Loan affordability – a consumer guide

September 2024

We sometimes receive complaints where the borrower says they cannot afford their loan or that they are struggling to repay it.

If the loan is not affordable because of a change in the borrower's circumstances, such as illness or job loss, the borrower should contact their lender to discuss their circumstances. We may be able to help with a complaint about hardship assistance.

If the borrower's circumstances have not changed or they have always struggled to pay their loan, we can consider whether the lender met their responsible lending obligations when they assessed and approved the loan.

If the loan is a consumer credit contract, the lender must make reasonable inquiries before they enter into the loan agreement to satisfy themselves that the borrower will be able to make their loan repayments without suffering substantial hardship.

Since December 2021, lenders must also make these inquiries before they agree to:

> increase a borrower's credit limit, or

> advance further money to the borrower under an existing loan agreement (if the further advance was not considered when the loan was assessed).

The legal obligation on lenders to make reasonable inquiries does not apply to loans that are not consumer credit contracts, such as business loans and loans to a trust.

This legal obligation also does not apply to buy now pay later. See our buy now pay later consumer guide for more information.

What happens to the loan when we are considering the complaint?

Our involvement with a complaint does not change the borrower's or lender's rights and obligations – for example:

> the borrower is obliged to keep repaying their loan

- the lender can continue to charge fees and interest under the loan agreement.

The only thing that changes is that the lender cannot take debt recovery action while we are considering the complaint unless they have our consent to do this.

Most borrowers that complain about loan affordability are not able to make their repayments in full, but we encourage borrowers to pay what they can afford to pay, even if this is a small amount. Intentionally stopping all loan repayments while we are considering the complaint may leave the borrower in a worse position.

We encourage borrowers to communicate with their lender about their repayments while the complaint is in the lender's internal complaints process. If we are investigating the complaint, the FSCL case manager assigned to the complaint can help the consumer and lender communicate with each other about the loan repayments while we are investigating the complaint.

Did the lender make reasonable inquiries?

When we investigate a complaint about loan affordability, we consider whether the lender complied with their obligation to make reasonable inquiries to satisfy themselves that the borrower would be able to make their loan repayments without suffering substantial hardship.

We take substantial hardship to mean that the borrower could make their loan repayments (for the loan they applied for) without undue difficulty and:

- pay their essential living expenses, such as accommodation, food, power and gas, transport, and medical expenses
- meet their other financial commitments, such as repayments on existing debts.

The fact a borrower is in hardship does not mean the lender did not meet their obligations when they approved the loan. A borrower may have fallen into hardship for other reasons – for example, because their income or expenses unexpectedly changed after they took out the loan.

We must consider what the law was at the time the loan was taken out. From December 2021, there were prescriptive requirements on lenders about the inquiries they needed to make when assessing a loan. These prescriptive requirements were revoked in July 2024.

We also consider the Responsible Lending Code that was in force at the time the loan was taken out. The Code sets out guidance about how lenders can comply with their responsible lending obligations.

If a lender has not followed the Code, it does not mean they have breached the law. However, we expect the lender to explain to us what they did to comply with their responsible lending obligations.

What information do we review?

When we investigate a complaint, we review the information the lender obtained from the borrower when they assessed the loan and their communications with the borrower about the loan application – for example:

- the loan application form
- the information the lender obtained from the borrower about their income and expenses, such as bank account statements and payslips
- emails and telephone calls between the lender and the borrower.

We also review the lender's affordability assessment. This is the lender's assessment of the borrower's income, essential living expenses, and their financial commitments.

If the lender does not have an affordability assessment, we expect them to explain to us how they decided the borrower could afford the loan without suffering substantial hardship.

We may also need information from the borrower to help us understand their financial circumstances at the time they applied for the loan – for example, we may have questions for the borrower about transactions on their bank account statements.

Did the loan cause the borrower financial difficulties?

We are unlikely to uphold a complaint if the loan did not cause the borrower financial difficulties.

It may not be fair to uphold a complaint if the lender made a mistake with their affordability assessment, but this mistake did not cause the borrower any harm. The purpose of the law is to protect consumers from ending up in substantial hardship.

We can usually establish from the lender's file whether the borrower had financial difficulties – for example:

- loan statements may show that the borrower was not able to keep up with their loan repayments
- the borrower may have asked the lender for hardship assistance because they were struggling to make their repayments.

If we cannot establish this from the lender's file, we will talk to the borrower to understand whether the loan caused them financial difficulties. We may ask the borrower for supporting information.

What happens if we uphold the complaint?

If we conclude that the lender did not meet their obligation to make reasonable inquiries and that the loan caused the borrower financial difficulties, we will encourage the parties to come to an agreed outcome that is consistent with our approach to remedies.

If an agreed outcome cannot be reached, we will make a decision on the complaint.

Our approach to remedies is set out in a separate guide.

What happens if we do not uphold the complaint?

If we do not uphold the complaint, the lender does not have to do anything to assist the borrower.

If the borrower is struggling to repay their loan, we will usually ask the lender whether they are able to assist the borrower – for example, by offering to restructure the loan so the repayments are affordable. However, we cannot require a lender to do anything to assist the borrower in these circumstances.

Who else can help?

We encourage borrowers that are struggling with debt to speak with a financial mentor.

MoneyTalks are a free service that help people and whānau with day-to-day money matters like budgeting and debt management. They can also help people and whānau find their way through processes to access government assistance and find community organisations that help people and whānau in hardship, such as food banks.

Some financial mentors also help consumers with complaints. A consumer does not need a financial mentor to use our service, but they are welcome to have a financial mentor or other support person help them with their complaint.

Case notes

The following are examples of complaints about loan affordability we have considered. Each case turns on its facts. More case notes are on our website.

I can't afford it!

Bruce borrowed money to buy a car. He subsequently surrendered the car to the lender because he could not afford the repayments. The lender sold the car and applied the sale proceeds to the loan. Bruce was left with a $20,000 debt.

Bruce complained that he was never able to afford the repayments.

We concluded that the lender did not make reasonable inquiries into Bruce's income and expenses before they approved the loan. His expenses, including his rent, were higher than what the lender had estimated. The loan application the car dealer filled out said Bruce paid $100 a week for board, but his bank statements showed that he paid $500 a week for rent.

The lender refunded all interest and fees they had charged Bruce, and they accepted an affordable repayment plan for the remainder of the debt he was left with.

Alleged irresponsible lending with no evidence of harm

Dean borrowed money to buy a car. Two years later, he complained that the loan was not affordable.

We had concerns about the lender's affordability assessment. They did not include some of Dean's expenses in their affordability assessment, and they should have asked him about his rent. The lender used half of Dean's rent when assessing the loan because he shared the tenancy with his partner, but the full amount of rent was coming from his bank account and there was no evidence his partner paid half the rent.

However, we decided that it was not fair to uphold the complaint because there was no evidence the loan had caused Dean financial difficulties. He had made his loan repayments for two years and he did not give us any evidence to show that he had suffered hardship to make the repayments.

More information

We have other consumer guides about lending on our website.

The current and past versions of the Responsible Lending Code are available in the Ministry of Business, Innovation and Employment's document library.

Consumer Protection and the Commerce Commission have information for consumers about borrowing money. This includes information about the rules lenders must follow.