



RECOMMENDATIONS

1. We support the core principles of the consultation paper - bring Buy Now Pay Later under the Credit Contracts and Consumer Finance Act and a requirement to use and supply comprehensive credit reports

Lending has benefited from Aotearoa New Zealand having a mature set of standards for both responsible lending checks and the credit reporting information that underpins it.

These will be strengthened by adopting key proposals made in the *Draft Credit Contracts and Consumer Finance (Buy Now Pay Later) Amendment Regulations 2022 consultation paper* [‘consultation paper’].

Equifax supports the proposal to include BNPL under the Credit Contracts and Consumer Finance Act (CCCFA). The Consultation paper seeks feedback on two options for BNPL credit risk checks, either by application of the full CCCFA requirements, or by a simpler test of making reasonable inquiries to be satisfied that the borrower can make repayments without substantial hardship.

2. We support mandating use and supply of comprehensive credit reporting information - enabling all lenders to better assess credit applicants and helping consumers to evidence good credit behaviours

The Consultation paper proposes that where the amount of a BNPL is under a threshold amount (proposed to be \$600), then the credit risk assessment required need not be either of the two proposed options, on the condition the BNPL lender both obtains a credit report with comprehensive credit reporting information and supplies the same information.

The addition of BNPL information will assist other lenders to see the full range of a consumer’s commitments and reduce consumer harm from over-indebtedness. In addition, BNPL can enable greater inclusion of Kiwis by providing confirmation that a consumer has successfully met BNPL, helping people to more easily build their credit rating.

3. Use and supply of credit reporting information must align with the existing framework

The use and supply of comprehensive credit reporting information is highly regulated in New Zealand, both by the Privacy Commissioner’s Credit Reporting Privacy Code 2020 and by a set of industry agreed data standards established by the Retail Credit Association of New Zealand (RCANZ).

Industry data standards ensure the meaning of information on a credit report can be universally understood. These standards have been updated to enable BNPL to operate effectively for their more regular payment cycles (weekly or fortnightly instead of monthly).

Supply of information consistent with industry standard is important because:

- It ensures consumers can understand information on their credit report and be able to dispute its accuracy;
- It enables credit reporting agencies to meet the Credit Reporting Privacy Code requirement that information held is “accurate, up to date, complete, and not misleading”;
- It helps lenders who enquire on a new applicant to have a consistent view of credit commitments and incorporate that into scoring.

4. The existing regulatory framework of the CCCFA can support BNPL participation in comprehensive credit reporting, including resolution if transitional issues arise

Historically, lenders in New Zealand have shown a high level of willingness to share credit reporting information, recognising there is a broader benefit for all; most importantly, to avoid consumers getting trapped in a debt spiral.

BNPL lenders have had limited participation in NZ credit reporting. Within the CCCFA, there are mechanisms relating to the use of credit reporting information. These can assist the transition to use and supply of comprehensive credit reporting information.

BACKGROUND

For more than three decades, lenders in New Zealand have looked to Equifax for credit reporting information. Information held on credit reports enables greater confidence in lending and the ability for a lender to reduce the risk of loss creates more competition to offer credit and more competition on the terms of that credit.

People having access to credit is fundamental to creating a more equitable society. Innovations in credit, such as Buy Now Pay Later, help achieve that goal, enabling access for those who might otherwise struggle for approval and whose only alternative may then be high cost small amount loans.

In the past, credit was heavily rationed and eligibility restricted.

For decades after World War II, fundamental household goods such as a refrigerator or carpeting were obtained through hire purchase, with fixed payment schedules extending for many years, incurring significant interest costs. Then, in the eighties, credit cards were introduced and became the preferred form of obtaining goods, with their interest free period and the capacity for customers to vary repayment amounts over a time of their choosing.

Now BNPL has arrived and proven highly attractive to consumers, emerging as New Zealand's fastest growing form of credit; in contrast, credit card applications have dropped by 31 per cent comparing 2022 with 2019.

However, with less than five years of widespread use, there is only limited research globally on the impact of BNPL on consumers and even less so during differing economic conditions (recession) or changed personal circumstances (breakdown of relationships).

The impact of BNPL has triggered concern by regulators in New Zealand, Australia and the UK, with all jurisdictions declaring that BNPL should be regarded as credit. All are now debating the extent to which their existing credit regulation frameworks will then subsequently be applied to BNPL, a debate that has highlighted concerns that a consumer's total credit payment obligations must be readily understood by the consumers themselves and discernible by other lenders considering whether or not to extend further credit.

Unlike a personal loan or credit card, the BNPL amount sought at initial application ("origination") is typically very small (~\$100) and then increases either in the form of consecutive separate transactions or as an increasing ceiling on a line of credit. This pattern of rising credit limits may also be simultaneously repeated with other BNPL providers, resulting in a consumer having to meet commitments of thousands of dollars across multiple BNPL providers.

The proposals set out in the consultation - to include BNPL under the CCCFA, and ensure participation in the New Zealand credit reporting system - can bring consumer benefit and avoid potential consumer harms.

RESPONSE TO QUESTION 4

“Aside from the dollar amount, do you have any comments on how the threshold is drafted in regulations 18I(1) and 18I(2), or the exemption condition requiring comprehensive credit reporting is drafted in regulations 18I(3)(a) and 18I(3)(b)?”

Comprehensive credit reporting

Key Benefits

Greater financial inclusion

Repayment history information shows if a consumer has met a required payment on a line of credit. This helps evidence a person’s recovery from past financial difficulties. It can also help consumers who, because they do not have a mortgage or credit card, have a “thin” credit file, lacking information. This is particularly important if there is a sustained trend away from credit cards in favour of BNPL.

Easier to avoid over indebtedness

An applicant for credit must be able to make payment on the new credit without substantial hardship. This means, in part, that lenders must be able to identify a borrower’s financial commitments. This is particularly important where there is a trend of escalating payment amounts across multiple providers.

Background

Since 2012 credit reports in New Zealand have been able to include the amount of credit extended on a credit account and the repayment history of that account. These elements make up what is known as comprehensive/positive credit reporting and applies to mortgages, personal loans, credit cards, telecommunications and utilities. Being able to see a person’s total payment obligations and how well they are currently managing them is critical when assessing whether to extend further credit, be it mobile phone, home loan or credit card.

New Zealand has a competitive credit reporting environment, with three actively competing credit reporting agencies (CRAs). All aspects of credit reporting activity such as use, disclosure, access, accuracy, correction and retention must comply with the Credit Reporting Privacy Code (“CRPC”) made under section 32 of the Privacy Act 2020 by the Privacy Commissioner¹. To ensure the information on credit reports can be understood by the consumer or lenders accessing the information, data standards have been developed the Retail Credit Association of New Zealand (RCANZ)² (“Data Standards”).

An integral part of the Consultation Paper is that BNPL beneath a threshold (proposed to be \$600) would be exempt from more prescriptive CCCFA affordability assessment on the basis that lenders participate in (i.e. use and supply) comprehensive credit reporting.

¹ <https://www.privacy.org.nz/privacy-act-2020/codes-of-practice/crpc2020/>

² <https://rcanz.org.nz/resources/data-standards/>

Financial Inclusion

The Consultation Paper calls for the provision of not only the current credit limit a consumer has, but also the reporting of repayment history - confirmation that a person is meeting their credit obligations.

Repayment history is particularly important for consumers who previously went through financial difficulties and may have incurred adverse information on their credit report, such as a default, which stays on their file for five years; however this negative information can then be counterbalanced by the contribution of repayment history information, enabling consumers to evidence financial recovery.

Another part of the population helped by repayment history information are people with little data on their credit report, known as a “thin file”. For these Kiwis, the lack of credit information creates barriers for access to credit. People with no or limited credit information may find themselves denied access to credit, asked to find a guarantor, or be required to provide a greater amount of documentation.

Reporting of BNPL repayment has a critical role in helping people with either a poor credit rating or a lack of credit reporting information.

Equifax USA analysed 123,000 consumers with a “subprime” credit score (see appendix for more detail) and found:

- 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 score increase of 13 points.
- Those most benefiting were individuals with either a “thin” credit file or a “new” credit file. These saw an average score increase of 21 points with the addition of on-time BNPL repayment history information.

Visibility of multiple credit commitments

The availability of information on a person’s total credit commitments, recorded and supplied in a way that conforms with recognised data standards, protects consumers from the harm of becoming over-indebted.

Evidence has emerged in Australia of the importance to responsible lending of being able to assess the number of BNPLs a person may have and their collective limit. A recently released Australian study analysed bank transaction data³ and found that:

“approximately 40% of BNPL users operate more than one BNPL account. Relative to consumers with a single BNPL account, the average multiple BNPL account holder is more likely to be from a lower socioeconomic area, more likely to be receiving government benefits, has a higher credit card utilisation rate, and uses more personal loans. Multiple BNPL users thus likely represent higher credit risk for financial institutions, including BNPL platforms. However, as BNPL is not regulated as credit, the risk such customers pose is not completely visible to market participants.

³ https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4216008

Also noteworthy is the submission by the Australian Financial Complaints Authority⁴ to the current Australian consultation on BNPL regulation, which stated under the heading “Issues observed through complaint resolution”:

...the Options Paper notes problems that arise due to non-reporting of BNPL debts. AFCA’s complaint resolution experience suggests that non-reporting can contribute to financial over-commitment. When considering complaints about provision of unsuitable loans, AFCA has received complaints where the borrowers had BNPL debts that were not reported and not taken into account by lenders.

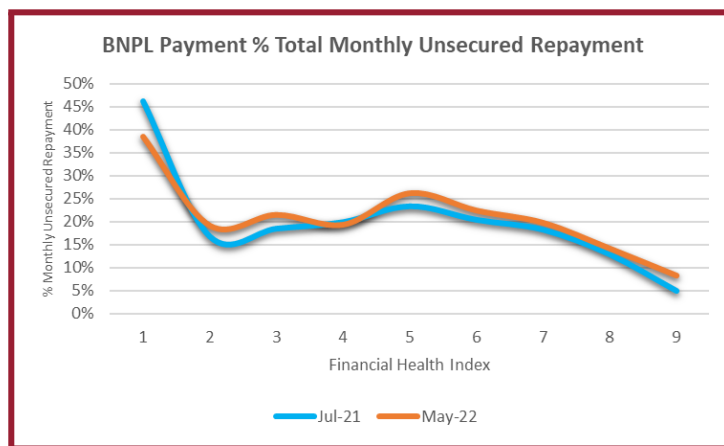
Utilisation of BNPL

To understand the attractiveness of BNPL and the consumer impact it may potentially be having, research undertaken by Equifax UK analysed transaction data from 20,000 consumer current accounts for two months (July 21 and May 22).

The financial health of these consumers were rated using Equifax UK’s Financial Health Index (FHI) measuring from 1 (least healthy and least likely to repay credit) to 9 (most healthy, most likely to repay credit).

This revealed that:

- Payment of BNPL is a significant - and rising - percentage of monthly unsecured credit (personal loans, credit cards) obligations;
- For consumers of average risk, around 20 to 25 percent of their monthly payments for unsecured credit went to a BNPL;
- For the worst risk consumers, payments to BNPL increased to more than 35 per cent.



Payment of BNPL on credit card

Other research has pointed to the potential for risk of repayment stress being transferred from the BNPL issuer to the other lines of credit.

In March 2022, an academic paper “Buy Now, Pay Later (BNPL)...On Your Credit Card” was released finding that a material portion of UK consumers charge their interest-free BNPL to their credit card:

⁴ <https://treasury.gov.au/sites/default/files/2023-02/c2022-338372-afca.pdf>

- 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 consumers⁵.

Participation in comprehensive credit reporting

Standards and obligations

New Zealand's move in 2012 to comprehensive credit reporting was noteworthy for the consensus amongst lenders - large and small - that they should contribute the new data elements⁶ which included the total amount of credit extended and repayment history information.

The CRPC requires that information on credit reports must be “accurate, up to date, complete, and not misleading”. This is an important objective, particularly as lenders rely on the information on a credit report to meet aspects of responsible lending requirements.

The proposal to require BNPL participation in credit reporting supports both New Zealand's responsible lending obligations and helps CRAs to fulfil the “accuracy” objectives of the CRPC.

Buy Now Pay Later operators have shown limited appetite for contributing data and/or making it available in the agreed industry data standards so all lenders can readily access and absorb the critical data. This hinders lenders assessing risk per the Responsible Lending Code and continues to disadvantage consumers.

As noted above, the Retail Credit Association of New Zealand has developed Data Standards (currently Version 3.02 of the Comprehensive Credit Reporting specification), which considers the accurate reporting of BNPL by consolidating an individual consumer's credit lines per BNPL provider, and displaying the worst payment status of the consolidated “accounts” (credit lines).

Meeting this standard allows a BNPL to reflect a payment status relevant to their product's terms of weekly or fortnightly payment cycles, whilst keeping the reporting of obligations consistent with those reported by other providers.

Mandatory reporting - smooth transition

Two of New Zealand's CRAs were part of Australia's move to legislate that its major banks participated in comprehensive credit reporting. The Australian law required bulk supply of comprehensive credit reporting information in two tranches, although, in reality, banks did not wait for the date to start supply.

Aspects of the Australian law included

- The appointment of a regulator to oversee compliance;
- Auditors to ensure the claimed supply aligns with what CRA's received;

⁵ https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4001909

⁶ In contrast in Australia, while second tier lenders flocked to comprehensive credit reporting, such was the recalcitrance by some larger credit providers to contribute their data that ultimately the Government intervened and legislated to mandate contribution by the Big 4 banks.

- To avoid market distortions or manipulation, the Australian framework effectively required contribution to at least two CRAs.

New Zealand's more co-operative civil engagement should mean the existing CCCFA framework is sufficient to resolve any transitional issues to greater participation in comprehensive credit reporting.

APPENDIX

BNPL REPAYMENT HISTORY HELPS PEOPLE WITH WEAK CREDIT SCORES

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, using anonymised data on 123,000 consumer population with 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 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.

