



Approved dispute resolution schemes' approach to applying remedies for irresponsible lending

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This document outlines the financial dispute resolution schemes' approach to applying the remedies available under section 89 of the Credit Contracts and Consumer Finance Act 2003 (CCCFA).

It explains the general approach. However, each complaint is considered on its own facts. There will be cases where the specific circumstances mean that the scheme will recommend a different remedy in order to ensure a fair result.

Section 9C of the CCCFA is the starting point

The starting point for any investigation of a complaint about irresponsible lending is section 9C, Lender responsibility principles.

Under section 9C(3)(a) lenders are obliged to make reasonable inquiries that:

- the loan will meet the borrower's requirements and objectives and
- the borrower will be able to repay the loan without suffering substantial financial hardship.

Remedy for breach of CCCFA is set out in section 89

The remedy available for a breach of section 9C(3)(a) is set out in section 89(1)(aaa).

Remedy for irresponsible lending

Under section 89(1)(aaa), if a lender has failed to make reasonable inquiries before entering into a loan agreement, the lender is obliged to refund:

- interest charges
- credit fees
- default fees.

The rationale behind this remedy is that the lender should not profit from their lending if they have breached their responsible lending obligations under the CCCFA, but because the borrower has had the benefit of the loan amount, they are obliged to repay the principal borrowed.

The amount of the interest and fees charged on the loan are calculated and deducted from the balance owing.

If the refund of interest and fee refunds results in a credit balance on the loan account, the lender refunds this balance to the borrower.

The lender may not charge any further interest or fees on the loan. This approach is consistent with section 94(1)(caa)(ii) of the CCCFA which allows a court to make an order prohibiting the further charging of interest, fees, and other charges under the contract.

Loan top-ups

Generally, where the original decision to lend was responsible but the lender did not meet their responsible lending obligations with respect to a loan top-up, only the interest and fees charged on the amount of the top-up will be refunded.

Debt consolidation improving borrower's position

Where an irresponsible lending decision allowed the borrower to consolidate existing higher interest-bearing debt, the lender will not generally be required to refund all interest and fees. Although the lender should not have approved the loan, by refinancing existing, more expensive debt, the lender has improved the borrower's circumstances. To require the lender to refund all the interest, including interest on the consolidated debt, will mean that the borrower may be unjustly enriched. In this case, the lender will likely be required to refund only the interest on the additional money advanced.

Repayment of residual debt owing

If, after the interest and fee refunds, the loan has a debit balance, the scheme may also help the parties negotiate a repayment plan. Where possible, if the loan is secured, the aim is for the borrower to keep the secured item and to repay the debt back at an affordable rate that would allow the debt to be repaid over a term as close to the original loan term as possible. If the original loan term has already expired, the scheme may help the parties to negotiate a new loan term.

This approach is consistent with section 94(1)(caa)(i) of the CCCFA, which allows a court to make an order allowing for the affordable repayment of debt.

If repayment of residual debt is unaffordable

In cases where the refund leaves a considerable debt to be repaid that the borrower cannot afford, the borrower may be asked to provide a statement of position.

If the borrower cannot afford a realistic repayment amount, the borrower may need to surrender the security to be sold, with the sale proceeds used to reduce the debt owed to the lender. Generally, it is not fair to require or expect the lender to accept a very low repayment amount, and the administration costs that go with an extended repayment arrangement, if the borrower has not done everything they can, like surrender security, to reduce the debt.

Residual debt owing after security is surrendered

If the security is sold, leaving a residual debt, the lender is encouraged to consider writing-off the residual balance of the debt if:

- the amount is very small;
- there is evidence that repayment would cause the borrower significant financial hardship; and
- waiving the debt on compassionate grounds is appropriate, for example, where the borrower is a vulnerable consumer.

If it is not appropriate for the lender to waive the debt, the lender is encouraged to allow the borrower to repay the residual debt at an amount affordable for them, even if this amount is very small.

Some financial mentors have suggested that the scheme should use section 94(1)(caa)(iii) of the CCCFA to require lenders to write-off any residual debt on the basis that this is necessary to remedy a breach of section 9C(3)(a) of the CCCFA. As discussed above, there may be some circumstances where it is appropriate to encourage lenders to write-off debt but, in most cases, the other remedies in the CCCFA will be sufficient and an order requiring a write-off of residual debt is not required.

Borrower's refusal to co-operate

If the borrower refuses to co-operate and surrender the security, or pay anything at all, the debt will be reduced by the interest and fees and the lender will not be able to add any further interest and fees to the debt, but will be able to take debt recovery action.

Unrealistic claims

From time to time, the schemes see requests from borrowers, seeking compensation that the CCCFA does not provide for. For example, the borrower expects a lender to:

- buy the borrower a replacement car; or
- refund all the payments the borrower has made towards the loan; or
- compensate a borrower for the stress and inconvenience associated with the financial distress caused by the unaffordable lending.

The scheme is most unlikely to award compensation that is not provided for under the CCCFA, except for compensation for inconvenience (see below).

Stress and inconvenience

Financial hardship is both stressful and inconvenient. However, the borrower has had the use of the loan money.

Where a scheme is considering compensation for inconvenience, the benefit of having the loan must be balanced against the inconvenience caused by the financial stress.

In some instances, making the loan repayments might have caused or exacerbated financial hardship for the customer, leaving them worse off than if they had not taken the loan. In other words, the impact of the irresponsible lending may sometimes exceed the benefit derived from the loan. Customers may have forgone other expenses or social events in order to meet repayments, and may have experienced stress, damage to relationships and/or disruption to financial planning as a result of the irresponsible lending. The scheme may consider it appropriate to compensate customers for these impacts under the stress and inconvenience category.

Other provisions within section 89

Section 89(1)(aab) requires the lender to refund the full amount the guarantor has paid under the guarantee.

Section 89(1)(aac) requires the lender to refund the amount they have charged under an insurance contract where the lender has breached clause 9C(5)(a) of the CCCFA and breached responsible lending obligations with respect to the sale of insurance. This may go hand in hand with an irresponsible lending complaint requiring a refund of interest but, if it did not,

the lender is expected to refund the interest relating to the inappropriately charged insurance.

Section 89(1)(aad) relates to high-cost lending, and requires a refund of interest, credit fees, and default fees.

Sections 89(1)(a), 89(1)(b) and 89(1)(c) relate to disclosure.

Section 89(1)(d) is a catch-all clause that applies in the case of any other breach and allows a refund of \$6,000 or 5% of various amounts. This section will not be used to compensate borrowers where a remedy is available under sections 89(1)(aaa)-(aad).

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