

Mr David Murray AO
Chair
Australian Financial System Inquiry
Via email: fsi@fsi.gov.au

Dear Mr Murray AO

The Australian Retail Credit Association (ARCA) welcomes this opportunity to provide additional material to the Australian Financial System Inquiry.

We congratulate the Inquiry panel on the release of the interim report. ARCA has appreciated the opportunity to engage meaningfully with the Inquiry secretariat on our policy objectives, and we have appreciated the extension of time to provide this additional material.

For any additional information, or to discuss this submission further, please contact Matt Gijselman, ARCA Head of Government, Regulatory & Industry Affairs on 02 9236 2426 or email mgijselman@arca.asn.au.

Thank you for the opportunity to provide this additional material, and I wish the FSI Panel all the best in your deliberations.

Yours sincerely



DAMIAN PAULL
Chief Executive Officer

8 September 2014

Australian Retail Credit Association

Additional submission to the

Australian Financial System Inquiry

September 2014

The Australian Retail Credit Association (ARCA) is the peak industry body dealing with credit reporting and representing all major credit providers and major consumer credit reporting bodies in Australia.

ARCA wishes to record our thanks for the work of the Panel and secretariat staff in preparing the Interim Report for the Financial Services Inquiry. That report provided a useful summary of the complex and significant issues that the Panel faces as you prepare your final document.

ARCA has restricted our comments to those matters of direct interest to our Members relating to credit reporting and consumer credit risk.

Increasing the data fields that are exchangeable in the credit reporting system

The Inquiry has sought views on the costs, benefits and trade-offs of:

- No change to current arrangements;
- Adding new fields to the credit reporting system

A fundamental principle for ARCA Members is that more data can equal better credit decisions. ARCA notes that various global studies have supported this premise, and ARCA believes that there is an opportunity for specific classes of data to be considered for inclusion into Australia's credit reporting system.

Recent research suggests that over 3.1 million Australians are 'financially excluded', meaning they lack effective insurance, access to a transaction account or are not able to access modest and responsible mainstream credit¹. International experience suggests that an increase in the exchangeable data in the credit reporting system – particularly repayment history information for telecommunications and utilities accounts – has the capacity to improve access to credit for minorities and other consumers that would otherwise struggle to access credit.

ARCA has provided links to some of this research in Appendix A.

ARCA also supports a review of the current credit reporting system in late 2016 or early 2017, in order to examine the impact of the most recent reforms to the credit reporting system. This review will be able to examine whether or not the most recent reforms to credit reporting have been successful and whether additional data is likely to further support the needs of system participants.

In examining the success or otherwise of the most recent reforms, the review should examine whether or not credit providers (CPs) and credit reporting bodies (CRBs) are making use of the data currently allowable in the credit reporting system, and whether this additional data is providing consumers, industry and the wider economy the benefits

¹ http://cr.nab.com.au/docs/nab_csi_measuring_financial_exclusion_in_australia_2013.pdf

of better credit decisions and more access to credit to those that can responsibly manage it.

Mandatory credit reporting arrangements

The Inquiry has sought views on the costs, benefits and trade-offs of:

- No change to current arrangements;
- Expanding comprehensive credit reporting by making it mandatory.

ARCA's view is that there ought to be no change to the current arrangements.

ARCA is currently finalising the Principles of Reciprocity and Data Exchange (PRDE), an industry agreement for the exchange of comprehensive credit reporting. The PRDE seeks to encourage data quality and integrity and a more informed credit reporting system by encouraging and incentivising all CPs to provide comprehensive credit reporting information to CRBs.

The PRDE will effectively create a data exchange system for the new comprehensive data. It is intended that this data exchange system will be the sole system for new data to be exchanged.

The key features of the PRDE are as follows:

- A set of principles which are binding upon signatories by entry into a deed poll (with the PRDE annexed).
- Creates three tier levels for data exchange:
 - Negative (that is, the data typically disclosed pre-12 March 2014);
 - Partial (consumer credit liability information, that is, information about current credit accounts, plus the data at negative tier); and
 - Comprehensive (repayment history information plus the data available at the other tiers).
- A signatory will nominate a tier level for exchange, and will only receive reciprocal data at that level. Only signatories to the PRDE will have access to partial and comprehensive data.
- When credit information is contributed, it will be required to comply with a single data standard (the Australian Credit Reporting Data Standards, which has been developed by ARCA).

The reciprocal data exchange is supported by a compliance process, where signatories are able to raise an issue with any alleged non-compliance by another signatory. These disputes will be transparent between signatories, and escalated through a signatory-to-signatory resolution, to peer review and, as a final process of appeal, an eminent person.

The PRDE has been developed following extensive consultation between ARCA Members, and external consultation with industry associations (Communications Alliance, Mortgage & Finance Association of Australia, Australian Collectors and Debt Buyers Association, Insurance Council of Australia, Energy Retailers Association of Australia, Australian Banking Association, Australian Finance Conference), consumer advocate groups and government organisations (the Office of the Australian Information Commissioner and the Australian Securities and Investments Commission).

Given the conditions the PRDE may place on the data exchange in the credit reporting market, some of its clauses will be subject to an application for authorisation to the Australian Competition and Consumer Commission. This application will be submitted in

late-September 2014 and will likely take a period of six months to process. This means that it will not be until at least March 2015 that comprehensive credit reporting is utilised. Further, given transitional requirements (12 months in the PRDE), it will not be until late 2016 and early 2017 that significant portions of comprehensive credit information will be exchanged.

In these circumstances, mandatory credit comprehensive reporting would be both premature and may, following authorisation and implementation of the PRDE, prove to be unnecessary.

ARCA supports a review of the credit reporting arrangements in late 2016 or early 2017 to examine the impact of the recent reforms to credit reporting in addition to the impact of the operation of the PRDE.

Small Medium Enterprise (SME) Credit Reporting

In addition to seeking views on making comprehensive credit reporting mandatory, the Inquiry has sought views on extending comprehensive credit reporting to SME lending.

Given that comprehensive credit reporting in the retail credit sector is in its infancy, an imposition of compulsory comprehensive credit reporting to the SME sector would be premature. ARCA considers that any extension of compulsory comprehensive credit reporting to SME lending should only take place where it has been demonstrated that a market failure in the SME sector necessitates such reform.

Whilst we support the Inquiry's moves to lower the cost of funds for SMEs and increase their access to funding – any increase in the regulatory burden for either SMEs or participants in the credit reporting system is unlikely to decrease costs.

ARCA recommends that this proposal is included in a review of the credit reporting regulatory framework that should be undertaken at the end of 2016 or beginning of 2017.

Supporting financial literacy

The Inquiry has sought additional information regarding the effectiveness of financial literacy strategies in enhancing consumer confidence and decision making.

ARCA's consumer education goal is as follows:

"Improving consumer awareness on the importance of credit history and improving their credit footprint".

Recent credit reporting reforms will give consumers greater protections and controls of their credit reporting information. Consumers now have the right to:

- a free credit report from each credit reporting body each year, and additionally access to a free report within 90 days of a credit refusal;
- greater protections associated with potential identity theft;
- clearer powers to request a credit reporting body or credit provider investigate and fix incorrect listings as these listings may affect a person's ability to get credit in the future;
- request a credit reporting body put a ban on sharing their credit report if there is suspicion that identify theft has occurred; and

- a clear dispute resolution process that is free to consumers, including a requirement that credit providers and credit reporting bodies are members of an external dispute resolution scheme².

According to independent research commissioned by ARCA, 59 percent of consumers had not heard of credit reporting. As a result, there was strong agreement from consumer advocates, industry and the regulator that consumer education was a high priority – given both the need for consumers to manage their credit worthiness going forward as a result of the additional information within the credit reporting system, and also to allow consumers to understand their new rights.

In mid-2013, the Office of the Australian Information Commissioner (OAIC) made it clear that it had minimal funding available to support consumer education relating to these significant changes, and requested ARCA to assist. In consultation with the ASIC MoneySmart team, it was further determined that the MoneySmart website could contain a high level summary of the credit reporting changes, but that that a separate site was required for in-depth coverage. As a result of these findings, ARCA persuaded its Members to voluntarily fund the development of a consumer website and media campaign.

In early December 2013, ahead of the commencement of the reforms in March 2014, ARCA launched creditsmart.org.au, supported by a media campaign. The site provides a range of tools and tips to help educate consumers on the basics of credit reports and how they can proactively manage their credit history, by providing information about the system that is unbiased and fair - assisting them to better manage their financial position.

ARCA has this week received the 2014 MoneySmart Week Outstanding Achievement Award by Financial Literacy Australia in recognition of its significant contribution to improving the financial literacy of Australians. ARCA was awarded the Outstanding Achievement Award – industry category – for its CreditSmart campaign which explains the recent credit reporting changes and the growing importance of maintaining a clearer credit history to Australians. ARCA continues to build and develop the CreditSmart brand – as a trusted source of information on credit and credit reporting.

ARCA considers that this initiative has been effective in helping to address issues of financial literacy. However, much more can be done to improve the issue of financial literacy, including funding for public education campaigns to promote initiatives such as CreditSmart.

The Australian and State Governments, regulators, industry and consumer advocates spend significant funds on improving financial literacy and building financial resilience. ARCA supports the development of a comprehensive co-ordinating strategy to ensure this funding is targeted, co-ordinated and comprehensive. We would welcome the opportunity to contribute to such a strategy.

Trans-Tasman credit reporting data sharing

The introduction of reforms to Australian credit reporting in March 2014 has provided for a range of positive benefits to Australia's consumer credit risk system, where more data (Consumer Credit Liability Information and Repayment History Information) will eventually mean better credit decisions for a range of lenders. The introduction of this comprehensive credit reporting goes some way towards bringing Australia in line with the majority of members of the Organisation for Economic Co-operation and Development (OECD).

² Subject to limited exceptions provided for in the Privacy Regulations 2013

ARCA Members are supportive of the introduction of credit reporting data sharing arrangements between Australia and New Zealand. There are strong economic and public policy benefits to be gained through introducing such arrangements such that this microeconomic reform would bring positive economic activity whilst supporting social benefits associated with better consumer credit risk assessment for consumers in both markets.

The total accumulated bilateral investment of both countries is over AU\$90 billion³. At present, Australia is New Zealand's largest trading partner, occupying 21% of their total export trade. Australia is also New Zealand's second largest source of imports at 15.3% of all their imports⁴.

In the context of the exchange of consumer credit data between Australia and New Zealand, there is a significant flow of people between Australia and New Zealand. At 30 June 2013, an estimated 640,770 New Zealand citizens were present in Australia⁵.

A joint study⁶ produced by the Australian and New Zealand Productivity Commissions identified a number of areas of cross-border engagement where barriers can potentially be reduced.

The regulatory status of cross-border credit information sharing is not uniform, and ARCA Members support a change to this arrangement to ensure continued responsible credit provision in each market.

In Australia, credit reporting bodies are not permitted to share credit information with organisations without an Australian link. In New Zealand, the regulatory framework recognises that information can potentially be shared extra-territorially, but we are not clear on the best mechanism which would be allowed to facilitate this. This lack of a cooperative focus in the regulation of credit reporting can affect cross-border credit decision-making.

The inability of credit providers to access credit information sourced across the Tasman can present a hurdle for them when servicing temporary residents that seek credit across jurisdictions. Credit providers in Australia that assess new resident credit applications make assessments on information that excludes borrowing behaviour that may be available in credit reporting information from across the Tasman. Having access to this information would allow credit providers to comply more easily with their responsible lending obligations.

Cooperative regulation in the sharing of economic activity information can reduce difficulties in cross-border credit assessment. The Financial System Inquiry's fourth term of reference recommends that policy options *inter alia* promote competition and a stable financial system. Further to this they should contribute to Australia's productivity growth and meet the needs of participants with appropriate financial products and services. ARCA considers that enabling the sharing of credit reporting information between Australia and New Zealand will promote achievement of this goal.

³ Department of Foreign Affairs and Trade (Cth) '2010 Ministerial Forum: Joint Statement' (Joint Statement, 23 June 2010).

⁴ <https://www.dfat.gov.au/geo/fs/nz.pdf>

⁵ Fact Sheet 17 – New Zealanders in Australia (produced by the National Communications Branch, Department of Immigration and Border Protection, Canberra, last reviewed December 2013)

⁶ Australian Productivity Commission and New Zealand Productivity Commission 'Strengthening trans-Tasman economic relations' (Joint Study, November 2012) 9.

Corrections in the credit reporting system

ARCA is aware that the Inquiry has an interest in understanding the corrections arrangements that now apply to the credit reporting system, following the passage of the Privacy (Enhancing Privacy Protection) Amendment Act 2012.

The Office of the Australian Information Commissioner (OAIC) is the national regulator for credit reporting. They have recently published a series of fact sheets on the credit reporting system. Fact sheet 32⁷ "Seeking correction of your credit report" outlines the process consumers can now follow to correct their credit report.

Briefly, it notes that consumers can approach any CRB or CP that holds personal information about them and request to have any incorrect personal information included in their consumer credit report corrected.

It does not matter whether that particular CRB or CP holds the specific piece of information that the consumer wants to have corrected.

A CRB or CP is required to make a decision about the correction request within 30 days of the consumer making it. Once the CRB or CP has made a decision, the CRB or CP has 5 business days in which to notify the consumer about the outcome.

In certain circumstances a CRB or CP may request that the consumer agree to an extension of time for the correction to be made. If the consumer agrees, this must be done in writing.

In the event that the CRB or CP refuses the correction request, or is unable to respond within 30 days, the consumer is able to refer the matter to an external dispute resolution (EDR) scheme for review.

Introduction of a trusted digital ID

The Inquiry has sought views on the costs, benefits and trade-offs of:

- No change to current arrangements;
- Adding new fields to the credit reporting system

ARCA supports the establishment of a de-regulated digital identity framework, with active Australian Government support, to enable innovation and technological neutrality in the delivery of trusted digital identity.

ARCA Members welcome the FSI's interest in identity, and the focus on the opportunities provided through a digital identity to support Australia's future and globally-connected economy.

The prevalent approach to identity verification by some Australian authorities already ignores the opportunities afforded in an online economy to utilise new and emerging technologies to meet identity requirements. These opportunities will increasingly shape the globally-connected economy. Australia risks missing out on or hampering economic growth opportunities if we retain our unwarranted mistrust of digital identity in favour of paper-based identity approaches.

ARCA supports the Inquiry examining this matter. As organisations that rely heavily on the exchange of sensitive data, our Members acknowledge that ensuring trust and

⁷ <http://www.oaic.gov.au/privacy/privacy-resources/privacy-fact-sheets/credit-and-finance/privacy-fact-sheet-32-seeking-correction-of-your-credit-report>

confidence in any digital exchange is critical. To that end, the engagement of the Australian Government in the establishment of a trusted digital identity will be critical.

Whilst ARCA welcomes moves by the Australian Government to utilise the data assets of the Commonwealth, including the expansion of the [MyGov](#) portal, there still seems little appetite to move beyond knowledge-based authentication (KBA) in most interactions with government. This adherence to KBA simply no longer makes sense when authentication tokens, dynamic transaction-based authentication or other more modern methods of identification are already in the market.

Appendix A: Additional materials

ARCA has collated a range of external reports and articles to support the inclusion of additional data into the credit reporting system, across three main classes of data, as outlined in ARCA's original submission to the Inquiry, namely:

- The inclusion of government data into the credit reporting system;
- The inclusion of balance and/or utilisation data; and
- Non-financial credit providers submitting and gaining access to repayment history data.

We commend the reports/articles to the Inquiry:

The inclusion of government data into the credit reporting system

US Department of Health and Human Services publication that includes that child support payment defaults in the US are reflected in credit reports:

<http://idaresources.acf.hhs.gov/page?pageid=a04700000Df6Aq>

Article originally printed in *The Australian Financial Review* that reported ATO second commissioner Geoff Lepper suggesting that introducing tax debts on credit reports may encourage people to pay their tax obligations:

<http://www.lockwood.com.au/ato-wants-name-debtors/>

The inclusion of balance and/or utilisation data

FICO is generally recognised as the 'universal' consumer score – it combines the 3 scores from the major US credit reporting bodies (Equifax, Experian and TransUrban). They utilise a range of factors in determining your score. Credit utilisation accounts for approximately 30% of the weighting for a FICO score in the United States:

<http://www.myfico.com/CreditEducation/Amounts-Owed.aspx>

A publication from the US Department of Health and Human Services that explains how the US credit reporting system usually calculates a credit score. It generally indicates a heavy reliance on credit balance/utilisation information to calculate the score:

<http://www.idaresources.acf.hhs.gov/page?pageid=a047000000B7oys>

Publication by Federal Reserve Bank of Philadelphia, pg 2 explains how credit utilisation is used:

http://www.philadelphiafed.org/bank-resources/publications/consumer-compliance-outlook/2010/third-quarter/cco_q3_10.pdf

Non-financial credit providers submitting and gaining access to repayment history data

Political and Economic Research Council (PERC) report explaining how NICOR and DTE Energy benefitted from having their defaults show up on a person's credit report, although it doesn't strictly say that utilities gain access to credit reports:

http://www.perc.net/wp-content/uploads/2013/09/bizcase_0.pdf

PERC report that specifically explores the effect of adding alternative data (ie, from utilities and telecommunication companies) to credit reports:

<http://www.perc.net/wp-content/uploads/2013/09/WEB-file-ADI5-layout1.pdf>