



COVERSHEET

Minister	Hon Dr David Clark	Portfolio	Commerce and Consumer Affairs
Title of Cabinet paper	Impacts of Recent Changes to the Credit Contracts and Consumer Finance Act 2003 – Findings and Options for Further Change	Date to be published	2 August 2022

List of documents that have been proactively released		
Date	Title	Author
July 2022	<i>Cabinet paper – Impacts of Recent Changes to the Credit Contracts and Consumer Finance Act 2003 – Findings and Options for Further Change</i>	<i>Office of the Minister of Commerce and Consumer Affairs</i>
4 July 2022	<i>Cabinet Minute – Impacts of Recent Changes to the Credit Contracts and Consumer Finance Act 2003</i> <i>CBC-22-MIN-0038</i>	<i>Cabinet Office</i>
23 June 2022	<i>Regulatory Impact Statement – Response to the investigation into 1 December 2021 credit law changes</i>	<i>Ministry of Business, Innovation and Employment</i>

Information redacted

YES

Any information redacted in this document is redacted in accordance with MBIE's policy on Proactive Release and is labelled with the reason for redaction. This may include information that would be redacted if this information was requested under Official Information Act 1982. Where this is the case, the reasons for withholding information are listed below. Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

Some information has been withheld as confidential advice to Government.

Office of the Minister of Commerce and Consumer Affairs

Cabinet Business Committee

Investigation into the impacts of recent changes to the Credit Contracts and Consumer Finance Act 2003: Findings and options for further change

Proposal

- 1 This paper seeks Cabinet's agreement to:
 - 1.1 release the final report into the investigation of the 1 December changes to the Credit Contracts and Consumer Finance Act (CCCFA); and
 - 1.2 further changes to address specific issues with the Credit Contracts and Consumer Finance Regulations 2004 (the Regulations) that are driving unintended impacts.

Executive Summary

- 2 In January 2022, I asked the Ministry of Business, Innovation and Employment (MBIE) to commence an investigation, in collaboration with the Council of Financial Regulators (CoFR), into the impacts of recent changes to the CCCFA and associated regulations that came into effect on 1 December 2021 (CCCFA changes).
- 3 The CCCFA changes were made as part of a number of changes to the CCCFA following a wider review of the CCCFA in 2018 [DEV-18-MIN-0204; CBC-20-MIN-0076 refer] which intended to address irresponsible lending and prevent problem debt in the form of unaffordable loan repayments. The CCCFA changes that came into effect on 1 December 2021 do this by placing clearer affordability and suitability assessment requirements and a stronger penalties and liability regime on all lenders. There are also other changes, such as requiring directors and senior managers to be certified as 'fit and proper persons', and introducing interest and fees caps on high-cost consumer credit contracts which came into effect before 1 December 2021 and were not within the scope of the investigation. I want to ensure that the reforms continue to address irresponsible lending and unaffordable debt.
- 4 I provided Cabinet with an overview of the final investigation report (**the Report**) on 16 May 2022. I am now seeking Cabinet approval to publish the Report. I propose to announce decisions on several potential changes identified in the Report, with a view to making changes to the Regulations, subject to further public consultation on the detail.
- 5 Key findings in the Report are that:
 - 5.1 Since 1 December 2021 there has been a reduction in lending activity across a range of consumer credit products, including home loans, personal loans, credit cards and vehicle lending. MBIE has concluded that the CCCFA changes are having a moderate impact on home loans (alongside other concurrent factors, including changes to loan-to-value ratio restrictions,

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increased interest rates, inflation and a general property market slowdown), and a high impact on other kinds of consumer lending.

5.2 While it is too early to say whether or not the CCCFA changes are likely to be successful, they are having some of the impacts intended. However, some unintended impacts are emerging. These include:

5.2.1 More borrowers across all lending types who should pass the affordability test are subject to declines of credit or reductions in credit amount.

5.2.2 Borrowers are subject to unnecessary or disproportionate inquiries that are perceived by them as being intrusive.

5.3 These unintended impacts are being driven by the following:

5.3.1 Lending processes, in practice, have become more restrictive and onerous than was expected when the CCCFA changes were made. This is a consequence of the way several specific provisions in CCCFA regulations are designed and drafted, combined with interpretational difficulties, and many lenders taking a more conservative approach to compliance than anticipated given the CCCFA's strong liability regime.

5.3.2 The prescriptive nature of the CCCFA changes and their application to almost all consumer lending means lending has been impacted outside of areas where there is a high risk of irresponsible lending and consumer harm.

6 Prior to the investigation being completed, Cabinet agreed to initial changes to clarify various aspects of the Regulations and the Responsible Lending Code (the Code) to expeditiously address issues identified early in the investigation [CBC-22-MIN-0012 refers].

7 Having met with lenders, banks and financial mentors in February to hear directly about the challenges they were experiencing, and given early indications of the final report's likely findings through an interim report-back, I mapped out some initial changes. These initial changes responded directly to concerns from lenders, and addressed key causes of the unintended consequences identified, improving access to credit without presenting significant risk of consumer harm.

8 The initial changes were targeted to address the most clearly articulated concerns in the shortest timeframe. This was considered a pragmatic response to consumer sector concern, and appears to have been well received by the public. At the time, and subsequently, banks, other lenders, and financial mentors each presented differing views on the question of scope, capture and treatment of discretionary expenses and debt consolidation, and so these matters were not considered suitable to progress in the initial suite of 'no regrets' changes. Debt consolidation and scope aside, the early changes addressed the burden of issues covered in meetings.

- 9 These changes come into force on 7 July 2022. I consider that these will go much of the way towards addressing unintended impacts of the CCCFA changes by addressing interpretational issues with the Regulations. The changes mean that lenders no longer need to label regular 'savings' and 'investments' as outgoings in affordability assessments and have clarified the nature of inquiries that lenders have to make on information required by the borrower. In addition, they provided alternative guidance and examples for when it is 'obvious' that a loan is affordable.
- 10 The Report identified a range of further changes to the CCCFA and regulations that could be considered to address unintended impacts of the 1 December CCCFA changes. These changes can be grouped into five options:
- 10.1 Option 1: counterfactual – initial changes agreed by Cabinet in February only
 - 10.2 Option 2: amend the affordability regulations to better target specific kinds of lending, lenders, or certain consumers where there is a higher underlying risk of substantial hardship
 - 10.3 Option 3: changes to the design of specific affordability regulations relating to borrower expenses, borrower surplus requirements and exceptions
 - 10.4 Option 4: changes to the penalties and liability regime
 - 10.5 Option 5: repealing the affordability regulations.
- 11 I consider that lenders are further refining their processes and consumers are becoming more familiar with the new requirements. This can be seen through lending complaints to the Banking Ombudsman falling 21% in the March 2022 quarter. In addition, while housing market headwinds and rising interest rates mean that banks have commercial incentives to continue de-risking their loan books, we have seen bank loan assets grow to \$531 billion in April 2022 and bank quarterly profits reaching a record \$1.8 billion in the first quarter of 2022.
- 12 I do not intend to target the affordability regulations only at particular types of lending due to the likely negative impact this would have on consumer protection. Targeting particular types of lenders or products may also harm competition. I note that when options to target 'high risk' borrowers were consulted on during the development of the Regulations, banks did not consider them to be workable or desirable. I anticipate that the initial changes together with further changes to address issues with certain provisions in the CCCFA regulations will sufficiently address the drivers of any unintended impacts, and as described above, there are already signs of improvements in lender processes and consumer experiences.
- 13 I am proposing to make further changes to address the remaining issues with specific Regulations that are contributing to the unintended impacts. These changes are:
- 13.1 more explicitly excluding discretionary expenses from the range of expenses captured by the regulations
 - 13.2 providing lenders with more flexibility about how repayments under revolving credit contracts (e.g., credit cards and buy-now pay-later schemes) may be calculated

- 13.3 extending the exceptions from a full income and expense assessment for refinancing of existing credit contracts (regulation 4AH) to also cover refinancing of credit contracts from other lenders.
- 14 I consider that these changes would further address the intended impacts identified in the final report, but there are risks that they reduce some consumer protections.
- 15 Financial mentors and some consumer advocates may view these further changes unfavourably. Lenders may believe these changes do not go far enough in addressing their concerns.
- 16 To mitigate these risks, the precise design and wording of these changes will be important. The CCCFA also requires that changes to the affordability regulations be consulted on. Accordingly, I ask Cabinet to approve the release of a public exposure draft of the Regulations.
- 17 I intend for these changes to the Regulations to be made in early February 2023, and to be in force by mid-March 2023.

Background

On 1 December 2021, new affordability and suitability requirements and penalties for lenders under the CCCFA came into force

- 18 The Credit Contracts Legislation Amendment Act 2019 (the Amendment Act) was intended to address irresponsible lending practices and prevent problem debt in the form of unaffordable loan repayments, particularly in relation to people and whānau in vulnerable circumstances.
- 19 The Amendment Act followed a review of the CCCFA conducted by MBIE in 2018. The review's findings were based on feedback from a range of consumer advocates, as well as MBIE's discussions with lenders and other parties about lender processes.
- 20 Consumer advocates identified irresponsible lending across all types of lenders (though there was little information about the prevalence of problems across particular types of lenders). Examples provided by consumer advocates, and Commerce Commission complaints data, suggested problems were particularly concentrated across finance companies and high-cost lenders. Credit card lending by banks was also cited as a source of issues.
- 21 In 2020 MBIE commissioned a survey which found that in 2019 around 18% of consumer borrowers reported that repayment difficulties were having a moderate to severe impact on their lives.
- 22 Several changes were made to the CCCFA and Regulations to address issues with non-compliance, unreasonable fees, high cost of borrowing and harm from debt collection and mobile traders. [DEV-18-MIN-0204; CBC-20-MIN-0076 refer]. Some of the changes related specifically to high-cost credit (broadly, credit where the annual interest is 50% or higher). These changes included include caps on interest rates and the total cost of credit and new restrictions on repeat lending. However,

most of the changes affected all consumer lenders and all forms of consumer loans, including car finance, personal finance, and mortgages.

- 23 On 1 December 2021, the parts of the Amendment Act and the Regulations that provide for prescriptive affordability and suitability requirements and duties on directors and senior managers of lenders came into effect. Amendments to the Regulations now require that, as part of an affordability assessment, lenders must estimate the borrower's likely income and expenses. The lender must show that the borrower's income exceeds their expenses (including payments under the new loan) and make an allowance for error (e.g. overestimation of income or underestimation of expenses). Further detail is prescribed as to what information is to be used to estimate income and expenses and how this may be done.

In light of concerns raised by lenders and consumers, in January 2022 I commenced an investigation into the impacts of these changes

- 24 Since the CCCFA changes came into effect, concerns have been raised by lenders, financial advisers (e.g. mortgage brokers) and consumers about the impacts of the changes on lending.
- 25 On 14 January 2022, I asked MBIE, in collaboration with the Council of Financial Regulators (CoFR), to commence an investigation into the impacts of the changes to affordability and suitability requirements. As part of the investigation, MBIE conducted a series of stakeholder engagements and, working in collaboration with CoFR agencies, gathered relevant data.
- 26 MBIE has prepared a report on the early implementation and impacts of the CCCFA changes. The Report is attached as Annex One and is ready for public release, subject to Cabinet approval.
- 27 The terms of reference for the investigation set its scope to identify any intended and unintended impacts of the CCCFA changes and consider whether further actions are needed. Lines of inquiry included observable changes in consumer credit markets, factors outside of the CCCFA which may be impacting these changes, and evaluation of the CCCFA's impact. The findings are summarised below.

Official statistical data, independent credit reporting data, and lender data available to date indicates that there has been a reduction in all types of lending since 1 December 2021

- 28 Since 1 December 2021 there have been reported reductions in lending activity across a range of consumer credit products, including home loans, personal loans, credit cards and vehicle lending.
- 29 The CCCFA changes are one of several factors that have had an impact on home lending, alongside changes in loan-to-value ratio restrictions, increased interest rates, inflation, and a general property market slowdown¹. For other consumer lending, which tends to be higher risk, there may be some impacts from other factors (such as cost of living increases), but the relative impact of CCCFA changes on lending activity appears to be higher.

¹ from 1 November 2021, the Reserve Bank reduced the speed limit for lending on owner-occupied property from a max of 20% of new lending at LVR above 80% to a max of 10% at LVR above 80%.

- 30 The findings in the Report have limitations due to the short time period since implementation of the CCCFA changes. Officials' analysis was primarily based on data provided by the Reserve Bank, credit rating agencies and interviews with some lenders in January and February 2022. Data collection methods and measures varied between sources, and much of the data provided by rating agencies and lenders was incomplete or not in form where it could be readily aggregated with data from other sources. Finally, housing market conditions and inflationary pressures have changed rapidly in the past six months. I consider that this limits the conclusions that can be drawn from the Report in terms of the persistence of unintended consequences identified and the areas where further change should be explored.

It is too soon to tell whether the main benefits sought by prescriptive affordability and suitability assessments are being achieved...

- 31 Throughout the investigation, financial mentors and other consumer advocates consistently told MBIE that most of the benefits sought by the CCCFA changes would take 6-12 months to be visible. This was on the basis that most debts encountered by financial mentors tend to be incurred some time prior to clients contacting financial mentors, and in some cases, clients have been struggling with debt for a considerable period of time before they see a financial mentor.
- 32 However, lenders have strengthened their affordability assessment processes, financial mentors have reported being more empowered by the new enforcement and liability regime and recordkeeping requirements, and referrals to financial helpline MoneyTalks have been increasing. In addition, there has been reduced lending in some areas such as motor vehicle finance, which in the past has been identified as being particularly harmful to consumers. This appears to be consistent with the outcomes sought by the CCCFA changes.

Some unintended consequences are emerging

- 33 The investigation has highlighted some unintended consequences arising from the CCCFA changes to the affordability and suitability requirements, including that:
- 33.1 More borrowers across all lending types who should pass the affordability test are subject to declines of credit or reductions in credit amount.
- 33.2 Borrowers are subject to unnecessary or disproportionate inquiries that are perceived by them as being intrusive.
- 34 These unintended consequences are the result of the following:
- 34.1 Lending processes, in practice, have become more restrictive and onerous than was expected when the CCCFA changes were made. This is a consequence of the way a number of specific provisions in the CCCFA regulations are designed and drafted, combined with interpretational difficulties and many lenders taking a naturally conservative approach to compliance given the CCCFA's strong liability regime.

34.2 The prescriptive nature of the CCCFA changes and their application to almost all consumer lending means that lending has been impacted outside of areas where there is a high risk of irresponsible lending and consumer harm.

Cabinet agreed to initial changes

- 35 Cabinet agreed to a set of initial ‘no regrets’ changes prior to the conclusion of the investigation to expeditiously address some of the concerns raised by consumers and lenders [CBC-22-MIN-0012 refers]. These changes primarily focused on clarifying the Regulations and the Code to address interpretational issues, hence, are relatively low risk.
- 36 I issued the revised version of the Code on 9 June 2022, and the amended Regulations and the revised Code will come into force on 7 July 2022.
- 37 I consider that the initial changes, combined with customer familiarity and lenders continuing to refine their processes, have gone a substantial way to addressing the unintended consequences identified by the investigation.
- 38 This is reflected in recent data shared by the Banking Ombudsman, which indicates that, after an initial spike following the 1 December changes, lending complaints fell 21% during the March 2022 quarter. The biggest change has been in home loan complaints, which are down 37% after a rise of 19% the previous quarter. Complaints about personal loans also fell 18%, while credit card complaints remained steady.
- 39 Banks are changing their behaviour and refining their processes as guidance and enforcement expectations become more familiar. It is not surprising this “bedding in” period has taken some time. Some banks have told me they made the most significant changes to their processes since the global financial crisis.
- 40 Meanwhile, bank assets and profitability have continued to grow, even as banks are likely to look to de-risk their loan books in light of a cooling housing market. Bank gross loan assets have grown to \$531 billion in April 2022, up 2.2% on November 2021. From December 2021, when the CCCFA changes came into force, to March 2022 there has been a 6.6% increase in bank profits after tax, maintaining a steady upward trend since June 2021. Bank profits reached a record \$1.8 billion for the first quarter of 2022.
- 41 Interest rates have risen above historic lows, putting more pressure on the affordability of mortgages. While non-performing bank loans in April 2022 were at lows of 0.2% and 1.2% of loan assets for housing and personal loans respectively, Reserve Bank data shows they have been significantly higher in the past: in 2009–2010 housing loan arrears were 1.2% of loan assets (six times the current rate) and bank personal loan arrears 2.4% (double the current rate). Given the risk posed to borrowers, I consider it appropriate for the Government to help protect prospective first home buyers from unaffordable debt, and the CCCFA changes are a key ingredient of this.

A number of possible changes were identified in the Report, but it did not make recommendations

- 42 The Report identifies 15 potential changes to address the drivers of unintended impacts, but does not make recommendations. Many of these potential changes were raised in the course of engaging with stakeholders during the investigation. These changes can be grouped into five options:
- 42.1 Option 1: counterfactual – initial changes agreed by Cabinet in February only
 - 42.2 Option 2: amend the affordability regulations to better target specific kinds of lending, lenders, or certain consumers where there is a higher underlying risk of substantial hardship
 - 42.3 Option 3: changes to the design of specific affordability regulations relating to borrower expenses, borrower surplus requirements and exceptions
 - 42.4 Option 4: changes to the penalties and liability regime
 - 42.5 Option 5: repealing the affordability regulations.
- 43 In the accompanying regulatory impact statement, MBIE recommends further investigating options to target the Regulations towards particular types of borrowing (option 2), and also addressing issues with the design of specific regulations (option 3).
- 44 The Report suggests that potential further changes could be explored which would target the scope of the affordability regulations to higher-risk lending on the basis of product type, class of lender, and/or characteristics of the borrower (option 2). This would be consistent with the original policy intent and would address a key underlying driver of the unintended impacts, which is that the Regulations apply to almost all consumer lending with limited exceptions.
- 45 The Report suggests that if well targeted, option 2 could go a considerable way to reduce unnecessary inquiries by lenders. Credit contracts which fell outside the targeted scope would be subject only to the inquiries deemed necessary by the lender under the principles-based approach in the CCCFA. It would also promote access to affordable credit, by allowing lenders more discretion, in some circumstances, about when lending is likely to be affordable.
- 46 However, the Report and advice from Officials is that further work would need to be undertaken to ensure that targeting the scope of the Regulations does not result in negative consumer outcomes.
- 47 I have considered the findings of the Report, advice from Officials, and information provided by key stakeholders. I do not recommend undertaking further work to target the Regulations.
- 48 Whilst further changes to target the scope would address the issue of the Regulations impacting borrowers who might not be considered high-risk, I am concerned that any further changes to target the scope of the affordability regulations would significantly reduce consumer protection and that the benefits of doing so would be marginal.

While there may be certain lenders, product types, or borrowers where there is greater risk of irresponsible lending, this does not preclude those not captured under the targeted scope from irresponsible lending as well.

- 49 For example, I am informed by financial mentors that even where borrowers use lenders with low default rates and ‘low risk’ credit such as mortgages, an unexpected expense may find them going without essentials or living off food parcels in order to meet payments. I consider that this risk is exacerbated by a higher than normal interest rate environment, where people refinancing will face ongoing servicing costs higher than they have historically.
- 50 This would suggest that whilst targeting the scope of the affordability regulations to exclude mortgage lending would increase access to credit to first home buyers, it would likely come at the cost of consumer protection and result in an increase in this kind of substantial hardship.
- 51 Targeting borrowers with particular characteristics (e.g. low credit scores, or low income) could incentivise lenders to refuse lending to those borrowers, even when it might otherwise be affordable. This would exacerbate existing barriers to them obtaining safe credit and may lead them towards less scrupulous lenders. Similarly, specifically relaxing affordability requirements for a lender’s existing borrowers (one of the options discussed in the Report) could lock vulnerable borrowers into predatory lenders and reduce competition.
- 52 Some targeting mechanisms are likely to disproportionately impact certain lenders and harm competition. If the scope is targeted on the basis of a particular class of lender (for example, non-bank finance companies), this would disproportionately impact those lenders and give others (such as incumbent banks) a competitive advantage. There is also the risk that where particular product characteristics are targeted, lenders may adapt their business practices and lending behaviour to avoid having to comply with the prescriptive requirements. For example, targeting personal loans may cause some lenders to exit that market, reducing competition and the availability of this type of credit for consumers.
- 53 I also note that targeting the scope of the Regulations was considered at the time the Regulations were being developed, but banks did not consider the options proposed to be workable or desirable. Banks were concerned that use of credit scores would not be transparent (due to a lack of visibility as to how they are calculated) or sufficiently relevant to affordability, and risked borrowers ‘gaming’ credit scores. Use of debt-to-income ratios or applying the regulations only to ‘vulnerable’ borrowers were also rejected as options. The option most favoured by lenders, and adopted, was an exception for ‘obvious’ affordability similar to that used in the United Kingdom.
- 54 I anticipate that the initial changes together with further changes to address issues with certain provisions in the CCCFA regulations will sufficiently address the drivers of any unintended impacts, improving ease of access to safe and affordable credit. This is because the unintended impacts are, by and large, being driven by the implementation of specific provisions in the Regulations, and because (as discussed above) there are already signs of improvements in lender processes and consumer experiences.

- 55 The additional time required to consult on targeting would also delay more important changes to address issues with certain provisions in the Regulations.
- 56 I also note that, the initial changes agreed by Cabinet have already clarified use of the exception for ‘obvious’ affordability, which is more principles-based than other blunt alternatives to targeting.
- 57 Accordingly, I do not propose to make changes to the scope of the Regulations.

I propose to make further changes to address unintended consequences

- 58 I am seeking agreement to further changes to address issues with the design of specific CCCFA regulations (option 3 in the Report). With this proposal I aim to realise a balance between ensuring access to credit for those who can afford it, whilst ensuring those who may experience hardship as a consequence of irresponsible lending are suitably protected.
- 59 While one option considered was limiting changes to those decided by Cabinet in March, to allow for more ‘bedding in’ and refinement of lender processes as interpretational difficulties reduce, I propose to go further than the initial changes to address the risk that remaining unintended impacts persist.
- 60 I do not propose to make changes in other areas. Changes to limit the affordability regulations to particular types of borrowing or the liability regime would likely tip the balance towards creating the same issues with irresponsible lending and unaffordable debt that were identified in the 2018 review of consumer credit law.
- 61 The reasons for my proposals are explored in more detail below.

Proposals to address specific issues relating to the capture and treatment of discretionary expenses

- 62 Regulation 4AF(2)(a) requires lenders to estimate ‘likely relevant expenses’. These are the ‘listed outgoings’ that the borrower will incur in the 12 months after entering into the credit contract. Paragraph (d) of the definition of ‘listed outgoings’ specifies that they include ‘regular or frequently recurring outgoings... that the borrower is unable or unwilling to cease...’.
- 63 The investigation found that in practice this regulation is driving inquiries that are disproportionate or unreasonable, and causing lenders to include discretionary expenses in their estimates of borrower expenses. Lenders may be able to address this to some extent over time by careful redesign of their processes, in line with new Code guidance. However, it could be addressed more directly through changes to the Regulations themselves.
- 64 I propose to amend the Regulations to narrow the expenses considered to exclude discretionary expenses more explicitly. Under this proposal, lenders would only need to estimate expenses that are essential to borrowers or which they would be unwilling to give up if faced with hardship.

- 65 There are a number of ways this proposal could be given effect in the Regulations, including:
- 65.1 amending the concept of ‘likely relevant expenses’ in Regulation 4AF(2)(a)
 - 65.2 narrowing paragraph (d) of the definition of ‘listed outgoings’ to exclude those that a responsible lender would reasonably expect the borrower to cease if at risk of hardship
 - 65.3 removing paragraph (d) of the definition of ‘listed outgoings’ entirely.
- 66 Drafting would be tested with stakeholders through the public exposure draft.
- 67 This proposal would be consistent with the affordability principle in the CCCFA and would further alleviate the disproportionate and intrusive nature of inquiries and reduce the overestimation of borrower expenses.
- 68 However, depending on how it is drafted, this proposal could create some risk that lenders misclassify non-discretionary expenses as discretionary. Whether borrowers will cease various expenses to avoid substantial hardship will often depend on their circumstances, including social expectations. For Pacific peoples in particular, expenses such as tithing, contributions to family expenses, and sending remittances to families in the Pacific might not necessarily be viewed as discretionary even in the face of hardship. However, certain lenders could interpret these to be discretionary expenses.
- 69 This risk is mitigated by section 9CA, which requires lenders’ records to substantiate the affordability of lending. These changes would also be supported by providing additional guidance in the Code around what kinds of outgoings it would be reasonable to expect the borrower to cease.
- 70 The detailed design should also consider the role of the borrower in the classification of discretionary expenses. This would be more appropriate for long-term contracts such as mortgages where a borrowers’ discretionary expenses are more likely to change over the course of the credit contract. This would need to be carefully designed and subject to consultation given the need to manage the risk of intrusive inquiries.

Proposal to address specific issues relating to revolving credit contracts

- 71 Regulation 4AL(2) sets out a prescriptive approach for lenders to estimate the expenses that may arise from revolving credit contracts, such as credit cards and Buy Now Pay Later (BNPL) facilities, as part of their estimation of the borrower’s likely relevant expenses. This does not take into account borrowers who use these facilities for day-to-day transactions and pay them off quickly, rather than making large purchase to be paid back over months or years. This could result in ‘double counting’ of both the assumed debt payment on the revolving credit contract and the regular expense being paid under the revolving credit contract.
- 72 I propose to amend the Regulations to remove ‘double counting’ of expenses associated with revolving credit contracts under regulation 4AL(2).

- 73 This could be done by excluding existing revolving credit facilities where the borrower routinely repays them without incurring interest. This change would not change the treatment of any new revolving credit contract that borrowers apply for. This change to the Regulations could be supported by additional guidance in the Code.
- 74 This proposal would have some risks, if not carefully implemented. The current treatment of repayments of revolving credit contracts is based on the fact that borrowers have access to credit up to the limit of existing facilities. By making changes there may be a risk that after a loan has been advanced, the borrower may change their usage of their existing revolving credit contracts in a way that creates a substantial new liability. For example, a borrower who has been paying for living expenses with a credit card may instead decide to make a large one-off purchase that needs to be repaid over months or years. This could be mitigated through additional guidance in the Code which could suggest what borrowers may do to minimise this risk.

Proposal to address issues in relation to the exception for variations and replacements of existing credit contracts

- 75 Regulation 4AH provides an exception from a full affordability assessment where lenders refinance or consolidate debts owed to them. However, there are situations where borrowers facing financial difficulty seek to refinance or consolidate debt from other lenders with lower repayments. The current scope of regulation 4AH may be limiting access to safe credit in these instances. This has the potential to contribute to financial hardship or could contribute to a delay in access to credit as lenders are required to conduct a full affordability assessment.
- 76 I propose to amend the Regulations to expand the exception in regulation 4AH to include refinancing of credit contracts that borrowers have with other lenders where this would be in the best interests of the borrower.
- 77 There are a few ways this proposal could be given effect in the regulations, including:
- 77.1 providing an alternative exception to regulation 4AH for replacing credit contracts with other lenders, where the total repayments are equal to or lower in the new arrangement, or
 - 77.2 providing an alternative exception to regulation 4AH for replacing credit contracts with other lenders, where the lender is satisfied that refinancing is in the best interests of the borrower.
- 78 This change would improve ease of access to safe credit and has the potential to benefit consumers, as there are instances where refinance or debt consolidation from one lender to another can reduce harm, for example by reducing the interest rate and extending the repayment term so debt is less costly and more manageable.
- 79 However, this change may create some risk to consumer protection for some borrowers if it encouraged unscrupulous lenders to provide unaffordable debt consolidation services in circumstances where borrowers would be better off seeking hardship relief from their existing lender. This is mitigated by the general lender

responsibilities in the CCCFA and liability regime, as well as specific requirements in the Regulations for lenders to determine the borrower's objectives for refinancing and that the borrower accepts any additional costs they would incur.

Other changes not proposed

- 80 The Report notes that a range of other approaches could be considered to address unintended impacts. These include relaxing liability settings or removing the prescriptive regulations altogether and reverting to the previous 'principles-based' regime.
- 81 Changes to liability settings (option 4 in the Report) would likely increase access to affordable credit and reduce unnecessary inquiries by reducing conservative interpretations of the Regulations. However, this option would also disincentivise compliance with responsible lending obligations and reduce consumer protection.
- 82 Repealing the Regulations (option 5) would result in a return to the principles-based model and would do the most to improve access to affordable credit by improving lender discretion. However, this option is likely to reduce consumer protection where lenders adopt less rigorous affordability assessments.
- 83 I do not propose to further explore these options. While these changes may ease access to credit in some instances, they would reverse key policy decisions Cabinet took in 2018 and risk the CCCFA changes not adequately addressing irresponsible lending and resulting consumer harm.

Consumer Data Right

- 84 I also note that many of the issues identified with the CCCFA changes stem from lenders having insufficient information about borrowers. These concerns could be addressed through the Consumer Data Right (CDR), if applied to the banking sector. In July 2021 Cabinet agreed to introduce a CDR which will allow consumers to share the data held about them with trusted third parties. This could allow lenders to access accurate data about borrowers, on the borrower's consent, to improve the efficiency and accuracy of lending decisions, and incentivise competition.

Confidential advice to
Government

Actions to be progressed for further changes

- 85 Subject to Cabinet approval of the final policy recommendations, I propose to undertake further public consultation on regulatory changes and therefore seek Cabinet approval for the release of a public exposure draft of the regulations. I anticipate regulations being made in February 2023, and in force in March 2023.
- 86 Consultation during the process is a statutory requirement, as well as being important to ensure that any changes will work as intended and achieve the benefits desired, while continuing to protect consumers.
- 87 An indicative timeline is provided in the table below.

Event:	Date:
Public release of Report	Soon after Cabinet agreement
Public release of exposure draft	22 September 2022
Submissions close	20 October 2022
LEG	3 February 2023
Cabinet	8 February 2023
Executive Council	8 February 2023
Gazetted	13 February 2023
Regulations come into force	13 March 2023

Financial Implications

88 The proposals in this paper do not have any financial implications for the Crown.

Legislative Implications

89 Changes to the Regulations will be needed to implement the above proposals. Parliamentary Counsel Office has been consulted.

Impact Analysis

90 MBIE’s Regulatory Impact Analysis Review Panel has reviewed the attached Impact Statement prepared by MBIE. The Panel considers that the information and analysis summarised in the Impact Statement is sufficient to meet the criteria necessary to make informed decisions on the proposals in this paper.

Climate Implications of Policy Assessment

91 The Climate Implications of Policy Assessment (CIPA) team has been consulted and confirms that the CIPA requirements do not apply to this proposal as the threshold for significance is not met.

Population Implications

92 Officials have not yet undertaken an analysis of whether there are any impacts on particular population groups as a result of addressing issues identified in the Report.

93 Further analysis will be undertaken by officials during the further development of proposals to determine whether there any impacts on particular population groups.

Consultation

94 The following agencies were consulted on this paper: the Department of Prime Minister and Cabinet, Treasury, Ministry for Pacific Peoples, Ministry of Housing and Urban Development, Reserve Bank of New Zealand, Commerce Commission, Office of the Privacy Commissioner and Financial Markets Authority.

- 95 The Acting Privacy Commissioner expressed that it is encouraging to see MBIE consider the impacts on privacy as an unintended consequence to the CCCFA changes. The recommendations suggested aim to address the over collection of personal information by refining regulations and wherever necessary to provide additional guidance to industry players. They support these proposed amendments and look forward to the Office being further consulted on the Regulations and guidance when they return to Cabinet.
- 96 Engagement with a number of key stakeholders took place during the investigation, and as part of the initial changes to the Regulations and the Code. However, stakeholders have not been consulted on the options discussed in this paper.

Communications

- 97 The Report will be published on MBIE's website.
- 98 I intend to publicly announce the Government's response to the Report, including decisions on further changes.
- 99 There is a risk that lenders will argue the changes sought by this paper do not go far enough to address the unintended impacts of the CCCFA changes, differ from MBIE's preferred options and do not include the full range of options discussed in the Report.
- 100 I intend to emphasise that these changes will, on top of those already agreed by Cabinet, make a material difference to streamlining affordability assessments, while maintaining consumer protections. Further change to target the affordability regulations risk an increase in unaffordable lending that will ultimately harm consumers, is unlikely to improve access to affordable credit, and would introduce unnecessary boundaries between different types of lending which would have negative impacts.

Proactive Release

- 101 I intend to release this paper proactively within 30 business days of decisions being confirmed by Cabinet.

Recommendations

The Minister for Commerce and Consumer Affairs recommends that the Committee:

- 1 **note** that in January 2022, the Minister of Commerce and Consumer Affairs initiated an investigation into changes to the Credit Contracts and Consumer Finance Act 2003 and associated regulations (**the Regulations**) that came into force on 1 December 2021 (**CCCFA changes**);
- 2 **note** the investigation found that:
 - 2.1 the CCCFA changes appear to be contributing to a reduction in lending, including home lending but more significantly to other personal lending (e.g. credit cards, car loans);

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- 2.2 it is too early to tell whether the CCCFA changes will achieve their objectives of addressing irresponsible lending and resulting problem debt, however, some early impacts which have been identified appear to be consistent with the outcomes sought by the changes;
- 2.3 some unintended consequences resulting from the CCCFA changes have emerged, including:
 - 2.3.1 more borrowers across all lending types who should pass the affordability test are subject to declines of or reductions in credit amount; and
 - 2.3.2 borrowers are subject to unnecessary or disproportionate inquiries that are perceived by them as being intrusive;
- 3 **note** the investigation identified a range of further changes to the CCCFA and regulations that could be considered to address unintended impacts of the 1 December CCCFA changes:
 - 3.1 Option 1: counterfactual – initial changes agreed by Cabinet in February only
 - 3.2 Option 2: amend the affordability regulations to better target specific kinds of lending, lenders, or certain consumers where there is a higher underlying risk of substantial hardship
 - 3.3 Option 3: changes to the design of specific affordability regulations relating to borrower expenses, borrower surplus requirements and exceptions
 - 3.4 Option 4: changes to the penalties and liability regime
 - 3.5 Option 5: repealing the affordability regulations.
- 4 **agree** to adjust the scope of expenses that need to be estimated by lenders to more explicitly exclude discretionary expenses;
- 5 **agree** to amend the Regulations to reduce ‘double counting’ of expenses associated with revolving credit contracts such as credit cards and buy-now pay later schemes;
- 6 **agree** to expand the exception in regulation 4AH to include refinancing of credit contracts that borrowers have with other lenders where this would be in the best interests of the borrower.
- 7 **agree** not to make changes to further target the scope of the affordability regulations;
- 8 **invite** the Minister of Commerce and Consumer Affairs to issue drafting instructions to the Parliamentary Counsel Office to give effect to the above paragraphs;
- 9 **authorise** the Minister of Commerce and Consumer Affairs to release an exposure draft of the amendment regulations;

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- 10 **authorise** the Minister of Commerce and Consumer Affairs to make decisions on minor or technical matters, consistent with the policy in this paper, on any issues that arise during drafting or from stakeholder consultation;
- 11 **agree** to the public release of the final investigation report on the early implementation and impacts of the CCCFA changes.

Authorised for lodgement

Hon Dr David Clark

Minister of Commerce and Consumer Affairs