COMMERCE COMMISSION NEW ZEALAND
Te Komihana Tauhokohoko

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Submission to Ministry of Business, Innovation & Employment on the Responsible Lending Code Discussion Document

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CONTENTS

Commission's introductory remarks

A. The Commerce Commission's purpose is to achieve the best possible outcomes in competitive and regulated markets in New Zealand. We have been responsible for enforcing and providing guidance on the Credit Contracts and Consumer Finance Act (2003) (**CCCF Act**) for over 10 years.

B. We recognise that lenders provide a valuable service to New Zealand consumers, and we are committed to protecting those consumers who seek to access credit. In our enforcement decision-making, and in the guidance that we issue, we strive to balance our consumer protection objectives with ensuring that credit markets are competitive and operate efficiently.

C. The Credit Contracts and Consumer Finance Amendment Act 2014 (**Amendment Act**) gives lenders important new responsibilities. The code will elaborate on these responsibility principles and provide important guidance as to what steps lenders should follow to comply with them. As such, the Responsible Lending Code (**code)** will be an important and much-referenced document in New Zealand's credit landscape.

D. Depending on the code's final content, it may be unnecessary for the Commission to publish revised credit fees guidance. So with that in mind, we have provided very full responses to each of your discussion questions.

E. Our general preference, however, is that the code is not drafted with minute prescription. An overly prescriptive and detailed code could lead in a short time to the code lagging behind case-law, and would necessitate the code's frequent revision. We suggest instead an approach that focusses on the processes that should be followed to satisfy the lender responsibility principles, and leaves responsible lenders to make day-to-day decisions through applying these processes. We appreciate the opportunity to make submissions on the discussion document for the code.

Relationship with Fair Trading Act 1986

F. The relationship between the Amendment Act and the Fair Trading Act is not the subject of direct questioning in the discussion document. Nevertheless, we wish to make comment on it.

G. The Commission has enforcement responsibilities under both the CCCF Act and the Fair Trading Act. Presently, we either choose which statute we will take enforcement action under, or take action under both.[1]

H. The Amendment Act preserves the independence of the Fair Trading Act as a consumer protection statute of wide application. Section 9C(3)(f) requires that a lender must meet all obligations to the borrower arising under (among other

[1] For more information see our published Enforcement Response Guidelines at http://www.comcom.govt.nz/the-commission/commission-policies/enforcement-response-guidelines/

statutes) the Fair Trading Act, including prohibitions on false or misleading representations and unfair contract terms.

I. Inasmuch as the lender responsibility principles also require accuracy in advertising,[2] the overlap with the Fair Trading Act becomes clear.

J. Section 9D(2) deals with this in part by enacting a double-jeopardy provision: the Commission cannot commence proceedings under both the Fair Trading Act (for example) and under the Amendment Act for breaches of ss 9C(3)(f) or 9C(4)(e).

K. The Commission is likely to update its Enforcement Response Guidelines once the code has been issued, to provide further guidance on how we will make enforcement choices between these statutes.

L. In the meantime, we wish to note and reinforce that there is a wealth of long-established case-law precedent governing the application of the Fair Trading Act provisions, including to lending. This jurisprudence will apply to any action brought under the Fair Trading Act, but is also relevant to our interpretation of whether a lender has fulfilled the responsibility principles of complying with the Fair Trading Act and ensuring that the lender's advertising does not mislead.

M. We would also like the code to draw to lenders' attention the fact that the Fair Trading Act applies alongside the principles, and that the Fair Trading jurisprudence will be applicable to determining whether, under the principles, the Amendment Act and the CCCF Act have been complied with. The code should note that neither it nor the lender responsibility principles limit the general application of the Fair Trading Act.

N. The Fair Trading case law is accessible, comprehensive and provides excellent guidance – but there is simply too much case law for the code to do more than scratch the surface. We suggest instead that the code:

- only describes process, practices and procedures that are consistent with established principles of general application under the Fair Trading Act, so as to avoid confusion and uncertainty for lenders and consumers; and
- cross-refers to good external sources of Fair Trading information, such as the Commission's consumer fact sheets and other guidance.

References in this submission

O. The question headings below (in bold) correspond to the question numbers in the discussion document.

P. Section references are to the Amendment Act unless otherwise stated.

[2] See for example ss 9C(2)(a)(i) and 9C(3)(b)(i).

Responses to the discussion document

Introductory Questions

1. Do you agree with the proposed criteria for assessing what guidance should be set out in the Code as set out in paragraph 18? Should retaining sufficient flexibility to allow lenders to adapt the guidance to different products and business models be another criterion? Are there any other key criteria to be considered?

1.1 The purpose of the code is to elaborate on the lender responsibility principles, and to provide guidance on how those principles may be implemented by lenders (s 9E).

1.2 We agree that the primary and overarching criterion is whether the code promotes consumer protection, reflecting the new purpose statement in s 3(1).

1.3 We also agree that promoting certainty for lenders and the enforcement agency are important criteria, helping to reduce transaction and compliance costs for lenders and enabling more timely and cost-effective enforcement.

1.4 The other criteria mentioned in paragraph 18 of the discussion document, such as minimising compliance costs and not unnecessarily restricting access to consumer credit, are worthy considerations. However these criteria are subordinate to the primary objective of promoting the effectiveness of consumer protection through responsible lending.

1.5 If, when drafting the code, tension arises between the primary consumer protection criterion and these secondary criteria, the balance should weigh in favour of consumer protection. Consumer protection should not be traded-off against reduced lender compliance costs, or the provision of credit by lenders who are not compliant with the lender responsibility principles.

1.6 It is always desirable for published guidance to be flexible enough to adapt to innovations and developments. To the extent that this is possible, it is a worthwhile objective, but we do not think that this needs to be elevated to a criterion.

1.7 What is crucial is that the code is clear, concise, guides standards of responsibility, and is easy to understand and applies to all participants in the industry.

1.8 Because compliance with the code will be treated as evidence of compliance with the lender responsibility principles (s 9E(3)), the code needs to dovetail effectively with the principles. Any flexibility that might be provided in the code must not create uncertainty about the application of the lender responsibility principles.

1.9 A key criterion that should be added is the need to address s 9F, which sets out the matters that may be usefully articulated within the code.

2. Are there any particular features of the New Zealand market which would differentiate our approach from international approaches?

2.1 Yes. New Zealand's small market economy, and the small size of many third tier lenders in New Zealand, are potentially differentiating features of the New Zealand consumer credit market. However, we would not like to see the small scale of the New Zealand credit market being used to justify a dilution of otherwise transferable responsible lending guidance from overseas agencies. This would undermine the effectiveness of the lender responsibility principles and the code.

2.2 New Zealand's consumer credit markets are – even with the changes in the Amendment Act – relatively lightly regulated compared with other countries. Many other countries that have responsible lending obligations also have various forms of cost of finance (interest rate) caps or price controls. The Government has said that cost-of-finance caps are unnecessary in New Zealand because, among other things, the lender responsibility principles are being introduced. This means that New Zealand is placing greater reliance on the lender responsibility principles than is the case in the comparison countries. Therefore the code needs to provide very clear guidance so that lenders are aware of what they need to do to satisfy the lender responsibility principles at all stages of the contract, and so that the Commission can take action where appropriate to achieve the primary consumer protection purpose of the legislation.

2.3 Within New Zealand, there are clearly groups of consumers who are particularly vulnerable to harmful lending practices because of factors such as low financial literacy, low income, desperation caused by straitened financial circumstances and few options to access credit. This group often includes recent immigrants, who may also be unfamiliar with consumer finance in New Zealand. The social and economic pressures on Pacific families who can no longer be categorised as immigrants have also been documented.[3] We are aware that some lenders specialise in providing credit to those consumers (eg, truck shops, payday lenders).

2.4 While having vulnerable consumer groups is not unique to New Zealand, we believe it is essential that the code has effective measures to protect the interests of these consumers.

3. We consider that the structure of the Code should reflect the lifecycle of a consumer credit contract, do you agree?

3.1 Yes, it is sensible for the structure of the code to reflect the lifecycle of a consumer credit contract to the extent that it can.

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[3] Families Commission, *Pacific Families and Problem Debt,* (November 2012), Ministry of Consumer Affairs, *Pacific Consumers Behaviour and Experience in Credit markets, with Particular Reference to the "Fringe Lending" Market,* (August 2007).

3.2 We do think that this will require repetition and cross-referencing. Many lender responsibilities apply across more than one stage of the life-cycle of the contract. For example:

3.2.1 The requirement for information to be presented in a manner that is not misleading, deceptive or confusing, applies before an agreement is entered into (s 9C(3)(b)) and in subsequent dealings (s 9C(3)(c)).

3.2.2 The obligation not to be oppressive applies to inducing the borrower to enter into the agreement, the terms of the agreement and to the exercise of powers under the agreement (s 9C(3)(e)).

3.2.3 The general obligation to comply with all relevant laws also applies across the life-cycle of a consumer credit contract (s 9C(3)(f)).

3.3 The code should make these types of wider obligations clear at the outset and throughout the code if a life-cycle structure is adopted.

3.4 The code should also include sections dealing with the 'optional' services that will not necessary apply during the life-cycle of every contract. For example, the lender responsibilities relevant to guarantees (section 9C(4)) and credit-related insurance (section 9C(5)) will need to be tackled separately and would not easily fit into a structure based rigidly on the life cycle of a consumer credit contract.

4. Are there lenders/borrowers/agreements or classes of lenders/borrowers/ agreements that should be treated differently under the Code? If so, why, in what way and how should any such lenders/borrowers/agreements be defined?

4.1 Yes, we agree with the suggestion that guidance should be tailored to the specific situations under which borrowers commonly access credit.

4.2 The lender responsibility principles effectively set the standards of lender behaviour. The code is intended to elaborate on those standards, and address appropriately applicable processes, practices and procedures to meet (and evidence compliance with) the principles.

4.3 Therefore, we see the lender responsibility principles as recording the standards, and the code guidance as addressing how lenders can – in specific situations – satisfy those standards.

4.4 In our view the code should provide tailored guidance for common situations such as the following.

4.4.1 **Product-specific guidance** (eg mortgage lending, store credit facilities, payday loans etc).

4.4.2 Loans to **vulnerable borrowers** (as above at 2.3). We see this guidance as applying to lenders who target vulnerable borrowers, as well as to

lenders who ought to apprehend that they may be dealing with a vulnerable borrower).

4.4.3 Different **methods of lending** (eg online, in person, point-of-sale lending).

4.5 We do not agree that guidance should be tailored by **lender** type. What matters is what the lender sells, to whom and by what method. All lenders offering similar products should be required to compete under the same rules. Using different rules according to the type of lender will not lead to the best possible competitive and consumer outcomes.

4.6 **Examples** of specific credit situations that lend themselves to tailored guidance include:

4.6.1 Mortgage lending.

4.6.2 Reverse equity mortgage lending.[4]

4.6.3 Credit card lending.

4.6.4 Store credit facilities.

4.6.5 Point-of-sale lending.

4.6.6 Online lending.

4.6.7 Truck shops and other 'mobile' lending.

4.6.8 High-cost short-term loans, also referred to as payday loans.

4.6.9 Lending to vulnerable borrowers.

4.7 Because this list cannot hope to be complete, and because lenders are innovative in their product offerings and methods of transacting, we recommend that the code provide additional **default guidance for the category of "other" situations.** This generic guidance would elaborate on how, for example, in other situations a lender might go about making reasonable enquiries, or assisting a borrower.

4.8 This default guidance would capture any non-tailored situations, and allow for the code to be flexible and adaptive to credit methods. When 'other' practices develop to the point of being common, the code should be updated to provide tailored guidance on those common situations.

[4] We see this subset of mortgage lending as justifying tailored guidance, given the responsibility to assist the borrower (often elderly and potentially vulnerable) to understand the full implications of entering into the agreement.

4.9 When a lender has a combination of tailored guidance applying to it – for example, (a) credit card lending to (b) a vulnerable borrower – then the code should state a requirement to have regard to both sections of guidance (a+b).

5. Should the concept of "*scalable*" guidance apply to the Code? If so, which principles or responsibilities should be scalable?

5.1 No, we have real concerns about the concept of scalability, because, under the Australian Regulatory Guide that refers to scalability, the lender has the discretion to 'scale' the guidance according to a number of factors.

5.2 The discussion document defines "*scalable*" as follows: "Some guidance may also be "scalable" in that what constitutes compliance with the principles may differ according to the circumstances and the type of lender or borrower or agreement involved." [5]

5.3 In our view, the guidance in the code should be tailored for specific situations (see our response to Q4 above) but the lender should not decide what are the appropriate processes, practices, or procedures in different circumstances. This would decrease the clarity of the guidance, and work against the effective implementation and enforcement of the lender responsibility principles.[6]

5.4 Rather, our response to Q4 applies: tailored guidance in the code for differing circumstances will do the work of 'scaling' what compliance looks like, leaving little residual lender discretion to determine what compliance should entail.

6. How prescriptive should the guidance in the Code be?

6.1 The code is not itself a set of requirements, because lenders can choose not to adhere to what the code says. The purpose of the code is to elaborate on the lender responsibility principles, and to provide guidance on "how those principles may be implemented by lenders" (s 9E(1)).

6.2 Section 9F states that in order to achieve this purpose, the code may:

6.2.1 set out the nature and extent of inquiries to be made before entering into an agreement; and

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[5] The Discussion Document states that scalability is a concept used in the Australian Securities & Investments Commission (ASIC) guidance: Regulatory Guide 209: *Credit Licensing: Responsible Lending Conduct.* This guide states that factors relevant to the scalabilty of reasonable inquiries and verification obligations include the potential impact on the consumer of entering into an unsuitable credit contract, the complexity of the credit contract, capacity of the consumer to understand the credit contract and whether the consumer is an existing customer or a new customer.

[6] We are, for example, aware from our ASIC colleagues that the concept of scalability has been applied by some creditors to scale down their responsible lending obligations for payday loans, to a level that may breach the terms of their legislation. ASIC is now awaiting judgment on a case that tests the meaning of a number of the legislative provisions. This includes testing what constitutes reasonable enquiries about the customers' requirements, objectives, and financial situation; what constitutes taking reasonable steps to verify the customer's financial situation; and what a suitability assessment should entail.

6.2.2 set out the processes, practices and procedures that responsible lenders should follow.

6.3 In determining how prescriptive the code needs to be, the requirements for certainty and clarity must be balanced against the need for lenders to have sufficient flexibility to operate successfully in a commercial environment.

6.4 In terms of clarity, lenders, borrowers and the Commission will need to be able to assess whether a lender is complying with the code in any given situation. It is absolutely essential that the code is not so loose or vague that lenders who use harmful lending practices could argue that they are complying with the code.

6.5 We think the code should be as prescriptive as it needs to be to ensure that lenders and the Commission can clearly identify whether behaviour does or does not comply with the lender responsibility principles. We refer to our Q4 answer in which we propose the concept of tailored guidance. This should allow lenders be able to confidently design compliance systems that meet the standards for responsible lending.

6.6 We would not expect these processes, practices and procedures to be described in minute detail, or for lenders to have no flexibility in how they choose to operate their businesses. The code should not be so prescriptive as to be a tick-box checklist.

7. Should the level of prescription differ for different classes of lenders/borrowers /agreements? If so, which classes and why?

7.1 Yes, as we answered in Q4, we recommend tailored guidance which will allow lenders to focus in on their specific situation and elaborates on what compliance will look like depending on product, borrower circumstance or transaction method.

Before entering into a consumer credit agreement

Advertising

8. What are the elements of a best practice internal process to ensure that advertising is not misleading, deceptive or confusing? (For example, in relation to training and checking marketing material).

8.1 Lenders should have in place:

8.1.1 training systems to ensure that the relevant staff are aware of the legal obligations and relevant law; and

8.1.2 a review process for each advertisement (possibly including obtaining legal advice).

8.2 As noted in the discussion document, the Commission has existing guidance for traders on how to comply with the provisions of the Fair Trading Act concerning misleading and deceptive conduct. We suggest that this guidance would be a useful start for informing best practice internal processes for responsible lenders. Lenders will also be able to obtain good compliance information from law firms and other compliance advisers.

9. Should guidance on advertising processes take account of the size and nature of the lender? If so, how?

9.1 No. All lenders who advertise must ensure they are complying with their legal obligations under the principles and the Fair Trading Act. We do not think the code should describe differing processes, depending on the size of the lender. In our experience, the advertising practices of some of the smaller lenders raise more concerns than those of larger companies, eg, misleading per-week interest rate advertising.

10. What existing guidance or codes of practice for advertising will help inform the Code? Should these codes be referred to or translated into the Code?

10.1 We consider that the guidance provided by the Financial Conduct Authority (FCA) in the United Kingdom, contained in the UK Consumer Credit Sourcebook is highly relevant[7]. We believe that much of this material would be appropriate for inclusion in New Zealand's code.

10.2 Our Advertising Standards Authority also has a code for Financial Advertising standards that is relevant.[8]

10.3 The Commerce Commission has published guidance that is relevant to aspects of lending advertising (eg, fine print, jargon & puffery, etc.) We suggest that some of the information contained in these fact sheets could usefully be incorporated in the code.[9]

11. Are there specific advertising practices that lenders should follow? Or are there specific advertising practices that lenders should refrain from following?

11.1 As noted, we consider that the guidance contained in the UK Consumer Credit Sourcebook is relevant, and in particular the guidance on credit advertising could usefully be incorporated in the code.

11.2 We would expect that the code would provide for responsible lenders to ensure the following:

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[7] The United Kingdom Financial Conduct Authority (FCA) *Consumer Credit Sourcebook* (2014), 3.5.3

[8] www.asa.co.nz/fa.php

[9] http://www.comcom.govt.nz/fair-trading/fair-trading-act-fact-sheets/fine-print/, http://www.comcom.govt.nz/fair-trading/fair-trading-act-fact-sheets/jargon-exaggerations-and-puffery/

11.2.1 Advertising containing daily or weekly percentage interest rates should include the annual percentage interest rate in no less prominent font, because this is how consumers most clearly understand and compare the cost of credit.

11.2.2 Advertising referring to per week payments should include the total amount payable in no less prominent font. While this is relevant for loans we consider it even more relevant for goods and services purchased on credit. We are aware that some catalogues and shop display cards only advertise “per week” prices.

11.2.3 Advertising of goods to be bought on credit must ensure that details about both the consumer good and the credit obligations are accurately described. We have seen catalogues/flyers that show a picture of a generic television, tablet or similar, with no clarity as to the brand and value of the good, or the terms of credit being offered.

11.2.4 Any advertising of low introductory interest rates should clearly state the period for which the low introductory rate applies, and what the standard interest rate will be for the remainder of the loan. The advertising should also prominently state any fees that apply to the transaction.

11.3 In general we consider that responsible lenders will refrain from the following practices:

11.3.1 Expressing the interest rate as a weekly rate, rather than a more easily-understood and comparable annual interest rate.

11.3.2 Emphasising the speed of the loan approval process (we also do not see how a lender who is advertising “15 minute” or “instant” loan approvals can meet the lender responsibility principles).

11.3.3 Advertising and promoting payday loans and other short-term high-cost credit as appropriate for spending on luxury or non-essential purchases (“treat yourself”, holidays etc.).

11.3.4 Stating or implying that credit is available regardless of the borrower’s financial circumstances and that there are no significant credit criteria/ approval processes required (“bankrupt – ok”; “bad credit – ok”; “no credit checks”).

11.3.5 Celebrity endorsements, particularly when they are designed to model or normalise customer behaviour in respect of high-cost credit. The finance company collapses have shown that celebrity endorsements are often successful in inducing a customer to invest or borrow.

12. Should advertising of certain credit products be accompanied by risk warnings?

12.1 Yes. We think this would be beneficial to some borrowers, for example in relation to payday loans. Payday loans often have interest rates of 300%-1000% pa. These loans are not designed to be for anything longer than a few weeks and, if they go beyond this period, the financial impact on borrowers can be very significant.

12.2 The UK Consumer Credit Sourcebook at 3.4 and 3.6 sets out risk warnings that we consider would be useful guidance in the advertising of certain credit products (particularly payday loans, and secured lending). An example of a clear risk warning relates to payday loans and state "*Late repayment can cause you serious money problems. For help, go to moneyadviceservice.org.uk."*

13. Should there be specific guidance in relation to advertising which is targeted at a specific group or persons known to have specific characteristics? If so, which groups/characteristics?

13.1 Yes. The guidance should state that, as a general rule, lenders should not target customers with credit agreements that are unsuitable for them by virtue of their age, health, disability or any other reason. We consider that useful guidance on this issue is provided in the UK Consumer Credit Sourcebook[10].

14. What other matters should the Code address in relation to advertising?

14.1 We have nothing further to add.

Assisting informed decisions

15. Apart from complying with disclosure obligations, how do/should responsible lenders assist borrowers to understand the terms of the credit agreement? How should any guidance cover different methods of providing credit? (eg, online applications) Should certain information be required to be given orally for face-to-face or telephone interactions with customers?

15.1 The obligations to assist the borrower to reach an informed decision and to be reasonably aware of the full implications of entering into the agreement are important. A lower standard should not be accepted simply because of transaction method, for example on-line vs face- to-face. Otherwise, lenders may be commercially incentivised to transact using the method that seems to attract fewer or less exacting compliance obligations.

15.2 We consider that in the case of on-line applications for credit, a lender should take all reasonable steps to ensure that a consumer understands the key terms before making an application. We would not expect that a "tick box" confirming that a debtor has read the terms and conditions will be sufficient

[10] The United Kingdom Financial Conduct Authority (FCA) *Consumer Credit Sourcebook* (2014): 2.2.2

under the code to demonstrate that the borrower understands the terms of the credit agreement. Nor would simply reading a script to customers over the telephone suffice. Rather the responsible lender should take steps to actively ensure that the borrower understands the terms of the agreement. A telephone call or series of email exchanges would be the minimum required.

15.3 For example, a lender could have a checklist of questions to ask a borrower/guarantor to ensure that they understand the agreement.

15.4 Consistent with s 9J of the Amendment Act, borrowers should be able to take away a copy of a contract and any terms and conditions to enable them to further consider the documentation and/or seek advice or assistance with the decision-making. Lenders should not refuse or discourage this practice. Similarly, if the lender maintains a website, a generic copy of a contract and any terms and conditions should be available for a customer to download or print.

16. What are/should be responsible lenders' practices where English is not a borrower's first language?

16.1 The lender needs to ensure that the borrower understands the product, and that the lender otherwise complies with the principles. The principles cannot be fulfilled when there is a significant language barrier between the parties. A good and sufficient exchange of information is needed, using translation/ intermediary services if necessary.

16.2 Lenders who regularly solicit custom from people of a particular ethnicity or who speak another language should provide key documents translated into the relevant language. However, we recognise that translation and the production of documents in multiple languages may be impractical for lenders. An alternative is for lenders to help borrowers to access translation services, preferably at the lender's cost.

16.3 Lenders should not accept as translators close family members or a child under the age of 18.

17. What opportunities do/should responsible lenders provide to borrowers to ask questions about the agreement? Would providing access to frequently asked questions be sufficient?

17.1 We regard frequently asked questions as a useful device, but not as one that should take the place of a ready means of contacting the lender to directly work through questions and issues.

17.2 Borrowers must be able to communicate directly with the lender if the lender is to assist borrowers to make informed decisions. In particular, without the opportunity for dialogue that addresses the borrower's specific situation, the lender cannot comply with the lender responsibility principles.

17.3 Lenders must give borrowers the opportunity to ask specific questions of the lender, whatever the transaction method (for example, face-to-face or remote). Access to frequently asked questions may be a useful additional option, but we would not expect them to be sufficient by themselves.

17.4 All lenders should have easily accessible contact points, by telephone, electronically or in person.

17.5 Similarly, at the start of the contract, the lender should ask the borrower for a preferred method of communication (eg. text, email, phone call to a particular number at a particular time of day).

18. What practices do/should responsible lenders undertake to ensure that credit agreements are in plain English, clear, concise and intelligible?

18.1 Section B of the Financial Markets Authority Guidance Note on Effective Disclosure sets out some very useful examples of writing in a clear, concise and effective way[11]. This includes, for example, using the active voice, avoiding double negatives and using short sentences. This guidance suggests that issuers test their documents for readability and accessibility with members of the public.

19. How do/should responsible lenders assist borrowers to understand the implications of the credit agreement? For example, if technical or legal concepts are referred to, should the agreement explain the implications of those concepts?

19.1 Yes, we believe that lenders should provide explanations for all technical terms used in consumer credit contracts, including words such as "guarantor." Any concept that has real-world implications for the borrower (or third-party) should be plainly explained, and illustrated through the use of clear examples.

19.2 There are various ways that lenders could check the borrowers' understanding of an agreement. For example, a lender could have a checklist of questions to ask a borrower/guarantor to ensure that they understand the agreement. (For example, how much are you borrowing? How much do you have to pay back? What happens if you don't pay the loan back? Can the interest rate change?)

19.3 This process is probably easier in a face-to-face environment. But the code must reflect the lender's obligation to ensure that the borrower has a reasonable awareness of the full implications regardless of the transaction method.

[11] www.fma.govt.nz/media/1105126/guidance_note

20. Can you point to good examples of credit agreements that are in plain English, clear, concise and intelligible?

20.1 In our experience, the best credit agreements have all the key information contained in one document, so that a debtor does not have to flip between documents. We think it is preferable if information is contained under relevant headings, simple and well-structured, and that important content is not referenced to another paragraph or page of the document. (For example, there should not be a heading "Default fees" with text that then states "Default fees chargeable are set out in clause 5.2.13").

20.2 Layout, font size and the prominence of key information are more important than keeping the information on one page – we have seen documents where the lender has tried to keep information on one page and resorted to dense text and small font size to do so. This inhibits reader comprehension. We believe that clear headings, spacing (with sufficient white space) and normal font are important for legibility.

21. What are/should be responsible lenders' processes in relation to independent budgeting or legal advice for borrowers and guarantors? In which circumstances should the lender require or recommend independent legal advice?

21.1 Budgeting advice and legal advice are not equivalent because budget advisers tend to be voluntary organisations, staffed mainly by volunteers. Lawyers are an independent profession. Therefore, it would be inappropriate for the responsibilities of lenders to be transferred to budget advisers.

21.2 A responsible lender should insist that borrowers and guarantors seek independent legal advice if their house is used as security, and for all reverse equity mortgages.

21.3 Responsible lenders should also recommend independent legal advice for a range of other transactions with very significant potential consequences, especially guarantees.

21.4 Some lenders have documents that seek to limit liability through statements like *"I have been advised to obtain legal advice… but [I] have voluntarily chosen of my own free will and volition not to so".* We do not regard this as effective to discharge a responsible lender's obligations in relation to independent advice, especially when the item is given no genuine emphasis but is just another page in a large series of documents requiring signature.

22. What do/should responsible lenders do to assist guarantors to make informed decisions?

22.1 A responsible lender should be required to emphasise the risks and consequences of guaranteeing a loan. Nearly all the lender responsibility principles will apply to guarantees. This includes the lender being satisfied that the guarantor will be able to comply with the guarantee without

suffering substantial hardship, and assisting the guarantor to reach an informed decision whether or not to enter into the guarantee.

22.2 How lenders will assist guarantors to make informed decisions will be a crucial aspect of the code. We have received complaints involving guarantees that have caused us concern, for example the assumption that a young person or a person who does not have English as a first language understands the term 'guarantor'; or a friend or neighbour becomes a guarantor without first understanding the risks.

22.3 As well, we think it would be useful if lenders discussed with guarantors how, and at what stage, a lender will advise the guarantor of any default by the borrower. Some guarantors may want to be informed after a set number of days. If the lender cannot accommodate this, then at the very least the guarantor needs to know when and how they will be told of any problems.

23. What information do/should responsible lenders give a borrower to assist them to make an informed decision on credit-related insurance?

23.1 The central lender responsibilities will apply to advertising and selling credit-related insurance, including:

23.1.1 meeting the borrower's requirements and objectives;

23.1.2 the lender being satisfied that the borrower will be able to make the payments under the contract without suffering substantial hardship; and

23.1.3 the lender assisting the borrower to reach an informed decision as to whether or not to enter into the contract.

23.2 We consider that responsible lenders would provide summary information that shows the costs of the policy (including the cost of interest which will accrue over time) and the potential benefits.

23.3 The ASIC guidance on consumer credit insurance referred to in the discussion document[12] is relevant and could usefully be incorporated into the code. Documentation relating to credit-related insurance could also usefully follow some of the UK recommendations following a market investigation on payment protection insurance arising from the Competition Commission's investigation into payment protection insurance[13]. For example, the UK guidance recommends that marketing material should contain information about the cost and key information about the policy, including clarifying that insurance is optional and is available from other providers.

[12] Australian Securities and Investments Commission, *Consumer credit insurance; review of sales practices by authorised deposit taking institutions* (2011).

[13] Davis, P (2009) *Market investigation into payment protection insurance*. United Kingdom: Competition Commission, Payment protection insurance market investigation order 2011, Financial Services Authority Finalised Guidance payment protection Insurance (2012).

23.4 A responsible lender will also ensure that borrowers are aware of the conditions and exclusions of the credit-related insurance policy, and not sell them unsuitable products. For example, we have seen premiums for credit-related insurance costing between $1,200-$1,500 on loans of $12,000-$14,000, but where the benefit provided by the policy (apart from the death cover) is three months scheduled repayments, which can be less than the cost of the premium.

23.5 In our experience, many borrowers are unaware of the conditions and exclusions that relate to their credit-related insurance contracts. Some of these conditions and exclusions result in insurance that is clearly unsuitable for the borrowers' needs. For example, it would be irresponsible to sell income protection insurance to a borrower who is receiving a benefit, or who is self-employed and therefore could not claim on the particular policy.

23.6 Many payment protection insurance policies cover the borrower in the event of illness or joblessness, but the borrower is not covered if the contract is in default at the time of the event. A responsible lender will ensure that a borrower knows this information prior to making a decision to purchase credit-related insurance.

23.7 The insurance policy offered must also be suitable in terms of the duration of the insurance policy and how it relates to the duration of the underlying credit contract.

23.8 If the cost of the insurance is to be included within the loan, this should be made clear, along with the interest rate that is to be charged. This includes explicit statements setting out the interest rate that is to be charged, and the cost of interest on the premium.

24. How do/should responsible lenders ensure that any advertising of credit-related insurance products distributed by the lender is not misleading, deceptive or confusing?

24.1 Many of the matters referred to in our response to Q23 apply, so we refer you to that answer.

24.2 When marketing credit-related insurance products, a responsible lender should specifically make it clear that the product is a consumer credit insurance policy. The term "insurance" should be used, rather than terms such as "payment protection plans."

24.3 Credit-related insurance must be marketed accurately in terms of the costs and the benefits that it will provide. Lenders should clearly indicate any conditions and exclusions.

24.4 Where insurance is optional, a responsible lender should make this clear and avoid the perception that the insurance is compulsory. The Commission does not consider that having 'opt-out' insurance is acceptable, as many borrowers

will in our experience not notice that by default they are purchasing insurance.

25. How do/should responsible lenders ensure that borrowers have sufficient time to make informed decisions?

25.1 Lenders have a responsibility to assist the borrower to make an informed decision, and to be fully aware of the implications of entering into the agreement. This means that borrowers need sufficient time to consider the information without being rushed. Lenders should encourage borrowers to take the documents away to think about the transaction (and perhaps discuss it with others) before signing the documents, especially for significant loans, such as when purchasing a car.

26. What processes and practices do/should responsible lenders undertake to assist informed decision for agreements when the application and approval is undertaken remotely?

26.1 The lender responsibility principles apply whatever the transaction method. The code could usefully set out processes tailored to meeting these expectations for online documents and forms, and what opportunities should be available for borrowers to ask questions.

26.2 But the Commission considers – as above at Q17– that all lenders should exchange information directly with borrowers by telephone or email, at least.

27. What other matters should the Code address in relation to assisting informed decisions?

27.1 This is a situation where tailored guidance should be provided in the code, as discussed in our response to Q4. Additional steps will be necessary to assist vulnerable borrowers to make informed decisions in relation to consumer credit. When the Commission is investigating whether a lender has met the lender responsibility principles of care, diligence, skill and assistance, for example, we will look at the circumstances of the sale and the 'cues' that were there for the lender that the customer might not have understood the terms of the loan or found it suitable for them.

27.2 So we think the code should set out an expectation that lenders will take additional steps to ensure consumers' interests are protected where:

27.2.1 certain kinds of credit agreements are more likely to be taken up by more vulnerable consumers (eg, payday loans, reverse equity loans); or

27.2.2 the lender has reason to believe that the borrower has a vulnerability (health, language, age etc).

27.3 Responsible lender practices for vulnerable consumers may include the lender giving more time to consider the information provided by the lender, taking extra steps to test that the borrower understands the full implications of the loan, recommending that the borrower seeks independent financial or legal advice, or ensuring that translation services are available.

Making reasonable inquiries

28. What information do/should responsible lenders require from a borrower when they apply for credit? How much reliance should a lender place on a credit check?

28.1 We expect that there is existing market best-practice as to the information lenders obtain that will be relevant to the responsible lending obligation to make reasonable inquiries. The code should refer to that existing market best-practice.

28.2 In terms of how much reliance should be placed on credit checks, we believe that credit checks should be an option but they should not be required in all cases. We expect that there will be low-value loans where the cost of the credit check outweighs its benefit.

29. What do/should responsible lenders explain to the borrower in relation to the purpose of the checks and assessments of affordability?

29.1 A lender should advise a borrower that it is making inquiries because the lender has a responsibility to be satisfied that the borrower can repay the credit without incurring substantial hardship.

30. How do/should responsible lenders assess whether the information a consumer has provided is correct? In what circumstances do/should responsible lenders be able to rely on information provided by a borrower?

30.1 We envisage that responsible lenders are already undertaking basic due diligence. For example, it is likely that banks already have information about their clients' income, assets and expenditure. It is also standard practice in mortgage lending, at least, for all customers (including existing ones) to be required to verify these details with current payslips and other proof.

30.2 The Australian Securities & Investments Commission guidance on Responsible Lending (ASIC Regulatory Guide 209) provides a useful list of the steps lenders can take to verify information, which would be relevant to include in the code.[14]

30.3 There will be some circumstances when relying on information provided by a borrower will be appropriate, such as where the lender cannot readily obtain verification (eg health status) or where it is impracticable to expect lenders to do so.

[14] The Australian Securities & Investments Commission guidance: Regulatory Guide 209: *Credit Licensing: Responsible Lending,* Rules 209.42 – 209.48

31. How does/should a responsible lender's checks differ for existing customers and new customers?

31.1 Where a contract is refinanced, the parties enter into a new loan contract. A responsible lender should go through the same practices that it would apply when assisting the borrower to make an informed decision in relation to the original loan.

31.2 Where the lender refinances a loan it already has with a borrower, the lender will have an existing relationship with the borrower. It will have information about the borrower that will give it a 'head-start' in assisting the borrower to understand the implications of the new contract.

32. How do/should responsible lenders consider whether credit does/does not meet the requirements and objectives of the borrower?

32.1 Responsible lenders must communicate with borrowers, and ask questions about their circumstances to find out why the borrower wishes to take out the credit. We would not expect the lender to make moral or lifestyle judgements about the borrower's use of the credit, but the lender should be in a position to make a judgement about whether the credit product being offered is appropriate for the borrower's circumstances. For example, a responsible lender will advise that credit card borrowing is more costly and, in many cases, less suitable than longer-term borrowing on a revolving credit facility or similar.

33. How should the lender responsibility to be satisfied that it is likely that the credit will meet the borrower's requirements and objectives be balanced against not unduly restricting consumer choice?

33.1 If the responsible lending principles conflict with consumer choice, then the responsible lending principles must prevail. Responsible lenders are obliged to refuse credit when their reasonable inquiries prevent them from being satisfied that borrowers can repay the credit without substantial hardship, or that the credit is not appropriate for the borrower's requirements or objectives.

33.2 Consumers will not be deprived of appropriate and suitable choices, but may be deprived of unsuitable lending choices; this is inherent in the Act, if the principles are being adhered to by lenders.

34. What proportion of credit applications are processed without the involvement of financial advisers permitted to give personalised advice in relation to category 2 products under the Financial Advisers Act 2008? Will regulation under both the lender responsibilities and the Financial Advisers Act impose significant costs for lenders?

34.1 The Commission has no information on this.

35. How do/should responsible lenders deal with the potential conflicting incentives posed by payments of commission/bonuses and the need to be satisfied that it is likely the credit agreement meets the requirements and objectives of the borrower and will be repaid without substantial hardship?

35.1 Lenders need to ensure that the incentive arrangements for the sale of credit do not work against their responsible lending obligations. Potentially the code could require compliance with the principles to be built into incentives, alongside volume-based incentives and bonuses. We think it is for each lender to ensure that its incentive arrangements, and all other aspects of its business, meet the lender responsibility principles.

36. What factors should be taken into account in considering what should constitute substantial hardship?

36.1 The substantial hardship guidance in the UK Consumer Credit Sourcebook and in the ASIC Regulatory Guide 209 appears to be reasonable. For example, the ASIC guide[15] includes a list of factors to take into account when considering whether a transaction is likely to result in substantial hardship such as:

36.1.1 The money the consumer is likely to have remaining after their living expenses have been deducted from their after-tax income.

36.1.2 The source of the consumer's income (including whether all or part of the consumer's gross income is sourced from benefits).

36.1.3 How consistent and reliable the consumer's income is (and the size of the payment obligations relative to their income level).

36.1.4 Whether the consumer's expenses are likely to be significantly higher than average (eg, because they live in a remote area).

36.1.5 The consumer's other debt repayment obligations and similar commitments (eg, child support).

36.1.6 How much of a buffer there is between the consumer's disposable income and the repayments (eg, how vulnerable they are to an increase in interest rates, or the impact once any 'honeymoon' rate ends).

36.1.7 Whether the consumer is likely to have to sell their assets, such as a car, to meet their payment obligations.

36.1 We expect the submissions from lenders and consumer advocacy groups will assist in determining what other factors should be taken into account in the New Zealand context.

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[15] The Australian Securities & Investments Commission guidance: Regulatory Guide 209: *Credit Licensing: Responsible Lending,* Rule 209.95, page 33.

37. Should substantial hardship be assessed by reference to any particular indicators or reference budgets?

37.1 Please refer to our answer to Q36.

38. Should the Code specify a threshold for substantial hardship? If so, what is an appropriate threshold?

38.1 On balance we think a defined threshold may not be practical. A defined threshold would be helpful from the point of view of providing certainty and supporting the enforcement of the responsible lending principles, but it may work against lenders being able to take account of the unique circumstances of each borrower. We prefer a list of possible factors instead of a bright-line threshold.

39. To what extent do/should responsible lenders take into account likely future market conditions (eg, interest rate rises) when assessing affordability for the borrower (particularly for long term credit agreements such as mortgages)?

39.1 When assessing affordability, responsible lenders should take into account the interest rate that, to the best of their knowledge, will likely apply for the remainder of the loan. This will likely involve sensitivity testing for increases in interest rates. Lenders should share the results of such sensitivity analysis with borrowers as a part of their responsibility to inform borrowers of the full implications of entering into the loan.

40. Do/should responsible lenders engage in lending that relies primarily or solely on the value of any security provided by the borrower?

40.1 Yes. In some limited circumstances asset lending may be appropriate (eg, reverse equity mortgages where the borrower is fully informed about the risks and consequences; or pawnbroking).

40.2 However, there are situations where debtors are unlikely or unable to repay their loans in the ordinary course, and lenders are relying solely on the security provided. In these situations the code should set out the steps that lenders should take to ensure that the borrower understands that the security will most likely need to be sold for the loan to be repaid. We have come across situations where the lender and the borrower have had completely different expectations about the repayment of loans of this nature.

41. Are there circumstances in which it should be presumed that the consumer will only be able to make repayments with substantial hardship?

41.1 The Amendment Act does not provide for any presumptions in relation to substantial hardship. It is difficult to see how such a presumption could be created through the code when there is no statutory basis for it in New Zealand.

41.2 In contrast, the Australian National Consumer Credit Protection Act 2009 sets out the circumstances where a presumption of hardship will be made. These include where a borrower is currently in default under an existing low value credit contract, or had been a debtor under two or more small amount credit contracts in the 90 day period before the assessment of their application for credit. The ASIC Regulatory Guide 209[16] reflects these presumptions.

42. What policies do/should responsible lenders have in place to assess whether the security taken is excessive relative to the size and length of the credit provided?

42.1 Lenders make commercial decisions about how much security is necessary to secure the repayment of a loan. A responsible lender will not over-reach by taking more security than is necessary to secure the repayment of the loan.

42.2 If the credit is provided to purchase specific goods, we believe that generally, the security should be limited to those goods. The life of those goods should be fairly reflected in the term of the credit.

43. What other matters should the Code address in relation to making reasonable inquiries to assess whether the credit agreement meets the borrower's requirements and objectives and can be repaid without substantial hardship?

43.1 We have no further comments.

During the life of a consumer credit agreement

Dealing during the term of the agreement

44. Question 44: What practices and processes do/should responsible lenders have in place to assist borrower decision-making in relation to variations to a contract (eg, credit card limit increases) or refinancing? What types of variations do/should such practices apply to?

44.1 We have combined our answers to Q44 and 45 under Q45 below.

45. What practices and processes do/should responsible lenders have in place in relation to whether a credit agreement would likely meet the borrower's requirements and objectives and can be repaid without substantial hardship following a variation or refinancing? What types of variations do/should such practices apply to?

Refinancing

45.1 Where a contract is refinanced, the parties enter into a new loan contract and the principles set out in s 9C(3)(a) and (b) (and corresponding parts of the code) apply. We have observed through complaints received by the Commission that refinancing can amplify difficulties with existing commitments if the refinanced commitments are not sustainable.

[16] Ibid.

45.2 The code confirms that a responsible lender should go through the same practices that apply to assisting borrower decision-making and ascertaining their circumstances and commitments as when taking out the original loan.

45.3 We think the code should also take into account the following:

45.3.1 Where the lender refinances a loan it already has with a borrower, it will have an existing relationship with the borrower. It will have information about the borrower that will give it a 'head-start' in assisting the borrower to understand the implications of the new contract.

45.3.2 The lender is also likely to be aware that the borrower has other loan contracts that are being refinanced, and the lender may have information about the borrowers' ability to meet their obligations under those contracts. A responsible lender would need to take that information into account in considering whether the new loan meets the borrower's requirements and can be repaid without substantial hardship.

45.3.3 In any event, the nature of a refinancing is that the borrower is seeking to change their lending arrangements. Something in the borrower's circumstances or preferences has changed. A responsible lender will make comprehensive enquiry to ascertain the borrower's financial position and other commitments, and to assist with advising on the suitability and affordability of the proposed loan product for the borrower's requirements. In our view these enquiries cannot be satisfactorily made using FAQ type forms alone, but should require a conversation (at least by email) between lender and borrower.

Variation

45.4 When the Commission refers to a "variation" to a contract we mean a change to a contract that is **agreed** between the parties.

45.5 However a responsible lender will also have obligations under the principles where it **unilaterally** makes changes using a power under the contract. We would not expect that a responsible lender who increased fees or an interest rate pursuant to a power under the contract would be obliged to contact the borrower and ensure they understood the change or that the change would not cause the borrower substantial hardship. However, where a contract allowed the lender to make unilateral changes we would expect at the commencement of that contract that a responsible lender would:

45.5.1 ensure that the borrower understood that the lender was able to make changes under the contract without the agreement of the borrower; and

45.5.2 the scope of those potential changes and how they may affect the contract during its term and the implications for the borrower.

45.6 In terms of **agreed** variations, the principles only explicitly require a lender to ensure that it expresses any variation to the agreement in a clear and concise and intelligible manner. However, because variations can have such a material impact on a borrowers' obligations we think that a responsible lender would take steps (similar to those taken by the lender when entering into the original contract) to assist the borrower to make informed decisions about whether to agree to the variation and to ensure that the variation did not cause substantial hardship.

45.7 How a responsible lender meets its obligations will depend to some extent on the nature of the variation and who seeks it. For example, the principles may require different things from a responsible lender who seeks to obtain additional security for a loan than from a responsible lender who has been asked by a borrower to extend the term of the loan. However, at a minimum we would expect that a responsible lender would make contact with the borrower to:

45.7.1 Obtain updated information about the borrowers' financial situation before a variation is made. Lenders should not permit variations that would not meet the borrower's requirements and objectives, or that would be likely to cause substantial hardship.

45.7.2 Explain the effect of the variation on the total amount payable under the loan (if any.)

45.7.3 Explain the effect of the variation on the rights and obligations of the borrower and lender (if any) including on any rights or obligations relating to securities.

45.8 Where a variation is sought by the lender that increases or significantly changes the borrower's obligations under the contract (for example by changing the total amount payable under the contract or by substantially changing the nature of any security taken) we would also expect a responsible lender to make it clear that the borrower:

45.8.1 is not under an obligation to agree to the variation; and

45.8.2 should take advice about whether or not to agree to the change.

45.9 We think that a responsible lender would not harass or put undue pressure on a borrower to agree to a variation.

46. Other than complying with disclosure requirements, what information do/should responsible lenders provide to borrowers in relation to the credit agreement during the life of the agreement? For example, should lenders provide certain

information to borrowers to enable borrowers to make decisions as to whether to exercise their rights under the agreement?

46.1 Parliament has expressly set out in the disclosure provisions of the CCCF Act (eg, continuing and variation disclosure) the information it considers to be essential to enable borrowers to monitor their loan agreements. All other information provided by lenders to a borrower is optional and it is difficult to see how a failure to provide additional information could breach the principles.

46.2 It is unclear in what other circumstances it might be essential for lenders to provide additional information to borrowers in order to comply with the principles. If lenders are required to provide further information to enable borrowers' to make decisions about whether they should exercise their rights under the agreement, that information could include:

46.2.1 Reminding a borrower who was in default about the hardship process or right to terminate the agreement (if any).

46.2.2 Reminding a borrower who expresses concern about the contract at an early stage about their right to cancel the contract.

46.2.3 In appropriate circumstances, reminding a borrower who wished to prepay an agreement that they are required to pay a prepayment fee and the amount of that fee.

46.2.4 Reminding a borrower of their right to complain to the lender's Financial Disputes Resolution provider if other problems arise.

46.3 Where a lender provides additional information to the borrower during the life of the agreement, it is important that all such information is clear, concise and not likely to mislead, deceive or confuse a reasonable person. Information provided by lenders that might be subject to this obligation might include, for example, advice on whether a borrower should fix their mortgage interest rate, or whether they should insure their credit card debt.

47. What practices do/should responsible lenders refrain from during the life of the credit agreement? (For example, should responsible lenders refrain from the practice of holding multiple direct debit forms so that one can be re-submitted if a form is cancelled?)

47.1 We have observed a number of practices that lenders engage in during the life of the contract that we consider are a misuse of a lender's powers or that take advantage of borrowers. In our view a responsible lender should refrain from the following practices.

47.1.1 Increasing credit limits on credit agreements without the consent of borrowers or guarantors.

47.1.2 Allowing borrowers to exceed agreed credit limits (using so-called 'shadow limits') without the customer's awareness.

47.1.3 Holding multiple direct debit forms.[17]

47.1.4 Taking guarantees when a borrower is in default under a credit agreement.

47.1.5 Holding passports and other critical documents (such as drivers licences) to incentivise payments.

47.1.6 Continuing to receive money under a direct debit authority when there is no money owing under the credit arrangement.

47.1.7 Engaging in oppressive repossession practices (refer to our submission answers to Q76 - 78).

47.2 We also think that during the life of a credit agreement a responsible lender should:

47.2.1 notify borrowers within 45 days if their account goes into credit; and

47.2.2 notify borrowers who are approaching making final repayment, so that automatic payments or direct debits can be cancelled.

48. What practices should lenders follow in order to set a fee that is not unreasonable?

48.1 In the Commission's view a responsible lender should adopt the process set out below in setting reasonable fees. This process is, in our view, consistent with the High Court judgment in *Commerce Commission v Sportzone & MTF,*[18] in which the Commission's submissions on these points were accepted.

48.2 A responsible lender should adopt the following process:

48.2.1 **Identify the costs** that it wants to recover.

48.2.2 **Quantify those costs using an accepted accounting method**. Where the lender is seeking to quantify its average costs we would expect a responsible lender to take into account the costs it incurred in the preceding 12 months and any projections of costs it reasonably expects to incur in the next 12 months. Where a lender relies on a cost projection in setting its fees we would expect that projection to be commercially reasonable and able to be substantiated by the lender.

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17 We are aware of situations where a lender holds multiple direct debit forms so that it can lodge another form if one is cancelled by the debtor.

18 *Commerce Commission* v *Sportzone Motorcycles Limited (in liquidation), Motor Trade Finances Limited and MTF Securities Limited* [2013] NZHC 2531.

48.2.3 **Determine if and how the costs are closely relevant** to the matter giving rise to the fee. If the costs are not closely relevant to the matter giving rise to the fee they should not be recovered in that fee by a responsible lender. For example:

(a) Where the fee is an establishment fee, a responsible lender should determine how the costs are closely relevant to the application for credit, processing and considering that application, documenting the consumer credit contract and advancing the credit.

(b) Where the fee is an administration fee, a responsible lender should determine how the costs are closely relevant to administering the loan.

48.2.4 **Allocate the proportion of the costs that are closely relevant** to the matter giving rise to the fee using an accepted accounting method.

48.2.5 For example where costs relate to staff remuneration a responsible lender should:

(a) Assess the average time taken by the employee or employees to undertake the task that is closely relevant to the matter giving rise to the fee.

(b) Assess the total cost of remuneration for that employee or those employees (including performance schemes where that scheme or a proportion of that scheme is closely relevant to the particular task rather than the overall profitability of the company).

(c) Determine an hourly rate for the total cost of remuneration and multiply that by the average time taken to perform the relevant task.

(d) Where costs are fixed (such as the cost of premises or IT costs) the lender should be able to show how any proportion of those costs are closely relevant to the matter giving rise to the fee.

48.3 We consider that a responsible lender would seek external accounting advice in quantifying, determining and allocating costs to fees particularly where it has:

48.3.1 a complex business structure; and/or

48.3.2 significant costs; and/or

48.3.3 a large loan book.

48.4 Lenders may unintentionally, despite their best efforts, generate a profit through fees. Setting fees is often a forward-looking process (potentially involving an estimate of future costs and a projection of the number of contracts the lender expects to enter into) and there may be circumstances where, despite a lender's best efforts, those estimates and projections are not accurate and the lender does generate a profit through fees.[19] In these circumstances we would expect that:

48.4.1 any inadvertent profit will be small, if the lender has properly followed the process set out above; and

48.4.2 a responsible lender would re-assess the reasonableness of the fee at the earliest opportunity.

49. What costs should the lender be able to recover through establishment fees (eg, overheads, administration costs)?

49.1 As above, the close relevance test should apply and a responsible lender can recover costs that are closely relevant to receiving applications for credit, processing and considering applications, documenting the consumer credit contract and advancing the credit. Where the lender seeks to average those costs over a class of credit contract[20] the lender should:

49.1.1 Identify the class of contract.

49.1.2 Identify the number of those contracts the lender expects to be affected by the matter giving rise to the fee taking into account the number previously entered into and any business projections. We would expect any business projection to be commercially reasonable and able to be substantiated by the lender.

49.1.3 Divide the proportion of costs allocated to the matter giving rise to the fee, by the estimated number of contracts.

49.2 The Code could usefully provide further specific guidance about the sort of cost categories that are likely to be closely relevant to the establishment of loans. We have set out below at Table 1 some of the types of costs categories we have considered in our enforcement of the fees provisions. These cost categories are based on our 2010 draft fee guidelines but we have refined them here taking into account the development of our approach to certain cost categories and the Court's decision in *Commerce Commission* v *Sportzone & MTF.*[21]

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19 A lender will be able to ascertain whether it is earning a profit through its fees by subtracting the actual costs it has incurred and allocated to the fee from the revenue earned from the fee.

20 A "class of credit contract" is not defined in the Act but we expect it to mean a group of contracts that are likely to incur the same or similar types of costs.

21 Ibid. We have added here performance schemes and staff training costs, and refined our draft position on securitisation costs and cost of capital.

Table 1 – Establishment fees: recoverable costs

Cost Item	Comments
The wages or salaries of staff directly involved in the establishment of loans	A lender can recover the proportion of the wages or salary relating to the time spent by staff directly involved in the establishment of loans on establishment activities (subject to our comments about performance schemes set out below). We note that we would expect the wages and salaries of staff to reflect the cost to the commercial lender rather than a notional charge-out rate.
Performance schemes	A lender may be able to recover the proportion of performance schemes that are closely relevant to the establishment process. In order to be closely relevant, the performance scheme, or aspects of it, would need to be based on the establishment process, rather than other aspects of employee performance or the overall financial performance of the creditor.
IT costs	A lender may be able to recover costs associated with aspects of IT systems that are closely relevant with the establishment process. We do not think that costs associated with aspects of IT systems that support marketing and the administration of the business as a whole will be closely relevant to the establishment process. So if an IT system deals with a number of different aspects of a creditor's business the lender will need to allocate only the proportion of those costs that are closely relevant to the establishment process in order to recover them in an establishment fee.
Premises costs (including rent, rates, insurance and outgoings)	A lender may be able to recover costs associated with its business premises that are closely relevant to the establishment of loans. A lender would need to be able to adequately identify the proportion of space used for the establishment of loans and the time spent using that space for establishing loans in order to recover these costs in an establishment fee.
Asset depreciation	A lender may be able to recover some or all of the depreciation on the cost of an item provided a lender can demonstrate that some or all of the cost of that item is closely relevant to the establishment process (for example: depreciation on a computer used for loan establishment).

49.3 There will also be costs that we think will not be closely relevant to the establishment of loans, and which a responsible lender will not seek to attribute to establishment fees.

Table 2 – Establishment fees: costs not recoverable

Cost Item	Comments
Business administration costs	These costs are not closely relevant to a particular credit contract or class of credit contract. These costs are also not closely relevant to the establishment process.
Securitisation costs or costs relating to creditors' funding arrangements and operating structure.	Every business needs funds. These costs are not related to a particular credit contract or class of credit contract. These costs are also not related to the establishment of particular loans and we do not think that a responsible lender should recover these costs in establishment fees.
Costs relating to the development of credit-related products (for example credit-related insurance products)	These are costs that are incurred in order to "grow" or maintain a business and its level of profitability. The costs of developing new optional products for long term profit, even if they are developed for use in conjunction with the provision of credit, are not costs incurred in connection with the establishment of individual or classes of consumer credit contracts.
Staff training costs	These costs are not closely relevant to a particular credit contract or class of credit contract. These costs are also not closely relevant to the establishment of a particular loan.
Entertainment costs	These costs are not closely relevant to a particular credit contract or class of credit contract. These costs are also not closely relevant to the establishment of a particular loan.
Cost of Capital[22]	Cost of capital is not a genuine accounting cost of the type contemplated by ss 41, 42 and 44. In all but exceptional cases cost of capital will not be closely relevant to the establishment process, and should be recovered through interest charges. Exceptionally, where capital is obtained for a major or one-off transaction it may be sufficiently closely relevant to be recovered through establishment fees.
Marketing and advertising costs	These costs are not closely relevant to a particular credit arrangement or class of credit arrangement. These costs are also not closely relevant to the establishment of a particular loan.
Bad debt "write	This "cost" is not closely relevant to the establishment process.

[22] By opportunity cost we mean the benefit the creditor forgoes in order to lend to the debtor, eg, if the creditor could have earned a return of 5% on its capital investment in some alternative investment, then it would not be willing to invest in its current credit business were it not expecting a return of at least that amount. As such, a return of up to 5% could be treated as a cost, or more specifically, an opportunity cost.

off"[23]	
Costs associated with declined loan applications	These costs are not closely relevant to the establishment process as they do not result in a loan being established.
Provision for doubtful debts	These costs are not closely relevant to the establishment process.
Costs related to debt recovery	These costs are not closely relevant to the establishment process.

50. What costs should the lender be able to recover through credit fees generally?

50.1 A responsible lender should only recover costs that are closely relevant to the matter giving rise to the fee. We would expect that the matter giving rise to the fee would involve a particular transaction or particular service such as sending statements, administering or maintaining a loan account or cancelling a credit arrangement.

50.2 There should also be 'truth in advertising' so that a fee name accurately describes what costs it is charging for. For example, a 'billing fee' cannot include the costs of the lender's Christmas function.

50.3 We have noted at Table 3 some costs that, by their nature, may be recoverable through credit fees.

Table 3 – Credit fees: recoverable costs

Cost Item	Comments
The wages or salaries of staff directly involved in the transaction or service giving rise to the fee.	A lender can recover the proportion of the wages or salary relating to the time spent by staff directly involved in the particular transaction or service giving rise to the fee (subject to our comments about performance schemes set out below). We note that we would expect the wages and salaries of staff to reflect the commercial cost to the lender rather than a notional charge out rate.
Performance schemes	A lender may be able to recover the proportion of performance schemes that are closely relevant to the particular transaction or service. In order to be closely relevant, the performance scheme, or aspects of it, would need to be based on the particular transaction, rather than other aspects of employee performance or the overall financial performance of the lender.

[23] By "bad debt "write off" " we mean the debts that the lender has "written off" in accounting terms.

Asset depreciation	A lender may be able to recover some or all of the depreciation on the cost of an item, provided a lender can demonstrate that some or all of cost of that item is closely relevant to the particular transaction or service (for example: depreciation on a computer dedicated to a particular transaction or service).
IT costs	A lender may be able to recover costs associated with aspects of IT systems that are closely connected with the particular transaction or service giving rise to the fee. We do not think that costs associated with aspects of IT systems that support marketing and the administration of the business as a whole will be closely relevant to a particular transaction or service. So if an IT system deals with a number of different aspects of a lenders' business, it will need to allocate only the proportion of those costs that are closely relevant to the particular transaction or service in order to recover them through a credit fee.
Premises costs (including rent, rates and insurance)	A lender may be able to recover costs associated with its business premises that are closely relevant to the particular transaction or service. A lender would need to be able to identify the proportion of space used for the particular transaction and the time spent using that space for the particular transaction in order to recover these costs through a credit fee.

50.4 There will also be costs that we think will not be closely relevant to a particular transaction or service.

Table 4 - Credit fees: costs not recoverable

Cost Items	Comments
Administration costs of the business	These costs are not closely relevant to a particular credit arrangement or class of credit arrangement. They are also not closely relevant to a particular transaction or service.
Securitisation costs or costs relating to creditors' funding arrangements and operating structure.	Every business needs funds. These costs are not closely relevant to a particular credit arrangement or class of credit arrangement. They are also not closely relevant to a particular transaction or service and we do not think that a responsible lender should recover these costs in credit fees.
Costs relating to the development of credit-related products	These are costs that are incurred in order to "grow" or maintain a business and its level of profitability. The cost of developing new optional products for long term profit, even if they are developed for use in conjunction with the provision of credit, are not costs incurred in connection with any particular transaction or service. They do not

	relate to a particular credit contract or class of credit contract.
Staff training costs	These costs are not closely relevant to a particular credit contract or class of credit contract. They are also not closely relevant to a particular transaction or service.
Entertainment costs	These costs are not closely relevant to a particular credit contract or class of credit contract. They are also not closely relevant to a particular transaction or service.
Marketing and advertising costs	These costs are not closely relevant to a particular credit contract or class of credit contract. They are also not closely relevant to a particular transaction or service.
Cost of Capital	Cost of capital is not a genuine accounting cost of the type contemplated by ss 41, 42 and 44. In all but exceptional cases cost of capital will not be closely relevant to the transaction or service, and should be recovered through interest charges. Exceptionally, where capital is obtained for a major or one-off transaction or service it may be sufficiently closely relevant to be recovered through credit fees.
Bad debt "write off"	This "cost" relates to a debt that have not been paid by a particular borrower and have been written off by the lender. The cost is only closely relevant to that particular defaulting borrower and the lender should not seek to recover it from other borrowers. Bad debt "write off" is also not closely relevant to any particular transaction or service.
Costs associated with declined loan applications	These costs are not closely relevant to a particular credit contract or class of credit contract. They are also not closely relevant to a particular transaction or service.
Provision for doubtful debts	These costs are not closely relevant to a particular credit contract or class of credit contract. They are also not closely relevant to a particular transaction or service.
Costs related to debt recovery	These are costs that only arise on default and must be described as a default fee.

51. What costs or losses should the lender be able to recover through default fees?

51.1 In our view a responsible lender should only recover costs or losses that are closely relevant to the consequences of a particular default. The loss is specific to loss caused by the borrower, not by some other debtor or class of debtor. Lenders incur costs managing loans that are in default, but those costs should only be recovered from the defaulting borrowers.

51.2 In our view there are likely to be cost categories that, by their nature, we think will not be closely relevant to the debtors' default.

Table 5 Default fees: costs not recoverable

Cost Item	Comments
Bad debt "write off"	This "cost" relates to a debt that have not been paid by a particular borrower and have been written off by the lender. The cost is only closely relevant to that particular defaulting borrower and the lender should not seek to recover it from other borrowers
Marketing and advertising costs	These costs are not closely relevant to the particular borrowers' default
Costs associated with declined loan applications	These costs are not closely relevant to the particular borrowers' default.
Penalties or a charge designed to deter debtors from defaulting	This is not a genuine accounting cost. Nor is it a loss. It is not closely relevant to the borrowers' default. We consider that it is not a reasonable standard of commercial practice to include such charges in default fees.[24]
Cost of Capital	Cost of capital is not a genuine accounting cost of the type contemplated by ss 41, 42, and 44. Nor is it a loss. It will not be closely relevant to a particular debtors' default.

52. Are there any particular reasonable standards of commercial practice that should be taken into account when deciding whether a fee reasonably compensates the lender for a reasonable estimate of costs or losses incurred by the lender as a result of the borrower's acts or omissions?

52.1 We have not identified any particular standard of commercial practice that should be taken into account.

52.2 Reasonable standards of commercial practice are a safety check – or in other words, a 'limiting factor' on the fees that may be charged. These should be taken into account in addition to applying the cost allocation methodology.

52.3 In the process of fee-setting a responsible lender would, in addition to following the process described in our answer to Q48, have regard to whether there are reasonable standards of commercial practice that bear on whether a proposed fee "reasonably compensates" the lender (new s44(2)). We think that a responsible lender should particularly consider whether the

[24] Depending on their precise details, and on developing case law, such fees may to be unenforceable as penalties, as well as being unreasonable fees under the CCCF Act.

costs that the fee seeks to recover are commercially reasonable. By that, we mean that its costs are not artificial, fictional or inflated.

52.4 A common standard of commercial practice is not necessarily reasonable. And so the fact that a fee-charging practice is common does not, by itself, dictate that a proposed fee is reasonable.

52.5 But as a matter of practice, if a responsible lender was aware that its fees were higher than similar fees charged in the industry we would expect that it would trigger an enquiry into whether its fee is out of step with reasonable commercial practice, over-compensates for costs incurred and should be reduced.

52.6 We would not expect a responsible lender to increase a fee, after having undertaken the process set out our answer to Q48, in reliance on the commonality of commercial practice. If lenders were to increase fees, they would over-recover or profit from these fees.

53. How and when should fees be reviewed to ensure they remain reasonable?

53.1 In our view a responsible lender should review its fees at least annually to ensure that they remain reasonable. A responsible lender should also review its fees:

53.1.1 If there is a significant change to its costs or business structure.

53.1.2 If it is averaging its costs over a number of loans, there is a significant increase or decrease in the number of contracts it enters into.

53.1.3 If there is a change to the law on what can be recovered through credit fees.

53.1.4 If a lender inadvertently generates a profit through fees (see our answer to Q48).

54. What is a reasonable amount of commission for a lender in relation to credit-related insurance?

54.1 We suggest the code could set a 'safe harbour' threshold as to the commission that a lender could responsibly receive on selling credit-related insurance.

54.2 We do not have enough information to indicate what that safe harbour should be. We note the Australian National Credit Code has capped commissions on credit-related insurance at 20% of the gross premium. The Commission has previously issued guidance indicating that commissions below this level would not meet its enforcement criteria (meaning that the

Commission would be unlikely to investigate whether commissions under this level were reasonable).[25]

55. Should the code incorporate parts of the Commerce Commissions draft guidelines of fees? What changes would be needed to those guidelines to reflect subsequent case law views on unreasonable fees and changes to the CCCFA?

55.1 We support the provision of detailed fees guidance in the code, as set out in our responses to Q48-53 above. These submissions reflect our current approach to unreasonable fees. Our approach is based on recent judicial guidance, and supersedes the draft fee guidelines that we issued in 2010.

55.2 The Commission's draft guidelines were issued as an educative tool at the time, but the approach underpinning that draft guidance is no longer current. Lenders should already be complying with the unreasonable fees provisions in the CCCF Act, as applied by the Court.

55.3 As mentioned in our Introductory Comments above, depending on whether detailed fees guidance is provided in the code, the Commission may decide not to issue further guidance on the practical application of the unreasonable fees tests.

56. What other matters should the Code address in relation to fees?

Prepayment fees

56.1 We think that the code should provide guidance on how a lender should estimate its loss on prepayment. Prepayment fees are clearly within the scope of the code at 9F(1)(vii). Guidance in this area would be useful. The safe harbour formulae set out in the regulations are not mandatory and lenders are able (and do) use alternative methods of calculating their loss.

Buy-back fees

56.2 In our view the code should also provide guidance about how a responsible lender would set buy-back fees. In our view a responsible lender would recover through buy-back fees its reasonable costs that were closely relevant to establishing, maintaining or administering a buy-back transaction. We would expect a responsible lender to undertake the process set out in our answer to Q48 above in identifying, quantifying, determining and allocating those costs.

56.3 A responsible lender should only charge buyback default fees that compensates it for costs or losses that are closely relevant to the consequences of a particular default.

[25] http://www.comcom.govt.nz/dmsdocument/1833

Default, enforcement and the end of a consumer credit agreement

Repayment difficulties and other problems

57. How do/should responsible lenders monitor whether the borrower may be facing actual or possible repayment difficulties? Is it practical to check for possible repayment difficulties?

57.1 We support the inclusion in the code of guidance similar to that appearing in section 6.7.3 of the UK Consumer Credit Sourcebook (referred to at 165 of the discussion document.) We expect that submissions from lenders and consumer advocacy groups will assist in determining whether this guidance represents best practice in the New Zealand context.

58. What policies or procedures do/should responsible lenders have in place for dealing reasonably with borrowers who have or may breach the agreement or when other problems arise? (eg, in relation to assistance to be provided to the borrower)

58.1 We support the inclusion within the code of content for dealing reasonably with borrowers who have breached or may breach an agreement. Content could usefully be derived from:

58.1.1 the Financial Services Federation Guidelines (referred to at 163 of the discussion document); and

58.1.2 the UK Consumer Credit Sourcebook (referred to at 166 of the discussion document).

58.2 The code guidance should also acknowledge and permit the current practice whereby some lenders demonstrate leniency towards a borrower who is in difficulties. One specific aspect of 'dealing reasonably' concerns interest.

58.3 We are aware of lenders who currently have policies resulting in no or reduced interest being charged when borrowers are in default and struggling with repayments. Sometimes this is at the request of the debtor or a consumer advocate, and sometimes this is proactively offered by the lender.

58.4 We note that interest holidays can improve the prospects of full and timely repayment when the borrower's incapacity or unforeseen hardship has passed, and he or she is able to resume payment. Such measures can benefit both borrowers and lenders by preventing debts from spiralling out of control.

58.5 When a borrower is in default, accommodations between the parties may be able to resolve the difficulties. Responsible lenders should, as a matter of ethical practice, seriously consider all requests to stop/reduce interest. This is particularly relevant to payday loans where borrowers frequently encounter difficulties in repaying, leading to a default.

58.6 These borrowers may seek assistance from intermediaries (such as consumer advocates) to help them manage the situation with the lender. We would expect responsible lenders to be willing to liaise constructively with any intermediary who is assisting a borrower to try to manage a situation of default.

59. What do/should responsible lenders do to assist borrowers to be informed of their rights? (eg, in relation to unforeseen hardship relief and access to dispute resolution schemes.)

59.1 Information about unforeseen hardship relief and access to dispute resolution schemes are to be added to the 'key information' for initial disclosure in Schedule 1 of the CCCF Act.

59.2 However the lender responsibility principles require lenders to assist borrowers by providing information beyond the statutory disclosure, including in dealings subsequent to the credit being initially provide. We expect a responsible lender would remind borrowers of their rights if an event such as if a late payment, default or breach occurs. We also refer to our response to Q46.

60. How do/should responsible lenders communicate with borrowers in relation to breaches or potential breaches of the agreement to ensure that they treat borrowers reasonably and in an ethical manner? (-eg, in relation to staff training and policies and enforcement of those policies)

60.1 A responsible lender will attempt to prevent its customers' debts from spiralling out of control because of default interest and fees. A responsible lender will therefore contact the borrower at any early stage when concerns emerge, and actively manage breaches and potential breaches.

60.2 A responsible lender should consider the appropriate time to advise a guarantor of any default by the borrower, and the guarantor should be aware of this timing.

60.3 We expect a responsible lender would have a documented list of steps it will take if there is a default or other breach. We expect these steps would escalate from low level interventions like writing to or calling the borrower, up to more serious action including debt recovery through the courts.

60.4 We are aware of lenders repeatedly writing to customers in default (and charging repeated letter fees) even when the borrower is not responding to its letters. We do not consider that this is appropriate (or effective) conduct from a responsible lender. A responsible lender would review its processes (see our responses to Q64 and 65), to ensure that it was taking effective steps.

60.5 We would also expect a responsible lender to ensure that it carries out any follow-up of breaches in a discrete, confidential and private way. For

example, we have heard of lenders that leave a message with colleagues at a borrower's workplace. This is not treating a borrower reasonably and in an ethical manner, and could additionally amount to a privacy breach.

61. What do/should responsible lenders take into account when considering repayment plans proposed by a borrower (in connection with an application for unforeseen hardship relief)?

61.1 When considering a repayment plan proposed by a borrower, a responsible lender should at least:

61.1.1 Adopt a good-faith attitude towards the borrower.

61.1.2 Consider any commercially reasonable request by the borrower for relief or assistance in meeting their repayment obligations.

61.1.3 Take into account the lender's own need to preserve its commercial position.

61.2 A responsible lender would not act arbitrarily in considering a repayment proposal but would give careful and due consideration to the proposal.

62. What are the elements of a good internal complaints process?

62.1 A good internal complaints process will:

62.1.1 Be clearly explained to borrowers and potential borrowers in any documents, websites and other information.

62.1.2 Be easily navigable by a borrower of basic comprehension ability.

62.1.3 Provide for and deliver prompt resolution of complaints.

62.1.4 Clearly describe the process for taking any unresolved complaints further, such as to dispute resolution services.

63. What other matters should the Code address in relation to borrowers facing repayment difficulties or other problems?

63.1 Some debtors resort to the no asset procedure, or bankruptcy, as a final measure to deal with repayment difficulties. In these cases, a secured lender can exercise their rights in relation to their security.

63.2 Some lenders take securities that they have no intention of enforcing, or that they are unable to enforce, for the purpose of insolvency-proofing their debt. In our opinion, a responsible lender will discharge any security it holds when the debtor is:

63.2.1 bankrupt or has entered into a no asset procedure; and

63.2.2 the lender does not wish to or is unable to exercise its rights under its security agreement.

Enforcement action and the end of the credit agreement

64. What is the range of enforcement responses that lenders take in response to default by the borrower?

64.1 We are aware that options can include:

64.1.1 Phoning, texting, emailing or sending letters to borrowers.

64.1.2 Using a disabling device on a vehicle (if one is installed).[26]

64.1.3 Sending prepossession notices to a borrower (in some cases as a first response, but in others after they have undertaken any of the methods above).

64.1.4 Repossessing a specific vehicle or chattel security.

64.1.5 Issuing a Property Law Act notice.

64.1.6 Enforcing a Property Law Act notice by proceeding to mortgagee sale.

64.1.7 Exercising rights under an Assignment of Wages.

64.1.8 Exercising rights under cross-security agreements.

64.1.9 Seeking repayment by a guarantor (and then seeking to collect the debt using any of the procedures listed).

64.1.10 Engaging an agent to collect a debt – and possibly entering into a payment arrangement.

64.1.11 Seeking judgment for the debt.

64.1.12 Enforcing that judgment via an Order for Examination and an Attachment Order.

64.1.13 Selling the debt to a company that purchases non-performing debts (who will then seek to collect the debt using any of the procedures listed).

65. What policies or procedures do/should responsible lenders have in place for considering whether their enforcement response is proportionate?

65.1 A responsible lender should act proportionately in enforcing its security, and take into account the impact of enforcement action on the borrower.

[26] See section 83L of the Amendment Act regarding the activation of disabling devices, if installed.

65.2 This can only be achieved if the lender has in place a documented series of steps to attempt to recover payments due before resorting to enforcement action. It would be appropriate for the code to include the expectation that there should be such a process in place.

65.3 Any description of such a process in the code should take into account information from lenders about their existing enforcement practices, and adopt appropriate aspects of those practices.

66. What steps do/should responsible lenders go through before taking enforcement action? For example, before sending debts to a debt collection agency?

66.1 Please refer to our response to Q65. It would plainly be irresponsible for a lender to refer a borrower to a debt collection agency without taking reasonable steps to ensure that the borrower is aware of their default, and given a chance to remedy the default.

67. What are/should be responsible lenders' practices in relation to charging interest and/or fees once they have started enforcement action? (For example, once a debt has been sent to a collection agency.)

67.1 We are aware that some banks charge interest on credit card debts after they are sent to collection agencies, while other banks do not.

67.2 Once credit card debts (or any other unsecured debts) are sent to collection, significant fees are generally added to default interest and fees, and make it even harder for the borrower to meet their obligations. A responsible lender would consider not charging the accumulating default interest and fees when the debt is sent to a collection agency.

68. What steps do/should responsible lenders take to ensure that they treat borrowers and their property reasonably and in an ethical manner during the course of any enforcement action (including the manner in which the lender or their agents communicate with the borrower)?

68.1 Responsible lenders would treat borrowers reasonably by doing the following:

68.1.1 Requiring their debt collecting agents to notify borrowers shortly before loans will be repaid. Payment arrangements between a debt collector and a borrower can continue for a considerable time, and borrowers can lose track of the final repayment date. This can result in a borrower overpaying the amount owed.

68.1.2 Requiring their agents to promptly refund any over-payments.

68.1.3 Notifying WINZ or the borrower's employer to ensure that the borrower does not overpay the amount owed where debts are being collected by an Attachment Order. It is possible that the amount

required to be repaid will end up being less than the Court-ordered Attachment Order (eg, if repossession action is taken, or voluntary payments are made).

68.1.4 Not "naming and shaming" defaulting debtors eg, by placing them (or threatening to place them) on Facebook or by taking out advertisements in local/ethnic newspapers. This is particularly unreasonable in small or ethnic communities.

68.1.5 Our response to Q60 in relation to communication with borrowers is also relevant here.

69. What other matters should the Code address in relation to enforcement action?

69.1 We have no further comments.

70. What do/should responsible lenders do once they have been fully repaid? (For example, arranging release of securities).

70.1 In our view, the choice should be the borrowers as to whether security interests are released, and this entails the lender explaining the options and implications, and obtaining the borrower's preference.

70.2 Responsible lenders should promptly provide a letter or statement to borrowers confirming that a loan has been repaid, the nature of any securities held and options or processes for release of those securities.

70.3 We note that there can be distinct advantages to a borrower if a mortgage remains registered on their property after the underlying loan is repaid, and significant transaction costs if the security is required to be released (and possibly replaced later).These transaction costs would be borne by the borrower.

70.4 It may, in contrast, be valid for responsible lenders to be required to release personal property securities from the Personal Properties Securities register within a specified period of a loan being repaid. The costs of registering and de-registering a security interest are much lower.

Repossession

71. How/what steps should a lender take to satisfy itself on reasonable grounds that goods are at risk in accordance with Part 3A?

71.1 At a minimum, lenders should record why they reasonably believe the goods to be at risk, and the evidence of risk that they are relying on.

71.2 Lenders need to be able to substantiate their reasonable belief that one or more of the elements of the definition of "at risk" exist (i.e. the goods have been or will be destroyed, damaged, endangered, disassembled, removed, concealed, sold or otherwise disposed of contrary to the relevant credit

contract: s83E(2)). A responsible lender would not repossess goods on the grounds that they are at risk without having such evidence.

71.3 The evidence relied on does not need to be conclusive, but it needs to provide a reasonable basis. It therefore needs to be more than a suspicion, and it must exist before the goods are repossessed. We do not expect that a reasonable ground to believe the goods are at risk is merely that the borrower is in default under the contract.

72. What policies do/should responsible lenders have in place in terms of considering alternative options that could be explored before exercising the remedy of repossession?

72.1 Responsible lenders who take security over consumer goods should treat repossession as a last resort. Repossession has a significant impact on borrowers and their families, and is costly.

72.2 Responsible lenders should therefore have a documented series of steps they would take to attempt to recover payments due before resorting to repossession, and it would be appropriate for the code to include the expectation that there should be such a process in place.

72.3 Any description of such a process in the code should take into account information from lenders about their existing responsible lending practices and adopt these where appropriate.

73. Should the Code provide guidance on the repossession of items of little economic value?

73.1 Yes, we recommend that the code includes a clear expectation that responsible lenders should only take securities that are capable of securing repayment of the debt (in full or in part). This should exclude the use of items for security purposes that have sentimental, emotional or cultural value but low economic value.

73.2 If goods are of low economic value are taken as security, a responsible lender should not repossess them.

73.3 The Commission is aware of repossession of goods of minimal or no economic value. Examples include dilapidated couches, bags of clothing and cutlery, and broken appliances.

73.4 The Commission is also aware of examples where lenders have used security (and the threat of potential repossession) for leverage, or to intimidate consumers. The Commission believes the code should address this conduct, and make it clear that the reason for security is to secure the loan – not to act as a threat hanging over a debtor, or to punish debtors who are in default by depriving them of items that are useful to them (dilapidated tables, couches etc) but that have no economic value to anyone else.

73.5 If a lender repossesses low-value goods, or goods that prove unsaleable after a reasonable time, they should be returned to the borrower or made available for collection by them.

74. What arrangements should a responsible lender have in place for borrowers to voluntarily return goods when a repossession warning notice is issued?

74.1 If a repossession warning notice is issued, borrowers will have the opportunity to avoid the embarrassment, inconvenience and cost of a repossession by voluntarily delivering secured goods to the lender.

74.2 The repossession warning notice will be required to specify a "reasonable place" to which the borrower can deliver the goods for the purpose of exercising this right.

74.3 The code should provide guidance on what constitutes a reasonable place. A reasonable place should be as accessible and as convenient as possible to the borrower. For example, the place should be in the same locality as that in which the loan was entered into, and should have reasonable opening hours. As a minimum, we would expect the opening hours to be normal business hours. The place should not be a place, such as a residential address, that could cause the borrower to be concerned for their personal safety.

74.4 A responsible lender should provide its contact details to enable borrowers to voluntarily deliver goods.

74.5 A responsible lender (or its agent) would advise borrowers of the type and amount of fees likely to be incurred in preparing the goods for sale and would also acknowledge receipt of goods that are voluntarily surrendered to it.

75. Should the Code refer to the internal complaints resolution process used to resolve borrower complaints (given that a lender must not begin or continue repossession enforcement action until a borrower's complaint in relation to any repossession enforcement action has been resolved)?

75.1 Yes, having a clear and reliable internal complaints resolution process is consistent with the lender responsibility principles to treat borrowers and their property reasonably and in an ethical manner (s 9C(3)(d)).

75.2 Lenders are also required to be members of dispute resolution schemes under the Financial Service Providers (Registration and Dispute Resolution) Act 2008. Under that Act, members must have their own complaints processes.

76. What guidance should the Code provide in terms of how lenders or their repossession agents should enter premises?

76.1 The lender responsibility principles include the general requirement for lenders to treat borrowers and their property "reasonably and in an ethical

manner", and s 9C(3)(d)(iii)) of the Amendment Act refers to the right to enter premises not being exercised in an unreasonable manner. It would be appropriate for the code to provide guidance on the processes, practices and procedures lenders should have in place to ensure they act reasonably and ethically, and as to what practices might be unreasonable or unethical.

76.2 We suggest that the code should say it would not be reasonable for lenders or repossession agents to:

76.2.1 Enter premises where they have no right to enter.

76.2.2 Enter if the lender or repossession agent discovers during the repossession process that the address used on the Repossession Warning Notice is not the correct address for the debtor. (A new Repossession Warning Notice should be issued to any new address and this should include the 15 days period to remedy the default).

76.2.3 Use more force than is necessary to gain entry to premises.

76.2.4 Behave in a threatening or intimidating manner in entering or while on the premises.

76.2.5 Disturb or disrupt the premises more than is necessary.

76.2.6 Use or threaten to use violence towards anyone in connection with the repossession.

76.3 We also interpret the obligation to act ethically in relation to repossession as being an obligation to act fairly and honestly. So lenders and repossession agents should not:

76.3.1 Gain access to premises through trickery or subterfuge.

76.3.2 Take property they have no right to take, or where ownership is disputed (eg. in a flatting situation.

76.3.3 Take advantage of the immediate stress of a repossession to extract additional rights or concessions from borrowers.

76.3.4 Mislead borrowers about the rights the lenders (or the borrowers) have.

76.4 Lenders are also responsible for the actions of their servants and agents, so lenders are responsible for compliance by their repossession agents with their obligations under the CCCF Act. The code should include processes for lenders to ensure that their repossession agents fulfil these obligations.

77. What policies do/should responsible lenders have in place to consider whether repossession (and the costs involved in repossession) is proportionate to the scale of the default?

77.1 A responsible lender should act proportionately in enforcing its security, and take into account the impact of enforcement action on the borrower.

77.2 Referring to Q72 & 73 above, we would question the proportionality of repossession where goods are repossessed (or repossession is threatened) for relatively small amounts of debt, such that repossession would be disproportionate to the scale of the default.

77.3 A responsible lender will not repossess goods that a reasonable lender would apprehend have no resale value. We are aware of cases where the lender knows that the borrower has no assets of value, but has taken repossession action to intimidate or punish borrowers. This deprives borrowers of the utility of the goods and leaves them with the costs of the repossession action.

78. How do/should responsible lenders ensure that ethical behaviour is observed when effecting repossession?

78.1 Lenders will need to have systems and training in place to ensure the people carrying out repossessions are aware of the standards of reasonable and ethical behaviour, and to hold those people accountable (whether they are employees or repossession agents). We expect that effective oversight of the complaints processes would be part of the lender's compliance systems.

79. Should the Code provide guidance about how responsible lenders should carry out the process of selling repossessed goods?

79.1 Yes, the code should provide guidance on aspects of this process. In particular, guidance on time-frames for the sale of goods would be useful. A responsible lender would not hold on to security for an unreasonable period of time, given the nature of the seized goods. When a lender simply holds goods, the borrower is deprived of the use of the goods but the debt is not reduced and interest continues to accrue.

79.2 We are aware of situations where a lender has repossessed goods that they then decide are not saleable and has then simply disposed of them. As above at Q73, a responsible lender would return the unsold repossessed goods, or allow the borrower to collect the goods.

79.3 The terms under which a lender is required to sell repossessed goods under the Amendment Act are principles-based rather than prescriptive. Under section 83Z, the lender must ensure that "every aspect of the sale, including the manner, time, place, and terms, is commercially reasonable," and the lender must take reasonable care to obtain the best price. The tests are not new; they correspond with section 26 of the Credit (Repossession) Act 1997.

79.4 No means of selling was mandated under the Credit (Repossession) Act or the new Amendment Act.

79.5 The code should provide guidance on what is commercially reasonable, and how the lender can satisfy the duty to obtain the best price.

79.6 The lender should use a marketing and selling technique that has a reasonable chance of attracting interested buyers for the goods. The code should encourage lenders to use the most effective ways of selling second-hand goods to minimise their own losses, and the losses of borrowers.

79.7 Public auction is an often-used and effective means of selling repossessed goods. But if the goods are of an unusual kind or high value, a sales technique more likely to attract the best price for the goods should be used.

79.8 A lender has a conflict of interest if it sells repossessed goods to a related party and the code should provide guidance on this. If lenders sell to related parties, they should do so on the basis of independent and verifiable third-party valuations.

80. What other matters should the Code address in relation to repossession?

80.1 We have no further comments.

80.2 We appreciate the opportunity to submit on the discussion document.