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ACCIS White Paper

Complementarity of public and private credit reporting in Europe to promote responsible lending

Executive Summary

Protecting consumers from over-indebtedness is a European priority. Creditworthiness assessments are one of the main tools to achieve this. These assessments are more effective when more comprehensive data is available to allow lenders to use the most relevant and insightful evidence.

Different European countries make credit data available in different ways. Some rely entirely on private credit bureaus (PCBs), and a very small number rely entirely on public credit registers (PCRs). There are also countries where both PCBs and PCRs coexist. Where both types of credit reporting services providers operate in a stable and complementary way, data comprehensiveness is higher, which leads to better outcomes for consumers.

Stability and complementarity between PCBs and PCRs are unbalanced when PCRs are expanded in ways that damage PCBs' ability to access and share data, and to provide other services such as credit scores to strengthen creditworthiness assessments. When complementarity is unbalanced significantly or for too long, PCBs may be forced to leave the market.

Looking at a European context, this paper highlights policies that can be implemented to ensure PCBs can operate sustainably and in a way that increases availability of comprehensive credit information thereby promoting responsible lending.

Introduction

Over-indebtedness is a serious social and economic problem across the European Union, not least as a result of the ongoing COVID-19 pandemic. In 2016, 21% of people of European citizens were at risk of being over-indebted[1]. The numbers are likely to rise even further.

In addition to financial education and social protection, policymakers use credit regulation to prevent over-indebtedness. In the EU, the Consumer Credit Directive (2008/48/EC)[2], the Mortgage Credit Directive (2014/17/EU)[3] and the more recent EBA Guidelines on Loan Origination and Monitoring[4] enshrine the principle of responsible lending.

Responsible lending means that a lender should only offer a loan to a consumer if it suits his needs and circumstances. To fulfil this principle, the lender must assess the creditworthiness of the consumer. In order to do that, lenders typically consult information about consumers contained in external credit databases, run by providers of credit reporting services. Other companies such as

[1] Eurofound (2020), Addressing household over-indebtedness, Publications Office of the European Union, Luxembourg.
[2] Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers.
[3] Directive 2014/17/EU of the European Parliament and of the Council of 4 February 2014 on credit agreements for consumers relating to residential immovable property.
[4] EBA/GL/2020/06

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utilities (electricity, water, gas) or telecoms companies may also use those databases, to ensure that consumers can use their services without running into financial difficulties.

The information held by external databases in the EU vary in terms of the breadth and depth of data they hold.

Breadth of data refers to the level of credit product coverage in the database, such as mortgages, credit cards and consumer loans. It also includes the sectors covered, such as financial services, utilities and telecommunications.

Depth of data refers to the amount of information held about a particular credit agreement reported in the database, such as the value of the credit, the balance and payment history. An important aspect of depth of information is the difference between positive and negative data:

- Positive data. According to the World Bank[5], this includes information that covers facts of contractually compliant behaviour – i.e. a record of the payments the borrower has made in line with their obligations. It also includes detailed statements about outstanding credit, amount of loans, repayment patterns, liabilities, as well as guarantees and/or collateral.

- Negative data. According to the World Bank[6], this consists of statements about defaults or arrears and bankruptcies. It may also include statements about lawsuits, liens and judgments that are obtained from courts or other official sources.

The depth and breadth of data available to data users in one country represents the degree of data comprehensiveness. Studies show that creditworthiness assessments that use comprehensive information significantly outperform those based on less comprehensive information[7]. Using more comprehensive data reduces the rate of over-indebtedness and non-performing loans. It also increases financial inclusion and increases the supply of credit.

So, in order to minimize the risk of over-indebtedness, policymakers need to address a crucial policy challenge: how to ensure the relevant data is available for creditworthiness assessments?

Public and private providers of credit reporting services

Before analysing the various options to tackle the policy challenge, it is necessary to recall some basic concepts about the credit reporting industry.

According to the World Bank[8], credit reporting is the "*cycle of collecting, storing, processing, distributing and, finally, using information to support credit-granting decisions and financial supervision*".

The World Bank[9] also distinguishes between two main types of providers of credit reporting services, based on the objectives that each of them fulfils:

[5] Ibid World Bank. 2011. General Principles for Credit Reporting – see Glossary.
[6] Ibid World Bank. 2011. General Principles for Credit Reporting – see Glossary.
[7] Barci, G.; Andreeva, G.; Bouyon, S.; *Data sharing in credit markets: Does comprehensiveness matter?* - *Research Report* Nº 23, September 2019, Brussels, European Credit Research Institute (ECRI), 2019 ISBN 978-94-6138-745-5. Also as recognized by the World Bank, studies confirm that the use of positive data is "*empirically associated with lower incidences of extension of credit to bad debtors, and at the same time successful extension of credit to debtors with little previous experience"* – see footnote 8.
[8] World Bank. 2011. General Principles for Credit Reporting. Washington, DC. © World Bank. https://openknowledge.worldbank.org/handle/10986/12792 License: CC BY 3.0 IGO.
[9] Idem

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- those service providers that primarily aim to improve the quality and comprehensiveness of data for financial and non-financial creditors to make more responsible decisions; and

- those service providers whose primary purpose is to assist banking supervision and to facilitate economic research and macroeconomic policy control. As a secondary purpose, some also aim to improve the quality and availability of data for supervised financial intermediaries.

For the purposes of this note, the first type of services provider will be referred to as a private credit bureau (PCB), while the second type will be referred to as a public credit register (PCR). PCBs are usually privately-owned and administered[10]. PCBs are capital-intensive businesses, requiring significant investment in data quality, data acquisition, value-added services and advanced analytics, security, compliance with the legislation, and more. PCRs are publicly owned and run usually by the local Central Bank[11].

There are other several important differences between PCBs and PCRs. They relate to:

1. Who provides data. PCBs generally enter into voluntary agreements with different parties including banks, credit card companies, telecommunications and utility companies, retail lenders, and other nonbank financial institutions to exchange data in a systematic, reciprocal manner. As private companies that aim to maximise shareholder value, PCBs have incentives to attract information from a large variety of relevant data providers and other sources, such as court records and public databases to better respond to their clients' needs as regards responsible lending. By the same token, PCBs have the incentives to produce added value products as explained below.

   On the other hand, given that their main purpose is to assist banking supervision, all regulated financial institutions are mandated to supply information associated with credit and loans to PCRs. PCRs therefore do not hold data from non-supervised institutions such as retailers, telecoms or micro-finance institutions, etc.

2. What type of data they have. As PCBs work on the basis of voluntary agreements, in some countries banks and other creditors refuse to voluntarily reveal that their clients are repaying back their credits (positive information). Banks do this to prevent other banks from offering products to their best clients. This situation is more frequent when a small number of banks have a very large share of the credit market and so there are less incentives to share credit information on a reciprocal basis with other organisations[12].

   PCRs on the other hand typically compel regulated institutions to share both positive and negative information, given their main supervisory role[13].

3. Size of loans. PCBs usually target retail credit and small business lending markets, where the average loan volumes are small, and advanced data analytics enable the processing of a large number of standard loan applications cost-effectively.

   PCRs typically focus on large loans as those may pose a systemic threat to financial stability. Also, by establishing a relatively high loan size for inclusion in their databases, PCRs can drastically reduce the size of the database, making it easier to manage and to enforce quality standards.

[10] Some examples are: Experian, Equifax, CRIF and Schufa.
[11] Some examples are the Fichier des incidents de remboursement des crédits aux particuliers (Banque de France) or the Central de Información de Riesgos (Banco de España).
[12] Bruhn, M., Farazi, S., & Kanz, M. (2013). Bank competition, concentration, and credit reporting. The World Bank.
[13] For more on the incentives to share positive and negative data, please see Jappelli T., and M. Pagano (1993) "Information Sharing in Credit Markets," The Journal of Finance Vol. 43(5), December, 1693-1718.

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4. What data and service they provide to creditors. Mainly based on the data they collect, PCBs develop specialised products and services such as credit reports, credit scores and portfolio monitoring, which enable more responsible lending. These PCB products and services are typically offered for a fee.

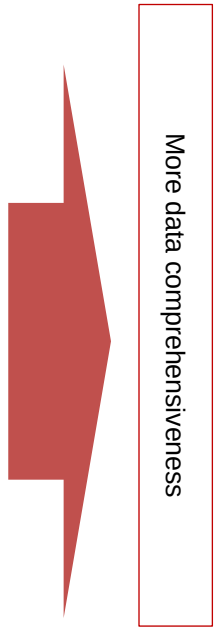
   PCRs in general only supply basic information and many do not supply a credit history but a snapshot of the current status of a borrower with the financial system. PCRs usually provide their data at low or no cost to the lenders[14].

5. Data protection legal rules. In the EU, both PCRs and PCBs need to comply with the GDPR. However, depending on where they are headquartered, PCBs may be subject to additional, sector-specific laws that introduce more stringent requirements over the ones in the GDPR for the same type of data processing.

6. Digital innovation. Initiatives such as the EU European Digital Finance Strategy[15] highlight the potential gains for consumers and the economy from digital innovation in financial services. Often working in partnership with other Fintechs, PCBs are successfully developing new digital services in areas including credit risk and identity verification and driving forward progress in open finance and advanced analytics. The development of new products and services is not a permanent objective for PCRs.

Table 1: Key differences between PCB and PCRs

	Public Credit Register PCR	Private Credit Bureau PCB
Data providers	Regulated financial institutions	Regulated financial institutions + others (e.g. credit card companies, telecommunications and utility companies, nonbank financial institutions, public bodies)
Data sharing rules	Compelled by regulation	Voluntary; data being shared to implement credit risk mitigation requirements
Size of loans	High value loans for banking supervision	No threshold
Data distribution and type of services	Basic information, for free	Credit report, often additional services (scores, credit risk models) for a fee
Data Protection	General framework (e.g. GDPR)	General framework and specific, sectoral legislation (depending on HQ)
Digital innovation / Future readiness	Less incentive to adapt	Strong commercial incentive to innovate and respond to clients' needs.



Why does complementarity matter

The differences between PCRs and PCBs outlined above show that these providers of credit reporting services are not substitutes. Indeed, the actual market structure of credit reporting systems regarding

[14] According to the World Bank, of the 87 credit registries that provided information to the World Bank survey on their costs to inspect data, only 14 listed a fee. See World Bank Group, 2019. "Credit Reporting Knowledge Guide 2019," World Bank Other Operational Studies 31806, The World Bank.
[15] https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52020DC0591

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PCRs and PCBs in many countries - in Europe and beyond - demonstrates that they are not mutually exclusive either. In other words, that they co-exist and can be complementary.

Studies have shown that, where PCBs and PCRs manage to operate in a complementary way, several benefits materialise:

1. Lenders can access more comprehensive credit information and more innovative services. This allows lenders to better meet their responsible lending obligations.

2. Responsible lending is reinforced, which leads to better outcomes for consumers and the economy[16], such as:

    - Reduction in the risk of missed repayments and over-indebtedness.
    - Increases in financial inclusion and consumers' access to responsible credit[17]
    - Increases in the availability of consumer credit

3. Credit markets become more competitive[18]. More information regarding credit and affordability risk makes credit markets more competitive. More comprehensive credit information heightens competition between banks and other credit providers (e.g. non-banks, peer-to-peer lenders, etc.) for the benefit of consumers.

The beneficial co-existence of PCRs and PCBs for data comprehensiveness and better consumer outcomes is dependent on a crucial, preliminary condition: PCB's financial sustainability. This means that PCBs must receive a significant volume of inquiries to their databases, which in turn allows the business to generate sufficient profits to be a financially viable ongoing enterprise.

Over the years, the financial sustainability of PCBs in some countries has come under pressure as a result of PCRs expanding from their core objective of supporting banking supervision and macroeconomic oversight. As mentioned above, a number of PCRs distribute the data they collect for supervisory purposes back to lenders, to improve the quality and availability of the data lenders use to meet their credit risk management requirements. For the purposes of this note, this data flow will be referred to as a feedback loop.

Feedback loops operate differently in different countries. They vary in which lenders can access the data; normally, it is only the institutions that are regulated by the banking supervisor. They also vary on what information is distributed - such as whether information is aggregated - and the value of the loans.

The scope and implementation of feedback loops can unbalance the complementarity between PCBs and PCRs, and make it unsustainable for PCBs to operate, in particular when:

- the PCR's database is significantly expanded by, for example (i) reducing the threshold of reported loans; (ii) expanding the number reporting entities; or (iii) reducing the time in which public data should be made available to reporting agents; and / or

- the threshold of the loans to be fed back to the participating entities is the same as the threshold of the reported loans; and / or

[16] Ibid Barci, G.; Andreeva, G.; Bouyon, S.
[17] It has been estimated that more comprehensive credit data would facilitate access to responsible credit for over 2,5 million vulnerable consumers in the EU – see Ibid Barci, G.; Andreeva, G.; Bouyon, S.
[18] For more on the complementarity between private and public systems: Andrew Powell et Al., Improving Credit Information, Bank Regulation and Supervision: On the Role and Design of Public Credit Registries, World Bank Policy Research Working Paper 3443, November 2004, accessible at: https://www.researchgate.net/publication/23723009_Improving_Credit_Information_Bank_Regulation_and_Supervision_On_the_role_and_design_of_Public_Credit_Registries

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- the feedback loop is provided at low or no cost.

A substantial expansion of a PCR and its associated feedback loop:

- removes an incentive for regulated financial institutions to share data on a reciprocal basis with PCBs, because each of them can individually obtain those data from the PCR.

- reduces the ability of creditors who cannot access the PCR to lend responsibly. If regulated financial institutions stop sharing data with PCBs, then other lenders cannot use that data in their creditworthiness assessments. Less comprehensive data will (i) reduce the supply of credit and/or services provided on credit; (ii) reduce financial inclusion and (iii) increase the rate of over-indebtedness.

- eventually, reduces the financial sustainability of PCBs in a country. Demand for PCBs will fall as existing clients (i) can access data for free from the PCR instead; and / or (ii) decline using the PCB's database for creditworthiness assessments / responsible lending inasmuch lenders stop contributing data to it. PCBs will leave the market if the revenue arising from checks against their databases makes the business financially unsustainable.

The unintended consequence of expanding PCRs and the associated feedback loops is that the level of data comprehensiveness in the credit system, the availability of related added value services and the capacity of the financial system to innovate are reduced. The credit information infrastructure of the country is subsequently less equipped to support robust creditworthiness assessments and hence protect borrowers and consumers against over-indebtedness. This may ultimately affect the financial stability of a country.

As evidenced in the academic literature[19], the more the PCR is designed like a PCB, the more its role will be substitutional but with less optimal capabilities to protect consumers. However, if PCRs are designed in a way that allows private credit reporting, both institutions can operate in a complementary way.

Annex I reviews features of credit reporting systems in several key European jurisdictions, including illustrative cases of:

- successful complementarity (Germany and Italy)
- failed complementarity (Portugal), and
- those that are in a process of change (Spain)

Improving complementarity and data comprehensiveness

There are certain policy choices that can be considered to maintain complementarity between PCRs and PCBs and increase the availability of comprehensive credit information. For example:[20]

1. Limiting the data collected by PCRs. Public authorities may consider introducing limits to the scope of information that is collected by PCRs. Limits can be applied to the depth and breadth of collected information and to the threshold of loans that are reported to the PCR. For example, PCRs may only collect information about certain products. And / or, they may only collect a certain, minimal amount of loan information. And / or they may consider only including information on larger loans (given the PCR´s main objective is to aid supervision of the banking sector, information on small loans is unlikely to be particularly important).

[19] Financial Privacy: An International Comparison of Credit Reporting Systems (2006-2007) p. 110, by Nicola Jentzsch.
[20] The OECD discusses many of these recommendations in their paper OECD (2010): Facilitating access to finance. Discussion Paper on Credit Information Sharing, accessible at http://www.oecd.org/global-relations/45370071.pdf

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2. Limiting the data returned by PCRs. The PCR may return less information to regulated financial institutions than it collects from them. Additionally, PCRs may only make current (or relatively current) data available to data contributors and prohibit access to historical data. Differences in the data collected by the PCR and the information returned to data contributors generate an "asymmetric" feedback loop that strengthens the complementarity between PCBs and PCRs.

3. Sharing PCR data with PCBs. Public authorities may consider introducing provisions to ensure that PCR data is passed on to PCBs (i.e. not only to regulated financial institutions). The PCR could act as a "system consolidator" of loan information for all regulated institutions, that would then be passed on immediately to PCBs. PCBs would then combine PCR data with other available information. This would allow PCBs to continue providing advanced products and analytical services. Availability of PCR data will further enhance the quality and predictiveness of the PCB products resulting in better and fairer lending decisions helping both lenders and consumers alike.

4. Increase the supply of data to PCBs from financial institutions. Public authorities may consider actions to encourage or enable all regulated financial institutions to also report credit data to external databases (as they report to PCRs), in particular, with regard to positive information.

5. Level data processing rules. Public authorities may subject both PCR and PCBs to the same data processing requirements for the same type of data processing. This would create a level-playing field with regard to the data protection requirements PCBs and the PCRs need to comply with.

6. Promote and facilitate data comprehensiveness. Public authorities may promote the importance of data sharing for the wider social interest, including the use of positive information and non-traditional credit data (such as data from telecommunications, utilities and payment accounts / open banking). Public authorities may remove any legal or supervisory barriers that prevent the use of relevant data for creditworthiness assessments.

Conclusion

Creditworthiness assessments are one of the main tools to protect European consumers from over-indebtedness. The availability of comprehensive data and added value services contributes to more effective creditworthiness assessments.

Countries with more comprehensive credit data and more sophisticated products are those where PCRs and PCBs operate in a stable and complementary way. The purpose of PCRs is mainly defined by bank regulation and supervision reasons, and by ensuring financial stability. The profit orientation of PCBs means that they tend to collect credit information as comprehensive and relevant as possible. PCBs constantly compete in the process of introducing new products and services to better help their clients to lend responsibly.

Countries should choose policies that ensure complementarity between PCBs and PCRs to increase the availability of comprehensive credit information and related services to promote responsible lending. Conversely, countries should discard policies that unbalance the complementarity between PCBs and PCRs and make it unsustainable for PCBs to operate.

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Annex 1 – Case Studies

1. Germany Italy: successful complementarity

a) Germany

In Germany, the PCR (Evidenzzentrale für Millionenkredite) is run by the Deutsche Bundesbank. It was established in 1934, as a response to the systemic risks highlighted by the depression. Credit and financial services institutions and financial companies report by the 15th of January, April, July and October those borrowers in Germany and abroad whose credit volume at any time during the three months preceding the reporting date amounts to EUR 1 million or more or exceeds the limit for large exposures under Art. 394 Capital Requirements Regulation (CRR). On a quarterly basis, the Bundesbank provides lenders with up-to-date information on the debt level of all borrowers.
The establishment of PCBs in Germany dates from a few years earlier. SCHUFA f.e. was formed in 1927 by a group of banks and retailers and is today the largest bureau in Germany. Other PCBs are active in this market. German PCBs collect information on contracts (positive information), including any outstanding loan amounts to be repaid. The breadth of data PCBs collect and share includes positive and negative information from a wide range of financial institutions, as well as on agreements in the utilities and telecommunications sectors. Government departments, insurance companies and crowdfunding platforms also supply data to PCBs

b) Italy

The Italian Centrale dei Rischi (CR) was established in 1962 and is run by Banca d'Italia. On a monthly basis, the CR is fed by the information that the participating intermediaries (banks, financial companies and other intermediaries) transmit regarding the loans and guarantees granted to their customers, the guarantees received from their customers and the loans or guarantees purchased from other intermediaries. Loans are reported as long as the amount to be returned to the intermediary is equal to or greater than EUR 30,000. The reporting threshold drops to EUR 250 for loans that the reporting agent classifies as non-performing. The classification assumes that the intermediary has assessed the financial situation of the customer and was not based solely on single events, such as one or more delays in paying the debt. The Bank of Italy communicates to the participating intermediaries the overall indebtedness of its customers, the type of financing they have received and the regularity or otherwise of their payments. Intermediaries can also request information on non-customer subjects but who have submitted a loan application or are about to issue a guarantee and could, therefore, become their customers, exclusively to assess their creditworthiness, i.e. the customer's ability to repay the loan.

The PCR co-exists with a thriving community of PCBs (or SIC, Sistemi di Informazioni Creditizie, in Italian). The first PCB to be established was the Consorzio per la Tutela del Credito, in 1964. Other players include CRIF s.p.a., Experian Italia s.p.a., and Assilea – Associazione Italiana Leasing. Italian PCBs collect positive information, including any outstanding loan amounts to be repaid.

2. Portugal: failed complementarity

In 1994, Credinformações (a private company that arose from the association of Equifax with ASFAC, Associação de Instituições de Crédito Especializado) started operating in Portugal. Co-existing with the public system guaranteed by the Bank of Portugal (Central de Responsabilidades de Crédito), Credinformações collected a wider range of data (both in terms of credit values and sources of information) compared to the Bank of Portugal.

In July 2001, the Bank of Portugal established (Instruction 16/2005) that, when the total liability of a borrower was above 50 euros, financial services providers were mandated to send their data to the public register. In 2009, a new consumer credit regime was approved, which made it compulsory to exclusively consult the public credit information system. This situation was corrected shortly

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afterwards but caused irreversible damage. Finally, in 2015, a new law introduced three modifications in the functioning of the public credit register:

a) Inclusion of, and access by the reporting organization to, operational historical information.
b) Inclusion of information from organizations which are not subject to supervision by the Central Bank of Portugal
c) The possibility for participating organizations to access information on declared operations and balances of legal entities independently of the existence of a contractual relationship or a credit request.

The compounded impact of the successive expansions of the public register has reduced the scope for private bureaus to operate in Portugal to almost zero.

3. Spain: quo vadis?

The Spanish PCR (Central de Información de Riesgos) was established by Bank of Spain in 1962, preceding the establishment in the country of PCBs. The CIRBE has positive and negative information on credit from regulated financial institutions on consumers borrowing more than EUR 9,000.

Two main PCBs operate in the country, Equifax Iberia and Experian España, that collect only negative data. In 2019, the national law transposing the EU Mortgage Credit Directive obliged lenders to consult the CIRBE and a PCB in a creditworthiness assessment for mortgage credit. It is also permitted lenders to share positive credit information with PCBs on both mortgages and consumer credit. However, lenders have not shared positive data with PCBs and there has been no government or regulatory action to encourage them do so.

In July 2020, a Ministerial Order included significant changes to the CIRBE aimed at strengthening creditworthiness assessments. The changes - which will take place in July 2022 - include:

- A reduction in the threshold of the loans that are reported to CIRBE (from EUR 9,000K to EUR 1,000).
- An expansion of the reporting entities to CIRBE, to include payment services providers that also provide credit services.
- A reduction in the time CIRBE data should be made available to reporting agents (from 30 days to 20 days).

PCBs have objected to the changes, expressing concerns that the expansion of the CIRBE will make their operations unsustainable in Spain.

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