

Submission

to the

Ministry of Business, Employment
and Innovation

on the

Exposure draft of Credit Contracts and
Consumer Finance Amendment
Regulations (No 2) 2022 and updated
Responsible Lending Code

20 October 2022

About NZBA

1. The New Zealand Bankers' Association (**NZBA**) is the voice of the banking industry. We work with our member banks on non-competitive issues to tell the industry's story and develop and promote policy outcomes that deliver for New Zealanders.
2. The following eighteen registered banks in New Zealand are members of NZBA:
 - ANZ Bank New Zealand Limited
 - ASB Bank Limited
 - Bank of China (NZ) Limited
 - Bank of New Zealand
 - China Construction Bank
 - Citibank N.A.
 - The Co-operative Bank Limited
 - Heartland Bank Limited
 - The Hongkong and Shanghai Banking Corporation Limited
 - Industrial and Commercial Bank of China (New Zealand) Limited
 - JPMorgan Chase Bank N.A.
 - KB Kookmin Bank Auckland Branch
 - Kiwibank Limited
 - MUFG Bank Ltd
 - Rabobank New Zealand Limited
 - SBS Bank
 - TSB Bank Limited
 - Westpac New Zealand Limited

Introduction

NZBA welcomes the opportunity to provide feedback to the Ministry of Business, Innovation and Employment (**MBIE**) on the Exposure Draft of Credit Contracts and Consumer Finance Amendment Regulations (No 2) 2022 and updated Responsible Lending Code (**Exposure Draft**). NZBA commends the work that has gone into developing the Exposure Draft.

Contact details

3. If you would like to discuss any aspect of this submission, please contact:

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Summary

We appreciate MBIE's engagement with NZBA and its members on the proposed changes to the CCCFA Regulations and the Responsible Lending Code (**Code**). We support the intent behind the proposed changes, to address the unintended consequences of the December 2021 amendments, and improve safe access to credit for consumers.

However, we consider that some current drafting may not achieve this intent. We set out our feedback on the drafting in line with the intent of the policy decisions and, where relevant, how we think consumer protection could be improved through alternative drafting. Our alternative drafting is contained in the appendix to this submission.

To realise any benefits from the proposed changes, lenders will need to make significant changes to technology, systems and processes, and train frontline teams, requiring time to implement. Consumers and mortgage advisors will expect lenders to have implemented these changes by the time they take effect in March. It is critical that these changes are finalised and communicated to lenders as soon as possible and, at the latest, before the Christmas shut-down period.

Treatment of Discretionary expenses

We support the aims of paragraph 18 of the consultation and the proposed simplification of the definitions of 'listed outgoing' and 'relevant expenses' in Regulation 4AE. Additionally, we appreciate being provided with options for draft Code guidance.

NZBA does not support Option 1 of that Code guidance. We broadly support Option 2, but propose a few drafting changes below.

Comments on Option 1

Option 1 is unlikely to support Cabinet's intention to reduce the information sought from most borrowers and mitigate disproportionate or unreasonable enquiries. The expenses that could still be considered at "significant risk" of not being discretionary, based on the proposed Code guidance, would still require lenders to make broad enquiries. Further, more detailed enquiries would then be needed to discount those expenses later. This effectively results in a two-step approach and would also increase, rather than reduce, the time required to assess expenses. The proposed guidance will exacerbate rather than address the current issues experienced by customers when applying for credit.

Comments on Option 2

We believe Option 2 more closely aligns with the outcomes Cabinet is seeking. Option 2 better allows lenders to reduce the extent of initial inquiries made into a customer's discretionary expenses while also ensuring that the borrower's individual circumstances are considered.

We acknowledge the risk stated by MBIE at paragraph 16 of the consultation regarding lenders taking a 'blanket approach' to discretionary expenses. However, the guidance provided in the Code, 'unless the lender has reason to believe that this is not correct for a particular borrower', provides sufficient guardrails and expectations for lenders. That guidance will mitigate the risk, with the overarching requirements in section 9C of the CCCFA.

We recommend some drafting changes in the appendix to both the draft regulations and Code guidance, with explanatory comments.

Treatment of Credit Card and Buy-Now-Pay-Later Expenses

We have provided separate comments on the proposals for the treatment of credit cards and buy now pay later schemes because the implications of the proposals on these facilities are materially different.

Credit cards

We appreciate Cabinet's intent to reduce the potential for double counting of expenses in relation to some credit cards. However, we don't believe that any double counting caused by the existing Regulations is causing a significant issue for consumers and changes may remove a layer of necessary consumer protection. We are concerned that the proposal, as drafted, may have the potential for customer harm by underestimating the borrower's likely relevant expenses and may not meet the test in s9C(3)(a)(ii).

A borrower may currently use their credit card in the 'transactional' way described in paragraph 22 of the consultation. But, that borrower will also have a pool of available credit which could develop into a substantial debt. For example, if their circumstances change (e.g., job loss or matrimonial separation) or circumstances dictate they change the way they use their card.

The proposed drafting of 4AL(2A) does not protect against this risk. A borrower may encounter substantial hardship or have a change in circumstances that they aren't reasonably able to predict at the point of the lending application. Not accounting for this risks customer harm should the customer's position deteriorate.

The proposed drafting also creates a two-tier system between lenders who comply with the Australian Prudential Regulation Authority's guidance and those who don't, as acknowledged in paragraph 25 of the consultation paper. The potential to more easily switch between lenders could cause vulnerable borrowers to seek credit under less stringent affordability criteria, when a more appropriate approach would have been to approach their existing lender for support.

We believe the existing position in 4AL remains appropriate and do not recommend the Regulations are amended and we believe there are other ways in which Cabinet's intent can be achieved as set out below.

Buy-Now-Pay-Later

In our view, the proposed addition of subclause 4AL(2B) will not achieve Cabinet's intended outcome. We consider that the current drafting will result in a material over or under-estimation for relevant expenses.¹

We instead suggest clarification is provided in the Code to permit lenders to use an appropriate approach in 4AL(2) given the unique features of BNPL schemes, including:

- They have a short repayment term of a maximum of 6 weeks.
- Customer credit limits are often not ascertainable (the limit is often unknown by the customer as it is not disclosed by the provider and is not required to be).
- BNPL schemes do not all provide reporting to Credit Bureau Agencies.
- The facilities may be used once only or used by the customer on a revolving basis for varying amounts.
- The expenses associated with the use of the BNPL products may have likely already been captured in the borrower's living expenses.

Careful consideration needs to be given to whether BNPL arrangements are to be treated as debts or expenses. There are dependencies in this regard on the work RBNZ is undertaking presently in relation to debt-to-income ratios. To the extent it hasn't already, we recommend MBIE liaises with RBNZ so that there is a consistent approach in relation to the treatment of BNPL arrangements going forward.

We also note MBIE's separate consultation on the BNPL regulation more generally, and encourage MBIE to consider changes and impacts holistically.

Variations and replacements of existing credit contracts

We support and acknowledge the intent of widening the exemption in Regulation 4AH to allow refinancing of contracts with other lenders. However, our members have formed differing views on which option is preferred.

Regardless of which option is chosen, members do believe changes are needed to ensure consumer protection remains robust and ensure any exemption is practical.

In particular, we note:

¹ For example, if the customer at the time of application has a \$600 BNPL debt the proposals would require us to assume this debt would continue at the repayment value for the next 12 months. In fact, the customer will have repaid within 6 weeks which overestimates the expenses they may incur. Alternatively, by spreading the cost to repay \$600 over 12 months, when this is actually payable within 6 weeks, we underestimate the expenses they incur over that shorter period. The customer may also at any time after the application incur more BNPL liabilities within their existing limit (which wouldn't be accounted for under the proposal) or increase their BNPL limit or incur more BNPL liabilities, furthering underestimating relevant expenses.

- Option 1 is broad and will go beyond supporting borrowers who may be facing financial difficulties caused by higher cost debt. Option 1 will apply to any re-finance arrangement where the monthly repayments under the new credit contract will be equal to or lower than existing monthly repayments.

The option would improve flexibility for consumers to move lenders where affordability can be assumed because the consumer will be paying less each month. But without appropriate guiderails as to the nature of inquiries that should be made, this approach could undermine the policy intent of the CCCFA Regulations and create consumer harm. While some members did not support this option, all members agree if the option is implemented then tighter criteria should be imposed on how lenders use the exemption, and we've suggested some drafting in the Appendix.

- Option 2 is narrower and will only allow a re-finance where this is necessary to address a borrower's financial difficulties and the borrower's credit limit will not increase. However, the option includes an overly complex and impractical daily interest rate calculation, which could create an unnecessary barrier to lenders providing practical support to customers in time of need. Again, if this option is chosen, we've suggested some drafting the Appendix.

We note that neither Option 1 nor Option 2 address the situation where lenders need to provide emergency credit to borrowers where there are regional or national events, like natural disasters or COVID. In those situations, lenders, acting responsibly, should be able to support consumers by providing emergency, low-value overdrafts or other lending, to help with immediate needs. We strongly suggest widening Regulation 4AH to incorporate this scenario for registered banks.

Proposed drafting amendments

Content	Comment
Discretionary Expenses – Regulations	
<p>Regulation 4AE definition of 'listed outgoings', replace paragraph (d) with:</p> <p>'any regular or frequently recurring outgoings (for example, tithing or remittances) that are material to the estimate of relevant expenses, excluding savings and investments'</p>	<p>We question whether including these examples here is necessary. Given these expenses may be discretionary, we recommend removing these as examples. This is consistent with the removal of the gym memberships and entertainment costs examples.</p> <p>If this wording is retained, replace or define the term 'remittances'.</p> <p>A 'remittance' usually means a payment from one party to another, usually to pay an invoice or bill. Given draft content for the Responsible Lending Code, we understand 'remittance' is intended to refer instead to a transfer or gift of money to family, usually from someone working overseas to family back home.</p> <p>We suggest using the term 'gifts or money transfers to family overseas'.</p>
<p>Regulation 4AE definition of 'relevant expenses', insert paragraph (aa):</p> <p>'may exclude discretionary expenditure <u>any listed outgoings that are discretionary and</u> that a responsible lender would <u>could</u> reasonably expect the a borrower to cease <u>or reduce</u> if they were at risk <u>likely to suffer</u> substantial hardship'</p>	<p>We suggest strengthening the intent to create an objective test for the exclusion of discretionary expenses by replacing the term 'the borrower' with 'a borrower'.</p> <p>We also note that the term 'discretionary expenditure' is undefined. We think it may be better to refer back to the definition of 'listed outgoings' in this context (which is defined).</p> <p>We suggest replacing 'would' with 'could' to reflect that it is context specific and not definitive.</p>

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	<p>We suggest replacing 'at risk of' with 'likely to suffer', to align with the terminology used in s 9C(3)(a).</p> <p>We suggest adding 'or reduce', to align with the guidance proposed at paragraph 5.10 of the Code.</p>
<p>New Regulation 4AM(2A):</p> <p><u>'Regulation 4AM(2) does not apply to the remaining amount of an expense that a borrower tells a lender they could or would reduce if they were likely to suffer (see regulation 4AE(ab)).'</u></p>	<p>If MBIE makes the above proposed change, we consider a new 4AM(2A) needs to be added to ensure the intent of the new relevant expenses definition can be realised. Without this new provision, the requirement to verify any reduced discretionary expenses would negate the simplification intention of the proposed change to Regulation 4(AE).</p>
Discretionary Expenses – Code	
<p>Option 2: Lenders may presume that all expenses, other than those defined, are discretionary, unless the lender has reason to believe this is not correct for a particular borrower. The proposal is to set out a number of categories of non-discretionary expenses.</p> <p>Draft content in Responsible Lending Code for Option 2:</p> <p>'The definition of 'relevant expenses' provides that lenders may exclude <u>any listed outgoings that are</u> discretionary from their initial estimate.</p> <p><u>Broadly, discretionary expenses are those a borrower can choose to spend money on, or not, depending on their financial situation and goals. They are expenses a reasonable lender could expect a borrower to stop or reduce if experiencing financial difficulty.</u></p> <p>In considering whether any listed outgoings are discretionary expenditure that a borrower <u>could</u> cease or reduce, lenders may</p>	<p>We broadly support Option 2, but recommend changes to better align with Cabinet's decision and improve workability for lenders.</p>

Content	Comment
<p>presume that expenses other than the following are discretionary, unless <u>a responsible</u> the lender <u>would have</u> has reason to believe that this is was not correct for a particular borrower.:</p> <p><u>Generally, fixed financial commitments, payments of debts, and essential living expenses (including for dependants and pets) are unlikely to be discretionary expenses</u>—including any expenses with underlying contractual requirements or significant break fees associated with ceasing them (eg some pay television subscriptions, gym memberships, and bundled mobile phone plans);</p> <ul style="list-style-type: none"> (a) payments of debts; (b) essential living expenses; and (c) regular or frequently recurring outgoings associated with tithing, remittances to a family member overseas, and pets. <p><u>Expenses that are not for essentials or basic quality of living are likely to be discretionary. Where a lender has concerns that certain expenses may not be discretionary, the lender may need to check whether the borrower would be prepared or able to reduce or cease those expenses (like tithing or gifts or money transfers to a family member overseas).</u></p> <p><u>Lenders may rely on what a borrower tells them about whether any listed outgoings can be stopped or reduced, unless the lender has reasonable grounds to believe the information is not reliable.</u></p> <p><u>For high-cost consumer credit contracts, the lender should assume that expenses are unlikely to be discretionary, unless the borrower advises otherwise.</u></p>	

Content	Comment
Credit Card and BNPL – Regulations	
<p>4AL(2A):</p> <p>Despite subclause (2), relevant expenses in respect of a payment under any revolving credit contract excludes repayments on a credit card if the lender –</p> <ul style="list-style-type: none"> (a) is satisfied that, in the previous 90 days, the borrower has not had any interest charged on the credit facility; and (b) has no reason to believe that the borrower will incur interest after entering the revolving credit contract; and (c) is satisfied that the interest free period on the revolving credit card facility is no longer than 60 days; 	<p>As discussed above, we do not support this inclusion.</p>
<p>4AL(2B)</p> <p>Subclause (2) does not apply in respect of a buy now pay later contract.</p>	
Credit Card and BNPL – Code	
<p>5.34</p> <p>If a borrower has an existing buy now pay later facility, any payments due should be treated as debt payments under the definition of listed outgoings.</p> <p><u>Lenders should consider how they best account for the debt commitment or expense a borrower has under a buy now pay later</u></p>	<p>The Code could provide guidance that clarifies that the affordability assessment of BNPL schemes under 4AL, should consider the short-term and transactional nature of the debt, and by association, a lender should consider the impacts of this in their assessment.</p>

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<p><u>contract in their affordability assessments, in a way that avoids overstating or understating that expense.</u></p> <p><u>As advances are often approved on a transaction by transaction basis and paid off in instalments over very short periods of time, taking into account the value of the good or service purchased as an expense in an affordability assessment may be preferable to avoid overstating that expense. However, the lender should consider whether, given the borrower's circumstances, a debt over a longer repayment period, or credit limit, should instead be taken into account.</u></p>	<p>The practical application of this may vary between lenders, however, would be more appropriate given varying surpluses and buffers that each lender may seek to implement.</p>
<p><i>Variations and replacements of existing credit contracts</i></p>	
<p>Option 1:</p> <p>(1A) Regulations 4AF and 4AI do not apply if:</p> <p>(a) the <u>lender (Lender A) will replace</u> an existing credit contract <u>the borrower has</u> with another lender (Lender B); and</p> <p>(b) the total monthly repayments under the new credit contracts will be equal to or lower than the monthly repayments under the existing credit contracts; and</p> <p><u>(c) the total credit limit will not increase or will only increase to the extent necessary to allow Lender A to replace the contract with Lender B; and</u></p> <p><u>(d) the new credit contract that Lender A will provide is not a high-cost consumer credit contract.</u></p> <p>(1B) For the purposes of subclause (1A) <u>the lender must</u>(b):</p>	<p>As noted there are differing views between members as to the appropriateness of the options. Regardless, members have suggested drafting changes to each to better support consumer protection and practical workability.</p> <p>In suggesting changes to Option 1, members note that the scope of the option is wide and, as currently drafted, will apply beyond refinancing to address financial hardship. As such, we suggest limiting the scope to situations where the total credit limit will not increase, so there is 'like for like' for any 'assumed affordability' under the exemption. The exemption should also not apply where the new contract is a high-cost consumer credit contract.</p> <p>We have also suggested specifying the inquiries that must be made, similar to the approach taken in the Responsible Lending Code for guidance around use of Regulation 4AG. That content could be included within the Code, although it may be preferable, given the</p>

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<p><u>(a) make reasonable inquiries into the borrower’s likely income, as if Regulation 4AJ applied;</u></p> <p><u>(b) make reasonable inquiries into the borrower’s likely expenses and obtain a credit report;</u></p> <p><u>(c) make reasonable inquiries into any other debts the borrower has;</u></p> <p><u>(d) explain and confirm the customer accepts they may pay more interest over the life of the loan, if the loan term of the new credit contract is longer;</u></p> <p><u>(e) explain to the customer and confirm the customer accepts they may pay more interest over the life of the loan, if the interest rate of the new credit contract is variable or is a promotional rate that will apply for less than 12 months; and</u></p> <p><u>(f) determine whether, based on their reasonable inquiries, the borrower’s income will exceed their likely expenses, and it is likely the borrower will meet their repayments without suffering substantial hardship.</u></p>	<p>Code is not mandatory, to incorporate the requirements within the Regulations.</p>
<p>Option 2:</p> <p>‘(1A) Regulations 4AF and 4AI do not apply if:</p> <p>(a) the lender <u>(Lender A) will replace</u> an existing consumer credit contract <u>the</u> with a borrower <u>has with another lender (Lender B);</u> and</p> <p>(b) <u>Lender A is satisfied on reasonable grounds that replacing the existing contract with Lender B is necessary to reduce financial</u></p>	<p>Again, members have suggested drafting changes to each to better support consumer protection and practical workability.</p> <p>We have suggested replacing the daily interest calculation, which could become complex and create unnecessary barriers, with a simple assessment of whether the interest rate on the new contract is the same or lower than the existing contract. We also suggest</p>

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<p><u>difficulties the borrower is experiencing or reasonably expects to experience; and</u></p> <p>(c) <u>the total credit limit will not increase, or will only increase to the extent necessary to postpone or reduce existing payments to address the financial difficulties the borrower is experiencing or reasonably expects to experience; and</u></p> <p>(d) <u>the annual interest rate will be equal to or lower than the existing annual interest rate for at least six months; and</u></p> <p>(e) <u>the new credit contract that Lender A will provide is not a high-cost consumer credit contract.</u></p>	<p>ensuring the exemption does not apply where the new contract will be a high-cost credit contract.</p>
<p>Additional option:</p> <p><u>(1X)Regulations 4AF and 4AI do not apply if:</u></p> <p>(a) <u>the lender will provide emergency access to credit, with a credit limit up to \$X,000, to an existing customer; and</u></p> <p>(b) <u>the existing customer is directly impacted by a regional or national event, like a natural disaster or pandemic; and</u></p> <p>(c) <u>the lender is satisfied on reasonable grounds that the credit is necessary to provide emergency support to that customer to meet their immediate needs as a result of the event; and</u></p> <p>(d) <u>the credit contract is not a high-cost credit contract.</u></p>	<p>We believe there is a need for an exemption to allow lenders to provide immediate access to credit to respond to events impacting large numbers of customers. The Kaikoura earthquake, recent 100 year flooding events and COVID pandemic highlighted that the CCCFA requirements are barriers to lenders acting responsibly and providing swift access to credit to support customers facing extreme situations.</p>