Thorn Finance

4th February 2020

Competition and Consumer Policy Team
Building, Resources and Markets
Ministry of Business, Innovation and Employment
PO Box 1473
Wellington 6140

By email to: consumer@mbie.govt.nz

Submission on discussion document: Exposure draft of the Credit Contracts and Consumer Finance Amendment (CCCFA) Regulations 2020

Thorn Group Financial Services Limited (Thorn) appreciates the opportunity to provide this submission to the Ministry of Business, Innovation and Employment's (MBIE) in order to assist with refining the policy as well as the drafting of the proposed regulation.

Thorn has operated in the New Zealand market for 55+ years, providing finance across all market segments (prime, near-prime and non-prime) under the dtr and Thorn Finance brands. Our suite of lending products includes personal lending, vehicle lending and point of sale financing through our own and other retail channels.

Thorn is a member of the Financial Services Federation (FSF), a Registered Financial Services Provider, a member of an Approved Dispute Resolution Scheme operated by Financial Services Complaints Limited (FSCL), and a Qualifying Financial Entity approved by the Financial Markets Authority (FMA).

Introductory Comments

Thorn favours a more effective regulatory regime that places a stronger emphasis on increased routine enforcement. The reality is the majority of the market works consistently to meet compliance obligations and in fact, it's not in the best interests of any lender to not lend responsibly because this practice results in bad debts and losses. Even in the event that circumstances change for the borrower during the term of a loan, responsible lenders routinely work to find a fair and reasonable outcome for both the borrower and the credit provider. There are a small number of lenders who don't currently abide by the rules (it's already illegal to lend irresponsibly), and without increased enforcement, this will not change despite increasing regulatory compliance obligations on all lenders.

Thorn also has material concerns about the scope and effectiveness of some of the options put forward in the Exposure Draft. In particular, we're concerned about removal of the existing presumption in section 9C(7) of the CCCFA that allows lenders to rely on information provided by borrowers and guarantors without objective verification. Based on our experience, there are some circumstances whereby lenders will simply need to rely on what the customer tells them. This is especially true in scenarios whereby application information can't be reliably verified by a third party (e.g. age of dependants) and instances whereby lenders are now expected to make additional enquiries (e.g. significant cash withdrawals) – in these scenarios the only practical solution is for lenders to rely on what the borrower tells them. The removal of this presumption also removes borrower responsibility in the lending relationship. The lending contract is entered into by two parties and whilst we're supportive of a robust responsible lending

regime, the consumer also needs to assume some responsibility. We believe the removal of this presumption will undermine personal responsibility of the borrower which may lead to reduced financial literacy and worse consumer credit outcomes.

Thorn is also concerned about the exclusion of buy now buy later (BNPL) propositions from CCCFA obligations. We're witnessing more and more customers with multiple buy now buy later type contracts that must be serviced. These customers are struggling to meet their commitments as BNPL lenders often don't complete any affordability checks despite the fact some limits are in excess of $1,500 (more than typical payday loans). In our view, material harm is being caused by these propositions and lenders are exploiting the law by keeping their contracts under 8 weeks to ensure they are exempt from CCCFA obligations. It is our firm belief, that BNPL propositions must be captured by CCCFA obligations to ensure that borrowers are likely to repay without substantial hardship.

Thorn believes the problem that the MBIE is generally trying to solve for largely relates to the high cost lending segment. The draft regulations are taking a 'one size fits all approach' however and as it's currently drafted the new requirements are largely being applied to all lenders. We understand the concerns around the high cost lending segment and believe the drafting should allow for more specific provisions to be introduced for this segment in order to address the issues that exist.

Unless otherwise stated, Thorn supports the submission of the FSF on the same, and as a member has played a constructive role in the creation of this submission. The nature and operation of Thorn's business warrants a separate submission as this allows for further commentary and context from our perspective.

Responses to discussion document questions

Assessment of whether credit or finance will meet the borrower's requirements and objectives

New Regulation 4AA - Lender must collect and assess information
Thorn has no objection to the information collection and reassessment requirements of Regulation 4AA on the basis that this is in line with our current practice.

Subclause 2(d) states that if the agreement is a revolving credit contract the lender must assess whether the borrower requires credit on an ongoing basis. At a practical level, it's challenging for a lender to assess whether a borrower will require credit on an ongoing basis. We believe that the lender needs to ensure that the product is fit for purpose and indeed there could be a range of products and services that might meet a borrower's needs. The customer should have some discretion in making this choice and should take some responsibility in deciding whether they will require credit on an ongoing basis. It should also be noted that a revolving credit facility gives borrowers the ability to repay their loan faster and reduce the total cost of borrowing.

With respect to whether a particular type of contract is appropriate, there are numerous lenses that must be considered including nature of retailer, breadth of product range, frequency and value of purchase e.g. if the retailer is selling a car, it is unlikely that credit is required on an ongoing basis vs. if the retailer is selling smaller everyday items, ongoing credit may well be required.

Subclause 2(f) requires the lender to ask whether additional features need to be added to the finance, or whether the borrower would prefer to pay for them separately and not incur these costs as part of the cost of borrowing. The disclosure requirements of the CCCFA already adequately cater for educating the borrower around the fees that are interest bearing and those that are not. Thorn submits that further regulation around this component is not required as it catered for adequately currently.

Thorn has no objection to the proposed process for assessing the borrower's requirement and objectives however recommends that the proposed process be technology agnostic to allow for advances and innovation in consumer offerings. To be clear on Thorn's position, technology advances must adequately apply appropriate rigour and required protocol to meet all compliance requirements including responsible lending outcomes.

New Regulation 4AB- Additional requirements for waivers, warranties and insurance

Thorn has no objection to the purpose and application requirements of Regulation 4AB.

Thorn has some concerns in relation to the information the lender must collect, specifically under Regulation 4AB (2) (a)(i) where the lender is required to make enquiries into whether the borrower has existing cover that may protect against some or all of the risks for which the borrower is seeking cover. Thorn believes that this suggests that an enquiry needs to be made into whether the customer has an existing form of cover. The regulation does not consider that lenders don't have any means by which to verify this information from insurance providers. Hence lenders should be required to make reasonable enquiries into the existence of cover and should then be able to reasonably rely on the information provided by the customer. It should also be noted that lenders are not qualified to determine the best form of insurance cover in terms of the options that may be available, rather lenders must simply inquire into whether current cover exists or not.

How these regulations could be refined to minimise cost for lenders?

A centralised insurance register with detailed insurance policy information would enable lenders to accurately check and verify the existence of existing insurance cover. Without this option, we believe that the lowest cost option would be allowing the lender to rely on the information provided by the borrower.

Assessment that a borrower is likely to repay without substantial hardship

In terms of the General Rule, Thorn supports robust affordability assessment rules that ascertain whether a borrower is likely to repay their loan without substantial hardship. In terms of current practice, Thorn already applies substantial rigour to its borrower affordability assessment and this includes procurement of 90 days of bank statements, application of benchmarks to apply a minimum cost of living and verification and reconciliation of declared income and fixed financial commitments – the MBIE observed this directly on their site visit to Thorn's offices late last year.

The requirement requiring lenders to obtain 90 days of bank statements is a reasonable one and Thorn supports this approach as we believe this is the only way to truly verify and reconcile income and fixed expenses, determine applicable surplus and the borrower's ability to repay the debt without substantial hardship.

New Regulation 4AE - General rule for assessing whether a loan is affordable

Thorn understands that the regulation requires lenders to determine that the borrower will have a reasonable surplus after their 'likely' expenses have been subtracted from their 'likely' income over a reasonably foreseeable period of time.

Thorn supports the requirement for a surplus to be factored into the affordability calculation as this is the most practical way in which lenders can allow for unplanned future expenses (rather than trying to calculate 'likely' future variable expenses as these often aren't known until they actually occur – see comments on 4AG below). We would also assert a surplus should be calculated as a percentage of surplus

vs. a percentage of income as we believe the assertion that higher income earners have more discretionary cash is often not correct as expenses are often aligned to a corresponding level of income.

While further clarification around the term 'likely' would be helpful, Thorn is generally comfortable with the first part of this regulation which requires lenders to estimate the borrower's likely income. Our current practice is to reconcile declared income with income evidenced on the borrower's last 90 days of bank statements as we believe this approach most accurately captures the borrower's true income over time.

In terms of the requirement around 'likely' relevant expenses, Thorn is generally comfortable with this applying to regular fixed financial commitments however believes this approach isn't practical for discretionary expenses are these often unknown at the point of application and are by their very definition discretionary (not fixed) in nature. Borrowers often elect to reduce their discretionary expenses in order to meet any additional financial commitments they may undertake. We believe the most practical way to allow for unplanned expenses is to allow for a reasonable surplus to account for these future, unknown expenses. Most lending assessments reasonably consider a borrower's current financial position and ability to repay a debt hence a surplus would allow for some expense contingency within the lender's affordability calculation.

New Regulation 4AF- Lenders must estimate borrower's likely income

Regulation 4AF provides guidance in relation to how a lender must estimate the borrower's likely income. Thorn has no objection to this requirement as this represents Thorn's current practice.

Regulation 4AF (1)(c) requires the lender to ask the borrower about any future changes to their income. Thorn suggests more clarity is needed around how any future change to income should be verified e.g. if a borrower's income is likely to increase, will the lender be required to obtain a letter from the employer for verification purposes or be able to reasonably rely on what the borrower has told them? Again, the removal of 9C(7) needs to be reconsidered as there will be scenarios whereby a lender will simply need to practically rely on the information provided to them by the borrower.

New Regulation 4AG & 4AH- Lenders must do initial estimate of borrower's likely expenses and Lenders must adjust initial estimate of borrower's likely relevant expenses

Thorn is generally comfortable with verifying and reconciling a borrowers regular fixed financial commitments. Our practice is to compare declared, reconciled and minimum benchmarks for key expense categories and apply the highest of the three values to our affordability calculations. This approach isn't reasonable for unplanned or discretionary expenses however as these are often unknown at the point of application. Again, we believe the most practical way to allow for unplanned and/or discretionary expenses is to allow for a reasonable surplus to provide contingency for these expenses.

The regulation also requires lenders to ask the borrower about *any* cash withdrawals from their accounts that may contribute to a payment of a relevant expense. Thorn notes a potential inconsistency in that paragraph 51 of the Exposure draft of the CCCFA Regulations 2020 references *significant* cash withdrawals. We believe reasonable inquiry into significant cash withdrawals is reasonable especially in relation to a segment of borrowers that operate primarily in cash – this means most if not all of their money is withdrawn out of their bank account the same day on which it was deposited. Thorn believes this is a scenario that represents 'significant cash withdrawals' whereby additional inquiry is warranted – again in this scenario, the lender will need to reasonably rely on what the borrower tells them in terms of the utilisation of any such cash withdrawals as reliable verification may not be practical.

Where the customer does not withdraw all of their cash, details of the cash withdrawals have already been included as part of the affordability assessment and the assessment shows that the loan is affordable, Thorn submits that further enquiries into cash withdrawals should not be necessary.

Thorn also notes that the use of credit reports to obtain information in relation to outstanding debt commitments that may need to be paid in the future has been included in the proposed approach. MBIE may have assumed that Comprehensive Credit Reporting (CCR) data, that is repayment history and account limits, is freely available to the whole industry. The reality is CCR is permissive in New Zealand and lenders only receive this data if they are currently supplying their own data to a credit bureau. CCR is still maturing in the NZ market and many lenders do not currently participate hence this information is not readily available to all lenders.

4AH (3) requires lenders to have regard to the ages of dependents and verify the age of dependants, if relevant. This is yet another scenario whereby a lender must reasonably rely on what the borrower tells them as there is currently no practical way in which to verify the age of dependents. Further, Thorn does not believe that the age of dependants is required, and an affordability calculation based on the number of dependents and actual expenses reconciled to 90 days of a borrower's bank statements should be sufficient.

New Regulation 4AI – High-cost consumer credit contracts - Presumption of substantial hardship

Thorn is not a high cost lender, per the prescribed definition and threshold, however notes that any future review of the applicable high cost lending threshold must not be pre-determined and must be in line with lenders' cost structures.

Proposed Process for Guarantors

The affordability assessment for guarantors should be completed in the same manner as borrowers because payment liability for the guarantor is formally invoked once the borrower fails to meet their contracted financial commitments. Hence it must be ascertained that the guarantor could reasonably afford to repay the loan without substantial hardship.

Advertising

While Thorn believes sufficient customer protection already exists in relation to advertising, we're generally supportive of the proposed regulations for responsible advertising standards. Consideration however must be given to the different advertising mediums that exist as these are not equal in terms of space and ability to display information - reasonable, practical guidelines should apply here. Additionally, the ability to disclose total cost of borrowing should only apply if this is ascertainable. Lenders operating under a risk-based pricing model will apply the relevant risk weighted premium to each specific borrower at the time of application hence total cost of borrowing is only known at this point.

Failure to accommodate this scenario in the regulations could see lenders defaulting back to 'blanket' interest rate pricing and as a result, see consumers lose the benefits of risk-based pricing.

New Regulation 4AK – Advertising of payment amounts

This regulation provides that if an advertisement is being distributed to the public or section of the public refers to an amount of a payment, it must state the total amounts of payment or the annual interest rate and this information must be at least as prominent as the amount of payment. Thorn submits that the ability to disclose all requirements in the prescribed format i.e. the same font size for all mediums is

neither practical nor workable. In an example whereby numerous products are being advertised and a range of interest rates apply, Thorn believes it is reasonable to display the interest rate range prominently once on the page vs. on all products – see Appendix One for visual examples. The alternative is very cluttered, and we believe, no more effective than advertising the interest rate range once prominently on the page. Clarification to this effect is required to ensure lenders reasonably understand the requirements and corresponding obligations.

Further, in a risk priced pricing environment, whereby the individual credit profile of a borrower drives the interest rate, the term of the loan and repayment amount will vary depending on affordability hence disclosing this in an advertising forum is impossible as the interest rate is specific to the individual. Again, Thorn believes it is reasonable to display the interest rate range prominently once on the page.

Thorn further asserts that information in relation to payment amounts and interest rates is also disclosed to the customer before the borrower signs the loan agreement and makes the decision to accept the offer of credit.

New Regulation 4AL – Advertising of interest rates or charges

Thorn supports this proposed regulation and currently operates per these guidelines.

New Regulation 4AM – Advertising of credit fees if advertisement states there is no interest

Thorn supports this proposed regulation and currently operates per these guidelines.

New Regulation 4AN- Prohibited Advertising practices

Thorn agrees with the intent of the regulation in relation to prohibited advertising practices. However, Thorn wishes to clarify the incorrect correlation between time to decision and irresponsible lending. Stating that a loan will be 'approved in 15 minutes' does not necessarily mean that the lender will not inquire fully into the borrower's circumstances. What is relevant is the process and protocol applied each time to determine a borrower's affordability as this will determine whether the credit decision is appropriate and compliant with responsible lending requirements. For example, a company could take a week to make a credit decision and this could be irresponsible if repaying this debt caused the borrower substantial hardship. In contrast, compare this to a 15-minute decision from a lender who has invested in analytics and automation to improve their customer experience and meet all compliance obligations (including responsible lending) simultaneously. Additionally, automated protocols provide more consistent outcomes when compared to subjective human assessments. Hence any rule should focus on adequate process being applied (not on the specific time taken), compliance being met and be technology agnostic.

We must also adequately consider consumer expectations and demands in this equation. We are in a day and age where consumers want to do business 24/7, online in their homes, they want instant decisions as they are time poor and simply want to know whether they will be approved for the funds they require or not. There has to be some balance in terms of customer expectations, needs and demands so that regulations are generally in line with market trends and consumer behaviour.

Variation Disclosure

Thorn is generally comfortable with the new regulations 4F, 4G and 4H relating to matters that must be disclosed as part of variation disclosure.

Debt Collection Disclosure

Thorn engages a third-party debt collection agency and is comfortable with the requirements prescribed under regulation however notes that Section 24(1)(c) requires that the debtor's purpose of the credit when the credit contract was entered into be disclosed. It is unlikely that this information will be available as this has not always been a requirement under the CCCFA. Thorn recommends that this requirement be applied to all contracts entered into post enactment date.

Other regulations inserted by the Bill

New Regulation 5A(3) – Requirement to provide contact details for MoneyTalks in payment reminders

While Thorn is comfortable in principle, the way in which this requirement is currently drafted requires lenders to provide contact details for MoneyTalks service in every payment reminder sent. A payment reminder is generally issued when a payment has been missed and this gives the borrower an opportunity to organise payment to bring their account up to date. In our experience, there is a high incidence of self-correction in early arrears (5-30 days) following an initial reminder or prompt.

The regulation needs to include guidance around the process to notify and what the exceptions might be. For example, if it's early stage arrears (5-30 days), given the high rate of self-correction by borrowers, we don't believe a referral is appropriate. A more practical approach would be to require lenders to provide this referral once the customer is past 30 days overdue on their payment and only once in each arrears cycle as the customer will reasonably have this information after 30 days. Consideration must also be given to different communication methods as these represent different amounts of real estate to communicate this referral e.g. a lender who communicates their payment reminders via text message will have less room for this message vs. a lender who communicates their payment reminders via email.

New Regulation 5A(2) and 5A(4)- Requirement to provide information about disputes resolution schemes and financial mentor services

Again while Thorn is comfortable in principle, the way in which this requirement is currently drafted requires lenders to refer customers to a dispute resolution scheme each time a complaint ('an expression of dissatisfaction related to its services to which a response or a resolution is explicitly or implicitly expected') is received. This drafting does not reasonably provide the lender an opportunity to first work directly with the borrower to resolve the matter before involving the dispute a resolution scheme provider. We believe if, and only if, the complaint cannot be resolved by the lender in a reasonable timeframe then a referral to a dispute resolution scheme would be reasonable.

Thorn believes resolving disputes early in the process and in an effective manner is mutually beneficial and this is something we consistently strive for. Further details of Thorn's dispute resolution scheme provider are available on our website and on all of our loan contracts.

Formulae in relation to the rate cap

Thorn is comfortable with this requirement.

Credit Contract Legislation Amendment Act Commencement Order 2020

Thorn notes that the implementation deadline for material aspects has been pushed out to 2021 however highlights even 12 months is likely insufficient for the industry to comply with wide sweeping changes.

Content of the annual return

Thorn understands the purpose of collecting this type of information in order to support the Commerce Commission's monitoring and enforcement functions. In principle, Thorn supports this concept however notes that unless expressly defined, definitions will be wide and varied across the industry e.g. refinance vs. restructure and further clear guidelines on how the information will be interpreted across different market segments is essential e.g. a second tier mortgage lender will always have higher arrears profile than a major bank, however this doesn't necessarily mean they are lending irresponsibly – this simply represents different risk profiles across segments.

Thorn would suggest the requested data is streamlined to represent relevant industry recognised measurements and ratios and that appropriate guidelines are developed to ensure any interpretation of this data contemplates different dynamics and segments in market. As it stands gathering this data will be a time-consuming exercise for lenders and the data received will vary widely in quality, definition and content.

Thorn also notes paragraph 140-144 states that details in relation to number of loans with insurance where a claim was approved and paid out need to be provided. It should be noted that these records are not held by lenders - this information will need to be obtained from insurance companies directly.

A further example of where clear definition is required is in paragraph 160 which requires creditors to provide information in relation to complaints. Clarity is required in relation to whether this data set will need to include all complaints or only those escalated to disputes resolution providers. These numbers will vary widely and again clear definition and guidelines on interpretation are required.

Thank you again for the opportunity to provide Thorn's perspective on the proposed regulations. Should you require any clarification or wish to discuss any aspect further, please feel free to contact me on mark.spring@thornfinance.co.nz or +64 27 431 7157.

Regards

Mark Spring
Managing Director
Thorn Group Financial Services Limited

Appendix One – Advertising examples


buy now, pay nothing until april 2020*
SONY 55"
TCL 55"
SAMSUNG 55"
TCL 65"
SAMSUNG 65"
TCL 75"
TCL 80"
SAMSUNG 80"
TCL 85"
plus get one of these free*
or
or
or
32"