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## *Man's registered debts*

*The purpose of this study is to analyse and present the position and judgement of private individuals and private entrepreneurs – as debtors – in the sphere of economy and in the society. This document sheds light on the exposed position of debtors, while providing both easily comprehensible and professional guidelines to the participants of the Hungarian lending market on either side. Because law and lawyers should not consider individuals as subjects and contracting parties only, but as persons with dignity – untouchable essence –, personality and privacy, all of which represent universal human values in all fields of life, and, accordingly, in lending relations, too. From this point of view, key significance is attached to presenting the regulations on debtor lists – urged by financial institutions –, as well as the related issue of data protection, enhanced by a brief presentation of historical and technical antecedents.*

Registration of debtors goes well back in history, to the beginnings of money and banking services. Data are recorded on lending banks from the ancient Kaldean empire from 2300 B.C. As early as at that time, a record was probably kept on which customers were worthy of credit, and which ones did not comply with their obligations. It is the history of ancient Greece where we see the best-known measure that assumes comprehensive registrations.

Solon (Σολων), elected archon (αρχων) in 594 BC for a year with unlimited power, introduced as one of his first measures the shaking off of burdens or *seisachtheia* (σεισαχθεια), which meant concurrent and full cancellation of all debts.<sup>1</sup> Another historical reference to a debtor register – at the time of the Roman Republic in 367 BC – is a provision of a law motioned by tribunes C. Licinius Stolo and L. Sextius Lateranus: 'de aere alieno' ruling that any interest paid must be deducted from the principal, and that any further outstanding principal debt must be repaid in equal instalments for three years.<sup>2</sup> A similar solution is seen in the third book of Moses, which decrees that debts must be waived in the year of jubilee blowing of trumpets recurring every fifty years. Medieval customs and registration systems are accurately reflected by stigmatisation for example in the form of the 'cap of shame'. The lender was allowed to force insolvent debtors to wear a green hat all the rest of their lives, and if the debtors appeared anywhere without the hat, they were imprisoned.<sup>3</sup> The credit information systems as we mean today evolved only as late as in the 1980s in Western Europe.<sup>4</sup> Participants of the credit world today use debtor lists combined with two attributes: negative or positive, depending on whether only defaulting debtors are registered, or every

debtor. Both types raise a number of economic and legal problems – particularly in terms of constitutionality, data protection and civil law.

## DEVELOPMENT OF DEBTOR LISTS IN HUNGARY

Traditionally, the most typical active engagement of credit institutions is lending credits, where contracting is preceded by a thorough examination of the customer, called credit assessment. Between the world wars, banks used so-called credit notification letters to cater for this issue.<sup>5</sup> In such a letter, the credit institution inquired about their potential client's financial standing, reliability, business character, reputation, etc. from the future client's customers. This solution was fairly reasonable because it yielded a comprehensive first-hand view of the loan applicant's economic standing as seen by direct business partners. Frauds were also possible even in these circumstances, moreover, a credit notification represented no liability whatsoever, but the business morale of the time was utterly different from today's, and integrity was much more palpable in the day-to-day business of enterprises. In view of that, the mechanism of loan assessment wore off in the decades of socialism, and was assigned only slight significance, and had no established practice or a set of criteria after the regime change in Hungary – in the young two-tier banking system –; consequently, these factors also contributed considerably to the crashes and bank consolidations of the time.<sup>6</sup> A peculiar solution to this problem was represented by credit insurance, when an insurance company vouched for the customer in case of non-payment for a certain fee, as shown by the practices of the State Insurance Company (Állami Biztosító) in the 1980s and ÁB-Generali in the 90s. For this insurance type mostly used with consumer loans, the insur-

ance company paid the bank instead of the customer on the latter's default, which meant that the bank was compensated.

Bank crashes generally result from imprudent loan extensions, or, from the opposite aspect, from insolvent debtors; frauds and other crimes are only encountered as an exception.<sup>7</sup> Parallel to that in the 1990s, Hungarian credit institutions – adopting western examples – started to set up and keep debtor lists, wishing to make the contents thereof available to one another. The key point was to reduce lending risk, which assumed efficient and mutual exchange of information among credit institutions on indebtedness, solvency and willingness to pay of loan applicants. Even at that time, the idea of setting up a central registration emerged, which required a uniform legislative background to ensure legal and effective operation of such a system.

The initial problems surfaced around the protection of personal data and the method of implementation among financial institutions. The Constitution and the data protection act establish strict rules on the protection, handling and disclosure of personal data. At the same time, also credit institutions used the protection provided by civil law to business and banking secrets as a reference. Each would have been breached in the absence of a change in the legislation. The banks as data providers initially did not wish to disclose all their problematic and difficult cases to one another and the public – for obvious reasons – as those could have shaken public confidence in them and deteriorated their reputations and trustworthiness.<sup>8</sup> The other side of the coin is that – as users – they are precisely interested in a more complete and detailed registration, as only a reliable registration can provide efficient help on decision preparation. Establishment of the legal background at that time affected the standard text of Act LXIX of 1991 on financial institutions and activities of financial institutions

(AFI). The modification was adopted by the National Assembly in October 1993, and, as a result, eight leading banks<sup>9</sup> founded Interbank Information Services Plc. (Bankközi Informatika Szolgáltató Rt.) on 15th February 1994 in the form of a private limited company. Finally, as of 28th June 1995<sup>10</sup>, the Interbank Debtor and Loan Information System (known as BAR) commenced operation. Establishment of such a centralised registration initially represented a major challenge to the Hungarian data providers of the time – considering the current facilities and development of information technology –, as they were required to record loads of information quickly and accurately, and ensure easy access and usability at the same time. The first system to start operation was the central system (BAR KR); later, end-point interface (BAR IR) systems were also installed. It was only after this point that an initial population of the database could take place,<sup>11</sup> and query facilities were also phased in. Within a relatively short time, a database with a usable volume of data was set up. Subsequently, minor financial institutions, savings and credit associations also joined. By mid-1996, all the participants of the current lending market were connected to the registration, and by the end of year, the loan contracts database of enterprises could be considered complete.

Originally, BAR was only allowed to contain data on enterprises, given that the legal background of the time prohibited any registration of personal data of natural persons, and commercial banks also stayed away from this line of business; actually, OTP ruled this market alone. Requirements of the lending market, however, urged extension of the registration to natural persons due to similar problems seen in retail lending.

This issue, on the other hand, raises an indispensable examination of the issue from a constitutional aspect. Section 59 of the Constitution decrees that protection of personal data is a fun-

damental right of citizens, and as such, its restriction may only be in line with the principle of a constitutional state – observing the provisions of the Constitution and the legal practice of the Constitution Court –, on condition that it does not affect material content of any of the fundamental rights;

- its aim is to protect another fundamental right or obligation;
- public interest justifies restriction of this right;
- the aim cannot be achieved in any other way;
- the restriction is suitable to achieve the aim.

A negative debtor list meets the above criteria, as it enables improved safety for the Hungarian market economy and lending sphere. On the other hand, the interests, the right to private property and its protection of both financial institutions and their customers also justify preventing those listed in such a database from accumulating further debts, endangering the situation of compliant participants of the lending market. As a result of that, pursuant to an amendment to Act CXII of 1996 on credit institutions and financial enterprises (ACIFE) in 1997, the data of natural person debtors having accumulated outstanding debts through a contract breach have been added to the system as of 1998<sup>12</sup>. It was in the same year that joining this system was made mandatory for financial institutions pursuing certain activities. Later – although to a more limited extent, compared to banks,<sup>13</sup> – the Student Loan Centre also joined the BAR system; consequently, breaches of payment obligations stipulated in student loan contracts specified in a dedicated provision of law are also subject to the same uniform legal conditions as for other debts.

In May 2003, a major change took place in the group of shareholders of Interbank Information Services Plc., when GIRO Elszámolásforgalmi Rt. became the sole owner. The most comprehensive reform to the system

was performed under the ACIFE amended by Act CLXXXVIII of 2005. A highlight of this change to legislation was that the legislator broadened the obligation of notification for credit institutions. The main reason for its necessity was that the commissioner for data protection received a number of complaints – mostly at the time of the “great housing loan application fever” in 2003<sup>14</sup> – concerning the fact that a considerable percentage of debtors only found out that they were included in the debtor list when they were refused another loan application with reference to that. In addition, customers also objected to being unable to obtain data or being posed difficulties on doing so; in the event of their erroneous or incorrect inclusion, no appropriate system of legal remedies was available to them. According to the amendment, banks are required to inform the debtor of the consequences of their default in writing prior to concluding the loan contract, moreover, in the event of a subsequent non-payment, the customer must be informed of the consequences of their default thirty days before being listed. Parallel to that, the system was developed even in the same year, which resulted in a new form of query facilitating better processing of a credit report and clearer representation of customer details, also catering for handling different name versions of natural persons.

## THE CENTRAL CREDIT INFORMATION SYSTEM

As of 1 January 2006, the official name of the registration was changed to Central Credit Information System (referred to as KHR). The basic rules are specified in chapter XX/A of the ACIFE. According to a definition laid down in law, KHR is a closed-system database with the aim of promoting and improving the safety of business activities, lending and customer rating activities of financial institutions, in addition to further reducing lending risk through authentic reference data<sup>15</sup> – defined and taxatively listed by law – sourced from reliable registrations. In 2002, the KHR recorded approximately 1.220 million cases of default (1.1 million of which were corporate, 120 thousand retail) by a total of approximately 155 thousand debtors (of which 80 thousand corporate, 75 thousand retail). The number of queries per month exceeds 27 thousand (7 thousand corporate, 20 thousand retail).<sup>16</sup> By the end of 2006, the number of private individuals exceeded 370 thousand, with a total number of retail defaults surpassing 550 thousand. The company operates a quality management system that complies with standard MSZ EN ISO 9001:2001. Currently, more than 400 domestic financial institutions<sup>17</sup> are connected to the database. (See Table 1)

Table 1

### PARTICIPANTS OF THE KHR IN 2006 AND 2007

Form of financial institution	1 January 2006	1 March 2007
Banks	29	33
Specialised lending institutions	7	7
Financial enterprises	212	232
Savings cooperatives	167	155
Credit associations	5	5
Investment enterprises	4	5
Other	0	7
Total	424	444

Source: based on [http://www.bisz.hu/bisz\\_felhasznaloklistaja.php](http://www.bisz.hu/bisz_felhasznaloklistaja.php) <sup>18</sup>

Based on a licence issued by the Hungarian Financial Supervisory Authority, the exclusive operator is Bankközi Informatika Szolgáltató Központi Hitelinformációs Zrt. (BISz Zrt.),<sup>19</sup> which complies with the conditions stipulated in the ACIFE.<sup>20</sup> The nucleus of this system is a central unit installed at the head office of BISz Zrt., interfaced to the data providers as data entry points, and also to the users. BISz Zrt. installs the interface, and trains the persons eligible or required to use it. Connection to the head office is only possible via a defined communication channel, using the appropriate password, which eliminated the problems and risks related to data traffic via the Internet. Rules that provide guarantee are: KHR operates with equal conditions for all connected financial institutions, it may only accept reference data delivered by them, and it may only deliver reference data managed by them to the supplier of the reference data; furthermore, a record is kept by both the data suppliers and BISz Zrt. on each data delivery and data request in terms of contents, time and fact. The entered data can only be modified by the data providers on compliance with pre-defined rules. The stored information is supplied to querying users, also according to strict requirements. Actually, participants of the lending and money markets connected to the system are data providers and users concurrently. However, these two notions do not fully overlap, as a portion of the organisations carry out activities that are not required to be registered in the KHR; they mostly join the system for a reference element. The other group includes those that only maintain business relations with a couple of enterprises; consequently, queries are hardly used subsequent to contracting and data supply.

The keeper of the registration is furthermore responsible for complete and up-to-date registration of data, and the completeness and continuous maintenance of the database. However,

this list does not give rise to the requirements of authenticity and accuracy, which should be basic elements of a reliable system. A lack of authenticity can be explained with fraudulent debtors, but even in this case, certain facts (e.g. public instruments and the contents thereof) must be accepted as true until proved otherwise. This means that BISz Zrt. is not answerable for the authenticity and reliability of data, which may question justification of existence of the whole system. The obligation to ensure an up-to-date status lies with the data provider, who is required to enter any change into the system within 5 working days. Reference data are handled for five years, and then irrestorably deleted by BISz Rt. In connection with this, the data protection commissioner was informed<sup>21</sup> in 2005 that data were archived in the KHR for another five years after the lawful five years were up, in a way that ensures inaccessibility for suppliers of lending data, but can be retrieved and disclosed to courts and the public prosecutor's office for evidencing purposes on written requests. The ombudsman called on BISZ Zrt. to refrain from the planned data handling on the one hand, and to discontinue illegal data handling on the other hand. Finally, the data handler, having accepted the stance, has made the necessary measures. It is worth calling attention to the fact that the abovementioned legal period of five years starts when the debtor repays their debt, or when the queuing of the contract or receivables is terminated, or when data are disclosed due to frauds or crimes.

The most important point is that subjects cannot attain removal from the KHR through subsequent compliant behaviour or contractual performance. From this aspect, subjects on passive and active debtor lists<sup>22</sup> are distinguished; the former include those that have settled their debts, while the latter ones that have not. Certainly, on applying for subsequent loans, banks also consider this, as being listed

on the negative list does not suggest an automatic rejection of the loan application, because the particular credit institution always decides on the application using their own internal criteria for deliberation. Accordingly, these loan products are not as favourable as seen in the media. Those listed can select from a number of options on applying for another loan: a close kin signs the contract, or they can provide another collateral (particularly real estate), or use expensive Austrian loans or private loans (typically usurers). Austrian loans are the best-known ways to solve this problem; however, caution and prudence must be exercised with foreign contract elements, this is why the first two solutions can be recommended more.

The Central Credit Information System consists of three parts:

- details of data suppliers;
- details of natural persons;
- details of enterprises.

Logically, the latter two subsystems constitute the debtor list. Registration of data suppliers is important because KHR may only request and disclose reference data from and to those within the system. The legal rules of being listed are different for private individuals and enterprises. A shared feature is that the debts must be related exclusively to the following transaction types: loans,<sup>23</sup> borrowings; financial leasing; cashless means of payment; co-signing or assuming bank guarantees. Listing of natural persons due to their debts – which must be considered typical in case of a debtor list – may only take place if they meet a set of criteria: being in arrears for over 90 days continuously with an amount of the minimum wages as of the starting date as a minimum. This deadline is sufficient to settle a debt, however, the amount is relatively low, considering that the current minimum wages as of 1 January 2008 amount to HUF 69 000 per month only. An overdue loan debt entails other burdens as well, which increase the debt

through late payment interest, bank procedure, costs of foreclosure, and, in the event of a transaction secured by a collateral, there is also a potential of losing the collateral (typically real estate). So, due to minor lapses of attention or being hindered, the loan applicant may easily end up on the debtor list for five years – as mentioned above. Other cases are associated with crimes or fraudulent behaviour:

- disclosing false data;
- using false or forged documents;
- fraud with cashless means of payment.

For natural persons, these conditions must be considered separately for each legal relationship.

The subsystem that maintains enterprises is all-inclusive,<sup>24</sup> and consists of three parts. The first one includes all the borrowers – this is not yet a negative debtor list –, irrespective of whether they are legal entities or not, and of the amount of the loan contract. The real debtor list contains those that have payables queued on their bank accounts – due to insufficient funds – for an uninterrupted period exceeding thirty days and over an amount of HUF 1 million. Considering the specific structure of the Hungarian economy, i.e. the high number of small and medium enterprises, we may deem that much more lenient rules are applicable to the business sphere, as a considerable part of these companies generate an annual turnover approximately equal to that sum. The third option for being listed in the KHR is stricter, because it is not related to committing crimes or fraudulent behaviour, it is sufficient for the enterprise to breach their obligation undertaken in the contract concluded to accept cashless means of payment, and the credit institution terminates or suspends the agreement. Actually, in this case it is the bank that decides whether the company is added to the debtor list or not, as they may select an option different from the previous two sanctions, such as rescission.



## CUSTOMER AND DATA PROTECTION

In the law, one side of customer protection represents the right and obligation concerning information given in writing. The two customer types are also distinguished here. For natural persons, it is a difficult regulation that unnecessarily complicates practice, requiring that the customer must be told different information prior to the initiation of concluding a transaction and prior to concluding the transaction. It would be simpler to instruct the potential contracting customer as early as in the first case. However, all further rules have a significance of guarantee. Thirty days prior to being listed in the KHR, the customer must be informed that their debt meets the criteria specified above. As there is no provision, the banks can decide whether to extend those ninety days or send the letter after sixty days stating that the customer will be added to the debtor list in thirty days. However, the law is clear on an obligation of the credit institution to notify the debtor of the delivery the reference data within a maximum of eight days following the event. Simpler rules apply to enterprises: the conditions of being listed must be disclosed prior to contracting. Nevertheless, it is deemed to raise concerns that no notification is required to be provided prior to or after actual addition to the KHR. This is followed by collective rules. Anyone at any credit institution is entitled to receive information on what data are registered in the KHR on them, and on which bank disclosed these data. The duration of this procedure cannot be longer than nine days.<sup>25</sup> Such a customer request for information is free of charge once every year, and a fee is payable for all additional requests for information. According to the cogent provisions of law, data supply to or from the KHR does not represent a breach of the bank secret for the credit institution.

Another major area of customer protection

is the ensuring of the right to legal remedy, and the specification of associated procedural rules. By virtue of this, customers are authorised to raise objections if the data are incorrect or handled illegally. As a result, the registration is either rectified, or the entry is deleted, but in an extreme case, leaving it unchanged is also possible. The credit institution or BISz Zrt. must examine all objections within fifteen days following their receipt, and immediately or within two working days at the latest, notify the registered person of the examination results in writing, in the form of a document posted with certificate of delivery, and perform the adequate measures (rectification, deletion, notification of credit institutions concerned). If the customer has not been informed, or the information has not been satisfactory, or, if they receive an unacceptable answer to their objection, they may enter an action against the credit institution and BISz Zrt. – within a 30-day term of preclusion following the notification, to the court competent on the basis of the place of residence –, to achieve remedy of the legal injury, i.e. delivery, handling, rectification or deletion of the reference data. If a legal action is started on loan details, it must also be registered in the KHR in addition to the existing information and data. It is an important provision of customer protection that the burden of proof evidencing that the conditions of delivering and handling the reference data in the KHR were met lies with the bank or the financial enterprise managing the KHR. During the legal action, the court may rule suspension of data handling, but the data cannot be handled after the ruling until it becomes final. The final ruling on changing or deleting reference data must be sent to the HFSA.

The credit institutions wished to construe provisions of law related to data in a restrictive sense, limited to reference data only, thus evading, for example, giving reason for loan assess-

ment. However, the defining provisions of Act LXIII of 1992 on the protection of personal data and the publicity of data of public interest (DP Act) rule that it is not only the data but also the consequences that can be drawn for a person that are deemed as personal data. Consequently, pursuant to section 12 of the DP Act, it is compulsory to provide information on this, i.e. the reasons for awarding or denying loan. Giving reasons for creditworthiness or the absence of it in banks' opinions violates the protection of business secrets also ensured for them, as it may reveal their internal rating method. Some have tried to evade provisions of the DP Act by inserting a stipulation in the general terms and conditions or the points of the application form signed by the customers whereby the bank does not give reasons for its loan decisions, and the debtor is not allowed to raise objections to the assessment criteria or the result. This is certainly against the law, because a cogent provision of law cannot be evaded by an adhesion contract. This is also reinforced by recommendation of the data protection commissioner as of 22 December 1999, as well as a subsequent consultation with the president of the HFSA in 2002, and even a case from 2005. Should the credit institution not comply with its above-mentioned obligation, citizens are entitled to apply to the court, considering these recommendations and with reference to section 17 of the DP Act.

On the other hand, personal data may also be involved in the course of a loan assessment. A number of banks happen to inquire into other personal information in addition to the reference data allowed to be handled: such as health related data, income status, salary, photos of real estate, etc. If the customer consents to these being handled and disclosed, their constitutional rights are not breached, but considering today's lending relations, these have become general practice.

In certain cases, mandatory provisions are stipulated in a dedicated piece of legislation. Decree 25/1997. (VIII. 1.) issued by the Ministry of Finance has special provisions for the methodological principles applicable to mortgage loans; consequently, subsection 5 of section 2. c) of Appendix 4 states that photos demonstrating the real estate state and value constitute mandatory parts of the expert opinion. The data protection commissioner has received a number of relevant complaints to the effect that such photos may contain details referring to personal data. In 2004, the ombudsman sought the Minister of Finance who in his response to repeated letters of request stated that he had forwarded the letter of request to the Hungarian Banking Association, and from there to all the credit institutions concerned, calling on them to seek to act as provided in the recommendation, and stating that he agreed with the standpoint of the data protection commissioner. The Banking Association has even pointed out that a photo taken of real estate may be deemed personal data even if it pictures no personal belongings that refer to the identity of the owner.

In addition to the KHR – similarly to most countries in Europe<sup>26</sup> – a so-called private credit bureau also functions in Hungary. It was established back in 1998 under the name of Girodat Rt., which was subjected to dissolution in 2003. Its activity was resumed by GIRinfO as of January 2004, operated by Giro Zrt. On commencing operation, the founders planned to set up a credit information system using a positive debtor list that would contain data of private individuals, as seen with the German SCHUFA. This, however, is still not possible due to legal limits. The credit bureau does not have its own database such as the KHR, and participants can access the necessary information using one another's registrations through a common search engine. In



addition, they have authorisation to access a number of other databases – also available to the members –: personal ID, passport, driving licence, registration of residential addresses; a database of portrait photos and signatures; company registration and a registration of lien contracts. Credit institutions are allowed to join the company on a voluntary basis, but given that it is mandatory to join the KHR, and it also keeps a registration of enterprises – and is much more comprehensive, owing to these two benefits – GIRinfO is in contact with few financial institutions. In this respect, no change is expected for the next couple of years, considering that joining such a database is rather cost- and labour- intensive, and can hardly provide extra services compared to the existing one. In addition, BISz Zrt. has also set up a debtor rating system<sup>27</sup>: enterprise/personal BAR index, rating customers by a risk factor between 0 and 9. 1 signifies worst customers, 5 customers of temporary risk, 9 the best contracting partners, and 0 means that no data are available. Logically, the personal BAR index only goes from 1 to 5, given that it contains negative information only. Experience shows that banks do not use this customer-rating service; they tend to use their own internal methods instead.<sup>28</sup>

## DEBTOR LISTS IN THE EUROPEAN UNION

Since Hungary's accession to the European Union in 2004, virtually all legal issues of domestic law are also raised in the EU dimension. It is also the case with the Hungarian debtor list, as all countries in the European Union have one or more organisations that provide loan reference or loan information services. As a result of the four liberties, as well as the integration of lending markets, a demand has been raised for a uniform EU loan registration system. A key obstacle to this are the considerable differences in conditions in the member states: mandatory/voluntary, positive/negative list, state founded / organised on a market basis, and appearance of threshold values. Even on examining few countries, it is to be seen that the participants are of a great variety. (See Table 2)

Currently, only private credit bureaus have been able to establish a cross-border association, under the name of European Association of Consumer Credit Information Suppliers, ACCIS. Certainly, the European Union has set it as a goal to ensure on revising its Consumer Credit Directive 87/102/EEC that lenders in a member state have access to a credit information system operated in another country under the same conditions as in their own country.

Table 2

### PARTICIPANTS OF CREDIT REFERENCE SYSTEMS IN A FEW EU MEMBER STATES

Country	Participant institutions
Austria	National financial institutions, insurance companies, leasing and factoring companies, and foreign subsidiaries of these
Belgium	National credit institutions and their foreign subsidiaries
France	National credit institutions and their foreign subsidiaries, leasing and factoring companies
Germany	National credit institutions and their foreign subsidiaries, national insurance companies
Italy	National credit institutions and their foreign subsidiaries, Italian subsidiaries of foreign banks
Portugal	National credit institutions, Portuguese subsidiaries of foreign banks, leasing and factoring companies and credit card companies
Spain	National credit institutions, Spanish subsidiaries of foreign banks, leasing and factoring companies

Source: Árvai – Dávid – Vincze: Credit information systems (Hitelinformációs rendszerek), Credit institutions review (Hitelintézeteti szemle), 2002/5

But, as seen with support for similar approximations, and also considering the conduct of member states concerning approximation of laws, this will take a long time yet. In spite of this, a uniform registration system for the European Union will be developed in the medium term, and business life will no doubt force it through, given the increasing movements of private individuals and enterprises among member states. Even today, independent institutions providing references operate with success, which offer reliable business information on potential borrowers on request by foreign financial institutions, and are not liable to corruption in the interest of their creditworthiness.

### THOUGHTS ABOUT THE POSITIVE LIST

The other type of debtor lists is a positive list, containing the full credit history of borrowers, which renders a more complete picture of a person's creditworthiness; payment habits, willingness, ability to pay and solvency. Considering international practice, this can be considered as typical (for instance, in the United States of America, Great Britain, Germany, Poland, Italy), but a number of countries use a negative list exclusively (such as Portugal, France, Finland, Australia). Certain authors believe that the negative list has a disadvantage compared the positive one, namely, that the former registers problem clients only, which yields a higher non-payment ratio resulting in a lower acceptance of loan applications from those on the list. Another benefit of the positive list is that it does not only reference payments but also events like the customer acting wantonly or fraudulently on loan assessment, this being the reason why the bank did not contract with them. If a person's full credit history is known, it reveals their general habit in the field of finances, their indebtedness com-

pared to their financial standing, and their ability to assume additional burdens. It is generally true for solvency that those paying always in due time and not accumulating a large amount of debts represent a lower risk of non-repayment, which means that such customers are worthy of (more) favourable assessment of loan applications.<sup>29</sup> For natural persons, familiarity with the full credit history may be of significance because private individuals are not required to produce an official report on or account of their indebtedness.

The thought of building a positive debtor list has haunted the Hungarian credit information area from time to time. When in 1998 a database registering private individuals was launched, retail lending had not reached a degree where the existence of a system containing full credit histories could be convincingly argued for. In 2002, the National Bank of Hungary and the Banking Association tabled a joint proposal to the Ministry of Finance on completing the system to contain comprehensive data. Coordinating discussions and negotiations among the ministry, the HFSA, the National Bank of Hungary and the ombudsman have been going on since. It is important to note here that it was not until August 2006 that the supervision assumed a standpoint to promote an amendment to the ACIFE to this effect.

Establishing a domestic positive debtor list can be viewed from two dimensions: one involves IT issues, the other legal aspects. Technically, the question is raised whether to develop the existing one, or to set up a new one. In the former case, the most obvious method would be to adopt the Polish system, while in the latter, Germany may be an example to follow. Even a reorganisation of the current KHR would take a minimum of nine months.<sup>30</sup> Considering the situation of Girodat in terms of credit information, further development of the private credit bureau is not even raised as an

issue. The key problem would be to manage a suddenly enlarged data volume. The current number of clients just exceeding 400 thousand would jump to as many as 2–3 million, and surpass it in no time. This size of a database would be difficult to run based on the natural identifiers currently in use with the KHR (name, date of birth, mother's name), which means that a new one should be generated for all entries. Some authors argue for the personal identification number as an obvious solution, and regret that BISz. Zrt. has not been authorised to handle this authentic identifier. The personal identification number should not be related to the credit information system in any way, given that, firstly, its role is diminishing in everyday life, secondly, it gives rise to easier connectivity of systems with different functions as an issue of concern, and, thirdly, it would evoke the feeling of the socialist state administration in many, which is difficult to agree with a modern two-tier banking system. Therefore, it is felt that the issues of legal aspect are more complex than the technical ones. The question also emerges what date to designate as the starting date of entering debtors and transactions. This is certainly conceivable for the future only, meaning that only contracts concluded subsequent to adopting a positive debtor list can be entered. Consequently, such a system would be populated with a usable volume of data only after 3 or 4 years. For a full view, it is necessary to mention that since the Student Loan Centre has joined the KHR, this means automatic entry of a high number of young people starting college or university with a student loan. The set of registered data is also a debated issue. Many believe that not only credit information but also data on commitments related to income and property, public utility payments, etc. should be considered on assessing solvency.

The other issue is associated with data protection. Authorisation of the KHR to handle all customer data requires an amendment to the

law. For the time being, neither the legislator, nor the data protection commissioner urge introduction of a positive debtor list,<sup>31</sup> as the combined set of conditions related to the restriction of fundamental rights as described above does not reassuringly justify building such an all-inclusive registration. It is widely read that extension of the database would result in long-term cost-savings for credit institutions by reducing the costs of administration, given that everyone would use the same centre. A more complete credit report would improve the quality of loan assessment, as well as the lending risk, which would result in a lower lending loss, which, in combination with the previous point, would decrease loan interests, leading to an even more stabilised lending market. This, however, is only an assumption, with no clear and adequate calculation method to support it to exclude any doubt. It is true that loans are cheaper in the European Union than in Hungary, but it is rather naive to trace it back to positive lists,<sup>32</sup> as there are certain macro-economic instruments and phenomena (central bank base rate, stock exchange index, exchange rate changes, inflation, etc.) that exert quantifiable influence on loan interests. So – with respect to customers performing contractually, such a database would be in many cases (in the magnitude of millions) a pointless stockpile of data.

Debtors are already in a position highly exposed to credit institutions. The data protection commissioner receives a lot of complaints<sup>33</sup> that shed light on abuse by banks and unlawful data handling. It is not justified for lenders to receive an even more detailed picture of debtors, as they extend loans only on a due amount of collaterals, consequently, the variety of collateral obligations securing the contract as specified in the Civil Code provides sufficient security even for an event of non-payment. A group of economic experts believe that a positive list would favour customers, because com-

petition among banks would grow as a result of their being well-informed, and, as a result, they would develop much more debtor-oriented and debtor-friendly terms and conditions. Others point out the protection of integrity and reputation, saying that reference to an index score and inclusion in the list could yield benefits in business life. It is rather sad, at the same time, that today in the realm of domestic economy the issue of reputation and integrity is not raised as something to protect from attacks but rather something to prove the existence of.

Introduction of a positive list in a multi-party democracy and in a constitutional state is ultimately decided by the National Assembly, whether they amend the currently effective regulation applicable to the Central Credit Information System. Based on what has been discussed above, it can be stated: considering that expert opinions differ significantly, the decision is delayed. The media and the press occasionally publish news on the KHR's positive list; the current guesses predict introduction by mid-2008 or by 2009.

## NOTES

<sup>1</sup> It is still debated today whether this regulation also applied to commercial and financial deals, or it was only relevant to debts that burdened estates or entailed loss of personal liberty. In: *Lexicon of the ancient world (Ókori Lexikon)*; ed.: Pecz Vilmos; 1902

<sup>2</sup> Better known as: *Leges Licinia Sextia*; in: *Lexicon of the ancient world (Ókori Lexikon)*; ed.: Pecz Vilmos; 1902

<sup>3</sup> This custom is also reflected in court rulings in France in the 16th century. In: *Ráth-Végh István: Power and money (Hatalom és Pénz)*; Gondolat, 1964

<sup>4</sup> Spain (1983), France (1984, 1989) Belgium (1985), Austria (1986) – a curiosity: a central registration was in place in Germany as early as in 1934 and in Italy in 1964.

<sup>5</sup> In: *Révai's lexicon of trade, finance and industry (Révai Kereskedelmi, Pénzügyi és Ipari Lexikona)*; ed.: Schack Béla; 1930

<sup>6</sup> This happened despite the fact that even in 2001 the retail bank loan portfolio equalled only 6 per cent of the GDP, while 46 per cent in the European Union. (Hungarian Central Statistical Office, KSH)

<sup>7</sup> In: *Meir Kohn: Banking and financial affairs, financial markets*; Osiris, 2003, page 335

<sup>8</sup> The fact that the exchange of information is uneven among credit institutions also contributed to this. Leading banks are in contact with more participants,

and consequently hold more information. Accordingly, it is conceivable that, due to the competition among banks, sharing information results in actually more loss for the banks compared to the benefits of using data disclosed by minor banks. This is discussed exhaustively by M. Pagano and T. Japelli, in: *Information Sharing in: Credit Markets, Journal of Finance*, December, 1993

<sup>9</sup> This is a difference compared to western European systems, as they were typically founded by central banks and are operated by supervisory bodies. Founders: Budapest Bank, Inter-Európa Bank, Kereskedelmi és Hitelbank, Külkereskedelmi Bank, Magyar Hitelbank, Takarékbank, Országos Takarékpénztár és Kereskedelmi Bank Rt, Postabank. In 1995, another four banks (Commerzbank, Creditanstalt, Magyar Fejlesztési Bank, Mezőbank) and Fűzesabony és Vidéke Takarékszövetkezet joined the owners in the course of a capital increase. In the light of this, it is also worth observing that the transformation the Hungarian banking system has undergone during more than a decade.

<sup>10</sup> This date is debated in the literature: 28 June 1995 is used on BISz. ZRt.'s home page ([www.bisz.hu](http://www.bisz.hu)), but [www.webbank.hu](http://www.webbank.hu) has 1 June 1994.

<sup>11</sup> [www.bisz.hu](http://www.bisz.hu)

<sup>12</sup> Material operation of the retail system actually started in 1999 only.

<sup>13</sup> Subsection (5) of section 130/A of the ACIFE: No reference data can be transferred from the KHR to

the Student Loan Centre – other than specified in subsection (4) of section 130/J.

<sup>14</sup> For the terminology, visit [www.pszaf.hu](http://www.pszaf.hu).

<sup>15</sup> Any data, including the personal identification data of the registered person, that is allowed to be handled by the financial enterprise running the central credit information system pursuant to this law. (chapter V of Appendix 2 of the ACIFE)

<sup>16</sup> In: Árvai-Dávid-Vincze: Credit information systems (Hitelinformációs rendszerek); Credit institutions review (Hitelintézeti szemle), 2002/5.

<sup>17</sup> Users of the KHR may be financial institutions whose joining is approved by the HFSA, and which conclude a Cooperation Agreement with BISZ ZRt. The participant are varied: banks, specialised credit institutions, savings and credit associations, factoring and leasing companies, investment companies and other financial enterprises.

<sup>18</sup> Unfortunately, data have not been updated since March 2007.

<sup>19</sup> home page: [www.bisz.hu](http://www.bisz.hu)

<sup>20</sup> see section 130/B of the ACIFE

<sup>21</sup> In: The data protection commissioner's annual report, 2005, case No.: 1653/K/2005

<sup>22</sup> The distinction in terminology is taken from the page [www.bankweb.hu](http://www.bankweb.hu).

<sup>23</sup> Both bank loans and consumer credits

<sup>24</sup> This is the basic difference between the retail and corporate subsystems; for natural persons, only outstanding overdue debts are registered, while for enterprises, each contract is recorded in the KHR.

<sup>25</sup> The credit institution forwards the request for information to BISz Rt. immediately, or within two working days at the latest, which sends the requested data to the bank in a closed format within five days, which, having received it, sends it to the requesting party in a similarly closed format, as a document posted with a certificate of delivery, immediately or within two working days at the latest.

<sup>26</sup> In Germany, a similar one is Bundes-SCHUFA and Creditreform Experian GmbH; In Great Britain, the Equifax and Experian. The most significant credit information company in the world is the CRIF Group, which was founded in 1989 in Italy, and is present in a number of countries today (England, USA, Germany, Austria, the Czech Republic, Mexico, Canada, Holland, Denmark).

<sup>27</sup> Credit scoring has a long-time practice in the American economy; customers may receive credit only above a certain threshold. In more detail, see in: Meir Kohn: Banking and financial matters, financial markets; Osiris, 2003

<sup>28</sup> In: Background material to retail credit information systems (Háttéranyag a lakossági hitelinformációs rendszerekről), PSZAF, 2006

<sup>29</sup> A number of studies have been produced on this subject, the most significant one was written in the USA by J. Barron and M. Staten: The Value of Comprehensive Credit Reports: Lessons from the U. S. Experience, 2000 Draft. They claim that a full-scale credit bureau system run and managed in a responsible way has an outstanding role in the significant development of financial services seen in the past decade.

<sup>30</sup> This was calculated by Polish operators, in addition to offering delivery of a reorganised version of their system. In: Árvai-Dávid-Vincze: Credit information systems (Hitelinformációs rendszerek); Credit institutions review (Hitelintézeti szemle), 2002/5.

<sup>31</sup> For more details, see the website [www.abiweb.obh.hu](http://www.abiweb.obh.hu): A stand on the positive debtor list, and the relevant parts of annual reports.

<sup>32</sup> The HFSA's document entitled Background material to retail credit information systems, 2006 (Háttéranyag a lakossági hitelinformációs rendszerekről, 2006) also contains this approach.

<sup>33</sup> In 2005, nearly 120 complaints were received on data handling by financial service providers, almost 40 per cent of which were constituted by reports objecting to the operation of the central credit information system.