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Re: Submission to Review of 'Consumer credit reporting and hardship'

The Westpac Group (**Westpac**) welcomes the opportunity to contribute a submission regarding how financial hardship arrangements are reflected in the credit reporting system (**the Review**). We thank the Government for agreeing to the Review which we hope will result in much-needed clarity on the reporting of hardship into the future. We are members of both the Australian Banking Association's and the Australian Retail Credit Association (**ARCA**) and we have been actively involved in discussions with both in relation to this review.

For over 20 years Westpac has been providing financial assistance to customers in hardship through our hardship programs, ensuring vulnerable customers get the best financial support. The Assist Group's Solution Specialists assess customers' individual situations, and provide personalised assistance, information and solutions to help customers manage their financial obligations with Westpac during their time of financial hardship. In the last year, we have supported around 40,000 customers with hardship arrangements.

Westpac supports the introduction of the mandatory Comprehensive Credit Reporting (**CCR**) scheme, which will provide long term benefits for both customers and credit providers (**CPs**). Westpac believes that customers will benefit because CCR will result in credit being accessible to more customers, as CPs develop a deeper understanding of a customer's creditworthiness and individual circumstances. CCR will give CPs access to additional information to make a more robust assessment of credit risk and complement responsible lending obligations. We also note the Explanatory Memorandum to the *Privacy Amendment (Enhancing Privacy Protection) Bill 2012 (Amendment Act)* concluded that the addition of repayment history as part of CCR information will provide CPs with "the opportunity to access enhanced information to establish an individual's credit worthiness. It is expected that this will allow more robust assessments of consumer credit risk, both in the market as a whole and in relation to individual applications, which can assist with responsible lending and potentially lead to lower consumer credit default rates."¹

We note that the Review is not a general review of Repayment History Information (**RHI**), but instead its interaction with 'hardship arrangement information'. Nonetheless we make a series of short points below to echo those points made in the introduction of the consultation paper as a platform to Westpac's argument.

¹ Explanatory Memorandum, p. 29

As the Australian Law Reform Commission (**ALRC**) points out, credit reporting can be seen as “facilitating responsible lending”. That is, the information provided by credit reporting to CPs may help to prevent individuals becoming financially overcommitted”.² As the Review points out, the ALRC recommends including RHI in CCR due to its predictive value.³ Our own analysis of de-identified sample data available to us has indicated that applicants with RHI showing current arrears levels greater than two payments are more than nine times more likely to default on a subsequent credit card account.

Background

Prior to the amendments to the *Privacy Act 1988* (**Privacy Act**) in 2014 which introduced voluntary comprehensive credit reporting, the Australian Prudential Regulation Authority (**APRA**) published Prudential Standard APS 220 Credit Quality (**APS 220**) in relation to how authorised deposit-taking institutions (**ADIs**) must control their credit risk through appropriate risk management policies and procedures. One of the key requirements of this Prudential Standard relates to reporting of impaired facilities. On this requirement Westpac has received guidance from APRA that specifies loans under hardship arrangements may not be returned to non-impaired status (or restructured) until the loan has been fully performing under the agreed terms for at least six months or three payment cycles (whichever is greater).⁴

However, under the mandatory CCR scheme, CPs will be required to report RHI in accordance with section 6V of the Act, Regulation 12 of the Privacy Regulation, and paragraph 8 of the Credit (Privacy Reporting) Code 2014 (**CR Code**). Under the mandatory CCR scheme, CPs will not have the option to withhold the fact that customers have not met repayments in accordance with their contract. In the case where a customer has been granted a hardship arrangement under section 72 of the National Credit Code (**NCC**), the contract is considered to have been varied. Following regulatory guidance provided by the Office of Australian Information Commissioner (**OAIC**), Westpac will be required to report what is ‘due and payable’ in relation to the terms of the varied contract. For other scenarios that fall outside of hardship arrangements, CPs may sometimes grant temporary arrangements (also known as an indulgence or forbearance) without varying the original credit contract. The OAIC’s guidance notes that what is ‘due and payable’ depends on the nature of the arrangement.⁵

Whilst APRA guidance predates the amendments to the Privacy Act in 2014 and pertains to the measurement and reporting of impaired loans (rather than an ADI’s management of lending relationships with borrowers), the mandatory CCR scheme gives effect to a parallel reporting mechanism for CPs who are also ADIs. This disconnect between regulatory requirements is unfortunate (see below).

² Australian Law Reform Commission, *For Your Information: Australian Privacy Law and Practice*, Report No 108, 2008, p. 1709

³ Attorney-General’s Department, *Consumer credit reporting and hardship*, Discussion Paper, 2018, p. 4

⁴ APRA letter to ‘All Authorised Deposit-taking Institutions’ 8 August 2012, p. 2

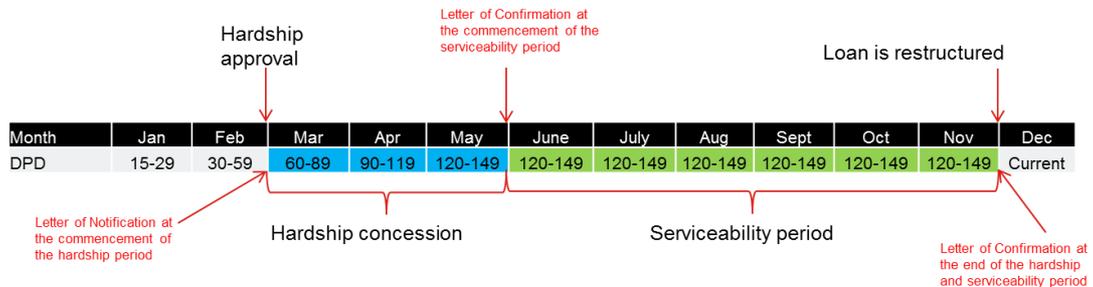
⁵ Attorney-General’s Department, *op. cit.*, p. 9

Question 1

Is there sufficient certainty in how the forms of hardship arrangements discussed in this paper are currently treated in relation to consumer credit reporting? If not, what are the imbalances that are evident in the current system? That is, what are the reasons for change and why should hardship arrangements be included in the credit reporting system?

The imbalance in the current system is due to the different objectives of the Credit legislation, the Privacy Act and APS 220. The Credit legislation is designed to manage how CPs provide credit, and the credit reporting provisions in the Privacy Act are designed to be reported based on the facts (matter of fact). APS 220 requires ADIs to manage credit risk by adopting prudent credit risk management policies and procedures to recognise, measure, report and provision for impaired facilities.

ADIs reporting RHI for hardship arrangements under APS 200



Non-ADIs reporting RHI for hardship arrangements

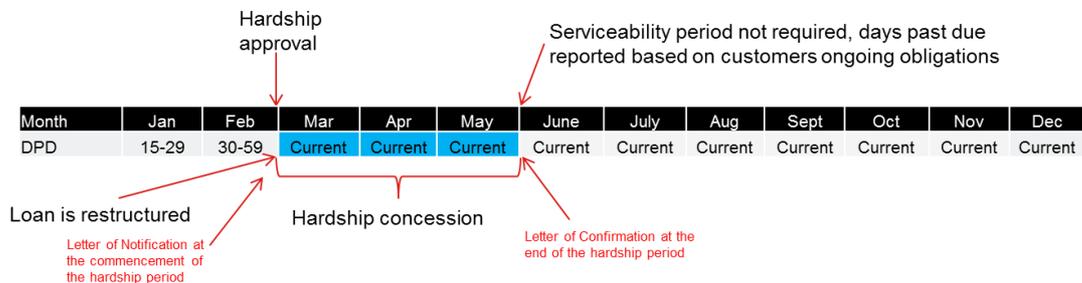


Figure 1: the disjuncture between APS 220 and the framework proposed by the CCR system creates system problems for ADIs

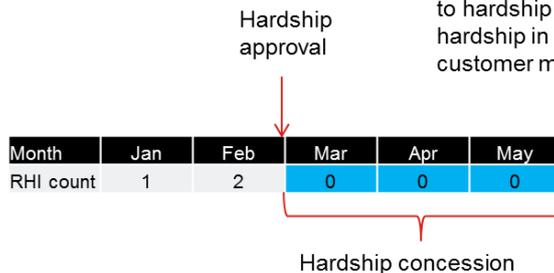
Specifically, in the context of hardship arrangements, APS 220 requires ADIs to continue to age the debt until the customer has met (the greater of) their contract obligations for six months or satisfy three payment cycles. APRA has set the standard for a serviceability period which ensures the customer is capable of fully servicing all their future obligations in a timely manner under the facility. On the other hand (and in the same context of hardship arrangements), the Privacy Act and the Credit legislation requires ADIs to report RHI as being ‘reset’ to the varied contract obligations.

ADIs do not have two sets of ledgers that monitor account performance and reporting repayment history information to credit reporting bodies (CRBs). Therefore, to ensure the integrity of ADI reporting systems, Westpac supports legislative change to allow for one consistent reporting scheme. Non-ADIs will not have

to grapple with such imbalances in their reporting systems because they are not required to abide by APS220 (see Figure 1 above).

Scenario 1a: Customer in hardship

In this scenario the customer misses two monthly payments due to hardship (e.g. loss of job), applies for and is approved for hardship in March. The RHI is reset to 0 (up-to-date) whilst the customer meets the obligations of the new terms of hardship.



Scenario 1b: Customer able to pay

In this scenario the customer misses two monthly payments due to an overseas trip, has the ability to pay and pays arrears in full in March. The RHI is reset to 0 (up-to-date) in March as all of the arrears were paid.

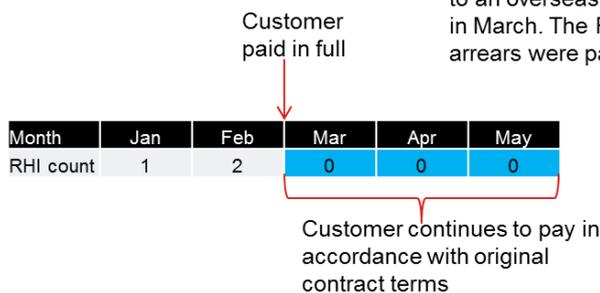


Figure 2: showing customer in hardship arrangement and a customer who is able to pay

As the consultation paper outlines, the Privacy Act does not provide for the reporting of Hardship agreements in the credit reporting system. Given the above disconnect with regard to the reporting of hardship information, Westpac seeks legislative change to the CR Code to allow for a hardship arrangement to be clearly identified. This is in the best interest of customers. Currently, the framework does not allow CPs to differentiate between a customer who is experiencing Hardship and other customers.

For instance, a customer who has been granted a hardship arrangement under s72 of the Credit legislation (e.g. because of illness or unemployment) after missing two payments may be reported as up-to-date under CCR; which will exactly mirror a customer who has not suffered hardship but has missed two payments due to other circumstances (e.g. away on holiday). The impact of this is a real risk that the customer in the first scenario would be approved a loan from a new lender because that customer would appear as if they are up-to-date and in a healthy financial situation. Figure 2 illustrates how this will appear in the credit reporting system.

The scenarios in Figure 2 illustrates the need for a hardship indicator to meet the policy intent of the *National Consumer Credit Protection Amendment (Mandatory Comprehensive Credit Reporting) Bill 2018 (the Bill)* which, according to the Explanatory Memorandum, seeks to “correct for information asymmetry

[and...allow] CPs to obtain a comprehensive view of a consumer's financial situation, enabling a provider to better meet its responsible lending obligations."⁶

As displayed in Figure 1 above, CPs will not be able to identify customers who are experiencing Hardship with another lender, which will create lending risks to the CP and add to a customer's financial stress. In short, a hardship flag would give CPs access to additional information to make a more refined assessment of credit risk in tune with an individual's particular circumstances and complement responsible lending obligations.

Question 2

If the current mechanisms for how hardship arrangements (formal or informal) are reported are not effective to facilitate an efficient credit reporting system while ensuring that the privacy of individuals is respected, how should this be addressed? Are there reforms that could be implemented within the current regulatory framework? Are there non-legislative options available?

In our submission to Treasury dated 23 February 2018, Westpac provided context of the current credit reporting framework and suggested an amendment to the CR Code as this requirement needs to apply to all ADIs and non-ADIs (who are also CPs) participating in CCR, not just large ADIs who are caught by the mandatory CCR scheme.

Westpac submits that it is important for any hardship indicator to be attached to the RHI component to ensure that only CPs who are Australian credit licensees have access to this CCR data and to preserve the existing protections around how RHI may be used by CRBs.

A hardship indicator does not divulge any sensitive information about a customer (such as if a customer's hardship arrangement resulted from an illness), the indicator should record 'the fact' that they have a hardship arrangement with their CP. As suggested in our first submission to Treasury in respect of the Bill, the Paragraph 8 of the CR Code could be expanded to include hardship indicators as part of RHI reporting requirements.

We also note the Explanatory Memorandum to the Amendment Act concluded that the addition of repayment history as part of CCR information will provide CPs with "the opportunity to access enhanced information to establish an individual's credit worthiness. It is expect that this will allow more robust assessments of consumer credit risk, both in the market as a whole and in relation to individual applications, which can assist with responsible lending and potentially lead to lower consumer credit default rates. The economic benefits to industry and individual alike outweighs the reduction of privacy protections to these categories of personal information".⁷

Westpac does not believe non-legislative options would be strong enough to ensure that ADIs and non-ADIs adopt the same interpretation of how RHI and hardship indicators should be reported in the credit reporting system. Clarity in regulation (through expanding the CR Code) on these issues will ensure

⁶ Explanatory Memorandum, p. 6, 1.11

⁷ Explanatory Memorandum, p. 29

consistency across the industry, such that the Financial Ombudsman's Service (**FOS**) and consumer advocates can clearly advise their clients.

Westpac supports ARCA's position that legislative change is required to achieve a hardship indicator and notes the considerable work that industry and ARCA has undertaken. With a view to correcting the imbalance between the regulatory and legislative frameworks outlined above, Westpac takes the view that it is important to be able to flag both the hardship concession and the subsequent serviceability period.

Question 3

Some of the matters to be considered in determining regulatory/non-legislative options for action include:

- a) What hardship information should be covered, and why? How should informal arrangements/indulgences be addressed?
- b) Should information about the reasons for hardship (such as loss of employment or ill health) be included? If so, how will this information be used and would this mean different consequences for individuals depending on the reason for hardship? If credit decisions are to consider the reasons for hardship, why can't this information be obtained directly from the individual (or, with their consent, from the relevant credit provider)?
- c) Should hardship information be a separate type of credit information which is separately reported and subject to specific rules, or should it be reported incidentally, as part of RHI? What is the appropriate relationship between hardship information and RHI?
- d) How will the hardship information be used and should there be any restrictions on the use of this information? Who should be able to access hardship information and in what circumstances?
- e) What are the expected consequences for individuals about whom hardship information is reported? How might any risks arising from these consequences be mitigated?
- f) Should there be other limitations or restrictions on the hardship information that is included in the credit reporting system? For example, should retention of the hardship information be limited (eg no retention once hardship period over)?
- g) How is the inclusion of hardship information expected to operate in practice? For example, noting that most credit application processes are automated, what are the expected consequences of including hardship information in this context, and how are practices in industry around these matters to be made consistent so that consumers are not dis/advantaged depending on the credit provider?

- a) What hardship information should be covered, and why? How should informal arrangements/indulgences be addressed?

We are comfortable that the OAIC's guidance provides sufficient clarity on how a CP is to address temporary arrangements. We submit it is possible for a CP to explain clearly in its communication to customers what happens in a temporary arrangement where there is no variation to the customer's credit

contract. As such, CPs will report RHI in accordance with the age of the debt as provided in paragraph 8 of the CR Code. Westpac provides temporary arrangements where these are more appropriate.

Each CP will have their own Hardship policies, which align with s72 of the NCC, and will assess a customer's request in accordance with that policy. We do not think there is a need to report such granular detail to explain one hardship versus another hardship arrangement such as whether a customer is in hardship because of illness versus divorce.

- b) Should information about the reasons for hardship (such as loss of employment or ill health) be included? If so, how will this information be used and would this mean different consequences for individuals depending on the reason for hardship? If credit decisions are to consider the reasons for hardship, why can't this information be obtained directly from the individual (or, with their consent, from the relevant credit provider)?

As indicated in our response to Question 3(a), we do not think it is necessary to report hardship reasons in granular detail. Industry is seeking a hardship indicator. A flag to indicate that a customer is under a hardship arrangement (or Disaster arrangement) would assist. It would be the responsibility of the new lender to make further enquiries with the customer as to the reason for the hardship and take into consideration along with the purpose for applying for the additional credit.

- c) Should hardship information be a separate type of credit information which is separately reported and subject to specific rules, or should it be reported incidentally, as part of RHI? What is the appropriate relationship between hardship information and RHI?

As explained in Question 2, Westpac believes hardship information should be reported as part of the RHI component so that the same legal framework for RHI can be applied to hardship information as well. This means hardship indicators will be subject to the same restrictions as RHI, which also extends to how CRBs can use and disclose this type of CCR data.

- d) How will the hardship information be used and should there be any restrictions on the use of this information? Who should be able to access hardship information and in what circumstances?

Westpac takes the view that the same protections which cover RHI in the Privacy Act should cover hardship information as well. For example, only CPs who are Australian credit licensees can report and have access to RHI and CRBs are prevented from using or disclosing RHI for direct marketing purposes.

- e) What are the expected consequences for individuals about whom hardship information is reported? How might any risks arising from these consequences be mitigated?

Westpac takes the view that when the customer recovers from financial difficulty and has been making regular and up-to-date payments, CPs should be able to recommence lending in accordance with their lending policies. Hardship information covering the relevant period will simply allow CPs to perform better lending assessments on credit applications and ensure the quality of credit information they use and disclose is 'accurate, up-to-date, complete and relevant', as required by the Privacy Act which also complements our responsible lending obligations.

- f) Should there be other limitations or restrictions on the hardship information that is included in the credit reporting system? For example, should retention of the hardship information be limited (eg no retention once hardship period over)?

If hardship information is enabled within the current RHI reporting structure, the existing restrictions on use and disclosure of RHI would apply to hardship information including the same retention period of 24 months. As explained in 3c above, Westpac holds that hardship information should form part of RHI to preserve the legislative protections afforded to RHI. However Westpac supports removing the flag after the Hardship/Serviceability period if a change to the legislative framework could permit this

Westpac is comfortable that no other restrictions are necessary for hardship information if the RHI framework is adopted.

- g) How is the inclusion of hardship information expected to operate in practice? For example, noting that most credit application processes are automated, what are the expected consequences of including hardship information in this context, and how are practices in industry around these matters to be made consistent so that consumers are not dis/advantaged depending on the credit provider?

Hardship information would assist CPs to make further enquiries about a customer's financial situation. In an automated application environment, should an application be referred for manual processing, hardship information will assist with customer discussions to better understand their individual circumstances. When the customer recovers from financial difficulty and has been making regular and up-to-date payments, CPs should be able to recommence lending in accordance with its lending policies.

Question 4

If financial hardship was included in consumer credit reporting, how would this impact credit providers' engagement with their responsible lending obligations:

- a) Where a credit provider is assessing a new application for credit where a consumer's credit report represents that the consumer has recently entered into a hardship agreement.
- b) Where a credit provider has extended credit to a consumer (whether ongoing, or a single loan), and the consumer enters into a hardship agreement with another credit provider which is then reported on that consumer's credit report.

- a) Where a credit provider is assessing a new application for credit where a consumer's credit report represents that the consumer has recently entered into a hardship agreement.

We would ask more questions before lending to determine if the customer's financial situation has changed since entering a hardship event, which will help feed into a CP's responsible lending assessment.

- b) Where a credit provider has extended credit to a consumer (whether ongoing, or a single loan), and the consumer enters into a hardship agreement with another credit provider which is then reported on that consumer's credit report.

Responsible Lending obligations are triggered when CPs are assessing a new credit contract and when assessing an application for a limit increase. Therefore, if financial hardship was included in the consumer credit reporting framework, this information will interact with the lender's credit assessment processes in respect of the circumstances that triggers responsible lending.

The Privacy Act currently allows CPs to obtain a consumer credit report to help customers avoid defaulting on their obligations in relation to consumer credit. The additional hardship information included with RHI will enhance this current process.

Question 5

Are there any other issues involving hardship and the credit reporting scheme that should be considered in the course of the review?

Another issue to consider in hardship arrangements is how should RHI be reported when a customer breaches the conditions of their hardship arrangement such as missing agreed repayments?

In the circumstance where a customer cannot meet their obligations under the hardship arrangement the terms of the hardship agreement have not been met and the original terms come back into effect. The customer would be removed from the Hardship arrangement and returned to the original terms of their contract. RHI should be reported according to the age of the debt under the terms of the original contract.