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By email: cp18-12@fca.org.uk

Dear James,

CP18/12 High-cost Credit Review: Consultation on rent-to-own, home-collected credit, catalogue credit and store cards, and alternatives to high-cost credit

The Financial Services Consumer Panel welcomes the opportunity to respond to the FCA's consultation on 'High-cost Credit Review: Consultation on rent-to-own, home-collected credit, catalogue credit and store cards, and alternatives to high-cost credit'.

The Panel's main points are as follows:

- The FCA's excellent analysis shows serious harm to consumers who are on lower incomes and have lower credit scores than the generality of the population. We believe the evidence provides a strong basis for the FCA to take bolder action. Information disclosure and consumer prompts have had very limited impact on deep-rooted problems with firms' business models and culture, and are likely to be even less effective with the target market for these products. Bolder action would demonstrate that the FCA is serious about delivering better outcomes for financial services consumers, in line with its stated Mission.
- We question the effectiveness of the authorisations gateway for consumer credit. There is strong evidence of poor practice among some newly-authorized lenders (including guarantor lenders who are not included in this review). For example, rent-to-own lenders were authorised despite the well-known problems with extended warranties that are integral to their business model. The FCA should review whether its Threshold Conditions are fit for purpose, particularly for lenders because of the particular risks to consumers of irresponsible lending.
- The FCA should extend its Equality Impact Assessment so that it assesses how proposed remedies are likely to work for target groups, given the profiles of those target groups and the mechanics of lending. For example, information disclosure is unlikely to have much impact in sectors such as home credit that rely heavily on personal relationships and where evidence clearly shows low levels of 'shopping around' by borrowers; or in catalogue credit and store cards where the emphasis is on friction-free customer journeys to get consumers (usually women) borrowing and spending as much as possible.
- The Panel continues to urge the FCA to adopt a holistic approach to the credit market, and set out a vision for what a well-functioning credit market looks like for consumers. A piecemeal approach risks regulatory arbitrage and poor outcomes. The FCA continues to ignore its own evidence that one of the key predictors of problem debt is a high debt to income ratio. [We continue to call for the FCA to work with industry and consumer groups](#)

[to develop a simple rule of thumb](#) to determine the maximum unsecured consumer credit limit for an individual, based on affordability. The Panel looks forward to engaging with the FCA and others in its Debt Project, which will explore these issues and possible solutions.

Summary of the Panel's recommendations

Rent-to-own: Unless the FCA can demonstrate a stronger case for consumer benefit for extended warranties, it should immediately ban all extended warranties for rent-to-own products.

Home credit, s49 CCA: The FCA's approach to s49 CCA seems timid. The proposed guidance does not create legal certainty for firms and does not provide remediation for consumers whose providers have – in FCA's current view – committed a criminal offence. FCA should bring a test case to clarify the meaning of s49, and, in light of the outcome, consider ordering retrospective reviews by firms.

Refinancing home credit loans: The FCA should ban the refinancing of home credit loans, rather than expend time and resource implementing measures that we know from experience are unlikely to achieve much.

Catalogue credit and store cards BNPL proposals: The FCA should regulate so that all firms only charge interest on the unpaid part of the balance (rather than the whole balance).

Catalogue credit and store cards credit limit increases: The FCA should: (1) ban unsolicited credit limit increases; and (2) regulate for lenders to conduct an affordability check that considers all the consumer's debt before any credit limit increase.

Catalogue credit and store cards early intervention and persistent debt: We support the FCA's effort to ensure consistent standards across credit sectors. However, we repeat the calls we made in [our response to the credit card market study](#) for the FCA to mandate earlier action to avoid consumers being left in debt for long periods and to mandate better data-sharing so that firms have a full picture of a consumer's financial position.

Below we set out our responses to specific questions. Where appropriate, we answer related questions together.

Rent-to-own

Q3: Do you agree with our proposals for a point of sale ban on extended warranties?

Q4: Is the two day deferral period the right length of time?

Q5: Do you have any comments on the proposal to provide adequate explanations to enable the consumer to make an informed decision?

Q6: Do you have any comments on our proposed definition of rent-to-own?

Q7: Do you have any comments on the proposed period for firms to implement the new rules?

The Panel is not opposed to all forms of extended warranty but agrees that in the rent to own market this product is of limited value to consumers when similar cover is provided by standard manufacturers' warranties. FCA's proposals for a point-of-sale ban on extended warranties are based on thin evidence of consumer benefit. Unless the FCA can demonstrate a stronger case for consumer benefit from this approach, we believe the FCA should implement an immediate outright ban on extended warranties for rent to own products.

If the FCA goes ahead with a point-of-sale ban rather than an outright ban, it should monitor and evaluate its effectiveness, with a view to an outright ban if lender practices do not quickly improve (say, within 12 months). In addition, the information that lenders must provide to consumers about extended warranties should clearly state that most goods are covered by a manufacturer's warranty for at least the first year at no extra cost.

The lender should also be required to provide the borrower with basic information about any warranty for the specific goods they are renting-to-buy at the point of purchase e.g. a separate, clearly written document that tells the borrower whether the goods have a manufacturer's warranty, the duration of that warranty, and what the warranty does/does not cover. This means that borrowers stand a better chance of making an 'informed choice' if they are later offered an extended warranty, bearing in mind that most consumers do not read terms & conditions.

Home-Collected credit

Q8 Do you have any questions on our draft guidance on interpretation of s.49 CCA?

We continue to be concerned that financial services firms seem to find it difficult to understand and interpret the legislation and regulation that governs their profit-making activities. In response, the FCA invests considerable resource producing (non-binding) guidance on a whole raft of issues that it must then consider in its supervisory activities. While this approach may sometimes reassure firms that they are complying with the letter of law, s49 guidance continues to defer to the Courts and therefore does not provide legal certainty for firms.

In its recent discussion paper on retained CCA provisions, the FCA did not signal any concerns about the ambiguity or unenforceability of s49. We believe the FCA should bring a test case so the Courts can rule on their interpretation of s49 in relation to umbrella permissions. Depending on the outcome, the FCA should consider a review of past business that is found to be in breach.

In any case, we would like to know how the FCA plans to demonstrate its approach is delivering better outcomes for consumers.

In the interests of transparency, the FCA should publish information about the action it has taken where home credit firms have breached its interpretation of s.49 CCA (or to explain why it did not take action where breaches were identified). This would help home credit firms understand the likely consequences of breaches of s.49 CCA. The Panel believes that transparency is an important regulatory tool that is under-used by the FCA.¹

Q9: Do you agree with our proposed new rules on explaining the costs of refinancing compared with a concurrent loan?

Q10: Do you have any comments on the proposed period for firms to implement the new rules?

The Panel is sceptical about the likely effect of new rules to explain the costs of refinancing an existing home credit loan compared with a concurrent loan. On balance, refinancing benefits the firms and their agents far more than it does the borrower (who gets lower repayments but pays more overall than if they had taken out a concurrent loan instead). The new rules may add some friction into the process, but it seems likely that firms and their agents will find ways to encourage refinancing where it is in their financial interests to do so. We would like the FCA to

¹ As set out in our response to the FCA's *Approach to supervision*, available here https://www.fs-cp.org.uk/sites/default/files/fscp_response_approach_to_supervision.docx__0.pdf

take bolder action and ban the refinancing of home credit loans, rather than expend time and resource implementing measures that we know from experience are unlikely to achieve much.²

Catalogue credit and Store Cards

Q11 Do you agree with our proposals for new rules clarifying that firms must explain clearly upfront how interest will be charged if the customer does not repay within the BNPL offer period?

Q12: Do you agree with our proposals to require firms to prompt customers to repay before the expiry of a BNPL or similar offer period?

Q13: Do you agree the rules should not include a specific time or period to issue the prompt? If not, what should it be?

Q14: Do you have any comments on the guidance on how firms may comply with this rule?

Q15: Do you have any comments on our proposals to extend the existing rules for credit cards and store cards regarding credit limit increases to catalogue credit?

Like the [FCA's trials of overdraft prompts](#) these proposals may benefit those who can afford to repay before the offer expires but do help those who cannot.

Nor do the proposed remedies directly address the FCA's fundamental concern about the practice of charging interest on the whole balance from the date of purchase if the borrower fails to repay the entire amount at the end of the BNPL period. The evidence shows that some lenders use this approach, while others charge interest on the unpaid part of the balance. We would like to see the FCA regulate so that all firms only charge interest on the unpaid part of the balance (rather than the whole balance), which would treat customers fairly.

Q16: Do you have any comments on our proposals for a three month implementation period?

Q17: Do you have any comments on our proposals for a three month implementation period?

Q18: Do you have any comments on our proposals to extend the existing rules for credit cards and store cards to not increase credit limits or interest rates for customers at risk of financial difficulties to catalogue credit?

Q19: In particular, do you have any comments on our proposal to use the same definition of 'at risk of financial difficulties' for catalogue credit?

Q20: Do you agree with our proposals that firms should have to take steps to be compliant as soon as the rules come into force?

It is shocking that there were almost 8,000 credit limit increases in 2016 where the consumer was two or more payments in arrears. This represents 8,000 opportunities where lenders failed to prevent consumer harm, at unknown cost to the consumer.

We agree with the FCA's proposal to extend the existing credit and store rules on treatment of consumers at risk of financial difficulty to catalogue credit as soon as the rules come into effect. If it has not done so already, the FCA should also require lenders to review customer records to

² See, for example, the Competition Commission's evaluation of its largely information-based home credit remedies http://webarchive.nationalarchives.gov.uk/20140402170609/http://www.competition-commission.org.uk/assets/competitioncommission/docs/2013/remedies/130228_home_credit_evaluation.pdf

identify irresponsible credit limit increases, and to compensate those consumers for any harm they experienced as a result.

We also want to see the FCA regulate more robustly 'upstream' at the point of sale or extension of credit to prevent this irresponsible lending. [As we've already pointed out regarding credit and store cards](#), we want the FCA to (1) ban unsolicited credit limit increases and (2) regulate for lenders to conduct an affordability check that considers all the consumer's debt before any credit limit increase.

We are unhappy about a voluntary industry agreement for catalogue lenders like that for credit cards. [We believe the proposals for credit cards](#) were over-complex and went against the general direction of travel in terms of clear and unambiguous informed consent, as set out in the General Data Protection Regulations (GDPR). They are a good example of what the behavioural economist Richard Thaler calls 'sludge' - confusing jargon that deters people from making informed choices.³

Q21: Do you have any comments on our proposals to extend the existing rules for credit cards on earlier intervention to catalogue credit and store cards?

Q22: Do you consider that there are any particular aspects of data that is particular to catalogue credit and store cards which firms in these markets should also monitor?

Q23: Do you have any comments on a six month transition period for implementation?

Q24: Do you agree with our proposals to extend the existing rules for credit cards on persistent debt to catalogue credit and store cards?

Q25: Do you agree with our proposals on the implementation period?

Q26: Do you agree that we should adapt the guidance to remove the reference to a reasonable repayment period of 3 to 4 years?

Q27: Do you have any comments on our definition of 'retail revolving credit'?

Q28: Do you have any comments on what types of product may be caught over and above catalogue credit and store cards?

We support the FCA's effort to ensure consistent standards across credit sectors. However, we repeat the calls we made in [our response to the credit card market study](#):

- Lenders should consider all forms of debt that a borrower has, not just the debt owed to their firm, for example using CRA or open banking data. Otherwise valuable opportunities for early intervention are missed.
- To enable this, the FCA should mandate that all firms report new lending commitments to credit reference agencies (CRAs) serving the UK market, and share real-time data.
- In addition, the FCA should collate and publish anonymised examples of good and poor practice in early identification and intervention by firms, as it proposed in *CP17/20 Staff incentives, remuneration and performance management in consumer credit*.
- In keeping with its consumer protection objective, the FCA should mandate firms to intervene sooner, requiring them to contact customers in persistent debt at 12 rather than 18 months. Firms would have to contact more customers, some of whom might get out of debt without any intervention. There would be no harm caused to those customers who would have been able to repay anyway, but large benefits for those who would otherwise continue in persistent debt for another six months before their lender took any action.

³ See for example <http://tonyisola.com/2018/02/financial-sludge/>
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We support the proposal to remove the reference to a reasonable repayment period of three to four years (as with credit cards), given that catalogue debt is smaller. The FCA should also remind catalogue lenders that where debt repayment is not possible, other courses of action should be followed, such as debt relief or write-off, with referrals to independent debt advice where appropriate.

Alternatives to high-cost credit

Q29: Do you have any comments on our draft guidance for registered social landlords?

We don't have any comments on the guidance for social housing landlords on referring tenants to credit unions or CDFIs. However, we urge the FCA to be more ambitious on high-cost credit alternatives, especially as access issues will become more urgent when it enacts its proposals on high-cost credit and overdrafts. The FCA should:

- Use competition and product powers to help plug the mid-cost credit gap;
- Devote whole Innovate cohorts to the problem; and
- Run tech sprints and other "solution sessions" to try to make a market.

This may demonstrate there is not a viable large scale market for high-cost credit alternatives. The fact remains that some consumers are too risky to be served at a price they can afford. It is a matter of public policy whether these consumers should have access to subsidised loans. The FCA should join other stakeholders to call for a coherent Government policy about whether these loans should be subsidised and, if so, by whom.

Equality and Diversity Assessment

Q30: Do you agree with our initial assessments of the impacts of our proposals on the protected groups? Are there any others we should consider?

Up to a point. However, the Panel believes that the FCA should extend its Equality Impact Assessment to assess how proposed remedies are likely to work for target groups, given the profiles of those target groups and the mechanics of lending. For example, information disclosure is unlikely to have much impact in sectors such as home credit that rely heavily on personal relationships and where evidence clearly shows low levels of 'shopping around' by borrowers; or in catalogue credit and store cards where the onus is on friction-free customer journeys to get consumers (usually women) borrowing and spending as much as possible with scant regard to long-term affordability.

Yours sincerely,

Sue Lewis
Chair, Financial Services Consumer Panel