

Consumer Credit Unit
Financial System Division
Treasury
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sent by email to: CreditReforms@treasury.gov.au

Submission to Treasury: Buy Now Pay Later regulatory reforms

Kadre welcomes the opportunity to provide this feedback to Treasury on the exposure draft legislative package relating to Buy Now Pay Later regulatory reforms. We also refer to our submission to Treasury on 23rd December 2022 which provided feedback on the future regulatory framework for buy now, pay later.

We acknowledge that our previous submission was ambitious in seeking broader changes to the Credit Act; however, we are pleased that Treasury has taken steps to address issues we raised in our feedback relating to licensing, scalability and credit reporting.

Our expertise and experience are in relation to assessing the financial situation of the customer and our comments in this submission are principally about Section 28HAD of the Exposure Draft.

Credit Information

In relation to Credit Information (Section 28HAD parts 2, 3 & 4), it is our understanding that Treasury is proposing that LCCC Credit Providers obtain the following from a credit reporting body:

- “Negative” credit report where the LCCC contract is less than \$2,000, or
- “Partial” credit report where the LCCC contract is \$2,000 or more.

As discussed in our submission of 23rd December 2022, the current Credit Reporting framework poses significant challenges in adequately supporting the assessment of the financial situation of a customer. While we will submit our reasons for this view as part of the planned review of the broader credit reporting framework scheduled for October 2024, we believe that the value of credit reporting information for LCCCs under the current regime, and in respect of the currently proposed LCCC regime, is deeply problematic.

In our view, the primary objective for including credit reporting information in the assessment of a customer's financial situation is to understand their level of indebtedness based on their current credit liabilities as well as their credit history. Negative credit reports do not adequately provide the depth and breadth of data required for this assessment. Typically, a negative credit report displays:

- The length of time the customer has had a record on the CRB's database.
- Details of credit for which the customer has applied (called a “credit enquiry”), but not whether it was approved.
- Details of serious adverse credit information such as loan defaults (generally 180 days past due), bankruptcy or court judgements.

The negative report does not provide information about a customer's current credit facilities, which means the Credit Provider will not be able to identify the customer's level of indebtedness from the credit report. As a result, the negative report provides no conclusive information to support an assessment of the customer's financial situation.



What we have found across industry is that negative credit reports create the need for a highly inefficient process whereby the Credit Provider needs to go back to the customer to make additional inquiries about any credit enquiries that are present on the report but for which there is insufficient information. In order to identify customers at risk of financial difficulty, this will also be the case for LCCCs.

The use of a Partial Credit Report does not completely solve the problem of evaluating the level of indebtedness and the credit history of the customer, but it is a big step in the right direction.

In terms of indebtedness, if mandated, a Partial Credit Report would provide the LCCC with a list all of the customer's credit facilities reported to the particular CRB. Using this in an appropriate serviceability algorithm, the Credit Provider can assess whether the customer could face financial difficulty from increasing their indebtedness by taking out additional credit through an LCCC.

Regarding credit history, like the negative report, the Partial Credit Report only contains details of serious adverse credit information. While not as powerful as a "full" credit report which includes detailed repayment history information, it will only alert the Credit Provider to the most serious red flags on customers with very poor credit history.

Notably, if the requirement were for LCCC providers to obtain a Partial Credit Report, the Principles of Reciprocity and Data Exchange (PRDE), which administers the transfer of data to and from a credit reporting body (CRB), would require those LCCC providers to submit data to the CRB at the same level that they request it. This means that LCCC providers would be required to include details of the customer's LCCC facilities to the CRB for inclusion on the customer's credit record. As a result, all Credit Providers that access a particular CRB will be able to see that the customer has one or more LCCCs – a far more efficient and reliable process than would result if only a "Negative" credit report is required to be obtained by LCCCs. An additional benefit of inclusion of LCCC in Partial Credit Reporting is that will provide a mechanism for young customers (where LCCC has a high take-up rate) to build a meaningful credit score.

While this does not solve the problem of differing data between CRBs, it provides a material step in the right direction that could be further advanced under the planned review of the credit reporting framework scheduled for October 2024.

Differentiation based solely on the size of the LCCC facility

In our view, the requirement for different types of credit reports based solely on the dollar amount of the LCCC is of no value as it does not consider the financial circumstances of the customer – a central and, in our view, sound tenant of the responsible lending regime. We found through our work with Sydney University that for some customers, even a LCCC of less than \$2,000 can cause financial difficulty. While harm will be unlikely to occur for most LCCC users, it is highly likely to eventuate for those for whom the amount of credit is more material (relative to their income) or who already have substantial credit, which would be revealed in a Partial Credit Report.

It should be noted that the process for digesting Partial Credit Report information into the systems of a Credit Provider is no more difficult than accessing negative information. The delivery of all types of credit reporting information has been largely automated by the CRBs through well-established APIs between their system and the Credit Providers' system.

Using Partial Credit Report information in a serviceability algorithm would be straightforward and generate an immediate real-time response. In our experience, such an approach would not mean an undue delay in the LCCC approval process, nor would it impose high costs to implement, either for the CRBs or for LCCC providers.



We see mandating Partial Credit Report reporting across the full spectrum of LCCC regardless of amount as striking a far better balance between consumer protection and Credit Provider efficiency. To compromise the core responsible lending tenant is neither justified nor necessary. We contend that, at a minimum, obtaining a Partial Credit Report (and the associated provision of such information to CRBs):

- is not an excessive impost on LCCC providers;
- delivers far greater efficiency than the alternative (i.e. only “negative credit reporting”);
- enhances the credit reporting ecosystem for all users; and
- offers demonstrably better consumer protection.

Other Information

In relation to Other Information (Section 28HAD part 5), it is our understanding that Treasury is proposing that LCCC Credit Providers obtain information about income and expenses to support the unsuitability assessment policy required in Section 28HAF. As unsuitability assessment includes assessment of customer financial situation, there is still a need to ensure the LCCC facility will not cause the customer to suffer financial difficulty.

As discussed in our submission of 23rd December 2022, in simple terms, capacity is defined by the equation of net income, less expenses, and less financial liabilities. Customers with high capacity are less likely to suffer financial hardship than those with low or negative capacity. We have evidenced this through our work with Sydney University, where it is clear that better-off customers with a good credit history do not fall into financial difficulty even if they have an LCCC debt of \$2,000 or more. However, repaying even a small additional LCCC loan can result in significant financial difficulty for those on low incomes or with proportionally large credit liabilities.

We note that Section 28HAD part 5 defines three types of information:

- a) the income of the consumer;
- b) the expenditure of the consumer;
- c) any low-cost credit contracts, small amount credit contracts or consumer leases to which the consumer is currently a party.

It is our view that item (c) should be defined as credit liabilities rather than just LCCC, SACC, and consumer leases. In our view, a Credit Provider cannot have an effective unsuitability assessment policy unless they consider all credit liabilities of the customers.

The key issue is understanding the customer's financial position and ability to repay the LCCC. Partial Credit Reporting is a good step towards this goal.

Summary

In summary, we suggest that a Partial Credit Report be obtained for a LCCC regardless of the dollar amount. This can be achieved by removing Section 28HAD part 2 and removing “will be \$2,000 or greater” from Section 28HAD part 3 (a).

We suggest that LCCC Credit Providers be required to seek to obtain information about all of the customer’s credit liabilities. This can be achieved by altering Section 28HAD part 5 (c) to read:

- c) the credit liabilities of the consumer.

Yours sincerely,

Steve Johnson (Director)

Kadre is a community of risk, retail credit, compliance, and data science specialists that provides advisory and consulting services to the financial services industry. The Kadre community comprises former senior executives of many large institutions, fintechs and service providers in the consumer lending sector. Many of these executives were at the forefront of the development and implementation of major initiatives such as Comprehensive Credit Reporting and Responsible Lending Obligations. With this knowledge and experience, Kadre is well-placed to offer practical and well-informed feedback on critical areas highlighted in the Treasury Consultation paper.

Kadre has provided this submission as an independent group seeking only to protect consumers from financial harm by creating a fair credit regime that is in the best interests of the Australian economy.

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