

Legal And Regulatory Issues in Credit Bureau Development

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Agenda for discussion

- When and why a law is preferred for CBs
- History of credit bureau in Asia
- Role of public sector
- Way forward for South Asia on CB
- Enabling Legal environment –suggestion
- More on consumer protection (slides 17-26)
- The US fair Credit Reporting Act-an example
- Conclusion

Law has been/is preferred when

- Financial market is not sophisticated
- Credit reporting system is open up to non banks and others
- Financial system is dominated by banks-to force sharing of information with non banks.
- Existing law on secrecy is too restrictive-to legally permit information sharing
- Existing system is “liberalized” to allow private sector entrants.
- There is lack of trust in private sector in general- to lend credibility.
- An orderly development of credit reporting system is aspired-need for an overseer

History of Credit Bureau

Central Banks often own part of and run Credit Bureau in developing countries –Why?

- Statutory requirement of law
- System dominated by banks and banking secrecy was tight-Tournier case and bankers book of evidence-another law was needed
- Supervisor needed consolidated information on NPLs
- Foreign banks not keen and state owned banks not be bothered
- Cost factor

State owned/run credit bureaus

- Most state owned and or run CBs -
 - Are poorly managed
 - Have poor infrastructure
 - Are generally inefficient- timeliness, veracity of data and usefulness
 - Are limited in service provision-negative data only
 - Have high cut off limits –loan size
 - Are not commercial viable-subsidy and limited business
 - Provide poor or no consumer protection
 - Have no linkages to other data sources
 - Closed membership-banks/institutions under supervision of central bank

Role of public sector

- Despite poor performance – public sector or central banks have a role to play in orderly development of credit reporting system. It can-
 - Take a lead in policy decision on CBs
 - Champion the legislative endeavor
 - Register or license credit bureaus
 - Provide legal oversight over CBs
 - Provide dispute settlement avenue
 - Incentivize participation and compliance through regulatory requirements and supervision

Way forward – for CBs in SA

Target: Credit Reporting System that-

- Is self sustaining/profitable
- Is privately owned
- Has clear legal and regulatory basis
- Is efficient and competitive
- Has wide participation
- Balances the right of the stakeholder and facilitates data collection and exchange
- Has sufficient legal oversight

Way forward – CBs in SA..cont

Steps to an ideal credit reporting system –

- Remove central bank as shareholder
- Corporatize CB if it is a statutory body
- Publicize role of CBs and build public confidence
- Amend existing statute on CB to-
 - empower central bank or functional equivalent (FE) to register/ license/ authorise privately owned cbs
 - Allow Central bank or FE to issue regulations to oversee CBs and ensure consumer protection
 - Permit interface and interaction of existing players
 - Allow existing CBs to be legalized under the law
 - Allow CBs to do related businesses- credit scoring

Enabling Legal Framework- e.g.

Ensure that the law has clear legal provisions to-

- Override secrecy restriction
- Do away with consumer consent
- Empower Central bank or functional equivalent to-
 - oversee CBs and license/authorize CBs
 - Have access to data in CBs for supervision purpose
 - Settle disputes amongst participants, including consumers and participants
 - Make regulations on *inter alia*-
 - data collection and dissemination
 - Consumer protection
 - Other incidental or necessary matters

Enabling Legal framework cont..

Regulations can be made to empower the central bank or FE to -

- Set criteria for registration/ authorization
- Set criteria for access-credible lenders/ with consent
- Require validation of information by CBs
- Nature of data collection-objective and relevant
- Prohibit unauthorized dissemination
- Prescribe retention periods
- Set rules for distribution of negative information
- Mandate internal grievance mechanism to handle consumer complaint
- Sanctions and penalties

Enabling Legal Framework cont..

Law must also provide sufficient protection to consumers by-

- Ensuring that data is not misused by CBs
- Creating a balance between privacy protection and effective information sharing
- Allowing borrowers to access credit reports at a fair price
- Prescribing clear procedures to challenge and correct incorrect entries
- Efficient out of judicial system dispute settlement mechanism

Enabling Legal Framework...

Law must be carefully crafted so that -

- It is not overly restrictive
- It is not unnecessarily severe on penalties/sanctions
- It is not complicated
- It does not have extensive and expensive procedures for information collection and exchange
- It provides clear legal basis for the CBs'

This is because-

- Firms will be discouraged from entering credit reporting business and
- They will pass on the cost to borrowers through higher lending rates

Enabling Legal Environment..

In drafting the the law, flexibility must be given to the central bank or FE to choose the instruments for implementing the law-either through regulations, rules/prescription or guidelines

- Regulations can be used if the issue is of general application, for public knowledge, certain and grave.
- Rules can be used to govern central bank or FE's own procedures or conduct in relation to overseeing the CBs
- Guidelines are generally used for matters which have to be tested and of pure form.

US Fair Credit Reporting Act

Some Highlights

- If consumer is questioning a credit refusal made within the past 60 days, the bureau cannot charge a fee for giving the information.
- If the business which reports the credit problem does not agree to a change or deleted entry, the consumer can add a 100-word statement to the file explaining their side of the story. This becomes a part of any future credit report.
- The credit bureau must help consumer to interpret the data in the report because the raw data may take experience to analyze.

US Fair Credit Reporting Act...

- Consumer must be told what's in their credit file and have any errors corrected.
- If a lender refuses credit due to unfavorable credit report, consumer has a right to get the name and address of the agency that keeps the report.
- Consumer can request information from that credit bureau by mail or in person.
- Consumer receives information contained in the file- not copy of report sent.
- When consumer has written in about a possible error, a creditor must not release information to other creditors or credit bureaus that would hurt his/her credit reputation.
- Until consumer complaint is answered, the creditor cannot take any action to collect the disputed amount .

US Fair Credit Reporting Act...

- Information about criminal convictions may be reported without any time limitation.
- Bankruptcy information may be reported for 10 years.
- Information reported in response to an application for a job with a salary of more than \$75,000 has no time limit.
- Information reported because of an application for more than \$150,000 worth of credit or life insurance has no time limit.
- Information about a lawsuit or an unpaid judgment can be reported for seven years or until the statute of limitations runs out, whichever is longer.

More on Consumer protection

Consumer protection covers issues such as-

- Fairness
- Accuracy and Transparency
- Type of information collected
- Privacy
- Assistance to consumers
- Fees structure
- Disputed information and Incorrect information
- Information retention period

Fairness and Privacy

- Credit bureaus have a duty to treat subscribers and consumers as fairly and impartially as possible
- Credit bureaus may only contract with subscribers who-
 - warrant that they have a bona fide risk management reason for accessing the information and
 - who agree not to disseminate the information to any person other than the consumer concerned.

Accuracy and Transparency

Credit Bureaus must –

- follow reasonable procedures to ensure the information they obtain is accurate, relevant and unbiased.
- record the source of information received and the subscribers who access the information.

Type of Information

- Credit Bureaus may record only information relating to credit and business dealings.
- Personal information such as name, date of birth, identity number, addresses, telephone numbers, employment and marital details may also be recorded
- Information to be excluded- race etc.

Privacy

- Credit bureau must upon request by consumer, disclose the nature and sources of the information on its file on that consumer.
- No telephonic disclosures should be made.
- The disclosure can either be to the consumer in person, or in writing if the bureau is satisfied regarding the consumer's identity.
- Disclosure may be made to a consumer's attorney.

Assistance to Consumers

A bureau must provide trained personnel to explain to a consumer any information furnished and to provide advice on how to obtain corrections to a consumer's record where possible.

Fees

- A bureau may charge a reasonable fee to allow consumers to view any information about themselves.
- If it is found that any information is incorrect then the bureau must refund the fee.

Disputed Information

- If a consumer disputes the accuracy of any information in his file, the bureau must reinvestigate such information
- Inaccurate information or that cannot be verified, must be deleted and subscribers who have received such information must be informed.
- If dispute is not resolved, the consumer must be entitled to file a brief statement explaining the nature of the dispute and request the agency in charge of dispute settlement to investigate the matter

Information Retention Periods

- Period of retention of information must not be too burdensome on consumers
- Information is retained between 3-5 years
- Information on bankruptcies and rehabilitations are usually retained for a period of 5-10 years from date thereafter.
- In the case of judgments, information is retained for 5 –7 years

Incorrect Information

- Person suffering harm from inaccurate or incomplete information must be entitled to bring action against the credit grantor/credit bureau.
- Consumer must prove that lender negligently provided the information and harm has been caused.
- Consumer must also quantify harm in monetary terms.
- Consumer must also be entitled to request an injunction from court for impending harm.
- Injunction is to prohibit publication of inaccurate information or to remove the inaccurate adverse notation.
- Injunctions are effective when a person finds it difficult to quantify the actual harm which might be sustained.

Conclusion

- Clear legal and regulatory framework necessary.
- Regulatory oversight needed in most situation.
- Sufficient publicity and trust building needed
- Rules must balance the right of consumer and need to share information effectively.
- Clear cost effective procedures need to be advocated on nature, submission and retention of information.
- Appropriate procedures to verify information must be present.
- Avenue for dispute resolution needed.
- Reasonable penalties for non compliance will be useful to ensure orderly development of credit reporting system.



Thank You