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EQUIFAX

Starting in 1967 as the Credit Reference Association of Australia, a mutual made up of retail stores and large banks, we remain Australia's leading provider of credit risk and due diligence solutions, employing around 1,000 people in Australia and New Zealand and, since 2016, have been part of Equifax, the global data, analytics and technology group headquartered in Atlanta, USA.

We welcome the opportunity to comment on the Treasury's *Regulating Buy Now, Pay Later in Australia* Options paper [the Options paper]. Equifax supports a modified Option 3, requiring BNPL to be fully brought under the National Consumer Credit Protection Act but subject to provisions of Regulatory Guide 209 that have been modified, simplified and scaled back to be suitable for the characteristics of BNPL.

Our submission on regulatory options for Buy Now Pay Later [BNPL] is primarily focused on what is now being described as traditional BNPL - non-bank providers offering low amount BNPLs. From this segment, Equifax receives credit reporting information from a number of significant providers, who also consume credit risk solutions from Equifax, typically at the initial enquiry stage ("origination"). We note that while some BNPL offer a facility akin to a line of credit, others offer a transaction-by-transaction product; absorbing transaction accounts into the existing credit reporting data standards creates challenges, which industry association ARCA is addressing.

KEY PRINCIPLES FOR REFORM

- 1. The regulatory framework for BNPL must not impede BNPL's automated, low-friction, origination experience.**

To achieve this, Equifax supports Option 3 via a modified Regulatory Guide 209 (RG 209). The National Consumer Credit Protection Act and RG 209 should be the central framework document for all lending. Presently it includes scaled up obligations for payday loans/small amount credit contracts (SACCs); in future, to meet the needs of BNPL and the often very small amounts involved, RG 209 should allow for *scaled down* obligations.

We note New Zealand has announced it will bring BNPL under its existing regulatory framework, but with modifications to the existing responsible lending code:

- BNPL will be brought under New Zealand's Consumer Credit Act (CCCFA), similar to NCCP, but the obligations imposed will be applied proportionately to the size of the BNPL.
- For smaller BNPL below a threshold (likely \$600), the NZ Government proposes credit reporting checks.
- For loans above the threshold, BNPL lenders will be required to assess affordability - but how these assessments are done will be subject to further consultation.

A similar approach should be adopted here and already the Options paper refers to the use of credit score checks as a proxy for assessing a consumer's credit risk, particularly for low amount BNPL.

This light touch approach would see an amended RG 209 applying core consumer protections to BNPL (e.g. membership of external dispute resolution, or protection for victims of financial abuse) while modifying other provisions or waiving them entirely.

2. Like other credit products, there needs to be insight into BNPLs wider impact on people & the economy. This can be achieved via BNPL providers reporting on a range of metrics to either ASIC or Treasury, who in turn should publish aggregated insights.

BNPL launched in Australia in 2015, representing the Fintech evolution. Six years later BNPL is being offered by some Big 4 banks. Understanding how this credit product is impacting the economy and Australian households is still developing. Other forms of household credit have formal reporting requirements to APRA, decades long analysis by ASIC and extensive academic research. Collectively, there is an extensive understanding on the use of credit through recessions, credit booms, high unemployment and property booms.

As part of the current reforms, Equifax calls for BNPL providers to be required to report to either ASIC or Treasury on a range of metrics, such as the numbers of people who fail to meet their BNPL commitment in full; the average original BNPL amount and subsequent increased limits; and the credit risk assessment practices undertaken, including the extent and nature of supply and use of credit risk information.

Overlaid with demographic information, this undertaking, collected commercially in confidence and released in aggregate form, would give the debate about BNPL some hard evidence to underpin assertions on the benefits or harms of BNPL. It would also greatly assist on credit reporting issues, which the Options paper has deferred consideration of to the scheduled independent review due to report by October 2024.

3. The regulatory framework should enable and support contribution of credit reporting information; this helps other credit providers to better assess credit inquiries from people who are, or are at risk of, becoming over committed.

The Australian Government has made clear its belief that BNPL is credit, similar to New Zealand where BNPL is now being described as a loan. For credit providers considering any credit inquiry, understanding the extent of a person's total repayment obligations is critical. In the instance of BNPL, the existence of a BNPL enquiry on a credit report may merely reflect a \$25 pizza or a shouted round of drinks.

Where a BNPL becomes of greater concern is where higher amounts are subsequently granted, or a consumer has multiple BNPL accounts, and the total obligations create the potential for a consumer to be entering into financial stress. Equifax note - and support - consumer advocate's call for BNPL providers to be reporting consumer credit liability information to CRBs (i.e. the total current credit limit a consumer has).

Reinforcing this is research from Equifax UK, which looked at two different months and showed a significant percentage of monthly repayments for unsecured credit went to pay BNPLs, particularly for those in the worst financial health scoreband where payments to BNPLs made up a third of their payments to unsecured credit (e.g. credit cards and personal loans).

4. Contribution of credit reporting information, including repayment history information, lifts financial inclusion of consumers, particularly those who lack significant information on their credit report and may struggle to access mainstream credit ("thin file").

Equifax Australia research shows that 2.5 million people aged 18+ have little or no information on their credit report ("thin files"), creating potential barriers to accessing mainstream credit or accessing it at the best price. Thin files often occur in younger demographics, as is commonly found with BNPL enquiries - 41% of the BNPL enquiries were from people aged between 18 and 30 (versus 28% of the overall population).

The same demographic attracted to BNPL have deserted credit cards; but whereas young people holding a credit card and meeting their monthly obligations are positively building their credit risk profile, traditional BNPL providers do not provide this information.

Research from Equifax USA showed the inclusion of repayment history information helped consumers, with on-time repayment history information lifting an average FICO® Score by 13 points and an increase of 21 points for those with either a "thin" credit file (two or less accounts) or a "young" credit file—where all credit history is no more than 24 months old.

For the sake of clarity, we note that while this age demographic are very likely to have a mobile phone, monthly repayments on a telco cannot assist to build a positive credit file. This is because Telcos are not eligible for an Australian Credit Licence (ACL) - and an ACL is a necessary requirement for supplying repayment history information on a credit file. Under the Options paper, options 2 and 3 would mandate BNPLs to hold an ACL, enabling the contribution of RHI information, as is currently the situation with BNPL offered by banks.

5. The introduction of a regulatory framework for BNPL should not impede further credit innovation

In 2009 the then Minister for Financial Services introduced the National Consumer Credit Protection Bill, displacing state-based regulation and introducing an Australian Credit Licence. In February 2010 ASIC issued its first version of Regulatory Guide 209. Simultaneously, reforms to the Privacy Act, including Part IIIA and credit reporting, were also in development.

All of this was done in an environment where consumers were rapidly shifting from in-branch physical applications for credit to desktop website applications. Credit reporting then did not allow for positive information and bank transaction data required paper copies of statements.

The regulatory frameworks of time are still in place today. Rapid changes in technology, a maturing expanded credit reporting regime and the concept of Big Data are challenging those frameworks. BNPL is only one example, albeit a very successful one, of recent innovation.

Consideration should be given to a rewrite of RG 209 for more adaptable, simplified lending governance, embedding core consumer protections across all products and then allowing for more tailored requirements to be developed specific to meet the needs of emerging credit innovations.

BUY NOW PAY LATER RESEARCH

USA Equifax

In July 2021 Equifax USA, in conjunction with FICO, conducted a study in July 2021 to assess the impact of BNPL on consumer credit scores.

Anonymised data on 123,000 consumers was used; this sample population had subprime credit scores (~90% had a FICO score below 670). All had at least one Buy Now, Pay Later offered as a revolving line of credit with an average credit limit of \$USD 1,212 and an average duration of four months.

- The majority of consumers in the study were helped by having an on-time BNPL repayment history information on their credit file, with an average FICO® Score increase of 13 points
- The study showed that individuals with either a “thin” credit file consisting of two or less accounts with repayment history or a “young” credit file - where all credit history is no more than 24 months old - saw an average FICO® Score increase of 21 points with the addition of on-time BNPL repayment history information to their credit file
- BNPL can also help consumers rebuild their credit. Consumers who had significantly late payments reported on their traditional credit file experienced an average FICO® Score increase of 13 points with the addition of on-time BNPL repayment history information to their credit file

Subsequently Equifax was the first credit reporting body to introduce a formal standard process for reporting BNPL for inclusion on traditional consumer credit reports.

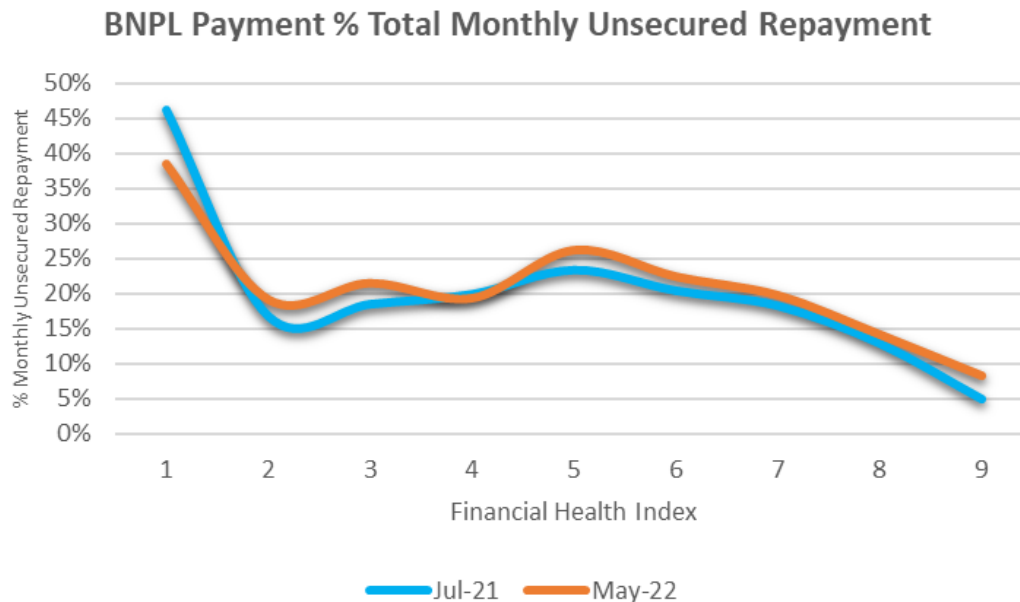
UK Equifax

Equifax UK analysed bank transaction data in 20,000 consumer current accounts for two months, July 2021 and May 2022

These were assessed for the financial health of those consumers, using Equifax’s Financial Health Index (FHI) from 1 (least healthy and least likely to repay credit) to 9 (most healthy, most likely to repay credit).

The results show:

- The share of consumers who used BNPL was lowest in the groups with the very worst (1) and very best FHI scores (9).
- Those most likely to use a BNPL were a consumer with a very low FYI score (2)
- The share of consumers using BNPL was fairly consistent across other groups
- A rising percentage of monthly repayments for unsecured credit goes to a BNPL account.
- For people of average financial health (group 4,5,6), between 20-25% of their monthly repayments on unsecured credit went to a BNPL. For those in the worst financial group (1), this figure is more than 35%.



Equifax Australia

Equifax research was done on BNPL enquiries received in the financial year 2020/2021.

- Half of consumers applying for a BNPL had no other mainstream credit facilities on their credit file; essentially their credit reports had negative only information. One in four had little or no prior credit history at all.
- A third of applicants had a below average credit score (versus 15% overall population). These scores typically indicate higher risk credit enquiries, a person at increased risk of future defaults.
- 41% of the BNPL enquiries were from people aged between 18 and 30 (versus 28% of the overall population).

Provision of comprehensive credit reporting information from BNPL providers would allow this cohort to demonstrate their ability to manage small, low cost credit and improve eligibility for mainstream credit in future.

Academic research

In March 2022, an academic paper¹ *“Buy Now, Pay Later (BNPL)...On Your Credit Card”* was released claiming to be the first quantitative BNPL research using credit card transaction data. They found that a significant portion of UK consumers charge their interest-free BNPL to their credit card (a higher interest product) and such practices were more common among those in more deprived areas:

- In December 2012, 19.5% of active credit cards had at least one transaction by a BNPL provider
- The incidence of paying a BNPL on a credit card was higher in more deprived areas and younger consumers
- The median value of BNPL spending over a year on cards incurring a BNPL charge was £157 (~\$266 AUD)

¹ Guttman-Kenney, Benedict and Firth, Chris and Gathergood, John, Buy Now, Pay Later (BNPL)...On Your Credit Card (March 10, 2022). Available at SSRN: <https://ssrn.com/abstract=4001909> or <http://dx.doi.org/10.2139/ssrn.4001909>