



**ASIC**

Australian Securities & Investments Commission

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# **Consumer credit reporting and hardship**

## **Submission by the Australian Securities and Investments Commission**

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## A Background

### ASIC's role in regulating credit

- 1 The Australian Securities and Investments Commission (ASIC) is the national conduct regulator for consumer credit, which includes oversight of credit providers, consumer lease providers and credit assistance providers offering consumer credit products.
- 2 ASIC administers the *National Consumer Credit Protection Act 2009* (National Credit Act), which includes the following requirements:
  - (a) credit providers must meet responsible lending obligations and not enter into, suggest or assist a consumer to apply for a credit product that would be unsuitable for a consumer; and
  - (b) consumers experiencing circumstances where they consider they will be unable to meet their obligations under a credit contract can give their credit provider notice, and the consumer and credit provider may then agree to a change to the terms of the contract.

Note: The National Credit Act, including the financial hardship provisions in the National Credit Code at Sch1 of the Act, applies to both credit contracts and consumer leases. For ease of reference, in this submission:

- (a) 'credit products' includes credit contracts, consumer leases, and increases to the credit limit for these products;
  - (b) 'credit providers' includes credit providers under credit contracts and lessors under consumer leases; and
  - (c) 'consumers' includes debtors under credit contracts and lessees under consumer leases.
- 3 ASIC will also be responsible for monitoring compliance with the new mandatory comprehensive credit reporting regime as part of our broader mandate to administer the National Credit Act.

### Financial hardship

- 4 Under the National Credit Code, if a credit provider is given 'notice' by a consumer that they are experiencing financial difficulty (i.e. a hardship notice), the provider must decide whether to agree to change the contract to address the consumer's financial difficulty and what changes may be made.
- 5 If the credit provider agrees to change the contract, they must give the consumer written notice that the change has been agreed and the details of the change. If the agreement defers or reduces the consumer's obligations for

90 days or less (simple arrangement), this written notice does not have to be given to the consumer by the credit provider.

Note: Temporary relief from the requirement to give written notice about an agreed change to the terms of a contract that is a 'simple arrangement' was originally given under regs 69A and 69B of the National Consumer Credit Protection Regulations 2010 (National Credit Regulations). This relief was subsequently extended by ASIC: see [Class Order \[CO 14/41\]](#) *Extension of transitional credit hardship provisions*.

- 6 If the credit provider does not agree to change the contract, they must give the consumer a written notice that includes reasons for their decision, contact details for the Australian Financial Complaints Authority (AFCA) scheme and the consumer's rights under that scheme.
  
- 7 Since the release of [Report 152](#) *Helping home borrowers in financial hardship* (REP 152) in 2009 and reforms to hardship variations introduced by the *Consumer Credit Legislation Amendment (Enhancements) Act 2012*, we have observed general improvements in how credit providers (particularly larger banks) respond to consumers who are experiencing financial difficulty. This view is shared by other stakeholders.

Note: For example, the Financial Ombudsman Service (FOS) reports that disputes about financial difficulties continue to decline, in part, due to continuing improvements by financial service providers in managing hardship requests and customer complaints: see FOS, [2016–17 Annual review](#). Surveys by Financial Counselling Australia (FCA) in 2013, 2015 and 2017 have also found that the major banks continue to improve their response to customers in financial hardship: see FCA, [Rank the banks](#) (March 2018) (PDF file, 607 KB).

## **B Principles for an effective credit reporting system**

- 8 We consider that the following principles are integral to promoting responsible lending and facilitating an effective credit reporting system:
- (a) *Fair treatment for all consumers*—Consumers who experience financial difficulty, whether they are deemed to be in ‘hardship’ under the National Credit Code or not—should be treated fairly and not be disadvantaged (e.g. by the credit reporting system) due to the structure or categorisation of any alternative repayment arrangement.
  - (b) *Accurate credit information*—Credit providers should be given an accurate impression of a consumer’s circumstances to help them meet their responsible lending obligations.
  - (c) *Encouraging consumers to talk to their credit provider*—Consumers who are experiencing financial difficulty should be encouraged to approach their credit provider early for help in meeting their obligations under the credit product and avoiding default.

## C Repayment history information

### Key points

Under the current reporting framework, repayment history information (RHI) would be reported differently for consumers based on how their credit provider has classified their alternative repayment arrangement.

This difference in reporting means that consumers who are *substantively* in similar circumstances are very likely to be treated differently in the credit reporting system because of how they have been *formally* classified by their credit provider. This is a concerning outcome.

The requirement for reporting RHI should be amended so that this information accurately reflects the *substance* of the arrangement with the consumer.

### Credit reporting and the National Credit Code

- 9 The discussion paper distinguishes between two types of alternative repayment arrangements:
- (a) ‘permanent variations’, which seems to refer to hardship variations under the National Credit Code; and
  - (b) ‘temporary arrangements’, which seems to refer to informal forbearances and indulgences, under which the credit provider maintains that the terms of the contract have not been changed.
- 10 Temporary arrangements appear to be practices developed by credit providers, which fall outside the hardship process in the National Credit Code (either being treated as occurring before a ‘hardship notice’ is given—avoiding the procedural requirements in the National Credit Code—or after a ‘hardship notice’ is given and the credit provider and consumer do not agree to change the contract).
- Note: This kind of informal arrangement is not the same as a ‘simple arrangement’ under regs 69A and 69B of the National Credit Regulations and [CO 14/41]. Simple arrangements involve a change to the terms of the contract—the instrument merely relieves the credit provider from the requirement to give the consumer written notices that record the fact of the agreement and the details of the agreed change.
- 11 It is not clear why credit providers seek to provide informal ‘indulgences’ rather than agreeing to simple arrangements. We note that the relief for simple arrangements was given to minimise the administrative burden on credit providers in entering those arrangements.

Note: See the [Explanatory Statement to regs 69A and 69B](#) and the [Explanatory Statement to \[CO 14/41\]](#).

- 12 In our view, it is desirable for credit providers to be flexible when responding to consumers who are in financial difficulty, as this will promote fair treatment of consumers, as well as encouraging consumers to talk to their credit provider. Historically, it has not mattered a great deal in practice whether a consumer is given a permanent variation or a temporary arrangement due to how the credit reporting system works.
- 13 We have therefore not focused specifically on what hardship is in administering the National Credit Code: instead, our focus has been on encouraging credit providers to respond flexibly and fairly to consumers in financial difficulty. We do not believe there is a clear line between hardship and other forms of financial difficulty.
- 14 In our view, RHI should not be used to treat consumers differently. This is because changes to the agreed repayment arrangements of the debtor are, from the perspective of the consumer, ‘changes to the contract’ regardless of whether those changes are temporary or permanent, and whether they must be documented or not.
- 15 An arrangement that does not involve a change to the contract—for example, where a credit provider allows the consumer to meet reduced payment obligations for a period, but maintains that the consumer is in default and subject to enforcement action—is arguably unfair as it places consumers in an uncertain legal position even if they act in accordance with the agreed arrangement.

## Imbalances in the current system

- 16 As noted above, the practices that credit providers have developed do not appear to have caused significant problems for consumers. Even if an ‘indulgence’ is not treated by a credit provider as a change to the contract, consumers are not materially affected by the form of the arrangement as long as the arrangement continues and the credit provider does not start enforcement action.
- 17 However, the current framework for the credit reporting system will create an imbalance in the way repayments made under substantively similar payment arrangements are reported. This is because RHI will, under the current framework, assign different treatment to consumers in similar circumstances, depending on whether their credit provider classifies the arrangement as a hardship variation under the National Credit Code or a temporary arrangement (i.e. an indulgence).

Note: There may also be additional inconsistencies if credit providers sought to treat ‘simple arrangements’ as if they were informal indulgences, on the basis that simple arrangements are temporary (i.e. for a period not more than 90 days) and are not documented in a written notice to the consumer.

- 18 Under the current framework, RHI will reflect:
- (a) the terms of the varied contract for permanent variations; and
  - (b) guidance from the Office of the Australian Information Commissioner (OAIC) for temporary arrangements (i.e. repayments will be recorded as 'missed' if the arrangement does not state that the credit provider will postpone enforcing the original terms of the credit contract).

Note: See OAIC, [Privacy Fact Sheet 34](#) *Repayment history information and your credit report* (PFS 34).

- 19 These different classifications could result in substantially different outcomes for affected consumers as illustrated in the following examples.

#### Example 1: Credit provider agrees to a formal contract variation

Fred takes out a personal loan to make some improvements to his home. During the loan term, his car breaks down. He calls the bank to defer some of his loan repayments, so that he can afford urgent car repairs.

The bank tells Fred that he can repay a lower amount for the next two months, in exchange for higher repayments over the remaining loan term. This deferral is classified as a formal hardship variation (although it is not recorded in written notices to Fred, because it is a simple arrangement).

If Fred makes these agreed repayments, the RHI on his credit history will report that he did not miss any repayments.

#### Example 2: Credit provider grants an indulgence

Annette takes out a five-year car loan from her bank, with repayments of \$487 each month. Twelve months later, she is injured in an accident and is temporarily unable to work. Annette calls her bank to defer her repayments.

The bank tells Annette that it will be okay if she makes her next repayment one month after the original due date. The bank classifies this deferral as an indulgence.

Even if Annette makes her next repayment by the agreed time, the RHI on her credit history will likely report that she 'missed' the repayment.

- 20 In our view, consumers are unfairly disadvantaged if RHI records a repayment as 'missed' even if the consumer took positive steps to avoid missing the payment, and paid on time under an arrangement agreed with the credit provider. We also consider that recording a payment as 'missed' in these circumstances inaccurately represents actual repayment behaviour.

- 21 Consumers are likely to have little understanding of how an informal temporary arrangement would be reflected in their RHI. The Senate Economics Committee highlighted that:

Consumer representatives noted that most consumers will have limited understanding of how entering into financial hardship arrangements with a

credit provider and how their credit report may be adversely affected. This could lead to further distrust of the industry and increased complaints.

Note: See the report by the Economics Legislation Committee on the National Consumer Credit Protection Amendment (Mandatory Comprehensive Credit Reporting) Bill 2018 [Provisions], 5 June 2018 ([Senate Report](#)) at para 2.53.

- 22 If a credit provider has told a consumer that repayments can be made under an arrangement that differs from the original credit contract, whether through a change to the terms of the contract or an informal indulgence, we consider that consumers and the community would ordinarily expect that payments made on time under such an arrangement would not be reported as ‘missed’ in their RHI.
- 23 If the current system continues—under which a credit provider might record a payment as ‘missed’ even when the consumer made the payment on time under a temporary arrangement approved by the credit provider—we think the credit provider could potentially breach their obligations under the National Credit Act and the *Australian Securities and Investments Commission Act 2001* (ASIC Act) by granting such arrangements.
- 24 This is because:
- (a) the credit provider may be failing to respond to a hardship notice as required by the National Credit Code (unless the credit provider first gives notice to the consumer that a change to the contract has not been agreed, and gives reasons for that decision); and/or
  - (b) by responding to a hardship notice outside the framework in the National Credit Code, and knowing that the decision to use an informal arrangement will have a negative impact on the way the consumer’s RHI is recorded, the credit provider may be causing harm to the consumer. We consider that engaging in this conduct would be inconsistent with the ordinary expectations of consumers, and may breach prohibitions against engaging in misleading or deceptive conduct under the ASIC Act.

Note: See Subdiv D of Div 2 of the ASIC Act.

- 25 We consider that it is unlikely that a credit provider could clearly explain to consumers, consistently and in an understandable manner, that the credit provider will agree to an arrangement, and yet still record repayments as ‘missed’ even if they are paid on time under the agreed arrangement. In other words, while ASIC accepts the OAIC guidance as set out in PFS 34, we have significant doubts about whether credit providers can apply this guidance in practice in a consistent and effective manner.

## ASIC guidance on ‘hardship’

- 26 Some stakeholders have suggested that ASIC could ‘solve’ the different treatment (i.e. permanent variations vs temporary arrangements) of consumers who are in arrears by providing guidance about the concept of ‘hardship’ under the National Credit Code.
- 27 Under this view, only consumers who are ‘genuinely’ in hardship would be provided with hardship assistance (i.e. permanent variations) while those who are in financial difficulty but not in ‘genuine hardship’ may be provided with some informal repayment arrangement (i.e. temporary arrangements). It then follows (under this view), that it is acceptable for the credit reporting system to treat these two types of consumers differently.
- 28 We do not accept this view. Based on information from a recent industry workshop, approximately 90% of repayment arrangements for consumers who are more than 14 days in arrears are temporary arrangements. This means that, even if more consumers were classified as being in hardship (and therefore ‘eligible’ for permanent variations) because of ASIC guidance about the concept of hardship, a very significant number of consumers in financial difficulty would continue to be provided with temporary arrangements.
- 29 We are not confident that—even with ASIC guidance—credit providers can ensure that all consumers who may need hardship assistance will receive it. Instead, credit providers should focus on responding flexibly and fairly to all consumers in financial difficulty, rather than trying to segment them based on a technical view of what is hardship under the National Credit Code.

## RHI to reflect the actual arrangement

- 30 We consider that legislative changes are necessary for RHI to accurately reflect the arrangement that has been agreed to with the consumer.
- 31 We think that RHI should record payments as being met if a consumer is making repayments under any arrangement, where an ‘arrangement’ can be:
- (a) a temporary arrangement (e.g. an indulgence or forbearance);
  - (b) a change to the contract under the hardship process set out in the National Credit Code that is agreed to and described in written notices to the consumer;
- Note: See s72(4) and 73(1) (for credit contracts) and s177B(4) and 177C(1) (for consumer leases).
- (c) a change to the contract under the hardship process that is a ‘simple arrangement’ (i.e. that is not required to be documented in a written notice to the consumer);

- (d) a change to the contract that is agreed to under provisions other than the hardship process (e.g. a change which defers or reduces the obligations of the consumer for a specified period), whether or not that change is required to be documented in a written notice; or

Note: See s71 (for credit contracts) and s177A (for consumer leases).

- (e) a change to the contract unilaterally made by the credit provider under other Code provisions outside the hardship process (e.g. a change that reduces the repayment obligations of the debtor, or extends the time for payment, under the contract).

Note: See s65 (for credit contracts).

- 32 We consider this change could be achieved by amending the definition of ‘due and payable’ in s6V of the *Privacy Act 1988* (Privacy Act). The Economics Legislation Committee has highlighted that:

A number of inquiry participants expressed concern that they thought [the credit reporting system is] without clear legislative provision as to how credit providers must report repayment history information where a customer has entered into a financial hardship agreement with the credit provider.

Note: See [Senate Report](#) at para 2.48.

- 33 For example, a notation to s6V(1) could state that, when an arrangement is in place, a payment is to be considered ‘due and payable’ by reference to that arrangement instead of under the original contract.

## D Hardship indicators

### Key points

Credit reports should include accurate information about hardship arrangements so that credit providers can better assess whether the proposed credit products are unsuitable.

This could be achieved by introducing two indicators:

- an indicator to show when a consumer has given 'notice'; and
- an indicator that reflects an arrangement has been entered into to help a consumer meet their repayments.

### Why hardship indicators should be introduced

#### Responsible lending

- 34 There is overall agreement among participants in the credit reporting system that comprehensive credit reporting should help Australian credit licensees (licensees) meet their responsible lending obligations.

Note: See [Senate Report](#) at para 2.10.

- 35 As well as the proposed changes to RHI (see Section C), including hardship indicators would allow licensees to differentiate between consumers who:
- (a) made a payment on time under their original contract;
  - (b) missed a payment under their original contract without an arrangement;
  - (c) made a payment on time under an arrangement; or
  - (d) missed a payment under the arrangement.

- 36 This would also help licensees in identifying where additional inquiries should be made and assessing whether a new credit product would be unsuitable for the consumer. We consider that this would enhance the ability of licensees to lend responsibly.

Note: See [Senate Report](#) at paras 2.59–2.61 for similar views expressed by the Australian Banking Association and Westpac.

- 37 We consider that credit reports should include accurate information about hardship arrangements so that licensees can better assess the proposed credit. This could be achieved by introducing indicators to show if:
- (a) a consumer has given 'notice' that they are experiencing financial difficulty and their credit provider is deciding whether to agree to an arrangement; or
  - (b) an arrangement has been entered into to help a consumer meet their repayments.

## Access to credit

- 38 The responsible lending obligations prohibit licensees from entering into, suggesting or assisting a consumer to apply for a credit product that is unsuitable for the consumer (e.g. where the consumer does not have the capacity to meet repayments required by the contract).
- 39 Consumer advocates have raised concerns about hardship indicators because a signal that the consumer has, or is, experiencing financial difficulty may restrict the consumer's ability to access credit under a new product.
- 40 We recognise that including hardship indicators may in some circumstances lead a licensee to refuse a credit application where the application would have otherwise been accepted. However, in our view, consumers would not be unfairly disadvantaged by changes that result in a credit reporting system that more accurately portrays a consumer's credit history.
- 41 The presence of an indicator should not lead a licensee to automatically refuse to offer a proposed credit product. An indicator, by itself, does not contain sufficient information for a licensee to draw conclusions about the extent to which a proposed credit product would be unsuitable.
- 42 We consider that the presence of an arrangement indicator should prompt a licensee to make additional inquiries about the circumstances surrounding the consumer's financial difficulty. These additional inquiries may include:
- (a) details of the consumer's changed circumstances that led to the arrangement;
  - (b) whether those circumstances have been addressed or are continuing;
  - (c) how long the revised repayment obligations will continue; and
  - (d) the likelihood that the circumstances which led to the arrangement will occur again.
- 43 We understand that many tools for credit providers to make decisions about credit are substantially automated. If an indicator appears on a credit report, any additional inquiries may need to be conducted manually.
- 44 These inquiries should allow licensees to better understand the consumer's current financial position, leading to a more informed assessment. This would be beneficial for both licensees and consumers.
- 45 The introduction of Open Banking means that credit providers can also contextualise these inquiries against a consumer's broader transaction history. On 9 May 2018, the Government announced that it will phase in Open Banking from 1 July 2019.

## Termination of credit contracts

46 We understand that consumer advocates are concerned that if a licensee has provided credit to a consumer and discovers that hardship information has been subsequently reported on the consumer's credit history, the licensee may cancel existing credit contracts with the consumer. In our view, this would be unacceptable.

47 The Privacy Act prohibits credit providers from using or disclosing credit information, except in specific circumstances and for specific purposes. Permitted purposes include, but are not limited to, 'processing an application for credit made to the credit provider' and 'assisting the consumer to avoid default'.

Note: See Privacy Act, s21G and 21H (item 5).

48 It may be necessary to consider whether changes to these protections are required to prevent the use and disclosure of credit information for inappropriate purposes.

## Use of hardship information more broadly

49 We consider that the restrictions which apply generally to the use and disclosure of credit information should also apply to hardship indicators.

## How hardship indicators could work

50 When and how hardship indicators operate would need to be closely examined. We suggest the following:

- (a) *Indicators should be promptly recorded*—Ensuring that credit providers record indicators in credit reports in a timely manner will:
  - (i) improve incentives for consumers to actively manage missed repayments and contact their credit provider early; and
  - (ii) give prospective credit providers up-to-date information about the consumer's circumstances to help them meet their responsible lending obligations.
- (b) *Indicators should only appear once*—The indicator would only be recorded when a relevant event occurs. If indicators appear in each month that the arrangement is in place, this may discourage consumers from seeking long-term arrangements or contract variations.
- (c) *Indicators should be kept on credit reports*—The retention period should be consistent for indicators and RHI. This means credit reports would remain accurate and give prospective credit providers a full

picture of the consumer's credit history. This is unlikely to unfairly disadvantage consumers because:

- (i) indicators should be treated as a prompt for prospective credit providers to make additional inquiries about the consumer's current financial position, not as a conclusive indicator that a new credit product would be unsuitable for the consumer; and
- (ii) as with default information, the impact of indicators on a consumer's overall credit score will decrease over time.

51 We consider that information about the reasons for a consumer's hardship should not be captured in credit reports. This is because:

- (a) there may not be a single event that has led to a consumer's hardship and it may be difficult to categorise;
- (b) credit information needs to be accurate and this may create an unreasonable expectation on credit providers to verify the reasons for hardship;
- (c) prospective credit providers may not be able to rely on the information, as they have no oversight or knowledge of how the previous credit provider collected and verified the information; and
- (d) an obligation to record reasons may increase the administrative cost and complexity of granting an arrangement, reducing the incentive for credit providers to offer an arrangement.

## Key terms

Term	Meaning in this document
AFCA	Australian Financial Complaints Authority
AGD	Attorney-General's Department
ASIC	Australian Securities and Investments Commission
ASIC Act	<i>Australian Securities and Investments Commission Act 2001</i>
[CO 14/41] (for example)	An ASIC class order (in this example numbered 14/41)
consumer	A natural person or strata corporation  Note: See s5 of the National Credit Act. In this submission, this includes debtors under credit contracts and lessees under consumer leases.
credit or credit product	Credit to which the National Credit Code applies  Note: See s3 and 5–6 of the National Credit Code. In this submission, this includes credit contracts, consumer leases, and increases to the credit limit for these products.
credit assistance provider	A person who provides credit assistance to a consumer and who is not the credit provider
credit provider	Has the meaning given in s5 of the National Credit Act  Note: In this submission, this includes credit providers under credit contracts and lessors under consumer leases.
discussion paper	The discussion paper on consumer credit reporting and hardship issued by the Attorney-General's Department
FCA	Financial Counselling Australia
FOS	Financial Ombudsman Service
hardship notice	Has the meaning given in s72(1) and 177B(1) of the National Credit Code
licensee	A person who holds an Australian credit licence under s35 of the National Credit Act
National Credit Act	<i>National Consumer Credit Protection Act 2009</i>
National Credit Code	National Credit Code at Sch 1 to the National Credit Act
National Credit Regulations	National Consumer Credit Protection Regulations 2010
OAIC	Office of the Australian Information Commissioner
Privacy Act	<i>Privacy Act 1988</i>

Term	Meaning in this document
reg 69A (for example)	A regulation of the National Credit Regulations (in this example numbered 79A)
REP 152 (for example)	An ASIC report (in this example numbered 152)
responsible lending obligations	The obligations under Ch 3 of the National Credit Act
review	The review of financial hardship arrangements by the Attorney-General's Department
repayment history information (RHI)	Has the meaning given in s6 of the Privacy Act
s160F (for example)	A section of the National Credit Act (in this example numbered 160F)
<a href="#">Senate Report</a>	The report by the Economics Legislation Committee on the National Consumer Credit Protection Amendment (Mandatory Comprehensive Credit Reporting) Bill 2018 [Provisions], 5 June 2018