MINISTRY OF BUSINESS, INNOVATION & EMPLOYMENT
HĪKINA WHAKATUTUKI

COVERSHEET

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

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

Information redacted **YES**

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

Some information has been withheld as confidential advice to Government.

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Regulatory Impact Statement: response to the investigation into 1 December 2021 credit law changes

Coversheet

Purpose of Document	
Decision sought:	The Minister proposes to amend credit affordability regulations relating to estimation of borrower expenses and treatment of refinancing.
Advising agencies:	Ministry of Business, Innovation and Employment
Proposing Ministers:	Minister of Commerce and Consumer Affairs
Date finalised:	15 June

Problem Definition

Changes made to the Credit Contracts and Consumer Finance Act 2003 (**CCCFA**) and associated regulations on 1 December 2021 (**CCCFA changes**) are having the following unintended impacts:

- More borrowers across all lending types, who should pass the affordability test, are subject to declines or reductions in credit amount.
- Borrowers are subject to unnecessary or disproportionate inquiries that are perceived by them as intrusive.

Executive Summary

On 29 April 2021, MBIE, in collaboration with the Council of Financial Regulators (CoFR) completed an investigation into the CCCFA changes (**the investigation**). The CCCFA changes were part of a wider reform to the CCCFA, and included amendments to requirements for affordability and suitability assessments and the associated liability regime. The CCCFA changes were intended to address concerns about continued irresponsible lending that was harming some borrowers.

The investigation found that the CCCFA changes are having some unintended impacts:

- More borrowers across all lending types who should pass the affordability test are subject to declines or reductions in credit amount.
- Borrowers are subject to unnecessary or disproportionate inquiries that are perceived by them as intrusive.

These unintended impacts are the result of the following:

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

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- The prescriptive nature of the CCCFA changes and their application to almost all consumer lending also means that lending has been impacted outside of high-risk consumer lending.

Cabinet has also already agreed to clarify a number of aspects of the CCCFA regulations through amendments to the regulations and guidance in the Responsible Lending Code [CAB-22-MIN-0012].

The investigation identified a range of further changes to the CCCFA and regulations that have been considered to address the unintended impacts of the CCCFA changes. These are based on the underlying drivers of the unintended impacts summarised above, and are in broad terms:

- Option 1: counterfactual – initial changes agreed by Cabinet in February only
- Option 2: amend the affordability regulations to better target specific kinds of lending, lenders, or certain consumers where there is a higher underlying risk of substantial hardship
- Option 3: changes to the design of specific affordability regulations relating to borrower expenses, borrower surplus requirements and exceptions
- Option 4: changes to the penalties and liability regime
- Option 5: repealing the affordability regulations.

The accompanying Cabinet paper proposes Option 3, in response to the investigation, and rules out further work on Options 2, 4 and 5.

This RIS provides an analysis of the impact of the above options. We conclude that further policy work should be directed towards Option 2 and 3, on the basis that options based on these approaches are most likely to achieve the objectives of the CCCFA changes, while addressing the unintended impacts of the CCCFA changes. While there has been extensive consultation on the impacts of the CCCFA changes, a lack of stakeholder consultation on detailed policy changes makes it difficult to make firmer recommendations about the changes that should be made.

Stakeholders have expressed a range of views on the problem and potential solutions during the investigation. Lenders generally consider that further change is necessary to address unintended impacts of the CCCFA changes, and have proposed a range of options, encompassing all of the above approaches. Consumer advocates such as financial mentors have generally not supported further change, on the basis that it would weaken consumer protections.

Limitations and Constraints on Analysis

This RIS is based on primarily the evidence obtained by the investigation, and the investigation’s findings. The investigation was focussed on identifying intended and unintended impacts of the CCCFA changes, and the range of options that could be considered to address any unintended impacts. As part of the investigation, MBIE conducted a series of semi-structured interviews with 32 stakeholder organisations. These included lenders (bank and non-bank lenders), mortgage brokers, associated industry organisations, and consumer advocates such as financial mentors. MBIE also spoke with credit reporting agencies and financial dispute resolution schemes. For lenders, the interviews included questions about their implementation process, impacts on customers, impacts on loan approval timeframes and rates, specific changes to loan approval processes as well as other concurrent factors. Following the interviews, MBIE asked

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stakeholders to provide more detailed information on the above in writing, including any specific proposals for changes to legislation and guidance. Data on lending was also gathered from the Reserve Bank, credit reporting agencies and individual lenders.

While most of the options considered in this RIS were put forward by various lenders and their representatives in the course of the investigation, as noted above, there has been limited consultation carried out on specific options and approaches. Consideration of the likely impacts of some of the options is informed to some extent by earlier policy work and consultation undertaken during the development of the CCCFA changes themselves, and by informal conversations with lenders and consumer advocates. The views of stakeholders on options, at a high level, are well known.

For these reasons, the RIS provides a high-level analysis of the options, but suggests that further work and consultation is needed to inform the appropriate package of options. If Cabinet proceeds with Option 3, more detailed work will be undertaken during drafting and subsequently through release of a public exposure draft. We expect lenders to support this option, based on proposals they put forward during the investigation. This means that recommendations in the Cabinet paper should be pitched at a high level and may need to be revisited in light of feedback from stakeholders.

Quality Assurance (completed by QA panel)	
Reviewing Agency:	MBIE
Panel Assessment & Comment:	MBIE's Regulatory Impact Analysis Review Panel has reviewed the attached Impact Statement prepared by MBIE. The panel considers that the information and analysis summarised in the Impact Statement is sufficient to meet the criteria necessary for Ministers to make informed decisions on the proposals in this paper.

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Section 1: Diagnosing the policy problem

What is the context behind the policy problem and how is the status quo expected to develop?

1. On 14 January 2022, the Minister of Commerce and Consumer Affairs asked the Ministry of Business, Innovation and Employment (**MBIE**), in collaboration with Council of Financial Regulators (**CoFR**), to conduct an investigation into the impacts of the parts of the Credit Contracts Legislation Amendment Act 2019 and Credit Contracts and Consumer Finance (Lender Inquiries into Suitability and Affordability) Amendment Regulations 2020 that came into force on 1 December 2021 (**CCCFA changes**).
2. This section summarises information from the resulting report, *Early implementation and impacts of 1 December 2021 credit law changes* (**the investigation report**) about the CCCFA changes, their unintended impacts, and the underlying drivers of those unintended impacts. More detail can be found in the investigation report.
3. The CCCFA changes were part of a wider reform to the Credit Contracts and Consumer Finance Act 2003 (**CCCFA**), and included amendments to requirements for affordability and suitability assessments and the associated liability regime. Some parts of the reforms came into force earlier (from December 2019), while the 1 December CCCFA changes were the final tranche of obligations. The CCCFA changes were intended to address concerns about continued irresponsible lending that was harming some borrowers. The CCCFA changes were intended to result in all consumer lenders implementing credit assessment processes that conformed to the lender responsibility principles around affordability and suitability, including performing 'minimum steps' prescribed in regulations.
4. The original 2018 RIS, *Consumer credit regulation review*, sets out what was known about the issues with the previous law and analyses a range of options, some of which eventually became the CCCFA changes.[1] In particular, the RIS notes that, while there was some uncertainty about prevalence, consumer stakeholders had identified "continued irresponsible lending practices across all types of lenders… particularly concentrated across finance companies and high-cost lenders and among vulnerable consumers". This included some lenders performing only superficial testing of loan affordability, accepting income and expense information provided from borrowers without proper verification and approving subsequent loans without carrying out affordability checks again. These practices were considered to cause harm to some borrowers, by resulting in them taking on unaffordable debt that then caused financial hardship and associated social and mental health issues.
5. Throughout this RIS, we make reference to the problem definition and conclusions of the original RIS. These remain relevant to considerations of further changes, as the CCCFA changes have only been in effect for a short time, and the conclusions of the original RIS have not so far been disconfirmed by evidence or otherwise significantly revised.[2] Any further changes to the law therefore need to also take into account the problems identified by the original RIS and its analysis of options.
6. The CCCFA changes of relevance to this current RIS are summarised in Table 1 below.

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[1] https://www.mbie.govt.nz/assets/c09d5636b6/coversheet-consumer-credit-regulation-review.pdf

[2] However, see section 3 of this RIS, where we set out how both the CCCFA changes and any further changes will be monitored and evaluated.

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TABLE 1: 1 DECEMBER 2021 CHANGES TO CREDIT LAWS

Change	*Description of law before 1 December 2021*	*Description of law after 1 December 2021*
Prescriptive affordability and suitability assessment requirements	Lender responsibilities were principle-based, supported by non-binding guidance in the Responsible Lending Code.	Regulations set new minimum requirements for affordability and suitability assessments (new regulations 4AA-4AO).
Affordability and suitability inquiries for further lending	No express obligation to carry out an affordability or suitability assessments for loan top-ups and credit limit increases (unless a new contract was entered into), but the Code recommended taking some steps to ensure that additional lending was affordable.	Affordability and suitability assessments required for top-ups and credit limit increases (amended section 9C(3)(a) and new section 9C(8)).
Record keeping of affordability and suitability assessments	No record-keeping requirements.	New requirements to keep records of affordability and suitability assessments (new section 9CA).
Directors and senior managers duties	No duties on directors and senior managers, except for potential liability for offences and compensation orders where individuals have intentionally contributed to a breach of the CCCFA.	Directors and senior managers of lenders must exercise due diligence to ensure that the lender complies with its duties and obligations under this Act. This includes taking reasonable steps to ensure that the creditor has appropriate procedures for complying with the CCCFA, identifying deficiencies in CCCFA compliance, and remedying any deficiencies discovered (new section 59B).

7. Of particular significance are the prescriptive affordability assessment requirements introduced into the Credit Contracts and Consumer Finance Regulations 2004 (**the Regulations**), as noted in the first row of Table 1.

8. Prior to the CCCFA changes, lenders were required to comply with lender responsibilities in the Act. These include that a lender must make reasonable inquiries, before entering into a consumer credit contract, so as to be satisfied that it is likely that the borrower will make the payments under the agreement without suffering substantial hardship. This is often referred to as a requirement for the lender to conduct an **affordability assessment**.

9. Amendments to the Regulations now require that, as part of that affordability assessment, lenders must estimate the borrower's likely income and expenses (regulation 4AF(2)(a)). The lender must show that the borrower's income exceeds their expenses (including payments under the new loan) and make an allowance for error (e.g. overestimation of income or underestimation of expenses) (regulation 4AF(2)(b)).

10. An income and expenses assessment is not required if:

    - initial inquiries show that it is obvious that the borrower will be able to make payments under the agreement (regulation 4AG)
    - the borrower will not rely on income to make the payments and the lender is satisfied that payments will not cause substantial hardship (e.g. the borrower will pay off the loan using the sale of an asset) (regulation 4AF(1)(b) and regulation 4AI), or
    - the loan does not advance any significant new credit (e.g. it is a restructuring of existing obligations to respond to a hardship application from the borrower) (regulation 4AH).

11. The borrower's likely income and expenses are estimated by collecting information from the borrower (or records that the lender holds about the borrower) and then conducting further checks or adjustments on that information to help ensure that the information is complete, and the estimates are robust.

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12. To estimate income, lenders can use recent and reliable records that they have on file, which they can confirm with the borrower, or ask the borrower about their income and verify based on evidence (such as pay slips) (regulation 4AJ).

13. For expenses, lenders can ask the borrower, use their existing records, or determine the borrower's expenses from bank transaction records (regulation 4AK(2)(a)). Lenders will need to make further inquiries into the borrower's financial commitments by obtaining a credit report, or (if the borrower is an existing customer) asking the borrower about commitments they've taken on since they last received credit (regulation 4AK(2)(c) and (3)). If estimated expenses are based on asking the borrower, or there is a risk that expenses have been missed or underestimated, lenders have a choice about whether they verify expenses (e.g. through bank account transactions, or a copy of a contract) or use a statistical benchmark (regulation 4AM).

14. Income is required to exceed expenses (regulation 4AF(2)(b)), and there must be one or both of the following:

- a reasonable surplus on top of likely expenses, to allow for potential overestimation of income or underestimation of expenses, and/or
- adjustments and buffers to income and expenses, to allow for potential overestimation of income or underestimation of expenses.

Lending activity has dropped since 1 December 2021

15. Since the CCCFA changes came into force on 1 December 2021, there have been reported drops in lending activity across a range of consumer credit products, including home loans, personal loans, credit cards and vehicle lending.[3]

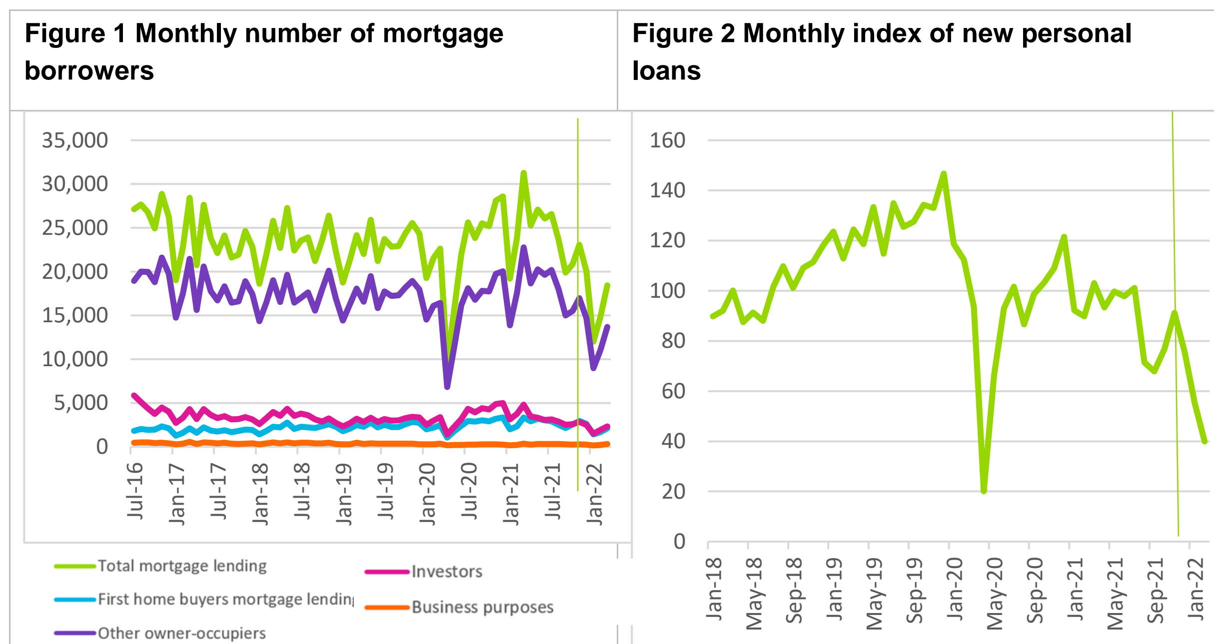

Figure 1 Monthly number of mortgage borrowers

Figure 2 Monthly index of new personal loans

[3] Section 4.1 of the investigation report.

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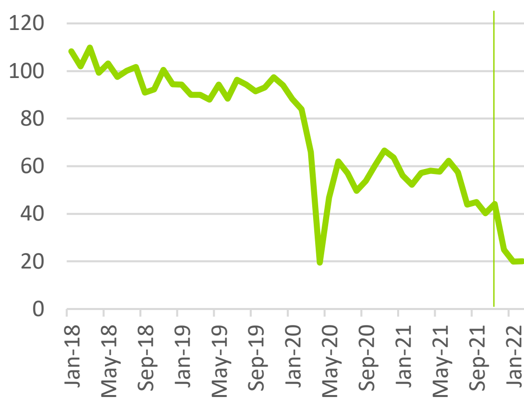
Figure 3 Monthly index of new credit card accounts	Figure 4 Monthly index of new vehicle loans



Source: Reserve Bank of New Zealand, C31: New residential mortgage lending by borrower type, https://www.rbnz.govt.nz/statistics/c31

The CCCFA changes are contributing to drops in lending activity

16. The investigation report found that the CCCFA changes are one of several factors that have had an impact on home lending, alongside LVR changes, increased interest rates, inflation and a general property market slowdown. For other consumer lending, which tends to be higher risk, there may be some impact from other factors (such as cost of living increases) but the relative impact of CCCFA changes on lending activity is higher.[4]
17. While declines in lending volumes seem to largely be driven by reduced number applications, data shared by credit reporting agencies also indicates that conversion rates have fallen for borrowers across all lending products, indicating that more applications are being withdrawn or declined. This is consistent with data supplied by individual lenders.
18. This evidence is strengthened by both:
    - case studies provided by lenders showing how processes implemented in response to the CCCFA changes have led to credit being declined – either through greatly increased expense estimates, large surplus requirements or a lack of discretion to consider wider factors
    - information we have gathered about features of the Regulations, including the way they have been interpreted and applied, that we expect to have driven increases in declined and withdrawn applications, i.e. providing a plausible mechanism.
19. These drivers are discussed in more detail in the next section on the policy problem.

Borrowers and lenders have reported that lending processes have become more intrusive and time consuming

20. Lenders have said that borrowers are complaining that the new, more in-depth inquiries being conducted as part of the affordability assessment are time consuming and intrusive in nature. This was a common theme amongst lenders interviewed as part of the investigation, and is consistent with media reports of borrower experiences.
21. All lenders indicated their processing time for applications on all products had increased by 50% or more following implementation of process changes in accordance

[4] Section 4.2 of the investigation report.

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with the CCCFA changes. This is driven by the need to capture a wider range of expenses in accordance with the Regulations, and more in-depth inquiries being made into those expenses.

22. The above impacts are supported by evidence from the Banking Ombudsman, who has noted an increase in lending complaints between October (when some lenders began to implement new processes) and December last year compared with the previous quarter. The complaints related to delays, banks not acting as expected, and borrowers having to provide more information.

We expect most of these changes to persist into the future, although lender process improvements will diminish some

23. We expect that most of the effects of the CCCFA changes will be enduring without further regulatory change, though there are likely to be some increase in lending volumes and reductions in declines and withdrawals due to refinement of lender processes and changes to guidance.

24. Following implementation, further adjustments are being made by lenders to lending processes, and increased familiarity with new requirements and consumer awareness appear to be reducing processing times. The introduction of new systems and processes necessitates a learning period, and we expect reduced concerns about processing times in the future.

25. Cabinet has also already agreed to clarify a number of aspects of the Regulations through amendments to the Regulations and guidance in the Responsible Lending Code [CAB-22-MIN-0012]. These will come into force on 7 July and include clarifying various aspects of how lenders can inquire into and estimate expenses, clarifying that borrowers are not always required to have a surplus, and clarifying exceptions in the Regulations from the need to carry out a full affordability assessment. These changes accord with the original policy intent of the CCCFA changes.

What is the policy problem or opportunity?

26. To some extent, more onerous lending processes and reductions in lending volumes are intended and expected outcomes of the CCCFA changes. The CCCFA changes were intended to address non-compliance with requirements for lenders to perform adequate affordability and suitability assessments and the resulting harm to some borrowers from unaffordable debt. The original 2018 RIS identified the following risks or possible impacts:

    - reduced access to credit, where this was previously granted in unaffordable or unsuitable circumstances
    - increased cost of credit, where lenders passed on additional compliance costs to consumers
    - more ‘black market’ lending (although it noted that creditors who were wilfully non-compliant with new requirements were unlikely to have been complying with the previous ones).

27. However, the investigation identified two unintended impacts from the CCCFA changes:

    - More borrowers across all lending types who should pass the affordability test are subject to declines or reductions in credit amount.
    - Borrowers are subject to unnecessary or disproportionate inquiries that are perceived by them as intrusive.

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28. All consumers who enter into consumer credit contracts are *potentially* affected by one or both of these unintended impacts. 42% of people aged 18 and over entered into a credit contract in the two years to November 2020.[5]

29. There are some estimates of the proportion of borrowers actually affected by these issues, although care is required in interpreting these figures. In the case of declines, individual banks have estimated that 6–7% of their home loan borrowers who would have previously qualified are now being turned down.[6] Data from credit reporting agency Centrix showed the 'conversion rate' of home loan 'enquiries' fell from 38.4% in November 2021 to 34.9% in December 2021, suggesting around 9% of borrowers who would have gone on to receive lending in November no longer received a loan in December.[7] This equates to 14,000–21,000 home loan borrowers each year.[8]

30. There are greater uncertainties about declines in other lending, given that this tends to be higher risk, but an upper limit based on Centrix data suggests 14% of previously qualifying personal loan applicants no longer received loans, and 35% of previously qualifying credit card applicants no longer received credit cards.

31. However, it is difficult to determine whether borrowers who were declined were *unnecessarily* declined, or whether there were actually significant affordability risks (and therefore the borrower should have been declined under the responsible lending principles).There is also evidence that for some types of credit contracts, like temporary overdrafts, borrowers have been dissuaded by the more onerous process itself, which is not reflected in declines in conversion rates (since an enquiry would not have been made to the credit reporting agency at all).

32. The investigation report concluded, based on analysis of available data, lender processes maps and case studies, that some portion of the above impacts were unintended consequences of the CCCFA changes, rather than being justified by underlying affordability concerns. The investigation was not able to estimate what portion of the above impacts were 'intended' versus 'unintended'. That some of the impacts were unintended was supported by:

    - Centrix data showed that conversion rates fell significantly for lenders with higher credit scores (>700) but were much less for borrowers with low credit scores (<500) – the opposite of naïve expectations that low credit score (i.e. 'high risk') borrowers should be more affected[9].
    - case studies provided by lenders showed how processes implemented in response to the CCCFA changes have led to affordable credit being declined – either through greatly increased expense estimates, large surplus requirements, or a lack of discretion to consider wider factors.
    - information gathered about features of the Regulations, and the way they have been interpreted and applied, that were expected to have driven increases in

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[5] New Zealand Consumer Survey 2020, p. 28, https://www.mbie.govt.nz/dmsdocument/14642-nz-consumer-survey-2020-report-pdf.

[6] See: https://www.rnz.co.nz/news/business/461196/asb-blames-new-credit-act-for-refusing-some-loan-applications; https://www.stuff.co.nz/business/opinion-analysis/127694806/lending-slowdown-government-stuffup-or-lenders-crying-wolf.

[7] Investigation report, section 4.1.8.

[8] Estimate based on the average number of borrowers taking our home loans regulated under the CCCFA over the past five years prior to December 2021. RBNZ, New residential mortgage lending by borrower type (H31), https://www.rbnz.govt.nz/statistics/c31.

[9] This interpretation assumes that credit scores are a good proxy for loan affordability. It is also possible that it reflects some combination of: a. lenders screening out borrowers with lower credit scores and weaker repayment histories, regardless of loan affordability, or b. some lenders previously highly weighting credit scores and repayment history in credit assessments, in the absence of underlying affordability.

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declined and withdrawn applications, i.e. providing a plausible mechanism. These underlying causes are set out in below.

33. These unintended impacts were the result of the following:

- Lending processes, in practice, have become more restrictive and onerous than was expected when the CCCFA changes were made. This is a consequence of the way a number of specific provisions in the regulations are designed and drafted, combined with interpretational difficulties and many lenders taking a naturally conservative approach to compliance given the CCCFA's strong liability regime.
- The prescriptive nature of the CCCFA changes and their application to almost all consumer lending also means that lending has been impacted outside of areas where there is a high risk of irresponsible lending and consumer harm.

34. These underlying drivers are set out in more detail below.

Underlying driver: lack of targeting

35. A fundamental driver of the unintended impacts is that the Regulations apply to almost all consumer lending with limited exceptions, rather than just lending where there is a significant risk of harm. While the Regulations were intended to apply to all consumer lending, they were not expected to significantly impact many low-risk situations, on the basis that lenders already implemented similar processes to those required. For example, banks providing mortgage lending to first home buyers were generally thought to have robust processes for assessing affordability, and much of the design of the Regulations was based on these processes. This issue is resulting in unnecessary or disproportionate inquiries to low-risk borrowers (who arguably should not require a full affordability assessment to establish loan affordability) and has some implications for borrowers being unnecessarily declined.

36. The impact of this driver is strongly connected to lenders' uncertainty around use of the exception for 'obvious' affordability, which is the main exception to a full affordability assessment for low-risk borrowers. Where borrowers fall outside this exception, or it is not otherwise used, the prescriptive nature of the regulations means borrowers are subject to the same extent of inquiries as higher risk borrowers. Low risk borrowers are more likely to find this intrusive, as they are unlikely to have been subject to the same level of inquiries prior to the CCCFA changes.

Underlying driver: design and drafting of specific provisions in the Regulations

37. A number of specific provisions of the CCCFA changes may be contributing to the unintended impacts:

- Regulation 4AF(2)(a) requires lenders to estimate likely relevant expenses, which goes beyond the minimum needs of the borrower to include expenses that the borrower intends to make or continue after entering into the contract. This means that some discretionary expenses are included in the lenders' estimates of the borrower's expenses, which result in additional inquiries, while also inflating expense estimates making it more likely that borrowing is declined. For example, a lender estimating a borrower's food expenditure may note regular dining out on the borrower's bank statements. The lender may then ask the borrower about their likely approach to dining out after the loan is taken out – which some borrowers find intrusive. Alternatively, if the lender uses this bank statement information in its expense estimates without inquiring further with the borrower, the lender's resulting estimate of likely food expenses may be much higher than the borrower will truly continue to spend after taking on the loan.
- Similarly, the definition of 'listed outgoings' (regulation 4AE) includes 'other regular or frequently recurring' outgoings that are material and that the borrower is 'unable or unwilling to cease', which creates situations in which there is a

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mismatch between what borrowers say they intend to continue paying (on the basis of their own beliefs about affordability) compared to what they would actually continue with if at serious risk of substantial hardship. For example, a borrower may say that they intend continue their Netflix subscription (and therefore this expense forms part of the assessment) although they would be prepared to give it up if they faced hardship.

- Regulation 4AF(2) sets a formula for most affordability assessments. 4AF(2)(b) requires likely income must be greater than likely expenses, including appropriate surpluses or buffers/adjustments to account for uncertainty, which takes away the ability for lenders to approve lending based on other factors that might suggest affordability.
- Regulation 4AL(2) sets out a prescriptive and conservative approach for lenders to estimate the expenses that may arise from revolving credit contracts such as credit cards and buy-now pay-later schemes. Lenders are required to assume that the revolving credit contract is fully utilised up to the credit limit, and then fully repaid over a reasonable period. This does not take into account borrowers who use these facilities for day-to-day transactions and pay them off each month, rather than making large purchases to be paid back over months or years.

Underlying driver: interpretational issues

38. As well as the design and drafting of specific provisions in the regulations, it has become apparent that the interpretation and implementation of the Regulations has sometimes been more onerous and restrictive than the original policy intent:
    - In implementing regulation 4AK(2), some lenders appear to be estimating living expenses by asking the borrower to declare them, reconciling them from bank transactions records and comparing them against a benchmark. The policy intention was that, where a borrower declared living expenses, they could either be verified against bank transaction records or compared against a benchmark (where both of these were options).
    - Some lenders, in accordance with regulation 4AK(2), use recent bank transaction records to estimate likely expenses (with or without also asking the borrower to declare expenses), but are concerned that they are not able to adjust those expenses down appropriately (e.g., by asking the borrower whether they will forgo discretionary expenses and discretionary components of expenses) to reflect that borrowers are likely to cut back expenses.
    - Some lenders have set surplus income requirements (under Regulation 4AF(2)(b)(i)) in a way that does not appear to be ‘discounted’ for other adjustments and buffers used in income and expense estimates.
    - Although some lenders are using the ‘obvious’ exception (under Regulation 4AG) in certain cases, lenders have generally found it difficult to make systematic use of the exception based on current guidance.
39. These interpretational issues are intended to be addressed by the initial changes to the Regulations and Responsible Lending Code agreed by Cabinet.

Underlying driver: conservative lender approach given CCCFA liability regime

40. While the above interpretational issues reflect gaps in guidance and expected differences between potential interpretations, a key driver of more conservative interpretations of the CCCFA is its relatively strong liability and penalties regime, and particularly its imposition of duties on directors and senior managers.
41. The regulations typically provide multiple pathways for lenders to comply and, whilst overall prescriptive, include many provisions that involve judgements about what is ‘reasonable’ in the circumstances. Regulations 4AE through to 4AO (the substantive regulations covering affordability) include the words ‘reasonable’ or ‘reasonably’ 20

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times. Lenders are also invited to consider what income and expenses are ‘likely’, and to ‘take account’ of various information to inform their assessment of affordability. All these terms, and many more, require use of judgement in the design of processes to ensure that compliance is achieved.

42. Where there are multiple interpretations of a given regulation, the liability regime means that lenders have tended to take the interpretation that yields a more conservative and easily defendable result. A more conservative approach typically results in lower income estimates, higher expense estimates, more extensive surpluses, buffers and adjustments and therefore a greater likelihood that lending will be declined. It also results in more detailed inquiries than may be strictly necessary, and an aforementioned reluctance to make use of more subjective exceptions to a full affordability assessment, such as 4AG’s test of ‘obvious’ affordability.

What objectives are sought in relation to the policy problem?

43. The objectives sought in relation to the unintended impacts of the CCCFA are:
    - providing consumers with access to affordable credit
    - reducing unnecessary inquiries by lenders
    - continuing to provide consumer protections that address the problems identified by the 2018 review of consumer credit laws.

44. The problems identified by the review of consumer credit laws are described in MBIE’s 2018 RIS, *Consumer credit regulation review*, and summarised in paragraph 4 above.[10]

[10] https://www.mbie.govt.nz/assets/c09d5636b6/coversheet-consumer-credit-regulation-review.pdf

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Section 2: Deciding upon an option to address the policy problem

What criteria will be used to compare options to the status quo?

45. The criteria used to compare options to the status quo are as follows:
    - **effectiveness – access to credit**: the extent to which the option achieves the objective set out in section 1 relating to providing consumers with access to credit
    - **effectiveness – reducing unnecessary inquiries**: the extent to which the option achieves the objective set out in section 1 relating to reducing unnecessary inquiries by lenders
    - **effectiveness – consumer protection (triple weighted)**: the extent to which the option achieves the objective of protecting consumers from harms identified by the 2018 review of consumer credit laws
    - **compliance costs**: the extent to which the option minimises compliance costs on lenders.
46. These criteria have been selected on the basis that options that score highest against them are most likely to produce the highest net benefits.
47. There is some overlap between 'effectiveness – access to credit' and 'compliance costs' (because fewer inquiries will generally mean lower compliance costs). However, some options improve access to credit without significantly reducing compliance costs, which makes it useful to treat these as separate criteria.
48. We have triple weighted the third criterion around consumer protection. This addresses the bias that otherwise arises from having the other three criteria favouring options that would deregulate credit. It also reflects the conclusion of the original RIS that the CCCFA changes are likely to have significant net benefits overall, whereas the options being considered in this RIS to improve access to credit are more modest improvements. Options that would erode protections for vulnerable consumers are assumed to come with significant social and financial costs.
49. This means that the overall weighting of each criterion (out of 100%) is: effectiveness – access to credit (17%); effectiveness – reducing unnecessary inquiries (17%); effectiveness – consumer protection (50%); effectiveness – compliance costs (17%).

What scope will options be considered within?

50. This RIS considers that range of options that the investigation report raises as potential areas for further change. These largely comprise changes to the regulations, or relatively small changes to the CCCFA.
51. Non-regulatory options such as providing more guidance are already being implemented through the initial changes agreed by Cabinet in February. These changes therefore form part of the counterfactual against which we consider further changes.
52. Major changes to the CCCFA (e.g. reversing the changes made by the Credit Contracts Legislation Amendment Act 2019 generally) have largely been ruled out for the time being, based on the problem definition and analysis of options provided by the original RIS. The investigation did not reconsider the problems identified by the original RIS, and we are not aware of any evidence contradicting its broad conclusions. The changes recommended by the original RIS have only been in place for six months, and it is too soon to draw conclusions about their effectiveness. This means that we have largely sought options that address the problems identified with the CCCFA changes while remaining consistent with the analysis in the original RIS about what set of regulatory requirements are likely to have the highest net benefits.

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What options are being considered?

53. Based on the underlying drivers of the unintended impacts summarised above, this RIS considers the following options:
    - Option 1: counterfactual – initial changes agreed by Cabinet in February only
    - Option 2 (MBIE preferred): amend the affordability regulations to better target specific kinds of lending, lenders, or certain consumers where there is a higher underlying risk of substantial hardship
    - Option 3 (Minister preferred, MBIE preferred in addition to Option 2): changes to the design of specific affordability regulations relating to borrower expenses, borrower surplus requirements and exceptions
    - Option 4: changes to the penalties and liability regime
    - Option 5: repealing the affordability regulations.

Option 1: counterfactual – initial changes agreed by Cabinet in February only

54. Under this option, no changes would be made at this stage. Potential changes would be further considered once the initial changes have bedded in, and there has also been an opportunity to observe whether the CCCFA changes are having their intended impacts on irresponsible lending.
55. The timing of a further review could coincide with the statutory review requirement for provisions relating to high-cost consumer credit contracts. Section 45L of the CCCFA requires that the Minister of Commerce and Consumer Affairs must review subpart 6A of Part 2 (Provisions relating to debtors under high-cost consumer credit contracts) by 1 June 2023 – three years after commencement of that section.

Benefits

56. This option would have the benefit of allowing a more considered approach to be taken to further changes once lenders and borrowers have become more fully accustomed to the CCCFA changes. Lenders are likely to continue to refine their processes over time, which may go some way to resolve initial difficulties with interpretation.
57. At the same time, it would fully achieve the objective of protecting consumers from unaffordable lending (to the extent that the CCCFA changes successfully do so), in line with the original RIS.

Costs and risks

58. However, this option would not do any more to address the unintended impacts identified by the final report, and we expect that these will persist in some form.

Stakeholder views

59. We expect this approach would be publicly criticised by lenders, who have stated that further changes to the Regulations are necessary to deal with unintended consequences. It is likely to be supported by some consumer advocates such as financial mentors.

Option 2: amend the affordability regulations to better target specific kinds of lending, lenders, or certain consumers where there is a higher underlying risk of substantial hardship

60. Under this option, the affordability regulations would be amended to target situations where there is believed to be a higher underlying risk of substantial hardship, rather than all consumer credit contracts (with limited exceptions). The regulations would not apply to other lending situations, which would instead be subject to the lender responsibility principle relating to affordability in the Act (section 9C(3)(a)(ii)) only.
61. There are a number of different ways that the regulations could be more narrowly targeted, including one or more of the following:

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- towards certain **kinds of consumer credit contracts**, for example above a certain interest rate (e.g. a standard bank credit card rate of around 20-23%), specific types of lending (e.g. motor vehicle lending, or unsecured personal loans), lending under or over a certain dollar amount (e.g. $2,000) or lending over a certain period of time (e.g. under 12 months)
- towards certain **kinds of borrowers**, for example those with a credit score below a certain level, a high debt to income ratio, a record of personal insolvency or borrowers that are new to the lender
- towards specific **classes of lenders**, for example excluding lenders who have few or no documented instances of irresponsible lending in the past, are regulated by the Reserve Bank, or have been accredited by a third party as having strong compliance systems for responsible lending.

62. Targeting the Regulations would be consistent with the original policy intent and would address a key underlying driver of the unintended impacts identified above, which is that the Regulations are applied to almost all consumer lending with limited exceptions, rather than targeting high-risk consumer lending.

Benefits

63. If well targeted, it would go a considerable way towards the objective of reducing unnecessary inquiries by lenders. Credit contracts that fell outside the targeted scope would be subject only to the inquiries deemed necessary by the lender under the principles-based approach in the CCCFA.

64. It would also promote access to affordable credit, by allowing lenders more discretion, in some circumstances, about when lending is likely to be affordable.

Costs and risks

65. However, there would need to be further work and consultation on the precise design of the targeting mechanism to ensure that it was correctly targeted at lending where there was a higher risk of hardship, and the targeting mechanism did not generate unintended consequences.

66. Potential unintended consequences include:
    - Some targeting mechanisms could provide a competitive advantage to incumbent lenders and business models (e.g. an exclusion for registered banks), raise barriers to entry (e.g. providing for third party accreditation) or otherwise harm competition.
    - Targeting particular products could incentivize lenders to change their businesses to avoid being captured by targeted scope. If this were to occur this could also shrink the market for particular kinds of credit (e.g., credit cards, unsecured personal loans, etc.) and therefore result in reduced availability of these types of credit for consumers, in addition to reducing competition.
    - Targeting borrowers with particular characteristics (e.g. low credit scores, or low income) could discourage mainstream lenders from lending to those individuals, exacerbating existing barriers to them obtaining safe credit, and leading them towards less scrupulous lenders. Similarly, relaxing affordability requirements for a lender’s existing borrowers could lock vulnerable borrowers into predatory lenders.

67. The Commerce Commission would incur additional costs from this option. There would be one-off costs producing new guidance. There would also be an increase in ongoing costs enforcing lender responsibilities due to the increase in complexity with different rules applied to different loans.

68. There is also a risk that some lenders may not implement targeting by borrower characteristics, due to the added complexity of moving away from uniform assessment processes. We have heard anecdotally that some banks currently apply CCCFA

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processes to lending that is completely excluded from the CCCFA, such as credit for business or investment purposes. Similarly, if lenders continue to apply the prescriptive requirements in the Regulations to lending that is supposed to be excluded by greater targeting, this means the unintended impacts would not be addressed.

Stakeholder views

69. Stakeholder views on targeting are unclear, and it is likely that many stakeholders would want to see the detail of the proposed targeting mechanisms before having a firm view. However, it would accord with lender desires to move away from what they label a 'one size fits all' approach to requirements. Further targeting was considered during the original design of the Regulations, but was not pursued due to a lack of consensus from lenders about its practicality and desirability. The current exception in regulation 4AG for 'obvious' affordability was the preferred option. Stakeholders may be more open to exploring targeting now that the implications of the CCCFA changes and the limitations of the exception in regulation 4AG are more fully appreciated.

Option 3: changes to the design of specific affordability regulations relating to borrower expenses, borrower surplus requirements and exceptions

70. Under this option, a range of adjustments would be made to specific aspects of the affordability regulations to address those regulations that are seen to be contributing to the unintended consequences. These changes would be in the following areas:

    - The range of expenses captured by the regulations ('relevant expenses') would be narrowed to more explicitly exclude discretionary expenses. This could be achieved by:

        i. changing the test from expenses that the borrower was 'likely' to incur (regulation 4AF(2)(a)) to those that were necessary or would continue to be incurred even if the borrower was at risk of hardship

        ii. narrowing paragraph (d) of the definition of 'listed outgoings' (regulation 4AE), which covers 'other regular or frequently recurring outgoings' that the borrower is unable or unwilling to cease, to exclude those that a responsible lender would expect the borrower to cease if at risk of hardship, or

        iii. removing paragraph (d) of the definition of 'listed outgoings' (regulation 4AE) altogether, and only capturing fixed financial commitments, debt payments and living expenses.

    - The conservative assumptions that are required to be applied by lenders to estimate the amount of a borrower's repayments from existing revolving credit contracts (like credit cards or buy-now pay-later schemes) would be relaxed to reduce 'double counting' of expenses (regulation 4AL). For example, lenders may not need to account for these repayments if the borrower routinely repays their outstanding balance in a short time period without incurring interest. This would reduce the 'double counting' that occurs where borrowers use their credit cards for day-to-day living expenses: lenders are required to count both the living expenses and assume that the borrower needs to make payments on the credit card as if the credit limit were fully utilised by the borrower.

    - Exceptions from a full income and expense assessment for refinancing of existing credit contracts (regulation 4AH) would be extended to refinancing of credit contracts from other lenders. The existing exception only allows a lender to refinance its own credit contracts.

71. This option would address the most prominent 'pain points' for lenders and borrowers. However, it would not address the more fundamental concern that the prescriptive nature of the CCCFA changes and their application to almost all consumer lending mean that lending has been significantly impacted outside of 'target areas'. A downside

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of these changes compared to targeting is that this would reduce some protection for those that do need it while leaving a high level of prescriptiveness for everyone else.

Benefits

72. This option would help to achieve the objective of providing consumers with access to affordable credit by removing several aspects of the Regulations that, in practice, have sometimes resulted in excessively high estimates of borrower expenses.

73. However, the effect of the change to assumptions around revolving credit contracts may be reduced to the extent that some lenders (particularly major banks) applied the current approach of the Regulations prior to 1 December, and are likely to continue to do so in the future. We understand that for Australian-owned banks, this reflects rules set in Australia.

74. Some aspects of this option would also reduce unnecessary inquiries. By more explicitly excluding discretionary expenses, lenders would make fewer inquiries into these expenses. Borrowers have tended to find these inquiries particularly intrusive. Inquiries would be substantially reduced for refinancing of loans with other lenders.

75. Compared to Option 2, this option is expected to do relatively less to reduce unnecessary inquiries (since it doesn't remove many borrowers completely from the scope of prescriptive regulations) but may do more to address unnecessary credit declines.

76. Another benefit of this option would be to encourage competition in consumer credit markets, by relaxing affordability assessment requirements where one lenders' loans are refinanced by another lender. This will encourage customer switching – for example, between banks to achieve lower mortgage interest rates.

Costs and risks

77. This option does pose some risks to consumer protection and has the potential to result unaffordable lending in some circumstances. These risks may arise to the extent that:

    - lenders incorrectly assume that certain expenses are 'discretionary' that the borrower, in reality, requires
    - borrowers who were previously quickly paying off their revolving credit contract balances change the way they use their facilities after taking out a new credit contract – for example, making a large expenditure (like purchasing furniture, repairing their car, or going on a holiday) using their credit card that then needs to be repaid over many months or years

Stakeholder views

78. We expect that these changes would be supported by lenders. Most of these changes have been proposed by individual lenders during the investigation. Consumer advocates are likely to be concerned about these changes to the extent that they weaken consumer protections.

Option 4: changes to the penalties and liability regime

79. This option would reduce the risk and extent of liability for creditors and their directors and senior managers by:

    - reducing the onerousness of the due diligence duties for directors and senior managers of creditors (section 59B) by providing a defence where directors and senior managers exercised good faith, and allowing directors to indemnify themselves against liability
    - reducing penalties by capping the maximum amount of statutory damages that could apply to class actions (e.g. to $5 million).

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80. This approach is likely to result in a decrease in conservatism from lenders and may provide a partial alternative to changes which specifically address the design and drafting of the Regulations.

Benefits

81. It would support the objective of providing consumers with access to affordable credit by reducing the extent to which lenders favour interpretations of the Regulations that result in lower borrower income estimates, higher expenses estimates, and higher surplus requirements. It may address tendencies for lenders to prefer using historic expenses from bank transaction records over (less verifiable) borrower declarations about their likely expenses, which can result in inflated expense estimates. Similarly, lenders may be encouraged to engage less in the statistical benchmarking of expenses (which increase expense estimates in some circumstances) where expenses have already been verified against transaction records.

82. This option would also support the objective of reducing unnecessary inquiries, by encouraging lenders to rely on the minimum number of information sources required by the Regulations, and also giving lenders more confidence to use the exception for ‘obvious’ affordability (regulation 4AG) due to lower liability if their conduct is found to breach the Regulations.

83. Relaxing director and senior manager liability may also aid recruitment to these positions. Capping statutory damages would also be of significant benefit to some lenders – particularly large banks.

Costs and risks

84. A drawback of this approach would be a reduction in consumer protection for some borrowers, particularly those dealing with less scrupulous lenders who may be more willing to risk breaches and who were the main targets of the CCCFA changes. Directors and senior managers would have less incentive to oversee compliance, increasing risks of non-compliance with responsible lending obligations. Less scrupulous lenders may be encouraged to use exceptions in inappropriate circumstances and favour interpretations of the Regulations that do not comply with the overarching affordability principle in the CCCFA. On the other hand, lenders with a strong compliance culture (who are more likely to be compliant with the overarching affordability principle in any case) may continue to apply a relatively conservative approach to interpreting and applying the regulations, given the potential reputational harm from breaches.

85. Capping statutory damages would also reduce payments to consumers who were involved in class actions, and therefore reduce the incentives for lender responsibilities to be enforced.

Stakeholder views

86. We expect that reducing potential penalties would be welcomed by lenders, some of whom have cited liability as a barrier to adopting more flexible lending processes. Views of consumer advocates on these matters are less clear, but this option may be viewed negatively to the extent that it is seen to encourage less scrupulous lending practices.

Option 5: repealing the affordability regulations

87. Repealing the affordability regulations would result in a return to the principles-based model which was used prior to 1 December. This change may need to be made alongside changes to the Code to provide guidance on how lenders should meet the lender responsibility principles in Section 9C of the Act, for instance guidance on the recommended minimum inquiries.

Benefits

88. This option would do the most of all those considered to improve ease of access to credit, as lenders would no longer be required to conduct an affordability assessment in

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the prescribed manner. A return to a principles-based model would mean lenders would, in practice, have greater discretion regarding how they conduct affordability assessments to meet the lender responsibility principles.

Costs and risks

89. However, this option is likely to reduce consumer protection for some borrowers where lenders adopt less rigorous affordability assessments, and it would significantly lessen the extent to which the CCCFA changes address the problems identified by the original RIS. The original RIS stated that "the principles-based nature of the requirements in the CCCFA and its non-binding nature have been identified by stakeholders as contributing to problems with non-compliance. Where legal obligations are not clear, they can be difficult to apply and for the regulator to enforce." Prescriptive requirements for affordability and suitability were one of the key measures expected to significantly improve the 2018 status quo in respect of protecting consumers from unaffordable lending, providing clarity of legal obligations and reducing non-compliance.

90. Other aspects of the CCCFA recommended elsewhere in the original RIS may mitigate this to some extent: for example, requirements for lenders to keep records that substantiate that loans are affordable, the removal of the blanket ability for lenders to rely on borrower statements (unless they have reasonable grounds to believe the information is not reliable), and the enhanced liability regime. Changes to the Code to provide additional guidance may also help, though its benefits are limited due to its non-binding nature.

Stakeholder views

91. We expect that this option would be welcomed by lenders, who have generally opposed the prescriptive requirements. Consumer advocates would be almost certain to strongly oppose it.

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Key for qualitative judgements:	
++	much better than the counterfactual
+	better than the counterfactual
0	about the same as the counterfactual
-	worse than the counterfactual
- -	much worse than the counterfactual

How do the options compare to the status quo/counterfactual?

	Option 1 – Counterfactual	Option 2 – target regulations	Option 3 – amend specific affordability regulations	Option 4 – reduce liability	Option 5 – repeal regulations
Effectiveness – improving access to credit	0 Borrowers continue to be unnecessarily declined	+ Improves access to credit by allowing lenders to exercise more discretion in some situations	++ Addresses regulations that result in overestimation of expenses, and eases refinancing	+ Reduces conservative interpretations of requirements	++ Principles-based approach gives lenders more flexibility and discretion in assessments
Effectiveness – reducing unnecessary inquiries	0 Borrowers continue to be subject to unnecessary inquiries	++ If well targeted, would considerably reduce unnecessary inquiries by lenders	+ Reduces unnecessary inquiries somewhat – particularly discretionary expenses and refinancing	+ Reduces conservative interpretations of requirements	++ Lenders design own inquiries based on their understanding of the principle
Effectiveness – consumer protection (triple weighted)	0 Addresses original 2018 problem definition	0 Assuming that higher-risk lending is correctly targeted, consumer protection should not be impacted. However, risks if not carefully designed	0 Assuming that resulting estimates of net income better reflect reality	- - Would significantly reduce incentives for less scrupulous lenders to comply	- - Principles-based approach gives lenders more flexibility and discretion in assessments
Compliance costs	0 No change to compliance costs.	+ Streamlined processes in some situations would cut operational costs	0 Fewer inquiries may marginally reduce compliance costs	0 Unlikely to change compliance costs, except marginally to the extent that less due diligence is conducted	+ Streamlined processes would cut operational costs
Overall assessment	0	4+	3+	4-	-

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What option is likely to best address the problem, meet the policy objectives, and deliver the highest net benefits?

92. On the basis of the assessment against criteria, we consider that Options 2 and 3 should be further pursued. In both cases (and especially Option 2) this assessment is preliminary, with further work needed to complete the detailed design of options.

93. The assessment of the impact on effectiveness at achieving consumer protection assumes that, following further consultation on draft regulations, risks discussed above do not materialise around:

- targeting causing unintended consequences, or
- lenders making incorrect assumptions about discretionary expenses.

What are the marginal costs and benefits of the option?

Option 3 only (recommended by Cabinet paper)

Affected groups	**Comment** *nature of cost or benefit (eg, ongoing, one-off), evidence and assumption (eg, compliance rates), risks.*	**Impact** *$m present value where appropriate, for monetised impacts; high, medium or low for non-monetised impacts.*	**Evidence Certainty** *High, medium, or low, and explain reasoning in comment column.*
Additional costs of the preferred option compared to taking no action			
Regulated groups	One-off changes to systems.	Medium. One-off costs to implement the CCCFA regulations totalled hundreds of millions of dollars, but these changes are likely to be substantially less.	Low – will require further feedback from stakeholders.
Regulators	One-off costs communicating new guidance.	Low	Medium
Others (e.g., wider govt, consumers, etc.)	Some consumers may be adversely affected by reduction in protections.	Low	Medium
Total monetised costs			
Non-monetised costs		Low	
Additional benefits of the preferred option compared to taking no action			
Regulated groups	Ongoing increase in lending and associated revenue.	Medium	Medium – lenders have indicated that options along these lines will have benefits.
Regulators	-	-	
Others (e.g., wider govt, consumers, etc.)	Improved access to credit	Medium	Medium

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Total monetised benefits			
Non-monetised benefits		Medium	

Options 2 and 3 (MBIE preferred)

Affected groups	**Comment** *nature of cost or benefit (eg, ongoing, one-off), evidence and assumption (eg, compliance rates), risks.*	**Impact** *$m present value where appropriate, for monetised impacts; high, medium or low for non-monetised impacts.*	**Evidence Certainty** *High, medium, or low, and explain reasoning in comment column.*
Additional costs of the preferred option compared to taking no action			
Regulated groups	One-off changes to systems.	Medium. One-off costs to implement the CCCFA regulations totalled hundreds of millions of dollars, but these changes are likely to be substantially less.	Low – will require further feedback from stakeholders.
Regulators	One-off costs producing new guidance, and an increase in ongoing costs enforcing lender responsibilities due to the increase in complexity with different rules applied to different loans.	Medium.	Medium.
Others (e.g., wider govt, consumers, etc.)	Some consumers may be adversely affected by reduction in protections.	Low	Low – further work required to design targeting mechanism.
Total monetised costs		-	
Non-monetised costs		Medium	
Additional benefits of the preferred option compared to taking no action			
Regulated groups	Significant increase in lending and associated revenue.	High	Low – more information needed about potential uptake of targeting.
Regulators	-	-	
Others (e.g., wider govt, consumers, etc.)	Ongoing improvements in access to credit and streamlined credit assessment processes for many borrowers.	High	Low
Total monetised benefits	-	-	

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Non-monetised benefits		High	

94. As with our assessment against criteria, these tables assume that the design of the final regulations is such that the risks identified in paragraph 66 and 77 do not materialise. If these risks were to materialise, significant additional costs that would be incurred by some consumers due to unaffordable lending, as outlined in those paragraphs.

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Section 3: Delivering an option

How will the new arrangements be implemented?

95. Prior to implementation, it is important that there be thorough consultation on an exposure draft of amendment regulations. This will provide more certainty about the likely costs and benefits of the options and ensure that the final design delivers on the objectives.

96. If the Cabinet paper recommendation of Option 3 is pursued, amendment regulations are expected to be made by the end of 2022, and to come into force in early 2023.

97. If both Options 2 and 3 were pursued, the further development time required for Option 2 would likely push finalisation of the amendment regulations to the first quarter of 2023. MBIE would be likely to seek further data from lenders in order to identify characteristics of lenders, borrowers and credit products that were correlated with risk of unaffordable lending.

98. Regulations may be able to come into effect relatively quickly (e.g. 28 days after being made), as lenders' systems for complying with the current regulations are assumed to also comply with the new regulations. Therefore, any changes that lenders make to systems to ease assessment processes will be voluntary – but are likely to be required in the medium term to maintain competitiveness.

99. Changes are also likely to be required to the Responsible Lending Code, which provides non-binding guidance on the CCCFA and Regulations and would ideally be made at the same time as the regulations. These changes could be developed while an exposure draft of the amendment regulations is being consulted on.

100. As with the CCCFA changes, the Commerce Commission will also have an important role in communicating any changes to lenders and other stakeholders. For the CCCFA changes, the Commission ran a number of well-attended lender seminars on their interpretation and enforcement approach in respect of the Regulations.

How will the new arrangements be monitored, evaluated, and reviewed?

101. We intend to check in with key stakeholders soon after any further changes to legislation to find out what changes are being made to processes, and the impacts of these on lending and borrowers.

102. In the medium term, the CCCFA changes have a baseline dataset that is intended to be used for a future evaluation, which is also relevant to the changes covered by this RIS. Key measures from the baseline of relevance to the objectives in this RIS include:

    - proportion of consumers applying for credit (54% in 2019)
    - proportion of consumers who applied for credit declined at least once (21%)
    - impacts on borrowers of being declined credit
    - proportion of borrowers who either default on a loan or have to reduce spending on important living expenses to keep up with repayments (34% in 2019)
    - proportion of borrowers who reported that repayment difficulties were having a moderate or serious negative impact on their lives (18% in 2019)
    - proportion of consumers who are confident that the lender properly considered income and expenses and assessed that repayments would be affordable (75% in 2020)
    - ease of enforcement of affordability obligations by the Commerce Commission.

103. A number of these measures are derived from 2020 consumer survey that is intended to be repeated as part of the evaluation, as well as the biennial New Zealand Consumer Survey.

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104. In addition, the investigation report relied on a number of measures that will be useful for assessing the impact of the amendments discussed in this RIS:

- number of borrowers by type of loan
- loan conversion rates by type of loan
- loan conversion rates by credit score
- dispute resolution service complaints data for certain categories of complaints such as delays, banks not acting as expected, and borrowers having to provide more information.

105. The CCCFA requires that Subpart 6A of Part 2 the CCCFA (which covers regulation of high-cost consumer credit contracts) be reviewed by June 2023. The fuller evaluation of the CCCFA reforms may be performed at the same time.

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