

6 May 2024

Consumer Policy team
Building Resources and Markets Group
Ministry of Business, Innovation & Employment
Wellington

Re: Credit Contracts and Consumer Finance Amendment Regulations (No 2) 2024 Exposure Draft

The rushed, wholesale removal of vital consumer credit regulations without evidence of issues and impacts, would risk many more borrowers facing extremely detrimental, but avoidable, financial challenges. The Government should instead pause and rethink the removal of practical affordability assessments regulations and allow time for a thorough examination of the appropriate, rather than the fastest, way forward.

FinCap welcomes the opportunity to submit in response to the Credit Contracts and Consumer Finance Amendment Regulations (No 2) 2024 Exposure Draft (**Exposure Draft**) in this targeted consultation round. However, we are deeply concerned at the short timeframe for response and a lack of opportunity for the wider public, including financial mentors, to have their say on significant roll backs of consumer protections.

FinCap strongly opposes the removal of these regulations, especially given the analysis behind this decision has been rushed through. Officials have had little scope to carefully consider all options and recent evidence. The rushed approach risks chaos, where some lenders charge ahead and recklessly ignore or do not carefully consider whether loans are unaffordable. Meanwhile borrowers, financial mentors and regulators scramble would have to navigate through the ambiguity created by the removal of clearly set minimum standards. Financial mentors need these clear regulated minimum standards to efficiently and effectively challenge these lenders for having breached the relevant requirements in the Credit Contracts and Consumer Finance Act (**CCCFA**).

Any mitigation of the risks created through improvements to the enforcement of the CCCFA's affordability requirements on lenders, through 'phase two' of the announced work programme, would lag far behind the wholesale deletion of clearly regulated consumer protections at 'phase one,' and leave an unacceptable gap. Guidance through the Responsible Lending Code is often given little weight by lenders, regulators and dispute resolution schemes. We do not expect changes to the Responsible Lending Code would effectively mitigate the risks created by the proposed deletion of regulated protections.

The wholesale removal, which has been described as 'crude' by officials in the regulatory impact statement¹, also deletes key protections for borrowers up against the potential of an annual interest rate of 50 percent or more. This is at odds with signals that the Government plans to extend protections at the riskiest end of the lending market.

The Government should pause and reconsider the sequence or necessity of changes to protections in this space. The discussion of 'phase two' of the work programme so far indicates it will consider the actual core issues. Evidence appears to point to liability regimes rather than the drafting of regulations as influencing the conservative approaches to affordability by responsible lenders.

¹ See: <https://www.mbie.govt.nz/dmsdocument/28287-regulatory-impact-statement-reducing-the-burden-of-affordability-requirements-in-consumer-credit-legislation-proactiverelease-pdf>

Instead of revoking protections that are working better and better for financial mentors and those they support, the Government should be focused on applying thorough affordability requirements to buy now pay later lenders to counter the debt spirals that financial mentors are seeing. Quicker enforcement responses where lenders are not following the requirements, as is signalled for 'phase two' work, should come before removing protections for consumers.

We expand on these comments further in the submission below.

About FinCap

FinCap (the National Building Financial Capability Charitable Trust) is a registered charity and the umbrella organisation supporting the 185 local, free financial mentoring services across Aotearoa. These services supported over 69,000 whānau facing financial hardship in 2023. We lead the sector in the training and development of financial mentors, the collection and analysis of client data and encourage collaboration between services. We advocate on issues affecting whānau to influence system-level change to reduce the causes of financial hardship.

Keep restrictions for where lenders emerge and charge over 50 percent per annum interest

FinCap's reading of the Exposure Draft is that it removes specificity as to the minimum standard for checks that take place for high-cost credit contracts before extra protections are applied, some of which are also being revoked. While the Exposure Draft retains the requirements at 4AO for high-cost lenders to presume substantial hardship when a borrower has defaulted on another loan within the last 90 days, other specific protections are up for deletion. For instance, a requirement at 4AK, is that high-cost lenders check 90 days of bank statements rather than relying on unverified information. Otherwise, the proposed change removes the clear minimum standards for a robust affordability assessment that are needed. This includes adding buffers and surpluses to counter any underestimation or unexpected variation, as well as thorough consideration of whether expenses that would need to be ceased to make the loan affordable, are discretionary.

The proposed changes in the Exposure Draft could see lenders who charge over 50 percent per annum re-emerge and offer unaffordable, high-risk loans. This should not happen at a time when the increased cost of living pressures, which whānau are facing, are already resulting in increased demand for financial mentors' support. Robust requirements on high-cost lenders should be retained now, ahead of the Minister's signalled initial view that the requirements should apply to loans which charge 30 percent interest or more, as is signalled for consideration at 'phase two' of this work programme.²

FinCap recommends at the absolute least that the application of general, regulated minimum standards for assessing affordability and relevant extra requirements are retained for lenders charging 50 percent or more per annum.

Unreliably evidenced and rushed 'crude' changes risk awful outcomes and would put even more strain on financial mentors

While officials' regulatory impact statement analysis recommended the approach taken, it clearly stated that this was not a strong preference. The analysis also gave the same weighting in selecting options to the quick and easy implementation of changes for lenders ahead of further reforms, as it did for minimising the harm where lenders approve unaffordable credit. This is inappropriate.

Where a loan is unaffordable from the start, whānau face substantial hardship that will often see them unable to afford the basics and face immense stress. Only some of these whānau will find their

² See para 42 here: <https://www.mbie.govt.nz/dmsdocument/28285-progressing-financial-services-reform-proactiverelease-pdf>

way to resolve the harm through a financial mentor and add to a financial mentor's already strained capacity. Even then, it can take months or years to reverse the damage done to finances and quality of life from an unaffordable loan, if it is possible at all. All of this is avoidable and much more important than lenders being able to quickly adjust their systems ahead of another change likely upcoming anyway, as a part of the 'phase two' work programme.

What should be a regulatory impact statement outlining thorough analysis, instead shares that shortcuts had to be taken and that there were significant gaps in evidence because of the rush to make changes. For example the regulatory impact statement says:

*"We are conscious that these constraints limit us to relatively crude options that may provide less effective solutions to the problem. They also limit our ability to build into options ways of mitigating risks associated with not specifying what steps constitute 'reasonable inquiries' for the purpose of the CCCFA's requirement to assess affordability."*³

And...

*"We have a low to medium level of confidence in the quality of evidence."*⁴

The analysis undertaken largely relies on evidence from a review in early 2022. Changes were made to the regulations since that review and their effectiveness has not been properly assessed. Otherwise there seems to have been some conversations between officials and stakeholders but nothing firm. Even then, officials noted that amongst lenders' calls for adjustments that apply less regulatory burden:

*"We heard from lenders that their procedures for complying with the affordability regulations are now more settled and less problematic than at first."*⁵

The regulatory impact statement also cautions the reliability of some figures being given as examples to justify the changes. For instance, that of the figure of a six to seven percent estimated drop in approvals for home loans it is not known what proportion were unnecessarily turned down.⁶

One unevicenced reason given for the need for the change is that vulnerable borrowers are increasingly turning to high-cost 'underground' lenders because they are being declined for other loans.⁷ Financial mentors are not seeing evidence of this and those making the claims have provided no evidence to demonstrate a trend at scale, other than a few anecdotes. Financial mentors have rightly pointed out to FinCap that if publicly available lenders are being prevented from giving unaffordable loans, then this is still the right outcome. Alternatives like support from Work and Income or No Interest Loan Schemes will still be available.

Another justification offered for removing the regulated affordability protections is that increased access to credit will help whānau deal with the cost-of-living.⁸ This clearly fails to see the issue of

³ See para 64 in: <https://www.mbie.govt.nz/dmsdocument/28287-regulatory-impact-statement-reducing-the-burden-of-affordability-requirements-in-consumer-credit-legislation-proactiverelase-pdf>

⁴ Ibid

⁵ Ibid

⁶ See para 40 in: <https://www.mbie.govt.nz/dmsdocument/28287-regulatory-impact-statement-reducing-the-burden-of-affordability-requirements-in-consumer-credit-legislation-proactiverelase-pdf>

⁷ See: <https://www.mbie.govt.nz/dmsdocument/28285-progressing-financial-services-reform-proactiverelase-pdf>

⁸ Ibid

borrowing for expenses someone cannot afford, only to have those repayments undermine the budget available for essentials going forward. This reflects the beginning of a debt spiral, especially where food is involved, and would drive more demand for financial mentoring. Increasing access to credit that could be unaffordable when many struggle with the cost of living already, is a flawed goal.

What the regulatory impact statement and FinCap's conversations with lenders reveal is that changes to the regulations alone are unlikely to see industry change their systems, unless it goes too far in removing protections. This is because fear of the liability regime continues to be cited as the main motivation for responsible lenders using their discretion not to risk any breach of the law. The regulatory impact statement notes:

"...the liability settings in the CCCFA are likely to undermine any options that increase the degree of judgment required of lenders to navigate the regulations..."⁹

This supports our recommendation that the Government does not rush a change which removes regulated consumer protections, because the perceived interim benefits are unlikely to eventuate in responsible lenders' actions anyway. For the avoidance of doubt, FinCap currently supports the liability settings but welcomes a thorough review of this, and other elements needed towards effective compliance and enforcement.

Both the cabinet paper and regulatory impact statement correctly identify that the Exposure Draft's proposed wholesale deletion of regulated minimum standards for affordability assessments would risk a failure to protect vulnerable borrowers:

The risk that the proposal to remove affordability requirements increases the incidence of unaffordable lending, if realised, is likely to disproportionately affect certain population groups. These would be groups who are more likely to be seeking credit from less scrupulous lenders or who are more vulnerable, by being less well equipped to judge affordability of the credit themselves (due, for example, to low levels of financial literacy, a poor understanding of English, financial stress, or pressure from family members to obtain credit). Māori, Pacific peoples and immigrants are likely to be over-represented in these groups."¹⁰

This under-mitigated risk is at odds with the Government's commitment to protect vulnerable borrowers. FinCap reiterates our and other organisation's joint statement that we are open to working with the Government towards meeting that commitment.¹¹ We strongly prefer the status quo and no amendments, other than to strengthen the robustness of the minimum regulated standards for affordability assessments. However, we also reiterate earlier feedback that 'option three' in the regulatory impact statement to 'disapply the affordability assessment regulations to home loans' is the least harmful option considered, if the Government is determined to make rushed changes before thorough work on the 'phase two' work programme.

FinCap recommends that the Government pause and reconsider 'phase one' of the work programme and maintains or strengthens current regulated minimum standards that clearly outline how a lender reasonably determines their actions will not cause substantial hardship.

Buy now pay later lending issues and timely enforcement should be the focus instead.

Financial mentors continue to see issues with buy now pay later lenders offering unaffordable credit. These lenders are not required to comply with the CCCFA at present, and are due to still be exempt

⁹ Ibid

¹⁰ Ibid

¹¹ See: <https://www.everydayborrowers.org/>

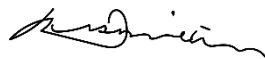
from making reasonable inquiries to assess affordability after the upcoming changes in September. We have not seen any discussion of this lending in the materials surrounding the 'phase one' or 'phase two' work programmes and we urge that this is a focus. Financial mentors report whānau continuing to present with multiple simultaneous unaffordable loans to these lenders, that were aggressively marketed.

The other major issue in the credit consumer protection space raised by financial mentors is the need to enforce the credit law around vehicle finance. Recent action by the Commerce Commission¹² and signals around the focus of 'phase two' are steps in the right direction towards faster follow-up of systemic breaches of the CCCFA that are causing widespread harm.

FinCap recommends resources are dedicated to improving protections for buy now pay later borrowers and more effective enforcement of the CCCFA instead of changes proposed in the Exposure Draft.

Please contact Jake Lilley, senior policy advisor at FinCap on 027 278 2672 or at jake@fincap.org.nz to discuss any aspect of this submission.

Ngā mihi,



Ruth Smithers
Chief Executive
FinCap

¹² See: <https://comcom.govt.nz/news-and-media/media-releases/2024/comcom-to-launch-action-against-two-car-finance-lenders>