



FCA Consultation Paper CP14/10

Proposals for a price cap on high-cost short-term credit

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- Citizens Advice Scotland and its member bureaux form Scotland's largest independent advice network. CAB advice services are delivered using nearly 250 service points throughout Scotland, from the islands to city centres.
- In 2012/13, the Citizens Advice Service helped consumers in Scotland with almost 207,000 consumer issues. That is 826 consumer issues for every working day. Just over a quarter of these were addressed by the Citizens Advice Consumer Service, handling nearly 57,000 issues, including 3856 about energy or post.
- Scottish citizens advice bureaux helped consumers with 150,000 consumer issues, covering topics as diverse as payday loans and car maintenance.
- In 2011/12, Scottish bureaux achieved a financial gain of almost £140million for clients based on funding of £16.9million.

Q1: Do you have any comments on our general approach to developing our proposals for the price cap?

Citizens Advice Scotland (CAS) welcomes the opportunity to respond to the FCA's consultation on a High Cost Short Term Credit (HCSTC) cap (CP14/10). CAS is broadly supportive of the aims and objective of the cap and we support the key principal put forward by the FCA that the benefits of such a cap outweigh the negatives. We do however have a number of specific issues regarding the nature of the cap, how it will be implemented and enforcement mechanisms to ensure best protection for consumers.

CAS believes that the work undertaken by the FCA to inform their decision making is robust and wide reaching. Indeed we were particularly pleased at the level of involvement afforded to consumer groups throughout the research stage of the cap formation. We particularly commend the consumer credit team and consumer intelligence team efforts to ensure that we were kept up to date with the progress of the FCA's work and consulted on our views as to how it should be investigated.

We agree with the FCA findings (point 3.13) that a large proportion of HCSTC users are in financial distress. Often the clients we support through our advice work on HCSTC products find themselves in particularly serious circumstances, sometimes relying on crisis support or charitable donations. Given that our Citizens Advice Bureaux (CAB) across Scotland are assisting with 100 issues regarding HCSTC products every week, we believe this is a unique financial market with a high level of financial stress. We share the view of the FCA that using HCSTC does little to bring the consumer benefit (point 4.35) and while we recognise that some users of such products may find benefit, on the whole distress and over-indebtedness is endemic to users of these products.

CAS are concerned however about the un-intended consequences of removing borrower's ability to access this market and we are pleased that the FCA considered this as part of their investigation. CAS is concerned about the threat of illegal money lenders as an alternative to mainstream lending. Last year we helped support 31 clients in Scotland with issues relating to such activity. While this figure is low we are aware that such activity is much underreported and that the true level of the current black market is hard to quantify. These cases are often some of the most distressing that our volunteers encounter and it cannot be under estimated how serious the impact of borrowing from such a lender can be. We do however agree with the FCA's findings in its consumer survey (point 4.44) that consumers will not seek to borrow from such providers as an alternative to HCSTC in large numbers. Indeed before such products were available on the market there was no evidence of illegal lending on a massive scale and research (*Illegal lending in the UK*, PFRC, 2006) shows that illegal lending is often focussed in particular urban geographies

(particularly the greater Glasgow area in the case of Scotland) and is long established in the communities in which they are active.

In recognising that borrowers will be excluded from this market it is important to realise a large number of people will struggle to make payments for essentials that we know they are using HCSTC for (point 3.13 & *Payday Lenders: Business as Usual*, CAS, 2014). Our evidence suggests that people who are heavily indebted and fail to secure additional funding to meet the costs of necessities may require other support. CAB evidence shows that more and more families in Scotland are living in poverty and require the support of charitable help such as food banks or government emergency support through the Scottish Welfare Fund. In our April 2014 paper '*Voices from the frontline: food parcels and the benefit system*' we revealed that when a crisis hits more and more people require food parcel support. It could be reasonably assumed that some people who face a crisis will use short term credit to see them through however if this is not available they may require such support. We believe therefore that the FCA has an important role in informing the government that as a result of this cap more families will require assistance to meet everyday living costs. It may be wise for the FCA to develop research proposals that can monitor these consequences to use in reporting to government. It is not sufficient to assume that because the FCA is not directly responsible that they do not have a duty to raise this. CAS are of the opinion that the HCSTC market has in recent years masked the reality, by providing short term answers, to large numbers of families in the UK whose incomes fail to meet the minimum required for basic living costs.

If the FCA's prediction on the number of firms exiting the market is correct then we would highlight to the FCA that many firms may sell on debts to other third parties. In the past we have found that compliance with providing debtors with a notice of assignment is poor and confusion over who is collecting often leads to debtors seeking advice from ourselves or other debt charities. We also note that in a case of a debt sold on, the new creditor is not obliged to keep to any previous repayment plan that may be in place. We encourage the FCA to consider the impact of this, reminding lenders of their duties regarding assignment of debts and consider how a potential peak in demand for debt advice will be provided for. We would support the use of fines levied against HCSTC to meet this demand or fund non-profit social lending schemes as alternatives to HCSTC.

Q2: Do you have any comments on the proposed price cap structure? & Q3: Do you have any comments on the price cap levels?

CAS welcomes the FCA's rejection of a simple cap on the APR of products. We previously intimated that such a cap would be unworkable, would not address the issues faced by consumers nor control other costs that may be increased. We

believe that setting a cap with a daily interest and total cost cap will help to focus firms on the need to properly and adequately check the affordability of a loan.

On the proposed daily rate cap of 0.8%, while we acknowledge the work the FCA has carried out to come to this figure, CAS is of the view that even under the proposals the cost of borrowing from the HCSTC market will still be very high and could be a root cause of borrowers becoming financially stressed.

CAS have long challenged default fees and other charges as unfair, punitive and not proportionate. While we support capping, we would have preferred that level of the cap be set at the actual cost of default involved to the company. Given the FCA's own findings (point 5.38) that altering this fees cap would have "limited impact on firms" due to firms' collection rates being "relatively low" we are surprised by the relatively large sum of £15 when considered next to the low value often borrowed. We agree with the FCA's point (point 5.37) that firms should be able to recover costs involved in a default to a point, but we believe in practice this is significantly less than £15. At £15 CAS are concerned that this may not meet the Scots common law definition of 'pre-estimate of loss' (Report on Penalty Clauses, Scottish Law Commission, 1999) and therefore be open to legal challenge as an unfair contractual penalty. CAS also find it interesting to note that Credit Card firms agreed to a cap of £12 on such fees and we are unclear as to why the FCA believe that the HCSTC market is different.

We are pleased that a ceiling cap on the total amount chargeable has been included in the consulted model. CAS understand the FCA's view that the 100% cap is easy to understand for consumers (point 5.54) when compared to another rate, such as 75%. However while we respect the FCA's well-placed motive to ensure the cap is easy to understand, we believe that the need for strong consumer protection from usurious rates overrides the simplicity of the 100% rate.

Having reviewed the findings of the FCA's research we understand that a 50% cap may mean the closure of the market, however we do not believe the same case can be made to reject a 75% cap. With this in mind we would draw to the FCA's attention their own findings regarding the Finnish model (Appendix 4, point 57). Despite concerns from Finnish lenders that a cap of 50% APR would mean the complete closure of the market, 50 out of the 90 firms still operate after the introduction of this cap. CAS are strongly of the opinion that after the introduction of even a more stringent cap than is being proposed by the FCA many firms in the UK will continue to operate in what will still be a lucrative industry. With regard to a 75% cap the FCA state that this may limit loans to three months or less which is presented as a cause for concern. However a review of Technical Annex 1 (point 3.1.2) shows the FCA found that very few loans last longer than 60 days, meaning the disruption caused to potentially limiting access to loans longer than three months is insignificant. We would therefore encourage the FCA to reconsider the total cap of 100%. CAS believes there are insufficient findings in the FCA's research that the market would

be unable to work at 75% or below and still serve the needs of borrowers using the market. We also ask that this cap is reviewed in six months and a report given on the impact on both the consumers but also the lenders in the market to see if it has altered the market in any way.

In addition to the proposals already set out in the consultation, CAS would recommend that consideration is given to an automatic freezing of the amount owed where a consumer contacts a lender with issues making repayment. We believe that where this is already practiced in the sector it is extremely helpful to consumers who are in financial difficulty and, in the long run, may lead to better rates of repayment for these firms

Q4: Do you agree with our proposals on repeat borrowing?

CAS is disappointed that the FCA have not proposed to include repeat borrowing within the cap (point 5.73). Given that the FCA's own research found that 52% of loans in this market are given within 14 days of another loan being paid off it is clear that repeat borrowing is endemic in this market. Reliance on such finance is extremely damaging and while we support the existing controls (such as roll-over caps) we would have hoped that action, possibly limiting repeat borrowing, would have seen the best protection for borrowers. In this regard we propose a number of actions: repeat borrowing to be limited as roll-overs currently are, a cooling-off period between loans introduced, a direct marketing ban on current customers, clear and proactive information as to where free and impartial debt advice is available to **every** repeat customer.

In practice, our proposals would mean:

- A consumer would be limited to taking a total of three loans (inclusive of roll-overs) from a HCSTC lender within a year of the first.
- A cooling off period of 28 days between a loan being paid off and a new loan offered by a given firm (although allowing the ability to roll-over).
- Ban on direct marketing to any borrower who has taken a loan from a lender within the last 12 months.
- All borrowers who seek second and subsequent loans or any rollover in a year should receive clear information on where to get free and impartial debt advice.

We believe that such measures are required to break the cycle of debt that is clearly widespread in this sector. Allowing a cooling off period and limit on the number of loans will still allow for consumers to make use of products where for example there is a late payment in wages but will stop the recurring nature and reliance on these products for everyday living expenses, which is unsustainable (*Payday Lenders: Business as Usual*, CAS, 2014).

We welcome the FCA's commitment that they will monitor to ensure that firms cannot use repeat borrowing as a method to avoid the total cost cap (point 5.76). We

support strong action against any lender that is seen to alter short lending terms that could mean a higher cost for the borrower by avoiding the cap.

Q5: Do you have any comments on the scope of the price cap?

CAS understand why the FCA considers the HCSTC market to be very specific and have therefore excluded home-collected credit, overdrafts and credit cards from these proposals. There are arguments that some of these products could benefit from the rules being proposed and we ask that the FCA consider this as part of their ongoing regulation of these markets.

With regard to points 5.69, 5.70 and 5.71 we welcome that brokerage firms, debt collectors and other chargers will be included in the total price cap. We believe this to be an important step in consumer protection. CAS are concerned from case evidence that firms in these sectors will be at a high risk of non-compliance and we urge the FCA to make sure debt collectors and credit brokers are aware of their responsibilities under this cap.

Q6: Do you have any comments on our proposed Handbook rules? & Q7: Do you agree with our proposals on unenforceability?

We have no comments regarding specific proposed rules but as per our answer to question 5 regarding debt collectors and brokers we believe there to be a high risk of non-compliance and the need for vigilant supervision and swift enforcement.

We agree with the approach as set out in the consultation regarding unenforceability. We welcome that breaches of the cap will mean that loans will become unenforceable either through the court or through the FCA. We would support that any debt collection activity is prohibited in the handbook rules when the price cap has been breached meaning that any attempts to collect a debt that has breached the cap is an offence and punishable by the regulator.

CAS would welcome action against named individuals from companies where the price cap is not complied with, as within the FCA's powers, which would act as a strong deterrent.

Q8: Do you agree that we should prevent UK-based debt administrators from enforcing HCSTC agreements on behalf of ECD lenders which include charges in excess of the price cap?

CAS agrees with the approach by the FCA on this matter to be sufficient to protect consumers from such unauthorised activity.

Q9: Do you have any comments on the proposed approach to data sharing?

CAS agrees with the FCA's approach and welcome developments in real time data sharing by the companies in this market. We understand from firms that they are progressing this and we look forward to this being implemented by the majority of the market in time for the FCA's deadline of November. If this is missed we again support the FCA's proposal that rules be set on data sharing, however we hope that this will be unnecessary.