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27 June 2018

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Dear Mr Minihan

Consumer Credit Reporting and Hardship

The Australian Finance Industry Association [AFIA] welcomes the opportunity to comment on the Attorney-General Department's discussion paper *Consumer Credit Reporting and Hardship*. Thank you also for the additional time provided to finalise our feedback.

AFIA Background

AFIA is well placed to advocate for the finance sector given our broad and diverse membership of over 100 financiers operating in the consumer and commercial markets through the range of distribution channels (including digital access). AFIA membership also includes the three largest consumer credit reporting bodies [CRBs] operating in the Australian market. More detail on AFIA is available from: www.afia.asn.au.

A significant number of our Members in both the consumer and commercial finance markets rely upon services provided by (consumer) credit reporting bodies (CRBs) as permitted by the (Cwlth) Privacy Act to facilitate access to finance underpinned by sound credit assessments. We anticipate that this will increase following the Government's decision to mandate comprehensive credit reporting [MCCR], the enactment of legislation to implement and disclosure of consumer credit account data (including repayment history information [RHI]) to the CRBs by the regulated entities.

What is the issue?

In AFIA's view, the current framework provided for in the Privacy Act (in particular Part IIIA and related regulations and Privacy Credit Reporting Code [credit reporting provisions]) to regulate the consumer credit reporting system does not provide sufficient compliance certainty to deal with an important issue relating to the exchange of information about a credit account where the customer experiences financial difficulty that impacts the ability to meet the contractual obligations.

More specifically, how the credit reporting information permitted to be collected and disclosed by a CRB includes information that a customer has experienced financial difficulty that impacts his or her ability to service repayments in line with the terms or schedule originally agreed under their consumer credit contract or consumer lease (generally badged 'financial hardship') and the credit provider has agreed to change that repayment arrangement to assist the customer 'get back on track' and pay what is contractually-owed.

The lack of certainty creates difficulty for all; customers, industry and regulators alike.

The need for resolution has become critical because of the shift of policy that sees the choice previously available to the largest Australian consumer credit providers of whether to disclose credit information into the credit reporting system potentially replaced with a statutory obligation mandating disclosure. The outcome will have flow-ons with other credit providers choosing to participate to be able to access data of significant relevance to credit-decisions and being bound to disclose credit information of their own customers under the reciprocal arrangement that underpins the system. This statement is not a criticism of the policy, but the identification of the reason why it has become essential for this matter to be clarified.

The issue is complex because of the interplay between the Privacy Act's credit reporting provisions, the statutory hardship right provided for in the National Consumer Credit Protection Act [NCA] including variation in terminology between the two Acts. At a more practical level because of the broad range of financial difficulty circumstances that may see a customer needing to work with provider. For our members that are Approved Deposit-Taking Institutions (ADIs eg banks, credit unions) it is further compounded by prudential risk guidance from APRA¹ requiring ADIs to have a full understanding of the risk profile of loans granted hardship forbearance to ensure the risks are appropriately reflected in internal management reporting, provisioning and capital adequacy calculations. The outcome is tension between the APRA reporting and credit reporting that requires clarity and consequently a black or white numeric approach to deal with financial difficulty situations which are highly complex and warrant more than a black or white response.

We welcome the Government's decision for the Attorney-General to review the operation of 'hardship arrangements' in the context of the Privacy Act's credit reporting provisions. We look forward to working with the Government to implement a solution to address this issue for the benefit of all participants in the consumer credit reporting system; consumers, regulators (OAIC / ASIC) and industry alike.

¹ Letter from APRA to ADIs 8 August 2012 [Regulatory Reporting of Loans Where Hardship Concessions Are Granted](#) and APRA Prudential Standard [APS 220 Credit Quality](#) (APS 220) and the associated Guidance Note [AGN 220.1 Impaired Facility Definitions](#)

Reporting Financial Difficulty – AFIA Position - Summary

It is critical for the sake of both consumers and credit providers alike that the consumer credit reporting system is an accurate, complete and up-to-date record of the permitted credit-worthiness data sets to facilitate good lending decisions. The 2014 changes to permit more data (eg current account information and RHI) facilitate better decisions with these datasets enabling more sophisticated analysis of credit-worthiness which will impact on access or availability and price.

The fact that a customer is experiencing (or has experience) financial hardship with a current consumer credit account is important information to be shared in the consumer credit reporting system for both customers and industry.

Equally, it is imperative that a customer in financial difficulty should raise this with the credit provider to enable a resolution to be agreed; an outcome that is beneficial to both the customer and provider. The sooner a consumer flags the problem the better for all involved. The importance of this is underpinned by the statutory right given to a consumer to seek variation of the contract where they experience financial hardship that has been included in consumer credit laws for several decades, most recently in the National Consumer Credit Protection Act [NCA]. We support a solution with the credit reporting exchange that does not detrimentally impact a customer in financial difficulty raising this at the earliest opportunity with the credit provider to facilitate early resolution.

The credit reporting system enables a process for a customer that has experienced financial difficulty and worked with their credit provider to continue to meet their contractual obligations to benefit from having this recorded and available through the credit reporting exchange to other credit providers considering a future application.

For the customer in financial difficulty it ensures information relevant to a credit assessment is available that will assist responsible credit-decisions and minimise the potential for further credit to be extended increasing the financial difficulty.

Other customers that have not experienced financial hardship (statistically the greater proportion) also benefit by inclusion of this information in the system. In the absence of the reporting of financial hardship information, the default position of a credit provider considering an application for credit from a customer would be to have to assume that the customer may have experienced financial hardship with their credit facilities in the past. This will impact serviceability assessments with the outcome some of those customers will be declined credit or pay more for it than had the 'true' position across the customer demographic been reported.

The fact that a customer has experienced financial difficulty that has impacted their ability to service a current credit account does not automatically mean that he or she will never be approved further credit going forwards. A credit-assessment takes into account a range of factors collectively grouped as: capacity, character, collateral, capital and conditions. Financial difficulty indicates the customer's capacity to service the repayments has been challenged. However, should the customer work with the credit provider to overcome the financial difficulty and get 'back on track' this is relevant to 'character' and will be taken into account in future credit decisions.

The key factor that distinguishes 'financial hardship' from other situations of non-payment/account work-out (eg where a customer is able to repay but chooses not to) is something has occurred that is outside the customer's control and has impacted the income available to service the payments owing to their credit provider under the credit contract. There is a broad spectrum of 'hardship' factors including: unemployment, illness, relationship breakdown, family addition through to natural disaster.

It may also be a one-off unplanned for event that sees income budgeted to service the credit having to be diverted to another purpose (eg to pay for a replacement of a fridge or washing machine or car maintenance in the event of breakdown). Prior to the 2013 Enhancement Amendments to the NCA hardship provisions the 'hardship factors' on which a consumer could look to use their statutory right to see contract variation on the basis of hardship were very narrow, limited to unemployment and illness, for example. It was however always open for a customer to approach the provider and negotiate a change to their contract in other circumstances. The 2013 Enhancement Amendments to the NCA looked to remove the prescription and reflect the practice. The outcome no longer limits a consumer seeking variation on the basis of financial hardship limited to specific 'hardship factors.' This outcome was also supported by a framework that recognised for some 'simple' situations, for example where a negotiated outcome could get the customer back on track within a short-term (eg 90 days) a less prescriptive process was warranted than for situations that required a longer-term solution. For these 'simple arrangement's this removed the need for the more formal 'written' notifications. We highlight this because it adds to the complexity of the credit reporting treatment of hardship.

In part the complexity arises because the solution to assist a customer overcome financial difficulty to 'get back on track' to meet their contractual obligations in a credit contract or consumer lease will largely depend on his or her particular circumstances and also the internal policies and risk management requirements of each credit provider. A solution offered to one customer may differ from that offered to another with the same product. Further a solution offered to a customer may not be the same that would be offered to that customer if a different credit provider had extended the finance. This is because credit

providers may assess credit risk differently depending on variables (eg funding sources, customer demographics, ASX public listing).

With this background, AFIA acknowledges that the solution to share in the credit reporting system information that a customer is (or has) experienced financial hardship:

- has to take into account the individualised customer circumstances;
- but to achieve the policy objective that underpins the consumer credit reporting system as a centralised repository of current and historic fact, the credit reporting process has to include information about the customer's financial difficulty in a way that facilitates consistent (and consequently fair) treatment in how it is reported by credit providers for the benefit of all participants in the consumer credit reporting system; customers, regulators and industry alike.

A more detailed analysis of AFIA's position and proposed solution follows.

AFIA Proposed Solution

1). The purpose of the credit reporting system

In line with Parliament's intention with the enactment of revised Privacy Act Part IIIA as noted in the Explanatory Memorandum that accompanied its passage, AFIA views the purpose of the credit reporting system to be both a current and historic record of fact held by an entity (a credit reporting bureau) designed to assist lending decisions for the benefit of both lenders and consumers.

The Australian Law Reform Commission in its 2008 Report noted that "*the role of a credit reporting agency is to provide rapid access to accurate and reliable standardised information on potential borrowers*". This information, as was noted in the Report, will reduce asymmetrical information between credit providers and borrowers. This allows credit providers to appropriately assess the provision of credit to potential borrowers.

The case for permitting more data in the consumer credit reporting system [**comprehensive credit reporting**] has been well-made and is reflected in the enactment of revised Part IIIA in March 2014. Under comprehensive credit reporting, the inclusion of current account information and RHI, for example, means borrowers are able to have key information available in the system that demonstrates to a credit provider considering an application the borrower's credit worthiness; both in relation to their capacity to repay and their character (current or historic). Borrowers with a good credit history and an exposure to an amount of credit that they are currently servicing well will be able to seek out credit (either refinanced or new) on more favourable terms. This contrasts to a system that only permits negative information to be included.

Reporting of more comprehensive information (including RHI) will also allow a customer's new application for credit to potentially be considered favourably after a negative event (like a default) by re-establishing credit worthiness more quickly than would have occurred in a negative-only system. More comprehensive information (including RHI) enhances the credit reporting system by facilitating a more holistic record of the customer's particular credit-worthiness circumstances on both a current and historic basis.

2). The current deficiency in not reporting financial difficulty

AFIA Members and other credit providers regularly work with a customer when he or she experiences periods of financial difficulty to provide a way for the customer to 'get back on track'. Members understand that it is in their interest to work with their customers in situations of financial difficulty, both from a commercial perspective and more broadly to meet community expectations.

As outlined in the Discussion Paper, under the NCA, in particular the National Credit Code [NCC] (sections 72 – 75 + [ASIC Class Order 14/41](#)), debtors have a statutory right to hardship assistance. All AFIA members support this process and want to work with customers who are experiencing financial difficulty to get back on track.

The area of financial hardship management under consumer credit contracts is complex both as an internal company policy of the credit provider but also in terms of imposing regulatory obligations on a credit provider. This is heightened because of the emotive circumstances in which it likely arises (e.g. unemployment, death, illness, relationship breakdown) are generally beyond the control of the customer, which in turn necessitate particular resolution skills on the part of the case manager. AFIA notes that Members use an array of solutions to assist customers in hardship, which depends on the circumstances of each individual situation – there is not a 'one-size-fits all' approach for hardship management. The key issue is working with the customer to assist them continue meeting their contractual obligations and if this requires modification of the contracted repayment arrangements, the provider will be open to this outcome.

The approach to how the contractual arrangement is 'modified' will vary (both in its terms (eg whether moratorium on enforcement for a short term, capitalisation of overdue/interest and extension of term), but potentially also in its manner (eg formal vs informal)) subject to the individual's particular circumstances and whether a short-term or longer-term solution is warranted.

Under the credit reporting provisions currently in place (including Part IIIA, credit reporting regulations and Privacy (Credit Reporting) Code), the fact that an account is subject to this sort of 'hardship arrangement' is not specifically permitted 'credit information' to be able to be exchanged in the credit reporting system.

As outlined in the discussion paper, up until 4 years ago, comprehensive credit reporting had been expressly prohibited since 1992. The 2013 amendments, through the introduction of a new Part IIIA, introduced a new comprehensive credit reporting system. However, the amendments did not specifically cater for the formal notification or exchange of information that a customer is (or has) experienced financial hardship.

The 2013 amendments allows new information about an individual's repayment history information (RHI) to be reported. This information shows whether or not the individual has met or is meeting their obligations under the credit contract for a particular month.

RHI is defined by subsection 6V(1) of the Privacy Act. For an individual to meet a commitment for a particular month the individual must meet their obligation to make a monthly payment that is due and payable in relation to the consumer credit. Critical to the assessment of RHI is what is 'due and payable' under the consumer credit contract or consumer lease. While the Privacy Act Regulations and the Privacy (Credit Reporting) Code 2014 provide further guidance on RHI it does not provide further guidance on the meaning of 'due and payable'.

The OAIC has published guidance to assist industry to understand the meaning of due and payable (see [here](#)). The guidance demonstrates that where there has been a variation to the terms of the consumer credit contract, 'an assessment of whether RHI is due and payable should be by reference to the terms of the varied contract'. This means where a consumer's credit contract has been varied then what is reported as RHI should be in respect to the variation. That is, if the consumer meets their varied commitments they will be considered up to date and meeting their monthly payment that is due and payable.

In the absence of the report reflecting the financial difficulty management, participants in the credit reporting system have no knowledge of the fact that the consumer is meeting their repayments but only because the repayments have been managed by the consumer credit provider in a way that assists overcome the financial difficulty that the customer has experienced.

To ensure integrity of the system and for it to achieve its overall policy objective, a credit report should not display a pattern of historic repayment that shows a consumer that has experienced financial difficulty but subsequently paid down arrears because of a windfall financial gain (e.g. through winning the lottery) being

reported the same as one that has paid down arrears through financial hardship management assistance offered by the credit provider.

The omission of reporting customers in hardship devalues the credit reporting process. Reporting these two very different situations in the same manner creates the environment for AFIA members and other incoming financiers to provide finance to customers in financial difficulty with the flow on detrimental financial impacts for those customers.

3). The benefits for consumers and credit providers in reporting financial difficulty

Reporting of instances of financial hardship will provide benefits to consumers and credit providers. More accurate data will lead to better credit decisions.

Customers will be protected as credit providers will have additional information when performing due diligence so to not inadvertently exacerbate a customer who is experiencing financial difficulty.

Showing periods of financial difficulty where there has been positive payment behaviour will allow future credit providers to understand this period of difficulty has passed and has since performed strongly.

Showing the period of difficulty can be explained and the consumer has since exhibited positive payment behaviours (paying on time and reducing the delinquency) demonstrates that the consumer's period of difficulty is over and is rehabilitated.

For customers that have not experienced financial difficulty (statistically the greater majority), credit providers will be able to with confidence consider their credit reporting information in the firm knowledge that the absence of hardship arrangement information is not because the system does not allow it to be reported, but because the customer has a clear, credit history,

4). Principles to report financial difficulty and proposed AFIA solution

We believe that a balance can be achieved that operates to ensure the customer uses their statutory financial hardship right and the credit reporting system is able to reflect the outcome to ensure prudent lending decisions that appropriately take note of the customer's particular financial circumstances going forward.

A solution to flag or indicate financial difficulty will work best and benefit both consumers and credit providers where it:

- a) ensures that the credit reporting system is a record of fact with information held for a reasonable period to facilitate good lending decisions;
- b) ensures that the recording of financial difficulty in a customer's credit file is treated fairly and reasonably – that it accurately reflects the customer's position
- c) utilises a 'bright line' test – this will ensure reporting is simple and remove any regulatory uncertainty for when credit providers should record financial difficulty, it will also facilitate consumer understanding of reporting this information
- d) interact appropriately and be aligned with the already existing repayment history information data field, this will ensure indicating financial difficulty and recording RHI is meaningful and a rich data source
- e) it retained as a 'historic' record and cannot be retrospectively changed (unless to comply with other obligations like to ensure data is accurate for example obligations in sections 20S, 20T, 21U, or 21V of Division IIIA the Privacy Act that allows for the correction of credit reporting data)
- f) does not impact a credit providers ability to flexibly work with their customers experiencing financial difficulty.

In line with the principles discussed above AFIA proposes that the credit reporting system should facilitate the reporting that fact that a customer is (or has) experienced financial difficulty.

The solution should have the following features:

- i. record that fact that a customer is (or has been) in financial difficulty warranting modification of the contract in the credit reporting system where there has been an agreement that will substantially change the terms (in particular repayments) of the original agreement (a bright line test). In line with the 'simple arrangement' a solution based around a 90 day period may be suitable. For example, if the modification will change the contract for a period longer than 90 days the credit provider should be able to disclose that fact to a CRB and have notified to other inquirers that the account is subject to an 'Arrangement'. This could be used in a range of situations where a contract is modified beyond the statutory hardship scenarios.
- ii. the record would complement RHI reporting. That is, a record of a customer's account being subject to an 'Arrangement' should not mask RHI reporting but sit alongside it. Where the account is reported as subject to an 'Arrangement' the manner in which RHI would be reported would reflect the contract as varied. This will allow credit providers to see positive behaviours where a customer is meeting their varied obligations and getting 'back on track'.
- iii. be retained for a reasonable period of the financial difficulty on a consumer's credit file.
- iv. credit accounts where the full balance owing has been accelerated should be excluded from reporting hardship information. The Australian credit reporting provisions do not appear to deal

appropriately with accelerated and assigned debts. In many if not all cases, involve a consumer who is in financial hardship. In these situations, credit providers work closely with these customers and are frequently making new or amending agreements with them in light of their financial difficulty. It would not make sense to require hardship information to be recorded in respect of these accounts. It would also create a compliance burden as the credit provider would be constantly updating the credit file to reflect where a new or amended agreement to vary the credit contract has been reached.

We believe our proposed solution would address the issue relating to reporting instances where the customer experiences financial difficulty. We believe that our solution would achieve a balance that will ensure the customer can use their statutory financial hardship right and the credit reporting system is able to reflect the outcome to ensure prudent and responsible lending decisions.

As discussed above, a record of an account being subject to an 'Arrangement' will make RHI much more meaningful and will allow a customer to demonstrate positive behaviour more quickly following a hardship event. A customer that has been in financial hardship and worked with their credit provider to continue to repay is substantially more likely to be offered credit in the future than one that has stopped paying and had recovery action taken. For others that have not had to deal with financial difficulty, their sound management of credit will also be enhanced by this outcome.

Next steps

We look forward to engaging with you further on this issue. We would welcome the opportunity to meet with to discuss our proposal further and discuss next steps.

Should you wish to discuss our submission further, or require additional information, please contact me at helen@afia.asn.au or Alex Thrift, Economic & Policy Senior Adviser at alex@afia.asn.au or both via 02 9231 5877.

Kind regards

A handwritten signature in black ink, appearing to read 'Helen M. Gordon', with a horizontal line underneath.

Helen Gordon
Chief Executive Officer