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Responsible Lending Code  
Competition and Consumer Policy Team  
Ministry of Business, Innovation and Employment  
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## **SUBMISSION on the Responsible Lending Code Discussion Document**

### **Introduction**

Thank you for the opportunity to make a submission on the Responsible Lending Code (Code) discussion document. This submission is from Consumer NZ, New Zealand's leading consumer organisation. It has an acknowledged and respected reputation for independence and fairness as a provider of impartial and comprehensive consumer information and advice.

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### **Responses to specific questions**

***Question 1: Do you agree with the proposed criteria for assessing what guidance should be set out in the Code as set out in paragraph 18? Should retaining sufficient flexibility to allow lenders to adapt the guidance to different products and business models be another criterion? Are there any other key criteria to be considered?***

We agree with the proposed criteria set out in paragraph 18 of the discussion document, with the exception of the last bullet point "not unnecessarily restricting consumer access to credit". The reason for the inclusion of this criterion is unclear and it appears inconsistent with the responsible lending principles in the Credit Contracts and Consumer Finance Amendment Act 2014 (Amendment Act).

The intent of the Amendment Act is to ensure lending is responsible and to remove irresponsible lenders from the market. In this sense, the legislation does seek to restrict access to credit, namely irresponsible credit. Provided lending is responsible, consumer choice will not be restricted.

***Question 2: Are there any particular features of the New Zealand market which would differentiate our approach from international approaches?***

One feature of the New Zealand market which needs to be considered is that a high proportion of savings is held in housing stock. If consumers are having difficulty repaying their mortgages then they will have less discretionary income and economic downturns are likely to be exacerbated. It is therefore important that the Code acknowledges the importance of responsible mortgage lending practices.

***Question 3: We consider that the structure of the Code should reflect the lifecycle of a consumer credit contract, do you agree?***

We agree that the structure of the Code should reflect the lifecycle of a consumer credit contract.

***Question 4: Are there lenders/borrowers/agreements or classes of lenders/borrowers/agreements that should be treated differently under the Code? If so, why, in what way and how should any such lenders/borrowers/agreements be defined?***

In our view, the Code should, as far as practicable, apply equally to all lenders. All lenders should be required to comply with the same high standards of responsible lending. While we do not favour specific exemptions, we acknowledge that there may need to be additional obligations on lenders in some cases.

***Question 5: Should the concept of "scalable" guidance apply to the Code? If so, which principles or responsibilities should be scalable?***

If additional protections are required for particular types of lending, we agree they should be specified in the Code.

***Question 6: How prescriptive should the guidance in the Code be?***

We support a Code that promotes certainty and consumer confidence. We would like to see adequate guidance in the Code to provide certainty for the market and to ensure lenders are interpreting the responsible lending principles consistently. If lenders have a wide discretion on how they give effect to the principles, consumer confidence will be undermined and the Code will fail to achieve the desired outcome.

***Question 7: Should the level of prescription differ for different classes of lenders/borrowers/agreements? If so, which classes and why?***

In our view, the levels of prescription in the Code should, as much as possible, be consistent for all lenders, borrowers and agreements. If a "one size fits all" approach works in practice then this will provide greater certainty.

***Question 8: What are the elements of a best practice internal process to ensure that advertising is not misleading, deceptive or confusing? (For example, in relation to training and checking marketing material.)***

The guidance provided in the Commerce Commission's Fair Trading Act Compliance Policy (Sample) outlines core elements of a best practice process. These elements include that staff undergo Fair Trading Act compliance training, and the lender has a system for checking publicity material is compliant with the Act.

**Question 9: Should guidance on advertising processes take account of the size and nature of the lender? If so, how?**

As a general rule, the same guidance should apply across the range of lenders.

**Question 10: What existing guidance or codes of practice for advertising will help inform the Code? Should these codes be referred to or translated into the Code?**

The Commerce Commission's guidance on the Fair Trading Act will be useful to help inform the development of the Code. As far as possible, the Code should be a self-contained document and not refer to other codes.

**Question 11: Are there specific advertising practices that lenders should follow? Or are there specific advertising practices that lenders should refrain from following?**

We support the approach taken in Australia and UK relating to disclosure of an annual percentage rate. We are aware of companies advertising weekly or monthly rates which are likely to underestimate the amount payable. A requirement for an annual percentage rate would also make it easier for consumers to compare the cost of credit.

We also support the Code including clear direction to lenders that the use of advertising which states or implies there will be "no credit checks" is unacceptable. This type of advertising is common. However, it is inconsistent with the responsible lending principles and the Code should make this clear.

In addition, we believe the Code needs to provide clear direction on the use of terms such as "interest free". The term implies there will be no cost to obtaining credit. However, we are aware that it is used by lenders who impose significant fees. These fees are a form of disguised interest and we consider the term "interest free" is misleading in these cases.

**Question 12: Should advertising of certain credit products be accompanied by risk warnings?**

We agree that advertising certain credit products should be accompanied by risk warnings. The risk warnings in the UK Financial Conduct Authority Consumer Credit Sourcebook (CONC) seem appropriate. These warnings may assist borrowers to understand the risks associated with the products.

**Question 13: Should there be specific guidance in relation to advertising which is targeted at a specific group or persons known to have specific characteristics? If so, which groups/characteristics?**

We would support the Code including specific guidance on targeted advertising. In principle, we support the approach adopted in the CONC.

**Question 15: Apart from complying with disclosure obligations, how do/should responsible lenders assist borrowers to understand the terms of the credit agreement? How should any guidance cover different modes of providing credit? (e.g. online applications) Should certain information be required to be given orally for face-to-face or telephone interactions with customers?**

We believe the Code should require face-to-face or telephone interactions with the borrower before credit is provided. This would allow questions to be asked and help reduce the risk of misunderstandings.

We suggest a video format may also be useful to explain the components of a credit contract and associated risks. This may be a tool that the Ministry or the Commerce Commission could develop and make available to both lenders and borrowers.

***Question 16: What are/should be responsible lenders' practices where English is not a borrower's first language?***

The lender should be required to recommend the borrower use the services of an interpreter. Where it is clear the borrower has significant difficulty understanding English, it may be appropriate for written disclosure to be provided in the borrower's spoken language.

***Question 17: What opportunities do/should responsible lenders provide to borrowers to ask questions about the agreement? Would providing access to frequently asked questions be sufficient?***

Providing access to frequently asked questions would be useful. However, it is unlikely to be sufficient. We think borrowers should also be given the contact details of a primary point of contact for the lender who can answer any of the borrower's questions.

***Question 18: What practices do/should responsible lenders undertake to ensure that credit agreements are in plain English, clear, concise and intelligible?***

The requirement that agreements are intelligible extends into the loan products themselves. If the terms of an agreement are so complex they cannot be understood by an average consumer without lender assistance, we would argue the lender is not being responsible because they are offering unacceptably complex products.

It is essential that the option of "taking away and reading" is a meaningful one for borrowers (it is the borrower's ultimate protection). If borrowers cannot understand the agreement on their own, they will not have the protection that is intended to be provided by disclosure.

Lenders can empirically test the intelligibility of their agreements.

***Question 19: How do/should responsible lenders assist borrowers to understand the implications of the credit agreement? E.g. if technical or legal concepts are referred to, should the agreement explain the implications of those concepts?***

If technical or legal concepts are an integral part of the credit agreement, the lender should be required to explain these concepts.

We believe there is also value in expecting lenders to go beyond disclosing information about the relevant product and discussing borrowing options more generally. People can more easily assess a product by having others to compare it with. With a range of options discussed, borrowers will be more likely to avoid making an inappropriate choice.

It is essential that lenders see their interaction with borrowers as more than just a sales role. Requiring the conversation to include an element of education and advice is consistent with our interpretation of "responsible lending" and is reflected in our view that financial advisers should be required for this work (see comments on question 34).

***Question 21: What are/should be responsible lenders' processes in relation to independent budgeting or legal advice for borrowers and guarantors?***

Lenders should be expected to provide information about independent budgeting and legal advice as part of their normal responsible lending practices.

***Question 22: What do/should responsible lenders do to assist guarantors to make informed decisions?***

We think there should be verbal disclosure provided by the lender to the guarantor before the credit agreement is entered into. This exchange should include an explanation of the worst case scenario for the guarantor to assist the guarantor to fully understand what will happen if the borrower defaults under the credit agreement.

***Question 23: What information do/should responsible lenders give a borrower to assist them to make an informed decision on credit related insurance?***

The lender should be required to give a borrower the following information to assist them to make an informed decision on credit related insurance:

- (a) whether the insurance is optional or compulsory
- (b) whether the borrower can obtain insurance from another provider
- (c) the cost of the insurance and whether this is built into the cost of credit
- (d) the duration of the policy and when it will expire in relation to the credit
- (e) what the insurance will and will not cover
- (f) any rights of cancellation.

***Question 25: How do/should responsible lenders ensure that borrowers have sufficient time to make informed decisions?***

In theory, requirements for lenders to make reasonable inquiries and to assist the borrower to make informed decisions should help to ensure the borrower has sufficient time to make their own decision. However, we believe lenders' practices should also ensure the borrower is given time to take away and read the credit contract before signing.

***Question 26: What processes and practices do/should responsible lenders undertake to assist informed decision for agreements when the application and approval is undertaken remotely?***

As mentioned above, we think there should be verbal disclosure by the lender to help ensure the borrower understands their obligations and the terms of the credit agreement. This obligation should apply whether the application is made remotely or in person.

***Question 27: What other matters should the Code address in relation to assisting informed decisions?***

We think it would be helpful for consumers if lenders are required to report all charges under the credit agreement in a simple standardised way (for example, see the TrueCost checklist available on the Ministry of Business, Innovation and Employment website).<sup>1</sup>

***Question 28: What information do/should responsible lenders require from a borrower when they apply for credit? How much reliance should a lender place on a credit check?***

Lenders should carry out a full affordability assessment, which takes into account the borrower's income, expenditure, the ability to repay in a sustainable manner, existing

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<sup>1</sup> See <http://www.consumeraffairs.govt.nz/for-consumers/motor-vehicles/truecost/checklist-english.pdf>

credit commitments, credit history, personal circumstances, and value and duration of the loan.

In our view, a lender should not rely solely on a credit check to inform their decision. Broader inquiries are required.

***Question 29: What do/should responsible lenders explain to the borrower in relation to the purpose of the checks and assessments of affordability?***

Lenders should explain the purpose of affordability assessments is to ensure lending is responsible. There is also a place for information about responsible lending to be provided by the Ministry and the Commerce Commission to ensure consumers have additional and independent sources of information.

***Question 30: How do/should responsible lenders assess whether the information a consumer has provided is correct? In what circumstances do/should responsible lenders be able to rely on information provided by a borrower?***

Lenders should be required to take reasonable steps to verify information provided to them by the borrower (for example, by getting copies of bank statements and pay slips). Lenders should not rely solely on verbal information provided to them by the borrower.

***Question 31: How does/should a responsible lender's checks differ for existing customers and new customers?***

Checks on new customers may need to be more thorough. However, in all cases, the lender must ensure they have a sound basis for determining whether the loan is appropriate for the borrower.

***Question 32: How do/should responsible lenders consider whether credit does/does not meet the requirements and objectives of the borrower?***

Lenders should be required to conduct an objective assessment of whether the credit would meet the objectives of the borrower. This should include assessing:

- (a) whether the borrower can pay the maximum amount payable under the credit agreement
- (b) what happens to the ratio of repayments if, for example, a couple apply for a loan and one of the couple loses their job
- (c) what happens to the borrower's equity if the asset the borrower is using as security falls in value
- (d) what happens to the repayment to income ratio if interest rates rise.

***Question 33: How should the lender responsibility to be satisfied that it is likely that the credit will meet the borrower's requirements and objectives be balanced against not unduly restricting consumer choice?***

We do not see a conflict between responsible lending and consumer choice.

***Question 34: What proportion of credit applications are processed without the involvement of financial advisers permitted to give personalised advice in relation to category 2 products under the Financial Advisers Act 2008? Will regulation under both the lender responsibilities and the Financial Advisers Act impose significant costs for lenders?***

We support regulation under both the lender responsibilities and the Financial Advisers Act (FAA). FAA category 2 products are not overly complex and the training required in

relation to these products is not onerous. It would be relatively simple for lenders to have staff licensed to provide advice on category 2 products.

***Question 35: How do/should responsible lenders deal with the potential conflicting incentives posed by payments of commission/bonuses and the need to be satisfied that it is likely the credit agreement meets the requirements and objectives of the borrower and will be repaid without substantial hardship?***

We have previously expressed concerns about the influence commissions can have on financial advice. Lenders must clearly disclose any commissions or bonuses they stand to gain from recommending a product to the borrower. There is also a need for practices in this area to be monitored by regulators to ensure commissions are not influencing advice.

***Question 36: What factors should be taken into account in considering what should constitute substantial hardship?***

The CONC approach points to several critical factors that should be taken into account. The CONC requires an assessment of the borrower's ability to meet repayments in a "sustainable manner", that is, making repayments without undue difficulty while meeting other reasonable expenses.

Critical factors in this assessment include:

- (a) the borrower's regular income and expenses
- (b) the number and age of dependents
- (c) any health related expenses
- (d) the maximum amount payable under the contract, including the cost of insuring the asset the borrower is borrowing against.

***Question 37: Should substantial hardship be assessed by reference to any particular indicators or reference budgets?***

We think there should be a clear trigger point/s that alerts the lender to hardship, for example, a debt-to-income ratio.

***Question 38: Should the Code specify a threshold for substantial hardship? If so, what is an appropriate threshold?***

As above, a debt-to-income ratio could be used as a threshold.

***Question 39: To what extent do/should responsible lenders take into account likely future market conditions (e.g. interest rate rises) when assessing affordability for the borrower (particularly for long term credit agreements such as mortgages)?***

Lenders should be required to take future market conditions into account when assessing affordability for the borrower. If a lender is aware interest rate changes would make the credit unaffordable, it would be irresponsible to not take this into account. As mentioned above, this is particularly important given the high proportion of savings in housing stock.

***Question 40: Do/should responsible lenders engage in lending that relies primarily or solely on the value of any security provided by the borrower?***

We do not think that responsible lenders should engage in lending that relies primarily or solely on the value of security provided. If lenders base their credit decisions on asset

values rather than a borrower's capacity to repay the credit, this would create unacceptable risks for borrowers and financial instability more generally.

***Question 41: Are there circumstances in which it should be presumed that the consumer will only be able to make repayments with substantial hardship?***

At a minimum, the tests applied in Australia should be adopted.

***Question 42: What policies do/should responsible lenders have in place to assess whether the security taken is excessive relative to the size and length of the credit provided?***

Any security should be proportionate to the size of the loan. Lenders should be required to demonstrate this in their lending practices.

***Question 43: What other matters should the Code address in relation to making reasonable inquiries to assess whether the credit agreement meets the borrower's requirements and objectives and can be repaid without substantial hardship?***

The Code should address the timing of inquiries because a borrower's financial situation can change quickly. In order to be relevant, any inquiries should be made around the time of the credit agreement being entered into. If a significant amount of time has passed between the making of inquiries and the granting of credit, then the lender should be required to make further inquiries to ensure there has not been any change in circumstances.

***Question 44: What practices and processes do/should responsible lenders have in place to assist borrower decision-making in relation to variations to a contract (e.g. credit card limit increases) or refinancing? What types of variations do/should such practices apply to?***

Our view is that any increase in a credit limit should be opt-in only. Lenders should also be required to provide the borrower with an explanation of the additional costs associated with opting-in to a credit increase.

***Question 45: What practices and processes do/should responsible lenders have in place in relation to whether a credit agreement would likely meet the borrower's requirements and objectives and can be repaid without substantial hardship following a variation or refinancing? What types of variations do/should such practices apply to?***

An affordability assessment should be carried out before a variation takes place.

***Question 46: Other than complying with disclosure requirements, what information do/should responsible lenders provide to borrowers in relation to the credit agreement during the life of the agreement? For example, should lenders provide certain information to borrowers to enable borrowers to make decisions as to whether to exercise their rights under the agreement?***

We would like to see lenders provide borrowers with information on how different repayment arrangements can affect the amount paid in interest and fees. We believe this would help borrowers select a repayment option that reduces the costs of servicing the debt and means it is repaid earlier.

***Question 47: What practices do/should responsible lenders refrain from during the life of the credit agreement? (For example, should responsible lenders***

***refrain from the practice of holding multiple direct debit forms so that one can be re-submitted if form is cancelled?)***

As mentioned above, we believe lenders should not increase a credit limit without the borrower's consent. We strongly agree that lenders should not hold multiple direct debit authorities to use in the event the borrower cancels an authority.

***Question 48: What practices should lenders follow in order to set a fee that is not unreasonable?***

Lenders should be required to set fees that are fair and transparent, and reflect the actual administrative costs they incur. They should not operate business models based on the income expected from a large number of borrowers paying default or other penalty fees.

We are aware of lenders who advertise "interest free" finance but who include significant fees in their contracts. In our view, the basis for, and amount of these fees, is highly questionable. However, it is usually very difficult for an individual consumer to challenge them.

We believe the Code should set out the specific fees that may reasonably be expected to be included in a credit contract. The Code should also set out the types of administrative costs that may be taken into account when calculating a fee, and the costs which should not be included in the calculation.

We would have liked to see further analysis in the discussion document on the issue of fees and the approach the Code may take. We are aware the appeal in relation to the Sportzone/MTF case may have made this difficult. However, we believe the Code must address this issue in a substantive manner in order to provide certainty for both consumers and lenders.

***Question 57: How do/should responsible lenders monitor whether the borrower may be facing actual or possible repayment difficulties? Is it practical to check for possible repayment difficulties?***

The CONC requirements provide a possible approach. As the discussion document notes, the CONC requires lenders to monitor a borrower's repayment record and take action where there are signs of actual or possible repayment difficulties. Lenders should be proactive in helping borrowers who are facing repayment difficulties.

***Question 58: What policies or procedures do/should responsible lenders have in place for dealing reasonably with borrowers who have or may breach the agreement or when other problems arise? (e.g., in relation to assistance to be provided to the borrower).***

Lenders should ensure they contact the borrower as soon as they become aware of the repayment difficulty to:

- (a) offer assistance to the borrower to remedy the situation
- (b) advise the borrower of their legal rights
- (c) provide information about independent budget advice services.

***Question 59: What do/should responsible lenders do to assist borrowers to be informed of their rights? (e.g., in relation to unforeseen hardship relief and access to dispute resolution schemes.)***

Lenders should be required to provide standard information to borrowers advising them of their rights. This information should be provided to borrowers at the time the credit

agreement is entered into and as soon as the lender becomes aware that the borrower is experiencing repayment difficulties.

Information about complaints processes and dispute resolution schemes should also appear on statements and other correspondence with the borrower.

***Question 60: How do/should responsible lenders communicate with borrowers in relation to breaches or potential breaches of the agreement to ensure that they treat borrowers reasonably and in an ethical manner? (e.g. in relation to staff training and policies and enforcement of those policies.)***

Lenders should have staff trained in dealing with situations of default. Staff should have an understanding of the issues that can be involved in these situations and be able to deal with them sensitively. They should also be able to provide borrowers with information about their legal rights with respect to the hardship provisions of the Act.

***Question 61: What do/should responsible lenders take into account when considering repayment plans proposed by a borrower (in connection with an application for unforeseen hardship relief)?***

Where a borrower has sought assistance from a budgeting service to develop a repayment plan, we believe the lender should accept the repayment plan.

***Question 62: What are the elements of a good internal complaints process?***

A good internal complaints process should be easy for consumers to access, ensure fair deliberation of the complaint, and provide a timely decision.

***Question 63: What other matters should the Code address in relation to borrowers facing repayment difficulties or other problems?***

Lenders should be required to take a pro-active approach in communicating with the borrower about repayment difficulties. Lenders should be required to contact borrowers at the first indication of difficulties and should not wait for the borrower to get in touch with them while the difficulties potentially worsen.

***Question 66: What steps do/should responsible lenders go through before taking enforcement action? For example, before sending debts to a debt collection agency?***

Lenders should be required to communicate with the borrower and exhaust all avenues of redress before taking any enforcement action. Enforcement should be a last resort.

We would like to see the Code include a specific requirement that a lender must not take disproportionate action against a customer in arrears or default. We have received complaints about goods being repossessed when a relatively small amount of money is outstanding. In one case, a couple had their car repossessed because of a \$240 debt.

***Question 67: What are/should be responsible lenders' practices in relation to charging interest and/or fees once they have started enforcement action? (For example, once a debt has been sent to a collection agency.)***

The lender should not be able to charge further interest or fees where a debt has been sold to a collection agency.

***Question 68: What steps do/should responsible lenders take to ensure that they treat borrowers and their property reasonably and in an ethical manner***

***during the course of any enforcement action (including the manner in which the lender or their agents communicate with the borrower)?***

As mentioned above, lenders should have staff trained in dealing with situations of default. Staff should have an understanding of the issues that can be involved in these situations and be able to deal with them sensitively. They must also have a sound understanding of the law.

***Question 70: What do/should responsible lenders do once they have been fully repaid? (For example, arranging release of securities.)***

The lender should be required to notify the borrower (and any guarantor) that the debt has been repaid and any other steps that the lender and/or borrower are required to take, including cancelling direct debit/payment authorities and releasing securities promptly.

***Question 71: How/what steps should a lender take to satisfy itself on reasonable grounds that goods are at risk in accordance with Part 3A?***

Part 3A places the onus on the lender to prove they had reasonable grounds to believe the goods were at risk. In our view, this requires the lender to have a strong evidential basis for action. The lender should therefore be required to document the evidence they have used to inform their decision. This evidence should be provided to the borrower.

***Question 72: What policies do/should responsible lenders have in place in terms of considering alternative options that could be explored before exercising the remedy of repossession?***

We would like to see the Code include a requirement for lenders to consider alternative options to repossession. Responsible lenders should be expected to make every effort to avoid repossession. Policies requiring early contact and proactive intervention when payment difficulties arise should be a minimum.

***Question 73: Should the Code provide guidance on the repossession of items of little economic value?***

We agree the Code should provide guidance on repossession of items of little economic value. As mentioned above, we think the Code should also prevent a lender from taking disproportionate action against a borrower in default. This would prevent lenders from repossessing items when the cost of doing so is greater than the item's value. Such a provision would help ensure lenders do not repossess items for purely punitive reasons.

***Question 75: Should the Code refer to the internal complaints resolution process used to resolve borrower complaints (given that a lender must not begin or continue repossession enforcement action until a borrower's complaint in relation to any repossession enforcement action has been resolved)?***

The Code should refer to the internal complaints process.

***Question 76: What guidance should the Code provide in terms of how lenders or their repossession agents should enter premises?***

Any repossession should take place in a manner not likely to threaten, distress or publicly embarrass the borrower.

***Question 78: How do/should responsible lenders ensure that ethical behaviour is observed when effecting a repossession?***

Lenders must ensure staff carrying out a repossession have a sound knowledge of the law and their responsibilities. At a minimum, the lender should be able to demonstrate staff or the lender's agents have appropriate training. Where an agent is used, the lender should have processes in place to check the agent is acting responsibly.

***Question 79: Should the Code provide guidance about how responsible lenders should carry out the process of selling repossessed goods?***

The Code should provide guidance on how responsible lenders should carry out the process of selling repossessed goods.

Thank you for the opportunity to make a submission on this discussion document. If you require any further information, please do not hesitate to contact me.

Yours sincerely



Sue Chetwin  
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