

Revisions to the Responsible Lending Code



DRAFT September 2022

[...]

5 Inquiries into and assessment of substantial hardship (borrowers)

Legal obligations

Lender responsibility

A lender must, in relation to an agreement with a borrower, make reasonable inquiries, before entering into the agreement, and before making a material change referred to in subsection (8), so as to be satisfied that it is likely that the borrower will make the payments under the agreement without suffering substantial hardship (see section 9C(3)(a)(ii) of the Act).

Regulations - minimum requirements for inquiries and assessment

As part of complying with the lender responsibility in section 9C(3)(a)(ii) of the Act, lenders must comply with the minimum requirements for inquiries and assessment prescribed in regulations 4AE–4AO (see section 9C(5A)).

Commentary

Regulation 4AD provides an outline of regulations 4AE–4AO, which set out requirements for making reasonable inquiries about the likelihood that the borrower will make the payments under the agreement without suffering substantial hardship.

Below is a diagram of this process. Note that this is illustrative only and does not represent every step or legal test provided by regulations.

S9C(3)(a) Borrower will enter a new agreement or make a material change increasing the credit limit

S9C(2) Exercise the care, diligence, and skill of a responsible lender (this may include a consideration of impact of variation on affordability)

Affordability Assessment

If **not** a new agreement or increase to the credit limit (e.g. variation makes other changes – even if for hardship)

Full assessment not required. Must still make inquiries and be satisfied that agreement is affordable (9C(3)(a)(iii))

4AH Lender is varying or replacing existing contract limit (save to enable deferral or reduction of
4AG Inquiries are sufficient to establish it is obvious that the borrower will make the payments without suffering substantial hardship

Exception

Borrower **will** rely wholly or in part on income to repay. The lender must:

Borrower **will not** rely wholly or in part on income to repay. The lender must:

4AI Make reasonable inquiries by which borrower intends to make payments AND be satisfied on reasonable grounds the borrower will make payments without suffering substantial hardship

Consider if any other reasonable inquiries needed before finishing assessment

4AF(2)(a)(i) Estimate likely income

4AF(2)(a)(ii) Estimate likely relevant expenses

4AE Definitions
Relevant expenses means any listed outgoings in respect of the relevant period (excluding discretionary expenditure etc)
Listed outgoings
(a) Fixed financial commitments like accommodation costs, insurance, school fees;
(b) payments of any debts
(c) living expenses including utilities, food, personal expenses, childcare, transport
(d) any regular or frequently recurring outgoings other than savings and investments (for example, gym memberships, entertainment costs, or tithing) that are material to the estimate of relevant expenses and that the borrower is unable or unwilling to cease after the agreement is entered into or materially changed

4AJ(3)(a) Ask the borrower about each source of income and then:
• verify based on reliable evidence
• if verification not reasonable, consider whether source/amount realistic
• disregard income the borrower will not rely on.

4AJ(3)(b) Estimate income based on recent and reliable information the lender holds about the borrower's income, confirmed by the borrower

4AK(2)(a)(i) Ask the borrower about relevant expenses in sufficient detail

4AK(2)(a)(ii) Obtain at least 90 days of transaction records from the relevant bank

4AK(2)(a)(iii) Recent and reliable information that the lender holds about the borrower's expenses confirmed with the borrower

4AJ(2)(b) Ask the Borrower about any likely changes to income

4AM Expense adjustment
If expense information was obtained from borrower or risk initial estimate understates expenses the lender must do 1 or more of:
(a) verify the expenses with reliable evidence (90 days transaction records, copies of contracts or invoices, other evidence)
(b) for benchmarkable expenses(4AN) use the higher of the initial estimate or the benchmark
(c) if (a) or (b) not reasonably practicable – adjust expense with estimate of reasonable cost
Lender must consider if expenses below a reasonable minimum cost of living and adjust as required

Significant risk that the expenses are underestimated

No significant risk that expenses are underestimated

4AF(2)(b) Lender must be satisfied on reasonable grounds that it is likely the borrower will make the payments under the agreement without suffering substantial hardship because income exceeds expenses and
(i) there is a reasonable surplus to minimize risk that income is overestimated, expenses under estimates, or additional expenses will cause hardship OR
(ii) the estimates of likely income/expenses include reasonable buffers to minimize risks that income is overestimate, expenses under estimates, or additional expenses will cause hardship

Consider if other reasonable inquiries into affordability needed before finishing assessment

4AL sets out detail of how to calculate expenses for revolving credit contracts and expenses requiring lump sum payments

Record keeping

The lender must keep records about the inquiries made by the lender under section 9C (including the results of those inquiries). Those records must demonstrate how the lender has satisfied itself as to the matters in section 9C(3)(a), (4)(a), and (5)(a) (see section 9CA of the Act).

Guidance

Inquiries

- 5.1. A lender should be satisfied that the scope and methods of inquiry are reasonable and will provide satisfaction that it is likely that the borrower will make payments under the agreement without suffering substantial hardship.

Commentary

Regulations 4AF and 4AJ–4AO require lenders to make particular inquiries into the borrower's income and expenses.

- 5.2. Depending on the circumstances, it may be reasonable for the lender to make inquiries into matters in addition to those specified in the regulations to be satisfied that it is likely that the borrower will make payments without suffering substantial hardship (for example, where conflicting information is received in response to prescribed inquiries).

Initial estimate of expenses

Commentary

Regulation 4AK(2)(a) requires lenders to create an initial estimate of likely relevant expenses, based on three potential information sources: asking the borrower, bank transaction records, and information the lender already holds.

- 5.3. Under Regulation 4AK(2)(a), a lender can choose how they collect information about likely relevant expenses to create an initial estimate:
 - a. A lender can ask the borrower, use statements, or use other reliable information.
 - b. A lender can choose to use different methods or any combination of methods, for different relevant expenses.

- 5.4. For example, financial commitments may be identified through a combination of information sources, while living expenses may be estimated solely by asking the borrower to declare their living expenses in accordance with regulation 4AK(2)(a)(i).
- 5.5. Where lenders are asking borrowers about their relevant expenses under regulation 4AK(2)(a)(i) to estimate some likely relevant expenses, but have also obtained bank transaction records for another purpose, lenders may choose not to use the bank transaction records to estimate the amount of those expenses.
- 5.6. Regulation 4AF also requires lenders to consider the borrower's likely relevant expenses, which are those relevant expenses the borrower will incur over the relevant period, which is after the borrower takes out the loan.
- 5.7. A lender should only include expenses the borrower will have after taking out the loan.
- 5.8. A lender **may** omit an outgoing from their initial estimate where it is clear in the circumstances the outgoing will stop **once the agreement is entered into**. For example, if the borrower is borrowing to buy a home they will live in, then the lender can omit any existing expenses for renting.

Option 1

- 5.9. The definition of 'relevant expenses' provides that lenders may exclude discretionary expenditure from their initial estimate. Lenders who inquire into the borrower's current expenses through any of the means described in regulation 4AK(2)(a) (as part of estimating likely relevant expenses), should in the first instance capture expenses that have a significant risk of not being discretionary. If it would be material to the lending decision, or the lender otherwise chooses to do so, a lender may make further inquiries into expenditure that was captured in the first instance to identify and exclude discretionary expenditure that a borrower would cease or reduce. In considering these matters, lenders should have regard to the following assumptions:
 - a. Borrowers can cease or reduce most expenses that are not fixed financial commitments, payments of debts or essential living expenses, subject to further considerations below.
 - b. Some expenses may have underlying contractual requirements or significant break fees associated with ceasing them (e.g. some pay television subscriptions, gym memberships and bundled mobile phone plans), in which case they are likely to be financial commitments rather than discretionary expenditure.
 - c. Many borrowers have social or moral obligations and expectations that prevent them from ceasing certain expenditures, such as tithing or remittances to a family member overseas.
 - d. Most borrowers are unlikely to give up pets.
 - e. Some borrowers may have special circumstances that prevent them from ceasing or reducing certain expenditures. For example, a truck driver who is away from home for extended periods may not be able to cease or reduce takeaway expenses.

- f. Reducing some expenses may be expected to increase other expenses. For example, if a borrower who consumes most of their food from restaurants and takeaways were to cease these purchases, their grocery and electricity bills may increase.

Option 1 ends

Option 2

5.10. The definition of 'relevant expenses' provides that lenders may exclude discretionary expenditure from their initial estimate. In considering whether expenditure is discretionary expenditure that a borrower would cease or reduce, lenders may presume that expenses other than the following are discretionary, unless the lender has reason to believe that this is not correct for a particular borrower:

- a. fixed financial commitments – including any expenses with underlying contractual requirements or significant break fees associated with ceasing them (e.g. some pay television subscriptions, gym memberships and bundled mobile phone plans);
- b. payments of debts;
- c. essential living expenses; and
- d. regular or frequently recurring outgoings associated with tithing, remittances to a family member overseas, and pets.

Option 2 ends

5.9. ~~A lender may need to check with the borrower if a change is likely, or the extent of any change likely to other outgoings.~~

~~○ For example: if a lender believes that likely entertainment expenses will reduce, the lender may ask the borrower how much those current expenses will reduce by, to adjust the amount used.~~

~~○ For example: a borrower's food expenses may include dining out or takeaway expenses that that the borrower would be prepared to reduce by replacing them to some extent with eating at home more often.~~

5.10. ~~Where a borrower says they're willing to or can stop an expense (before taking out the loan or later, if needed), a lender should not include that expense in their initial estimate under Regulation 4AK.~~ During the initial estimate the lender can rely on what the borrower tells them will happen with their expenses unless the lender has reasonable grounds to believe that the information is not reliable. The lender does not need evidence that the expenses will be, or have, stopped or reduced.

5.11. Where a lender uses statements to create the initial assessment, the lender should still consider how the expenses in the statement may change and should clarify this with the borrower.

Commented [A1]: Examples are no longer apt, given that entertainment expenses and most dining out will generally be discretionary (not just potentially reduced after taking out the loan).

Commented [A2]: Proposed to remove this sentence as it duplicates guidance above that these expenses can be removed from the initial estimate.

Credit reports

- 5.12. The regulations require a lender to obtain a credit report, in certain circumstances. A credit report must cover credit information that is relevant to identifying the borrower's financial commitments, however it need not contain positive credit information.

Adjusting the initial estimate of borrower's likely relevant expenses

Commentary

Regulation 4AM gives lenders a choice of either verifying expenses against evidence or using a benchmark. If neither option is reasonably practicable, lenders may use a reasonable cost estimate.

This only applies where the initial estimate was based on asking the borrower about relevant expenses and under regulation 4AK(2)(a)(i) or where there is a significant risk that the initial estimate materially underestimates relevant expenses.

- 5.13. Lenders may use different methods to verify and adjust different types of expenses under Regulation 4AM. For example, where a lender asks a borrower for their living expenses under Regulation 4AK(2)(a)(i) the lender may choose to:
- a. compare the benchmarkable expenses against a benchmark and verify the remaining living expenses using statements; or
 - b. verify all living expenses using statements.
- 5.14. Where a lender can't verify the expenses against a benchmark or statements or other reliable information, the lender must compare the expense to a reasonable cost estimate.
- 5.15. Where a lender uses statements or other reliable information under Regulation 4AK(2)(a)(ii) or (iii), a lender is not required to verify those expenses further. The only exception is where there is a significant risk those statements, or other reliable information, could miss or understate the expenses.
- 5.16. For example, consider a borrower is borrowing money to buy a house. The lender uses statements to collect fixed financial commitments, debts, living expenses, and other regular and recurring outgoings. The lender also uses recent and reliable information about the likely rates on the property and asks the borrower what the insurance expense is likely to be.
- 5.17. As the lender asked the borrower about the likely insurance expense, the lender must verify that expense under Regulation 4AM. As the borrower hasn't taken out the insurance yet, the lender can't verify the expense through the borrower's statements. So, the lender compares it to a benchmark or uses a reasonable cost estimate. Or, the borrower may have received an insurance quote, and provides this to the lender as reliable information about that expense. The lender is otherwise satisfied there is no significant risk of missing or understating the

borrower's expenses having used the statements or recent and reliable information. The lender does not need to verify those expenses further under Regulation 4AM.

- 5.18. If the lender only used statements to collect those expenses, there may be a significant risk of missing or understating the borrower's expenses. The statements would not show expenses for insurance or rates that the lender knows would arise given the borrower is buying a home. The lender must further verify the expenses under Regulation 4AM, by comparing to benchmarks or using a reasonable cost estimate for the likely relevant expenses.

Further verification of information provided by borrowers, financial advisers or other intermediaries

- 5.19. Subject to requirements in the regulations to verify particular information about income and expenses, lenders may rely on the information provided to them by the borrower unless the lender has reasonable grounds to believe that the information is not reliable. Where the lender has reasonable grounds to believe the information is not reliable, the lender should take reasonable steps to verify the information provided by the borrower.
- 5.20. A lender may ask for or receive information from financial advisers or other intermediaries acting on behalf of the borrower. Where that is the case:
- a. A lender may rely on information provided to it by a financial adviser or intermediary as though it had been provided to it by the borrower.
 - b. A lender should require financial advisers and intermediaries to implement and maintain appropriate policies and procedures to collect information from the borrower and perform any necessary verification, and to train their staff on the Code and the lender responsibility principles. The lender, not financial advisers or other intermediaries, remains responsible for ensuring the lender complies with its responsible lending obligations.

Surpluses, buffers or adjustments

Commentary

This part of the Code provides guidance on how lenders should assess the adequacy of surpluses, buffers or adjustments provided in accordance with regulation 4AF(2)(b).

Regulation 4AF(2)(b) requires that the surplus, buffers or adjustments adequately address the risks that likely income may be overestimated, likely relevant expenses may be underestimated or the borrower may need to incur other expenses that cause them to suffer substantial hardship.

- 5.21. Lenders should seek to have a consistent set of surpluses, buffers or adjustments across credit products the lender offers to adequately address the risk that income is overstated or relevant expenses understated.
- 5.22. However, lenders may apply different surplus, buffers or adjustments across credit products to reflect the different risks of those products to affordability. For example, a lender may apply a different uncommitted monthly income requirement for a lower risk loan compared to a higher risk loan.
- 5.23. Whilst the amount of a surplus, buffer or adjustment is not prescribed, the amount must adequately address the risk. The determination of what is adequate will depend on the nature of the credit provided and the risk that income is overstated or relevant expenses understated. For example, a buffer or adjustment may depend on the size, term or revolving nature of the credit product. A surplus, buffer or adjustment may be a percentage amount or an absolute amount.
- 5.24. Where the interest rate under an agreement can vary, a lender should take account of the risk that interest rates may rise. Lenders should consider applying buffers to the loan's interest rate, to mitigate the risk that potential increases in the interest rate adversely impact on a borrower's capacity to repay. For example, lenders could:
 - a. use a single, sensitised interest rate (which includes a buffer) regardless of the loan's actual interest rate or use the loan's actual interest rate plus a margin (which functions as a buffer); or
 - b. apply an interest rate floor, to ensure the interest rate buffer applied reflects higher likely average interest rates over the longer term when operating in a low interest rate environment.
- 5.25. For interest only loans, where the interest only period is shorter than the term of the loan, lenders should consider assessing the borrower's ability to repay the loan on a principal and interest basis, excluding the interest-only period. For example, if the loan's term is 5 years, and the interest-only period will be 1 year, the lender should assess affordability over the 4 years of principal and interest.
- 5.26. Lenders should consider adjusting volatile, irregular, or variable income, for example discounting seasonal income, bonuses, overtime, rental income, or investment returns.
- 5.27. If a lender applies buffers or adjustments that adequately address the risk that likely income may be overestimated, that likely relevant expenses may be underestimated, or that the borrower may need to incur other expenses that cause them to suffer substantial hardship, the lender does not also need to apply a reasonable surplus.

Payments where there is an option to extend a loan term

- 5.28. Where the borrower asks for a loan term that is shorter than the maximum available for that credit product, lenders may assess the borrower's ability to repay the credit over a longer loan term, if all of the following apply:

- a. the lender has told the borrower that the longer agreement term is available, but the borrower wants to keep a shorter term as more suitable for them;
- b. the borrower has a right to extend the term of the loan up to the longer term at any time without fee, and the borrower is aware of this ability;
- c. the borrower is aware that repaying over a shorter term may require more financial commitment or a further reduction in expenses; and
- d. the agreement is not a high-cost consumer credit contract.

Example

Borrower B is seeking a home loan of 25 years, but the maximum available for that product that the borrower can obtain is 30 years. The lender may assess the borrower's ability to repay the credit over 25 years, or over a longer period, up to 30 years.

Joint expenses

Commentary

This part of the Code provides guidance on how lenders should estimate a borrower's likely relevant expenses when a borrower shares expenses with others.

Some of the borrower's relevant expenses may be shared with other people (for example, a partner, spouse, or extended family).

- 5.29. Where the lending is joint between two or more borrowers, the lender should consider each borrower's individual relevant expenses, any relevant expenses the borrowers share together, and any relevant expenses each borrower shares with any other person.
- 5.30. Where the lending is to one borrower, the lender should consider that borrower's individual relevant expenses, and any relevant expenses that borrower shares with any other person.
- 5.31. When estimating the borrower's likely relevant expenses, lenders should consider whether it is appropriate to apportion shared expenses in the circumstances. If so, lenders should consider:
 - a. whether a known amount for that borrower's individual contribution to the shared expenses is reasonable and can be used (for example, a borrower who is in a flatting situation contributes \$30 a week towards power); or
 - b. whether apportioning expenses based on the salary of the borrower and other parties is appropriate in the circumstances; or
 - c. whether to apply the whole amount of the expense.

Example

A couple, A and B, have a joint home loan and a joint bank account into which they each have their income paid. A applies to a lender, L, for a personal loan, with A as the sole debtor. In apportioning payments on the shared home loan, L decides it is appropriate to apportion according to A's share of A and B's joint income.

- 5.32. In considering how to apportion shared expenses, the lender should take into account any information provided by the borrower about how their expenses are apportioned between them and others.
- 5.33. Lenders should consider the approach they will take when apportioning shared expenses to reduce the risk that the expenses are underestimated. If relevant, the lender should also consider whether the apportionment itself is likely to change over the relevant period. For example:
- If the partner of an individual borrower's income is known to be reducing during the period of the loan, and it is likely the proportion of expenses the borrower will need to meet will increase from 50% to 90%.
 - If a tenant with their name on the house lease shares rent and other expenses with flatmates who are not on the lease, the lender should consider whether there is a risk that the tenant will become liable for a greater share of those expenses.

Existing buy now pay later (BNPL) facilities

- 5.34. **If a borrower has an existing buy now pay later facility, any payments due should be treated as debt payments under the definition of listed outgoings.**

Commented [A3]: Query whether this guidance is necessary. Proposed amendment to 4AL carves buy now pay later schemes that are revolving credit contracts from 4AL(2). Payments due are treated the same as payments due on any other credit contract.

Exception to general rule if it is obvious there will be no hardship

Commentary

Regulation 4AG provides an exception from regulation 4AF (full income and expense estimates) if the lender makes inquiries that are sufficient to establish that it is obvious in the circumstances of the particular case that the borrower will make the payments under the agreement without suffering substantial hardship, so as to make the inquiries required by regulation 4AF disproportionate.

- 5.35. Lenders may establish that the exception in regulation 4AG applies by:
- undertaking some of the inquiries that would ordinarily be required by regulation 4AF and halting these inquiries once they are sufficient to establish that the 'obvious' test in regulation 4AG is met; or

- b. undertaking different inquiries in accordance with section 9C(3)(a) of the Act that are sufficient to establish that the 'obvious' test in regulation 4AG is met.
- 5.36. For the avoidance of doubt, credit scores and repayment history will not, in themselves, be decisive as to whether affordability is obvious. This is because, while past borrowing behaviour is relevant to the inquiry, it does not mean that previous lending was affordable without substantial hardship, and also does not automatically mean that any future loan will be affordable without substantial hardship.
- 5.37. Whether it is obvious that a borrower can meet their obligations under the agreement without suffering substantial hardship under section 9C(3)(a) is context specific. In establishing that, the lender could consider the below guidance where that this test may be met. Regulation 4AG may be met in other ways.
- 5.38. Scenario 1: A lender is likely to have sufficient evidence of obvious affordability where all of the following applies:
- a. a proposed material change is a small percentage of the total credit limit or unpaid balance of the contract;
 - b. the lender makes reasonable inquiries into the borrower's likely income as if Regulation 4AJ applies;
 - c. the lender makes reasonable inquiries into the borrower's likely expenses and obtains a credit report;
 - d. the lender makes reasonable inquiries into any other debts the borrower has;
 - e. the lender confirms with the borrower that there have not been any material adverse changes to the borrower's finances since they took out the original lending or last made a material change; and
 - f. the lender is satisfied the borrower's income is likely to exceed the borrower's expenses, including the material change.

Example:

A material change of \$10,000 is less than 5% of a total credit limit of \$250,000. The lender makes reasonable inquiries into the borrower's current income and other debts and confirms with the borrower that there have not been any adverse changes to their circumstances since they last borrowed. The lender is satisfied the borrower's income exceeds their likely expenses. The lender has sufficient evidence that it is obvious that the lending is affordable.

- 5.39. Scenario 2: A lender is likely to have sufficient evidence of obvious affordability where all of the following applies:
- a. the agreement is intended to be temporary (lasting no more than 3 months);

- b. the lender is satisfied the borrower is meeting their current expenses through their current income; and
- c. the borrower has confirmed the agreement will be repaid from a bonus, commission, or one-off or permanent increase to income that is verified in writing.

Example

The borrower is wanting to borrow \$10,000 for a holiday. The lender has made reasonable inquiries and verified the amount will be repaid in full from an expected bonus that is due to be paid by their employer in two months' time. The lender has sufficient evidence it is obvious the lending is affordable.

- 5.40. Scenario 3: A lender is likely to have sufficient evidence of obvious affordability where all the following applies:
- a. the lender makes reasonable inquiries into the borrower's likely income as if Regulation 4AJ applies;
 - b. the lender makes reasonable inquiries into the borrower's expenses and obtains a credit report;
 - c. the lender makes reasonable inquiries into any other debts the borrower has; and
 - d. the lender is satisfied the borrower's income is likely to exceed the borrower's expenses, including the new lending, with a large surplus.

Example

The lender makes reasonable inquiries and verifies the borrower's current income of \$6,000 per month, fixed financial commitments of \$400 per month and debts of \$1,000 per month. The lender obtains satisfactory credit report. The lender asks the borrower what their living expenses are, and benchmarks these where appropriate. The lender is satisfied that the borrower's income exceeds those expenses, including the new lending, by over \$1,500 a month. The lender has sufficient evidence it is obvious the lending is affordable.

Record keeping

Commentary

This part of the Code illustrates the kind of information that lenders should consider keeping to meet sections 9CA(1) and (2) of the CCCFA. These records are kept for 'successful' assessments in which a lender has entered into an agreement or agreed a material change with a borrower.

Lenders are required to ensure their records are fit for their intended purpose, including disclosure on demand to the Commission, dispute resolution service, the borrower, or guarantor.

However, the way information is presented by a lender under section 9CA(3) to (6) may depend on the way in which the lender collected and recorded information, verified that information where required, and made its assessments under section 9C(3)(a), (4)(a), and (5)(a).

- 5.41. Where the lender has followed the approach in regulation 4AF, the lender should keep a record of:
- a. the borrower's likely income on a weekly, fortnightly, or monthly basis;
 - b. the reliable evidence for that likely income or, if verification was not reasonably practicable, a concise summary as to why the source and amount were realistic ;
 - c. a statement about any likely changes to the borrower's income disclosed by the borrower;
 - d. the borrower's likely relevant expenses on a weekly, fortnightly, or monthly basis;
 - e. a list of relevant expenses, or groups of relevant expenses (eg living expenses), and the initial estimates used by the lender for each;
 - f. where those likely relevant expenses were derived by using 90 days' of transaction records or other reliable evidence, copies of that information;
 - g. any information or documents obtained when making reasonable inquiries into whether financial commitments were omitted, like a credit report;
 - h. where those likely relevant expenses were verified by using 90 days' of transaction records or other reliable evidence, copies of that information;
 - i. where those likely relevant expenses were benchmarkable expenses and were compared against a benchmark, a list of the relevant expenses or groups of relevant expenses that were benchmarked and a brief description of the benchmark;
 - j. where any likely relevant expenses were adjusted by estimating a reasonable cost for the expense, a statement to that effect and a list of relevant expenses that were estimated;
 - k. where any living expenses were compared to a reasonable minimum cost of living for a person in similar circumstances to the borrower, a statement to that effect and a list of relevant expenses or groups of relevant expenses that were adjusted;
 - l. if a buffer or adjustment (in accordance with 4AF(2)(b)(ii)) was applied to income or a relevant expense, a statement to that effect;
 - m. a list of relevant expenses, or groups of relevant expenses (eg living expenses), and the final estimates of those expenses used by the lender; and
 - n. any other inquiries made under section 9C(3)(a)(ii).

5.42. In recording how the lender satisfied itself as to the matters in [section 9C\(3\)\(a\)\(ii\)](#) where the approach in [regulation 4AF](#) was followed, the lender may choose to capture a concise summary of the lender's decision or some other record of how the lender satisfied itself. This may include references to its policies or procedures and how they were applied. For example, the lender could keep a record summarising that:

- a. the lender was satisfied based on inquiries made that the borrower's likely income of \$(amount) exceeded their likely relevant expenses of \$(amount); and
- b. the lender was satisfied based on inquiries made that:
 - i there was a reasonable surplus to adequately address the risk that likely income may be overestimated, likely relevant expenses underestimated, or that the borrower may need to incur other expenses that cause them to suffer substantial hardship;
 - ii the lender's estimates of likely income and likely relevant expenses included reasonable buffers or adjustments to adequately address the risk that likely income may be overestimated, likely relevant expenses underestimated or that the borrower may need to incur other expenses that cause them to suffer substantial hardship.

5.43. Where the lender has used the exception in [regulation 4AH\(1A\)](#), the lender should keep a record of:

4AH Option 1:

- a. the specific inquiries that were made to establish that the borrower's total monthly repayments in their new arrangement are lower than the borrower's monthly payments in their previous arrangement.

4AH Option 2:

- a. the specific inquiries that were made to establish that the borrower's total credit limit in their new arrangement with Lender B has not increased, or has increased only to the extent reasonably necessary, from their total credit limit under their previous arrangement with Lender A; and
- b. the specific inquiries that were made to establish the total daily interest charged in the borrower's new arrangement is equal to or less than the total daily interest charged in the borrower's previous arrangement.

5.44. Where the lender has used the exception in [regulation 4AG](#), the lender should keep a record of:

- a. the specific inquiries that were made to establish that it is obvious in the circumstances of the particular case that the borrower will make the payments under the agreement without suffering substantial hardship;
- b. the results of those inquiries; and

- c. the lenders' reasons why it is obvious in the circumstances of the particular case that the borrower will make the payments under the agreement without suffering substantial hardship.
- 5.45. Where the lender has followed the approach in regulation 4AI, the lender should keep a record of any specific inquiries made into the means by which the borrower intends to make the payments under the agreement and the results of those inquiries, including any documents or information relied on.
- 5.46. In recording how the lender satisfied itself as to the matters in section 9C(3)(a)(ii) where the approach in regulation 4AI was followed, the lender may choose to capture a concise summary of the reasons for the lender's decision. For example:
- a. the lender was satisfied based on inquiries made that the borrower has listed their existing property for sale and the likely sale proceeds will be sufficient to repay the lending by the end of the loan term;
 - b. the lender was satisfied based on inquiries made that the borrower has funds on term deposit that will be sufficient to repay the lending by the end of the loan term.

High-cost consumer credit contracts

Commentary

This part of the Code provides guidance for lenders under high-cost credit agreements when assessing whether the borrower has existing high cost loans or has had high cost loans within the preceding 90 days.

Under section 45F and section 45G of the Act, lenders are prohibited from entering into high-cost credit contracts with certain borrowers. Regulation 4AO applies a rebuttable presumption of substantial hardship if the lender has reasonable evidence that the borrower has defaulted in payment on a consumer credit contract in the preceding 90 days.

In the case of a high-cost consumer credit contract, a lender may not enter into a high cost credit contract with a debtor who:

- *has unpaid balance on any high-cost consumer credit contract with another creditor (s 45F(1)(a));*
- *has had, at any time within the preceding 15 days, an unpaid balance on any high-cost consumer credit contract with another creditor (s 45F(1)(b));*
- *has entered into 2 or more high-cost consumer credit contracts at any time within the preceding 90 days (s 45G(1)); or*
- *has been in default under one or more loans in the preceding 90 days. (see section 45F, section 45G and regulation 4AI).*

Lender's inquiries – high cost lending

5.47. In making reasonable inquiries, a lender should obtain information through all of the following:

- a. explaining to the borrower what a high-cost loan is;
- b. asking the borrower if they have entered into any high-cost loans in the past 90 days with another lender, and if so, determining the dates on which those contracts were entered;
- c. asking the borrower if they currently have any high-cost consumer credit contracts with another lender, or have repaid any high-cost consumer credit contracts with another lender over the past 15 days;
- d. collecting information from the borrower that would enable the lender to determine whether the borrower's recent or existing loans are high cost loans – eg copies of the contracts, or if these are unavailable, standard contracts or loan disclosures that may give a range of the interest rates of the relevant loans;

- e. verifying the information provided by the borrower and checking for any contracts that may have been omitted through:
 - i asking the borrower about any other names they use, and checking their own loan record systems and those of any associated lender;
 - ii bank statements (looking for deposits from other lenders, or outgoings to other lenders);
 - iii reviewing credit reports for enquiries or defaults;
 - iv asking the borrower for evidence that a high-cost consumer credit contract with another lender has been repaid; and
 - v going back to the borrower to clarify any discrepancies.

Pawnbroking

Commentary

Pawnbroking transactions are subject to and must comply with both the Act and the Secondhand Dealers and Pawnbrokers Act 2004 (SDPA).

For a pawnbroking transaction, a borrower can make payments under the agreement in the form of either:

- *monetary payment of the redemption price (as defined under the SDPA); or*
- *the sale of the pledged item by the lender on behalf of the borrower.*

- 5.48. In assessing whether it is likely the borrower can make payments without substantial hardship, the lender under a pawnbroking transaction may inquire into and assess:
 - a. whether the borrower can pay the redemption price through monetary payments without substantial hardship by making inquiries in accordance with regulations 4AF and 4AJ–4AO; or
 - b. whether the borrower can make the payments through a sale of the pledged item without substantial hardship, in accordance with regulation 4AI. Sale of the pledged item may cause substantial hardship to the borrower if the item is essential to the borrower.
- 5.49. If the lender makes an assessment under paragraph **5.46.b**, the lender should be satisfied that an item is not essential, taking into account the borrower’s circumstances.

Commentary

Regulations 4AJ(3)(a)(i) and 4AM(2)(a)(i) require verification (or allow for verification) of some information provided by the borrower about their income and expenses.

Borrowers may provide other information for the purposes of the lender's inquiries into whether the agreement is affordable.

[...]

7 Assisting borrowers to make an informed decision

Legal obligations

Principle

Every lender must, at all times, comply with all the lender responsibilities specified in subsections 9C(3), (4) and (5) (see [section 9C\(2\)\(a\) and \(b\)](#) of the Act).

Lender responsibilities

A lender must exercise the care, diligence, and skill of a responsible lender:

- *in any advertisement for providing credit or finance under an agreement or for providing credit-related insurance under a relevant insurance contract; and*
- *before entering into an agreement to provide credit or finance or a relevant insurance contract and before taking a relevant guarantee; and*
- *in all subsequent dealings with a borrower in relation to an agreement or a relevant insurance contract or a guarantor in relation to a relevant guarantee.*

A lender must, in relation to an agreement with a borrower or when providing credit-related insurance, assist the borrower to reach an informed decision as to whether or not to enter into the agreement or relevant insurance contract and to be reasonably aware of the full implications of entering into the agreement or contract, including by ensuring that:

- *any advertising complies with advertising standards set out in the regulations and is not, or is not likely to be, misleading, deceptive, or confusing to borrowers;*
- *the terms of the agreement are expressed in plain language in a clear, concise, and intelligible manner;*
- *any information provided by the lender to the borrower is not presented in a manner that is, or is likely to be, misleading, deceptive, or confusing*
- *reasonable steps are taken to offer to the borrower information about the agreement in another language (language A) if:*
 - *advertising that is wholly or significantly in language A is being, or within the preceding 6 months has been, distributed to the public or a section of the public; and*

- *the steps are necessary to ensure that the borrower can reach an informed decision (for example, if the borrower may not have a good understanding of the language in which the lender is otherwise providing information to the borrower under this Act) (see [section 9C\(3\)\(b\)](#) of the Act).*

Commentary

The lender responsibility to assist informed decisions is separate from, and additional to, the lender's obligations under the Act to:

- *publish standard form credit agreements and costs of borrowing information; and*
- *make initial disclosure of key information set out in [Schedule 1](#) of the Act and of all terms of the contract.*

Guidance

Advertising

- 7.1. See the earlier Guidance in [Chapter 3](#).

Communicating key features

- 7.2. To assist a borrower to make an informed decision as to whether to enter into an agreement and to be reasonably aware of the full implications of entering that agreement, a lender should inform the borrower of the key features of the agreement. The lender (or their agent) should clearly highlight those features in a way that draws the borrower's attention to that information. This information should be provided at a time that assists the borrower to make an informed decision. The key features should include:
- a. the amount of credit or finance under the agreement and the term of the agreement, if any;
 - b. the amount of any establishment fees and any other mandatory fees the borrower must pay when entering the agreement, and information on whether other interest or fees, including periodical or event-based fees, may be charged over the loan term;
 - c. any non-avoidable fees or charges for additional goods or services provided under the agreement;
 - d. in relation to any fees or charges to be financed under the agreement but which could be paid for separately (for example, premiums for insurance related to the credit, extended warranties or repayment waivers), that financing these under the agreement

means the borrower pays additional interest costs and the amount the borrower will ultimately pay will be larger;

- e. interest rates expressed as an annual rate (in terms of a percentage), and the total amount of interest payable, if ascertainable (but the lender may choose not to include the total amount of interest if the agreement would not, on the assumptions prescribed by regulations under the Act, be paid out within 7 years of the date on which credit is first provided under the agreement);
- f. where relevant, repayments on a periodic basis and the total amount of payments, if ascertainable (but the lender may choose not to include the total amount of payments if the agreement would not, on the assumptions prescribed by regulations under the Act, be paid out within 7 years of the date on which credit is first provided under the agreement);
- g. the cancellation period under section 27 of the Act and under section 36 of the Fair Trading Act 1986, and any other cancellation rights that the lender may offer;
- h. key risks and characteristics of the specific product. For instance, where applicable:
 - i that secured property is at risk if the borrower defaults or does not make the repayments, including in the context of a pawnbroking transaction;
 - ii the fact that the interest rate is variable or that the lender has the power to unilaterally change the interest rate;
 - iii that a prepayment fee may be payable under a fixed-rate agreement if the borrower repays some or all of the credit early;
 - iv the rate of any default interest and the amount of any default fee;
 - v for reverse equity mortgages:
 - how the reverse equity mortgage agreement works;
 - how the following can affect the borrower's net equity in the home: the amount of any loan being considered, changes in interest rates or the value of the home, and life expectancy (these may be highlighted through a home equity release calculator);
 - whether the borrower has a right to occupy the home for the rest of their life;
 - whether the borrower's liability under the agreement is or is not limited to the net realisable sale price for the home; and
 - the borrower's obligations to maintain the home;
- i. for buy-back transactions:

- i how the buy-back transaction works;
 - ii whether the borrower has a right to occupy the home for the rest of their life;
 - iii the amount and frequency of rental payments;
 - iv the terms of the borrower's right to repurchase, including the purchase price or how and when it will be calculated; and
 - v the borrower's obligations to maintain the home.
- 7.3. For borrowers who are refinancing an existing agreement, lenders may instead of highlighting the key features listed in paragraph 7.2, highlight to the borrower any differences in the key features between the refinancing agreement and the existing agreement, if known.
- 7.4. **If the lender is aware that the borrower is having financing difficulty and seeks to refinance an existing agreement with another lender, before proceeding a lender should:**
- a. check with the borrower that they have considered seeking repayment relief from their existing lender;
 - b. provide information about other options (such as how to contact a financial mentor, or personal insolvency); and
 - c. if their existing agreement is unsecured and the new agreement is secured, specifically point out the implications of this.
- 7.5. A lender should respond promptly to a borrower's requests for further information about the features of the agreement. Where a lender allows borrowers to arrange credit online or remotely, a lender should ensure that borrowers are provided with a simple, clear and timely way to seek further information from the lender.

Example

Lender L allows credit to be arranged via its website. Lender L provides a free call number, local rate telephone number or live web chat system for borrowers who wish to seek further explanation.

Legal advice

- 7.6. A lender should generally recommend that borrowers seek independent legal advice when the lender is aware that:
- a. more than one party will be the borrower under a credit agreement, but that only one of those parties will receive the direct benefit of all money lent; or
 - b. any borrower may be under undue influence from any other party, including another borrower or any third party who will receive the direct benefit of all money lent.

- 7.7. The lender should recommend that the independent legal advice be sought from a lawyer who is not also advising another borrower, guarantor or a third party who may be exerting undue influence over the borrower.
- 7.8. The lender should, where reasonably practicable, make these recommendations to the relevant borrower without the presence of other borrowers or guarantors, or any third parties who the lender has reasonable grounds to believe may be exerting undue influence over the borrower.
- 7.9. A lender should require borrowers to seek independent legal advice when entering into reverse equity mortgages or buy-back transactions. The lender should require that the independent legal advice be sought from a lawyer who is not also advising the lender in the proposed transaction.

Commentary

Lenders providing reverse mortgages and buy-back transactions may also refer to the Ministry of Social Development's Home Equity Release Schemes Code of Standards.

Guidance

Means and level of communications

- 7.10. A lender should highlight the key features identified at paragraph **7.2** to the borrower in a way that draws the information to the attention of the borrower and assists an informed decision, regardless of the channel through which credit is arranged.

Example

Borrower B is seeking credit from Lender L at Lender L's premises. One way that Lender L can draw the information about key features to the attention of Borrower B is by providing Borrower B with a credit agreement and explaining the key features of the agreement while at the same time highlighting the parts of the agreement relating to those key features.

- 7.11. A lender should be satisfied that the level of assistance provided when informing the borrower of the key features and the extent of any additional assistance provided (referred to below) will be sufficient to assist the borrower to reach an informed decision and to be reasonably aware of the full implications of entering into the agreement.
- 7.12. The level of explanation and assistance that are reasonable for a lender to provide when informing the borrower of the key features identified at paragraph **7.2** may differ depending on the circumstances. Greater or further assistance should be provided when informing the borrower of the key features where:

- a. there is a greater risk that a borrower may not be aware of the implications of entering into the agreement. This includes where:
 - i the agreement is complex or uncommon, such as a buy-back transaction or reverse equity mortgage;
 - ii the agreement is a high-cost credit agreement;
 - iii the borrower is a **vulnerable borrower**;
 - iv the borrower would be a new customer of the lender; or
 - v there is a greater risk that the borrower will not be able to comply with the agreement. This includes where the size of the loan is large relative to the borrower's ability to repay; or
- b. the consequences of the borrower not being able to comply with the agreement may be serious. This includes where:
 - i the potential consequences include the loss of a significant asset; or
 - ii the default interest plus default fees are high relative to the amount of the loan or the credit limit.

7.13. A lender may provide a lower level of assistance when informing the borrower of the key features where there is a low risk that a borrower may not be aware of the implications of entering into the agreement. This includes where:

- a. the credit agreement is a simple credit agreement that is widely understood, such as an overdraft; or
- b. the borrower will receive legal advice before entering into the agreement; or
- c. the borrower is a well-informed user of credit.

7.14. A lender should allow borrowers a sufficient opportunity to fully consider an offer of credit, including by:

- a. giving the borrower the opportunity to take information about the key features off-site where the credit is arranged in person;
- b. giving the borrower the opportunity to seek the advice of others; and
- c. making clear that the offer of credit is available for a reasonable period specified by the lender (subject to the closing dates of special promotional offers that are open for a reasonable period of time and changes to market pricing).

7.15. Where a lender reasonably suspects that the borrower does not have a good understanding of the language the lender is using to communicate with the borrower, a lender should provide, or refer the borrower to alternative mechanisms for receiving the relevant information. This could involve the lender providing access to, or referring the borrower to, an interpreter or

member of staff who is fluent in the relevant language or providing access to the information in that particular language. A lender should not rely on children under 18 or those with a potential conflict of interest to act as interpreters; for instance, where a parent is obtaining a loan for an adult child's benefit, the child should not be an interpreter. (See additional guidance below where a lender advertises in another language at paragraphs **7.22 to 7.24.**)

- 7.16. Where the lender has explained the key features of the agreement in detail but the lender is aware that the borrower has not understood the key features of the agreement as explained by the lender, a lender should take further steps to assist the borrower's understanding. For instance, the lender could provide further assistance by recommending that the borrower takes away a copy of the contract and other information provided and seeks legal advice or advice from organisations that provide information about consumer rights to obtain a better understanding of the implications of the agreement.

Online credit applications

- 7.17. Regardless of the channel(s) used for credit applications, a lender must assist the borrower to reach an informed decision as to whether or not to enter into the agreement and to be reasonably aware of the full implications of entering into the agreement.
- 7.18. In online formats, it may be more difficult to gauge whether the borrower has understood the terms of the contract, compared to in-person interactions. Where a lender provides an online application process, a lender should take reasonable steps to ensure that the borrower understands the key features before entering into the loan agreement.
- 7.19. As well as providing the key information in paragraph **7.2** in an online format, this includes:
- a. expressly encouraging prospective borrowers who wish to have the information explained further, or who may be unsure about the meaning or effect of the information provided to contact the lender for assistance before making a decision to enter into the credit agreement, and
 - b. contacting a prospective borrower by other means prior to entering into a credit agreement, in cases where:
 - i the lender knows from previous interactions with the borrower that the individual is unlikely to understand the nature of the transaction or information provided online (for instance because they do not have a good understanding of English or because they do not have basic knowledge about financial matters); or
 - ii where the lender's staff evaluating the application identify that the individual may not have a good understanding of English or may not have a basic knowledge about financial matters (eg. based on the individuals' answers on the application form or the staff member's other interactions with the individual).
- 7.20. In addition, a lender may also make available on their website a standard contract for different types of lending, with the key features highlighted.

Example

Borrower B is seeking credit from Lender L through Lender L's website. One way that Lender L can draw the information about key features to the attention of Borrower B is by ensuring that the borrower progresses through (and is unable to skip) screens that highlight information about the key features, giving the borrower the opportunity to see and read the explanations provided, and including prominent prompts encouraging Borrower B to ask questions, or request the information be explained verbally by a staff member.

Example

Borrower A has misunderstood the meaning of some questions in the online application form. In speaking with B to obtain the correct information, Lender C's staff member notices that Borrower A is not a confident speaker of English but can understand and respond to the staff member's questions when they are put to them verbally as part of a conversation. Lender C ensures that the information in paragraph 7.2 is provided as a phone conversation rather than relying only on the online presentation.

Further steps for lenders

- 7.21. Nothing in this section of the Code is intended to suggest that lenders should routinely ask questions specifically for the purpose of determining whether a borrower is vulnerable, may not have a good understanding of the lender's usual language, or may not have understood the information provided, in circumstances where lenders otherwise have no reason to suspect this to be the case.

Advertising in another language

Commentary

A lender must take reasonable steps to offer the borrower information about the agreement in another language if the lender is advertising in that language, and if this is necessary to ensure the borrower can reach an informed decision.

This obligation applies only if a lender distributed advertising that was wholly or significantly in another language to the public or to a section of the public in the previous 6 months. This obligation generally only applies to systematic advertising. For instance, a newspaper advertisement in another language would constitute an advertisement to the public or a section of the public, but an ad hoc discussion with an individual borrower by an employee of a lender in another language would not.

This obligation only applies to credit advertising and does not cover general brand advertising or advertising relating to non-credit products.

- 7.22. Where the lender has advertised in a language in the previous 6 months, a lender must take reasonable steps to offer information about the loan in the advertising language for the borrower to make an informed decision about entering the agreement.
- 7.23. Lenders should establish processes that give borrowers opportunities to opt in to receive information in the advertising language at relevant points before an agreement is entered into. Lenders may provide these opt-in opportunities in different ways, for example:
- a. Lenders may include a question in an application form about the borrower's primary language and whether the borrower would like to receive information in this language.
 - b. Lenders may advise borrowers that information is available in other languages when dealing with the borrower in person.
- 7.24. Where a lender reasonably suspects that the borrower does not have a good understanding of the lender's usual language and the lender knows that the borrower speaks the advertising language, the lender should offer to provide information about the type of agreement in the advertising language. Some of the ways that lenders may offer this information include:
- a. the lender may offer translated material in the advertising language that provides the borrower with the key features of the agreement (as per paragraph **7.2**); or
 - i by providing a key information sheet which includes:
 - ii Information about the type of loan and its features, including how interest is calculated and charged, and the nature of security taken;
 - iii Information about the right to cancel, what to do in the event of repayment difficulties and the lender's dispute resolution scheme; and
 - iv a translation guide on where to locate information about the loan amount, term, repayments, total interest and total amounts payable, within the loan agreement;
 - or
 - b. the lender may refer the borrower to an interpreter or a member of staff who is fluent in the advertising language or to translation services (at the lender's cost).

Plain language agreement

- 7.25. To comply with the lender responsibility to ensure that the terms of the agreement are expressed in plain language in a clear, concise, and intelligible manner, a lender should:
- a. set out agreements using a layout and font size that can be easily read;
 - b. set out the terms in a logical order that is easy for borrowers to follow;
 - c. highlight important information; and
 - d. explain complex information in plain language and include a clear explanation of any necessary jargon.

- 7.26. “Concise” refers to the presentation of specific information rather than the overall length of the communication or document. A longer but clearly written document, may take less time to read and understand than a shorter, but poorly written one.
- 7.27. “Intelligible” involves an overall assessment of whether the terms are understandable and comprehensible to borrowers in the target market.

Example

Lender L is putting together terms for a new credit product. Potential steps the lender could take to ensure that the agreement is in plain language in a clear, concise, and intelligible manner include:

- *using a communications or plain language adviser to help prepare the terms of their new credit product;*
- *consulting a focus group.*

*The focus group could be made up of a representative group of consumers (including individuals with no experience in credit agreements) and a **financial mentor**. The lender could ask the focus group to review whether the terms are clear, concise and intelligible, and take into account the focus group's feedback to refine the agreement.*

Manner of presenting information

7.28. To ensure that any information provided by the lender to the borrower is not presented in a manner that is, or is likely to be, misleading, deceptive, or confusing, a lender should apply the following Guidance to all information provided to the borrower in relation to the agreement before it is entered into, regardless of the form and time at which information is given.

7.29. A lender should comply with the following practices to ensure that information provided to the borrower is not misleading, deceptive or confusing:

- a. make sure important information is legible or audible, or both, and take care to disclose information in a level of detail that is commensurate with the importance of it;
- b. use technical language and statistics only where they are relevant and in a way that can be readily understood by consumers without specialist knowledge;
- c. where referring to fees or costs, avoid giving an unrealistic impression of the overall levels of fees and costs;
- d. where referring to an interest rate or an amount of interest:
 - i. convey with equal importance as any other interest rate or amount of interest an annual percentage interest rate;
 - ii. advise if that rate is fixed, variable or capped; and
 - iii. advise if fees will apply, and, if ascertainable, provide the amount of any establishment fees and any other mandatory fees the borrower must pay when entering into the agreement;
- e. where referring to the amount of regular repayments for a particular term loan, include an indication of the total costs of borrowing, which could be through an indication of:
 - i. the total amount payable under the agreement, if ascertainable (but the lender may choose not to include the total amount of interest, if on the assumptions

prescribed in the regulations under the Act, the agreement will not be paid out within 7 years of the date on which credit is first provided under the agreement);
or

- ii how the total amount payable under the agreement will be calculated;
- f. when referring to the amount of regular payments, the amount of any lump sum payments and when they are required to be made;
- g. when providing details of interest rates or fees that apply for an initial promotional period, state the period for which the discount applies and:
 - i where ascertainable, what the interest rate or fees will change to after that initial promotional period; or
 - ii where the subsequent interest rate is not ascertainable, how the subsequent interest rate will be calculated.

Processes

7.30. To comply with the above lender responsibility principle and lender responsibilities, a lender should have policies and procedures in place to ensure that any information it gives a borrower complies with legal obligations and is not misleading, deceptive, or confusing. Such policies and procedures may also include complying with relevant industry codes.

7.31. A lender's policies and procedures should include:

- a. requiring relevant staff and agents who have customer contact on the lender's behalf to comply with the Act, Regulations, Fair Trading Act 1986 and the Guidance in this Code and the lender being satisfied that they understand how to do so;
- b. being satisfied that relevant staff and agents who have customer contact on the lender's behalf are familiar with the features of the credit products which they deal in, as well as current promotions and representations; and

requiring that all online, print and other promotional materials are subject to an approval process, including being checked by a staff member with necessary product knowledge to ensure that the description is accurate.