

SHOULD WE HAVE POSITIVE CREDIT REPORTING?
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WHAT COULD LENDERS DO?

VS

WHAT WOULD LENDERS DO?

First of all I wish to say that I do not plan to say much on the privacy aspect of this issue. This doesn't mean that it is not an important part of this debate – consumers care about their privacy and any changes would put more of our personal information “out there” for our phone or electricity company – even our lawyer or orthodontist! However, for the purpose of this brief presentation I will focus on the question:

“What would lenders do?” - as opposed to “What could lenders do?”

There has been some clever marketing of positive credit reporting. It has emphasised potential benefits and ignored detriment that is likely to arise from an overall increase in consumer debt. The research commissioned by Mastercard (and I have general concerns about that research) found that there would be a “larger consumer credit market” (this was the one point omitted from the press release!). The push for expansion of credit reporting has also relied on simplistic arguments for a very complex issue. I know that's what marketing – and lobbying – is all about, but let's consider some of the claims:

- Credit providers will use the additional information to lend more responsibly;
- There will be less defaults;
- The pay day industry will decline as “battlers” get bank loans etc.

I don't have any arguments with the Barren Staten research, that shows more information could improve risk assessment, but I do have arguments with the way assumptions have been made about what credit providers would do if they could access more information. So, let's take some of these claims individually.

Lenders could lend more responsibly.

Yes, they could – and many lenders could lend more responsibly now, but it's not profitable to do so.

It is only half true that both lenders and borrowers benefit from a reduction in defaults. Many lenders target a particular part of the market, where defaults are high – and credit is priced to match the risk. More information could assist in more accurate pricing of risk – but this doesn't

make the lending any more responsible. We see an increasing number of lenders who do not even ask about income levels, but base a consumer loan on value of house equity alone.

One thing I think we all agree on is that access to more information will increase the overall level of consumer debt. Some of this increase could be “responsible” lending – but I suggest that we would see a significant increase in irresponsible lending as well.

Lenders could refuse credit if they know the borrower already has too many other debts.

Some lenders will – but again, it will depend on the type of lender. We know that many lenders specialise in borrowers who already have credit problems. Such a lender may further protect itself with security or a co-borrower, or may price the credit accordingly – but again this may help the lender’s bottom line, but won’t necessarily mean that the credit product will not cause harm.

Lenders could be held to account for their lending decisions.

This is an interesting claim. I work for a legal service that deals day in, day out, with irresponsible lending. In many cases the lender knew, or should have known, about the borrower’s circumstances. Does this mean that we can “hold the lender to account” in any way? With the exception of bank lenders (where the Code of Banking Practice provides some obligations) – no we can’t. We need major changes to credit and broker regulation that would place obligations on industry to lend responsibly – but would access to more personal information by lenders help us pressure lenders to do the right thing? In most cases, NO.

Lenders could use additional data to reduce defaults.

Yes, they could – but it will be up to each lender to decide whether they want to use the additional data to reduce defaults, to approve loans faster (perhaps by seeking less information from the borrower) or to lend more (and maintain the same default rate). If lenders choose to lend more – even maintaining their current default rate would increase the number of defaults overall.

Would some lenders simply use credit reporting information instead of other data such as income information? A current example is where banks make offers to increase credit card limits. The banks have

payment and other data, and for marketing purposes, choose to rely on this data alone to offer increases – rather than inviting the consumer to apply and provide income information (as well as enabling access to the credit reporting system). With more credit reporting information available lenders may choose to simply seek less information from other sources and thereby offer faster assessment. “30 second, no application finance?!”

Interest rates would come down – I assume that for some consumers they will, and for others they won't. Risk assessment can be used just as much to increase rates for risk, to price high risk products (such as a 70% credit card we've seen introduced overseas), as it can to reduce rates for lower risk consumers. While there may be arguments in favour of such pricing, we can guess who might be the winners and the losers here.

Under-served consumers would be able to have access to credit, and those borrowing from pay-day lenders and such will be able to get loans from mainstream lenders.

Yes, perhaps – but it's also likely to move some consumers the other way, from mainstream lenders to fringe lenders. Judging by what we see in the United States (where lenders can assess extensive credit reporting data), it is difficult to believe that the availability of more information will reduce the size of the fringe lending industry. It is naïve to suggest that consumers who cannot access credit now, but could under a changed credit reporting regime would all be “credit worthy” – or that the only products they would be offered would be reasonably priced, fair products.

Conclusion

Given that a change to the credit reporting regime is likely to increase the current high levels of consumer debt, the key question (that the hype about positive credit reporting does not answer) is:

“How would lenders change their practices and products – and how would this impact on different borrower groups?”