Credit where it's due

OVERCOMING THE BARRIERS TO MAINSTREAM CREDIT WITH DATA

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Key messages

The Financial Inclusion Commission found that too many people are still excluded from mainstream credit in its 2015 report. An estimated six million people are unable to access mainstream credit in the UK, leading them to borrow from unscrupulous lenders and worsening their financial exclusion.

The introduction of Universal Credit puts an emphasis on financial inclusion, and will hold information that can be used to widen access to financial services, while at the same time, data is increasingly being seen as an asset inside and outside of government. Policy in Practice were commissioned to investigate how new sources of public sector data can be used to widen access to mainstream credit.

By reviewing existing literature, speaking to key stakeholders in the sector and analysing new sources of public sector data, this report identifies the real value in opening up these new sources of data, and bringing them into the credit process, to boost access to affordable credit.

New sources of data can help in the whole credit process: by verifying identity, to support creditworthiness through credit scores and in affordability assessments. This helps individual households to access credit, while also helping lenders to make more accurate decisions based on richer data.

- Data from Rental Exchange shows a big jump from 39% to 84% in digital identity authentication for social tenants when rent data is included in credit files. Furthermore, 76% of tenants have an improved credit score from sharing rental data.
- Analysis by Policy in Practice suggests that additional information on household income and earnings could encourage lower income thresholds for loans, and make an additional 4.8m consumers more attractive to mainstream and lower cost lenders.

Benefits data is particularly strong in identifying and verifying households and in assessments of affordability and financial resilience, whereas data on payments (like rent or council tax) is useful for credit scores. The data also has the potential, as a result of a more rounded credit score, to further exclude some people. Evidence suggests it helps more people than harms, and can help to identify vulnerable households in order to target financial inclusion efforts to the people that need it the most.

To unlock these benefits, our key recommendations are that:

- Government must promote data sharing among public bodies and the credit reference industry;
- Consumers and mainstream lenders need to understand and appreciate the benefits before these new sources of data can be shared.

Government legislation will push forward a cultural shift toward better use of data and information sharing. Gaining informed consent from individuals is key to opening up the data, and highlighting the clear benefits of sharing data – with control over that sharing – will win over hearts and minds. While some lenders will be keen to use this richer picture to grow their consumer base, others will need to broaden their understanding of low income consumers to maximise the benefits that sharing this data could release. We believe the benefits to low income consumers and wider society are too great to be ignored.

Executive summary

The Financial Inclusion Commission in its 2015 report found that too many people are still excluded from mainstream credit. One of the key challenges to financial inclusion is the credit gap faced by people on low incomes who are not served by the mainstream market.

Policy in Practice has been commissioned by the Financial Inclusion Commission to investigate how public sector data can be used to widen access to mainstream credit, and improve the credit files of those who may be at risk of financial exclusion.

There are clear opportunities from the wider use of data to boost financial inclusion. Data is increasingly seen as an asset, inside and outside of government. The introduction of Universal Credit puts an emphasis on financial inclusion, and will hold information that can be used to widen access to financial services.

The literature shows the extent of financial exclusion, with mainstream credit inaccessible to 6 million people in the UK. Young people and migrant workers are most likely to have no credit file, whereas poorer households, older people and social tenants often have 'thin' credit files, with limited evidence to apply for credit. This leads people to borrow from alternative lenders, such as doorstep and payday lenders, at high interest rates. No, or limited, evidence in credit files is a key driver of this form of financial exclusion.

We built on our past research and looked at recent initiatives into financial inclusion, particularly to access mainstream credit, and on data sharing. We have outlined the key barriers to sharing data and highlighted learning from where these have been overcome. We have also spoken to credit reference agencies, lenders and owners of non-traditional sources of data to assess the impact of using and opening up this data.

The credit reference agencies and lenders we spoke to would value extra evidence in credit files. This would be valuable for three parts of the credit process: for **identification and verification**; to **assess risk and creditworthiness**; and in **assessing affordability**.

Unless applicants can verify their identity and address, they won't be able to access mainstream credit. The three credit reference agencies referred to the identification and verification stage of the credit process as the "gateway", or the first stop towards affordable credit.

Lenders take different views on creditworthiness. A mainstream bank lending a mortgage over 25 years will accept a different score to a high street lender for white goods lending over three years. But whereas the credit score protects the lender, the affordability check ensures the borrower can repay comfortably, without stretching themselves. Regulatory pressure has put more emphasis on these affordability checks as part of the credit process.

We then focused on understanding the barriers to the wider use of data, and where these had been overcome. There are privacy issues, technical barriers and market hurdles. We also looked into the approach to sharing data across institutions. This reinforced our view of the power of data and the general movement towards more and better use of data.

The recent Digital Economy Act, which seeks to break down costly barriers to data sharing within the public sector, is complemented by regulatory initiatives such as Open Banking as directed by the Competition and Markets Authority, and private sector programmes including the Rental Exchange. We found that public sector and other non-traditional data sources offer the opportunity to develop a more complete credit profile. Universal Credit places an emphasis on promoting financial inclusion, and alongside other government initiatives including GOV.UK Verify and Real Time Information on earnings, builds a rich pool of data that could be used by government to improve a range of outcomes, including financial inclusion.

Technical barriers include the ability to match non-traditional data with evidence already on credit files, as well as issues around data quality, privacy legislation and the ability to obtain the proper consent to allow for the sharing of data from public sector agencies and the lending market. Experian's Rental Exchange programme shows that these technical and privacy hurdles can be overcome. Although credit reference agencies need to understand, clean and turn any new source of data into evidence in credit files, they already have the experience to do this with data from a large number of varied sources. Standardised datasets, of the sort that already exist within the public sector, make it even simpler for analysis to be carried out at scale. Overcoming privacy issues by obtaining informed consent is possible, as shown by a range of initiatives including the Rental Exchange where opt-out rates were less than 1%.

Market acceptance of new sources of data may be a bigger challenge than the technical barriers. Lenders need to be convinced that new sources of data on credit files will improve their lending decisions. The lenders we spoke to were keen on having more data in credit files. One stakeholder told us that newer lenders, in contrast with the traditional banks and building societies, are most likely to accept new sources of data where they can see a statistical improvement in scores. We also have examples of telephone and utility data now being incorporated – and accepted – in credit files.

This report looks at the positive impact of a small number of datasets on the ability of people with thin or no credit files to gain access to mainstream credit. Lenders, credit reference agencies, local authorities and housing associations see the benefit in boosting credit files for people with no or limited evidence in their files. Evidence from Rental Exchange and administrative datasets including Housing Benefit data shows how these new data sources boost credit files:

- A big jump from 39% to 84% in digital identity authentication for social tenants when rent data is included in credit files;
- In 76% of cases, tenants with no significant arrears see their credit score improve, whereas only 8% of tenants have rent arrears, suggesting it helps ten times as many households as it harms.
- Additional information on household income and earnings could encourage lower income thresholds for loans, making an additional 4.8m consumers attractive to lower cost lenders.

A broader analysis of the available datasets, including transactional data on payments to government and on rents, could help many more households. A wider view of the benefits to financial inclusion and, more broadly, to the government and its partners in tackling exclusion and vulnerability, would also indicate that the potential gains are underestimated. Using benefit data to assess financial resilience, the

report finds 47% more households in work are financially vulnerable, compared with traditional measures.

Government legislation to open up public sector data is crucial for this to succeed. The collection of data can be done at a local or a national level and electronic 'data wallets' with informed consent offer different ways to collect and share this data. The barriers to sharing data can be overcome, but require legislation that recognises the benefits as well as the risks. Universal Credit is a great opportunity for doing this, because of the scale of information it will collect, but it must be backed up by education to show the public the real value in sharing data with their active and informed consent. Lenders also need to have a more sophisticated understanding of lower income consumers, and how the information on them can help them to open up markets and lend responsibly.

Introduction

Financial exclusion comes in many forms. The Financial Inclusion Commission in its 2015 report found a number of key challenges. One key barrier to financial inclusion is the credit gap faced by people on low incomes who are not served by the mainstream market.

Too many people are still excluded from mainstream credit. This affects 6 million people, and can lead them to seek credit from disreputable lenders or at very high interest rates. This often leads to spiralling debt and further financial exclusion[1].

Two barriers to accessing mainstream credit are the lack of a credit file or having a 'thin' file (without enough evidence on their credit records to gain a credit score). Many of these households will be on lower incomes and more likely to be in receipt of welfare benefits, or will live in social rented housing. However, both of these situations offer sources of evidence to bolster credit files and therefore to access mainstream credit.

This project has sought to identify how other sources of data, primarily public sector and housing data, could be used practically to build people's credit scores and promote access to financial services. This would enable more people to access more affordable credit. Policy in Practice has been working on behalf of the Financial Inclusion Commission to:

- Identify practical ways that credit scoring can be improved, primarily through the use of public sector data, to create a more informed view of the individual;
- Recommend ways to improve financial inclusion without a significant sustained increase in cost or risk to the sector;
- Communicate findings to industry and government, which has indicated it would consider legislating in this area.

We have done this by reviewing existing literature, speaking to the main credit reference agencies in the UK, Experian, CallCredit and Equifax, and meeting with lenders, local authorities and housing associations. We have delved into the current approach to credit scoring, the appetite for using new sources of data in credit files and how to overcome the practical issues in sharing this data.

Policy in Practice worked with local authority Housing Benefit data and the credit reference agencies' own credit files to explore the impact that combining the two sources of information could have. This analysis of local authority data builds on evidence of a tenant's payment history being used in their credit file, through Experian and the Rental Exchange, and points to the impact that public sector data can have on verification, credit scores and affordability, and how this can boost financial inclusion.

Next, this report outlines findings from the existing evidence, before looking at the potential use of new sources of data to boost credit files. It sets out three key uses of data in the credit scoring process and shows the real value in this data. We look at the challenges in harnessing this new data and how these hurdles can be overcome.

Existing evidence

Building on the previous work with the Financial Inclusion Commission we first reviewed existing literature on financial inclusion and data sharing, as well as recent initiatives in the credit scoring process.

What is financial exclusion?

People are financially excluded if they can't access financial services they want or need in order to manage their financial situation. To be financially included they must have access to financial products and services, and be capable of understanding them[2].

Studies show the extent of financial exclusion in the UK. In 1999, 7% of households lacked any mainstream financial products[3], equal to around 1.6m households. More recent publications show these numbers are still high – the Financial Inclusion Commission[4] found that in 2014 almost 2 million adults did not have a bank account, while a Birmingham University[5] study classed 22% of the population as 'financially vulnerable', meaning that they are having financial difficulties and have no expectation of an improvement in circumstances.

When it comes to access to credit, there is a similar story of exclusion, with many people resorting to high-cost loans due to restricted access to mainstream credit. Research from the European Commission[6] shows that in 2003, 30% of British adults had no credit facilities. A later publication from the House of Commons reports that mainstream credit was inaccessible to 6 million people in 2010, with 1.5 million of these individuals indebted to payday lenders. This is supported by data from the Financial Inclusion Commission[1], which found that in 2012 around 2 million people took out a high-cost loan due to lack of other options.

Who is excluded from mainstream credit?

Certain groups are more likely to face financial exclusion. The Joseph Roundtree Foundation[7] identifies the unemployed, young people, single parents, those with bad credit history and ex-offenders as being particularly at risk. There are also cultural and psychological barriers to financial inclusion, such as having a low income or being retired[4,8], the unrealistic conditions required to apply for mainstream financial products (e.g. high credit scores)[9] and the limited inclination to search for the most suitable option[10]. A Friends Provident Foundation study[11] considers those who are unwell, have a disability, are from an area of high deprivation or are from certain ethnic backgrounds (including African-Caribbean, Pakistani and Bangladeshi) as being at risk.

Our conversations with lenders have revealed other groups who struggle to get credit - immigrants, for example, due to the lack of UK-based evidence to support their application for credit. One high street lender told us that one in five of its customers is "unbanked", with no current account, though they may have a simple card account from the Post Office.

Building a strong credit rating can take time. Knowledge of how the credit scoring system works can help. For some the problem may be as simple as lacking the necessary identification documents, while for others the causes are more complex. For the purpose of this report we have split the financially excluded into two groups: those with no credit file and those with thin credit files. Young people and migrants are most likely to have no credit file, whereas other groups like those on benefits, older people and social tenants are more likely to have thin files. One housing association in the South West, for example, told us that 5.5% of their households had thin credit files, and were hoping to reduce this figure through the Rental Exchange.

What options do the financially excluded have?

Those who can't access mainstream financial products face few options when in need of credit. The usual options are borrowing from family and friends, applying for high-cost loans or obtaining a loan from an illegal lender[9].

For some, financial products are limited to costly products[4]. High interest products include payday loans and logbook loans, such as Wonga and QuickQuid, both with APRs over 1,200%, though the total cost is limited to double the initial amount borrowed thanks to price caps introduced to payday loans. Providers with moderate interest rates include credit card companies and loans from household goods websites or catalogues, such as the Capital One card (typically 29-35% APR) and Brighthouse, which sells household appliances with an APR of 69.9%. Finally, sub-prime mortgage lenders and credit unions offer lower interest rates to customers, usually less than 15% APR. However, all of these rates are higher than those on offer to people with a 'thicker' credit file.

The impact of Universal Credit on financial inclusion

Universal Credit places an emphasis on improving financial inclusion and financial capability. The introduction of fee-free basic bank accounts has in part been driven by the need to ensure that low income households can access a product that better meets their needs.

The transition to Universal Credit will be challenging for some households, particularly for those that are financially excluded. People will have to wait around six weeks for their first Universal Credit payment, and Universal Credit paid against earnings in the previous assessment period could lead to greater monthly peaks and troughs in cash flow[12]. The landlords we spoke with did not know how these households were coping with delays and are concerned that it may be increasing indebtedness. In fact, the spread of Universal Credit was encouraging many to address issues of financial and digital exclusion among their residents. The DWP offers budgeting advice and a benefit advance of up to half of the first month's Universal Credit award[13], but the lack of access to credit in this time will pose difficulties for some households.

The DWP also cites delays in payments due to problems in verification, so could benefit from the ability to verify household addresses and rent levels via the exchange of data with credit reference agencies.

The potential of data

The amount of data we generate and the pace at which we generate it is growing all the time. More data was created and stored in 2013/14 than in all previous years combined[14]. Governments across the world are recognising this and are making efforts to open up data for public good, including in the UK. This information has great potential if processed and used in the right way, including for financial inclusion.

The Digital Economy Act specifically aims to improve citizens' lives through data[15] and is supported by the response of the recent Cabinet Office consultation on the use of government data.[16] This includes sharing data between public bodies, which will help improve research and detection of fraud, plus much more. Other government initiatives include GOV.UK Verify[17] and Open Banking, proposed by the Competition and Market Authority (CMA)[18]. The drive for citizens to be 'digital by default' under Universal Credit is also pertinent.

GOV.UK Verify is a new way to prove who you are online, allowing individuals to access government services more easily. For example, it is possible to claim Universal Credit online, and to check driving licence information. Open Banking is a scheme the CMA designed to increase competition in the banking market and to encourage technological change. Customers can manage their accounts through a single app and obtain information on who offers the best rate for them.

Because many individuals are financially responsible but cannot prove this is the case, the government acknowledges that more data sharing could help improve lending decisions[19] and so benefit customers. Studies in the United States[20] support this, suggesting that many people with limited credit files have historically been considered to be bad risks, whereas in fact a large proportion of these people routinely maintain payments on their financial obligations. Customers and lenders could benefit from opening up new sources of data to assist in lending assessments. Lenders would have a larger base of reliable customers, while customers would have access to a wider range of financial products. Some alternative credit reference agencies are based on this idea, with Aire[21] in the UK and similar businesses in the US using different sources of information to build credit files. These sources of data can include an individual's income, expenditure and education, which are provided directly by the customer.

Credit reference agencies also recognise the value in new sources of information on individuals. The three main credit reference agencies in the UK are Experian, Call Credit and Equifax. In our interviews, all three stressed the importance of new sources of data to show an individual's creditworthiness. In one agency's words, they use "everything we can get our hands on". They have already started to collect and use data from utility companies, telecoms companies and social media, as well as home shopping data from firms like Littlewoods. Experian, the largest of the three agencies, has been working with Big Issue Invest to collect rental payment information from social housing providers so that it can be used to improve credit ratings for those with thin credit files[22]. Those with a thin or no credit file may well have been paying their rent on time for many years. Rental Exchange is predicated on this being proof of a household being able to make regular payments, something that would be taken into consideration by lenders in deciding whether to award credit.

How data is used in the credit process

Millions of people excluded from mainstream credit have rich data held about them by CRAs and other organisations, including the public sector. How do you marry the two together to boost financial inclusion? First, let's look at how data is currently used in the credit process.

Three key uses of data

From our conversations with lenders and credit reference agencies, there is huge potential for new data sources to help people with no or thin credit files. In particular, new sources of data can support the credit process in three ways: for **identification and verification**, to assess **creditworthiness and risk** and to establish **affordability**.

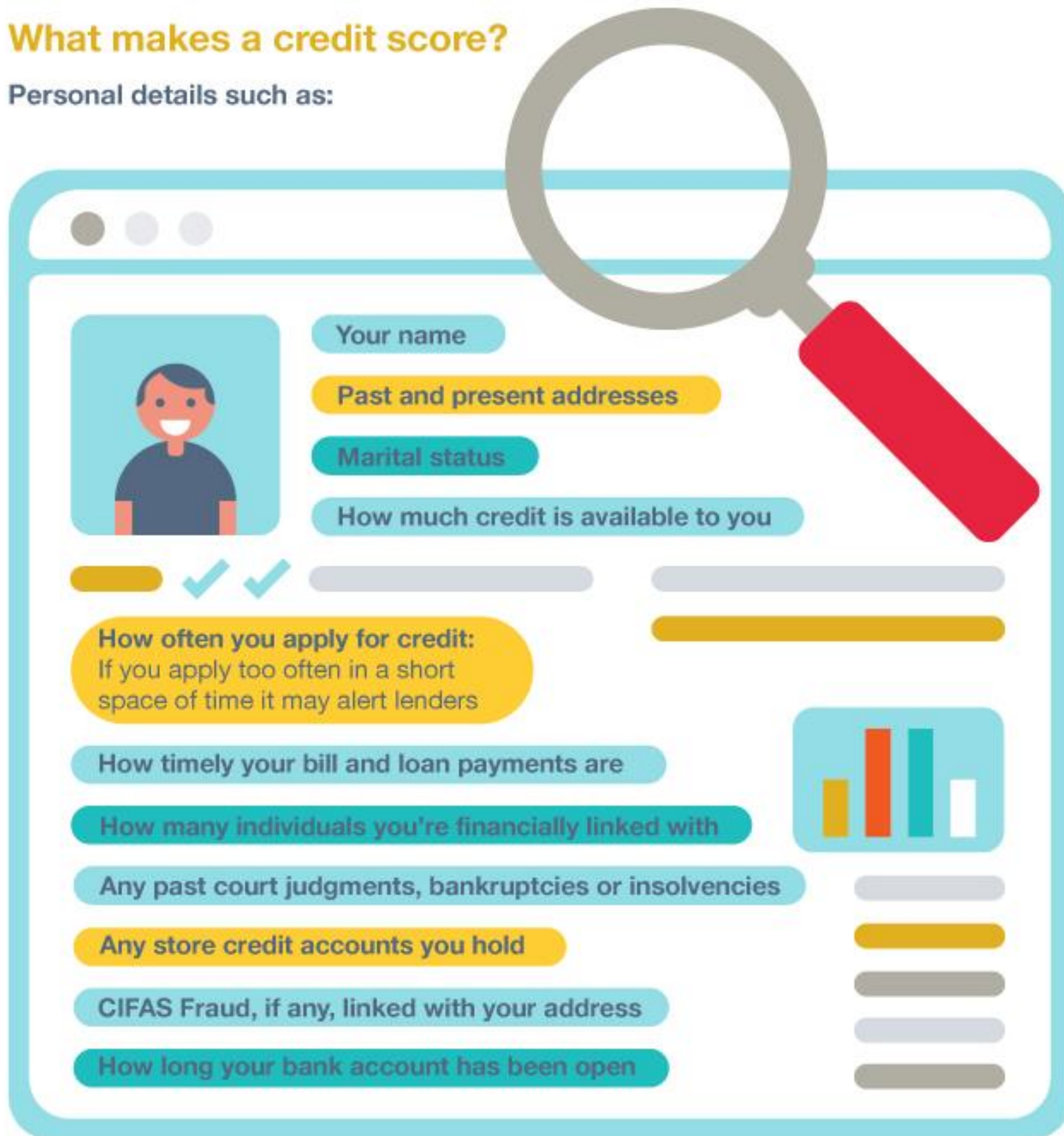
If an individual cannot be **verified** at a particular address, they cannot get credit. Without this verification there is a possibility of fraud or a lender may face difficulties tracking down borrowers who fail to keep up with payments. This poses an immediate barrier for some people, which could be countered by actions as simple as registering on the electoral roll or proving evidence of regular rent payments. A credit reference agency told us that, for many, 'the first step towards an improved credit score is getting **identified**'.

A person's credit score is determined by their **creditworthiness**. This is a borrower's likelihood of repaying the loan over the loan period. Lenders will accept different levels of risk – and charge an interest level based on that risk. Thirdly, lenders particularly emphasised that they must assess **affordability** within the lending decision, especially because of regulatory pressure. Is the lending in the borrower's interest? One lender put it bluntly: while the credit score protects the business, the affordability check protects the borrower.

A fourth area that came up in conversations about affordability was the concept of **vulnerability**. Lenders are expected more and more to offer support to consumers identified as vulnerable, who are struggling to pay their bills. CRAs and lenders told us that identifying who these households are was a challenge where public sector data could prove particularly useful.

> *"Utilities and Financial Services organisations are being asked to target support to vulnerable households. There is a market for this information if it's reliable." Evidence from a CRA*

How are credit scores put together?



Sainsbury's Bank, 2014. Guide to credit scores[23]

Each lender has its own approach to assessing somebody for credit. But there are some repeated elements. Credit reference agencies do much of this work, though the actual credit scores and thresholds adopted by each lender will vary.

Data is gathered from several sources: from electoral rolls, previous loan, credit and payment histories, bank account details and demographic data from applications and surveys, as well as financial connections to others and markers like defaults on loan payments and county court judgements. This is combined by credit reference agencies to produce a credit score, typically measured as a likelihood to repay within 180 days, which is then used by lenders in deciding a credit application. For now, a key

contributor to the credit score is payment history, whereas other elements simply add limited value to the score.

As well as credit scores, credit reference agencies also provide affordability assessments for lenders. Each lender decides what credit score they will accept and how to use an individual's affordability. For example, one high street lender told us that about half of new assessments go through an automated affordability check that uses income data and expenditure compared to ONS household spending in that postal sector. They will also use metrics like the existing debt-to-income ratio, to ensure that somebody is able to cover all of their debt repayments before being allowed to borrow any more.

Lenders are looking for "stability" in households. Someone who has lived at the same address for some time is a good indicator. If they pay their rent and bills on time is another plus point. Having enough income to cover bills and any loans is also positive. In contrast, somebody who moves regularly, misses bill payments and has several debts will score poorly.

Potential sources of data

To boost access to mainstream credit and therefore boost financial inclusion, we have reviewed how new sources of data can fill the gaps in the mainstream credit process.

We have identified potential sources of data from public sector bodies, local authorities and housing associations which are useful in building the credit files of those with a thin file or no file. This data includes the Single Household Benefit Extract (SHBE), effectively a register of everybody in a local authority that is receiving Housing Benefit; Council Tax Support payments; and Discretionary Housing Payments. All of these could provide a better picture of an individual's income and outgoings and ultimately evidence somebody's ability to make regular payments on time. Other sources include information on arrears, parking payments, student loans, child maintenance payments, HMRC data and information from social media.

Several key bits of public sector information can be used to **identify and verify** an individual. A lender told us that the first thing they ask for from new customers is proof of identity. Benefits data could be used, such as names, National Insurance numbers and dates of birth. Housing data could be used to show the amount of time an individual has lived at their address. Credit reference agencies told us that those who have been at an address for longer are considered lower risk, whereas those who have committed fraud are often linked to many addresses over a short time.

The credit reference agencies we spoke to told us that they, and lenders, are considering the potential of social media data to help verify people. If an individual has an active Facebook or LinkedIn account, with genuine connections, then this can support credit reference agencies in verifying their identity. The three credit reference agencies referred to the identification and verification stage of the credit process as the "gateway", or the first stop towards affordable credit. This helps to get people "on the radar".

Existing data to assess **creditworthiness and risk** focuses on payment history, often modelled on credit card payments. The key is to show that somebody can maintain regular payments over a period of time.

Data on income, employment and broader household circumstances can be useful here; however, it is secondary to payment history. This means that while benefits data may fill some gaps, it is payment data, such as rental or council tax payments that is the most useful. This data also exists within the public sector.

Housing Benefit and Universal Credit data captures information on an individual's earned and other income, working hours and savings, all positive measures; housing data can show rent paid; child maintenance payments data can also be useful. However, it is worth bearing in mind that this data can also negatively affect credit scores, something that the agencies and lenders clearly pointed out. Some flags on Universal Credit data, such as housing payments being made directly to the landlord, might do this, or if a claimant has an appointee or evidence of benefit fraud. Additionally, housing data that shows somebody to be in rent arrears would understandably be a negative factor in the assessment of credit worthiness. While the impact will not always be positive, credit reference agencies could all see the benefit in a more rounded credit score.

Assessing an individual's **affordability** is the final area in the credit process. Housing Benefit data can be useful here, especially to show liabilities, income and household characteristics such as rent due, council tax liability, income from earnings, benefits and other sources, savings, number of children, Discretionary Housing Payments and payments to a landlord. Housing data can add to this by showing rent and service charges due. One housing association told us that an individual's method of payment correlates with their level of arrears. Specifically, tenants paying by direct debit had arrears that were on average 25% lower than those paying by other methods. Similarly, tenure type could be a proxy for affordability, in the sense that people in shared ownership had under half the average arrears of people in secure tenancies, for example. Just as with creditworthiness, this new information has the potential to be positive *or* negative for individuals.

It is also possible that extra data can provide access to affordable credit by bypassing the credit score, while still verifying identity and showing that the loan is affordable. One example is a couple who want to buy a property with a mortgage, though have lived with their parents and therefore not built up a large credit file. They can prove their identity and have been on the electoral roll for some time. They can also prove they have sufficient money for a deposit and they can afford to repay monthly mortgage payments. Even though they have very little evidence to show creditworthiness, they are still in a position to get a mortgage. In this case, the affordability is more important than the thickness of the credit file.

One high street lender already has two approaches for new applicants, a fast track and non-fast track, depending on whether people pass an automated credit application. If they don't pass they can still receive credit but must provide extra evidence to prove identity, address and income. Mainstream lenders could use a similar approach for people with no or thin files.

Evidence to improve affordability assessments could also be used to identify households in need of additional support. Councils have used evidence of emerging arrears to target financial support, and analysis of Housing Benefit data has been used to increase take-up of affordability schemes. In one example, Cambridge Water, a lender, worked with their local authority to passport households identified by the local authority as vulnerable onto their low income tariff.

Assessing the value of new data sources

We have set out the three key uses of data and where non-standard data from public sector bodies, local authorities and housing associations can be useful. Building on the literature that outlines the potential of these new data sources to improve access to mainstream credit, we have also reviewed the evidence from housing association rental payment data from Experian's Rental Exchange programme[24], and considered the potential for Housing Benefit data to support financial inclusion, including the impact of combining it with information used by a CRA.

Identification and verification

Data from Rental Exchange shows a big jump from 39% to 84% in digital identity authentication for social tenants when rent data is included in credit files. The rent payments add a second source of identification, which makes a big difference in moving a lot of people into the "gateway" for affordable credit.

It is worth pointing out that one-fifth of housing tenants are on full Housing Benefit (and therefore not making any of their own rent payments). These cases would not see any change in their credit score as a result of factoring in rent payment data, as this information is not actually reflective of their own ability to pay, but rather of the DWP and the local authority that pays their Housing Benefit.

These cases could still benefit from digital authentication. Evidence from the Rental Exchange shows that digital authentication can reduce the cost of car insurance on MoneySuperMarket, for example. *With* authentication, 108 quotes were provided ranging from £161 to £177 per year. *Without* digital authentication, the number of quotes went down – to 98 – and the price went up, between £167 and £191 per year. So better authentication could still help people to improve their credit scores.

Creditworthiness

With the Rental Exchange, 76% of tenants see a positive increase in their credit score, whereas just 8% of tenants have rent arrears, which subsequently results in a worse credit score after sharing rent data. The remainder had no difference to their credit score, mostly because they were receiving full Housing Benefit so not making a personal contribution to rent. This means the payment history benefits almost ten times more social housing tenants than it harms.

Speaking to credit reference agencies, payment history is currently one of the biggest contributors to a credit score. Credit card limits and payment history are a good examples of where the total amount lent and the regularity of the monthly payments help lenders decide whether to lend again - hence the value in the history of rent due and of payments in Rental Exchange. However, income data – particularly Real Time Information included in Universal Credit records – would influence the credit score, especially for people who don't make enough transactions in their bank accounts (or don't have accounts); we were

told that some mainstream lenders might set a threshold of e.g. £15,000 turnover into the bank account before lending to a customer. This is backed up by evidence from BrightHouse whose typical customer's income falls just below this threshold at £14,000.

What would happen if mainstream lenders reduced the income threshold for loans?

Policy in Practice used data from the Family Resources Survey (FRS) on British households to calculate the number of households that fall under different income thresholds.

Number of working age households with income above a qualifying threshold			
(Millions of households)	>£15,000	>£12,000	>£9,000
Total number of households	20.3	25.1	28.9
Number of working age households	16.8	19.0	20.9
Number of pension age households	3.5	6.1	8.0

[25]

20.3 million households have take-home incomes exceeding the £15,000 threshold to share bank account details. If this threshold is lowered £12,000 per annum the figure is 25.1 million – 4.8 million more households could potentially qualify.

Lenders may be prepared to lower the crude threshold, if it were supplemented by additional information on household income and earnings. Administrative data is available that could help improve credit profiles. This more granular understanding of people's ability to repay could make a significant number of consumers more attractive to mainstream and lower cost lenders.

Affordability

To assess the impact of benefit data for affordability, Equifax on our behalf contacted some lenders in different industries to test the value in data like welfare benefit records. This has been useful to see the different attitudes adopted by different lenders. For example, a private wealth bank may well see the fact that an individual is in receipt of Housing Benefit as an immediate reason for a decline decision. However, a catalogue company selling clothes and household goods on credit may well have very large numbers of clients in receipt of Housing Benefit, and so it may well not play into their decision-making at all. One high street lender told us that data on affordability was "a big gap", so opening up new sources of data will help to open up the market for those with no or thin files.

The lenders contacted welcomed the addition of Housing Benefit data (and the housing element of Universal Credit) in the credit process. A standard affordability model subtracts the rent (or mortgage) due from the applicant's income, as it is a liability. However, receiving state support for some or all housing costs means the tenant has a lower personal liability. The standard model is therefore unfair to these households, who may well be able to afford more than predicted. Furthermore, some lenders may view being in receipt of Housing Benefit (or the housing element under Universal Credit) as a more secure tenure because it is "government-backed".

A tangible example from the Rental Exchange shows that buying a washing machine with a good credit score would cost £575 paying one year's credit at 39% APR. With no or a poor credit score the price rises steeply to £1,480 on three years' credit at 69.9% APR. So having a fuller credit file reduces the cost of borrowing and limits financial exclusion.

Credit reference agencies see the value in Housing Benefit data – and therefore Universal Credit data – in helping with affordability assessments. The data is rich in income details, employment status, demographic and household characteristics as well as warning flags. Some of these will be used by lenders to show a risk to payments (e.g. disability, being unemployed, large household size, housing payments going direct to the landlord rather than the claimant). But in the absence of a credit score, which focuses on transactions, a positive marker on affordability showing that the household has the ability to make repayments could be used to increase lending and counteract the impact of thin files.

Part of the reciprocity from Rental Exchange for housing associations is being able to check affordability with housing applicants. This helps the associations let responsibly, to people who are able to pay their rent and not get into debt. Housing associations are beginning to carry out pre-tenancy assessments in order to prevent further financial hardship as tenancies progress, in cases where tenants can't pay their rent and arrears start to mount up.

Wider benefits

As well as clear benefits in the credit process, opening up new sources of data can help in other ways.

The Financial Conduct Authority is currently exceptionally strict in its efforts to ensure that 'vulnerable' individuals are treated especially carefully and in a bespoke manner. All lenders are under scrutiny to demonstrate how they are proactively identifying and supporting vulnerable individuals.

Lenders may well associate people in receipt of benefits such as Housing Benefit as vulnerable. A broader understanding of the information available within benefit data will allow for a more sophisticated understanding of household circumstances. Markers available within Housing Benefit (and Universal Credit) include household composition, income, earnings, employment status, savings, disability and other indicators of need. It can also be used to assess future risks, and track the change in income and need over time. Having some or all of these markers in somebody's credit file, as well as widening access to credit for some, may also flag certain individuals with low financial resilience and either allow for a conversation between the lender and individual about the reasons for receiving benefits or reduce the need for an independent assessment before providing or referring them onto appropriate support.

Using Housing Benefit Data to identify financial resilience and financial vulnerability.

Croydon council worked with Policy in Practice to develop a measure of financial resilience.[26]

The measure used Housing Benefit data to give an accurate assessment of income. Policy in Practice used information from the Living Costs and Food survey, adjusted to take into account family size and location, to model the anticipated expenditure of the household.

The gap between actual income and modelled expenditure led to households being categorised as 'coping', 'struggling', 'at risk' or in crisis'. This approach offered a better measure of the financial resilience of each household, and improved upon the relative income measure of poverty.

Financial Resilience captures a greater proportion of families in work and living in the private rented sector, as well as a greater number of households overall. Croydon have been able to use this measure to target budgeting support and other help towards these households' financial commitments.

Living standards (Jan 2017)

	In relative poverty	At financial risk
Total number of households	79,252	**93,042**
Total number of children	71,856	**87,671**
Tenure types most affected	1. Social rent (59.8%) 2. Owner-occupiers (25.5%)	1.Social rent (58.9%) **2. Private rent (27.6%)**
Percentage in work	17.0%	**24.7%**
Average rent	£547.70	**£822.49**

In a similar way, more open data sharing can help local authorities and housing associations to target households who need most help. For example, the housing associations we spoke to recognised that some households will have a reduced credit score because of sharing their rental data. This helps the landlords to target support to these people, to identify any root causes, then to help to address them and hopefully boost their credit worthiness – and financial inclusion – in future. The same is true of local authorities, which have a duty to provide Universal Support delivered locally to those in need. The rich data available from Universal Credit, matched with data in the credit process, provides key intelligence to target those most in need and therefore target resources efficiently.

Harnessing new data sources in the credit process

In the previous section, we have shown the real value that opening up data collected by local authorities and housing associations could have in improving access to mainstream credit. To actually benefit people, however, the data needs to be shared with credit reference agencies and accepted by lenders. First, we look at some of the big hurdles in doing this, and then set out three ways to share data.

Challenges to opening up data

We identified four hurdles in opening up new sources of data into the credit process. These are informed consent, reciprocity, lender acceptance and technical issues.

The Data Protection Act 1998 demands that a clear purpose is needed to collect, store and use personal data and that individuals must provide **informed consent** in order for their personal data to be shared; for sensitive data this must be explicit consent. While some exemptions exist, such as to prevent fraud and crime, these do not extend to sharing personal data with credit reference agencies. However, this challenge can be overcome, especially where there is a clear benefit to those individuals, such as boosting financial inclusion.

To ensure compliance with the Data Protection Act, housing associations seek consent from individual residents in order to share data with the Rental Exchange. Those associations taking part show a very high degree of acceptance, with just 1% opting out. The opt-out approach was agreed after consultation with the Information Commissioner's Office because the benefit of rent data sharing to tenants is recognised by DPA 'legitimate interests' provisions. This opt-out approach ensures these benefits can be widely realised. Housing associations are now including the choice to share this data when residents sign tenancy agreements.

A study by the Children's Society[27] shows that legal and regulatory difficulties can be overcome. The idea here was to increase the sharing of live birth data so that families could be contacted about the availability of support from local centres. The report found that a consent box overcame many of the difficulties of sharing data, with almost all parents giving their consent when the box was included in forms.

There is an unintended consequence that sharing data can negatively affect credit scores. Yet evidence tells us that many more people benefit from sharing new sources of data than are hindered . It can also help to pinpoint those who are most financially excluded and in need of help, while also ensuring these people don't become burdened with loans they cannot repay.

For data to be shared with credit reference agencies, there must be **reciprocity** with those providing the data. Local authorities can see immediate benefits in this through improved fraud checks, but also in being able to target those households most at risk and therefore help those most in need. Boosting access to mainstream credit for these households can increase financial inclusion and put them in a stronger position financially, with less dependence on public services in future. If people can borrow at affordable

rates, they are less likely to go into debt and fail to pay rent or council tax. One London borough that we spoke to told us they would welcome this approach, as it would ensure that they continue to have access to data through which they can put together their own tailored financial inclusion strategies.

Lender acceptance is another key challenge. In order for data to be included in credit files, lenders must accept the value of it. The credit reference agencies and lenders we have spoken to have been positive about the potential for fuller credit files. Extra evidence provides a richer, more granular picture of households, thus offering a more accurate view of affordability. However, this needs to be tested further.

The discussions we've had with lenders show they are keen to have a more rounded picture of applicants: "In general more information leads to better lending decisions". However, credit reference agencies point out that actually getting lenders to accept new data takes time. Lenders need to be convinced it makes a material difference to their decisions. This is probably the area where most additional work is required.

Technical issues post a fourth obstacle. Ensuring that data is robust, comprehensive and consistent is important, and not always straightforward. It adds to the cost of data sharing initiatives, including the Rental Exchange. Standardised datasets exist within the public sector, and allow for analysis to be carried out at scale. The Single Housing Benefit Extract (SHBE) is an established protocol that local authorities already use to send data each month to the DWP. This therefore provides a firm and scalable basis to share and use this data more widely. It also provides the basis for data sharing with Universal Credit, though this time from DWP to local authorities and potentially credit reference agencies or lenders.

There is a high level of confidence in the reliability and accuracy of SHBE data, they are the basis upon which over £24bn of public funds are spent[28]. Many Housing Benefit claims are made through online forms, which flag errors if necessary fields are left blank or filled in wrongly. A range of different documents are needed to verify ID before a claim is processed. This includes National Insurance number, rent payments, earnings, self-employment earnings, student status, state benefits, pensions and tax credits, savings or capital, outgoings for children and more. To verify ID or an address, councils require a bank statement or council tax liability letter. Claims are reviewed by assessors, with consequences for local authorities if there is evidence of over/underpayments. A similar level of confidence in the information supplied to support Universal Credit claims should emerge as the new benefit is rolled out in the coming years.

Opinions over the coverage of data varied among the credit reference agencies. One told us that there must be good national coverage. Providing information from one area or region would not have much of an effect on credit scores as the amount of data would be too insignificant to influence their models. In contrast, the other two agencies recognised the value in the extra data in areas where it could be gathered, even if there were gaps elsewhere. Experian's Rental Exchange started with small amounts of rental data but has built up to some 1.2 million tenants today.

Three ways to share data

There are three routes to sharing the new sources of data currently collected by local authorities and housing associations as well as Universal Credit data held centrally. These methods are local collection, a data wallet or through government intervention, though they are not mutually exclusive and there is overlap between them.

The **local collection** approach is similar to the Rental Exchange model, where a credit reference agency collects data – say Housing Benefit or council tax data – from individual local authorities, as Experian does with housing associations. A current Policy in Practice project looking at the impact of welfare reform on low income Londoners shows that it is possible to collect this information from individual local authorities if there is a clear benefit, and appropriate safeguards are in place[26].

A clear drawback to this approach is the need for an agency to establish the data collection with individual local authorities, unless there is regulation to enforce this. The alternative to collecting data locally would be to rely upon central sources of data such as Universal Credit.

The incentive to credit reference agencies is having a competitive edge. If these new sources of data can improve the accuracy of their scores, and therefore help with lending decisions, then it could be viable for them to pursue this. This requires acceptance of any new data source and approach by lenders. This risks creating a 'chicken and egg' situation, where the investment in developing a new approach needs to be supported by evidence of existing market demand, and vice-versa.

The second option looks to the future when each individual holds their own credit file in an online **data wallet**, from which they add, take away and share information. The individual owns the information, though legislation may be needed to ensure the wallet owner has access to all the relevant data. The Open Banking regime is a step in this direction.

Some "information aggregators" are already doing this. MOGObankconnect (run by CallCredit) provides a quick and easy way to share online banking transactional data; Hello Soda[29] collates data from various sources to show the digital footprint of a consumer; and Insight Report[30]**Error! Bookmark not defined.** s another example. Models like this are the start of personal data wallets. In the current system data is exchanged and processed about individuals, often without their knowledge. With the data wallet an individual could, for example, share their bank statements to help calculate their credit score.

An individual can decide what to add to their file and which company or type of company they want to show the file to and for how long they want them to have access. For example, if somebody were looking for a loan they could share their data wallet with loan companies - but just for a month, until a loan was secured. This gives the individual full ownership over their information. It could also be possible to compare loans and financial products online, in a similar fashion to the platform the CMA have designed for banking[18], which could have the potential to increase competition in the sector and the quality of loans.

A drawback to this approach is the ability to access a data wallet. Just as some people are excluded financially, they can often be excluded digitally too. So whereas a data wallet may benefit the young or migrants, two groups identified as more likely to have thin credit files or no files at all, it may not be as powerful for older people or social housing tenants, who are less likely to be online. However, as more and more of the population becomes digitally included, the appeal of the data wallet should increase.

Of course, technical hurdles that we mention above – particularly about data quality – apply here. Convincing providers of identification and financial data to share this with data wallet suppliers will be a challenge. However, the increasing use of API technology, such as with Open Banking, shows we are moving in the right direction. But government action may be needed to push this further and faster, building on the work of GOV.UK verify and Open Banking.

The third way to drive this forward is through **government intervention**. In particular, this is about sharing data, such as between local authorities, other public bodies or housing associations and credit reference agencies or data wallet providers, in support of financial inclusion. The Rental Exchange is already having positive results for those tenants taking part, yet this is only a fraction of the total number of people who could benefit. This is particularly pertinent in the current context of rolling out Universal Credit and the drive to be digital by default.

Regulation could be designed to enforce data sharing, allowing credit reference agencies to obtain records on rental payments from private housing owners, letting agencies and housing associations. Action like this would be similar to that taken by the Competition Commission, which in 2006 acted to ensure home credit loan providers provided their data to at least two of the three major credit reference agencies**Error! Bookmark not defined.**. Further legal precedent has been set by the Small and Medium ized Business (Credit Information) Regulations 2015[31]. This imposes a duty on designated banks to provide information about their small and medium sized business customers to credit reference agencies, and vice versa. Regulation is a powerful option, if carefully designed and implemented.

This is the approach favoured by the local authorities we have spoken to during this project, especially in light of the roll-out of **Universal Credit** and the prospect of losing regular access to rich data on households such as Housing Benefit data. In their view, legislating to maintain data sharing between local authorities and central government would be the best way to tackle financial exclusion, and a range of other challenges facing vulnerable households. Not only does continued access to household level data help local authorities and housing associations in their own poverty reduction and financial inclusion strategies, but it provides the key enabler for them to co-ordinate their efforts with central government and an incentive to work with credit reference agencies and the private sector more broadly.

> *"We would welcome any process and sharing of information that will help our customers to be more financially included."* Feedback from a Welsh local authority.

Central government could also benefit from making Universal Credit data more widely available through a range of avenues. The DWP are currently struggling to verify information on rents, leading to delays in Universal Credit payments[32]. They could benefit from the reciprocal element of sharing information, if it

helped them to reduce fraud and error, and improve processing accuracy and timeliness through sharing information[13].

Local authorities and other local organisations would be able to use Universal Credit data as they use Housing Benefit data, to better allocate financial and non-financial support. Local authorities are able to use the information within benefit records to better target Discretionary Housing Payments, provide employment support and childcare to households most likely to benefit and be proactive by using triggers within the data to target preventative services. This benefit would be lost if Universal Credit data were not shared with local authorities.

Residents can benefit through the provision of better targeted services, faster and more accurate payments and lower cost public services. Their privacy can be protected through the ability to opt-out, so individuals can choose not to share data if they prefer not to.

Conclusion and recommendations

With some 6 million people excluded from mainstream credit, there is huge potential in opening up responsible lending to these households. There is a strong appetite among lenders and credit reference agencies to use new sources of data to help boost credit files.

Examples like the Rental Exchange and the work local authorities such as Luton and Croydon have done using Housing Benefit data show the real difference this data can have on verifying individuals, boosting credit scores and therefore providing more affordable credit. But we need government intervention to extend this and boost financial inclusion to many more people.

Data used to apply for welfare benefits is rich. Housing Benefit data includes demographic details, income levels, working status and rental charges. As more people move over to Universal Credit, this data will become richer still with the addition of Real Time Information on earnings. The reciprocal information received by DWP could be used to better target support to vulnerable households, and improve processing times.

Additional information on household income and earnings could make an additional 4.8m consumers more attractive to mainstream and lower cost lenders. But this data needs to be more widely shared to have a positive impact on financial inclusion. Legislation is needed to push this forward.

Our key recommendation is therefore for central government to open up data sharing between public bodies, credit reference agencies and lenders. This builds on existing work in Open Banking, greater use of public data and being 'digital by default'.

Our second key recommendation is for the regulator and industry itself to educate mainstream lenders of the benefits of wider data sources in the credit process. By keeping much of this rich data outside of credit applications, the rich, granular detail is missing. Rather than supporting financial inclusion, it is forcing households to borrow from unscrupulous lenders, putting them more at risk of financial exclusion.

Our third recommendation focuses on the need to better educate the public about the purpose and benefits of opening up data, and therefore the tangible value of consenting to share data more widely. We've seen with examples like Rental Exchange and the Children's Society work that explaining clear benefits to people and offering them active opt-outs from some data restrictions hugely boosts the good use of personal data.

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