CHAPMAN TRIPP

To: The Ministry of Business, Innovation and Employment

On: Exposure draft of the Credit Contracts and Consumer Finance Amendment Regulations 2020

5 February 2020

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INTRODUCTION

This submission is from full service law firm Chapman Tripp, PO Box 993, Wellington 6140. We have offices in Auckland, Wellington and Christchurch.

We would be happy to discuss any of the comments we have made with MBIE.

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Background

1 The Ministry of Business, Innovation and Employment (***MBIE***) has sought feedback on the Exposure Draft of the Credit Contracts and Consumer Finance Amendment Regulations 2020 (the ***Exposure Draft***), which, among other things, requests feedback on:

a. the Credit Contracts and Consumer Finance Amendment Regulations 2020: Draft for Consultation (the ***Draft Amendment Regulations***), which contain certain proposed amendments (the ***Proposed Regulations***) to the Credit Contracts and Consumer Finance Regulations 2004 (the ***Regulations***);

b. the Proposed Regulations contained in the Credit Contracts Legislation Amendment Act 2019 (the ***Amendment Act***);

c. the Credit Contracts Legislation Amendment Act Commencement Order 2020: Draft for Consultation (the ***Draft Commencement Order***); and

d. the proposed requirements for annual returns contained in the Exposure Draft (the ***Draft Annual Return***).

2 The Proposed Regulations will implement aspects of the Amendment Act, and the Draft Commencement Order will bring certain provisions of the Amendment Act into force. Among other things, the Amendment Act amends the Credit Contracts and Consumer Finance Act 2003 (***CCCFA***).

3 We welcome the opportunity to submit on the Exposure Draft, as the issues arising in relation to it are highly relevant to the advice we provide to many of our clients.

4 Our submissions focus on those proposals that we consider could be materially improved, particularly where we are concerned they do not (as drafted) meet the policy intent of the legislation. We also suggest some technical drafting changes.

5 Our submission does not purport to represent the views of any of our clients. We have no objection to our submission being published.

Summary of recommendations

1 Our key recommendations in relation to the Exposure Draft are below. More detail and explanation on each of them is contained in our detailed submissions.

"One size fits all" approach

2 Some of the Proposed Regulations are too restrictive as they take a "one size fits all" approach. The regulations should be flexible to take account of different customers, products and situations, for example, in the minimum standards in regulations 4AA to 4AI and the advertising standards in regulations 4AJ to 4AN.

3 In addition, a lower standard should be allowed in regulations 4AA to 4AI where appropriate.

Minimum standards for affordability

4 The minimum standards for affordability should better reflect the underlying legislative test and relevant case law. For example, materiality thresholds should be added in a number of places to reflect the stated intention that verification is not required of absolutely all income and expenses (e.g. a small amount of interest or dividend income for a well-off borrower).

5 In addition, the process should be consistent with the comments made in *Australian Securities and Investments Commission v Westpac Banking Corporation* [2019] FCA 1244 (*ASIC v Westpac*). The current proposal to use the higher of likely relevant expenses and a reasonable cost for those items and for borrowers to have a "reasonable surplus" left over is not consistent with *ASIC v Westpac*.

6 The Proposed Regulations need to be clear that lenders can rely on information collected from the borrower, to the extent that verification is not required or reasonable. An additional regulation along the lines of section 9C(7) of the CCCFA (which would apply to the extent the regulations do not provide otherwise) is required to enable this reliance.

7 In addition, the requirements in the legislation should be clear and objective due to the consequences of failing to meet the requirements. In particular, the minimum standards in regulations 4AA to 4AI should contain clear and objective requirements.

Agreed variation disclosure

8 Several of the proposed additions to agreed variation disclosure (number of payments, total payments and total interest payable) are problematic outside of initial disclosure, and are likely to cause confusion for borrowers. As such, proposed regulations 4F(2)(f), 4F(2)(h)(ii) and 4F(2)(h)(iii) should be removed.

9 If this submission is not accepted, clarity should be provided as to what is needed to meet these requirements, and how the statutory assumptions should be applied/used to calculate the amount of the total payments and total interest payable for the purposes of agreed variation disclosure. In addition, if proposed regulation 4F(2)(h)(ii) is to remain, the "number of payments" should be replaced with the "number of payments remaining".

Transfer disclosure

10 The proposed amendments to regulation 20 (in relation to transfer disclosure) are unnecessary and inappropriate for transfer disclosure. If they are to be retained, either the change should not apply to existing contract management arrangements or should be delayed until 1 January 2021 at the earliest.

Securitisation and covered bond entities

11 The proposed exception for the directors and covered bond entities needs to go further to cover the common practical scenarios of originating loans in the name of the securitisation vehicle, assigning between securitisation trusts and the appointment of substitute/standby servicers and

clarify the application of the liability regime to directors and senior managers of contract managers.

12 The threshold requirement that the contract management agreements specifically provide for the contract manager to comply with the CCCFA as if it was a creditor should be removed as we do not expect existing arrangements would meet that requirement. If this submission is not accepted, then either the regulations should include a grandfathering provision to protect existing contract management arrangements or the application of regulations 22 and 23 (and, consequentially, section 59B of the CCCFA) should be delayed.

13 A provision should be included in the regulations removing the certification requirements in respect of securitisation or covered bond entities, especially where the contract manager is itself a creditor that has received a certification.

Annual return

14 Given the nature and extent of the proposed content in the Draft Annual Return, consideration needs to be given to the fact that lenders may not have the data available to them in an easily accessible form (particularly for existing loans). We suggest dealing with this by providing an exception for reporting data on existing loans where that data is not readily accessible. In addition, the content covered by the first annual return should only relate to the calendar year after the annual return regulations are promulgated to allow lenders sufficient time to implement any necessary systems changes.

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Section 1: General themes

Issue 1 — One size fits all approach

1 We are concerned that some of the Proposed Regulations are too restrictive as they take a "one size fits all" approach, rather than taking into account differences in consumers and their circumstances, as well as differences in credit products and other situations.

2 For example, the minimum standards for suitability and affordability inquiries (regulations 4AA to 4AI) are extensive and it is questionable whether such an extensive process is appropriate in all cases (e.g. a small, unsecured bank overdraft). However no scaling down is permitted.

3 Given that these are minimum standards that lenders will be required to comply with under section 9C(5A) of the CCCFA, flexibility in the proposed process should be permitted, enabling lenders to adopt a "fit for purpose" approach.

4 This would be consistent in principle with other recent legislation. For example, there was a deliberate policy decision to allow some flexibility in the extent of inquiries required for compliance with anti-money laundering legislation by reference to a risk-assessment (i.e. a risk based approach).

Recommendations:
• provide flexibility in the minimum standards in regulations 4AA to 4AI, including to a lower standard where appropriate to reflect differences in consumers, consumer circumstances, credit products and risks • provide flexibility in the advertising standards in regulations 4AJ to 4AN to reflect differences in advertising channels, credit products and risks

Issue 2 — Use of "reasonable" in minimum standards

5 The minimum standards for suitability and affordability inquiries (regulations 4AA to 4AI) include various requirements to do things "reasonably" or for things to be "reasonable". Examples of this include:

a. regulation 4AE(b)(i) – "allowing a ***reasonable surplus*** to pay or save for other expenses"; and

b. regulation 4AG(1)(e) – the lender must "obtain a credit report, identify from that any other relevant expenses that the borrower is likely to have (for example, financial commitments), and undertake ***reasonable inquiries*** into the amount of those expenses",

(emphasis added).

6 The commentary in the Exposure Draft (paragraph 10) refers to regulations setting "minimum inquiries" (i.e. minimum standards). A failure to meet those minimums results in severe consequences, which have been introduced in the Amendment Act, such as statutory damages of the amount of the interest, credit fees and default fees, and pecuniary penalties. Given the consequences and the fact these regulations are ***minimum*** standards, they should contain clear, objective requirements that lenders can understand and clearly comply with.

7 In addition, as discussed above at paragraphs 2 and 3, a lower standard should be available where appropriate in the circumstances. Otherwise "reasonable" will be interpreted as best practice and lending processes will become time consuming and onerous for both borrowers and lenders.

Recommendations:
• provide clear, objective requirements in the minimum standards in regulations 4AA to 4AI • provide a lower standard in regulations 4AA to 4AI that can be applied where appropriate

Issue 3 — Relying on information provided by the borrower

8 The Proposed Regulations need to be clear that lenders can rely on information collected from the borrower, to the extent that verification is not required or (subject to our comments below at section 2, paragraphs 7 to 9) is not reasonable.

9 This is because section 9C(7) of the CCCFA has been removed without reinserting an equivalent in the Regulations. MBIE stated that they believe not all matters require verification (paragraph 96 of the Officials' Report to the Finance and Expenditure Committee on the Credit Contracts Legislation Amendment Bill of August 2019 (***Officials' Report***)).

10 For this to be the law, it needs to be clear in the compulsory process that some reliance on information provided by borrowers is permitted. Examples of when it is appropriate (and necessary) to rely on information provided by the borrower are:

a. when determining the borrower's requirements and objectives for the loan (i.e. regulation 4AA);

b. in relation to information provided by the borrower about changes to their expenses (regulation 4AG); and

c. when the amount of a type of income or expense is de minimus (e.g. $10 of dividends per annum) (regulations 4AG and 4AF).

Recommendation:
• include an additional regulation along the lines of section 9C(7) of the CCCFA, which applies to the extent the regulations do not provide otherwise

Section 2: Proposed Regulations

Regulation 4AA – borrower requirements and objectives

1 We have the following technical comments on the proposed regulation 4AA:

a. References in regulation 4AA(2) to "determining" information should be to "collecting" information from the borrower. The lender's "determination" is made under 9C(3)(a)(i), instead the regulation contains the process of ***collecting*** information to make that determination. If all of the evidence suggested the borrower's purpose was to buy a car, but they spend the loan proceeds on gambling instead, it is not appropriate to claim that the lender never determined the purpose of the loan.

b. Regulations 4AA(2)(c) and (d) should be combined as alternatives e.g. "the term of the credit or finance, or, if the agreement is a revolving credit contract, whether the borrower requires credit on an ongoing basis". This is because loans do not necessarily have a fixed "term" e.g. many forms of revolving credit, such as credit cards and overdrafts, do not have a fixed expiry date.

c. In regulation 4AA(2)(e), determining "whether the borrower requires those goods or services" should really be whether the borrower "wants" those goods or services. A borrower doesn't necessarily ***require*** insurance, but it can be a good idea.

d. Clarity should be provided about what "additional… services" are intended to be in regulation 4AA(2)(e). While this may be clear in some contexts, such as adding a servicing plan to the financing of a motor vehicle, it is not clear in others e.g. is it intended to cover ATM charges and foreign exchange transactions on credit cards?

Recommendations:
• in regulation 4AA(2), replace "determining" with "collecting" • combine regulations 4AA(2)(c) and (d) as alternatives, as set out above • in regulation 4AA(2)(e), replace "requires" with "wants" • provide guidance outside the regulations about what is meant by "additional… services" in regulation 4AA(2)(e)

Regulation 4AB – borrower requirements and objectives in relation to certain waivers, warranties and insurance

2 These provisions should not apply to any "relevant insurance contract" where the lender is not actually aware of the insurance contract prior to financing it and the insurance contract is actually arranged by the borrower. "Relevant insurance contract" technically includes insurance contracts financed by the lender, but not actually known to the lender, (under section 9B(2)(f) of the CCCFA) e.g. where a borrower uses an eftpos card or electronic transfer to pay for house insurance out of their revolving home loan account.

3 The lender in this situation is not able to comply with any such responsible lending requirements, as they do not actually know about the insurance. Alternatively, an exception could be made for this situation from the definition of "relevant insurance contract" for all responsible lending purposes under the CCCFA, as the CCCFA requirements assume that the lender is able to comply with the legislative requirements, but the extended definition of when insurance is "arranged by the lender", makes it impossible in this situation.

4 Our comments above at section 2, paragraph 1a, in relation to the references to "determining", apply equally to this regulation.

5 As a technical matter, it would be clearer if regulation 4AB(2)(a)(ii) referred to the borrower's circumstances making them at a particularly high risk of being ineligible to make claims. The use of "may" be ineligible in the current drafting is very broad.

Recommendations:
• either exclude certain credit-related insurance paid for by the borrower via eftpos or borrower-initiated electronic transfers from regulation 4AB or from the responsible lending principles generally • in regulation 4AB(2), replace "determining" with "collecting" • redraft regulation 4AB(2)(a)(ii) as set out above

Regulations 4AC to 4AH – minimum standards in relation to affordability

GENERAL COMMENTS

6 These regulations are an example of the "one size fits all" approach we discuss in our general comments.

7 Although the legislative requirement is to make "reasonable inquiries", this has not been carried over to the compulsory minimum requirements, for example by including materiality thresholds.

8 Section 9C(5A) of the CCCFA requires lenders to comply with these regulations. As a result, in the absence of a materiality threshold, the compulsory verification of expenses under regulations 4AF(1)(b) and 4AG(1)(b) is of *all* income and expenses, notwithstanding MBIE's comments at paragraph 96 of the Officials' Report.

9 Therefore, materiality thresholds need to be included for consistency with the underlying legislation, particularly given the severe consequences and penalties for failing to meet these responsible lending requirements. Examples of where an appropriate materiality / relevance threshold needs to be included are:

a. in regulation 4AE(a), "reasonably foreseeable time period" should be expressly capped at the term of the loan;

b. regulation 4AF(1)(b) should have a materiality threshold so that lenders do not have to verify ***all*** income, notwithstanding its immateriality (for example $10 per annum of dividend income for a well-off borrower);

c. regulation 4AG(1)(b) should have a materiality threshold so that lenders do not have to verify ***all*** expenses, notwithstanding their immateriality;

d. regulation 4AG(1)(b) should not require lenders to obtain statements for bank accounts into which immaterial amounts of income are received or transferred; and

e. regulation 4AG(1)(c) should have a materiality/reasonableness threshold for inquiring about cash withdrawals (for example, a $20 withdrawal is irrelevant in the context of a large income) for consistency with paragraph 51 of the Exposure Draft, which states that further inquiries are required in relation to ***significant*** cash withdrawals.

10 Additional flexibility is required to allow for non-standard situations or borrowers that do not fit within a "one size fits all" approach, or for which it is not appropriate. For example:

a. a lower standard should available for existing customers (except in relation to high-cost consumer credit contracts);

b. regulation 4AG(1)(b) needs to cater for people who do not receive their income into a bank account (e.g. receive cash income); and

c. regulation 4AG(1)(e), we query whether a credit report is always available (some people don't have a credit history).

11 If the requirement for a reasonable surplus is to be retained in regulation 4AE, paragraphs 5.2 and 5.3 of the Responsible Lending Code should be updated so that there is no doubling up of buffers.

REG 4AH(2) – LENDER MUST USE THE HIGHER OF LIKELY RELEVANT EXPENSES AND A REASONABLE COST FOR THOSE ITEMS

12 The relevant lender responsibility is that the lender must "***make reasonable inquiries, before entering into the [loan contact], so as to be satisfied that it is likely that the borrower will make the payments under the [loan contract] without suffering substantial hardship***".

13 According to the Responsible Lending Code, "To meet this lender responsibility, a lender should be satisfied that it is likely that the borrower will make the payments under the agreement without undue difficulty as well as:

a. meet necessities (such as accommodation, food, utilities, transport, required medical expenses); and

b. meet other financial commitments (such as repayments on existing debts),

without having to realise security or assets (other than any security or assets that the borrower is, at the time of approval, willing and intending to dispose of or realise the value of)."[1]

14 In ***ASIC v Westpac***, comments were made that law does not require a lender to take the higher of the declared living expenses and the statistical figures (in that case the Household Expenditure Measure benchmark numbers). As Perram J stated in ***ASIC v Westpac***, the inquiry about whether making the loan repayments will put the consumer in circumstances of substantial hardship, does not require a lender to know what the declared living expenses of the consumer are.

> *…the only way that one or more declared living expenses can be shown to be* necessarily *relevant to the issue of whether the consumer can afford to make the repayments is by identifying some living expenses which simply cannot be foregone or reduced beyond a certain point. For example, everyone has to eat so there must be an amount for food which is the minimum which can conceivably be spent. But that minimum is an entirely different concept to the declared living expense of what the consumer actually spends on food. Indeed, knowing how much the consumer actually spends on food does not tell one anything about that conceptual minimum. I may eat Wagyu beef everyday washed down with the finest shiraz but, if I really want my new home, I can make do on much more modest fare. Knowing the amount I actually expend on food tells one nothing about what the conceptual minimum is. But it is that conceptual minimum which drives the question of whether I can afford to make the repayments on the loan.*[2]

15 However, proposed regulations 4AE and 4AH require lenders to use the ***higher*** of the reasonable cost for an item (e.g. based on statistical information) and the borrower's declared living expenses, and to have a reasonable surplus. This approach is not consistent with the relevant Australian case, ***ASIC v Westpac*** discussed above. The test contained in the Proposed Regulations does not determine whether the borrower is able to meet payments under the loan contract without suffering substantial hardship, but rather that the borrower is able to meet payments under the loan contract and retain their desired lifestyle (i.e. with no hardship at all). In addition, if a borrower has a clear history of buying less expensive food than the average, why should they be assessed as paying the higher average amount? If the test is to change in the way proposed, this should be achieved by amending the lender responsibility principle in the CCCFA itself, rather than through regulation.

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1 *Responsible Lending Code* (revised June 2017), para 5.1.

2 *ASIC v Westpac Banking Corporation* [2019] FCA 1244 at para 76.

REG 4AH(3) - DEFINITION OF "REASONABLE COST OF EXPENSES"

16 We assume that MBIE have confirmed that the commercially available statistical information takes account of all of the listed relevant matters in the definition of a reasonable cost of expenses, particularly the ages of the dependent children.

17 Guidance should be given, potentially outside the regulations, as to what level of granularity is intended by "the location in which the borrower lives". For example, is it "urban", "Greater Auckland", "South Auckland" or a particular suburb of South Auckland?

Recommendations:

- in regulation 4AE(a), cap the "reasonably foreseeable time period" at the term of the loan
- regulations 4AF(1)(b) and 4AG(1)(b) should include materiality thresholds for verification of income and expenses
- regulation 4AG(1)(b) should not require lenders to obtain statements for bank accounts into which immaterial amounts of income are received or transferred
- regulation 4AG(1)(c) should have a materiality threshold for inquiries
- remove the requirement to use the ***higher*** of likely relevant expenses and a reasonable cost for those items
- remove the requirement for a "reasonable surplus"
- allow flexibility for non-standard borrowers or situations
- allow a lower standard for existing customers (except in relation to high-cost consumer credit contracts)
- provide guidance outside the regulations about the level of granularity intended by "the location in which the borrower lives"

Regulations 4AJ to 4AN – advertising standards

18 Given the extent of information required to be contained in advertisements that provide any concrete information about the lender's products, it is not possible to have all required information on the front of a small click-through website ad (such as those used in website banner or margin advertisements).

19 Therefore, it would be helpful if there was an exception from the regulation 4AL requirements for certain small click-through website ads that take you to full disclosure after clicking. This could be limited to the situation where the initial part of the ad shows an annual interest rate or range of interest rates, and the rest of the information contained by regulation 4AL(2) (including the relevant class(es) of contract) were on the landing page. This situation illustrates the difficulties with the "one size fits all" approach taken in the regulations (the first issue in our general comments).

20 For ease of assisting readers and ensuring they are not misled, the example provided in regulation 4AL should meet ***all*** of the relevant requirements set out in the advertising standards. As currently drafted, the example meets the requirements of regulation 4AL(2)(e), but breaches the requirements of regulations 4AL(2)(b) and 4AL(2)(d).

REGULATION 4AN – PROHIBITED ADVERTISING PRACTICES

21 We do not disagree with the proposal in regulation 4AN(a) to ban "15-minute approvals" from advertising as, while we do not believe that it is impossible for an approval to be made within 15 minutes, it is unlikely to be achievable for all borrowers of a lender.

22 However, we have some concerns about the basis for the ban as the Exposure Draft commentary (at paragraph 83) assumes that every loan should be considered by a human appraiser with

personal interrogations of the borrower. We do not believe that that should be a requirement in all cases. If appropriate questions are asked online and full, complete and verified information is provided by the borrower and reliably electronically reconciled, no human intervention is required.

23 Regulation 4AN(c) should be reworded as it mixes two different concepts and could be interpreted as banning a lender from telling a customer that their loan has been approved (after taking into account the required inquiries) and inviting the customer to enter into the relevant contract or variation. To meet the intention of the proposed ban, the Proposed Regulation should be split as follows:

(c) "that a loan has already been approved if the inquiries required by section 9C(3)(a) have not been completed:

(d) that a loan is available to the customer, if the credit contract has not been entered into or varied (as applicable) (for example, "$500 credit available in your account")."

Recommendations:

- provide an exception from the regulation 4AL requirements for small click-through website ads where the initial part of the ad shows an annual interest rate or range of interest rates and the remainder of the 4AL matters are on the landing page
- redraft the example in regulation 4AL to comply with all relevant requirements, as set out above
- split regulation 4AN(c) into two paragraphs, as set out above

Regulation 4F - disclosure of agreed changes

24 We understand that MBIE would like additional information disclosed on an agreed variation. However, we believe that the proposal goes further than is helpful to customers in all but the simplest of scenarios. Several of the proposed additional disclosure items for agreed variations (such as the number of payments, total payments and total interest payable) are problematic outside of initial disclosure, and are likely to cause confusion for borrowers.

25 In addition, the requirements make it difficult to show information before and after the change without being confusing (see section 2, paragraphs 29 and 32 for examples of this). Additional, likely lengthy, explanation would be required to make sense of what is being disclosed, when it would be preferable for disclosure be simple and concise. As a result, 'before change' information is likely to be omitted from agreed variation disclosure – which is less helpful to customers.

26 In addition, some of these requirements (particularly, total interest payable and total payments), are based on statutory assumptions that were not written to apply to variation disclosure, and it is unclear how they would apply to a variation e.g. should the "past" portion of the calculation be based on actual amounts or assumed ones? If assumptions are used for the pre-variation portion, it is misleading for customers in relation to what has already occurred. Given the severe consequences if numbers disclosed in the agreed variation disclosure are less than perfect and the risk of being misleading (and therefore in breach of the obligation that disclosure be clear), this lack of clarity is undesirable.

REG 4F(2)(F) AND 4F(2)(H)(III) - TOTAL INTEREST PAYABLE AND TOTAL PAYMENTS

27 As discussed above, we do not believe that the proposals in regulations 4F(2)(f) and 4F(2)(h)(iii) are helpful to borrowers after the start of the contract. If these are to remain, it should be clear how the calculations should deal with the difference between what has actually occurred prior to the variation and the initial disclosure estimate provided at the outset (e.g. it would appear that the current proposal is to ignore these, which then requires explanation to the customer to ensure the disclosed information is not misleading or confusing).

28 Initial disclosure can be based on the statutory assumptions set out in Schedule 1 of the Regulations. As a result, the disclosed total interest payable and total payments are not

necessarily the actual amounts payable by the borrower. Those assumptions (for example, that every day is a business day and that the variable interest rate disclosed will not change[3]) are unlikely to be true in practice. The variation disclosure regulations do not make it clear:

a. how the calculations should deal with the difference between what has actually occurred prior to the variation and the assumptions-based calculations for the period from initial disclosure to immediately prior to the variation (for example if a variable interest rate had changed);

b. how the assumptions in Schedule 1 of the Regulations should apply to these calculations; and

c. how/whether lenders should explain to customers that the disclosed numbers are not necessarily a result of the variation and that the pre-variation number was merely the initial estimate (or whether a new 'before change' calculation is effectively required).

29 The following example disclosure of "total interest payable" and "total payments" demonstrates some of the issues with this proposal. It is based on a scenario of a variable interest rate loan of $16,000 which was initially disclosed as 5% per annum, was unilaterally varied to 4.5% per annum after 6 months and a year later fixed by the borrower at 4.8% per annum for two years. The initial disclosure was of total payments of $18,900 and total interest payable of $2,900. Two different interpretations of what should be disclosed for the second variation are:

Interpretation 1:

	Before change	**After change**
Interest rate	4.5% per annum variable	4.8% per annum fixed for 2 years
Total payments	$18,900	$18,642
Total interest payable	$2,900	$2,642

Interpretation 2:

	Before change	**After change**
Interest rate	4.5% per annum variable	4.8% per annum fixed for 2 years
Total payments	$18,414	$18,534
Total interest payable	$2,414	$2,534

As demonstrated by that example, the total payments and total interest payable numbers differ depending on the interpretation of the uncertain requirements in the regulations. Two possible interpretations are:

- Interpretation 1: Under the statutory assumptions, it appears that the change to 4.5% should be ignored, along with any differences resulting from payments being due on non-business days – this gives a falsely high picture of the amount of the total payments and total interest payable once the interest rate is varied by agreement; or

- Interpretation 2: Use actual numbers for the interest and payments prior to the change. If the actual numbers are used in the 'before' picture, the customer has not seen those numbers before. In addition, using actual numbers for part of the calculations may be too complex for lenders, given that their calculators would have been created for initial disclosure.

If the 'before' information is omitted due to it being impractical to not mislead or deceive the customer, then a customer would need to compare the total interest payable and total payments with those in their initial disclosure. In this example, the customer's interest rate has actually

[3] Paragraphs 2 and 1(b) of Schedule 1 of the Regulations respectively.

increased (from 4.5% to 4.8% per annum), but their disclosed total payments and total interest payable *decrease* (from $18,900 to $18,534 and $2,900 to $2,534 respectively).

REG 4F(2)(H)(II) – NUMBER OF PAYMENTS

30 We query whether this requirement is of use to customers or whether it will just confuse customers. There are several issues with this proposal – whether the ***scheduled*** 'number of payments' is intended to be disclosed (and whether that is actually relevant to customers) and whether disclosing the 'number of payments remaining' would be clearer for customers.

31 The 'number of payments' is a function of the payment frequency and the term – if the term does not change as a result of the variation and instead the contract may be repaid in full early (for example, because that is what the terms and conditions of the contract provide), the 'number of payments' is either:

a. the number of payments that would be made over the ***scheduled*** term, which is not be of any particular relevance to the customer;

b. the actual number of payments the customer will make to repay the loan (ignoring the term and the contract), which may later cease to be accurate, due to other changes (including unilateral variations).

Which of these is required to be disclosed as part of the variation disclosure is unclear. This uncertainty is undesirable given the severe consequences of an interpretation error.

32 Some issues with the proposal are improved by requiring the 'number of payments remaining' to be disclosed if a 'number of payments' type disclosure is to be retained. For example, if a borrower was originally to make 24 fortnightly payments of $300 and varied their payment frequency to weekly payments of $150 after 7 payments had been made, the total number of payments varies from 24 to 41. Below is how the number of payments may appear in that disclosure:

	Before change	**After change**
Payment frequency	fortnightly	weekly
Payment amount	$300	$150
Number of payments	24	41

As you can see from the above example, complying with these rules makes it appear that there are 41 payments of $150, which is not correct – there are 7 payments of $300 and 34 of $150.

33 As such, explanation would be required from the lender to try to ensure that the disclosure was not misleading, deceptive or confusing, or the 'before' information would need to be omitted, resulting in a less helpful disclosure for customers. Using a 'number of payments remaining' disclosure is clearer and more useful for borrowers in this situation than the 'number of payments'.

REG 4F(2)(H)(IV) – FIRST PAYMENT DUE

34 As a minor technical point, the reference in regulation 4F(2)(h)(iv) to "when the ***first*** payment is due" should be to "when the next payment is due" or "when the next payment after the change is due".

Recommendations:

- remove proposed regulations 4F(2)(f), 4F(2)(h)(ii) and 4F(2)(h)(iii). If this submission is not accepted, then (a) clarity should be provided as to what is needed to meet these requirements and how the statutory assumptions should be used to calculate the amount of the total interest payable and total payments
- if proposed regulation 4F(2)(h)(ii) is to remain, replace the "number of payments" with the "number of payments remaining"

- in regulation 4F(2)(h)(iv), replace "first" with "next"

Regulation 5A – disclosure about dispute resolution and financial mentoring services

35 As further discussed below at section 2, paragraphs 49 and 50 in relation to the equivalent issues with the proposed debt collection disclosure:

a. We have the following drafting points for clarity:

i. the requirements set out in regulations 5A(5)(b) and (c) should be redrafted as:

"(b) an explanation of the service that the dispute resolution scheme provides:

(c) that the dispute resolution scheme will not charge a fee to any complainant to investigate or resolve a complaint"

ii. the reference in regulation 5A(6)(c) to ***a link to MoneyTalk's*** Internet site should be replaced with a requirement that is neutral as to the manner of disclosure e.g. "*MoneyTalk's* website address", as the existing requirement cannot be complied with if the disclosure is sent by post.

b. Guidance should be given about what MBIE intends will be disclosed as "an explanation of what that [dispute resolution] scheme provides" (regulation 5A(5)(b)).

Recommendations:

- redraft regulations 5A(5)(b) and (c) as set out above
- in regulation 5A(6)(c), replace "a link to *MoneyTalk's* Internet site" with "*MoneyTalk's* website address"
- provide guidance outside the regulations about what is meant by "an explanation of what that [dispute resolution] scheme provides"

Amendment to regulation 20 – change to contract manager role

36 The proposed changes to regulation 20, to require contract managers to agree to comply with the CCCFA as if they were a creditor, are redundant and would unnecessarily increase compliance costs for all existing contract management arrangements.

37 Borrowers are currently adequately protected through Condition D of regulation 20(5), which requires the contract manager to either be a creditor or to have submitted to a dispute resolution scheme that is able to resolve complaints against the contract manager as if it was a creditor. This already permits borrowers to pursue complaints against the contract manager in line with ordinary processes.

38 We further note that adding such a provision is not directly relevant to the purpose of Regulation 20. Regulation 20 is permissive and sets requirements for transferring loans without notice in securitisation situations; creditors are free to assign receivables without complying with Regulation 20 by providing notice to the relevant borrower. It is not clear how the additional contractual provisions are directly relevant to providing (or not providing) notice to the borrower.

39 Further, given that contract management agreements are private contracts between the transferring creditor and the contract manager, borrowers are not in a position to enforce such contracts, regardless of such provisions. They would obtain no protection from the proposed additional requirement (and already receive adequate protection as described above).

40 By contrast, such an additional documentation requirement may significantly increase compliance costs for existing securitisation arrangements. Before the first transfer of a receivable after the implementation date, the transferring creditor would need to review each of its contract management agreements, potentially renegotiate the agreement to include such additional language, and (if changes are required) potentially seek funder and/or trustee consent and additional legal opinions. This is made even more difficult given the short proposed implementation time (1 June 2020 effective date) and the many other changes made to lenders' compliance requirements by the Amendment Act and the Draft Amendment Regulations.

41 If, despite our submission above, this additional requirement is retained then:

a. it should be made absolutely clear (potentially through external guidance) that the provision is not intended to have retrospective effect, as few (if any) existing contract management agreements will currently include such language; and

b. either:

i. a grandfathering clause (similar to the current regulation 20(7)) should be included to provide that existing contract manager arrangements do not have to be amended to include this additional provision; or

ii. the implementation date should be extended until at least the start of 2021 to allow sufficient time to review existing documents and make appropriate changes, if necessary.

Recommendations:

- remove the proposed changes to regulation 20 as unnecessary. If this submission is not accepted, then:
  - provide guidance to confirm no retrospective application, to provide existing securitisation arrangements with appropriate comfort, and
  - either:
    - include a grandfathering provision to protect existing contract management arrangements; or
    - in regulation 2(1) of the Draft Amendment Regulations, replace "1 June 2020" with "1 January 2021" or later

Regulations 22 and 23 - securitisations and covered bond programmes

DUE DILIGENCE DUTY

42 We support the general intention of regulations 22 and 23, to apply section 59B to the contract manager rather than the creditor in certain situations. However, in our view there are a number of practical situations that are not currently adequately addressed in the drafting and that should be clarified:

a. In a number of existing securitisation structures, consumer credit contracts may be originated directly in the name of the securitisation vehicle as lender of record, as a matter of convenience. Regulation 22 should also capture these situations where there is no transfer, but a contract management agreement applies from the moment of origination onwards.

b. Another common scenario is the transfer of loans between securitisation vehicles in the same structure, for instance from an initial 'warehouse' trust funded by a bank lender, to a separate trust for funding by external investors. Regulation 22 should also be clear that it applies where the transfer is from an intermediate transferee rather than directly from the original "person who provides credit under [the] consumer credit contract", provided the

proposed contract manager requirements in regulations 22(2)(b) and (c) continue to be met.

c. It would be helpful to clarify how regulations 22 and 23 are intended to apply to substitute servicers, or standby servicers that have stepped in after a failure of the original servicer (i.e. contract manager). In those circumstances, we expect that section 59B should cease to apply to the original servicer/contract manager, and should instead apply to the substitute/standby servicer for actions taken (or omitted to be taken) after the date of appointment. However, this is not entirely clear under the current drafting and parties would benefit from certainty.

d. For completeness, the regulation should also permit parties to contract out of its application even where the requirements of regulation 22(2) are otherwise met. There may be structures that meet the set tests, but where it is more appropriate for the new creditor's directors to remain liable (and where the parties explicitly agree on this).

e. The drafting of regulation 23 should be clarified, as there is currently some uncertainty as to how section 59B applies in the context of regulation 23. Section 59B(4) refers to the "section appl[ying] as stated in the regulations". This may be read as inferring that the regulations should set out the adapted form of section 59B in full in such cases. In particular, it becomes unclear whether section 59B(2)(b) (which is not repeated in the regulations) applies in the context of a securitisation.

f. Proposed regulation 23(b)(i) is currently overly broad, as it refers generally to ensuring that duties and obligations of "a creditor" under the CCCFA are complied with. To align with section 59B(1), we submit that this should refer to the duties and obligations of the "new creditor" and/or the contract manager (on the basis that the contract manager is required to manage the contracts as if it were the creditor).

g. In relation to proposed regulation 23(b)(ii), under section 59B(2)(a) both size and nature of the credit provided are examples of the nature of business which should be taken into account. However regulation 23(b)(ii) seems to make the nature of the consumer credit contracts a separate criteria that needs to be taken into account, independent of the contract manager's business (e.g. its size). It is not entirely clear whether this is intended to be a different set of criteria to those set out in section 59B(2)(a).

h. As drafted, an order may be made against the new creditor (as defined in proposed regulation 22), with the directors and senior managers of the contract manager also being jointly and severally liable with that new creditor (section 116A, section 59B and proposed regulation 23). Given the importance of certainty of liability for directors, we submit that further guidance or other clarification be provided to give comfort that liability of the directors/senior managers would still be assessed against the contract manager's business in this case (proposed regulation 23(b)(ii)), despite the fact that the new creditor's liability may be assessed against the new creditor's (potentially smaller) business.

i. More broadly, we consider that there is a potential risk that making the directors and senior managers of one entity (i.e. the contract manager) jointly and severally liable for the actions of another person (i.e. the creditor) to whom the directors and senior managers do not owe any direct corporate fiduciary duties or statutory duties could be challenged as being contrary to corporate legal principles. For example, it is not clear how making directors of the contract manager jointly and severally liable for the actions of the creditor sits with the directors' duties to act in the best interests of the contract manager (or its holding company) under section 131 of the Companies Act 1993 or other aspects of the directors duties in Part 8 of the Companies Act 1993 in situations where there may be a tension between what is in the best interests of the contract manager and the obligations of the creditor.

j. Given this, we question whether it would be more appropriate if the liability of the directors and senior managers of the contract manager is dealt with using a liability regime that the market is already familiar with, such as the extended liability regime under the Financial Markets Conduct Act 2013 (*FMCA*). In particular, this provides a mechanism for persons that do not owe direct fiduciary or statutory duties to an issuer to be held liable for that issuer's compliance through the "involved in a contravention" regime in subpart 3 of Part 8 of the FMCA.

43 In respect of proposed regulation 22(2)(c)(ii), we also repeat our submission in respect of proposed regulation 20 above. That is, the requirement that the contract management agreement specifically provides for the contract manager to comply with the CCCFA as if it was a creditor be removed.

44 As noted above, our understanding is that few (if any) existing contract manager agreements meet this requirement and therefore the vast majority of them will need to be amended. Given the number of parties and the required approval processes, the process for amending such arrangements could be prolonged. As such, if regulation 22(2)(c)(ii) is to be retained in its current form, regulations 22 and 23 (and consequentially section 59B of the CCCFA itself) need to be delayed to allow a reasonable time to make the necessary changes - until at least the start of 2021, or a grandfathering clause should be included to provide that existing contract manager arrangements do not have to be amended to meet this requirement.

45 Lastly, the explanatory note in the Draft Amendment Regulations contains an error on the last page in that it states that "regardless of whether the circumstances prescribed in ***new regulation*** *22* are met… section 59B of the Act also applies to the directors and senior managers of the creditor". That statement is incorrect as the exception in section 59B is intended to, and does, make the contract manager's directors and senior managers liable ***instead of*** those of the securitisation or covered bond entity which is the actual creditor.

CERTIFICATION REQUIREMENTS

46 In addition, we propose that a new regulation 23A should also be included to provide a similar exemption from certification requirements of the new Part 5A of the CCCFA for the securitisation or covered bond entity (using the power in section 138(1)(da)(iii) and/or 138(hb)(i) of the CCCFA).

47 In particular, we consider it inappropriate for securitisation or covered bond entities to have to go through the certification process if their consumer credit contracts are managed by a creditor that has received a certification. In this regard we note that the new creditor's directors and senior managers are not subject to the section 59B duties regime, which would be a key factor in the context of the certification process under section 131G of the CCCFA.

Recommendations:

- clarify the application of regulations 22 and 23 (including in the common practical scenarios of originating loans in the name of the securitisation vehicle, assigning between securitisation trusts, the appointment of substitute/standby servicers and the application of the liability regime to directors and senior managers of contract managers), as described in section 2, paragraph 42 above
- remove the requirement that the contract management agreements specifically provide for the contract manager to comply with the CCCFA as if it was a creditor. If this submission is not accepted, then:
  - provide guidance to confirm no retrospective application, to provide existing securitisation arrangements with appropriate comfort, and
  - either:
    - include a grandfathering provision to protect existing contract management arrangements, or

- in regulation 2(1) of the Draft Amendment Regulations, replace "1 June 2020" with "1 January 2021" or later
- correct the explanatory note to the Draft Amendment Regulations in respect of new regulation 22
- include an additional equivalent provision removing the certification requirements of the new Part 5A of the CCCFA in respect of securitisation or covered bond entities

Regulation 24 - debt collection disclosure

48 Regulation 24(1)(c) should be removed as the content required in the debt collection disclosure should not include the purpose of the loan. The purpose of the loan will often not be known (e.g. because the information was not required to be known at the time the loan was entered into or is not required to be known under the current CCCFA (e.g. the purpose of a credit contract that is not a consumer credit contract)). Even if the purpose of the loan was known, unlike other of the required information, knowing the purpose of the loan is neither necessary nor helpful to the debt collection process or the customer.

49 Guidance should be given, possibly outside of the Proposed Regulations, about what MBIE intends will be disclosed as "an explanation of what that [dispute resolution scheme] service provides" (regulation 24(1)(f)(iii)). For example is it something simple such as "this is a service that can help you resolve complaints with us" or something more detailed? A model disclosure statement for debt collection disclosure may assist in providing this guidance.

50 We also have the following drafting points for clarity:

a. the introductory wording in regulation 24(1) should be redrafted as "So much of the following information as is applicable is the information that must be disclosed under section 132A of the Act concerning the contract". The current drafting of the introduction is difficult to follow given the number of concepts in it; and

b. the requirements set out in regulations 24(1)(f)(iii) and (iv) should be redrafted as:

"(iii) an explanation of the service that the dispute resolution scheme provides:

(iv) that the dispute resolution scheme will not charge a fee to any complainant to investigate or resolve a complaint:"

c. the reference in regulation 24(1)(h) to ***a link to MoneyTalk's*** Internet site should be replaced with a requirement that is neutral as to the manner of disclosure e.g. "*MoneyTalk's* website address", as the proposed requirement cannot be complied with if the disclosure is sent by post; and

d. the statement about the debt to be disclosed under regulation 24(3)(c) should continue on to say ", to the extent that those rates are ascertainable at the time of disclosure" as many of these will not be known at the time (e.g. if the debt collection disclosure is made by the original creditor, but the debt may later be sent to an external debt collector).

Recommendations:

- remove proposed regulation 24(1)(c)
- provide guidance outside the regulations about what is meant by "an explanation of what that [dispute resolution scheme] service provides"
- redraft the introductory wording in regulation 24(1) as set out above
- redraft regulations 24(1)(f)(iii) and (iv) as set out above
- in regulation 24(1)(h), replace "a link to *MoneyTalk's* Internet site" with "*MoneyTalk's* website address"

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- in regulation 24(3)(c), add ", to the extent that those rates are ascertainable at the time of disclosure" at the end of the proposed wording

Section 3: Draft Commencement Order

1 The section references in the Amendment Act have changed from those referred to in the Draft Commencement Order. We assume that these will be updated in the final Commencement Order.

Clauses 2(2)(a) and 3 – reliance on information provided

2 The Amendment Act removes a lender's ability to rely on information provided by a debtor or guarantor in relation to assessing affordability and suitability of a credit product by repealing section 9C(7) of the CCCFA. Under the CCCFA currently, a lender can rely on that information unless they have reasonable grounds to believe the information is not reliable.

3 When verification is (or is not) required should then be covered by the Regulations (with some further non-binding guidance in the Responsible Lending Code). The repeal of section 9C(7) of the CCCFA by section 10(7) of the Amendment Act should not occur until those regulations are in force. However, section 9C(7) of the CCCFA is currently due to come into force on 1 June 2020 (clause 3 of the Commencement Order), rather than 1 April 2021 when the Proposed Regulations will come into force (clause 2(2) of the Draft Amendment Regulations). Delaying the repeal of 9C(7) to 1 April 2021 is consistent with MBIE's recommendation in the Officials' Report at page 51.

Clauses 2(2)(a) and 3 –duty of directors and senior managers

4 As discussed above at section 2, paragraphs 43 and 44, if regulation 22(2)(c)(ii) is to be retained in its current form with no grandfathering of existing contract manager arrangements, sufficient time to amend the relevant arrangements is required. As a result, section 59B of the CCCFA should not come into force until 1 January 2021 or later.

Recommendations:
• delay repeal of section 9C(7) of the CCCFA until 1 April 2021 • if regulation 22(2)(c)(ii) is to be retained with no grandfathering of existing contract manager arrangements, section 59B of the CCCFA should not come into force until 1 January 2021 or later

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Section 4: Draft Annual Return

PROPOSED CONTENT

1 The specific content of the Draft Annual Return is not something we are generally able to comment on, although the requirements do appear to be excessive. This is also an example of our first general theme (of taking a "one size fits all" approach), as some of this data appears to be aimed at lower tier lenders, but will be required from all lenders.

2 We recommend that the proposed information requirements are clarified and made consistent with terminology used in the CCCFA. For example, 'consumer credit' is not a defined term in the CCCFA.

3 If the intention is to obtain data on all credit contacts entered into by a creditor (despite the requirement for an annual return only being triggered under section 116AAA(1) of the CCCFA if the creditor is a creditor under a consumer credit contract), this should be made very clear in the content requirements for the annual return. We note that creditors may have a mix of consumer credit contracts, non-consumer credit contracts and other business (for example, the taking of deposits). We expect that it is the first of these that are of interest to the Commerce Commission, given that only creditors under consumer credit contracts are required to provide annual returns. As such, where the current proposals are unclear as to whether the required content relates to consumer credit contracts, all credit contracts, the lender's whole business or something else, that should be clarified.

4 Examples of proposals which should be clarified if they are to be retained are:

a. paragraph 133 of the Exposure Draft should be clear that the annual interest rates referred to are standard (and not default) interest rates;

b. paragraph 134 of the Exposure Draft should be clear as to whether "refinanced" means refinanced with the applicable creditor (perhaps including their associates), or whether it means refinance with *any* creditor;

c. paragraph 136 of the Exposure Draft refers to the 'average term of a loan' – it should be clear that the relevant 'loans' are consumer credit contracts. In addition, it seems more useful for this information to be an average for each loan type (e.g. personal loan terms averaged separately to those for home loans). Doing otherwise would skew the results, given that different types of loans have very different terms;

d. paragraphs 156 and 157 of the Exposure Draft refers to "hardship" applications – these references should be to "unforeseen hardship" applications for consistency with the language used in the CCCFA;

e. paragraphs 158 and 159 of the Exposure Draft refers to the "number of *loans* for which there was a guarantor" and "number of *loans* where the guarantor was asked to repay debt" – presumably these "loans" are intended to be "consumer credit contracts", rather than all loans; and

f. paragraphs 160 and 161 of the Exposure Draft refers to "The number of complaints made to the creditor in the period" and "The number of complaints that were resolved internally in the period" – given that the annual return is in the CCCFA, the relevant complaints should be those in relation to consumer credit contracts, rather than those in relation to other products, such as deposits or transactional banking services.

PROPOSED TIMING

5 We note that the annual return could effectively be retrospective as the proposal is for the new section 116AAA to come into force on 30 June 2020, despite being a late addition to the Amendment Act. Given that the annual return is proposed to be for the preceding calendar year, this provision could be used to require an annual return by 31 July 2020 that covers content for the period 1 January 2019 to 31 December 2019. This timeframe is likely to be too short to

enable all lenders to obtain and gather the relevant information once the requirements are settled and the relevant regulations are promulgated. Instead, we propose that the annual return regulation not come into force until lenders have sufficient time to gather and calculate the required information (as it may be possessed by lenders, but not recorded in an easily accessible way to produce the annual return). As such, the content covered by the first annual return should only relate to the calendar year ***after*** the relevant regulations are promulgated.

6 Practically systems issues may arise with obtaining the required data, particularly for lenders with high volumes of loans, as their systems may not have been set up to report on all of the information contained in the Draft Annual Return. Even where changes are made to systems to capture this data in a usable way, it is unlikely that all of that data would be easily obtainable for pre-existing loans. As such, MBIE should consider providing an exception for reporting data on existing loans where that data is not readily accessible.

Recommendations:

- consider limiting the annual return content requirements
- use existing CCCFA language, for example:
  - in paras 136, 158 and 159 of the Exposure Draft, "loans" should be "consumer credit contracts"
  - in paras 156 and 157 of the Exposure Draft, "hardship" applications should be "unforeseen hardship" applications
- clarify the data requirements, for example:
  - para 133 of the Exposure Draft should refer to are standard (and not default) interest rates;
  - in para 134 of the Exposure Draft, clarify whether "refinance" means refinance with the applicable creditor (perhaps including their associates), or with ***any*** creditor
  - in para 136 of the Exposure Draft, the "average term" should be split into different loan types
  - paras 160 and 161 of the Exposure Draft should refer "complaints in relation to consumer credit contracts"
- ensure the content covered by the first annual return only relates to the calendar year after the annual return regulations are promulgated
- consider providing an exception for reporting data on existing loans where that data is not readily accessible

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