

Submission:

Abacus – Australian Mutuals

Australian Law Reform Commission:
*Review of Privacy – Credit Reporting
Provisions*

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Abacus
Australian Mutuals

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Introduction

Abacus – Australian Mutuals appreciates the opportunity to contribute to the Australian Law Reform Commission's *Review of Privacy – Credit Reporting Provisions*.

This submission addresses *Issues Paper 32* but should be read in conjunction with our earlier response to *Issues Paper 31*, which dealt with the private sector provisions of the *Privacy Act 1988* and included detailed information about the mutual sector, its regulatory environment and its experiences with privacy law.

As the peak association for the majority of credit unions and all mutual building societies, *Abacus* represents 90 per cent of the mutual financial sector. Credit unions and mutual building societies service 4.5 million customers around Australia.

Abacus and its members support the regulation of credit reporting at a Federal level within the scheme established under Part IIIA of the *Privacy Act 1988* and the limited data sharing regime covering an individual's credit worthiness, history, standing or eligibility.

However, *Abacus* believes the current picture available to credit providers does not deliver for consumers or business an accurate image of a person's credit risk. Consequently, credit providers are hamstrung when making lending decisions and some borrowers are denied access unfairly while others may be exposed to excessive credit.

The ALRC review is a timely consideration of possible changes to the Part IIIA regime to refine and improve the effectiveness of the regulatory framework in relation to credit reporting. In particular, *Abacus* urges removal of the barrier to comprehensive credit reporting and exploration of the use of credit information for identification purposes.

Abacus understands the appreciable risks associated with allowing the collection and sharing of more detailed information. In these circumstances, *Abacus* believes organisations seeking increasing amounts of information for risk management purposes or those wanting to rely on this data for identity verification should still be held accountable for the collection, use and disposal of this information and subject to the expectations of the privacy law.

Accordingly, this submission focuses on the following matters:

- the current Part IIIA credit reporting provisions;
- comprehensive credit reporting proposals; and
- using credit reports for identity verification purposes.

These matters have already been raised in concurrent forums with relevant regulators and Government. A notable example is the examination of credit reporting in Consumer Affairs Victoria's (CAV) *Report of the Consumer Credit*

Review in 2006 and in discussions on *Anti-Money Laundering and Counter Terrorism Financing* (AML/CTF) reforms.

1. Part IIIA – Credit reporting provisions

A person's credit worthiness directly affects their financial integrity and reputation and is critical to their ability to access funds or purchase goods and services on credit. Credit unions and mutual building societies rely on credit reporting services to inform their lending decisions.

Information contained in a person's credit report goes directly to assess an applicant's credit risk, especially in relation to their capacity and propensity to repay a loan. It is an important input into a credit provider's ability to manage the risks associated with the granting of initial or further credit to a particular customer.

Abacus highlights the economic function of credit providers to assess and take credit risks. But this must be done in a sensible way that protects the organisation's capital and resources and does not expose consumers to loss. That means adopting a prudential approach to credit management and avoiding over-indebtedness among borrowers.

Credit providers look to credit risk and the application of scorecards and other analytical tools to determine the suitability of credit applications. Adherence to these controls is important to ensure the safe and effective running of the organisation.

In addition to checking income and expenditure, credit unions and mutual building societies routinely look to credit reporting (in relation to systems and the information in credit reporting databases) as an important credit management tool. Understanding a person's credit risk is a fundamental precondition to the offer of credit. Credit unions and mutual building societies have an obligation to assess a borrower's capacity to repay as a requirement of the UCCC as well as a feature of prudential operations.

In addition to enquiries (applications) by consumers for credit, Australia's credit reporting scheme also includes defaults and other negative events information linked to a particular person. That means, other than application enquiries, credit reports are centred on default data and the accurate identification of an individual.

Because this information has such a material impact on a person's ability to access credit (as well as being critical to a lender's ability to make informed decisions), *Abacus* supports a framework where credit information is protected by the *Privacy Act 1988* in relation to its collection, retention and disclosure. The current regime also regulates (by limitation) how credit providers use the information recorded on credit files.

To assist credit unions and mutual building societies comply, *Abacus* provides credit reporting privacy training via a comprehensive compliance manual as well as access to an online computer-based training tool. These resources, together with activities undertaken at the local credit union or mutual building society level, promote

awareness, comprehension and compliance with the credit reporting provisions of Part IIIA.

Ultimately, credit unions and mutual building societies believe there is room for improvement around the accuracy of default listings, the quality of the system as a whole, consideration of adding positive data to the system and careful consideration of the organisations that are permitted to list and access credit data.

Abacus believes that within the boundaries set by the Act, Part IIIA functions adequately to balance the need to access credit data and the obligation to protect consumer privacy. That does not mean there is no need for reform and improvement. Indeed, one of the biggest challenges for all users – consumers and business alike – of the credit reporting systems is the quality of data.

Data quality can be compromised in terms of the accuracy of a person's identity, default listings, other data inaccuracies or system errors. There is a further hurdle in that data cannot be easily checked against existing data sources, such as information contained by Births, Deaths and Marriages, the electoral rolls, Whitepages information or other government-based registries.

Complaints received by the *Credit Union Dispute Resolution Centre* (CUDRC), the ADR scheme for the mutual sector whose jurisdiction includes privacy matters, is illustrative:

- in 2004-05, of the 155 cases received only 15 related to privacy and 12 of these addressed credit reporting; and
- in 2005-06, of the 167 cases received there were only 9 related to privacy and 6 of these addressed credit reporting.

The low-range number of privacy complaints – including credit reporting-related complaints – is indicative of the general effectiveness of the current regime. In as far as the bias in these complaints is towards credit report matters, it also points to the challenges associated with ensuring credit data is accurate. *Abacus* believes the relatively higher incidence of credit reporting complaints points to the tension in the credit reporting system where there is a significant reliance on the data but the ability to verify that data and make changes is complicated.

Access to credit data - determinations by the OFPC

Abacus understands the policy intention to find an appropriate balance between consumer and business needs in terms of access to and the use of the credit reporting system. In this context, *Abacus* believes it is critical the credit reporting system is accurate, complete and not misleading.

Broadening access to the credit reporting system should only be considered where use is subject to the same high standards and expectations as faced by credit providers covered by s.11B(1). This is a view *Abacus* has made to the Office of the Federal Privacy Commissioner (OFPC) about its 2006 *Assignee Determination* and *Class of Credit Provider Determination*.

Abacus has concerns that the practices of some non-traditional credit providers in terms of double listings, listing of statute barred debts or non-compliance (such as in relation to s.18E(8)(c) notices) are an indication of at best a lack of awareness or at worst examples of deliberate non-compliance with the Part III obligations. This malpractice undermines the accuracy and credibility of the credit reporting system as a whole.

2. Comprehensive credit reporting

A comprehensive reporting regime is likely to increase, in absolute terms, the number of consumers that have access to credit. But *Abacus* believes this can occur in a more informed market where credit decisions are more precise and deliberate and made cognisant of an individual's full credit picture.

It should be noted that some credit providers can already assess existing negative data alongside transaction and repayment history information volunteered by current customers seeking further credit. For larger credit providers, the ability to assess positive credit data (albeit outside the credit reporting scheme) on an individual or trend basis offers a potentially competitive advantage in terms of understanding the credit risk that a customer might pose.

In summary, the case for positive credit reporting is:

- better rationing of credit so that good risks access credit and bad risks do not;
- improving the chances of low-income earners gaining access to mainstream credit and diminishing reliance on payday and other fringe lenders;
- enhanced ability to price credit, as risk is better assessed leading to reduced defaults; and
- more competitive markets, as consumers are less reliant on existing institutional relationships to obtain credit.

This last point is particularly important from a competitive perspective. Those consumers with healthy repayment histories with one credit provider can, under a positive reporting scheme, transfer that good record to other credit providers. Under the current system, despite being able to demonstrate a capacity and propensity to repay, this positive data is not transferable within the credit reporting scheme.

Equally, *Abacus* is aware of the case against positive credit reporting. Primary among the concerns is a fear of the increased amount of personal information held on people, potentially enabling detailed profiles to be drawn about individuals. Opponents of positive credit reporting also point to the poor data quality in current credit reporting databases and posit that bureaus and credit providers should not be allowed to hold or access a wider range of information until they improve their existing performance.

In principle, *Abacus* supports consideration of an end to the Part IIIA ban on positive credit reporting, subject to necessary quality, privacy and review

assurances. *Abacus* agrees that efforts are required to enhance and improve credit reporting in relation to data collection, accuracy and maintenance. Such steps are necessary to improve decision-making by credit providers and to protect the interests of consumers. These steps are also an essential precondition to any attempt to introduce a broader pool of data for credit reporting purposes.

Features of comprehensive credit reporting

Comprehensive data includes the current range of default information but also has the potential to add information such as:

- the number and types of credit facilities – may includes date opened, date closed, days past due;
- the limits for each credit facility and outstanding balances; and
- repayment information – such as scheduled payment amount, actual payments, date of last payment.

This creates a more complete overall picture of a borrower's current position and means there is less reliance on default data alone. A consequence of such an approach is a rise in the amount of personal information captured for credit reporting purposes. This creates risks in terms of breaches in data security and reinforces the need for the highest quality data quality and assurance procedures.

In response to these concerns and risks, *Abacus* believes that whatever model might be contemplated borrowers should be entitled to a range of safeguards, such as:

- controlled access to the credit reporting system and potentially different levels of access for ancillary purposes (see discussion on identity verification below);
- access based on mandatory information collection to ensure users have a stake in the quality and safety of data collected – although caution should be exercised not to lock out smaller credit providers;
- parity in terms of the standards expected of all information collectors and users (beyond ADIs, consider also telecommunications, utility and retail firms);
- high standards of transparency in terms of collection and use if consumer consent and steps to ensure a strong understanding of the role of consents;
- use of sensible minimum thresholds for default listings and appropriately associated time periods;
- a clear mechanism for consumers to challenge errors and update information and an accountable data monitoring process by credit providers and bureaus;
- a clear mechanism for addressing compliance issues with credit bureaus and credit providers; and

- a well resourced regulator, in the OFPC, to monitoring and oversee the credit reporting scheme, including an annual audit function.

With appropriate stakeholder consultation and a full exploration with all stakeholders of the issues and challenges posed by a change to the credit reporting scheme as well as a costed regulatory impact statement (RIS) and privacy impact statement (PIS) assessment, *Abacus* believes comprehensive credit reporting could be introduced consistent with the existing NPPs and the intensive regulation required by the *Privacy Act 1988*.

Abacus believes comprehensive reporting could – if introduced in combination with significant improvements in existing practice for data collection, retention, use and quality¹ – provide a more effective tool for credit providers to assess risk and foster responsible lending practices. At the same time, such a scheme could bolster consumer protection by mitigating against over-indebtedness, providing greater portability of good credit histories and establishing confident mechanisms for ensuring the accuracy and currency of recorded data.

3. Identification using credit reports

The rise of identification theft and identity fraud is a constant reminder of the need for caution when relying on identification information. Equally, these growing threats are a reminder of the value of a robust, identity verification process.

Importantly, a one-off identity check is no longer sufficient; instead, being certain about a person's identity is increasingly a continuous obligation.

The verification of identity on the basis of credit file data could assist in reducing the incidence of false files being established within bureaus as well as establishing credible identities for other purposes.

The *Anti-Money Laundering and Counter Terrorism-Financing (AML/CTF) Act 2006* heightens the issue by introducing new obligations on reporting entities to collect identification information and verify it. Specifically, the *AML/CTF Act 2006* requires a reporting entity to carry out its applicable identification procedure prior to provision of a designated service.

The one-off identity checks under the *Financial Transaction Reports Act 1988* (FTRA) are no longer sufficient. Reporting entities, including credit unions and mutual building societies, must undertake ongoing scrutiny of customer identification data as well as their financial activity and account behaviour.

The level of scrutiny will depend on the risk of money laundering and terrorism-financing posed by the customer and their activities. *Abacus* raised a range of privacy-related issues in the earlier response to IP 31. Another matter relevant to the *Privacy Act 1988*, is the possible role for credit reports as a source of identification data.

¹ The Australian Retail Credit Association is pursuing these matters in relation to the current credit reporting regime.

Reliable and independent data

The *AML/CTF Act 2006* does not prevent a reporting entity from looking to various data sources for non-face-to-face identification, although it does not stipulate a particular approach. This means there are additional challenges for reporting entities without a broad branch network or those businesses that operate without a physical presence².

However, relevant to IP 32, there are barriers in terms of some electronic verification sources including credit reports. This creates a tension between requiring industry to perform more detailed identification checks but not making that task any easier.

The *Draft AML/CTF Rules* (initially released in July 2006 and then updated in March 2007³) allow the use of '*reliable and independent electronic data*' to verify the identity of medium or lower risk customers. The Attorney General's Department has previously cited the electoral roll, White Pages and credit files as potential databases for use in e-verification. However, whether these data sources are satisfactory or feasible remains unclear.

Recent clarifications by AUSTRAC suggest that access to credit bureau records for e-verification purposes are not possible due to prohibitions contained in the *Privacy Act 1988* and the status of the *AML/CTF Rules* as subordinate legislation. The *Consequential Amendments* accompanying the introduction of the *AML/CTF Act 2006* amended the *Privacy Act 1988* in relation to small business coverage but it did nothing to facilitate access to credit files data.

Abacus is currently seeking clarity from AUSTRAC and the OFPC in terms of access to credit file information as a *reliable and independent* data source. One proposition is to provide for access only in relation to the verification of name, address and date of birth information but not to other data on the file.

Additionally, on the policy front, there is a concern that the *AML/CTF Act 2006* requires greater degrees of identity verification but simultaneously it does not expand access to available databases for that purposes. In this environment, *Abacus* welcomes debate on whether credit reporting data should be available, perhaps with certain access conditions, for identification purposes.

Conclusion

Credit unions and mutual building societies are committed to protecting the interests of their members, including member privacy in relation to their credit report data.

But credit unions and building societies also believe that credit data offers an essential ingredient in the risk assessment process required when offering credit.

² The FTRA offered an Acceptable Referee identification method at s.21 where a person could produce an identification document to referee from a prescribed list and on that basis the referee would identify the person. This was an alternative to the 100 Point identification method.

³ www.austrac.gov.au

Accordingly, *Abacus* highlights the following observations:

- debate is encouraged on whether the current negative credit reporting scheme delivers outcomes sought by consumers and required by credit providers;
- further exploration is required into the development of a suitable, robust and consumer-minded comprehensive credit reporting regime;
- any credit reporting regime – whether it captures negative or positive data – should be subject to high privacy standards that limit the collection and use of credit data; and
- some exceptions may be warranted for to allow for the use of the credit reporting system for limited identity verification for other purposes.

Abacus appreciates the opportunity to contribute to the ALRC's assessment of the credit reporting provisions in Part IIIA of the *Privacy Act 1988* and looks forward to ongoing involvement in the consultation and review process.

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