

5 February 2020

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Submission on the Exposure draft of the Credit Contracts and Consumer Finance Amendment Regulations 2020

ASB Bank Limited (**ASB**) welcomes the opportunity to provide feedback to the Ministry of Business, Innovation & Employment (**MBIE**) on the exposure draft of the Credit Contracts and Consumer Finance Amendment Regulations 2020 (the **Draft Regulations**).

Our key submissions on the Draft Regulations are set out in the Appendix.

ASB has also contributed to the New Zealand Bankers' Association submission on the Draft Regulations (the **NZBA submission**) and endorses the views and recommendations made therein.

ASB wishes to acknowledge the proactive and positive engagement from the MBIE review team over the course of this consultation. ASB looks forward to further engagement with MBIE and industry on the Draft Regulations. In particular, if MBIE wishes to discuss any aspects of our submission, we would be happy to meet to do so.

Yours sincerely,



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APPENDIX: THEMATIC COMMENTS

1. ASB is proudly committed to its purpose of accelerating the financial progress of all New Zealanders. Lending to consumers is a key enabler of progress as it allows people to realise home ownership goals, equip themselves to succeed financially and cope with unexpected costs and events. ASB is proud of the contribution we have made to helping New Zealanders achieve these goals, having over the last three years considered over [redacted] customer applications for consumer lending, encompassing home-loans, personal lending and overdrafts.
2. ASB fully supports the policy intent behind the Credit Contracts Legislation Amendment Act (**Amendment Act**) and the Draft Regulations to reduce the harm that problem debt causes by ensuring credit providers lend responsibly. ASB supports the approach under the Amendment Act to differentiate between 'high-cost' and non-'high-cost' lenders given that the overwhelming evidence of harm from problem debt arises from lending by the high-cost credit sector.
3. However, this distinction between the treatment of high-cost and non-high-cost lenders is not appropriately reflected in the Draft Regulations. As a result, ASB considers that many of the proposed requirements are likely to lead to impractical lending practices by low-risk lenders (including banks and other mainstream lenders) which are unwelcome by customers. We are concerned that this may unintentionally result in an unwarranted tightening in the availability of credit, to the detriment of borrowers, particularly vulnerable customers, and the wider New Zealand economy. This in turn, may promote financial exclusion, which runs contrary to the policy goals of the Draft Regulations. To mitigate this, ASB would support the proposed regulations applying only to high-cost lenders. Failing this, ASB would support two sets of minimum standards being introduced – one that would apply to high-cost lenders and the other for non-high-cost lenders. We consider these options would better balance the policy goals while not unduly impacting access to credit.
4. ASB has a number of concerns with the Draft Regulations, which are covered off in detail in the NZBA submission. Our key areas of concern relate to the proposed prescriptive assessment that a lender must undertake under Regulations 4AC-4AH to be satisfied that a borrower is likely to repay without substantial hardship. These are outlined below:

The Draft Regulations lack scalability and customer-centricity

5. A key feature of the Responsible Lending Code and of the UK and Australian responsible lending rules is that they allow for scalability and tailoring of a lender's affordability and suitability assessments based on the nature of the lending and the borrower's individual circumstances¹. ASB believes that a pragmatic and customer-centric approach is essential. The Draft Regulations should reflect that individual borrowers' circumstances differ and allow for lenders, making reasonable inquiries of the borrower and of other information it has available, to exercise judgement.
6. By contrast, the Draft Regulations prescribe that lenders must make particular inquiries and take particular steps regardless of the nature of the lending (e.g. a small credit card limit increase vs. a new 30-year term home loan) or the borrower's circumstances, when this may not be appropriate

¹ We note that the Australian Securities and Investments Commission updated its responsible lending guidance (RG 209) in December 2019 to afford lenders greater flexibility through 'principles based' guidance following strong industry feedback cautioning against applying an overly prescriptive framework.

or necessary. For example, the Draft Regulations do not adequately accommodate factors such as:

- The term of the loan;
 - Whether the lending is secured or unsecured;
 - The quantum of the lending; and
 - Time elapsed since a prior full assessment.
7. Failing to appropriately recognise these factors will result in operational inefficiencies and frustration from customers who will in many cases be subjected to drawn-out application processes that do not take their needs and personal circumstances into account. This issue is particularly acute in the context of lending to customers that have an established relationship with a lender (discussed in paragraphs 11-13 below).

***ASB recommends** that the regulations afford greater scalability that takes into account factors such as (a) the term of the loan; (b) whether the lending is secured or unsecured; (c) the quantum of the lending; and (d) the time elapsed since a prior full assessment.*

The affordability inquiries and reconciliation requirements are impractical

8. Assessment of a customer's income and expenses cannot be narrowed down to a prescriptive accounting standard approach, which the Draft Regulations currently require. This will produce an unrealistic view of whether a customer can afford a loan. This prescription, as well as the requirements to undertake multiple reconciliations, will result in customers feeling they have been treated unfairly and will also significantly increase the time it takes for a customer's loan to be processed.
9. In particular, ASB has the following concerns related to identification, verification and reconciliation processed for income and expenses:
- Discretionary expenses and cash withdrawals when estimating a customer's expense position: The very nature of discretionary expenses is that they can be given up if needed – so they should not be included in the assessment of a customer's expense position. These are fundamentally different to fixed financial commitments. It will also be difficult for lenders to verify and reconcile discretionary expenses and cash withdrawals.
 - Identifying expense transactions across all accounts of a borrower in order to verify will be very onerous and not completely accurate due to inherent vulnerabilities in payment categorisations. Further, in terms of both verification and reconciliation, some expense types fluctuate from week to week (e.g. food) or on a seasonal basis (e.g. power bills), or a borrower may only contribute a portion towards a shared expense.
 - With respect to income, there may also be reasonably explained discrepancies in income due to add-backs or KiwiSaver / tax credits. ASB will where appropriate scale income because of known variances in income types e.g. boarder income, seasonal income.
 - In our view the language of reconciling "any conflict" is overly narrow and could result in minor differences needing to be reconciled, as there is no materiality threshold.

10. Fundamentally, the lender's role is to understand affordability rather than understanding every aspect of customer spend – which customers will find intrusive and inappropriate.

ASB recommends that the regulations allow for a more pragmatic approach to income and expense verification and reconciliation, which supports a level of judgment, supported by skill, robust processes and guidelines.

The Draft Regulations do not recognise a lender's existing relationships with its customers

11. A significant proportion of ASB's consumer lending is to customers who we have an existing relationship with. In the case of home loans, for example, [redacted] of all applications we accept originate from existing customers who are applying for top-ups to their home loans (equating to roughly [redacted]% of all home lending advanced by dollar). For these existing customers ASB can draw on a considerable amount of information on the customer that it can use to undertake affordability and suitability assessments, providing for an efficient and customer-centric lending application process.
12. However, the Draft Regulations are framed on the basis that the lender has no existing knowledge of the borrower, whereby lenders must refresh inquiries of a borrower on each application without the benefit of using information it holds on a customer. This issue is particularly acute in the context of lending to an existing customer of small amounts (for example a small loan to cover an unexpected expense (e.g. car repair costs)) or lending within a short time-period from the time of prior lending (for example a small top-up to a home loan) or a change to a credit card limit where the customers repayment capacity and behaviour is well understood.
13. This approach will inevitably result in (a) frustration from customers regarding the time and effort involved to obtain credit, (b) a perception that the lender does not trust the customer and (c) the feeling that the process has been invasive. This may run the risk that the customer will seek credit elsewhere from less responsible lenders at a significantly increased cost.

ASB recommends that the regulations provide for the lender to utilise existing customer income and expense information (either from transaction account data or previous applications) when conducting affordability and suitability assessments, that the borrower can then validate.

The Draft Regulations do not accommodate technological advances

14. The financial services industry is currently investing significantly in data capture capability that will bring changes to the way people control and share transaction information and data (i.e. Open Banking). Further, a lender's ability to extract insights from transactional and other information it holds on its customers is becoming increasingly sophisticated allowing a lender to have a far better grasp of a borrower's true expense position and to be able to present data to borrowers to discuss and confirm. This will have hugely beneficial implications on the lending application process for both lenders and borrowers.
15. However, given the Draft Regulations will hinder a lender from utilising information it holds on a customer or that it can procure from sources other than the borrower, we are concerned that the benefits that will arise from these technological advancements will not be realised.

ASB recommends that the regulations provide for the lender to utilise existing customer income and expense information (either from transaction account data or previous applications) when conducting affordability and suitability assessments, that the borrower can then validate.

Timeframes to implement

16. The proposed changes require significant uplift to processes, procedures (including training) and systems. This implementation will take time and significant input of resource and expertise. Accordingly, consideration should be given to whether the April 2021 effective date is reasonable, particularly if there are delays in finalising the Draft Regulations.

