

Improving bankruptcy and Insolvency laws

Proposals Paper

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Veda opposes any reduction in the retention period (Query 1.3.1); the credit reporting framework, the result of extensive inquiry and debate, has become intricately linked to responsible lending guidelines. Removal of bankruptcy information hampers responsible lending.

The bankruptcy retention period is aligned with that applying to other adverse information. Reducing the retention period would mean bankruptcy disappears after 12 months, but a \$200 mobile phone bill default stays for five years.

Contribution of credit reporting information to credit reporting bodies is not mandatory in Australia – lenders have choice as to whom and to what level they contribute. Bankruptcy information, however is uniformly available to all credit reporting bodies.

Analysis shows people going bankrupt typically don't have defaults on their credit report and will seek more credit, even when knowing they cannot meet any new commitments.

For an ageing bankruptcy event, the accumulation of good repayment history information will provide critical counterbalancing information.

Current access and availability on the National Personal Insolvency Index must not be changed (Proposal 1.3.1b). We note reduction in the retention period on credit reports will force lenders to obtain information from both credit reports and the Insolvency index – introducing red tape and additional cost into the economy.

Consistent with the objectives Productivity Commission inquiry into data and availability, bankruptcy information arrangements should not be changed.

Clarification

The *Improving bankruptcy and insolvency laws* proposal paper includes a section on access to credit and states that:

*“After a bankrupt is discharged from bankruptcy, a record of their bankruptcy will remain on their **commercial** credit record for the later of five years from the date of bankruptcy or two years after discharge. As such, discharged bankrupts may still have practical difficulties in obtaining credit.”*

Information relating to commercial credit is regulated by the Australian Privacy Principles, which does not prescribe a retention period for bankruptcy information. We are advised by the Commonwealth Treasury that the reference should have been to “**consumer credit record**”.

Our observations here relate to consumer credit reports, its legislative framework and associated industry practices.

Veda is a data analytics company, best known as Australia’s leading credit reporting body.

Part IIIA of the Privacy Act sets out what information can be collected by a credit reporting body about an individual. This includes information from credit providers and publicly available sources, such as bankruptcy information obtained from the Australian Financial Security Authority (AFSA)¹. This information is used in generating credit reporting information for use by credit providers when assessing credit applications. There is an obligation on credit reporting bodies to ensure that the information held is “accurate, up-to-date, complete, relevant and not misleading”²

Reduction in retention period on consumer credit reports (Query 1.3.1)

We are opposed to changes to the current retention period for information about bankruptcy (currently the later of five years from the day the individual becomes bankrupt, or two years from the day the bankruptcy ends)³. As a provider of risk and due diligence services, Veda is aware of the need for credit providers to access, in an efficient and cost-effective manner, information about credit worthiness, particularly as such information is directly relevant to credit providers meeting their obligations under ASIC’s Responsible Lending guidelines⁴.

¹ Privacy Amendment (Enhancing Privacy Protection) Act 2012, Section Part IIIA 20X

² Ibid, Section 20S

³ Ibid, Section 20X

⁴ ASIC responsible lending guideline 209

Retention of bankruptcy should be consistent with other adverse information

The Privacy Act provides for retention periods⁵ for all information including adverse information, such as defaults serious credit infringements and court judgements where the maximum retention period is five years. Bankruptcy is the most significant adverse event, yet the proposed changes would see it retained for a lesser period than a \$200 default on a mobile phone bill. Such an outcome undermines the intent of ASIC's responsible lending guidelines and is strongly opposed by Veda.

Bankruptcy may be the only sign of a significant problem with credit worthiness.

An important element in credit reporting is that contribution of credit reporting information – including defaults - is not mandatory. Even under the Principles of Data Reciprocity and Exchange (PRDE), lenders do not have to contribute all data to every CRB. This makes the appearance of bankruptcy information an important source of uniform truth in Australia's credit reporting system. Regardless of what other information each of the three CRBs may have, invariably bankruptcy will appear on all reports.

Contrary to common-belief, most bankrupts have a clean credit record, free of adverse information that would otherwise cause a credit provider to more carefully consider extending further credit. This is not because default information has not been provided to Veda; analysis in fact shows people going bankrupt knowingly avoid triggering the signals (defaults) that would alert a lender to risk.

In 2008 Veda did a sample study of bankrupts between March 2003 and 2006, using information on Debt Agreement Statement of Affairs.

- 57% of people declared bankrupt did not have any defaults listed on their credit file in the two years prior to bankruptcy;
- Critically, on the Debt Agreement Statement of Affairs, people were asked to nominate a "stress date". Analysis by Veda revealed 90% of bankrupts made further credit applications after that date ie overwhelmingly, most bankrupts sought more credit after they knew they were over-committed.

The proposal to reduce the retention period could see a person requesting substantial amounts of credit, but the information before the lender would be a credit report that shows neither defaults nor a bankruptcy.

The role of repayment history information

Veda notes the gradual collection of repayment history information will moderate the impact of adverse information and particularly historic adverse information. Veda expects the scenario whereby eventual-bankrupts have avoided defaults, they are less likely to be able to routinely make the required minimum monthly payments on time.

However, the participation of major lenders in providing repayment history information is proceeding slowly. Currently just over 24 per cent of all accounts contain repayment history information. While this will continue to increase, it is too soon to rely on repayment history information as a (misguided) rationale for removing

⁵ Privacy Amendment (Enhancing Privacy Protection) Act 2012, Section Part IIIA 20W

bankruptcy information after 12 months. Further, we note that as the collection of repayment history information does increase, the effect will be to give lenders much greater insight into the current ability of a person to manage additional credit. Adverse information – ageing defaults and bankruptcies – can be offset by the more recent insights offered by 24 months of repayment history. This is a far better “cure” for the impact bankruptcy has on credit worthiness than a slashing of the retention period without regard to credit risk assessment or the existing responsible lending obligations.

Retention on national personal insolvency index (Proposal 1.3.1b)

We note – and support – the Government’s intention to retain⁶ the permanent record of bankruptcy in the National Personal Insolvency Index. However, should the proposal 12 month limit on retention be implemented, the likely result will be credit providers requesting – and paying for – both credit reports and searches of the national personal insolvency index, creating red tape and additional cost for business.

Productivity Commission Inquiry into Data Availability and Use

Veda notes the start of the Productivity Commission’s inquiry into data availability and use, its objective to increase the availability and use of data, to boost innovation and competition in Australia. The data in the credit reporting system does exactly that and the addition of more data, such as repayment history information will increase the ability to accurately measure risk. The diminution of critical information is in contradiction to the objectives of the Inquiry.

Yours sincerely

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⁶ This must not only be retained, but must also be able to be accessed and disclosed.