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Competition and Consumer Policy Team
Building, Resources and Markets
Ministry of Business, Innovation & Employment
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Exposure draft of the Credit Contracts and Consumer Finance Amendment Regulations 2020

1. Introduction

- 1.1 This submission to the Ministry of Business, Innovation & Employment is made by FlexiGroup (New Zealand) Limited (**FlexiGroup, we, us**) in respect of the Credit Contracts and Consumer Finance Amendment Regulations (No 2) (**Amendment Regulations**).
- 1.2 FlexiGroup is an innovative financial services company offering a wide range of consumer credit products to New Zealanders, including interest-free credit, credit cards, long-term finance and Buy Now Pay Later products (**BNPL**). FlexiGroup has a strong focus on sustainable and long-term relationships with our customers for the entire customer lifecycle.
- 1.3 As a committed responsible lender, FlexiGroup supports regulation which targets predatory lending practices and protects vulnerable customers. It is, however, important that regulation achieves these aims while being workable in a modern commercial context and allowing innovation. FlexiGroup is concerned that regulation that prevents innovation will lead to responsible lenders withdrawing from the market and have the unintended consequence of driving customers to non-compliant or predatory lenders.
- 1.4 We take this opportunity to submit specifically on the new regulations as they relate to the assessment a lender is required to make to determine that a borrower is likely to repay without substantial hardship (**affordability**). These new requirements are set out in sections 4AC-4AI of the Amendment Regulations. References to the Amendment Regulations should be read as referring to the requirements in sections 4AC-4AI, unless indicated otherwise.
- 1.5 FlexiGroup does not seek confidentiality for these submissions. We would be happy to speak to our submissions or otherwise engage further on our points.

2. Summary and Recommendation

- 2.1 We believe that the Amendment Regulations will not lead to better outcomes for customers of responsible lenders and are likely to lead to poor customer experiences. In particular:
 - (a) The Amendment Regulations in their current form will lead to less competitive consumer credit markets as a result of the compliance challenge they represent. Imposing these high due diligence thresholds across the board will negatively impact

competition, giving large incumbent financial institutions the upper hand as they hold the relevant data and have the scale to comply.

- (b) A necessary increase in decline rates as a result of the multiple steps in the Amendment Regulations will drive customers to less responsible lenders in the market for consumer credit.
- (c) The Amendment Regulations take a “one size fits all” approach and are not feasible to comply with.

2.2 Accordingly, we submit that the affordability requirements in the Amendment Regulations should not be enacted. Responsible lenders such as FlexiGroup already take a robust approach to affordability assessment and should be able to take the regulatory risk that their processes are sufficient to discharge their obligations under the Credit Contracts and Consumer Finance Act 2003 (CCCFA) and Responsible Lending Code. In the area of predatory lending, increased enforcement under existing provisions should be undertaken. Customers are best served in different markets by retaining some scalability and flexibility to allow lenders to lend responsibly while adapting to different circumstances and lending products. Lenders are obliged to make reasonable enquiries into whether the borrower will make the payments under an agreement without suffering substantial hardship. The reasonableness of these enquiries should be assessed in the context of the customer, the transaction, and the information available.

2.3 We set out below the core problems with the Amendment Regulations which lead to our submission.

3. **“One Size Fits All”**

3.1 The “one size fits all” approach of the Amendment Regulations in their current form is not appropriate and does not reflect existing good practice. It requires all lenders to follow an approach which may be broadly appropriate for a traditional bank mortgage lender lending to a traditional salaried worker. However, unlike the existing regime, it does not permit different approaches for simple credit products, borrowing less significant amounts, online approval processes or those with variable income.

3.2 There is a considerable difference between the significance of getting a mortgage compared to borrowing small amounts to finance domestic products. We consider that it is unnecessary to require a lender under a consumer credit contract for household items to undertake the same level of affordability diligence as a lender under a mortgage.

4. **Complying with the Amendment Regulations in current form is not feasible**

Not practical online or through digital in-store process

4.1 Compliance with the Amendment Regulations is not practicable in an online environment. Following a lengthy manual process is not consistent with customer expectations online or in-store. We consider customers can still be protected where products such as BNPL allow for an automated affordability evaluation.

Not possible in absence of open banking

- 4.2 Neither is compliance feasible for non-banks (other than by following manual processes) in the absence of true open banking. The verification obligation in the absence of true open banking is not realistic, as access to information is restricted including by the banks' terms and conditions. To amplify this point, we note that using bank statements online (**BSO**) for expense verification as provided by third party providers forces customers to breach their bank's terms and conditions and banks will actively combat this, as has been seen in Australia. Our concern is that this may result in responsible Tier 2 lenders leaving the market as customers will only have banks or "Tier 3" (high cost) lenders as options. BSO providers also confirm that providing a customer's full banking information does not necessarily guarantee an accurate estimation of financials.

Benchmarking inadequate

- 4.3 Benchmarking, as essentially required by section 4AH of the Amendment Regulations (including the requirement to benchmark discretionary expenses under section 4AH(2)), is challenging with the limited data available in New Zealand, and should not be required where sufficient benchmark data is unavailable. We suggest that benchmarking would be more achievable if robust and complete benchmark data was made available by the Government.

Reconciliation challenging and of little benefit

- 4.4 Reconciliation as drafted in sections 4AF(2) and 4AG(2) of the Amendment Regulations is not practicable, and will pose a serious challenge to responsible lenders. There may be a number of reasons why a customer's information does not align with the documentary evidence provided, including:
- (a) Individuals now commonly have complex personal banking structures, with income and expenses flowing out of multiple accounts.
 - (b) People may have variable incomes based on the time of year or other factors, such as seasonal workers and those in the gig economy. Reviewing payslips or bank transaction records for these customers may not give an accurate picture of their income. Self-employed customers will not have an employer who can verify their income. The approach in the Amendment Regulations does not allow for flexibility in these common situations and may lead to customers who could otherwise afford to repay a loan being declined.
 - (c) Some expenses cannot be verified (such as cash withdrawals).

- 4.5 We also note that the reasonable surplus requirement described in section 4AE(b)(i) of the Amendment Regulations does not clearly capture that customers will adjust their spending patterns based on their debt obligations. In other words, determining likely future expenses based on analysis of pre-borrowing data is flawed and difficult to achieve. There is significant evidence that a customer's current spending behaviour is not a good indicator of spending behaviour once the customer enters into a credit contract.

5. Innovation and Competition

- 5.1 The Amendment Regulations do not permit different approaches for borrowing in an online context, including where approval processes are conducted online. New Zealand is slipping behind the rest of the world in financial services innovation, and FlexiGroup wants to prevent regulations stifling opportunity for innovative lenders to create good customer outcomes for a broad spectrum of borrower profiles.
- 5.2 Launching innovative products in New Zealand will become difficult if the Amendment Regulations are enacted. The significant burden of compliance with the Amendment Regulations will discourage innovative new entrants and current market participants from developing modern consumer finance solutions for New Zealand consumers. Moving away from a “one size fits all” approach will allow for more flexibility to innovate. We believe it is possible to allow for innovative products (i.e. online products or mobile applications) that still allow for good customer outcomes and uphold responsible lending practices.
- 5.3 Compliance with the Amendment Regulations will also restrict competition and give incumbent banks an anti-competitive advantage. Responsible Tier 2 lenders like FlexiGroup do not have the scale to meet the increased regulatory burden in the affordability provisions of the Amendment Regulations. The increased time and cost associated with compliance will decrease the attractiveness of lending into this space and begin to push FlexiGroup (as well as similar responsible lenders) out of the market. This will decrease competition in the market for consumer credit, leading to fewer options and higher prices for customers.
- 5.4 FlexiGroup adopts responsible lending principles for our BNPL products (including soft credit checks for BNPL products that do not fall within the CCCFA, monitoring of transactions and “limit shaping” (where some customers will be offered lower limits until they demonstrate good repayment behaviour)). FlexiGroup aims to introduce innovative consumer credit products into the New Zealand market that engage a more modern customer base. These products are carefully designed with affordability and suitability in mind – for example, our BNPL products include a budgeting component, allowing customers to track their spending.
- 5.5 FlexiGroup would also like to note that it is a strong and public advocate for a BNPL Code of Practice. Our parent ASX-listed entity led the development for a BNPL Code of Practice in Australia and FlexiGroup intends to adopt this approach in New Zealand.

6. Vulnerable Customers

- 6.1 The Amendment Regulations will result in a higher decline rate, which will push customers from FlexiGroup (as a Tier 2 lender) to Tier 3 lenders. In particular, many of our merchants provide what could be termed “necessary services” (such as dental services and medical care) and will still seek credit for these services rather than foregoing credit altogether if declined.
- 6.2 Tier 3 or high cost lenders demonstrate little care for customers. We consider that more rigour should be applied to enforcement of current provisions relating to high cost lending. The approach in the affordability provisions of the Amendment Regulations does not sufficiently discourage the harm caused by high cost lenders. In our view, vulnerable

customers will still be in danger even with the Amendment Regulations. We consider that there needs to be additional focus on enforcement and resolution for these customers, on top of the minimum standards discussed above. Lenders should also have a greater focus on hardship programmes and dispute resolution.

7. **APR**

7.1 FlexiGroup submits that the Amendment Regulations should specify whether a straight line or amortised approach to calculating an annual percentage rate is required to ensure customers are provided with “like for like” information on which to select a credit product.

8. **FSF Submissions**

8.1 FlexiGroup is a member of the Financial Services Federation (**FSF**) and endorses the key points made in the FSF submissions.

Thank you for the opportunity to provide FlexiGroup’s written submissions on the Amendment Regulations.

Chris Lamers
Chief Executive Officer