whether it is just and equitable to grant that relief (by either extinguishing or reducing the effect of the provisions).	99(1), 48 99(1A), 101(2), 102(2), 95A and 95B	Any disclosure failure that was not corrected before 20 December 2019 or occurred after that date, relating to any loan agreement entered into before the commencement of reforms agreed by Cabinet in 2024.
After commencement of reforms agreed by Cabinet in 2024	Same as the law prior to 6 June 2015, except that it would be possible to seek an order for redress comprising any or all of the costs of borrowing where a court finds a person suffered loss or damage from a breach of initial or agreed variation disclosure.	99(1), 48, 93 and 94 (as amended by the Bill)	Any disclosure failure that relates to a loan agreement entered into after the commencement date.
The preferred option would eliminate the 6 June 2015 – 20 December 2019 law by extending the application of the law that applies after that period back in time.			

In Confidence

Office of the Minister of Commerce and Consumer Affairs

Chair, Cabinet Economic Policy Committee

Financial Services Reforms: policy approvals and approval of the Credit Contracts and Consumer Finance Amendment Bill for introduction

Proposal

1. This paper is one of two papers seeking to progress the Government's Financial Services Reforms. This paper seeks approval for:

   1.1. some additional policy changes to be included in the Credit Contracts and Consumer Finance Amendment Bill (the **Bill**), and

   1.2. introduction of the Bill, which gives effect to these policy changes, as well as policies earlier approved by Cabinet.

Executive Summary

2. I am seeking to introduce bills implementing a package of reforms to financial services regulation. This includes changes to consumer credit regulation agreed by Cabinet, which are being given effect by a Credit Contracts and Consumer Finance Amendment Bill (the **Bill**).

3. The Bill streamlines conduct regulation by transferring regulatory functions under the Credit Contracts and Finance Act 2003 (**CCCFA**) from the Commerce Commission (**the Commission**) to the Financial Markets Authority (**FMA**) and aligning the regulatory model with that used for other financial markets. This includes transitioning consumer credit to a licensing model and equipping the FMA with regulatory tools that will support it to regulate consumer credit effectively, in the interests of consumers, and without unnecessary regulatory burden on lenders.

4. The Bill includes some further changes for which I am seeking Cabinet approval, including a retrospective amendment relating to consequences for historical disclosure breaches by lenders.

5. The Minister of Commerce and Consumer Affairs at the time made Cabinet aware when seeking approval for the majority of consumer credit policy changes that he would be taking further advice on this historical issue. The proposed solution is to backdate reforms made in 2019 that ensure the courts have the flexibility they need to determine what consequences would be just and equitable in the circumstances of the disclosure breach.

6. This would apply equally to active class litigation against ANZ and ASB, which is likely to involve perceived interference with procedural rights of those borrowers. However, this is necessary to ensure consequences for all disclosure failures from that period can be decided appropriately and on the same basis.

Policy

Cabinet has agreed to a range of reforms to financial services regulation

7. In 2024, the Government made a series of policy decisions aimed at streamlining and improving the effectiveness of three types of financial services regulation:

- consumer credit regulation (the subject of this paper);
- financial services conduct regulation; and
- financial dispute resolution schemes.

8. As part of the series of policy decisions, Cabinet agreed to transfer all regulatory functions under the CCCFA from the Commission to the FMA [EXP-24-MIN-0010 refers].

9. Following public consultation [CBC-24-MIN-0031 refers], Cabinet agreed to a range of reforms in September 2024, including to the CCCFA [ECO-24-MIN-0178 refers]. In November 2024, Cabinet agreed to further policy changes to consumer credit legislation [CAB-24-MIN-0445 refers].

Policy changes to consumer credit regulation provide a more effective regulatory model for the Financial Markets Authority

10. Policies so far agreed by Cabinet are largely focussed on ensuring the FMA will be well-equipped to regulate consumer credit effectively in the interests of consumers, while ensuring the regulatory burden on lenders is proportionate. They include:

Transferring responsibility to the FMA and streamlining regulation

10.1. transferring all regulatory functions under the CCCFA to the FMA;

10.2. replacing the current certification requirement for lenders and mobile traders with the market services licensing regime in the Financial Market Conduct Act 2013 (**FMC Act**), and deeming most existing entities to hold a relevant licence;

10.3. applying other aspects of the FMC Act to consumer credit regulation (e.g. stop order powers);

10.4. empowering the FMA to make adjustments or clarifications to the scope of CCCFA obligations through declarations and exemptions in particular circumstances;

Removing excessive penalties

10.5. removing the due diligence duty and attendant personal liability for senior managers and directors under the CCCFA (on the basis adequate accountability and oversight of compliance will be provided by the licensing regime); and

10.6. limiting the effect of section 99(1A) of the CCCFA (that a borrower is not liable for the costs of borrowing in relation to a period of non-compliant disclosure) to disclosure breaches that a court finds have caused harm.

11. To give effect to these policies, the Bill amends the CCCFA, the Financial Markets Authority Act 2011, the FMC Act, the Financial Markets Conduct Regulations 2014 (**FMC Regs**), and the Financial Service Providers (Registration and Dispute Resolution) Act 2008 (**FSP Act**), and makes other consequential amendments.

12. Industry has generally responded well to the consumer credit reforms that were announced following consultation. Other stakeholders also appear optimistic about the Government's intention to ensure the FMA is equipped to regulate consumer credit effectively. Concerns with particular proposals do not seem to be significant at this stage.

I am seeking further approvals consistent with the aims of consumer credit reforms…

Ensuring the FMA has effective regulatory tools: stop order and direction order powers

13. Cabinet agreed to CCCFA disclosure breaches being grounds for the FMA to issue a stop order. I am now seeking agreement to make stop order and also direction order powers available to the FMA for breach of any obligation under the CCCFA.

14. These are administrative powers the FMA has under the FMC Act to intervene where it has relatively serious concerns about a regulated party's conduct. They allow the FMA to respond proportionately to harm, do not rely on court proceedings, and provide consistency between how misconduct can be addressed under the CCCFA and FMC Act. The FMA might consider use of a direction order, for example, to prevent further immediate harm being caused by a lender whose disclosure statements contain misleading information about the interest rate applying to the loan.

15. Any breach of the CCCFA could have instances that justify use of these interventions, and I consider it best to afford the FMA flexibility to judge when intervention of this kind is appropriate.

Ensuring the courts have appropriate discretion over consequences for historical disclosure failures: retrospective change to section 99(1A) ***[contains legal advice]***

16. I am seeking approval for an amendment with retrospective effect to address a legacy problem with section 99(1A) of the CCCFA. When seeking policy approvals for financial services reforms in August 2024, the Minister of Commerce and Consumer Affairs at the time notified Cabinet that he would be taking further advice on this issue.

17. Section 99(1A) provides that borrowers are not liable for the costs of borrowing during a period where a lender has breached certain disclosure requirements. The CCCFA has equivalent provisions for consumer leases and buy-back transactions for land.

18. The proposed amendment would ensure the courts are empowered to reduce or extinguish the effect of these provisions where they consider it just and equitable to do so – in other words, if necessary to avoid consequences that would be grossly disproportionate in the circumstances. This discretion was provided in 2019, but was not applied retrospectively to the costs of borrowing pre-2019. This means the consequences for disclosure failures that pre-date the 2019 reforms are determined differently, and the court may be bound to require the lender to refund the full costs of borrowing to all affected borrowers in those cases.

19. There are still concerns about compliance issues lenders may have had before the 2019 reforms. Concerns about the potential consequences of the pre-2019 law on the consumer lending market have increased in recent years, because of active class litigation against ANZ and ASB. My officials are particularly concerned about the potential knock-on impact this could have on the position of smaller, domestic lenders.

20. Addressing these concerns through retrospective legislation is likely to attract criticism, Legal professional privilege [redacted] and consistent with the objectives of these reforms (e.g. simplification) to apply that position equally to the active class litigation, rather than have a different law apply uniquely to that case.

21. Legal professional privilege [redacted]

22. This amendment is different from the reforms Cabinet agreed in September 2024 to how consequences under section 99(1A) are determined (limiting them as noted in paragraph 10.6.). Those reforms tackle a different problem, which is not related to past conduct. They would therefore apply only prospectively (i.e. to agreements entered into after commencement).

23. The Bill includes this retrospective amendment, subject to Cabinet's approval, as the Minister obtained the Attorney-General's agreement to have it drafted in advance.

Less significant improvements to effectiveness and workability: minor and technical changes

24. On 28 August 2024, the Minister at the time indicated to Cabinet (via the Cabinet Economic Policy Committee) that he would consider Regulatory Systems Bill proposals for inclusion in this Bill. Cabinet authorised him to make additional policy decisions and minor or technical changes, consistent with the policy intent of the paper, on issues that arise during the drafting of the Bills and Regulations [ECO-24-MIN-0178 *refers*].

25. The amendments that are considered minor and technical have been included in the Bill (and are outlined in **Annex One**). They are mostly concerned with adjusting definitions and refining the scope of obligations in the CCCFA to better reflect the

policy intent. I am seeking approval for these changes because they are not directly related to previous Cabinet decisions.

Impact Analysis

26. A Regulatory Impact Statement was prepared in accordance with the necessary requirements and was submitted at the time that Cabinet approval of the policy relating to the Bill was sought [ECO-24-MIN-0178 refers].

27. When further policy decisions were sought, it was determined these proposals are exempt from the requirement to provide a Regulatory Impact Statement on the grounds they have no, or only minor, impacts on businesses, individuals, and not-for-profit entities [ECO-24-MIN-0262 refers]. An exemption on the same grounds was also given for the minor and technical changes in Annex One.

28. A quality assurance panel with representatives from the Ministry of Business, Innovation and Employment has reviewed *Regulatory Impact Statement: Whether to apply legislation retrospectively to give courts discretion when considering consequences for disclosure failures by lenders*. The panel has determined that the RIS meets the quality assurance criteria.

Compliance

29. The Credit Contacts and Consumer Finance Amendment Bill complies with:

    29.1. the principles of the Treaty of Waitangi;

    29.2. the rights and freedoms contained in the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993;

    29.3. the principles and guidelines set out in the Privacy Act 2020;

    29.4. relevant international standards and obligations; and

    29.5. the Legislation Guidelines (2018 edition), which are maintained by the Legislation Design and Advisory Committee.

30. A disclosure statement has been prepared and is attached to the paper.

Human rights implications

31. The Bill includes an amendment (discussed above) with retrospective effect, which would afford the courts discretion in determining consequences for certain disclosure failures. As this amendment would affect proceedings commenced before it takes effect, notably active representative proceedings, consideration has been given to implications for the right to natural justice, as well as certain legal principles and conventions relating to retrospectivity.

Consultation

Consultation on policy changes already considered by Cabinet and this paper

32. Following Cabinet approval in May 2024, the Ministry of Business, Innovation and Employment (**MBIE**) publicly consulted on options for reform over four weeks. MBIE considered 37 submissions from a range of stakeholders such as banks, other lenders, representatives of borrowers, and law firms.

33. MBIE consulted with the Commission, the FMA, the Treasury, the Reserve Bank of New Zealand, the Ministry of Justice, and the Ministry for Regulation during policy development and on this paper. The Department of the Prime Minister and Cabinet was informed when proposals were submitted to Cabinet [ECO-24-MIN-0262] and of this paper.

External consultation on further approvals in this paper

34. MBIE conducted targeted consultation with stakeholders on the minor and technical changes.

35. MBIE worked with banks to understand the historical problem with s99(1A) but was not able to consult on the proposed solution.

Binding on the Crown

36. The CCCFA binds the Crown. The Bill does not change this.

Creating new agencies or amending law relating to existing agencies

37. The Bill does not create any new agencies. It amends laws that determine the functions of existing Crown Entities, given the Bill transfers responsibility for regulation of consumer credit from the Commission to the FMA. It consequentially amends the Financial Markets Authority Act 2011, though not materially.

Allocation of decision-making powers

38. The Bill does not involve allocation of decision-making powers between the executive, the courts, and tribunals.

Associated regulations

39. Secondary legislation will be needed, and will commence at the same time as the relevant provisions of the Bill, to ensure those provisions can be given proper effect.

40. The exemptions in Regulations 27 and 28 of the Credit Contracts and Consumer Finance Regulations 2004 will be carried over to the Financial Markets Conduct Regulations 2014. Cabinet has already approved this change as a consequence of the move to the licensing regime [ECO-24-MIN-0178 refers].

41. Amendments to the Financial Markets Conduct (Fees) Regulations 2014 will also be required. This is to set a licensing fee for all providers of consumer credit contracts

and mobile traders that enter the market after the licensing regime commences. The Bill already 'deems' existing providers to hold a licence at no cost.

42. These regulations will be drafted separately to the Bill, requiring Parliamentary Council Office and MBIE to allocate a low amount of resources to this. The drafting will be completed after introduction of the Bill.

Other instruments

43. Clause 46 of the Bill empowers the FMA to make declarations and exemptions that would be secondary legislation. The provision would enable the FMA to change or clarify the scope of the CCCFA's application, but are subject to constraints designed to ensure they are only used to resolve less significant issues and in a manner consistent with the Legislation Design and Advisory Committee guidelines.

44. The departmental disclosure statement referenced in the explanatory note to the Bill sets out the reasons for these powers.

Definition of Minister/department

45. The interpretation section 5 of the Bill borrows the original definition of "FMA" from the Financial Markets Authority Act 2011 for the purposes of transferring functions to the FMA.

Commencement of legislation

46. Some provisions of the Bill would come into force immediately. The provisions relating to or reliant on the transfer of functions to the FMA would come into force by Order in Council (with a backstop of six months after Royal assent). This flexibility is necessary to support agencies in planning for implementation. If the Bill is enacted by the end of October 2025, I intend to bring a commencement order to Cabinet bringing these provisions into force by year's end.

Parliamentary stages

47. I intend to introduce all three Bills on 31 March 2025. I intend to seek Business Committee agreement to associate these three Bills for First Reading to save House time.

48. I propose the Bills should be passed no later than October 2025. Confidential advice to Government [redacted]

49. I propose the Bill be referred to the Finance and Expenditure committee for a period of five months.

Proactive Release

50. I propose to proactively release this paper on MBIE's website, subject to any redactions that may be required consistent with the Official Information Act 1982, within 30 business days of its consideration.

Recommendations

I recommend that the Cabinet Economic Policy Committee:

1. Confidential advice to Government

2. **note** that the Bill simplifies and streamlines regulation of financial services by aligning the regulator and model for regulation of consumer credit with that for other financial markets;

3. **note** that I will be returning to Cabinet while the Bill is before the House seeking approval for regulations relating to licensing fees and exemptions to be made;

4. **agree** to amend the Credit Contracts and Consumer Finance Act 2003 (the CCCFA) to apply sections 95A and 95B retrospectively, so that a court is able to provide relief from sections 99(1A), 101(2) and 102(2) regardless of when the disclosure failure occurred, and to actively apply this change to any relevant proceedings that have not been finally disposed of;

5. **agree** to the minor and technical changes included in the draft Bill (as set out in Annex one)

6. **agree** that, in addition to the situations earlier agreed by Cabinet, the FMA be empowered to make direction orders and stop orders as a possible response to breach of any obligation under the CCCFA;

7. **approve** the Credit Contracts and Consumer Finance Amendment Bill for introduction on 31 March 2025;

8. **agree** that the Government propose the Bill be:

    8.1. referred to the Finance and Expenditure committee for consideration;

    8.2. Confidential advice to Government

Authorised for lodgement

Hon Scott Simpson

Minister of Commerce and Consumer Affairs

Annex One: Minor and technical changes

#	Category	The status quo	Proposed change
1	Technical change to a definition	Trustees of a trust and partners in a partnership are not excluded from the definition in section 5 of a "guarantor" in relation to a credit contract. However, these parties are excluded from the application of other provisions of the Credit Contracts and Consumer Act 2003 (the Act), such as the definition of "consumer credit contract" (where they are borrowers) and under lender responsibility principles (where they are guarantors).	Amend the requirements for guarantors (and definition in section 9B) so they consistently exclude trustees of a trust or persons acting as a partner under the Partnership Law Act 2019.
2		One of the types of repayment waiver offered by lenders (an insurance shortfall repayment waiver) does not appear to fall within the scope of the Act as it doesn't meet the definition of either a "repayment waiver" or "credit-related insurance". An insurance shortfall repayment waiver (offered by lenders) waives payments if there is a shortfall between the amount owing on the borrower's credit contract and any amount paid out by the borrower's comprehensive insurer if there is a total loss on the vehicle (effectively providing the same cover as guaranteed asset protection (GAP) insurance, which is offered by insurers).	Extend the definition of "repayment waiver" in section 5 of the Act to include an insurance shortfall repayment waiver.
3		Section 9C(8) defines "material changes" to consumer credit contracts for the purposes of section 9C(3)(a).	Clarify that some transactions that result in a mortgage amount being increased because of property-related payments the lender is required or entitled to make on the borrower's behalf, are not "additional advances" requiring a suitability and affordability assessment (eg where a lender pays local government rate arrears).
4		While section 27 of the Act provides the right for consumers to cancel their credit contract within a prescribed period, there is no similar cancellation requirement for repayment waivers under the Act. Under section 9B(4), repayment waivers and extended warranties that are financed under a consumer credit contract are to be treated as forming part of the agreement for the purposes of the lender responsibility principles (Part 1A). However, this treatment does not extend to the rest of the Act, including section 27.	Amend section 27 of the Act to expressly provide for a consumer right to cancel a repayment waiver and extended warranty within five working days.
5		Section 132A(6) requires disclosure of certain information before debt collection begins. It excludes the sending of a "payment reminder" from counting as debt collection, and defines this as "a communication that is made within 5 months of a default in payment; only requests a payment that is overdue[…]"	Amend section 132A to exclude disclosure from being required where the lender is merely making the borrower aware they have exceeded a credit limit and/or requesting the limit be restored (on the same basis as the current exclusion of a notice that a payment is overdue).
6		In this section, a debt collector includes anyone engaging in an act to recover (or attempt to	Amend s132A(4) to provide additional

#	Category	The status quo	Proposed change
		recover) debt that is owing under a credit contract as a result of the borrower's breach of that contract. Theoretically, this could include parties, not acting for the lender, who contact the borrower about their debt, such as a guarantor or financial mentor. Section 132A(3) requires that disclosure must be made (again) within 10 working days by anyone who becomes a debt collector after debt collection starts.	exclusions from the definition of 'debt collector'. This exclusion should include some third parties such as financial mentors and guarantors, with the ability to extend this to other parties in future by regulations (for future-proofing purposes).
7	Clarification of policy intent	Section 22 requires information to be disclosed to borrowers about an agreed change to the loan agreement. The default position in that section is that disclosure must be made before the change to the agreement takes effect. However, section 22(3) enables disclosure to be made shortly after the fact in certain situations, including where the change would only reduce the borrower's obligations.	Clarify in section 22(3) that this includes other changes that are likely to the borrower's clear advantage, specifically: a temporary reduction (of no more than three months) in the amount of repayments required, such that any impact on the total interest payable is immaterial.
8		Section 132A provides that before debt collection starts, the debt collector must ensure that appropriate disclosure has been made to the borrower under the contract.	Exclude customers from debt collection disclosure requirements for actions taken under the Insolvency Act 2006, with the ability to exclude other cases by regulations (for future-proofing purposes).
9	Changes to practical application of provisions	Section 15(1) sets out contracts which are not consumer credit contracts regulated by the Act, including "a credit contract under which the debtor is a trustee acting in his or her capacity as a trustee of a family trust". A family trust is defined as "a trust that is established primarily to benefit either or both of the following: (a) a natural person for whom the settlor has natural love and affection; (b) an organisation or a trust whose income is exempt under section CB 4(1)(c) or (e) of the Income Tax Act 1994". This is a bespoke definition in the Act that requires lenders to investigate whether the terms of the trust are as described above.	Provide that the exclusion under section 15(1) applies to all express trusts within the meaning of the Trusts Act 2019, rather than just those currently described by the Act as a family trust.

LEG-25-MIN-0041

Cabinet Legislation Committee

Minute of Decision

Credit Contracts and Consumer Finance Amendment Bill: Policy Approvals and Approval for Introduction

Portfolio **Commerce and Consumer Affairs**

On 27 March 2025, the Cabinet Legislation Committee:

1 **noted** that a Confidential advice to Government

2 **noted** that the Bill simplifies and streamlines regulation of financial services by aligning the regulator and model for regulation of consumer credit with that for other financial markets;

3 **noted** that the Minister of Commerce and Consumer Affairs will be returning to Cabinet while the Bill is before the House seeking approval for regulations relating to licensing fees and exemptions to be made;

4 **agreed** to amend the Credit Contracts and Consumer Finance Act 2003 (the CCCFA) to apply sections 95A and 95B retrospectively, so that a court is able to provide relief from sections 99(1A), 101(2) and 102(2) regardless of when the disclosure failure occurred, and to actively apply this change to any relevant proceedings that have not been finally disposed of;

5 **agreed** to the minor and technical changes included in the draft Bill (as set out in Annex One under LEG-25-SUB-0041);

6 **agreed** that, in addition to the situations earlier agreed by Cabinet, the Financial Markets Authority be empowered to make direction orders and stop orders as a possible response to breach of any obligation under the CCCFA;

7 **approved** the Credit Contracts and Consumer Finance Amendment Bill [PCO 26160/4.0] for introduction by 31 March 2025;

8 **agreed** that the Government propose the Bill be:

8.1 referred to the Finance and Expenditure committee for consideration;

8.2 Confidential advice to Government

Tom Kelly
Committee Secretary

Attendance: (See over)

Present:
Rt Hon Winston Peters
Hon David Seymour
Hon Paul Goldsmith
Hon Louise Upston (Chair)
Hon Brooke van Velden
Hon Judith Collins KC
Hon Tama Potaka
Hon Casey Costello
Hon Nicole McKee
Hon Chris Penk
Hon James Meager
Hon Scott Simpson
Jamie Arbuckle, MP
Todd Stephenson, MP

Officials present from:
Officials Committee for LEG
Ministry of Business, Innovation and Employment