

Consumer Credit Reform – from principle to prescription

The need to revisit the whole customer lending journey in the wake of regulatory changes

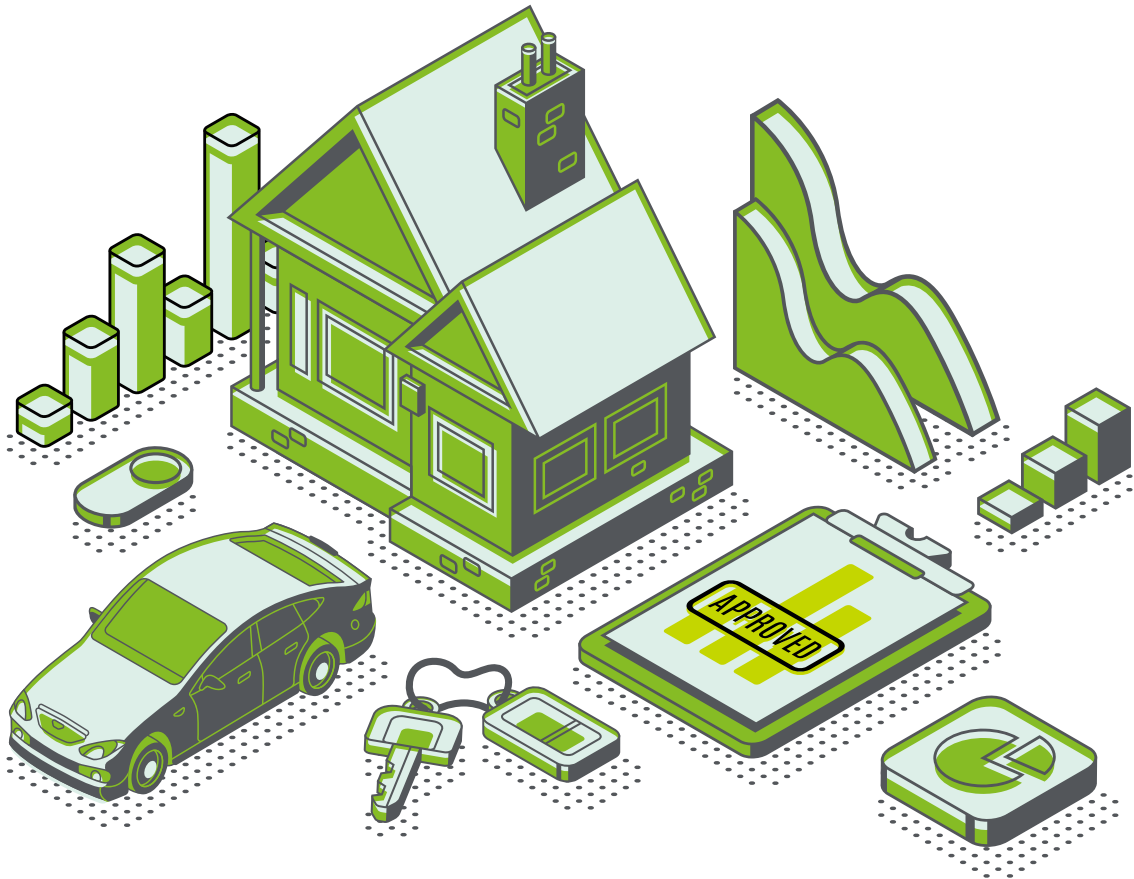
The Credit Contracts Legislation Amendment Act, which updated the Credit Contract and Consumer Finance Act, was passed into law on 19 December 2019 to take effect in stages from 20 December 2019.

The reforms introduced a number of important changes for lending and borrowing in New Zealand. This allowed for prescriptive requirements to be made in regulation to clarify what lenders must do to comply with their obligations and to better protect vulnerable consumers from getting into problem debt.

New enforcement provisions, including pecuniary penalties, tougher statutory damages and enforceable undertakings took effect, as did expanded options for creditors to make electronic disclosure.

In February 2021, the Responsible Lending Code was also updated to provide guidance about how to comply with the lender responsibilities, including the new affordability and suitability regulations. The Code and regulation take effect from 1 October 2021 and along with other obligations, means that the regulatory bar is now higher. There are now obligations in relation to:

- Regulations setting minimum requirements for affordability, suitability, responsible advertising and debt collection disclosure
- Requirements to undertake affordability and suitability assessments where there have been material changes to a contract
- Duties on directors and senior managers
- Requirements to keep records of affordability and suitability assessments, and how fees are calculated
- Providing disclosure to borrowers in languages used in advertising
- Providing information about disputes resolution schemes and financial mentoring services
- Requirements for creditors (excluding banks) and mobile traders to be certified (creditors and mobile traders already registered on the FSPR have until their next annual confirmation after 1 October 2021 to obtain a certification)
- Regulations relating to information to be provided for variation disclosure
- A need to provide positive assurance that regulatory obligations are met.



Not a simple fix

With the 1 October date looming, many lending organisations are still struggling in the midst of costly and complex programmes of work designed to meet the requirements which have been set out. Others may be of the view that actually the answer is simple – by having better conversations with customers around their current lending and making responsible decisions around credit.

That certainly can help but more detailed work needs to be completed. To effectively achieve what is required it is necessary to examine the whole consumer lending lifecycle, from origination through to debt recovery. Without doing this, an organisation cannot be confident that at every step of the process the right conversations are had, the correct information is provided and accurately evaluated and appropriate evidence is retained to assure directors and senior managers that all obligations are met.

The challenges

Since most industry experts can remember, one of the aspirations of many financial services organisations has been to achieve a 'single view of customer'. This is now an imperative.

A 'single view of customer' assists in meeting regulatory obligations by enabling an organisation to:

1. Easily observe all the customer information that is required to ensure a thorough and complete understanding of a customer's affordability and suitability position.
2. Better retain all the information needed to be able to demonstrate that the appropriate assessments occurred and customer lending costs are accurately provided every time.

Other challenges include tight timeframes:

- The crucial affordability and suitability regulations were passed in December 2020 while the Responsible Lending Code, which provides guidance on how to comply with lender responsibilities, was only finalised in February 2021. This means that the analysis of business and systems requirements in relation to the changes could only really begin to be finalised after this date.
- Typically in any complex financial services organisation, there is an equally complex myriad of systems inter-operating to provide consumer lending services. It isn't just about the core but all the peripheral

components, people and processes which need to work cohesively together to ensure good customer outcomes and enable informed lending decisions.

To effectively meet the regulatory changes, every component of retail lending technology systems needs to be examined and every process that touches the customer through their whole lending journey requires detailed examination. Front-line staff must be trained to do things differently and use additional toolsets to ensure the right lending and regulatory outcomes are achieved.

The breadth and depth of activity required to achieve those outcomes, whilst not transformational in an innovation sense, is comparable in terms of the body of work that must be completed.

Not taking a comprehensive, 'whole of customer' lending journey approach introduces the significant risk that directors and senior managers cannot attest to their compliance obligations.

Considerations for compliance

Meeting regulatory compliance obligations is a complex and challenging activity. The bar continues to rise as a result of

consumer and regulator expectations. Giving careful consideration to the following will go some way to simplifying matters and creating efficiencies:

1. **Be able to fully trace the regulations from your organisation's obligations, through to systems and processes.**

This is critical. On one hand, a legal interpretation is important but there is an imperative to implement sustainable future-proofed operational processes which can be reliably demonstrated and be resilient to scrutiny.

2. **Inventory your captured processes.**

This is impossible if you don't have good tools which document these and mechanisms which keep them up to date. Documenting processes is not just nice to have - it's a critical component of business process redesign and it's not practical or economical to have to redo this every time regulation changes.

3. **Understand what lending-related data exists.**

You should know where this data is held and what it is used for. Be confident over accuracy and completeness. This extends beyond the loans themselves and includes all aspects in relation to the lending lifecycle. Ensure you have systems and tools which support good data governance and that record keeping requirements are well understood and the supporting processes are reliable.

4. **Utilise automation and tooling.**

Regulatory compliance can no longer be effectively and consistently achieved using just spreadsheets and humans. The data pool is too vast and the systems too complex to achieve the necessary outcomes without use of modern Regulatory Technologies (RegTech). Invest where it makes sense in a way that helps drive down compliance cost through creating automation and efficiencies.

5. **Ensure good regulatory risk governance regimes are in place.**

Have clarity as to where system and process ownership lies because this will help determine the senior managers responsible and feed into the overall system of attestation necessary for boards. Consider utilising specific accountability regimes for senior management.

6. **Build in compliance and assurance mechanisms by design.**

To improve sustainability of the control environment and confirm that mechanisms in place are robust and deliver to the regulatory requirements, ensure that risk and control thinking is embedded into solution design. Focus on what must go right and create good automated preventative controls that you can be confident address the risk and operate consistently over time.

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