

# Responsible Lending



This describes new processes which lenders must follow from 1 December 2021 when assessing suitability and affordability, and their obligations when dealing with borrowers encountering payment difficulties.

Lenders must make certain inquiries before any consumer loan is entered into to make sure the loan will be suitable and affordable for the borrower.

These inquiries will also need to be made before a 'material change' is made to a loan. From 1 December 2021, new regulations provide for the process by which lenders are required to make the inquiries.

Lenders will have to keep records of the assessments made.

Most of the change comes into effect on 1 December 2021 with a revised Responsible Lending Code.

The guidance in chapter 12 of the Code about responsible lending obligations when repayment difficulties or other problems arise, comes into effect on 1 February 2022.

The purpose of these changes is to increase certainty about lenders' obligations when conducting loan suitability and affordability assessments, and to clarify lenders responsible lending obligations on payment default.

## **Lenders must comply with the Responsible Lending Principles.**

**They can be found in section 9C of the Credit Contracts and Consumer Finance Act (CCCF Act).**

Under the principles, lenders must at all times exercise the care, diligence and skill of a responsible lender in any advertisement for credit, before entering into a loan, and in all subsequent dealings with borrowers.

**These responsibilities include that a lender must make reasonable inquiries before entering into the loan, to be satisfied that it is likely:**

- that the loan will meet the borrower's requirements and

objectives (i.e. that the loan is suitable);

- that the borrower will make the payments under the loan without suffering substantial hardship (i.e. that the loan is affordable).

## **Key changes to these responsible lending obligations taking effect from 1 December 2021, include:**

- lenders must make suitability and affordability assessments before making a 'material change' to a loan;
- when making suitability and affordability assessments lenders must make the mandated inquiries set out in regulations;
- lenders must keep records of the suitability and affordability assessments, including the results.

## **A revised Responsible Lending Code also comes into effect on 1 December 2021 (except for chapter 12, the part dealing with lenders' obligations when borrowers encounter repayment difficulties—which comes into effect on 1 February 2022).**

The Responsible Lending Code provides guidance about what lenders can do to comply with the responsible lending principles, including the inquiries that have to be made under the regulations.

The Code is not binding on lenders, but the CCCF Act says evidence of compliance with the Code is to be treated as evidence of compliance with the principles of responsible lending.

**Lenders will need to make suitability and affordability assessments before they can make a 'material change' to a loan.**

A 'material change' will be a defined term, and covers increases to the credit limit or where the lender plans to

make an additional advance, and the lender didn't take that into account when the last suitability and affordability assessment was made.

Under existing law, the Commission would expect lenders to already be conducting similar assessments before increasing credit limits or advancing new funds as part of being a responsible lender in all subsequent dealings, but the law change now makes this explicit.

**As part of meeting the responsible lending obligation to assess loan suitability and affordability lenders will need to make inquiries and follow processes set out in the new regulations.**

A failure to comply with the regulations will be a breach of the relevant responsible lending principles. They can be found in section 9C.

Details of the new regulations are found in the Credit Contracts and Consumer Finance (Lender Inquiries into Suitability and Affordability) Amendment Regulations 2020.



As part of making reasonable inquiries to assess whether a loan is suitable for a borrower, the regulations require that lenders gather certain information about the borrowers requirements and objectives.

They can do that by asking questions of the borrower, including (but not limited to) the purpose for which the loan is planned to be used, the loan amount or credit limit sought, and the loan term.

The lender is then required to assess the information it has

gathered to determine if the loan will meet those needs and objectives.

**Lenders must also make inquiries in order to be satisfied on reasonable grounds that the loan is going to be affordable, and that it is likely the borrower will make the loan repayments without suffering substantial hardship.**

That's on the following basis:

- That the borrower's income exceeds their expenses. To account for the risk that the borrower's income has been overstated or expenses underestimated, in completing the assessment lenders must either ensure there is an adequate surplus, or that the income/expenses used to complete the assessment include reasonable buffers.
- That lenders can't just rely on what the borrower tells them in all cases. They must take certain steps to either verify income based on reliable evidence (which could include recent information held by the lender) or, where verification isn't practicable, consider whether the source of the income or the amount is realistic.

The lender's assessment of likely expenses is a two-part process:

- First, make an initial expense estimate by asking the borrower questions or obtaining reliable information and assess for omissions.
- Then, verify the details of any expenses given by the borrower with reliable evidence and, if necessary, adjust the expenses.

The above is a very high-level summary of some of the requirements, please refer to the Amendment Regulations for full details.

The Code contains helpful guidance about the regulations—including an affordability assessment flowchart.

## Other products

**In addition to loans, responsible lending obligations may also apply to some products sold together with loans.**

Things like extended warranties, repayment waivers, consumer credit insurance, and GAP insurance.

Lenders are already required to comply with certain obligations under the Responsible Lending Principles in relation to these types of products.

That includes the obligation to make inquiries so as to be reasonably satisfied that the products are likely to be suitable and affordable.

From 1 December 2021, new regulations will come into force which prescribe how to comply with these obligations.

## Records

**Lenders will be required to keep records (about inquiries made and the results of those inquiries) that demonstrate how the lender has complied with their responsibility to assess whether loans are suitable and affordable.**

The Responsible Lending Code provides more detailed guidance about record keeping.

Lenders must make these records available free of charge on request from anyone who is entitled to ask for a copy.

That includes the Commerce Commission, an approved dispute resolution scheme, and/or the borrower (or their representatives).

They must be provided within 20 working days (or any longer period specified by the Commission).

Lenders must keep these records for at least seven years.

**Next, the portion of the revised responsible lending code which covers repayment difficulties and other problems.**

**Details can be found in Chapter 12 of the code.**

You'll find Chapter 12 contains extensive revisions to the current June 2017 version of the Code.

Unlike other chapters, this one doesn't come into force until 1 February 2022.

**As well as an overarching obligation to be a responsible lender in subsequent dealings with a borrower, lenders are required to treat borrowers reasonably and in an ethical manner when:**

- there are breaches of the loan agreement;
- when problems arise;
- or where a borrower suffers unforeseen hardship.

The revised code has extensive guidance for lenders around how to comply with their obligations where problems with the loan arise, including:

- identifying repayment difficulties (including potential difficulties);
- managing loans where the lender is aware of, or expects, repayment difficulties;
- communicating with the borrower around repayment difficulties, including helping borrowers to make informed decisions;
- expectations around monitoring;
- processes around hardship relief, debt recovery, enforcement and dealing with complaints.

### **Links to existing and relevant resources:**

[MBIE Responsible Lending Code \(Revised February 2021\)](#)

### **These are the relevant sections of the Act:**

- Sections 9C(3)(a), 9C(7), 9C(8), and 9CA CCCF Act (as amended 1 December 2021 by sections 10 and 11 Credit Contracts Legislation Amendment Act 2019).
- Credit Contracts and Consumer Finance (Lender Inquiries into Suitability and Affordability) Amendment Regulations 2020.

(All section and regulation references are as at 1 December 2021).

## ACTION

Lenders need to ensure that they have policies and procedures in place to comply with responsible lending obligations, including the obligation to assess loan suitability and affordability, making the mandated inquiries, and to treat borrowers appropriately where repayment problems and other difficulties occur.

## IMPACT

It is significant. While lenders are already under an obligation to make inquiries to be sure that a loan will be suitable and affordable, the changes now mean they have to follow a particular process in order to do this. They also need to make these inquiries if material changes are made to existing loans. Lenders must keep records of all of this to demonstrate they've acted responsibly.

This material provides guidance only. It is not intended to be definitive and should not be used in place of legal advice. You are responsible for staying up to date with legislative changes.

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