14 April 2022

Claire McKay,
Director
Sectoral Assessments
Consumer Data Right Division
The Treasury
Langton Crescent
PARKES ACT 2600
by email: data@treasury.gov.au

Dear Ms McKay,

CDR Sectoral Assessment for the Open Finance sector - Non-Bank Lending

Thank you for the opportunity to comment on the CDR Sectoral Assessment for the Open Finance sector - Non-Bank Lending. This is a joint submission from the Financial Rights Legal Centre (**Financial Rights**), Financial Counselling Australia (**FCA**) and Consumer Action Law Centre (**Consumer Action**).

We believe that the Non-Bank Lending consultation paper focusses solely on the benefits of the application of the CDR to the non-bank lending sector and pays scant regard, if any, to the risks and threats that arise for consumers. The paper merely states that

> *"any sharing of non-bank lending data (which is likely to be the same type of data as for banking loan accounts) as a result of designation is likely to be appropriately managed through these existing mitigation strategies."*

We respectfully disagree with this view and this approach to designation and its impacts on consumers.

We do not deny that there are benefits of applying the CDR to the non-banking sector for some consumers. The application of the CDR has the potential to provide opportunities for greater financial inclusion if done with appropriate guide rails. It could improve the accuracy of lender's responsible lending checks. It could also assist other expected CDR participants to improve their processes including say, the general insurance sector obtaining financial data in insurance investigations more quickly if the appropriate protections are in place to prevent unfair fishing expeditions.

But all these mooted benefits do not exist in a vacuum. They must be balanced with an understanding of the sector the CDR is about to be applied to and the very real potential for it to exacerbate existing consumer harms and introduce new harms, if not appropriately constrained and mitigated.

Applying the CDR to the non-banking sector should be done with these issues clearly in mind. It is important to acknowledge that the non-banking sector serves different demographics, functions and purposes in the financial services sector. There are companies operating in this sector that have historically contributed to substantial consumer harm, and are not accountable to industry codes of any real value. When examining this more closely the following risks emerge:

- CDR will serve to support and increase poor non-bank lender behaviour that profiles risk and targets financial hardship;
- CDR will enable social scoring for credit provision;
- CDR applied to non-bank lenders enables circumvention of Comprehensive Credit Reporting regulations; and
- Applying CDR to non-bank lenders magnifies the harms to joint account holders under the opt-out consent model.

In order to mitigate these risks, we recommend a series of reforms including:

- limiting the scope of eligible participants to those credit licensees subject to the Comprehensive Credit Reporting regime;
- restricting specific uses of data including the collection of data to identify financial hardship for the specific purpose of direct marketing further high credit products;
- prohibiting non-bank lenders from using CDR data to circumvent the rules of the Comprehensive Credit Reporting regime;
- introducing a fair collection requirement under Privacy Safeguard 3;
- requiring "trusted advisors" to be accredited;
- introduce an offence for unaccredited firms to obtain, use or hold data obtained via the CDR;
- introducing a data fiduciary standard for CDR participants;
- reverting back to an opt-in consent for jointly held accounts;
- decreasing the complexity of the consent regime; and
- support the introduction of an unfair trading practices prohibition

The Non-Bank Lending Sector

The non-banking sector serves different demographics, functions and purposes than the ADI banking sector

The consultation paper describes the non-bank lending sector in a one dimensional fashion, taking a functional, product-centred approach. The paper barely touches upon the different business models in play and varying levels of consumer engagement, outside of the fact that:

- consumers "engage with a range of non-bank lending products including credit cards, home loans, personal and business loans on a regular basis,"
- small businesses are active in the space, and
- that payday lenders can charge higher fees.

The description of a consumer lease in the paper also incorrectly states that lessees may be given an option to buy a product at the end of a lease. Such an arrangement would actually be considered a sale of goods by instalment contract.[1] Consumer leases are explicitly defined to involve an arrangement where the lessee **does not** have a right or obligation to buy the goods at the end of the lease.[2] This is a good example of non-ADI lenders that adopt business models with a high risk of consumer harm. Consumer leases are an avoidant model lessors use instead of a sale of goods by instalment contract so their products are not subject to the 48% annual cost cap that would otherwise apply.

The only additional colour to this description centres on the complexities of differentiating between lending products, and the difficulties of comparing and switching products. While these are important and legitimate issues they do not paint the full picture.

What is missing from this description is the fact that non-bank lenders specialise in providing loans for "non-conforming borrowers." That is non-bank lenders provide finance to those with credit profiles who do not meet the authorised deposit-taking (**ADI**) banking sector standards – including self-employed people, first time buyers, and property investors.

More importantly, "non-conforming borrowers" also include those with people with impaired credit histories and bad credit ratings, those experiencing financial hardship and those that are generally considered a higher risk due to lower incomes. This includes, among others, people on Centrelink payments, seasonal workers, and others with erratic, unreliable income sources, as a result of the gig economy.

The number of Australian's experiencing financial hardship is significant. For example, 2019 research found that 2.1 million Australians are under severe or high financial stress.[3] And for many of them they have no choice but to engage with the non-bank lending sector many of

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[1] *National Consumer Credit Protection Act 2009*, Schedule 1 (National Credit Code), s 9.

[2] National Credit Code, s 169.

[3] NAB and the Centre for Social Impact, Financial Security and the influence of economic resources, December 2018, https://www.csi.edu.au/media/2018-Financial-Resilience-in-Australia.pdf

whom have built business models that specifically *target* financial hardship with higher priced credit. These include:

- small amount credit contract providers (pay day lenders),
- medium amount credit contract providers,
- consumer lease providers;
- Buy Now Pay Later services
- Wage Advance services; and
- unlicensed financial service providers including avoidant credit models such as that offered by Cigno. [4]

As the Senate Economic References Committee Inquiry into Credit and financial services targeted at Australians at risk of financial hardship[5] stated in 2019

> *The intractable maths of low income earners' family budgets pushes them towards the marginal credit products that were examined over the course of this inquiry—products such as payday loans, consumer leases and, in the end, debt management firms. Government can and should improve the terms under which these products are offered. Products that are targeted at Australians at risk of financial hardship should not be allowed to take advantage of their financial vulnerability. … Inclusion in Australia's financial system is critical for a successful and robust economy and social framework. Low income Australians should not be excluded from fair and appropriate access to financial services, and not be relegated to the use of high cost and potentially harmful products.*

We acknowledge that the CDR's role is not to necessarily to solve all the issues present in a designated sector - this despite the fact it seeks to solve other issues present including complexity, problems of switching and comparison. It is however important to at least understand the regulatory context and consumer harms present in a sector to ensure that the introduction of the CDR does not

- exacerbate existing harms;
- enable circumvention of the extant regulations and limitations preventing those harms; nor
- introduce new harms.

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[4] ASIC has attempted to use its product intervention powers to prevent Cigno avoiding the credit laws. See https://asic.gov.au/regulatory-resources/find-a-document/consultation-papers/cp-355-product-intervention-orders-short-term-credit-and-continuing-credit-contracts/

[5] Senate Economic References Committee Inquiry into Credit and financial services targeted at Australians at risk of financial hardship , 2019 https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/Creditfinancialservices/Report

Unfortunately, as currently conceived, the CDR's application to the non-bank lending sector has the potential to do all three.

Risks arising from the application of CDR to non-bank lending that require mitigation

We raise the following key concerns:

CDR will serve to support and increase poor non-bank lender behaviour that profiles risk and targets financial hardship

As we have raised in previous consultations, we are aware from our casework that some non-bank lenders obtain consumer's bank account passwords to screen scrape financial data. In so doing they hold on to these passwords and use them at later times to identify if a bank account is low in funds. If the account *is* low in funds they then proceed to spam the consumer with direct marketing material offering further high cost loans.

While access to quick credit may lead to benefits for some consumers, the reality is that this unscrupulous behaviour pushes many people into a spiral of debt.

This unethical practice is highly likely to become commonplace and more widespread once CDR is applied to the non-bank lending sector.

This is because Privacy Safeguard 3 - regarding collection of solicited personal information - is drafted in such a way that could give rise to abuse of the consent provisions. There are currently few if any restrictions on how often, how much or how regularly a non-bank lender can examine a consumer's financial data in order to identify financial hardship and subsequently target them with offers of additional credit. There is also little preventing them from selling or providing this information to other related or unrelated businesses who target people in financial hardship such as debt management firms. Critically, Privacy Safeguard 3 lacks an explicit "fair collection" requirement which would act to prevent and discourage unfair practices.

The CDR's current over-reliance on consent and disclosure to mitigate consumer harm is also unlikely to prevent unfair behaviour. Placing the onus on individuals to engage, comprehend and act upon the complex information being presented to them, or recognise the risks involved, when choosing to engage with the non-bank lending sector is unrealistic, is counter to our understanding of the failures of disclosure and ignores the low levels of literacy and numeracy in the population. This is magnified for people experiencing financial hardship. The relationship between a potential high cost lender and someone experiencing financial hardship is one characterised by an inherent imbalance of power where the consumer feels they have little choice but to agree to any and all consents, in order to obtain the credit they need.

CDR will enable social scoring for credit provision

A key use case for non-bank lenders accessing non-financial CDR data sources is likely to be social scoring for credit provision.

This has some marginal potential to improve financial inclusion for some but is also highly likely to lead to significant and inappropriate price discrimination and risk profiling.

What this means is that there will be some winners who may be able to access cheaper or at least affordable forms of credit, but there will be many losers who will be subject to high and untenable rates of credit. While this already occurs, the Consumer Data Right, supercharges this ability. The speed and analytical power that the CDR can bring to – and is core to mooted benefits of the regime - will concurrently play a central role in increasing risk segmentation and the targeting of financial hardship through inappropriate price discrimination and high cost credit. The CDR has the potential to widen the gap between the credit-haves and the credit-have-nots.

Access to CDR data by non-bank lenders will enable the circumvention of Comprehensive Credit Reporting regulations

Lenders in Australia share information about consumers' credit accounts, including consumers' repayment history with credit reporting bodies under the new Comprehensive Credit Reporting (**CCR**) regime. CCR means lenders now have more detail, and more context about how an individual interacts with credit, including positive financial behaviour. The scheme is mandatory for the big four lenders and voluntary for other lenders including non-bank lenders.

Previously, a credit report mainly showed 'bad' (also known as negative) credit behaviour such as payment defaults and bankruptcies. Now under CCR, a credit report also includes "positive" information like on-time monthly repayments. If an individual manages their debt well, their credit report will show a 24-month history of them making their repayments on time.

This additional information provides a more complete picture of a customer's credit history and means that credit providers may be better able to match their provision of credit to a customer's individual needs.

There are however significant rules and regulations in place under the newly introduced CCR regime to restrict the use of repayment history information, and financial hardship information. These restrictions are in place for important policy reasons – that is, to ensure the right balance between encouraging consumers to proactively seek out hardship arrangements in their best interests (and in turn, not discouraging those consumers from seeking these arrangements by potentially threatening their credit rating or score) and banks having enough information to make sound responsible lending decisions.

Some of these rules include:

- only licensed credit providers can share and receive repayment history information;
- financial hardship information is deleted from credit reports after 12 months – versus 24 months for regular repayment history information - so that a temporary setback does not have a lasting impact on one's credit report;
- financial hardship arrangement information cannot be included in the calculation of any credit scores developed by credit reporting bodies;
- limits are in place on what a lender can do with financial hardship information when they do find out e.g., a lender cannot use the information as the sole basis for closing a credit card or reducing a limit;

- the circumstances in which other lenders can be told about your financial hardship arrangement are also limited – so that other lenders can be told if you apply for another loan with them, but not if they are trying to collect overdue payments on existing loans.

The application of CDR to the non-bank lending sector however has the real potential to undermine these sensible policy settings and limitations. This can occur by CDR providing greater access to a consumer's entire financial history, such that lenders will be able to undertake analysis that provides insights in line or equivalent to that captured under the credit reporting system. This includes those licensees who are required to participate in the mandatory credit regime and those who are currently not required to (including pay day lenders).

In other words, access to the CDR will provide the non-bank sector (and potentially all other CDR participants) with the ability to circumvent the long negotiated limitations of the CCR regime.

Rules will need to be put into place in the CDR regime to prevent this outcome.

A further concern would arise if non-licensed credit providers in the non-bank lending sector such as Buy Now Pay Later services are provided with access to detailed financial data under the CDR. If they were, they too will have an ability to gain access to information repayment history information and financial hardship information using the right analytics, and avoid the current restrictions. This would be a particularly perverse outcome if providers of unregulated credit designed to avoid consumer protections (such as BNPL) used the CDR like this, when they are not even compelled to use financial data to lend responsibly.

Again the CDR cannot be seen to be neutral or only positive in its application and impact - restrictions will need to be put in place to reflect the sectoral regulations already in place.

Applying CDR to non-bank lenders magnifies the harms to joint account holders under the opt-out consent model.

By expanding the ability for joint account holders to obtain higher cost credit from the non-bank lending sector, without the active prior consent of their joint account holder, the potential for harm by perpetrators of family violence and economic abuse increases exponentially.

We remain of the view that the decision to introduce an opt-out consent regime for joint account holders contrary to the regime's own consent principles needs to be reversed.

Mitigating the risks in applying CDR to the non-bank lending sector

The risks outlined above are not fully mitigated under the current rules. The following reforms need to be considered:

- Limit the scope of eligible participants to those with a credit licence and who are mandatorily or voluntarily subject to the Comprehensive Credit Reporting regime.
- Restrict specific uses of consumer data – for example:

- limit the regular (or irregular) collection of financial data to identify when people are experiencing financial hardship and subsequently use this information to directly market further high credit products or sell this information to others;
    - introduce rules to prevent non-bank lenders (and all other CDR participants) from using financial data obtained via the CDR to circumvent the rules of the Comprehensive Credit Reporting regime;
- introduce a fair collection requirement under Privacy Safeguard 3. Privacy Safeguard 3 currently lacks an explicit "fair collection" requirement, which may encourage unfair practices;
- introduce an offence for unaccredited firms to obtain, use or hold data obtained via the CDR to prevent unaccredited non-bank lenders simply asking consumers to download their own data and provide it them.
- improve consent processes to ensure there is less reliance on mere disclosure and placing the entire onus on the consumer. This must include
    - introduce a data fiduciary standard for CDR participants. A data fiduciary standard is avoids an over-reliance on disclosure and consent by ensuring that those who hold data need to put the consumer's well-being first;[6]
    - revert back to an opt-in consent model for jointly held accounts to prevent economic abuse; and
    - decrease the complexity of the consent regime with its multiple forms of consent and multiple dashboards;
    - require "trusted advisors" to be accredited and agree to meet the requirements of the *Privacy Act* in line with the recommendations of the Privacy Impact Assessment.
- Support the introduction of an unfair trading practices prohibition to the Australian Consumer Law. As recommended by the ACCC in its Digital Platforms Inquiry, an unfair trading practices prohibition would eliminate deliberate predatory practices aimed at targeting consumers (like those experiencing financial hardship) with sales approaches when they are vulnerable.

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[6] For more information on the Data Fiduciary idea see Financial Rights' submission to the Independent Statutory Review of the Consumer Data Right (to be provided). Also see Balkin, Jack The Fiduciary Model of Privacy, *Harvard Law Review Forum*, Vol. 134, No. 1 (November 2020) https://harvardlawreview.org/wp-content/uploads/2020/10/134-Harv.-L.-Rev.-F.-11.pdf; Richards, Neil M and Harzog, Woodrow, A Duty of Loyalty for Privacy Law, 99 *Washington University Law Review* 961 (2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3642217 and Isabelle Guevara, *Data Fiduciaries And Privacy Protection In The Digital Age*, August 27, 2021 https://www.cba.org/Sections/Privacy-and-Access/Resources/Resources/2021/PrivacyEssayWinner2021#_edn24

Concluding Remarks

Thank you again for the opportunity to comment. If you have any questions or concerns regarding this submission please do not hesitate to contact Drew MacRae, Senior Policy Officer, Financial Rights on (02) 8204 1386 or at drew.macrae@financialrights.org.au

Kind Regards,

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Chief Executive Officer
Financial Rights Legal Centre