Submission on *Exposure draft of Credit Contracts and Consumer Finance Amendment Regulations (No 2) 2022 and updated Responsible Lending Code*

Your name and organisation

Name	Shula Newland
Organisation (if applicable)	FULL Balance Financial Coaching
Contact details	Privacy of natural persons

[Double click on check boxes, then select 'checked' if you wish to select any of the following.]

☐ The Privacy Act 2020 applies to submissions. Please check the box if you do <u>not</u> wish your name or other personal information to be included in any information about submissions that MBIE may publish.

☐ MBIE intends to upload submissions received to MBIE's website at www.mbie.govt.nz. If you do <u>not</u> want your submission to be placed on our website, please check the box and type an explanation below.

I do not want my submission placed on MBIE's website because… [Insert text]

Please check if your submission contains confidential information:

☐ I would like my submission (or identified parts of my submission) to be kept confidential, and **<u>have stated below</u>** my reasons and grounds under the Official Information Act that I believe apply, for consideration by MBIE.

I would like my submission (or identified parts of my submission) to be kept confidential because… [Insert text]

Introduction

About us

Full Balance Financial Coaching and its social enterprise, AffordIt NZ are one of the **few companies in the country** that provides affordable Independent Financial Planning and Financial Coaching service. As part of this service, we concentrate on the income and expenditure by clients as the base for coaching clients to build better financial behaviour and grow their financial security.

As part of our process, **we are all day, every day, assessing how people spend their money and** the changes they can make in their income and expenditure to get affordability for their current loan payments or future aspirations. So feel we are in a **good position to comment on how affordability can be calculated in a robust and accurate way**😊

We started the **social enterprise AffordIt NZ, to ensure those that got declined loans especially for essential costs, had access to other resources and help**. And also to promote the importance of True Affordability for loans, so that people weren't put into hardship.

We hold the major contract for Employee Assistance Program (EAP), and as such are dealing with the everyday working person that is either under stress with their finances, going through change or wanting to do better with their finances. We service a wide range of clients varying from those that are struggling due to debt and the burden of living costs, to those that are wanting to buy their first home, to those that are wanting to know how much they need for their retirement. Understanding how they spend their money and what basic requirements are needed for living, is a big part of this.

We have been **involved in the evolution of the of remedies to fixing the debt issue since 2011**, right back when the government started seeking feedback. Having dealt with many, many clients under loan stress we **saw the damage that was done by unaffordable loans** (even when the original responsible lending legislation was in place).

We in general **support the current legislation as it was**, but think looking at current expenses and then asking the borrower about future likely changes in expenses – as is done for the income, is a better way to go about an accurate robust assessment of expenses. Otherwise the **lenders and the borrowers could make anything up**, and there are only limited benchmarkable expenses (which represent an average person, not the person going for the loan).

We have **concern that some of the changes already introduced and these further changes, will cause a dilution of the intention of the act to prevent harm from unaffordable lending**. And will mean that the legislation becomes unenforceable, as lenders find ways around it. Our preference would be for **registered banks and mortgage lending to be removed from the affordable lending rules**, as they already have stringent and conservative measure in place, that look beyond the relevant period of 1yr. This would then allow this legislation to be more specific to dealing with harm from non mortgage/consumer lending.

Our Observations

We note that we would have expected clients coming to us because they had been declined a loan, and wanting to know what their other options were since the new legislation started in 1 Dec 2021. However, we have not had any people come to us in that were declined loans when they could afford them since the start of the legislation (although we did reach out to those that were used as examples in the media for home loans and found that often there were other reason they got declined).

We have however **started to see clients coming to us that were granted loans since the legislation came in force, that were <u>not</u> affordable and are causing harm**.

We have **found that lenders are not asking for sufficient detail of relevant expenses**, and **are relying on information provided by the borrower** (which is often made up by those most vulnerable) and then using **benchmarks (but not disclosing what these are) that may also not be relevant to the borrower**, and **not checking bank statements.**

We also note that the media statement that went out saying that **lenders could rely of what borrowers said their <u>future</u> living costs would be, as long as it was then benchmarked, is opening the door to "made up budgets".** Especially since the use of the word future is not in the code or legislation. So it is a bit of a feeling of daja vu, re the old legislation that wasn't enforceable – is this what we are looking at again??

I believe **lenders need to have a mind shift around what normal living costs are for people**, and <u>stop assuming that borrowers are happy to live in hardship to afford a loan</u>. This is going to take time, and I don't believe that reacting to media, lenders and mortgage advisors and rushing changes to the legislation and the code through, is going to get the intended reduction in harm that is needed.

I believe that registered banks and home loan lending needs to not be applicable to this legislation, so that the legislation can have the targeted reduction in harm from consumer lending, it was intended to have.

I was also like the **word <u>substantial</u> should be taken out of the definition of hardship**. This is NZ, not a 3rd world country where hardship is ok and is common. If we want to see better outcomes for our children, parents need to have the funds available for the children to partake in activities that enable them to thrive, not survive. Quite simply**, loans that aren't affordable, is what causes child poverty**!

Responses to questions

1	Do you agree with amending the definition of 'listed outgoings' along the lines proposed? Do you have any comments on the wording of these changes?
	I question the difference between a fixed financial commitment and a regular recurring and whether that needs to be made more obvious. The **only example of tithing seems unusual example and bias towards religion**, and the word remittance seems very general. I question whether more examples need to be included here or removed from here altogether and added to the code. What makes something material to the estimate of relevant expenses? I would have thought that if the borrower is unwilling or unable to cease, then this would make it material? Therefore I think the wording **the borrower is unwilling or unable to cease needs to be added back in** or in the definition of discretionary. Also I am not sure I agree that a gym membership is seen as a discretionary expense by everyone (any more than tithing is) – the investment return of that money in someone's mental and physical health is very high. This is a good example of a borrower being able and willing to stop something, and **discretionary being a subjective definition**.
2	Do you agree with amending the definition of 'relevant expenses' along the lines proposed? Do you have any comments on the wording of these changes?

It makes sense that if the legislation is about not causing substantial hardship, then discretionary expenses could be removed from the expenditure. However it **doesn't make sense that the lender should make this call alone on what is discretionary**.

History has shown that many lenders are not responsible, even though they claim to be responsible lenders on their websites and as part of their memberships. Lenders have also shown that they have traditionally had no regard and a **high level of ignorance about expenses that most would regard as essential**, but are not even included as a category in their budgets.

However, we also know that the borrower will falsely represent their expenses and agree with what the lender says, in order to get the loan approved.

The word **discretionary is also subjective to the person**, and the **best person to make that call is the borrower** as it is the borrower that will be living with consequences of getting the loan. The lender will as well to some extent, as the lender will be living with the consequence of the risk of the default of the loan.

For example **how will addictions be treated in this situation**? A person that is addicted to smoking, alcohol and/or gambling is unlikely to be able to just stop just to afford a loan. More likely they will prioritise their addiction, the loan payment, other bills and then usually food.

The best time to make that decision about whether to take on a loan, is before entering the loan. Therefore **advise to reframe to read that the borrower is willing and able to cease and a responsible lender would agree with**. After all, we want the borrower to make an informed decision and realise that they need to be willing and able to cease an expense in order to afford it, rather than just blindly signing the paper work. We also **don't want lenders to dictate how a borrower should live their life and what is discretionary and what is not**.

Regardless of the out come, I also think that the **lender needs to clearly state and show the borrower what expenses have and have not been included in the assessment of affordability, so the borrower can make an informed decision and sign off on it**. This would be what a responsible lender would do.

3 Which of the two options for guidance in the Draft Code relating to treatment of discretionary expenses is most appropriate and why? Do you have any comments on the wording of either of these options?

Option 1.

The **word <u>significant</u> needs to be removed from before the word risk**. As explained above the definition of the word discretionary is subjective and there needs to be a conversation with the borrower about what is discretionary first. Again the **<u>willing and able</u> if in significant hardship needs to be added back in**.

Can we remove the word assumption and add in the word point instead. Assumptions = risk.

Can borrowers cease or reduce most expenses? I think this is a naive assumption, changing habits with peoples lifestyle and spendin,g and making **behaviour change is not necessarily an easy thing to change, especially were people have entrenched habits**. Addictions also may be impossible to change without professional intervention that also costs money.

4	Do you agree with the approach to excluding some credit cards as proposed in regulation 4AL(2A)? If not, what changes would you make?
	No comment
5	Is any additional guidance needed for the exception in 4AL(2A) for certain credit cards? If so, what should this guidance state?
	No comment
6	Do you agree with explicitly excluding BNPL in its entirety from 4AL(2)? If not, are there alternative ways, that would be workable for lenders, to impute future BNPL expenses based on a borrower's existing BNPL facilities?
	No comment
7	In light of excluding BNPL from 4AL(2), is any further guidance in the Code necessary to address the treatment of BNPL expenses? If so, what should this guidance state?
	BNPL are difficult to represent. The importance is whether the items they have been used to purchase are **discretionary or non discretionary, and whether the payment will continue**. If they are non discretionary than an allowance will need to be retained in the expenses, otherwise need to have convo with borrower that are willing and able to stop.
8	Do you agree with the way that the Draft Regulations relating to the expanded exception for variations and replacements of existing credit contracts is phrased? If not, what changes would you make?
	I don't agree with allowing this to happen at all, it is **dangerous and essentially allowing new loans to be legally written that are unaffordable and causing harm**. This doesn't seem a good standard of practice. **Any loan should have to meet affordability**. If the borrowers can't afford the loan there are other **options that they can pursue such as hardship applications**, that would be much more favourable for the borrower. Consolidation loans are often marketed as an easy fix to the debt solution, but they are a **quick fix which doesn't address the underlying issue** (usually that the client needs to make changes to their situation). **Worse is consolidation loans can leave the client in a worse position** if they then reborrow against existing lines of credit and now have one large loan to pay off instead of smaller loans - which may have been able to been paid off from other means (eg selling/downsizing assets). The **borrower also will have no means of taking action** at the lender for a loan that is unaffordable, as technically it was a legal loan, where as they could have with the previous loan. For this to even be **considered, the only option would be because the payments and the interest rates are <u>significantly</u> lower, and that the borrower is advised to seek advice on other avenues from a Financial Mentor or Coach.** Otherwise why would you create an open door in the legislation that encourages unaffordable borrowing to continue – because the **lenders will exploit this and use this as a way to bring in more business**.

9	Which of the two drafting options for expanding the exception for variations and replacements of existing credit contracts would be most workable and why?
	Neither is acceptable. As discussed would have to be at significantly lower payments and interest rates to make it worthwhile for the borrower.
10	Do you agree with the suggested guidance in the Draft Code relating to the expanded exception? If not, what changes should be made to the Draft Code guidance?
	Agree with 7.4 being added in
11	Would any of these changes require changes to lender systems before they could come into force? If so, what are the likely timeframes for making these changes?
	No comment

Other comments

I have grave concerns about this legislation having the impact in reducing harm from unaffordable lending. This is due to lenders being able to rely on what borrowers say their future expenses will be (so potentially anything), coupled both lenders and borrowers having an ignorance of the type of costs required to live. Generic benchmarking and buffers and surpluses will alleviate this somewhat, only if sufficient categories of costs are included in the first instance.

Clarifying what expenses need to be taken into account if determining whether someone is in substantial hardship is key. The borrower also being able to make an informed decision of what future changes they are willing and able to make, to afford the loan, is also essential.