



FINANCIAL SERVICES FEDERATION

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Summary of Questions for Submitters:

INTRODUCTION:

The Financial Services Federation (“FSF”) is grateful for the opportunity to submit on the Responsible Lending Code Discussion Document.

By way of background, the FSF is the industry body for the responsible and ethical finance and leasing providers of New Zealand. The FSF has over forty members and associates providing first-class financing, leasing, investment, banking and insurance products and services to over 1 million New Zealand consumers and businesses. The FSF’s affiliate members include internationally recognised legal and consulting partners. A list of our members is attached as Appendix A.

It is the FSF’s experience that there are two misconceptions about lending that that the FSF would like to clear up from the outset. These are:

- That lenders lend money to consumers who can’t repay it – all responsible lenders enter into loan contracts having determined that, on the evidence provided, the borrower will be able to repay the loan. Responsible lenders want their loans repaid so that they can continue in business and carry on lending.
- That repossession of property is another way for lenders to make money – no responsible lender wants to repossess goods of any kind. It is an absolute last resort which takes place after many conversations and interactions with the borrower. No responsible lender wants to run a second-hand goods business disposing of assets which almost always result in a loss to the lender.

The FSF agrees with regulators and consumer advocacy groups that New Zealand consumers need the utmost protection from the very small number of unscrupulous businesses operating in New Zealand for whom ultimate repayment of the debt becomes less important over time because of the exorbitant level of interest they are charging and those businesses (probably the same ones) who take oppressive repossession action from which they profit at the expense of the consumer.

Throughout the process of the development of the amended Credit Contracts and Consumer Finance Amendment Act 2014 (“CCCFA”), it has been regularly and publicly acknowledged by the Minister of Consumer Affairs, officials from the Minister of Business Innovation and Employment and regulators that the Act and the consequent development of the Responsible Lending Code will have little if any effect on members of the FSF because they are already recognised as being responsible lenders.

The FSF appreciates this public acknowledgement of the work done by its members to proactively develop their Responsible Lending Guidelines (on which the Responsible Lending Principles in the CCCFA have in part been based) and the recognition that FSF members are already lending responsibly and are not behaving egregiously towards any section of the community – vulnerable or otherwise.

In addition to the Responsible Lending Guidelines to which every FSF member has committed to adhere, the FSF also has clear Rules and a Code of Conduct for Members which sets out the responsible and ethical way in which FSF members are expected to behave and which also include a disciplinary procedure should there ever be an instance of non-compliance. The entry criteria for admitting new members to the FSF also ensure that a robust due diligence process is carried out before a membership application is accepted to ensure that new members will uphold the same high standard of responsible and ethical behaviour towards their customers as do existing members.

The stated aim of updating the CCCFA is to ensure that creditors lend to consumers and manage consumer credit contracts responsibly and to provide improved protection for vulnerable consumers without unnecessarily restricting consumer access to credit.

The FSF therefore believes that the purpose of the Code of Responsible Lending should be to describe the process by which responsible lenders advertise, originate and manage their lending interactions with the public right through to the eventual repayment of the loan including respectfully and effectively managing arrears, default and repossession action if necessary for the mutual benefit of the borrower and the lender. To this end, the Code of Responsible Lending will be most effective in providing safe harbours, setting out how lenders can best comply with their new statutory obligations, rather than imposing additional requirements.

The FSF is grateful for the opportunity to be able to provide such input into the Code so it is clear that, if the processes are followed, the lender can be identified as being responsible and this will allow regulators to target those lenders who do engage in unethical practices.

The FSF believes that in this way overburdening the already responsible lending community with excessive compliance costs created just to ensure that boxes are ticked that do not necessarily add anything to the process they are already following, can be avoided. It is essential that this is kept in mind because not placing an onerous compliance burden is one of the stated objectives of the Responsible Lending Code and any increase in the cost of providing lending to the public will inevitably be passed on to the borrower and the cost of credit will increase as a result. It needs to be borne in mind that lenders are subject to a matrix of regulatory requirements, as this submission goes on to describe in more detail, as the CCCFA does not operate in isolation.

The FSF also believes that the key to providing more consumer protection once the Code of Responsible Lending has been developed and comes into force will be in the enforcement of it. The FSF is as keen as regulators to see egregious lending behaviour towards consumers stamped out and will provide whatever support it can to regulators to identify this behaviour and will be very supportive of the regulators' attempts to stop it.

Lastly the FSF points out that if the Code is overly prescriptive the time available for finance providers to comply with it and ensure that their systems, processes, documentation and staff are able to meet the requirements of a prescriptive Code before it comes into force is minimal given the short timeframe at the end of the Code development and sign off process for implementation.

Ultimately however the FSF would stress that once the Code is developed and comes into force, enforcement will be the key to ensuring the aims of the CCCFA and the Code are achieved. The FSF will work with regulators to define responsible and ethical standards of lending behaviour, to ensure that FSF members continue to lead the way in maintaining these and to identify those lenders that do not uphold such standards.

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?

The FSF agrees with the proposed criteria for assessing what guidance should be set out in the Code as set out in paragraph 18. The FSF is however keen to see how lenders' existing obligations under Fair Trading Amendment Act 2013 ("FTA") and the Consumer Guarantees Amendment Act 2013 ("CGA") will fit with the Code and is keen to avoid inconsistencies.

Lenders are also subject to the provisions of the Financial Advisers Act 2008 ("FAA") which included the introduction of the Code of Professional Conduct for Authorised Financial Advisers. The FAA provides a point of sale exemption for motor vehicle dealers and retailers and the FSF believes it is important for the Responsible Lending Code to reflect that, rather than to cut across it. The two Codes need to line up – it is important to avoid inconsistencies and overlap with other regulation. Given the range of regulatory obligations that apply, the FSF considers that this criterion (avoiding inconsistencies) is as important in the design of the Code of Responsible Lending as the criteria set out at paragraph 18.

The FSF would also agree that retaining sufficient flexibility to allow lenders to adapt the guidance to different products and business models should be another criterion. Lenders are skilled and experienced at assessing the inherent risk of a lending proposal. Each individual proposal is unique in terms of the risk it poses and therefore the product provided and the business model used to deliver it needs to be sufficiently adaptable to manage the risk.

The FSF believes that one criterion not included in paragraph 18 but which should be is the need for borrowers to act responsibly and that lenders should be able to rely on self-certification from borrowers. Lenders should not be held to account if customers provide false information. Principle 7 of the Lender Responsibility Principles states that the lender may rely on information provided by the borrower or guarantor unless the lender has reasonable grounds to believe that the information is not reliable.

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

The FSF believes that several of the Codes used in other jurisdictions are now quite old and do not take into account the increasing use of on-line business transactions. Because of the size of New Zealand and the spread of population throughout the country the cost is prohibitive for most lenders to maintain a large branch network and therefore it is not possible for every lending transaction to be conducted on a face-to-face basis. Conducting the loan process is increasingly done through the use of on-line tools and the Code needs to take this into account.

The FSF believes that the Code therefore needs to acknowledge that it is appropriate for lenders to rely on their automated process when providing credit via on-line facilities as these processes

are built around responsible lending criteria for originating a loan which are the same as that for assessing a loan application in a face-to-face situation and which is further described in the response to question 4 below. In fact if anything responsible lenders take a more vigilant approach to on-line loan origination than they would do in a face-to-face situation.

It needs to be remembered that access to credit on-line is good for consumers as it provides them with the opportunity to obtain finance from a greater number of credit providers than might be available in their home towns so there is wider consumer choice, it is often a faster and more convenient way to access finance for the borrower and increased competition means a better product range and outcome for borrowers.

The FSF also believes that the Code should also recognise that information provided by borrowers via an on-line lending facility can be relied upon in accordance with Principle 7 of the Lender Responsibility Principles.

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

The FSF would agree that the Code should be structured so as to reflect the lifecycle of a consumer credit contract, remembering that the vast majority of such contracts proceed through their lifecycle without issue for both the borrower and the lender.

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?

FSF Members are Responsible Lenders:

Members of the FSF are already widely recognised as the lenders who act responsibly. The FSF wrote the Responsible Lending Guidelines that are the model for the Responsible Lending Principles in the Act are in part based on. FSF members are also subject to the FSF's Rules and Code of Conduct for Members including the disciplinary process and it is the expectation that all members will abide by these Rules and Code of Conduct or they will face the disciplinary process which can include expulsion from the Federation.

If regulators were considering which class of lender should be treated differently under the Code, the FSF would strongly suggest that they can therefore assume that those lenders who are not members of the FSF require stronger scrutiny of their practices than do FSF members.

In many places throughout this submission, the FSF provides guidance as to the processes, systems and business practices undertaken by FSF members to ensure they remain responsible lenders. The FSF believes that all lenders should be required to do the same.

The Code can reflect this by providing that compliance with an industry Code is evidence of responsible lender behaviour.

Point of Sale Lending Providers:

There are two ways that point of sale finance can be documented. With the first, the financier is always the only lender that is named in the loan contract, and the contract never shows the

retailer or dealer as a lender at all. With this type of point of sale finance retailers and dealers are not “lenders” for the purposes of the CCCFA and accordingly will not be subject to the Code.

With the second type of point of sale finance, the dealer or retailer is recorded as the lender on the credit contract, and once the loan has gone through the application process provided by the financier to be approved and terms and conditions disclosed, then the loan is assigned by the dealer or retailer to the finance provider for ongoing management through to its conclusion. The assignment process typically happens within 24 hours of the loan being approved. With this kind of point of sale finance retailers and dealers **are** “lenders” for the purposes of the CCCFA and accordingly **will** be subject to the Code.

The Code may thus apply to some retailers and dealers but not to others, which the FSF submits is inappropriate as the only difference between the two types of point of sale finance provision is a matter of form but in substance they are the same consumer finance product. In both situations it is the motor vehicle dealers and retailers acting on behalf of a finance provider that interact with the borrowers, but ultimately they are not making the lending decisions, and in both situations essentially the same lender-provided systems are used, as set out below.

The FSF believes that because the situations are the same in substance, they should be treated the same by credit law and since the provision of finance at point of sale under the first method above is not subject to the Code but doing so on an assignment basis will be, the best way to achieve competitive neutrality is to make it easy for dealers under assignment to comply with the Code as minimally as possible.

The FSF points out that dealers/retailers providing point of sale finance on the assigned basis described above, have exemptions under the FSPA and the AML/CFT Act, and therefore suggests that if exemptions apply in those contexts, they should apply in respect of the Code, as this is the closest we will get to a level playing field between the two kinds of point of sale finance processes.

Whether point of sale loans are on an assignment basis or are made by the financier directly, responsible finance providers have very clear guidelines and systems that must be used by the dealer or retailer in order for them to be granted the right to provide finance on behalf of the financier.

In terms of the particular responsibilities that dealers and retailers will have under the Code of Responsible Lending unless they are mitigated, these include:

1. Ensuring the loan meets the borrower’s requirements and objectives,
2. Ensuring that the borrower will be able to make the payments under the agreement without suffering substantial hardship, and
3. Ensuring that the terms of the loan agreement are expressed in plain language so that the borrower understands what these terms and conditions are and how they apply to them using appropriate disclosure procedures.

FSF members who provide finance to dealers and retailers by buying the agreement on an assignment basis ensure that such dealers and retailers meet these three obligations in the following way:

1. Determining the borrower’s requirements and objectives for the loan in a point of sale situation is very clear. The borrower has seen a motor vehicle or an appliance or whatever

that is being sold by the dealer or retailer and they want to take out a loan in order to be able to purchase it.

2. Ensuring that the borrower will be able to make the payments under the agreement without suffering substantial hardship is done by the dealer or retailer using the finance provider's decisioning process which includes assessment of affordability using either a score card built into the loan origination system provided by the financier or assessment by trained loan analysts. Credit checks are normally made on the borrower to ensure no adverse information exists against them. The types of criteria built into a credit decisioning system are described further in the answer to this question but the FSF would point out that financiers looking to provide loans on assignment carefully manage the originations process for these loans in order to prudently manage the risk they are taking on and therefore they do not include room for judgement calls on behalf of the dealer or retailer in these systems. The process is very clear in terms of the information the financier requires the dealer or retailer to input into their decisioning system so that the appropriate assessment can be made of the loan's affordability. Anything falling outside of that criteria would either cause the loan to be declined or would require the dealer or retailer to contact the financier to allow the financier to use their judgement in the situation. Where a manual assessment is undertaken a financier will have trained analysts to assess the loan application and make a judgement on affordability along with all the other assessment criteria utilised by the financier. Where further information is required due to any questions this is referred back to the dealer in the first instance to seek this information from the customer. At no point does the dealer or retailer make judgement calls on the loan assessment.
3. The disclosure to determine borrowers' understanding of the terms and conditions of the loan and how they apply to them is carried out in these situations by the dealer or retailer using a process prescribed by the financier. Responsible lenders provide the dealer or retail staff with training in what must be disclosed and how it must be done. They provide summaries of key information in plain language that the dealer or retailer can use to ensure borrower understanding.

Ultimately responsible lenders providing credit products to dealers or retailers on an assignment basis take the responsibility to ensure that the loan origination and disclosure process are appropriately carried out on their behalf. They have mechanisms in place to ensure that appropriate staff training is provided to their dealers and retailers and a quality control mechanism to ensure that their processes are adhered to.

Because the loan is assigned almost immediately upon being written to the responsible lender providing the finance it is the lender who is responsible for the ongoing management and monitoring of the loans written on their behalf by their dealer or retailer network. It becomes obvious to them very quickly if loans are being mis-sold or their processes are not being followed when they start to see higher than usual loan arrears or complaints from borrowers. That would prompt the responsible lender to several courses of action from further training and oversight of a particular dealer or retailer through to withdrawing the right for that dealer or retailer to provide finance to their customers.

Once the loan is assigned by the dealer to the lender, the lender alone is responsible for managing the lifecycle of the loan through to its conclusion. The FSF therefore submits that it is satisfactory for the dealer/retailer to rely on lender to comply with the Code obligations beyond the origination of the loan and therefore the Code doesn't apply to the dealer/retailer after the loan is assigned which is the same as the treatment of point of sale finance under the FSPA.

Further, in respect of the short period before the loan is assigned, the FSF submits that a dealer or retailer will comply with the Code's obligations in respect of that initial phase if –

- a) They apply the systems and processes required by the lender to whom the credit agreement is assigned;
- b) They use advertising supplied by the lender;
- c) They use loan documentation supplied by that lender.

The effect would be to ensure that ultimate responsibility for Code compliance would be located with the real lender.

Classes of Borrower:

The FSF believes it would be dangerous and potentially discriminatory to try to define a specific class of borrowers as "vulnerable". To try to class groups of borrowers by virtue for example of their income, beneficiary status, socio economic status, or similar would be too subjective a judgement and is more likely to make credit inaccessible or more expensive rather than fair.

The FSF also believes that if any class of borrower with whatever characteristics relating to socio-economic status, level of financial literacy, command of English or whatever is dealing with an identifiably responsible lender such as a member of the FSF, it should be able to be assumed that they will be being treated ethically and that they will not be being lent money they are not going to be able to pay back (unless their circumstances change during the term of the loan).

Revolving Credit:

The FSF would also submit that there is one particular class of agreement that should be treated differently under the Code and that is the provision of revolving credit facilities which are increasingly more commonly offered by lenders to give borrowers greater flexibility. Good credit providers will always be monitoring such facilities in order to identify any change in circumstances that may affect the borrower, but it is unrealistic to expect the creditor to be able to meet a continuing obligation to reassess whether the facility continues to meet the borrower's needs through the life of such a credit contract, and the Code should make clear that is only required to be assessed by lenders at the outset.

What Responsible Lenders Do:

There are however certain things responsible lenders take into account when making lending decisions. These include (but are not limited to) the length and quality of the existing relationship the lender has with the borrower, repayment history with the lender, employment history, age, income, other outgoings, family situation, how informed any guarantor might be and their relationship to the borrower. What a borrower applies for and what is approved has to make sense according to the lender risk model and their judgement.

Responsible lenders use either a scoring model which is an automated credit assessment system or they use experienced analysts using a set of lending guidelines to ensure consistency. Responsible lenders use independent agencies such as credit reporting agencies to gain an insight into a potential borrower's credit history. Responsible lenders will give greater scrutiny to borrowers with a poor credit history because they are potentially the most risky.

The FSF would also point out that positive credit reporting is gaining momentum in New Zealand and this potentially provides responsible lenders with an improved picture of a borrower's ability to repay.

The FSF suggests that it should also be remembered that Principle 7 of the Lender Responsibility Principles allows the lender to rely on information provided by the borrower or guarantor unless the lender has reasonable grounds to believe the information is not reliable. The borrower therefore has a responsibility also to act responsibly. The Discussion Document is silent on borrower responsibility.

Question:

The FSF has a question as to where peer-to-peer lending sits in relation to such lenders' obligations under the Code. The CCCFA does not appear to address this.

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

The FSF would submit that responsible lenders already apply the concept of scalability as the best way in which to manage the risk inherent in lending in line with the prime objective to ensure the loan can be repaid in accordance with the contract without incurring unreasonable costs to the borrower or the lender.

It is a question of how much the lender has to do to demonstrate that appropriate scalability has been applied. Under the s29 of the CGA, lending is described as a service and is therefore required to be "fit for purpose". The CGA also requires that products such as loans are sold with reasonable care and skill.

As mentioned in the response to question 4 above, point of sale exemptions exist under the FAA and should also apply here.

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

The FSF strongly believes that the Code should be principles-based and outcomes-focused rather than prescriptive. The Code is intended to be a "safe harbour" which lenders can choose to utilise or not, as they see fit. Prescription is inconsistent with that concept.

The FSF would also point out that all other legislation with which lenders are required to comply is risk-based. Therefore the Code should be too but guidance is helpful if it can be relied upon. As stated in the response to question 5 above, lending is required to be "fit for purpose" under the CGA and some consumer laws are based on the concept of "reasonableness" which should apply here.

Lastly, if the Code is overly prescriptive the time available for finance providers to comply with it and ensure that their systems, processes, documentation and staff are able to meet the requirements of a prescriptive Code before it comes into force is minimal given the short timeframe at the end of the Code development and sign off process for implementation. An overly prescriptive Code will cause extra cost to credit providers in order to comply with prescriptive requirements with no apparent benefit to the consumer and which would be ultimately passed on to the consumer which is not consistent with the Code's objectives.

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

The FSF refers to the answer provided for question 4 and submits that membership of the FSF carries with it the distinction that the lender can be relied upon to act responsibly in all dealings with borrowers. The FSF also points out what it has already said in answer to questions 4 and 5 above with regard to the application of scalability, and in particular to the need for to recognise that lower levels of obligation are appropriate for retailers and dealers involved in point of sale finance.

Please also refer to the comments made with regard to the provision of credit on-line in answer to question 2 above.

The FSF also points out that the level of enquiry required depends on the relationship the lender has with the borrower and that more enquiry is typically needed for a new customer than an existing one.

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.)

All FSF members have a process to approve their advertising including taking legal advice as appropriate. This is a well-established part of business process for service providers in New Zealand, given their existing obligations under the Fair Trading Act.

For larger FSF members everything goes through an internal review by their in-house legal team. In these cases, the member's Marketing or Products team prepares the advertising which then goes to a legal or compliance review to ensure it's consistent with the law. There is rigour around the sign-off process by Compliance and Legal Departments and FSF members talk about a level 1 and 2 sign-off process.

For smaller FSF members their process takes account of whether they are signing off on advertising of a new product or concept or whether it is essentially something they have advertised previously. Existing advertising will have been through a process of external legal advice to ensure compliance and is therefore used as a template. When there are any changes or they are doing something new it goes through the external legal advice process to ensure compliance.

FSF members take their compliance obligations seriously. After meeting their obligations to get either internal or external legal sign-off for advertising, the lender still has to disclose the particular terms and conditions of the loan when the customer comes in to apply. Advertising is often just about awareness of the brand and the offer rather than any particular loan product.

Loan advertising is already covered by the FTA and industry codes (as noted below) and lenders have been working under these for some time. The recent consumer law reform has strengthened the provisions around unsubstantiated representations and the requirement for evidence to be available to back up any claims made in advertising. If the Code were to seek to impose an overly specific set of processes for lenders to follow this would at best duplicate

existing practices and at worst tie lenders in to a review process that would be of little benefit whilst also restricting access to information for consumers.

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

No. The FSF believes that it is irrelevant whether the lender is large or small, or whether its processes use internal or external legal sign-off or advice. Advertising needs to comply with legislation and the process ensures this is the case. Existing legislation such as the FTA should be sufficient. It is the lender's risk if they don't have a process in place.

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?

The FSF suggests that the Advertising Standards Authority's Code of Practice for Financial Advertising could be referenced as good practice as it is being used by FSF members. There is also Commerce Commission guidance that is helpful.

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

The FSF believes that all lenders should be producing advertising that is consistent with the laws that apply, has followed a sign-off process to ensure that that is the case and that it adheres to Codes of practice and guidance as per the answer to question 10 above. Responsible lenders will include disclaimers such as the approval of the loan being "Subject to normal lending criteria". The FSF does not believe that advertising of "No credit check lending" is consistent with responsible lending practices.

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

The FSF submits that to do so would be too prescriptive. Risk relates to the borrower as well as the lender. Responsible lenders go through a risk-based analysis process to determine whether to lend irrespective of whether the customer was attracted to them by an advertisement. Any risks to the borrower are explained in the disclosure process.

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?

Responsible lenders follow a legal process as described in the answer to question 8 above that avoids advertising that is misleading or targeted. It is the way in which the borrower is treated once a loan enquiry is made and throughout the life of the loan that is important.

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

The FSF does not believe that the Code needs to address anything in relation to advertising as relevant legislation, Codes of Practice and lender processes already exist as described above.

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 modes of providing credit? (e.g. online applications). Should certain information be required to be given orally for face-to-face or telephone interactions with customers?

FSF members already take acknowledgement from the borrower that disclosure has occurred and been understood. The FSF would also point out that the cooling off period applies (and has been increased). The same disclosure obligations also apply for on-line applications.

An application taken over the phone or online has the same information and disclosure requirements as a face-to-face application. If anything, the lender risk is greater when an application is not done face to face and the lending process is modified to reflect this.

The FSF would also point out that the borrower has responsibility under Principle 7 of the Lender Responsibility Principles to provide reliable information. The lender must be able to rely on the borrower's confirmation of understanding of disclosure as much as on the reliability of information.

Responsible lenders use their experience and judgement to determine when a borrower might require independent advice or assistance with translation. They also ensure that sufficient training is provided to dealers/retailers providing point of sale finance where appropriate.

The FSF would also point out that the FAA properly recognises that some creditor/financial advisers will provide class advice and this is perfectly legitimate under the legislation in respect of consumer lending products. However there is a genuine risk that the obligations of the Code of Responsible Lending could undermine that if the Code requires "assisting" the consumer to extend into the provision of personal advice. The FSF believes there is a potential conflict when dealing with customers face to face when non-QFE lenders find themselves unable to comply with the Code without breaching the prohibition on personal advice under the FAA.

Some lenders provide their borrowers with Key Fact Sheets or summaries to assist borrowers' understanding of the important terms and conditions and implications of their loan. The FSF believes that this is responsible lending practice in some cases but suggests that the Code should not mandate that such summaries should be provided in all situations because of the need to be careful that such summaries do not override the credit contract. There is a danger of the customer relying on the summary and not taking account the terms and conditions of the loan contained in the credit contract. Care needs to be taken that the credit contract itself does not become irrelevant or overlooked.

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

The FSF submits that the borrower's ability to meet the lender's lending criteria is the key consideration particularly with regard to the borrower's ability to service the debt and to provide whatever verification of this the lender requires.

For responsible lenders, if the borrower is unable to provide the information required by the lender the loan will not be approved.

With regard to paragraph 69 of the discussion document and the suggestion that the lender provides the information through a friend or relative of the borrower, the lender is unable to know that the friend or relative is translating accurately.

FSF members make a best effort to ensure each borrower understands what they are committing to or they don't proceed with the loan.

The FSF would point out that it is impossible to translate documentation into every language spoken in New Zealand other than English. Some FSF members whose market includes a larger number of people from Pacific Island communities employ Pacifica speaking staff and do translate their documentation and websites into Pacific Island languages to ensure borrower understanding.

The FSF suggests that the obligation on lenders should be that they refer the borrower to an adviser or interpreter and in some cases they should insist the borrower do so to ensure they fully understand the extent of their obligations.

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?

FSF members provide borrowers with whatever opportunity they need to ask questions and provide information on websites and in product collateral.

The cooling off period provides sufficient time for a borrower to seek advice or withdraw from the loan. The FSF believes that if a borrower or a lender is not getting the answers they need in a way in which they understand, they should not proceed with the loan.

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

FSF members go to great lengths to develop their credit agreements to ensure they are understandable by the widest possible number of borrowers. The FSF's Responsible Lending Guidelines were prepared using plain language standards.. FSF members ensure that all borrowers acknowledge their understanding of the terms of the credit contract.

The FSF would also point out the prohibition against the use of unfair contract terms which has been introduced into the FTA.

It is not in the interests of a responsible lender to have difficult to follow documents as it just creates more questions from the borrower and potential issues with the loan.

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

FSF members provide the information a borrower needs to understand the implications of the credit agreement. Where necessary, for example with regard to a complex lending product or complex security arrangements such as the inclusion of a guarantee, the lender always recommends that the borrower takes independent advice.

As regards the "technical or legal concepts" referred to in the question, some of these are dictated by the CCCFA's disclosure requirements being themselves "technical or legal" in nature, which means that FSF members are to some degree constrained by the CCCFA in respect of the language used to describe such matters.

Please also refer to our comments with regard to the potential conflict between the Code and the obligations the Code will place on lenders and the fact that they are not able to provide personal advice under the FAA under question 15.

The FSF would suggest that the concept of scalability applies.

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

FSF members strive to ensure that their documentation meets all legal and readability criteria.

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?

The majority of FSF members provide straightforward loans with short terms using standard documentation which the FSF does not believe are sufficiently complex as to require recommending borrowers seek legal advice to understand.

FSF members do however recommend and encourage borrowers and guarantors to ensure they understand the nature of their obligations under a contract or guarantee, and the implications of failing to comply with them. This includes a recommendation to take independent legal advice before they sign the relevant document.

However lawyers are not qualified to advise whether a loan is a good idea or suitable for the borrower. They can only advise on the terms and implications of failing to comply with them.

Lending products also include lending secured by mortgage over property which inevitably requires legal advice to be taken. Apart from that and for most other consumer finance transactions the FSF believes it is not realistic to expect people to get legal advice. Borrowers are often reluctant to pay for legal advice unless they understand the need for them to take it.

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

Please refer to the answer for question 21 as above. FSF members use their judgement based on skill and experience to know when they need to recommend guarantors get independent legal advice.

Responsible lenders would have exactly the same discussion with a guarantor as for a borrower but would choose to talk to the guarantor separately to the borrower particularly if they have any reason to believe they are signing under duress or do not understand what they are committing to.

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

The FSF strongly believes that the provision of appropriate insurance that meets the borrower's needs is a key part of responsible lending. When a person takes on a loan they are taking on extra risk to themselves and their family and insurance provides the necessary protection to them should something go wrong such as illness, loss of employment or death during the term

of the loan. Insurance provides another alternative when such events occur other than getting into arrears, default and potentially repossession.

In the FSF's experience, there is a misconception that credit-related insurance only serves to add to or increase a borrower's liability, when in fact it is specifically designed to assist a borrower when they suffer an adverse event (e.g. death, accident, illness, redundancy, hospitalisation, business interruption, suspension or strike-related action) that places them at risk of not being able to afford their weekly/monthly payments.

The stated aim of updating the CCCFA is to ensure that creditors lend to consumers and manage consumer credit contracts responsibly and to provide improved protection to vulnerable consumers. It therefore seems sensible to the FSF that the intention of the Code should be to encourage the promotion of appropriate and responsibly-sold credit-related insurance.

It is therefore prudent for responsible lenders to offer appropriate credit-related insurance so long as it is made clear to the borrower that taking the insurance is optional.

FSF insurance members already provide their lenders with point of sale material to provide to customers that includes the full policy wording plus a summary of cover – bullet point information on the contract – including claim limits/excesses etc.

FSF members ensure that borrowers can only access insurance options that are applicable or appropriate to them. Responsible insurance providers give training to lenders to ensure their products are sold responsibly.

Some responsible lenders use waivers acknowledging that the borrower has been offered and declined insurance and therefore does not have protection if something goes wrong for them throughout the course of the loan. This is a means to reiterate to borrowers the importance of being adequately protected when they take on debt.

It should be remembered that the ability to cancel the loan and therefore the insurance exists under the CCCFA.

FSF members also ensure that appropriate disclosure is carried out when the premium is financed by the loan.

The FSF is aware that some lenders offer a Payment Waiver to their borrowers. This is an arrangement whereby a lender or supplier agrees to waive their rights to repayments if the consumer dies or becomes incapacitated or unemployed. The consumer can purchase a payment waiver at an additional cost through the lender. The FSF believes that all such products should be treated by the Code in the same way as other credit-related insurance products for consistency.

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?

Please refer to the answer provided for question 8 as the obligations for advertising credit products should apply equally to credit related insurance. Responsible lenders will not make claims that cannot be supported.

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

FSF members allow borrowers as much time as they need before signing the loan contract. There is nothing to be gained by a responsible lender forcing a borrower to take a loan that the borrower does not need or cannot afford. It should also be remembered that the cooling off period has been extended and is sufficient.

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

FSF members provide the opportunity for borrowers to print off any documentation and take it away to consider before making a decision and to take whatever advice they feel is required before signing. They also take an acknowledgement of understanding.

Good on-line application processes prompt for customer responses throughout the process or it cannot proceed. The borrower provides confirmation of understanding at each step.

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

Apart from the “scaled” obligations for retailers and dealers suggested for a point of sale context above, the FSF does not believe there are any other matters the Code should address in relation to assisting informed decisions as all such means have already been covered and lenders have obligations under the FAA to ensure enough information is provided to allow borrowers to make informed decisions. There is a real risk that requiring lenders to provide any more documentation to borrowers could become confusing and probably wouldn't get read.

Making reasonable enquiries:

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?

Responsible lenders seek information and proof of other liabilities and source of income to determine the borrower's ability to repay the loan which is the most important criterion. The scale of the loan and the credit risk determines the quantity of additional information required.

FSF members believe that the credit check is an independent source of information but is only one of the tools they use to assess an application – there is firstly the collection of information from the customer and often some form of verification or validation. The AML/CFT Act provides the minimum standard for identification of the borrower.

A credit check highlights that a borrower has credit experience. Lack of enquiry can indicate higher risk in terms of the borrower's ability to understand what they are getting into or the need for a responsible lender to provide more detailed disclosure to ensure the borrower's understanding of what they are taking on. A credit check also enables a lender to look at the frequency and number of enquiries about a borrower which enables the lender to cross reference against disclosed commitments or seek further clarification. Not all borrowers disclose all existing commitments.

The credit check is a good indicator of credit behaviour and there is a close correlation between the credit score provided by the credit reporter and subsequent borrower behaviour.

Comprehensive credit reporting that provides information on a person's positive credit history as well as anything negative that may exist about them gives lenders a much better picture of a borrower's repayment history, existing commitments and commitment to meeting these.

For low levels of credit like a \$1,000 credit card limit FSF members would not support having to adhere to a long prescriptive list of required information to be taken from the borrower which should be proportionate to the amount borrowed and the risk inherent in the loan.

Responsible lenders will also take account of the nature of security being offered to secure the loan (if any).

Principle 7 of the Lender Responsibility Principles regarding the lender being able to rely on information provided by the borrower applies.

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

It is part of responsible lending practice to explain why questions are being asked. It is also a requirement of the Privacy Act that it is explained why information is being obtained and how the information is going to be used. FSF members can provide borrowers with a copy of the Responsible Lending Guidelines which explain why questions are being asked and what happens to the information gathered.

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?

FSF members understand when it is appropriate to ask the borrower for verification or validation of the information they have provided. Responsible lenders may rely on third party information, e.g. credit check, NZ driver licence for proof of identity, bank statement for proof of income, liabilities, utility bill for proof of address. Some of this information is available electronically e.g. credit check, NZ driver licence.

Principle 7 of the Lender Responsibility Principles allows the lender to rely on information provided by the borrower unless there are grounds for the lender to be on notice that the information may be incorrect.

Responsible lenders may treat new borrowers differently to those borrowers with whom they have an existing relationship and a repayment history. More enquiry or information verification or verification may be undertaken for new borrowers.

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

Please refer to the answers to questions 28 and 30 above. Previous repayment history is always a good indicator and borrowers expect recognition of a good repayment history in terms of making the subsequent application process easier for them. Responsible lenders should be able to rely on past favourable experience with a borrower. It is about knowing their customers and the scalability concept also applies. A proven level of loan servicing is a good guide as to customer affordability.

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

Responsible lenders will establish the purpose of the loan during the origination process. The FSF believes that borrowers should have freedom of choice with regard to the use of their loan proceeds. The lender's key responsibility is to determine the borrower's ability to service the loan without hardship.

In the case of point of sale finance providers, determining the objectives of the borrower is not an issue as it is obvious.

In the case of situations like debt consolidation loans responsible lenders often pay the other creditors directly from the proceeds of the loan rather than providing the funds to the borrower which is a protection for the borrower.

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?

As for question 32 above, responsible lenders will ask the borrower what their requirements and objectives are in order to determine the most appropriate product to meet their need. The CCCFA includes the requirement for the lender to do so and the CGA requires the lender to ensure the product offered is fit for the borrower's purpose.

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?

The FSF submits that a high proportion of credit applications at point of sale are processed without the involvement of financial advisers.

The FSF submits that the FAA takes care of this and is being adhered to. Please also refer to our comments with regard to the potential conflict between the Code and the obligations the Code will place on lenders and the fact that they are not able to provide personal advice under the FAA under question 15.

Even in the case of those who provide point of sale finance the loan is assessed by people who are registered and comply with the FAA. Every loan is assessed through a front end and back end process and the Point of Sale financier does not make decisions with regard to the affordability or otherwise of the loan, the lender does. Please refer to our answer to question 4 for more information on how this process is managed by responsible lenders.

The FSF would also point out that at point of sale borrowers expect convenience (access to funds simply and quickly) and the vast majority of customers do not incur any issues or problems. Responsible lending must not result in restricting access to credit or reducing economic activity.

If a change is introduced so that dealers, agents or retailers have to provide advice, the FSF submits that lenders will incur significant cost in staff training to ensure compliance etc. This could potentially result in the consumer being denied access to point of sale finance due to the

significant cost and training involved or at best is likely to have a negative impact on the cost of obtaining point of sale finance which is not in the best interests of consumers and will limit choice.

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?

FSF members ensure that the borrower demonstrates the ability to repay the loan regardless of whether commission is involved e.g. through broker-introduced lending. Responsible lending principles still apply.

Commissions and bonuses are common remuneration methods in many industries. The notion that a commission or bonus will lead to bad behaviour has no basis and the payment of commissions or bonuses does not mean there is a conflict nor is there any link between payment of commission and substantial hardship.

A responsible lender wants the customer to be satisfied with the product, the cost of the product and to come back to borrow again if required.

The payment of commission is built into the price of the product and is therefore controlled by market forces. The market is very competitive and responsible lenders will explain products to consumers so they can make an informed choice. No other legislation regulates the amount of mark-up built into the price of a product or any commission payable on the sale of the product.

In terms of commissions paid with regard to credit-related insurance, the FSF would also reiterate the points made in the answer to question 23 about the benefits of credit-related insurance to protect consumers when adverse events occur and that the Code should encourage not discourage the sale of credit-related insurance and should therefore avoid regulating the amount of commission payable.

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

At origination, responsible lenders are already ensuring that the approval of the loan will not put the borrower into a situation of substantial hardship. This is part of ensuring that the loan will be able to be repaid which as already mentioned is the most important consideration when providing finance.

Substantial hardship cannot be defined by a formula. A responsible lender will not lend to a borrower who cannot meet the terms of the contract.

Hardship may occur where borrower circumstances change post origination. Credit related insurance provides cover for the unexpected and should be offered, without being mandatory, on all loans.

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

No. Responsible lenders don't lend to someone who can't repay. They are skilled and experienced in judging whether the approval of a loan would put the borrower into a hardship situation and would make the decision to decline the loan application accordingly. It is not in the interests of either the lender or the borrower to lend money that cannot be repaid.

This goes back to the issue of scalability. Responsible lenders use a process to determine the borrower's ability to repay the loan as per questions 4 and 28. It is not always a one size fits all approach and individual borrower circumstances apply.

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

No. The FSF believes that this is subjective. Individual circumstances vary and how one borrower manages their finances does not compare to the way in which another one might do so. Responsible lenders are skilled and experienced and are therefore capable of using their judgment as to whether approving the loan application would place the borrower into substantial hardship. Specifying a threshold could be dangerous – as an example, first home buyers will make significant changes to lifestyle and spending habits in order to be able to get a house. Please also refer to the answer to question 36 above.

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

A lot of lending outside of mortgage finance is done on fixed rates that remain fixed throughout the term of the loan. It would depend on the product being offered and stress testing or a sensitivity analysis process could apply in situations where the amount being borrowed is significant. In saying that though lenders do not have a crystal ball. Trying to consider such things would not work for revolving credit situations as an example. The borrower has responsibility also to not get himself or herself into a situation they may not be able to manage. Changed conditions can also work in the borrower's favour e.g. salary increases.

Again a responsible lender will use their judgement based on accumulated experience of the inherent risk in making a loan to a particular borrower. Some responsible lenders might find it prudent to do a sensitivity analysis where serviceability for a mortgage is tight (as an example). If they have concerns about such things as interest rate rises they might suggest the borrower takes a longer fixed term to maintain certainty around outgoings.

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

For responsible lenders the lending criteria as a whole but in particular the borrower's ability to repay is first and foremost and no amount of security will suffice if affordability criteria are not satisfied. Lending decisions will not be based solely or primarily on the value of the security being offered.

A responsible lender relies on realisation of the security as a last resort when all other methods of bringing the loan in line with the contractual terms have failed. Realisation of security rarely meets the needs or expectations of either party.

However there are some circumstances such as provision of bridging finance in which the inherently higher risks involved and the size of the customer's temporary obligations typically necessitate reliance on security to a higher degree than usually. It's also customer choice.

Contracts with final balloon payments are an example when purchasing a motor vehicle. In these cases the borrower usually intends to trade the vehicle in and purchase a new one at the end or it will be intended that the borrower will refinance the remaining debt rather than make the final payment. The lender will have determined the borrower's ability to meet that commitment at the outset. Responsible motor vehicle lenders take a conservative view on residual values based on historical market resale values to aim the residual within future salvage or resale value. This knowledge protects both the borrower and lender.

In some cases the nature of the borrower's business may be speculative for example a property developer. Responsible lending judgement will apply.

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

No. Having said that though it could be assumed that anyone borrowing from a payday lender for example is already in hardship which is why they are borrowing. They should not necessarily be prevented from doing so but the Code could particularly address how such lenders should demonstrate responsible behaviour towards their borrowers.

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?

The FSF does not believe that this is a proper enquiry for the Code to address. In general the asset secured should have a link to the loan but this is not always the case e.g. loan secured against mortgage over real estate. Fundamentally there is nothing wrong with taking a large amount of security for a small amount of borrowing. Indeed it is common practice for borrowers to leave a mortgage in place rather than have it released when loan is repaid in anticipation of potential future borrowings. It is always about the quality of the underlying credit and the borrower's ability to repay.

The provision of security may have a bearing on the interest rate charged. Market forces apply and customer choice is important as a better interest rate might be available because of higher equity so long as the customer is aware that the security is in place.

Responsible lenders provide adequate disclosure of what security is being taking at the start of the loan and should advise the borrower of the potential consequences to the underlying security if they breach the loan contract. This would include making borrowers fully aware of the implications of All Present and After-Acquired Property clauses in security agreements and what is involved before signing.

It should also be remembered that Non-Bank Deposit Takers who also lend have a responsibility to their investors as well as their borrowers and they would not be discharging this responsibility if they allowed their security position to become too tight. Those lenders who are not Non-Bank Deposit Takers also have an obligation to their stakeholders to ensure that they are lending prudently and therefore that they are taking adequate security to cover their exposure.

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?

The FSF does not believe there are any other matters the Code should address in relation to making reasonable enquiries to assess whether the credit agreement meets the borrower’s requirements and objectives and can be repaid without substantial hardship.

During the life of a consumer credit agreement:

Dealing during the term of the agreement:

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

Responsible lenders use a process similar to that for loan origination including disclosure and documentation and also taking into account borrower repayment history. Hardship situations often require variation to the contract.

Scalability also applies depending on the size of the loan.

Responsible lenders will ensure compliance with existing legislation. Disclosure obligations also apply for variations to a contract.

Credit card limit increases are not automatically provided to customers by FSF members. Customers are invited to contact the lender to access an increased limit if they want it. These are only offered because of good repayment history.

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?

Please refer to the answer to question 44.

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?

The FSF does not believe that anything additional is required over and above what is already required in legislation. Responsible lenders have customer relationship or collections teams who will maintain contact with the borrower throughout the term of the loan as required.

Most lenders of substance provide online access to account information, which provides all the disclosure previously available only on paper based statements.

Continuing obligations defined under the CCCFA are helpful.

The FSF also believes that in the case of fixed rate/fixed term loans no further update should be required. It is common for motor vehicle lenders to lend on a fixed rate for the entire term of the loan so the FSF would ask what value is provided if nothing is changed.

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?)

Only bank-approved direct debit initiators can use a direct debit process. If this is going on banks could prevent the lender from being able to initiate direct debits.

Fees:

The CCCFA specifies that profit can only be made on interest and that non-interest costs may be recovered through fees, provided there is no profit on those costs and provided the costs are connected to the transaction, product or service.

The FSF supports the intention of the CCCFA that fees should not be a source of profit. The FSF also supports the intention of the CCCFA that only “the creditor’s reasonable costs in connection” or “the creditors average reasonable costs of the matters referred to in paragraph (a) for the appropriate class of consumer credit contract.” may be recovered through the fees charged against that transaction or service. A reasonable interpretation is that costs *not* in connection with a “class of consumer credit contract” may not be recovered in the fee charged on that “class of consumer credit contract” or “that application”. Thus, any costs that only relate to loan A, e.g. a home loan, may not be recovered through any fee charged on loan B e.g. a personal loan. All costs should be recoverable but only if there is a proven connection to a specific product, transaction or customer. This is reflected in the draft guidelines issued by the Commerce Commission in May 2010.

If there is any artificial limit placed on costs that can be recovered through fees, e.g. variable costs only, costs not recovered through fees will be recovered through an increase in the interest rate, with the undesirable effect of larger loans paying a disproportionate share of the costs not recovered.

The FSF feels that the issue of fees has been confused due to the lack of resolution of the MTF/Sportzone case and by the stance taken by the Commerce Commission in that case. In the Sportzone case the Commission argued that only variable costs could be connected to a specific transaction, whereas its own guidelines suggest that certain fixed costs and overheads, that are connected, can be recovered through fees. It is highly desirable for this to be resolved before any further guidance or requirement with regard to fees is produced. The whole industry is waiting to know what is allowable and what is not as the case referred to above has shown it is not possible to rely on the draft guidelines provided by the Commerce Commission.

In the FSF’s view in determining the cost of providing finance it is important not to distinguish between direct and indirect costs (which the draft guidelines referred to above did not). The FSF believes that if the lender can clearly demonstrate the amount that it spends on work stations and rental etc for establishing loans, then it is reasonable to recover those costs as part of the establishment fee.

In the FSF’s view, the issue of fees should therefore not be addressed in the Code until the issues arising from the Sportzone case are resolved.

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

Based on the CCCFA and the Commerce Commission guidelines, the principles that should apply to recovery of cost through fees are:

- there should be no profit earned on costs recovered through fees
- only costs that are connected with the product, transaction, service or activity may be recovered through fees i.e. any cost *not* connected with a specific product, transaction, service or activity may not be recovered by cross subsidisation
- costs include fixed, variable, direct and indirect
- allocation of fixed and indirect cost must be by some recognised and identifiable method of allocation
- fee setting must be verifiable without a costly forensic process
- third party costs may recovered in full, and without mark-up

Guidance on fee setting must be more accurate, in plain English and be easily understood by lenders and borrowers, without costly litigation or forensic examination. It is also responsible lending practice to provide disclosure so the customer knows what they're paying.

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

The FSF believes the lender should be able to recover all costs connected with the establishment of the class of transaction. The purpose of the Act and any regulations should be to preclude the recovery of costs not connected to the class of transaction e.g., direct cost related to a home loan should not be recovered from an unrelated personal loan fee. Indirect cost should be allocated using an appropriate allocation methodology.

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

As above, credit fees generally should be able to recover whatever it costs to provide the service in respect of which the fee is being charged.

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

As above, default fees should be able to recover all costs associated with 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?

The reference to "reasonable standards of commercial practice" in section 44 of the CCCFA does not sit well with the fact that the rest of the CCCFA's fee regime focuses on the costs of the particular lender charging them, as opposed to "commercial practice" generally. Consistent with that the FSF also does not think that any particular "standards of commercial practice" need to be referred to in the Code.

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

A prudent business will review costs and fees on a regular basis to ensure that costs are recovered and fees are not unreasonable.

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

Please refer to the answer provided for question 35. The FSF believes the rate of commission is largely irrelevant – what is important is whether or not the price paid for the insurance cover is reasonable, that the product will provide appropriate cover should an adverse event occur in the life of the borrower and that the borrower is made aware of the terms and conditions of the product via appropriate disclosure.

The FSF submits that the cost of the premium must be disclosed and therefore the amount of any commission paid is not relevant. Commission on other insurance products is not prohibited or regulated and nor should it be with regard to credit related insurance.

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

First, please refer to the comments about fees at 47 above. The Commerce Commission and the industry need to work together to develop guidelines that are definitive, accurately allow lenders to structure fees to reflect their costs and the guidelines need to be followed by the industry and the Commerce Commission.. The guidelines should be a safe harbour and they should be updated as required. Guidelines must be capable of interpretation without litigation.

Any guidelines should be set through consultation with the industry so that Commerce Commission actually understands the industry. The industry is demanding certainty with regard to the setting of fees. The MTF/Sportzone case has shown that lenders cannot rely on the draft guidelines produced by the Commission.

The FSF strongly submits that the guidelines need to be finalised to provide the certainty the industry is seeking.

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

The FSF submits that nothing further should be included in the Code in relations to fees.

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?

Responsible lenders have customer relationship or collections teams or similar who monitor loan behaviour to identify borrowers who might be under stress. Any arrears situation where the borrower is late in making a repayment would be a cause for concern and the lender would make a call as to whether this would require a phone call to follow up or remind the borrower of the need to make provision for a repayment or whether it is a sign of some deeper problem. Either way the lender will initiate communication with the borrower with the ultimate aim of getting the loan back on track. Repeated late repayments or arrears would be a cause for lender concern and would trigger a communications process to ensure the loan is brought back into order.

It is also the responsibility of the borrower to contact the lender if they are struggling. This obligation is written into (and disclosed) the credit contract.

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? (e.g. in relation to assistance to be provided to the borrower.)

The FSF refers to the first misconception about lending referred to in the introduction to this submission. Responsible lenders do not lend if they do not reasonably believe they will be repaid. Responsible lenders will work to ensure repayment for the mutual benefit of both the borrower and the lender. Repayment of loans is how responsible lenders remain in business and continue to lend to borrowers on an ongoing basis. Please also refer to the answer provided to question 57 above with regard to monitoring and collections teams.

The FSF believes that New Zealand must be careful not to replicate the Australian experience here where the lender has to offer hardship if the borrower advises they are having difficulty in repaying regardless of whether that difficulty has arisen from genuine circumstances like loss of employment or illness or whether it has arisen because the borrower has taken on extra debt since taking out the original loan.

In Australia, if hardship is refused by the lender in these circumstances, the borrower can then go to the lender's Disputes Resolution Scheme to complain and the lender cannot then enforce the loan contract. Lenders' arrears have increased as a result of this causing greater provisioning for bad and doubtful debt to be required on their balance sheets and ultimately causing the cost of credit to responsible borrowers to be increased to cover the extra costs associated.

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

Responsible lenders will provide borrowers with information on their rights through the disclosure process. Lenders are required under the Financial Services Providers (Registration and Disputes Resolution) Act 2008 to advise what their internal complaints process involves and which disputes resolution scheme they belong to.

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? (e.g. in relation to staff training and policies and enforcement of those policies.)

Responsible lenders have many communications with borrowers in relation to breaches before taking enforcement action including phone calls, letters and emails to encourage communication from the borrower. It is always the lender's aim to resolve the breaches and get the loan back on track before it gets to the point of enforcement.

It is also the borrower's responsibility to communicate with the lender. It is up to them to let the lender know as soon as possible if their circumstances change and the loan is at risk of default. This is consistent with Principle 7 of the Lending Responsibility Principles.

It is also the borrower's responsibility to respond to communications from the lender appropriately and to advise the lender of change of contact details.

It is also good business practice to treat borrowers reasonably and in an ethical manner. Lenders are customer-facing organisations so it is not in their interests for borrowers to have a poor customer experience.

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)?

A responsible lender has a process similar to that of the origination process. The borrower's ability to service and repay the debt on an ongoing basis will be the first criterion to consider. Responsible lenders use their judgement to determine the information required to provide the best outcome for both parties.

Since every situation is different, it is not possible to codify the appropriate process.

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

The Disputes Resolution Schemes have provided their members with advice on best practice internal complaints processes. There are requirements that already exist for lenders to have a transparent process, to keep a record of complaints, to advise borrowers of their rights, to provide timely responses to complaints to inform borrowers of the ability for the matter to be escalated to an external Disputes Resolution Scheme. Matters are escalated to Disputes Resolution when agreement cannot be achieved.

A responsible lender will seek to resolve a complaint to the satisfaction of both parties, without having to declare a dispute. Generally, complaints escalate when one or other party does not wish to resolve through an amicable process or where frontline staff do not have the authority to resolve at first interaction.

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

The FSF would submit that nothing further needs to be addressed by the Code in relation to borrowers facing difficulties or other problems. Responsible lenders want to work with borrowers and encourage 2-way communication. The FSF believes that it is impossible to set a template as to how to deal with borrowers facing repayment difficulties or other problems because individual circumstances apply and each case is different. The Code shouldn't be being prescriptive about processes – outcomes are more important with the key outcome being sought for the benefit of both borrower and lender being that the loan is repaid.

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?

The FSF believes that it depends on the scale of the default as to what enforcement response they might take. Responsible lenders will use their judgement as to what is the most appropriate action to take to ensure a resolution to the default that achieves the best outcome for both the borrower and the lender – which is ultimately to ensure that the loan is repaid.

The FSF believes this shouldn't be prescribed – it's about the outcome. The responses used by responsible lenders range from phone calls, letters or emails to initiate and continue communication with the borrower through to referral to a debt collection agency through to repossession. The appropriate repossession process is described in the Act.

65. What policies or procedures do/should responsible lenders go through before taking enforcement action? For example, before sending debts to a collection agency?

Please see the answer to question 64 above.

The FSF believes it must be understood that repossession is only ever the very last resort. Repossessions cost lenders money – they invariably do not recover the costs associated with it and/or the full amount of the debt. All responsible lenders would far rather work with the borrower to get the loan repaid than go down the path of repossession.

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

The FSF has a Memorandum of Understanding with the NZ Federation of Family Budgeting Services and members proactively refer borrowers for advice when they identify signs of stress. Ultimately, as already stated, the lender is trying to achieve the repayment of the loan to achieve the best outcome for the borrower and themselves..

There are a great many attempts made to communicate with the borrower before it gets to enforcement action – see the answer provided to question 64.

It should also be remembered that there is disclosure at the beginning of the loan contract so that the borrower knows that enforcement action could occur if they don't meet their obligations. Responsible lenders will ensure this is made clear at the outset.

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.)

This is covered in the Act.

Costs increase significantly during recovery action which is why it is the last resort of responsible lenders. Costs need to be recovered from the borrower – otherwise all borrowers will bear the cost but fees can only be charged on a cost recovery basis. The FSF would also point out that repossession is not a profit-making opportunity (please refer to the second lending misconception in the Introduction to this submission).

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)?

Responsible lenders want to recover the debt. It's not in their interests to treat borrowers or their property in any other way. Repossession agents now have to be licensed and responsible lenders will only deal with licensed agents that treat borrowers and their property reasonably.

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

The FSF believes nothing further needs to be included in the Code in relation to enforcement action as responsible behaviour is already defined in the Act.

However the Discussion Document references the Fair Debt Collection Practices Act in the United States under paragraph 178 which prohibits certain behaviours. Some of these are self-evident and the FSF submits that responsible lenders will already avoid such behaviour. Some however would seem to the FSF to be responsible behaviour in certain circumstances and should not be prohibited as to do so may preclude lenders from acting responsibly and ensuring the best outcome for both borrower and lender.

These include that responsible lenders should not be precluded from contacting a customer outside the hours of 8 am – 9 pm particularly where a borrower is only available outside of those hours e.g. due to work commitments etc. Also that a lender should cease communication upon request – communication is the key to ensuring a mutually satisfactory outcome to the loan (i.e. that it is fully repaid). Any prohibition on communicating with a borrower is potentially counter-productive.

Finally the FSF would disagree that publishing a consumer’s name or address on a “bad debt” list should be prohibited. Responsible lenders have internal systems that identify that a borrower has become a “bad debt” risk and should be allowed to continue to do so in order to be able to make a fully informed decision with regard to future lending. It also follows that other lenders should have access to a borrower’s previous bad credit history through a credit check so that the lender can make informed lending decisions.

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

The release of security when the loan is repaid is required by law already. Responsible lenders will send a final communication to a borrower who has repaid their loan thanking them for their business and possibly reminding them to cancel automatic payments for loan repayments etc as a means to continue their relationship with a responsible borrower.

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?

The FSF submits that this is already covered by new section 83E of the CCCFA and that the nature of the “at risk” concept is such that it is neither necessary nor desirable to try to be more prescriptive about it.

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?

The long process undertaken by responsible lenders before exercising the very last resort remedy of repossession has been described in answer to question 64.

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

The FSF believes that it should be up to the lender to determine when to repossess. If there was a minimum value this could result in borrowers losing motivation to pay on the basis that they would be aware they would still retain possession. It is already covered in the Act in terms of what cannot be taken as security.

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

A responsible lender will have communicated with the borrower before it gets to the point where repossession is a likely outcome so voluntary return would be received willingly and it is a means to avoid further cost to the borrower and the lender.

A Notice of Intent to Dispose of an Asset can sometimes trigger a borrower to voluntarily return goods.

The Code should allow for the borrower to liquidate the asset by private rather than forced sale if the lender agrees to this as the proceeds from the sale are often higher and/or associated costs are lower when an asset is sold voluntarily. This potentially provides a better outcome for both the borrower and the lender.

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)?

Please refer to answers to questions 59 and 62. The FSF believes that the legislation in place is adequate and nothing further is required.

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

This is described in the Act and nothing further is required.

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?

FSF members already deal with responsible repossession agents. Under the Act, such agents will now have to be licensed and therefore lenders will be dealing with licensed agents who will only be able to charge a reasonable amount as their charges are also subject to consumer law and to pass on the actual costs involved in the repossession.

Because there is cost involved in taking repossession action which is frequently not recovered, it needs to be stressed that repossession is the last resort of a responsible lender.

The FSF submits that it is difficult to relate the cost of repossession to the size of the default as it depends on factors such as whether the borrower is trying to conceal the asset and therefore it is more costly to determine where it is located or indeed how difficult the borrower is to locate.

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

Please refer to the answer provided for question 77 above. Agents have to be licensed and the Act describes ethical behaviour. If the agent does not behave ethically they will be in breach of the Act and could lose their license and therefore be unable to continue in business. FSF members insist on ethical behaviour from the agents with whom they deal already and upholding this behaviour is included in the supply agreement with the agent.

The borrower also has the option of using the lender's complaints process if they don't believe they have been treated ethically by a repossession agent including escalation of their complaint to the relevant Disputes Resolution Scheme.

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

Section 256 of the Credit (Repossession) Act (in future, new section 83Z of the CCCFA) already covers this by saying that the best possible price should be obtained. If goods are sold at auction they are now covered by the Consumer Guarantees Act which means that the lender is liable if the goods are faulty. Any costs associated with ensuring they are not cannot be passed on to the original borrower because the lender is the seller.

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

The FSF does not believe the Code needs to address any other matters in relation to repossession.

The FSF trusts that the above is helpful. If we can be of any further help, contact can be made via (04) 472 1731.



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APPENDIX A

Membership List as at 1 August 2014

Debt Issuers - (NBDT) Non-Bank Deposit Takers	Vehicle Lenders	Finance Company Diversified Lenders	Credit Reporting	Insurance	Affiliate Members
<p><u>Rated</u></p> <ul style="list-style-type: none"> • Asset Finance (B) • Avanti Finance (BB) • Fisher & Paykel Finance (BB+) • Medical Securities (A-) <p><u>Non-Rated</u></p> <ul style="list-style-type: none"> • Mutual Credit Finance • Prometheus Finance 	<ul style="list-style-type: none"> • BMW Financial Services • Branded Financial Services • Community Financial Services Limited • European Financial Services • Fleet Partners NZ Ltd • Mercedes-Benz Financial Services • Motor Trade Finances • Nissan Financial Services NZ Pty Ltd • ORIX NZ • SG Fleet • Toyota Finance NZ • Yamaha Motor Finance 	<ul style="list-style-type: none"> • Advaro Ltd • Centracorp Finance 2000 • Dorchester Finance • Finance Now • Future Finance • GE Capital • Home Direct • Instant Finance • John Deere Financial • Oxford Finance Ltd • DTR Thorn Rentals • South Pacific Loans 	<ul style="list-style-type: none"> • VEDA Advantage <p><u>Debt Collection Agency</u></p> <ul style="list-style-type: none"> • Baycorp (NZ) 	<ul style="list-style-type: none"> • Autosure • Protecta Insurance • Provident Insurance Corporation Ltd <p><u>Associate Members</u></p> <ul style="list-style-type: none"> • Southsure Assurance 	<ul style="list-style-type: none"> • American Express International (NZ) Ltd • Buddle Findlay • Chapman Tripp • Deloitte • Ernst & Young • Finzsoft • KPMG • PriceWaterhouseCoopers • SimpsonWestern