European Financial Services Limited

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

European Financial Services Limited and Euro Rate Leasing Limited ('EFS' 'We') appreciate the opportunity to submit its view relating to the draft regulations and the discussion document released alongside it.

We also thank the Ministry for the time it allotted EFS by way of teleconference, in hearing EFS's concerns around the draft regulations and how it will specifically affect EFS. As an aside we are an active member of the Financial Services Federation and we support their comprehensive submission on the above draft regulations.

EFS is a motor vehicle finance company. It was established over 15 years ago. EFS is wholly owned by the Giltrap Group. We only provide finance to those customers who purchase or lease certain European motor vehicles, which our related entity distributes in NZ. This includes Audi, Volkswagen, Skoda and Porsche.

We rely on our customers repaying their loan without defaulting; therefore it is in our best interest to ensure we know our customers can meet their repayments. We do this by looking at affordability and suitability before they take up the loan (or lease), and for the duration of the loan. We also provide our customers with information that enables them to make an informed decision about our products.

We comply with the Consumer Credit Contract Finance Act 2003 (CCCFA) and the Responsible Lending Code(RLC) as it ensures our business model will continue to be successful and further, it makes certain we are acting morally as a responsible lender when engaging with our customer; this is of upmost importance to our shareholders.

The requirements of the CCCFA 2003 and RLC have been met continuously by EFS. Of course, if all lenders complied with the CCCFA and the RLC there would be no need for the 2015 changes to the CCCFA and the proposed draft regulations. Those lenders, who practice predatory and irresponsible lending targeting vulnerable credit users, are, we believe, the exception rather than the norm.

The draft regulations aim to reduce irresponsible and predatory lending and the resulting customer harm. We agree and are very supportive of the fact that more needs to be done to tackle this type of behavior and to safeguard those that are vulnerable users of credit. We look forward to seeing the results of the Commerce Commissions further powers of enforcements in dealing with these types of lenders.
However, we have a number of concerns regarding the highly prescriptive draft regulations as it relates to financiers such as EFS. We set these out below.

The unworkability of the one-size fits all approach

The draft regulations have been developed to deal with, we believe, a small section of the lending industry. The majority of lenders are already responsible lenders and are subject to stringent obligations. Under the draft regulations, responsible lenders are effectively being tarred with the same brush as those exploiting the vulnerable and embracing predatory lending behavior.

Our customers are also being tarred with the same brush by default as the draft regulation takes a "one size fits all' approach presuming all borrowers are vulnerable users of credit. This is not the case. They are well informed borrowers who make their choices around why, when and if to use credit and with who – very different to the vulnerable users of credit. Our customers are "well informed users of credit' as defined in the RLC. The draft regulations will subject those well-informed users of credit to burdensome documentary evidence gathering in order to verify their expenses and income. This will extend to those existing customers who have had no repayment issues. It would appear from a customer perspective that the relationship with the lender, proven track record and element of trust built by their responsible behavior is no longer of value.

Of specific concern are draft regulations 4AF, 4AG and 4AH which look at the affordability of the loan and determining the suitability of the credit product for the borrower's needs. This is of concern in terms of practical application.

As raised with MBIE during our teleconference, our lending practices include a range of methods in assessing affordability and suitability of the credit. We do not apply a 'one size fits all' approach to our customers as the majority of our customers have semi to complex financial positions. Given the motor vehicle brands we finance with customers, our customers use credit as a choice, not as a need. They have good financial literacy that enables them to choose whether to pay in full for a motor vehicle or to finance the cost of the vehicle through EFS, another finance company or a bank.

Our customers expect an efficient and discreet service, one where they are not inconvenienced with preparing and supplying "surplus" documentary information. We meet this by using methods we have developed in line with the RLC. We use a number of online resources in which to verify what our customers has disclosed to us. This ranges from property ownership data, Equifax credit checks, PPSR, relevant registers to Companies Office, LinkedIn, and Google. We look at affordability (for the duration of the loan term) by performing a capacity test based on income (as approved by our internal guidelines) less expenses including the repayment of the loan, and there must be adequate surplus which is uncommitted and available to the customer for other discretionary uses or unforeseen circumstances. When required we will also speak directly to the customer and their accountant to understand further their financial statement of position and if the customer is an existing customer, we will look at their history with us.

Requiring a prescriptive assessment of our customer base will result in using documentary information which we will not rely on to base our lending decision on. For example, the requirement to gather 90 days' worth of bank statements from our customer is just not feasible and will not go any further in trying to adequately do an assessment of the customer. To illustrate; our customer may have a number of bank accounts in which they receive income (from potentially multiple sources such as trust income, dividends, salary etc.) to pay for everyday expenses. These expenses may be paid from multiple accounts also, including through the customer's credit cards. Our customer might also transfer funds into their partner's account to pay for everyday expenses on behalf of the household.

The draft regulations effectively forces our customers to go away and gather 90 days' worth of transactions from all of their bank accounts including accounts which are not in the name of the customer. Then EFS must spend a substantial amount of time deciding what the everyday expenses are and extract those expenses out. For our customer we are potentially looking at between 4 and 10+ accounts which they use for everyday expenses.

These bank statements will not add in giving us a clear understanding of our customers affordability and suitability, as the majority of our applications are approved without the need of bank statements using the more effective methods (for our customer base) mentioned above.

Our arrears portfolio and the number of hardship applications we have had in the past 5 years (shared with MBIE) reflects the robustness of our lending assessment methods and the retention of our customers. The draft regulations will require us to ask for excessive and unnecessary information on which, as explained above, we would not rely on to make a well-informed lending decision.

The impact of 4AF, 4AG, and 4AH

The impact of the draft regulations will be considerable impact both to EFS and our customers. In effect we will not be able to meet the expectations of our customer. The ease of our current methods of approving credit for our customer base will be replaced with onerous prescriptive requirements of gathering, analysing, extracting financial information from sources which may end up redundant when EFS apply their lending assessment.

The ineffective cost to our business will be substantial. Additional resources will be required to manually extract and analyse 90 days' worth of transactions from multiple bank statements to comply only with the prescriptive requirements of the regulations. It would likely serve no other purpose and have no bearing on the way we assess affordability and suitability. It would be redundant information.

Our lending assessment would be much more invasive to our customer and require our customer to gather additional substantial documentation.

The approval time will take much longer and the costs would ultimately be borne by our customers.

We envisage that this will all result in our customers dealing directly with their bank for convenience, discretion and reduced fees. There is a risk it will force our lending sector out of the market which will reduce healthy competition in the credit market.

An alternative to address predatory and irresponsible lending practices

We believe the draft regulations relating to the "assessment of likelihood of substantial hardship" - 4AF, 4AG and 4AH should only apply to those lenders that provide access to 'high-cost credit contracts' (HCCC) **or** where the lender provides credit to a 'vulnerable borrower' as this is where the most harm is caused. HCCCs' and vulnerable borrowers are already defined under the RLC. If further guidance or clarity is required for the definition of vulnerable borrower, it can be easily amended.

Lenders or borrowers that fall outside of those categories (i.e. where the borrower is a "well-informed user of credit" or the agreement is not a HCCC) should not be subject to the draft regulation 4AF, 4AG and 4AH. Instead lenders should continue to gather information about the customer's financial situation using a less prescriptive approach (i.e. the RLC), taking into account the risk profile of their customer base to determine the lending outcome and also adequate customer surplus for the duration of the loan.

If, after a period of time (for example 2 years) irresponsible lending is continuing and evidenced in other lending sectors, the regulators could always extend the regulations to address the issues , a 2-stage roll out addressing the immediate harm and then refining it (if necessary) as time goes on.

Alternatively, responsible lenders, such as EFS, should have the ability to apply for an exemption from these regulations (by application to the Commerce Commission). Those lenders would supply supporting documentation such as its Responsible Lending Programme, statistics of its customer type, its lending outcomes (i.e. arrears, hardship applications, repossession) and onsite visit by the regulator.

Annual Report

It is relatively unclear to EFS as to what the Annual Report (AR) will be used for. Unfortunately, we did not get the opportunity to raise this during our discussion with MBIE because of timing constraints.

Although the discussion document states the content of the AR will support the Commerce Commission functions of enforcing and monitoring we see a lot of the proposed content as being more statistical and if this is indeed one of the aims of the AR, then we submit that caution is required if comparison of the data is made. This is due to the vastly different types of lenders (from banks to finance companies), the different types of systems lenders have and how lenders define that content internally as compared to other lenders.

Other content proposed is ambiguous and will need further clarity. For example, the number of complaints made;

a. Will these be any complaints the customer makes, or will they be specific to the loan itself?
b. How does one define 'resolved internally', is this from our point of view or the customers?
c. How would you resolve the customer complaint say about the colour of their vehicle, would we need to document this? If so where etc.

The proposed list of content is substantial. We are very concerned that in order to pull that data together, it would result in a huge initial cost to us, we would need to reconfigure our IT systems and

then ongoing costs to allocate a resource to collate that data, verify it and then share it with the Commerce Commission. This cost will be in the tens of thousands of dollars to implement.

Also, some of the information we would simply not have or would be very difficult to obtain. For example, information where an insurance claim has been lodged or paid out sits with the insurer and we would need to request this information from the insurer (assuming our privacy consent authority extends to that information).

We believe further consideration is required and input by financiers representatives such as the Financial Services Federation and other lenders to determine for what purpose the annual return will be used for, what data should be gathered and the period in which it should be gathered and shared with the Commerce Commission (taking into account other information submitted to other regulators the Commerce Commission could use i.e. the DIA for AML/CFT Annual Report statistics). As offered to MBIE during the teleconference, EFS would be happy to participate in discussions on this issue.

Thank you once again for the opportunity to submit EFS's views on the draft regulations. Please do not hesitate to contact us if there is anything you require further clarification on.

Regards

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